

### Essay Q4

- (a) Explain the possible causes of an increase in the average standard of living in a country [10]  
(b) Assess whether high sustained growth rate should be the main macroeconomic objective of the Singapore government. [15]

### SUGGESTED ANSWER MODEL

#### Introduction

SOL consists of both material and non-material well-being. Hence, an increase in average SOL could arise from an increase in material well-being and/or an increase in non-material well-being. The possible causes of an increase in average standard of living in a country is an increase in aggregate demand and an increase in aggregate supply.

#### Development 1: Increase in AD, increases national output, results in actual economic growth and increases in material well-being

**[Explain material well-being]** Material well-being is determined by the quantity of goods and services that is consumed by the people in an economy. It is usually measured by real GDP per capita, where an increase in real GDP per capita would indicate that material well-being in an economy has increased.

**[List the components of AD]**  $AD = C + I + G + X$ , an increase in any of the components of AD will result in actual economic growth, assuming spare capacity in the economy. For example, a fall in interest rates due to an expansionary monetary policy will impact the cost of borrowing and increases  $I$ .

AD in the economy will thus increase resulting in a rightward shift in the AD as seen in fig 2.

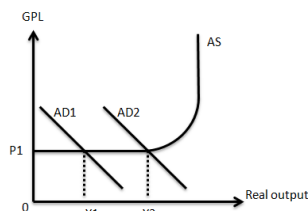
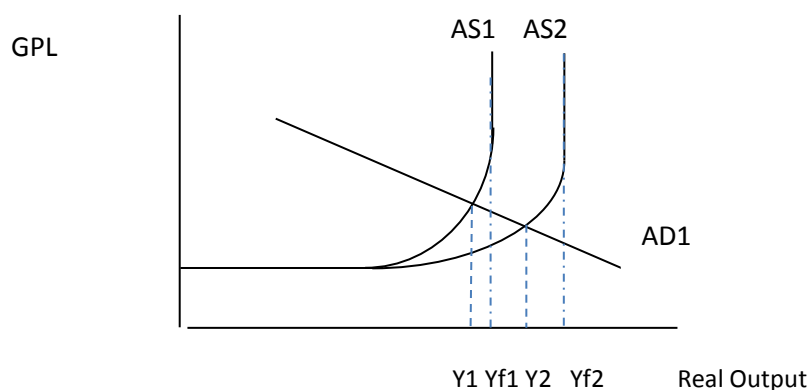


Fig 2: Increase in AD leading to actual growth.

There is an increase in real GDP, and assuming no change in population there will be an increase in national income per head in the economy. This indicates a rise in purchasing power of the average individual which allows him to consume a greater quantity of goods and services thus improving the material well-being.

#### Development 2: Increase in AS, increases productive capacity, results in potential economic growth and increases in material well-being

An increase in AS is caused by an increase in quantity and quality of resources. E.g. an increase in AS can be due to an increase in government spending on education in the economy. Education & training increases the skills of labour, leading to increases in labour productivity. The long run effect is the productive capacity of the economy increases and AS shifts right from  $AS_1$  to  $AS_2$ . The full employment level of output increases from  $Y_{f1}$  to  $Y_{f2}$ . Education and training promotes potential growth. There is an increase in real GDP to  $Y_2$  and hence increase in material SOL, c.p.



**Evaluation** : While AS increases in the long term – actual growth and hence SoL, this can only be realized with increasing and high levels of AD to utilize the productive capacity created by the rightward shift of AS.

### **Conclusion**

An increase in either material or non-material well-being, or both can result in an increase in average SOL in a country.

**[Conflict]** However, in some economies, an improvement in material well-being has led to a worsening of the non-material well-being. For example, high economic growth in an economy as a result of greater production in the economy, may bring with it a higher level of pollution in the economy. This negatively impacts the health and well-being of people in the economy resulting in a fall in material-being. Overall, the improvement in average SOL may be reduced or average SOL may have fallen. [\[link to part \(b\)\]](#)

**(b) Assess whether high sustained growth rate should be the main macroeconomic objective of the Singapore government. [15]**

#### **Intro**

Econ growth can be measured using changes in the real GDP in an economy. A growth rate of more than 3% can be considered high growth rates.

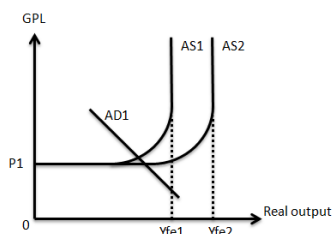
**Thesis: High growth rates are should be the main economic objective to an economy as (i) there are advantages of high growth including improvement in SOL and (ii) potential link to attainment other economic goals**

**[Explain Growth and impact on material SOL]** High growth rates means that the economy is experiencing large actual growth which is one of the macroeconomic goals in the economy. As mentioned in part (a) of the essay, this means that there is an increase in the material well-being of an economy, ceteris paribus.

**[Evaluation – encourage investment and additional impact on potential growth]** High growth rates may result in an improvement in consumer confidence and optimistic expectations for the future.

Consumers thus are more willing to spend, raising consumption. This impacts business confidence and there will be a rise in the volume of investment.

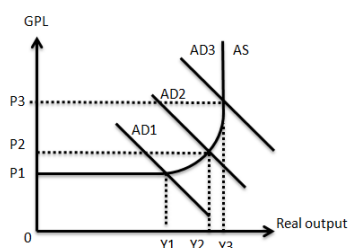
A rise in  $I$  in the SR fuels further growth and more importantly, in the LR, due to an increase in quantity of capital goods, will result in potential growth. This is illustrated by a rightward shift of the AS curve which implies a rise in productive capacity in the economy.



**[Evaluation]** High econ growth may be a result of greater openness to trade which can result in greater structural UE. Due to mismatch of skills of the labour, sunset industries in which the country may no longer have CA in will not be able to move to sunrise industries where demand for labour is increasing due to greater demand for their exports. This results in some labour being structurally unemployed.

**Anti-thesis:** There are some instances whereby high growth rates should not be the main economic objective because (i) there are disadvantages of high growth including worsening non-material well-being and hence SOL and (ii) potential conflicts with other macroeconomic goals

**[Conflicts - Inflation]** Experiencing actual growth may impact an economy negatively through higher demand pull inflation. High growth rates are likely to be due to large increases in the AD in the economy. If at a point of excess spare capacity, this can result in growth without changes in the GPL. However, if sustained over time with little or no change in productive capacity, it may eventually result in demand pull inflation in the economy.



Inflation may be considered to be the main economic objective due to impact on the cost of living of people in the economy. Furthermore, large & unpredictable changes in the GPL can negatively impact business confidence in the economy as it raises the cost of business decisions. Lastly, rising price levels may impact the price competitiveness of trade reliant economies which reduces the export competitiveness.

**[Worsen inequity]** Higher growth rates may result in greater income inequality.

Along with increased economic growth, economies will face an issue of rising income inequality where the income gap between the rich and the poor widens resulting greater social tension. This may be because the increase in real GDP is attributed to the minority rich in an economy and thus the widening income inequality suggests a disparity in the level of SOL among the people. This means that a majority of the people have not experienced a rise in material SOL or worse, a fall in material SOL.

**[Reduces non-material SOL]** As mentioned in part (a), a rise in econ growth may lead to a fall in non-material SOL. Economic growth achieved at the expense of environment damage or negative externalities that are unaccounted for in the GDP figures. Growth incurs environmental costs as in the course of production, non-renewable resources such as primary fuels are heavily used, causing greater carbon emissions and the contribution towards global warming.

Evaluation : While governments may be able to address this issue by redistributing income through transfer payments or better subsidized facilities for the poor, this policy option has varying outcome for different economies

**Address the question of 'high' rates of growth.**

**Reasoned Conclusion : Address the direction word 'Assess'**

High growth is 'should be the main economic objective' due to the many positive impacts on the economy and SOL, but it is not always should be the main economic objective as there are also some negative impacts.

**[Do the costs outweigh the benefits?]**

Whether high growth rates are overall should be the main economic objective depends if the benefits outweigh the costs or vice versa. This in turn is dependent on the nature of the economy. Some developing economies are aiming for high growth rates even if it means lower non-material SOL. This suggests that the govt or people value the positive impacts that economic growth brings over the negative impacts on SOL. However, for more developed economies, non-material well-being may be valued as more important to the people and thus high rates of growth may not be should be the main economic objective.

<b>Knowledge, Application, Understanding and Analysis</b>		
<b>L3</b>	Explanation of causes of an increase in average SOL that considers both material and non-material well-being. Two of the causes must be explained analytically.	<b>7-10</b>
<b>L2</b>	Underdeveloped explanation or an answer lacking in scope or rigour.	<b>5-6</b>
<b>L1</b>	For an answer which demonstrates some basic knowledge about SOL without any economic analysis	<b>1-4</b>

<b>Knowledge, Application, Understanding and Analysis</b>		
<b>L3</b>	For an analytical and balanced discussion on whether high growth rates are desirable by referring to the benefits and costs.	<b>9-11</b>
<b>L2</b>	For an analysis of <u>either</u> the benefits <u>or</u> costs <b>OR</b> A description of both benefits and costs.	<b>6-8</b>
<b>L1</b>	An answer which shows some knowledge or merely lists the benefits and costs of high growth rates.	<b>1-5</b>

<b>Knowledge, Application, Understanding and Analysis</b>		
<b>E2</b>	For an evaluative discussion based on economic analysis	<b>3-4</b>
<b>E1</b>	For an unexplained judgement, or one that is not supported by economic analysis.	<b>1-2</b>