

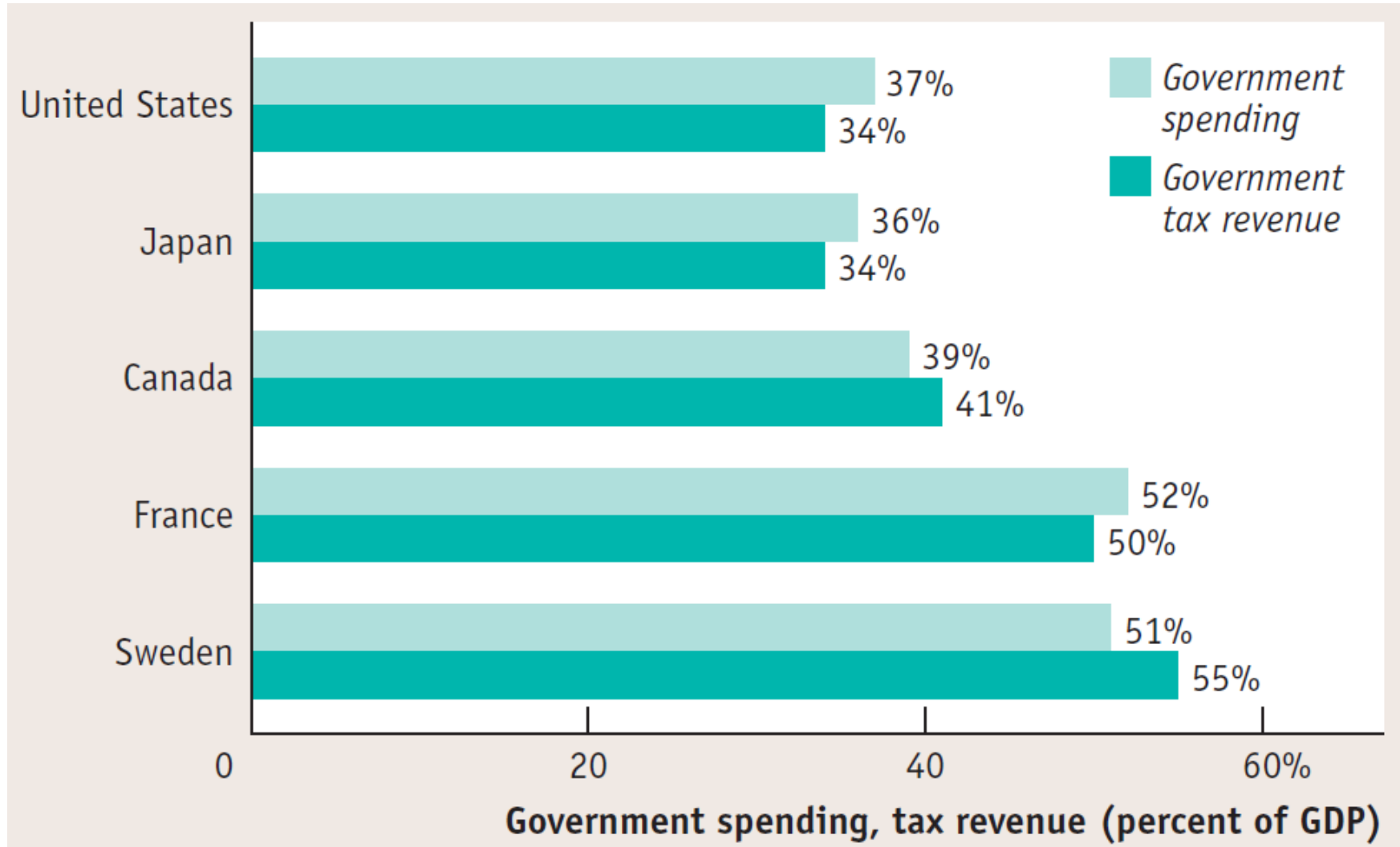
● 30 Fiscal Policy Basics

● 31 Fiscal Policy and the Multiplier

● 32 Budget Deficits and Public Debt



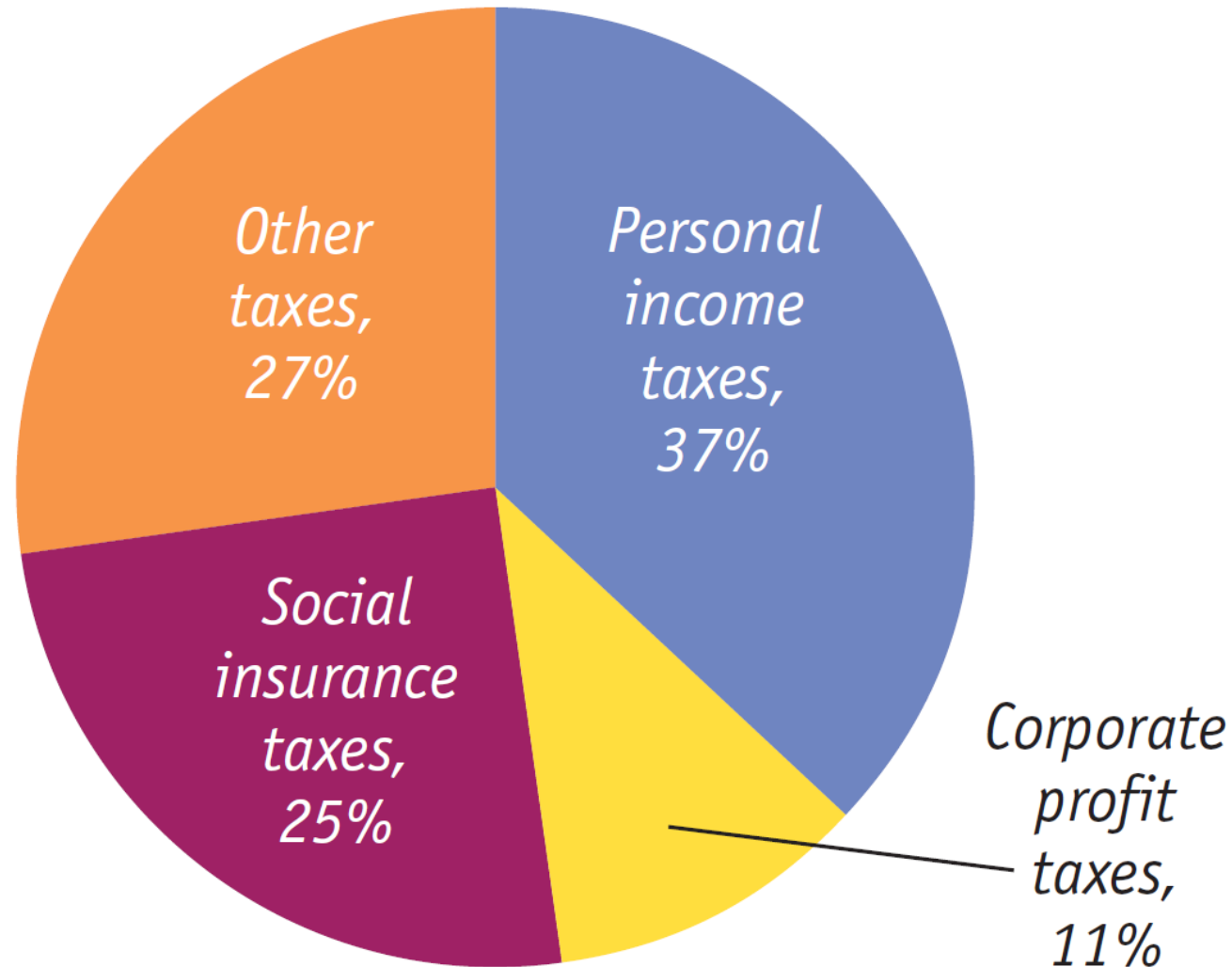
Government Spending and Tax Revenues



Taxes, Govt. Purchases, Transfers, and Borrowing

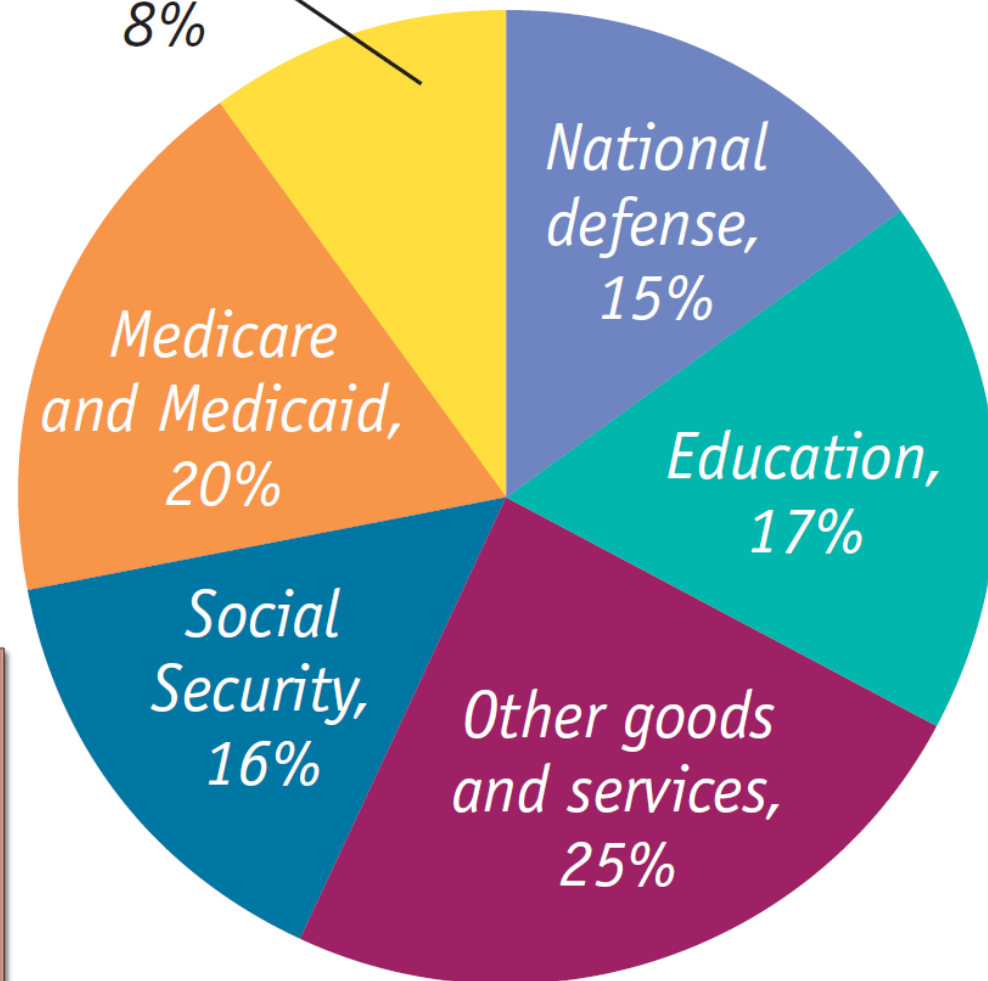
- Funds flow into the government in the form of taxes and government borrowing
- Funds flow out of the government in the form of government purchases of goods and services and government transfers to households

Sources of U.S. Tax Revenue in 2007



U.S. Government Spending in 2008

*Other government transfers,
8%*



Social insurance programs are government programs intended to protect families against economic hardship.

Government Budget and Total Spending

$$GDP = C + I + G + X - IM$$

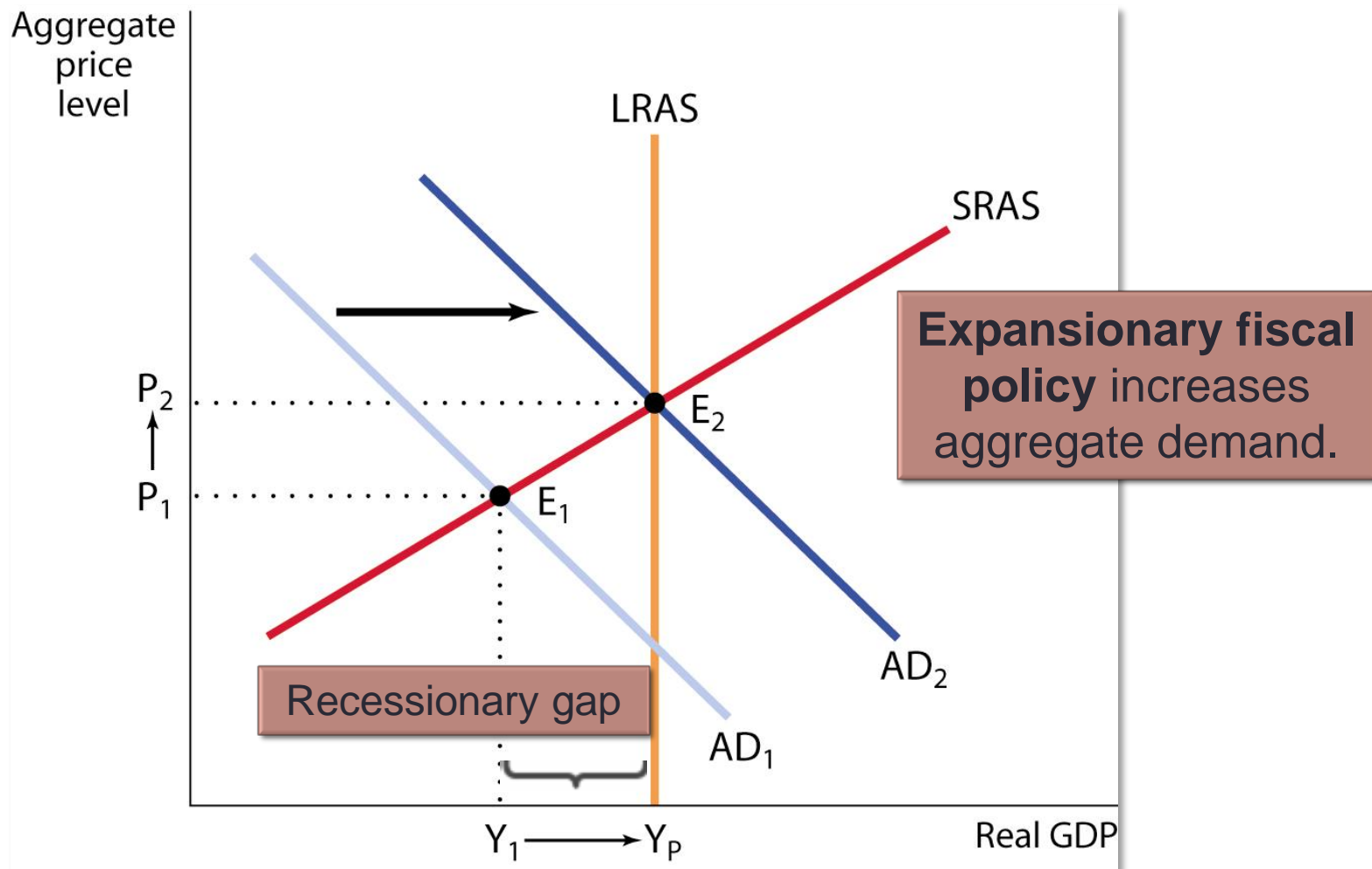
- **Fiscal policy** is the use of taxes, government transfers, or government purchases of goods and services to shift the aggregate demand curve.

Expansionary and Contractionary Fiscal Policy

- Expansionary fiscal policy *increases* aggregate demand and can take one of three forms:
 - an increase in gov't purchases of goods and services
 - a cut in taxes
 - an increase in government transfers
- Contractionary fiscal policy *reduces* aggregate demand and can take one of three forms:
 - a reduction in gov't purchases of goods and services
 - an increase in taxes
 - a reduction in government transfers

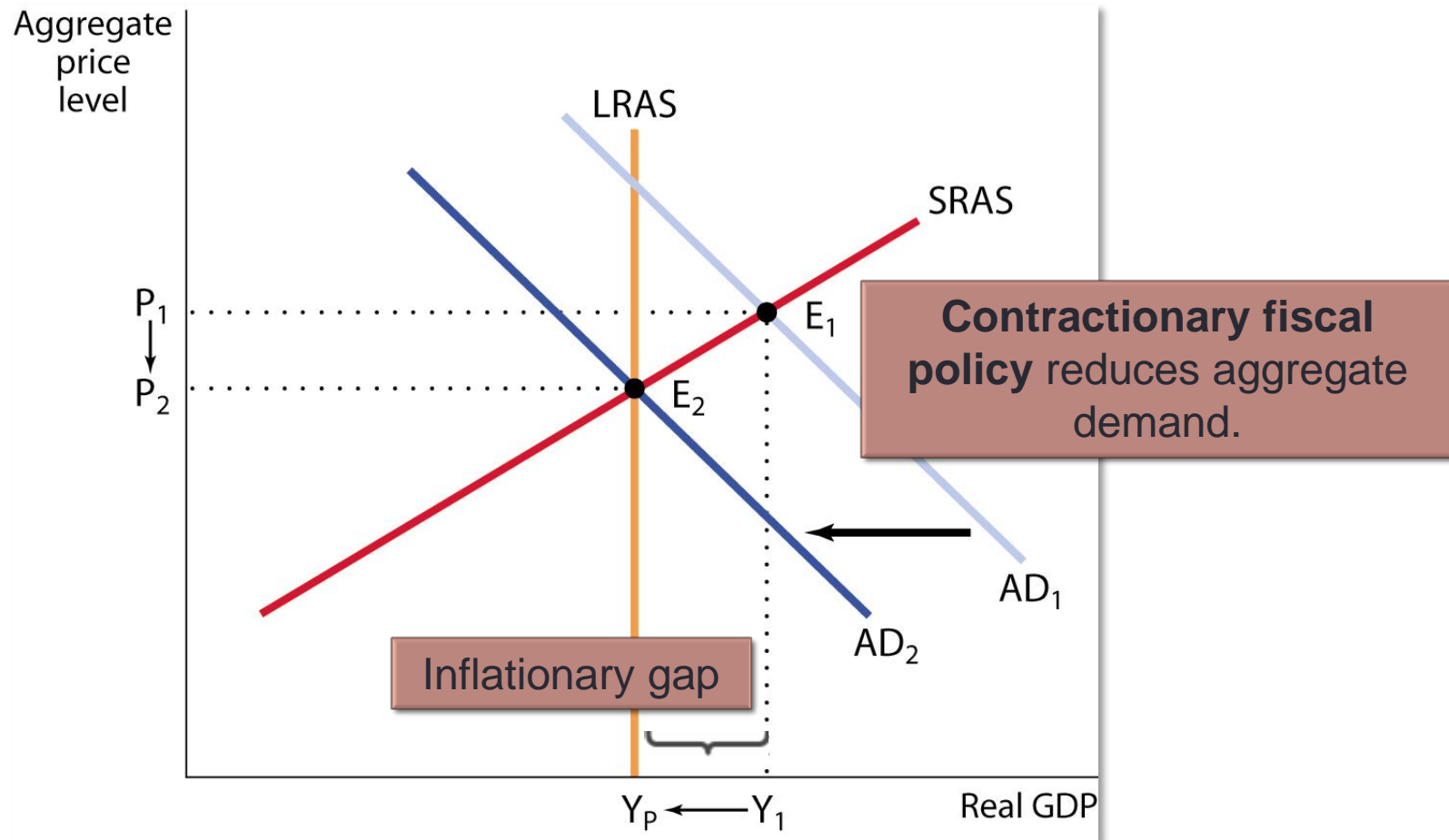
Expansionary and Contractionary Fiscal Policy

Expansionary Fiscal Policy Can Close a Recessional Gap



Expansionary and Contractionary Fiscal Policy

Contractionary Fiscal Policy Can Eliminate an Inflationary Gap



Can Expansionary Fiscal Policy Actually Work?

- Three arguments against the use of expansionary fiscal policy:
 - Government spending crowds out private spending
 - Government borrowing crowds out private investment spending
 - Government budget deficits lead to reduced private spending

A Cautionary Note: Lags in Fiscal Policy

- In the case of fiscal policy, there is an important reason for caution: there are significant **lags** in its use.
 - Realize the recessionary/inflationary gap by collecting and analyzing economic data → takes time
 - Government develops a spending plan → takes time
 - Implementation of the action plan & spending the money → takes time