In what ways can fiscal policy affect aggregate supply

Literature, Russian Literature

Economics Question In what ways can fiscal policy affect aggregate supply? Fiscal policies are strategies applied by the legislative and other arms of the government to control the country's economy. Mainly the government executes its fiscal policies through taxes and expenditure. Fiscal policies affect aggregate supply in many ways. Taxation affects supply of labor that in turn affects the supply of goods and services. Rise of direct taxes reduces the net income, thereby lowering motivation among employees. Reduced rates of corporation tax can also stimulate fixed capital investment. This will in turn boot supply due to increased supply of goods and services. In addition, establishment of infrastructures is a part of the government's spending and budget. Increased taxation can also promote production of goods and services within the country. This is an unprecedented impact of fiscal policies. Question 2: How do automatic stabilizers differ from discretionary fiscal policy tools? Automatic stabilizers increases or decreases the budget deficits during times of recessions and booms respectively. They are either expense or taxation items that forms as economic system. On the other hand, discretionary fiscal policy tools require legislative action and can take long time to implement. Ideally, fiscal policy will be used to increase aggregate demand during recessions and to restrain aggregate demand during boom times (McEachern, 2012). Automatic stabilizers include unemployment compensation subsidies to farmers and a progressive tax system. Unlike discretionary fiscal policy tools, automatic stabilizers do not suffer from economic lags. Lastly, Automatic stabilizers do not require government approval in order to take effect. Consequently, discretionary fiscal policy requires Congress or the President approval. Question 3:

Distinguish between crowding out and crowding in. Crowding out occurs when there is escalating government's borrowing. On the other hand, crowding-in results when private sector investment increases due to increases in government spending. Crowding in boosts demand for goods, thereby increasing demand for new output. Crowding out occurs when the government intends to increase its expenditure hence crowding out private sector investments (McEachern, 2012). Increased borrowing by the government leads to higher interest rates due to increased demand for money and loanable funds. Thus crowding out restrict or discourages private sector investments. Consequently, the government becomes a supplier of essential services previously provided by the private sector. Crowding in and crowding out also have different implication on autonomous expenditure and IS curve. For instance crowding in causes the IS curve to shift outwards due to increase in transaction and demand for liquid cash. Question 4: What problems are associated with the U. S. federal budget process? What solutions have been offered to these problems? The current US federal budget fails to meet key budgetary requirements. Ideally, the budget is supposed to provide a realistic and orderly roadmap for the country's annual spending against available income. However, it stifles debate and prevents cooperation hence creating a breakdown in the national economy and allocation of funds. The current system has been subject of abuse and a source of loopholes for lawmakers eager to exploit its structural flaws. In addition, the national budget is subject to political process, making it difficult to implement proposed economical progress (Bade, & Michael, 2002). For instance, in 2005 the Senate and the White House could not concur even on

essential budgetary structure. Moreover, the budget process is designed with a bias toward higher expenditure and taxes. In order to solve these problems, several solutions have been proposed. Firstly, compulsory expenditure should be accounted for in the annual allocations. Lastly, the Congress should establish an emergency reserve fund for rapid response (Bade, & Michael, 2002). Question 5: It is often said that we are passing our national debt on to our children and grandchildren. Is this true? Explain. The claim that we are passing our national debt to our children and grandchildren is true to the best of my knowledge. This is because most Americans are living beyond their own means. Indeed, the country's economy is an aggregate of individual's economy. Thus if individual/household's budgets exceed their income, then the national budget is in deficit. Currently, the national budget is financed through debts since our taxpayers cannot meet the country's demand. The consequences of a bloated budget that we currently operate are more likely to be paid by our grand children, if not by our children. Moreover, current economic measures such as the GDP are unrealistic. This is because the measures do not account for all our expenditures. For example, the GDP does not account for natural resources and the subsequent environment degradations that result from the economic activities. Thus, the national budget is financed through some hidden costs that have to be paid by our children. References Bade, R. & Michael, P. (2002). Foundations of Microeconomics. Boston, MA: Addison-Wesley McEachern, W. A. (2012). ECON Macro 3 (3rd ed.). Mason, OH: South-Western