

# LOCKIN EDUCATION @ BUGIS



## H2 ECONOMICS



**Link between EG, UnN and Income Inequality. How fiscal policy and exchange rate policy works.**

“The future belongs to those who believe in the beauty of their dreams” -  
Eleanor Roosevelt

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## **Explain the link between economic growth, unemployment and income inequality. [10]**

Basic answer: If AD increase ... AEG + fall in demand deficient unN.

Fiscal policy: [content knowledge] → Cut taxes + increase spending.

The govt can cut personal income tax and corporate tax. When personal income tax fall, increase in disposable income (after tax income), increase in purchasing power, increase in  $w+a$  to consume  $g+s$ , consumption expenditure increase. The govt can also reduce corporate tax, increase after tax profits, increase incentive to invest, increase investment expenditure. The govt can also increase spending on public work projects, increasing govt expenditure.  $C, I, G$  increase → AD increase .... AEG.

In the process of doing expansionary fiscal policy, the increase in AD will also ....DD deficient unN fall.

In the process of fiscal policy, the govt may also increase transfer payments. [Transfer payment IS PART OF FISCAL POLICY!] E.g Singapore gave our CDC/GST vouchers during 2025 and 2026 budgets, this helps to increase the income of the low income group, reduce income gap, reduce income inequality, improve GINI coefficient.

When the government increase its spending on technology as such integrating AI to reduce manpower and increase efficiency, this will lead to increasing productive capacity, increase LRAS, achieving PEG.

When there is an improvement in technology, there will be a shift in the economy, workers in the manufacturing sector will be made redundant and retrenched, lack relevant skills to be employed in sunrise industries like AI despite jobs available, skills mismatch, structural unemployment increase.

When there is a shift in tech, DD for low skilled labour fall, wage fall, DD for high skilled labour like those proficient in tech will increase, wage increase, income gap increase, income inequality worsens.

Common mistake: if unemployment increase, more people lose jobs, loss of income, fall in PP, fall in W+A to consume  $g+s$ , fall in C exp, fall in AD [NOT CORRECT!!] → AD cannot increase/decrease via income. If income affects AD, it is INDUCED CONSUMPTION → subsequent effects in multiplier effect, cannot be a starting point.

Better answer: if unN increase, poor economic outlook, fall in C/I investors, fall in C and I exp, fall in AD.

## Explain the possible causes of balance of trade deficit. [10]

BOT deficit means  $(x-m)$  negative, must explain how  $X$  fall,  $M$  increase.

R1: high domestic inflation. Price of  $g+s$  increase, that includes export. When  $P_x$  increase,  $PED_x > 1$  assume many substitutes (MUST USE PED NOT DD AS DD IS AFFECTED BY NON PRICE), qty  $dd$  will decrease more than proportionately,  $TR_x$  decrease. When domestic goods are more expensive, domestic consumers will switch to imports to seek for cheaper alternatives, hence  $DD$  for imports will increase (DD NOT PED, BECAUSE PRICE OF IMPORT DID NOT CHANGE),  $TE_m$  increase.  $(X-m)$  fall, BOT worsens.

OR USE APPRECIATION. (but choose one as inflation and appreciation have similar analysis)

**[Content to memorise]** Appreciation

Price of exports will increase in foreign currency, assume many subs,  $PED > 1$ , qty  $dd$  fall more than proportionately,  $TR$  for export fall.

Price of imports will fall in domestic currency, assume many subs,  $PED > 1$ , qty  $dd$  will increase more than proportionately,  $TE$  for imports increase,  $(x-m)$  falls, BOT worsens.

R2: If the quality of  $g+s$  produced domestically worsens, trading partners may shift taste and preferences away from domestic country,  $DD$  for exports fall,  $TR_x$  fall. Domestic consumer will not want domestic goods, choose to buy higher quality imported goods,  $DD$  for imports increase, total expenditure for imports increase.  $(x-m)$  fall, BOT worsens. [Chinese consumers may prefer imported EVs like Tesla instead of domestically produced EVs due to safety reasons]