Globalisation

Globalisation = Growing economic interdependence of countries worldwide through increasing volume and variety of cross-border transactions, largely in goods and services, free flows of international capital (i.e. FDI), spread of technology as well as labour migration.
FDI = Movement of capital that involves foreign ownership and control of production facilities
Migration = Movement of people from one country to another country

Long-term measures to improve global competitiveness
Global competitiveness = Export competitiveness + Ability to attract FDI + Ability to attract foreign talent/skilled labour

1. Exchange rate policy: Modest gradual appreciation
    - How it works:
        - Achieve low, stable inflation
            - Moderate ↑ in AD
            - Moderate imported inflation
        - Superior management of inflation helps to form expectation of low, stable inflation ⇒ Avoid wage-price spiral ⇒ Relatively lower rates of inflation compared to trading partners ⇒ ↑ Price competitiveness of exports in long term ⇒ ↑X in long term
    - Limitations:
        - Lose price competitiveness in the short term ⇒ ↓AD ⇒ ↓ real NY ⇒ Compromise AG + ↑UnN + Worsening BOP
2. Supply side policies
    - Improve human capital
        - e.g. Skillsfuture, promotion of lifelong learning
        - How it works:
            - ↑ Quality/productivity of labour + ↑SS of skilled labour ⇒ ↑ Export competitiveness (↑ quality + ↓ COP) + ↑ ability to attract FDI (more conducive to do business)
        - Limitations:
            - Loss of man hours esp if there is already shortage of labour in times of economic boom
            - High costs to company esp in times of recession
            - Takes a long time to come into effect
            - Depends on receptiveness of workers to new skills
    - Subsidise R&D/Research grants
        - How it works:
            - ↑ subsidies/tax incentives for firms to engage in R&D ⇒ ↑ incentive to conduct R&D
            - ↑R&D ⇒ ↑ technology level if successful ⇒ ↑ quality of products/New innovative products/More efficient production

        methods (↓COP ⇒ ↓P) ⇒ ↑ export competitiveness
    - Attract foreign talent in research by providing research grants
  - Limitations:
    - Expensive
    - Uncertain outcome of R&D
    - Takes a long time
- Improve infrastructure
  - e.g. Transport system
  - How it works:
    - Firms can reap eEOS ⇒ ↓ COP ⇒↓P ⇒ ↑ export competitiveness
    - Foreign firms attracted to conduct FDI
  - Limitations:
    - Expensive to build and maintain
      - e.g. Port of JB → Originally very competitive due to low prices but poor maintenance ⇒ No longer competitive
    - Takes a long time

3. Signing more FTAs with more countries
   - How it works:
     - Lower/Remove barriers to movement of G&S (e.g. Remove tariffs)
     - (Draw tariff diagram) ↓ Price of exports in foreign market from $P_{world+tariff}$ to P_{world} ⇒ ↑ price competitiveness of exports compared to their domestic goods ⇒ ↑Qd by foreign consumers + ↓Qs by foreign producers ⇒ Domestic firms replace loss in production by selling more exports ⇒ ↑Qx ⇒ ↑ profits
   - Limitations:
     - Trade diversion - Shift in trade from a lower cost non-member country to a higher-cost member country ⇒ Move away from Theory of CA ⇒ ↓ allocative efficiency
4. (For Singapore) Tripartite relationship between firms, workers and govt
   - How it works:
     - Manage wage negotiations and labour relations
       - Paces wage increments to labour productivity ⇒ Ensures that wages remain competitively priced ⇒ Attract foreign firms to conduct FDI
       - Flexible wages through incorporation of variable components into wage package
         - e.g. Year-end bonuses
         - Deals with price rigidity of wages → Enables firms to reduce wages in times of recession ⇒ Firms can reduce wages rather than shutting down ⇒ Attracts foreign firms as most other countries do not have flexible wages

Trade Policy (i.e. Sign FTAs with many countries)
Benefits: Trade Creation

- Signing FTAs with more efficient producers leads to shift in trade from a less efficient producer (usually already a member country) to a more efficient member country (recent)
- Based on Theory of CA ⇒ ↑ welfare gains due to ↑ allocative efficiency

Other benefits mentioned in international trade

Costs: Trade Diversion

- Signing FTAs with less efficient member country while tariffs imposed on most efficient non-member country ⇒ ↓P_M of member country to below $P_{M+tariff}$ of most efficient producer ⇒ Diversion of trade away from most efficient producer to less efficient member country due to lower prices to domestic consumers ⇒ More resources allocated to less efficient producer ⇒ On a global scale, this represents a waste of resources
    - Loss of tariff revenue

Developing Countries - Recipient of FDI, Source of Labour

	Advantages	Disadvantages
Labour	Remittances • ↑GNP ⇒ Labour that find jobs in developed countries may remit a portion of their income back to their home country ⇒ {Support their family ⇒	Brain drain • Movement of skilled labour to developed countries due to higher wages ⇒ {↓ productive capacity ⇒ ↓AS} + {↓ ability to develop higher value adding industries to improve terms of trade} Dutch Disease • Inflow of remittances ⇒ ↑ DD for domestic currency ⇒ Appreciation of domestic currency ⇒ ↑Px + ↓Pm ⇒ … (MLC) ⇒ ↓(X-M) ⇒ ↓AD ⇒ Export industry suffers

		↑mSOL in home country} + {↑ funds for households to start their own investments ⇒ ↑I ⇒ ↑AD + ↑AS} + {Improve current account ⇒ Improve BOP}	Exacerbates Income Inequality • Some industries grow faster than others due to specialisation and international trade ⇒ ↑DD for workers in industries which the country specialises in ⇒ Faster ↑ in wages of workers in industries which the country specialises in compared to other workers ⇒ ↑ Income inequality ⇒ ↑ social tensions ⇒ ↓nmSOL
Goods & Services	↑X • Able to produce for wider international market ⇒ ↑DD for exports ⇒ ↑X ⇒ ↑(X-M), c.p. ⇒ ↑AD + Improve BOP • Dynamic gains from trade • Reap ↑ iEOS and eEOS ⇒ ↓COP ⇒ {↓Px ⇒ ↑ export competitiveness} + ↓AS ↑ world output and consumption of G&S • ↑ Availability of goods and services that can be consumed due to Theory of Comparative Advantage ⇒ Trade allows a country to ↑ consumption of G&S to previously unattainable levels (outside the PPC) ⇒ ↑mSOL		Susceptible to external shocks • Vulnerable to DD-pull inflation in economic boom • Vulnerable to externally-induced cyclical UnN and ↓ real NY due to economic recession Worsening BOP • ↑M as domestic firms less competitive in terms of quality and poor terms of trade as they produce low value added goods ⇒ ↓(X-M), c.p. ⇒ Worsening BOP

	• ↑ Consumer choice ⇒ ↑ availability of higher quality goods and services ⇒ ↑mSOL	
	↑AD • ↑ funds for investments ⇒ ↑ I ⇒ {↑AD ⇒ m.t.p. ↑ real NY + ↓ cyclical UnN} + {↑ capital formation ⇒ ↑ productive capacity ⇒ ↑AS} ⇒ Sustained economic growth with low inflationary pressures ◦ ↑ corporate tax revenue • ↑ export oriented foreign firms ⇒ ↑X ⇒ ↑(X-M) c.p. ⇒ Improve BOP + ↑AG + ↓ cylcical UnN	**Crowding out • MNCs require land, resources and labour ⇒ Compete with domestic firms for scarce resources in the host country ⇒ Drives up factor prices ⇒ ↑COP for domestic firms + ↑ inflation ⇒ May drive out domestic firms if domestic firms unable to earn at least normal profits in the LR due to ↑COP **Instability in ER and BOP • Capital flows as MNCs constantly seek to move capital to maximise profits + ↑ imports of factor inputs + ↑ Repatriation of profits ⇒ Volatile ER and BOP ⇒ Difficult for long term planning Negative externalities (pollution) • Poor environmental regulation of activities of foreign investors by recipient country ⇒ Foreign investors may relocate pollutive industries

FDI	↑ Productivity • {Transfer of technology from developed to developing countries ⇒ ↑ technology level} + ↑ technical and managerial expertise ⇒ ↑AS (↓COP + ↑ productive capacity) ↑ Skill level of workers • ↑ Training of workers by foreign firms ⇒ Quality of labour force ⇒ ↑ productivity of workforce ⇒ ↑AS (↑ productive capacity + ↓COP assuming ↑ wage rates < ↑ productivity) Improve BOP (financial account) mSOL • ↑DD for workers ⇒ ↓UnN + ↑ wages for all workers in the country ⇒ ↑mSOL of local workers	to these countries ⇒ Destruction of environment ⇒ Negative externalities ⇒ ↑ allocative inefficiency Exacerbates Income Inequality (creates dual economy) • ↑ Income inequality as ↑ wages of workers demanded by foreign firms but the rest of the domestic sector remains poor ⇒ ↓ social cohesion • ↑ monopoly power of foreign firms as they outcompete domestic firms Monopoly of domestic market • Foreign firms enjoy large iEOS + large reserves of previous supernormal profits ⇒ Able to offer lower prices than domestic firms ⇒ Drives out domestic firms of the industry ⇒ ↑ market power of foreign firm ⇒ Country may become over-reliant on foreign firms + ↑ allocative inefficiency + Exacerbates income inequality as small firms forced out of the market Dutch disease • Inflow of FDI ⇒ ↑ DD for domestic currency ⇒ Appreciation of domestic currency ⇒ ↑Px + ↓Pm ⇒ …

		(MLC) ⇒ ↓(X-M) ⇒ ↓AD ⇒ FDI industries grow but the rest of the exports suffer

Developed Countries - Source of FDI, Recipient of Labour

	Advantages	Disadvantages
Labour	↑AS (productive capacity + COP) • Inflow of foreign talent ⇒ ↑ quantity + quality of labour ⇒ {↑ productive capacity ⇒ ↑AS} + ↑ ability to develop higher value adding industries to improve terms of trade • Inflow of foreign labour ⇒ ↑ SS of labour ⇒ {↓ wages ⇒ ↓ cost-push inflation} + {↑ productive capacity ⇒ ↑AS} ↑AD • ↑ population ⇒ ↑ autonomous C as immigrants have to consume necessities regardless of income	**Exacerbates Income Inequality • Inflow of foreign labour that are willing to accept lower wages ⇒ Depresses wages for domestic unskilled labour • On the other hand, ↑ global DD for high skilled workers ⇒ ↑ wages for high skilled workers ⇒ ↑ income inequality • If domestic labour unwilling to accept such low wages, may lead to ↑UnN of domestic unskilled labour ⇒ Mismatch of skills as unskilled labour unable to move over to higher value added industries ⇒ Structural UnN • e.g. Singapore Gini coefficient in 2015 was high at 0.463 or 0.410 after government transfers and taxes Social Costs • ↑ Immigration ⇒ Drain on government resources and country's infrastructure + {↑ external costs due to ↑ population growth ⇒

	level ⇒ ↑AD ⇒ m.t.p. ↑ real NY via multiplier effect	overcrowding ⇒ Social unrest} DD-pull inflation • ↑C ⇒ ↑AD ⇒ If ↑AD > ↑AS due to inflow of labour ⇒ Overheating economy ⇒ ↑GPL ⇒ Inflation • e.g. Singapore's car and housing prices
	Stand to gain more from specialisation and trade due to higher TOT • Comparative advantage in high value added goods and services due to higher supply of skilled labour + higher level of technology ⇒ Specialisation and export of these goods ⇒ Superior TOT, c.p. ⇒ ↑X > ↑M ⇒ ↑(X-M) with free trade ⇒ ↑AD ↑X • Able to produce for wider international market ⇒ ↑DD for exports ⇒ ↑X ⇒ ↑(X-M), c.p. ⇒ ↑AD + Improve BOP • Dynamic gains from trade • Reap ↑ iEOS and eEOS ⇒ ↓COP ⇒ {↓Px ⇒ ↑ export competitiveness} + ↓AS ↓ Inflation	Structural Unemployment • **Loss of CA in labour intensive industries ⇒ ↓DD for these goods ⇒ ↓ Production ⇒ ↓DD for unskilled labour ⇒ Mismatch of skills as unskilled labour unable to move over to higher value added industries ⇒ Structural UnN

Goods & Services	• ↑ Access to relatively cheaper imported goods + {imported raw materials ⇒ ↓COP ⇒ ↑AS} ⇒ Moderates inflation • Domestic producers exposed to foreign competition ⇒ ↑ competition ⇒ ↓ Market dominance of domestic producers + ↓ Complacency ⇒ ↓P + ↑ quality + ↓ X-inefficiency ⇒ Moderates inflation ↑ world output and consumption of G&S • ↑ Availability of goods and services that can be consumed due to Theory of Comparative Advantage ⇒ Trade allows a country to ↑ consumption of G&S to previously unattainable levels (outside the PPC) ⇒ ↑mSOL • ↑ Consumer choice Others • Cheaper option for lower income earners ⇒ ↑mSOL for this group • Dynamic gains from trade • Reap ↑ iEOS and eEOS ⇒ ↓COP ⇒ {↓Px ⇒ ↑ export competitiveness} + ↑AS	Worsening BOP • Opp cost of producing labour intensive goods and services is lower in developing countries than in developed countries ⇒ Based on Theory of CA, developing countries should specialise in these G&S and trade with developed countries ⇒ Developed countries import cheap G&S from developing countries ⇒ ↑M ⇒ ↓(X-M), c.p. ⇒ Worsening current account ⇒ Worsening BOP Susceptible to external shocks • Vulnerable to DD-pull inflation in economic boom • Vulnerable to externally-induced cyclical UnN and ↓ real NY due to economic recession

FDI	Repatriation of Profits - Outsourcing of production for domestic firms to foreign countries ⇒ ↓COP ⇒ ↑ profitability of the firm ⇒ ↑ profits for the firm - Repatriation of profits ⇒ Improve BOP (current account) in LR + ↑GNP Economic Growth - Stimulates exports of capital goods as subsidiaries set up overseas require capital equipment and factor inputs from the source country ⇒ ↑X ⇒ ↑AD ↑ employment + income in recipient country ⇒ ↑ purchasing power ⇒ ↑ consumption of G&S including M from source country = ↑X from source country	↓AD - If FDI to set up production plant in foreign country in order to directly supply exports through the plant without passing through source country ⇒ ↓X - If production plant in labour intensive industry set up in labour abundant country with lower COP, source country may have to import the goods produced in the foreign production plant ⇒ ↓M ↓(X-M) ⇒ Worsening BOP + ↓AD ↓ corporate tax revenue Structural Unemployment - Outsourcing of production ⇒ ↓DD for labour in domestic country ⇒ Structural UnN BOP - Worsening financial account in SR due to outflow of FDI

Other Benefits
<u>Labour</u>

- Equalisation of wages between countries → Originally average wage rates higher in developed countries and lower in developing countries ⇒ Workers in developing countries respond to the difference in wages by migrating to the developed countries ⇒ ↓SS of labour in developing countries and ↑SS of labour in developed countries ⇒

↑ wages in developing countries and ↓ wages in developed countries
    - Assumes that labour is homogenous and mobile
- ↑ world output → {Developing country has lower demand for labour and hence lower wages due to lower productivity of labour ⇒ Outflow of labour from developing country results in smaller reduction in output compared to increase in output from immigration of workers into developed country} + ↓ Geographical factor immobility between countries ⇒ ↑ world output

Anti-globalisation policies

FDI

Measures:

- Capital controls → Prevent FDIs from withdrawing capital within a given time period ⇒ Curbs capital outflow when FDI relocates to other countries ⇒ Ensures relative stability of country's BOP and exchange rate
- Impose quotas and issue fewer licenses to MNCs to operate in host country
- Provide subsidies to domestic firms to help them lower their costs of production so that they can survive and compete with the MNCs
- Set up more stringent environment controls and only issue licenses to foreign firms that set up factories that do not pollute the environment

Limitations:

- ↓ Inflow of FDI in LR ⇒ Worsen financial account in the LR
    - Capital controls deter MNCs from conducting FDI into the country as it makes it difficult for them to take steps to ensure the value of their profits or pull out of the country quickly in the case that the country is facing a major recession
- ↓ funds for I ⇒ ↓I ⇒ ↓AD ⇒ m.t.p. ↓ in real NY via reverse multiplier process + ↑ cyclical unemployment since labour is a derived demand ⇒ ↓mSOL in the country
- ↓I ⇒ ↓ Capital formation ⇒ ↓ productive capacity in the LR ⇒ ↓PG ⇒ ↓ future mSOL

Labour

Measures:

- Anti-immigration policies → Tighter control over immigration by imposing labour quotas to restrict inflow of labour + ↑ foreign worker levies to ↑ cost of hiring foreign workers ⇒ ↓SS of labour ⇒ ↑ wages of low-skilled workers ⇒ ↓ income inequality ⇒ ↓ social tensions

Limitations:

- Restriction on immigration may leave certain types of jobs vacant due to lack of supply of suitable labour in the market
    - Could be due to social stigma ⇒ Locals do not want to take up such jobs
    - Could be due to lack of sufficiently skilled labour ⇒ Locals unable to take up such jobs
- ↓SS of labour ⇒ ↑ wages ⇒ ↑COP for firms ⇒ May deter firms from conducting I ⇒ ↓I ⇒ ↓AD ⇒ m.t.p. ↓ real NY via reverse multiplier
- Also, ↑COP ⇒ ↓AS (upward shift) ⇒ ↑GPL + ↓ real NY

<u>Evaluation</u>

- While protectionist, anti-globalisation policies may be able to bring about economic benefits in the short run, it is likely that in the long run, these policies will worsen the current state of the global economy
- Hence, these measure should only be considered as a temporary measure
- In the long run, supply side policies should be implemented to ensure that the country is able to achieve potential growth and be less affected by the negative impacts of globalisation
    - e.g. Education policies help to improve the skill level of the workforce ⇒ Country will be able to gain CA in high value added industries ⇒ Address loss of CA in labour intensive industries
- However, at the same time it must be noted that social and political pressures to adopt protectionist measures may force the government to adopt anti-globalisation policies against the best interests of the future of the economy, succumbing to populist pressures