

Fiscal Policy Vocabulary



Since we decided to adopt the leaf as legal tender, we have all become immensely rich. But we have also run into a small inflation problem on account of the high level of leaf availability. In order to obviate this problem and effectively revalue the leaf, we are about to embark on a massive defoliation campaign and burn down all the forests.

I think you'll all agree that's a sensible move under the circumstances.

Douglas Adams, *Ultimate Hitchhiker's Guide to the Galaxy*



Fiscal Policy

...changes government makes in spending or taxation to achieve particular economic goals





Fiscal Policy

- Advantages of Fiscal Policy
 - Can have a significant impact on the economy.
 - Can be discriminating which allows different regions or consumption habits to prosper.
 - Makes the distribution of income fairer through progressive taxes and benefits.
- Disadvantages of Fiscal Policy
 - Can have effects on other areas which were not originally intended ... example: fall in taxes intended to boost consumption but results in consumers buying imports.
 - Time lag is huge with fiscal policy.
 - Some policies – high taxes – might be disincentives to work.

Expansionary Fiscal Policy



...an increase in government spending or a reduction in taxes in order to encourage spending and stimulate a weak economy



Contractionary Fiscal Policy



...a decrease in government spending or an increase in taxes in order to discourage spending and slow down the economy to control inflation

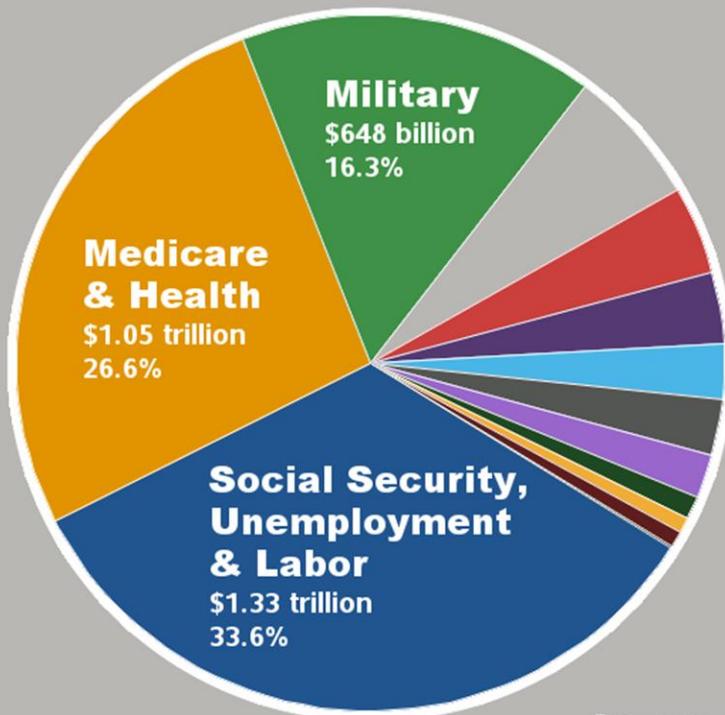




Crowding Out

...a situation in which an increase in government spending leads to higher interest rates and a reduction in private investment

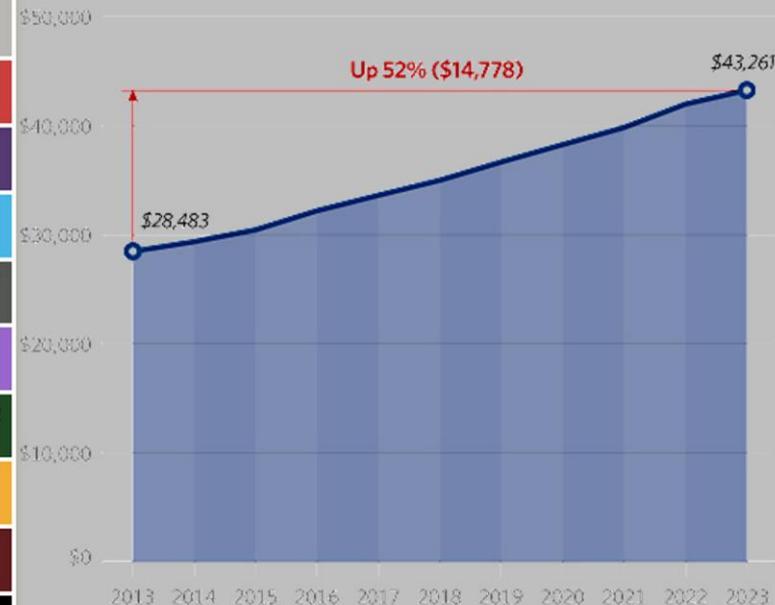
Total Federal Spending 2015: \$3.9 trillion



Interest on Debt	\$251 billion / 6.3%
Veterans Benefits	\$161 billion / 4.1%
Food & Agriculture	\$130 billion / 3.3%
Transportation	\$103 billion / 2.6%
Housing & Community	\$102 billion / 2.6%
Education	\$80.9 billion / 2.0%
Energy & Environment	\$44.5 billion / 1.1%
Science	\$29.3 billion / 0.7%
International Affairs	\$27.2 billion / 0.7%
Government	\$2.7 billion / 0.1%

Federal Spending per Household Will Rise by One-Half in 10 Years

IN CURRENT DOLLARS

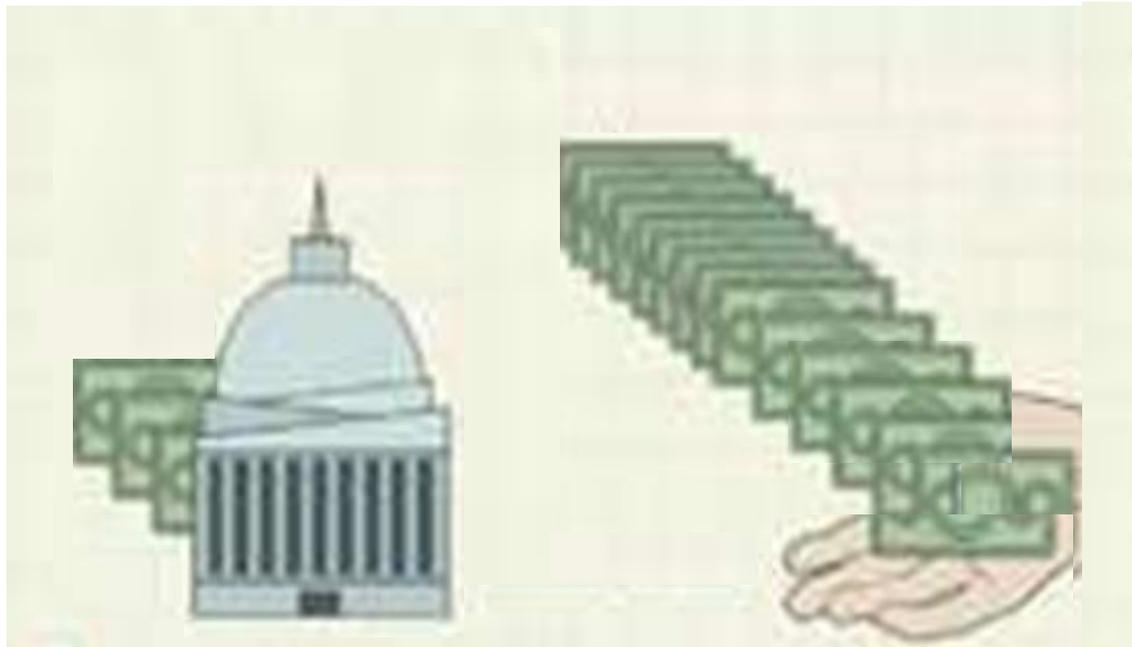


Source: Congressional Budget Office, *Updated Budget Projections: Fiscal Years 2013 to 2023*, May 2013, <http://www.cbo.gov/publication/44172> (accessed May 15, 2013).



Crowding In

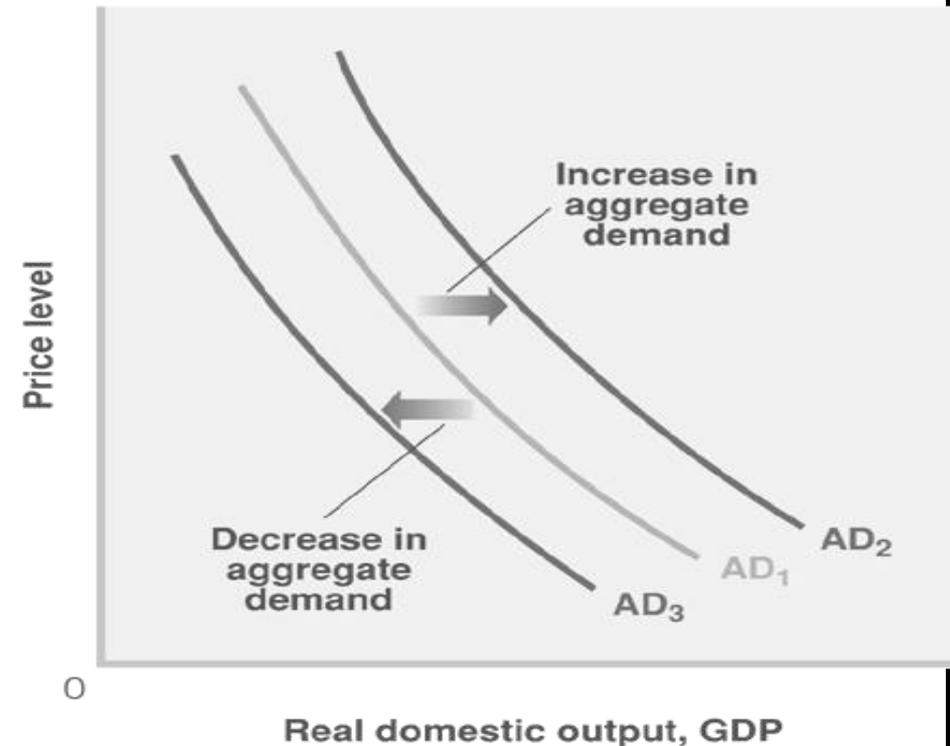
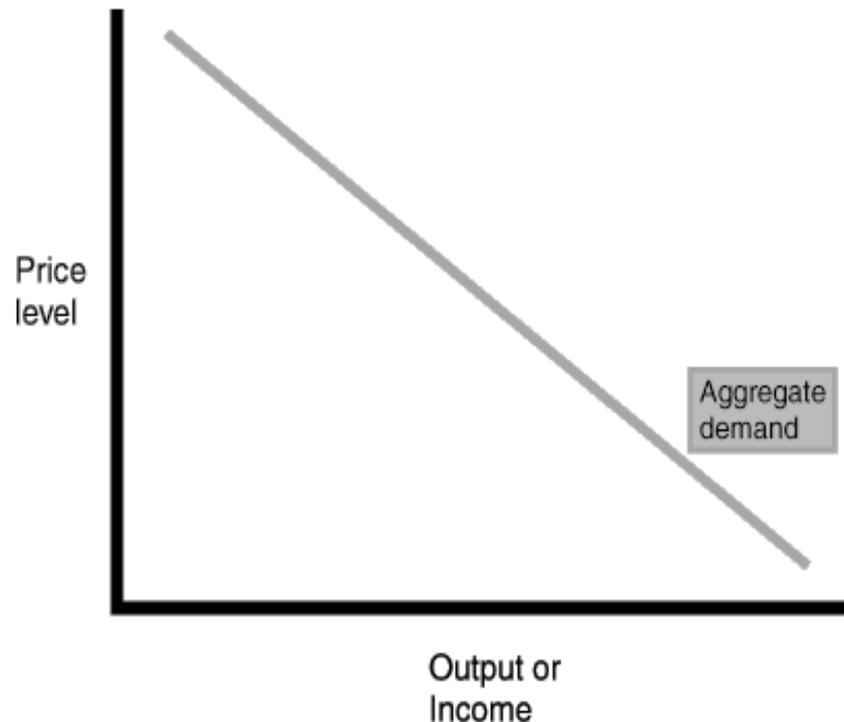
...a situation in which (1) contractionary policy allows for increased private activity in the credit market or (2) a raise in the general level of prosperity leads to an increase in private investment





Aggregate Demand Curve

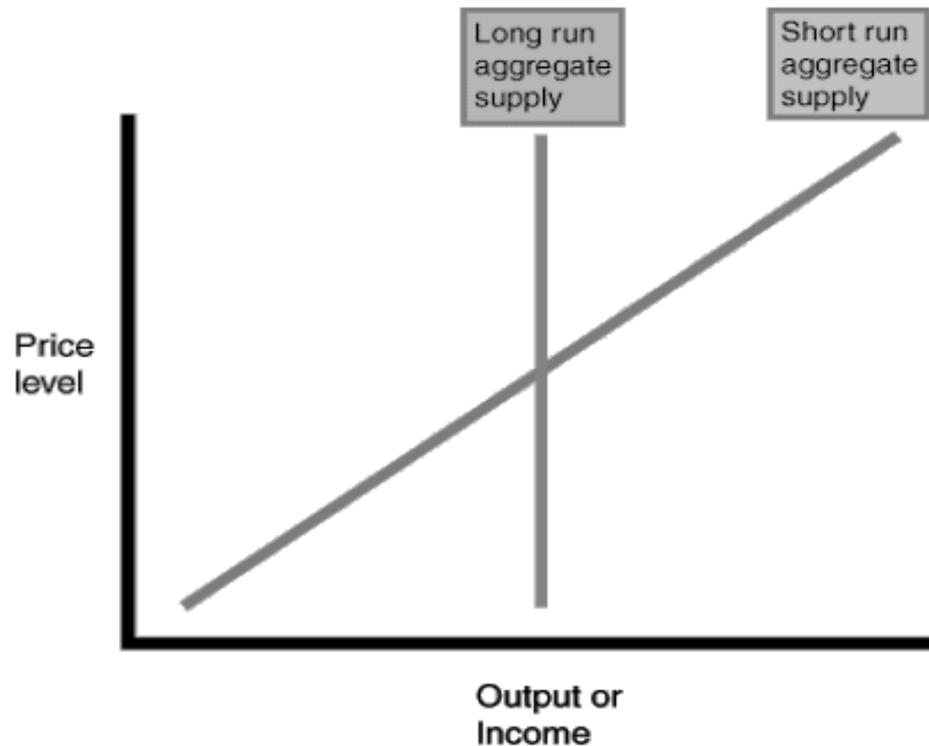
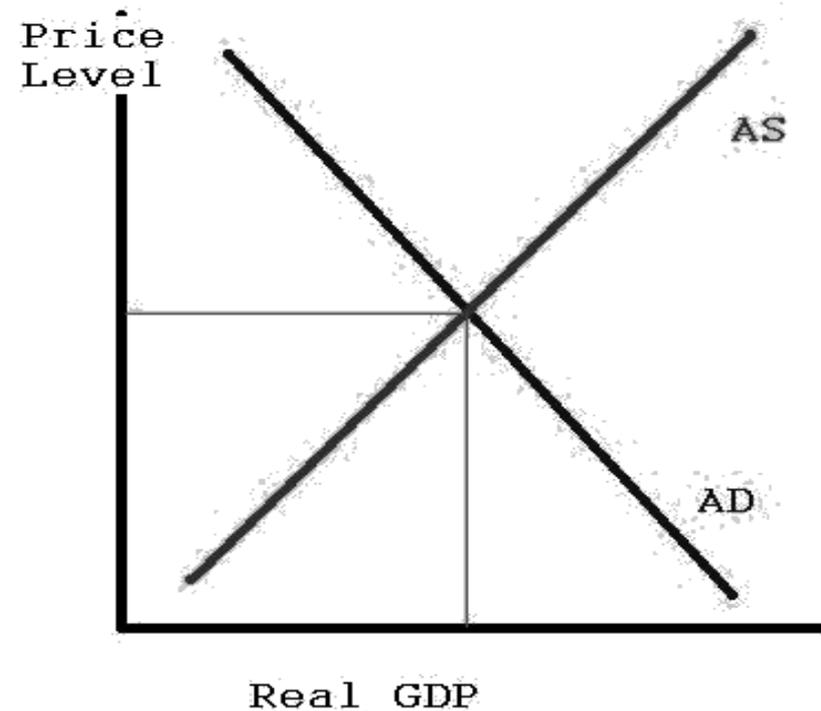
...shows the quantity of goods and services buyers are willing and able to buy at different price levels ... same as demand in microeconomics, but reflects all individual demand





Aggregate Supply Curve

...shows the quantity of goods and services producers are willing and able to supply at different price levels ... same as supply in microeconomics, but reflects all individual supply





The End

