

2017 J2H2 Prelim Essay Q6

- 6 While many will argue that globalisation benefits all countries, there are nevertheless some nations that have done better than the rest.

Source: <http://www.livemint.com>, 20 January 2017

- (a) Explain possible reasons that could cause a country to lose its comparative advantage in certain industries over time. [10]
- (b) Discuss whether globalisation brings more benefits than costs to different countries. [15]

Part (a)

Introduction

Define comparative advantage.

Explain that differences in relative opportunity cost explain the differences in comparative advantage in different countries.

A country thus can lose its comparative advantage in industries when there are increases in its opportunity cost as a result of changes in factor endowments and technological changes.

Body- Reasons for loss of CA

Failure to keep pace with advancement in technology

A country may not experience a rapid advancement in technology unlike that of other countries. R&D and technology play key roles in strengthening the comparative advantage. Thus a country that fails to keep up will cause her to lose out in terms of efficiency and productivity. As a result, it experiences a higher cost of production compared to others. Give examples.

Changing natural and human endowments

There are also changing natural and human endowments. Natural resources may get depleted over time and the country will lose its comparative advantage in these industries if it is not able find substitutes to maintain its comparative advantage. Give examples such as depletion of crude oil.

Human endowments such as the quantity and quality of labour can also change with time. A country can experience a fall in the quantity of labour due to falling population growth or changes in a government's migration policy. This results in shortage of labour which leads to rise in wages. Quality of labour can also fall as a country's education system fails to keep up with that from other countries. As a result cost of production rises causing OC to rise.

Globalization

Globalization has resulted in greater flow of trade, foreign direct investment and migration among countries. With the interconnectedness, it becomes relatively easier for certain industries in an economy to tap on the transfer of knowledge, skills, technology to lower the opportunity cost of production. However countries may also face greater competition with globalization causing them to lose their CA.

Government policies

Lastly, government policies can enhance or worsen the comparative advantage that a country has. Government policies such as increasing corporate tax or removing tax incentives or changing labour policies to reduce immigration and employment of foreign workers can also cause a country to lose its comparative advantage.

Part (b) Discuss whether globalisation brings more benefits than costs to different countries. [15]

Introduction

- ❖ Globalisation refers to the increased integration of national economies into the international economy through greater trade, foreign direct investment, capital flows, migration, and the spread of technology.
- ❖ There are potential benefits of globalization and this varies from country to country. However, there are also costs to everyone too. The extent whether benefits is more than costs depends on the characteristics of the economies. It also depends on the conditions in the economy and the mitigation policies that governments put in place to reduce the costs.

Body: Gains

Trade and its benefits to producers

- ❖ Globalisation leads to the expansion of export markets according to the Theory of Comparative Advantage. Elaborate
- ❖ Benefits is larger for small countries which are dependent on trade for growth.
- ❖ Benefits from increase in employment is larger for less developing countries producing labour-intensive goods.

- ❖ Globalization also provides more opportunities for sourcing cheaper and better quality imports from other countries. Cheaper imports will help to curb imported inflation.
- ❖ Benefits from cheaper and greater variety of import is very important for small countries such as Singapore as she lacks natural resources and is dependent on imports. Impact is larger for small countries which are dependent on trade for growth.

Capital flows

- ❖ Globalisation encourages both long-term and short-term capital flows across countries. The inflow of foreign direct investment (FDI) into a country creates job opportunities and results in a multiplier effect on the national income, achieving actual economic growth. The increase in capital stock increases productive capacity, LRAS and brings about potential economic growth and benefit society.
- ❖ The inflow of short-term capital enables local firms to gain access to foreign funds for their businesses. They may also be able to borrow at a cheaper rate with the abundance of foreign funds.
- ❖ Impact is large for a small and developing country which is dependent on FDI.

Labour

- ❖ With a freer movement of labour, smaller economies like Singapore with limited manpower are now better able to utilize workers from other economies to fill up the vacancies requiring a lower level of skills. The greater labour mobility due to globalisation can help a small country overcome its constraint of a small local labour force to attain economic growth.
- ❖ Impact is large in a small country which lacks labour. Developed countries however may experience more brain drain as the highly skilled workers leave to the developing countries which lack such manpower.

Costs

Structural unemployment

- ❖ However, globalization also has its costs. As the comparative advantage of countries changes over time, some industries like call center services start to move out from high-cost to low-cost countries. This will result in structural unemployment
- ❖ Impact might be large for countries where there is less policies to address such structural unemployment. Problem may also be larger for developed countries that experience a loss of CA of their labour-intensive products to the less developing countries.

Income gap

- ❖ The influx of low-skilled foreign workers into a country also tends to compete with the low-skilled local labour. The increase in the overall supply of low-skilled labour tends to reduce the wages of these workers. On the other hand, the increase in demand for high-skilled labour relative to the limited supply raises their wages. Thus, income disparity problem tends to worsen.

Vulnerable to external shocks

- ❖ As countries become more interconnected and integrated, small and open economy like Singapore tends to be more vulnerable to external shocks due to the contagion effect.
- ❖ Small open export oriented economies such as Singapore with a large trade sector (as a % of GDP) are more vulnerable to such threats.

Conclusion and evaluation

Stand and Justification

- Depends on characteristics of economy
- Depends on the policies that are used to mitigate the costs of globalisation.

Marking Scheme for Part a

Level	Knowledge, Application, Understanding, and Analysis	Marks
L3	Well-developed analytical explanation of the factors that leads to loss of CA.	7 – 10
L2	Descriptive explanation of the factors that leads to loss of CA.	4 – 6
L1	For an answer that shows descriptive knowledge of the factors that leads to loss of CA.	1 – 3

Marking Scheme for Part b

Level	Knowledge, Application, Understanding and Analysis	Marks
L3	For a well-developed explanation of the benefits and costs of globalisation and its extent in different countries.	8 – 11
L2	For a descriptive explanation of the benefits and costs of globalisation as well as compares the extent for different types of countries.	5 – 7

L1	For an answer that shows a descriptive knowledge of benefits and costs of globalisation.	1 – 4
Level	Evaluation	Marks
E2	For an evaluative assessment which weighs the benefits and costs of globalisation to arrive at well-reasoned judgement.	3 – 4
E1	For an answer that makes some attempt at an evaluative weighing of the benefits and costs of globalisation in different countries.	1 – 2