Economics of social issues

Literature, Russian Literature

of 26 January Question Built-in stabilizer programs are mechanisms that regulate the fluctuatingeffects of the business cycle automatically without any direct involvement of the government. These programs are effective because they reduce the lag time between a change and the response of the economic system. Taxation policies are one kind of built-in stabilizers. As the business cycle goes through an economic boom or growth phase, the government revenues through personal and corporate taxes decreases while expenditure on unemployment support programs also decreases. The opposite happens in an economic recession where taxation is generated from the rich to provide economic support for the unemployed.

Question 2

The total budget deficit does not reflect the effect of all expenses and revenues of the federal government. Some items of expense and revenue are marked as off-budget while others are on-budget. The total budget deficit is the combined effect of the off-budget and on-budget categories. The items that are not included in the on-budget category include the social security payments and unemployment benefits. For most of the past decades the on-budget categories have resulted in a deficit which has been offset by a surplus in the off-budget categories to result in a lower total budget deficit, as in 2012.

Question 3

Cyclical deficits are less of a concern than structural deficits because they are of a temporary nature while structural deficits can be more persistent and even lead to inflation. Cyclical deficits arise as the economy goes through different phases of the business cycle (Arnold, 2010, p. 236). They occur especially during the recession phase when the government has to increase spending on social support. Structural deficits are more permanent and reflect fiscal mismanagement despite the business cycle. If the government cannot derive a reasonable return on them, it may have to print more currency or take on additional debt to pay off the deficit.

Question 4

Budget deficits tend to result in a crowding out of private firm and as a result private sector investment is reduced (Arnold, 2010, p. 241). The government borrows from the private sector to fund its deficit spending and to pay off creditors. As a result, the private sector is left with fewer funds to invest. As this also reduces the employability of private firms, the number of jobs in the economy also reduces. The graph shows the effect of budget deficit on the loanable funds market. The government issues bonds to cover its deficit spending which increases the demand for credit and the demand curve shifts to the right from D1 to D2. The equilibrium point shifts from e1 to e2 along the supply curve S and the interest rate increases from r1 to r2.

Question 5

If the US budget deficit is perceived to have reached unsustainable levels, it could lead to a weakening of the US dollar against other currencies such as the Euro. The government will issue bonds or print more currency to pay off creditors. This increases the supply of the US dollar. Demand for the US dollar declines. As a result of the interaction of demand and supply, the value of the US dollar in the foreign exchange market could decline. The graph below shows that the increase in supply of US dollars lowers the equilibrium position and the further decline in demand lowers the equilibrium further resulting in a fall in the value of the US dollar.

Works Cited

Arnold, Robert, A. Macroeconomics. Mason, OH: South-west Cengage Learning, 2010. Print.