JC Economics Tuition

**Unemployment – CSQ**

**Challenging times ahead**

# Extract 1: UK economic growth has slowed dramatically, latest survey suggests

Britain’s economy is losing momentum, knocked by weaker household spending and worries about the global outlook, according to the latest in a string of downbeat business surveys.

Business activity grew at the slowest pace for more than two years in Britain’s dominant services sector last month, according to the closely watched Markit CIPS PMI report. “Weakness is spreading from the struggling manufacturing sector, hitting transport and other industrial-related services in particular. There are also signs that consumers have become more cautious and are pulling back on their leisure spending, such as on restaurants and hotels,” said Chris Williamson, chief economist at survey compilers Markit.

“Wider business service sector confidence has meanwhile also been knocked by global economic worries and financial market jitters.” The pound weakened against the euro and the dollar after the report, which economists saw as providing further reason for the Bank of England to hold off raising interest rates from 0.5%.

Source: The Guardian 5 October 2015

**Table 1: Key Economic Indicators in 2015**

|  |  |  |  |
| --- | --- | --- | --- |
| **Indicators** | **UK** | **China** | **Singapore** |
| Nominal GDP growth (annual %) | 2.2 | 6.9 | 1.9 |
| Inflation rate | 0.05 | 1.4 | -0.5 |
| Exports as a % of GDP | 27.6% | 21.9% | 177.9% |
| Imports as a % of GDP | 29.2% | 18.4% | 152% |

Source: The World Bank Data

Why China depends on export demand? – china needs mass production – mass employment to contain their unemployment

Singapore depends on export demand for high valued production – high-valued employment – high wage job – higher SOL and high tax revenue

Trade to GDP ratio – (X+M) GDP

Import demand – reflects Sol / potential growth

**Table 2: UK’s trade with selected countries in 2015**

|  |  |  |
| --- | --- | --- |
| **Countries** | **UK’s exports to (£) (Rank)** | **UK’s imports from (£) (Rank)** |
| United States | 96.4bn (1st) | 59.3bn (2nd) |
| China | 16.7bn (8th) | 38.4bn (3rd) |
| Japan | 10.5bn (11th) | 9.6bn (14th) |
| Germany | 48.5bn (2nd) | 70.4bn (1st) |
| Singapore | 7.1bn (17th) | 3.9bn (27th) |

Source: Office for National Statistics; www.visual.ons.gov.uk

# Extract 2: China pledges policy support to economy, reform in 2016

China will make its monetary policy more flexible and expand its budget deficit in 2016 to support a slowing economy, state media said on Monday. It cited top leaders who wrapped up the annual Central Economic Work Conference, a meeting keenly watched by investors for clues on policy priorities and main economic targets for the year ahead.

The government will take steps to expand aggregate demand next year. The People's Bank of China has cut interest rates six times since November last year and reduced banks' reserve requirement ratios (RRR), or the amount of cash that banks must set aside as reserves. The government has also stepped up spending on infrastructure projects and eased restrictions on home buying to boost the sluggish property market. Top leaders also pledged to push forward "supply-side reform" to help generate new growth engines, while tackling factory overcapacity and property inventories.

Source: Reuters, 21 December 2015

# Extract 3: Shedding light on slowing growth: What ails Singapore's economy?

# Singapore's small, trade-dependent economy is under the weather. While the country has not yet sunk into a full-blown recession, its fortunes are tied closely to those of the world economy and the outlook there is far from cheery. The Sunday Times looks at four key contributors to slowing growth in Singapore.

1. **Lacklustre Global Growth**

The world economy has yet to completely shake off the vestiges of the global financial crisis and continues to lack a strong growth driver. Singapore’s key trading partners have all been grappling with their own sets of challenges.

1. **Protracted Oil Price Slump**

World oil prices had been fairly stable from 2010 until mid-2014, at around US$110 a barrel. But they have almost halved since, plunging the oil and gas industry into a crippling slump. Companies in Singapore have not been spared the effects of this protracted downturn. More than two years of tumbling oil prices have wiped over US$24 billion (S$33.5 billion) from the market value of Keppel, Sembcorp Marine and other listed oil-services companies - or about two-thirds of their pre-July 2014 capitalisation.

Tens of thousands of jobs have been axed and some companies have defaulted on bond payments - sparking concerns over banks' exposure to the sector. The drag from this important sector is predicted to feed through to the rest of the economy.

1. **Shifting Trade Flows**

International trade has fallen to its lowest level since 2009, alongside lacklustre economic growth. But some economists say the slowdown is not merely cyclical, and lower levels of global trade might become the new normal.

This is because growth in developed economies like the United States is increasingly driven by services rather than the trade in goods. China is also becoming less exposed to international trade as it shifts away from an industrial-led growth model towards consumption and services. This means Chinese companies are increasingly sourcing from within the country, instead of importing. This trend could weigh on regional trade even in the long run - a gloomy prospect for Singapore, which depends not just on its own export but which also does a bustling trade in re-exports.

1. **Disruptive Change**

Prime Minister Lee Hsien Loong said in his National Day Rally speech in August that disruptive change is the "defining challenge" facing Singapore's economy.

(sectoral adjustment – influenced by technological development – structural unemployment – skill mismatch and displacement of worker with more machinery)

Technology has transformed almost every industry - from food delivery to manufacturing. These developments have left both challenges and opportunities in their wake, most obviously in the labour market. There are thousands of jobs waiting to be filled in growing sectors like IT, precision engineering, education and healthcare. But many workers who have been laid off lack the necessary specialised skills required in these roles.

There is no easy solution to this - the ever-increasing pace of technological change means that jobs will more or less be in a constant state of flux. There is help available for laid-off workers - including the option to upgrade their skills with SkillsFuture, or programmes which help mid-career workers move to industries with the potential to grow. But companies and workers also have a part to play - both in terms of skills upgrading and shifting mindsets.

 (manpower development – has both demand and supply side implication)

Source: The Straits Times, 30 October 2016

**Questions**

|  |  |  |
| --- | --- | --- |
| **(a)** | Using data from Table 1, |  |
|  | **(i)** | Compare the balance of trade position of UK, China and Singapore. | [2] |
|  |  |  |  |
|  | **(ii)** | Comment on the view that the Chinese economy performed well in 2015.  | [3] |
|  |  |  |  |
| **(b)** |  | Using data from Extract 1 and Table 2, explain and compare how ’weaker household spending and worries about the global outlook’ in the UK may impact the balance of trade for China and Singapore. | [4] |
|  |  |  |  |
| **(c)** | **(i)** | Explain what is meant by a budget deficit.  | [1] |
|  |  |  |  |
|  | **(ii)** | Using the concept of the circular flow of income, explain how ‘expanding its budget deficit’ (Extract 2) will affect the equilibrium level of national income in China.  | [4] |
|  |  |  |  |
| **(d)** | **(i)** | Assess whether ‘disruptive change’ (Extract 3) is the most significant cause of unemployment in Singapore.  | [8] |
|  |  |  |  |
|  | **(ii)** | Discuss the view that supply-side policy is the best way for the Singapore government to achieve low unemployment.  | [8] |
| [Total: 30] |
|  |

**Suggested Answers**

**(a)(i) Compare the balance of trade position of UK, China and Singapore. [2]**

(similarity and difference)

China and Singapore’s balance of trade were in surplus while UK’s balance of trade was in deficit. Balance of trade surplus (as a % of GDP) for Singapore was larger than for China.

**(a)(ii) Comment on the view that the Chinese economy performed well in 2015. [3]**

Table 1 shows that China recorded real GDP growth rate of 5.5% in 2015, indicating that it experienced economic growth and increase in real national income. Inflation rate was low at 1.4%, indicating price stability.

China recorded balance of trade surplus, which could indicate a favourable position on the balance of payments (assuming KFA account and other components of current account is already in a surplus)

However, there is no information in Table 1 on unemployment and therefore no indication of the level of employment and efficiency in the usage of labour resource.

There is also no information on the capital and financial account balance and therefore no information on overall balance of payments position.

**(b) Using data from Extract 1 and Table 2, explain and compare how “weaker household spending and worries about the global outlook” in the UK may impact the balance of trade for China and Singapore. [4]**

Point 1

Weaker household spending means a fall in consumption expenditure. Worries about the global outlook could lead to lower confidence in the economy for households and firms and this would result in fall in consumption and investment spending. Aggregate demand falls as consumption and investment spending are components of AD. The fall in AD leads to a fall in production levels and decline in national income in the UK.

As income falls, UK’s demand for exports from its trading partners, including exports from China and Singapore also fall.

Point 2

From Table 2, China is UK’s 3rd largest import partner while Singapore ranks 27th. This means that China exports more of its goods and services to UK than Singapore does and thus would suffer a larger fall in exports revenue, affecting its balance of trade more than the case for Singapore.

**(c)(i) Explain what is meant by a budget deficit. [1]**

A budget deficit occurs when government expenditure is larger than the tax revenue it collects.

**(c)(ii) Using the concept of the circular flow of income, explain how “expanding its budget deficit” will affect the equilibrium level of national income. [4]**

The circular flow of income refers to an economic model which describes the flow of payments and receipts between domestic firms and domestic households. Income flows from firms to households in the form of factor payments, and back again from households to firms as consumer expenditure on domestically produced goods and services (Cd). This circular flow of income can be increased by injections while reduced by withdrawals.

Injections comprise investment (I), government expenditure (G) and expenditure on exports (X) while withdrawals comprise savings (S), taxes (T) and import expenditure (M). National income is in equilibrium when planned injections are equal to planned withdrawals and there is no tendency for it to change.

When the Chinese government ‘expands its budget deficit’, G will increase while T will decrease. This will result in injections exceeding withdrawals (J>W) [1m] which leads to a rise in national income as more goods and services are produced and more households are paid more factor income. With the increase in income, households not only increase their spending on domestic consumption, they also save more (S), pay more taxes (T) and buy more imports (M), which increases withdrawals.

There will be successive rounds of induced increase in national income, causing an increase domestic consumption, S, T and M until withdrawals have risen to equal the new level of injections in the economy. [1m] At that point, national income will stop rising and a new equilibrium is attained in the circular flow where there would be a multiplied increase in national income.

**(d)(i) Assess whether the “disruptive change” explained in Extract 3 is the most significant cause of unemployment in Singapore. [8]**

Unemployment refers to the number of people who are actively looking for work but are currently without a job.

* Define demand-deficient unemployment and structural unemployment.

Perspective 1 (Disruptive change is a significant cause of structural unemployment)

Explain how “disruptive change” cause structural unemployment 🡪 technology changes and with no upgrading skills 🡪 demand for lower skilled workers fall while demand for higher skilled workers increase 🡪 Structural unemployment due to mismatch of skills

Perspective 2a

Disruptive change may not cause structural unemployment due to the presence of government policies (SkillsFuture)

Perspective 2b (Other factor can also cause unemployment) – sectoral disruption or adjustment

Shifting trade flows (China moving to own sources of FOPs) 🡪 Loss of CA in re-export industries 🡪 Workers are retrenched and unable to find jobs in sunrise industries due to mismatch of skills 🡪 Structural UnN

“Lacklustre global growth” and “shifting trade flows” 🡪 Fall in DDx 🡪 reduce net exports 🡪 demand deficient UnN

‘Protracted oil price slump’ could also be a cause of workers in the shipping and marine industry lose their jobs and may not have the skills to take on jobs in other growing sectors 🡪 Structural UnN

Evaluation

Whether or not disruptive change is the most significant cause of UnN in Singapore depends on how SG government deals with these changes. Nonetheless, in the short run, it is still likely to be a significant cause of S.UnN as the labour force needs time to be trained to adapt to these challenges.

In long run, disruptive change can also create employment opportunities in new sectors, thereby helping to create jobs and reduce UnN instead.

**(d)(ii) Discuss the view that supply-side policy is the best way for the Singapore government to achieve low unemployment. [8]**

**Perspective 1 (SSP is the best way for the Singapore government to achieve low UnN)**

Skillsfuture/Workfare

* Improving the skills of workers -🡪 reduce mismatch of skills🡪 **reduce structural UnN**
* subsidies for skills upgrading for workers 🡪 improves productivity 🡪 lowers COP 🡪increases SRAS 🡪 actual growth 🡪 **reduce DD-def UnN**
* Able to produce higher quality products 🡪 Increase demand for X 🡪 AD increases 🡪 actual growth🡪 **reduce DD-def UnN**

**Perspective 2a (Limitations of SSP)**

* May run into budget debt 🡪 increase in T in the LR 🡪 reduce C and I 🡪 reduce AD 🡪 **worsen DD-Def UnN** instead
* Difficult to change mindset of both companies and workers “shifting mindsets”
* No guarantee that training will translate to increased productivity

**Perspective 2b (Other policies may be better)**

* Exchange rate policy to reduce DD deficient UnN
* Depreciate (zero-appreciation) of SGD 🡪 FPx falls, Pm increases 🡪 Increase in price competitiveness of exports and domestically produced goods 🡪 (X-M) increases 🡪 AD increase 🡪 increase DD for Labour 🡪 Fall in DD-Def UnN
* (Will also be accepted) Modest and gradual appreciation policy to ensure price stability 🡪 attract FDI 🡪 link to AD/AS
* Explore new export markets through more bilateral/regional trade agreements with new trading partners, in view that “Chinese companies are increasingly sourcing from within the country” (Extract 3) 🡪 link to AD/AS

**Evaluation**

Depends on the root cause of the problem. If S.UnN (which is likely to be the most significant cause of UnN in SG) 🡪 SSP will be better as it addresses the root cause of the problem.

But if UnN is both DD-def and structural, and noting the importance of mindset change and longer time frame for SSP to take effect, may need to combine with depreciation in the SR to boost exports competitiveness and increase AD to reduce UnN, while implement SSP to build improve labour mobility and build capacity for the SG economy to deal with disruptive changes and shifting trade flows.