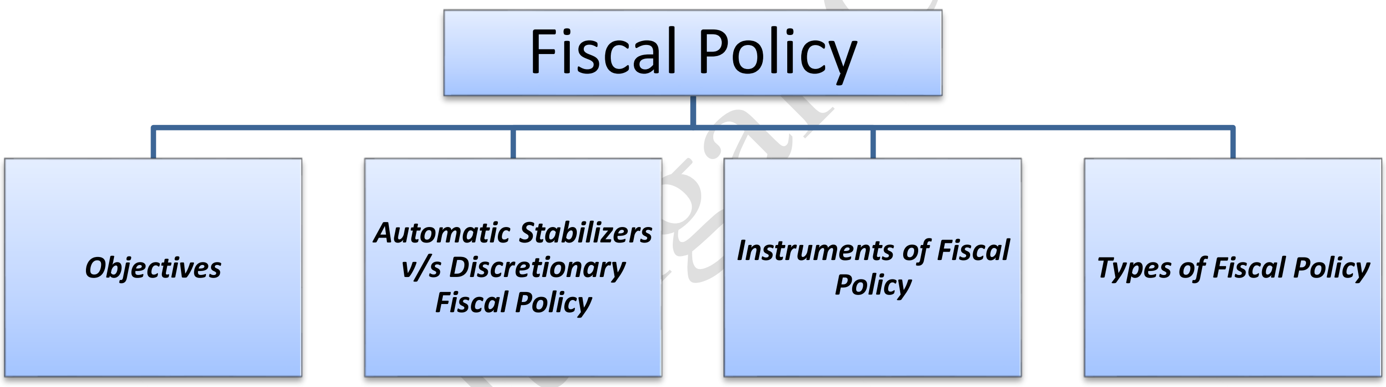
Unit-IV Fiscal Policy

Fiscal Policy: The focus of fiscal policy is on the aggregate economic activity of governments, aggregate expenditure, taxes, transfers and issues of government debts and deficits and their effects on aggregate economic variables such as total output total employment, unemployment rate, inflation, overall economic growth etc.

Through the use of budgetary instruments such as public revenue, public expenditure, public debt and deficit financing, governments intend to favorably influence the level of economic activity of a country.



Objectives

- Achievement and maintenance of full employment.
- Maintenance of price stability.
- Acceleration of the rate of economic development and equitable distribution of income and wealth.

Types of Fiscal Policy

- Expansionary Fiscal Policy
- Contractionary Fiscal Policy

Expansionary Fiscal Policy

An expansionary fiscal policy is used to address recession and the problem of general unemployment on account of business cycles.

Contractionary Fiscal Policy

- Decrease in government spending.
- Increase in personal income taxes and/or business taxes.
- A combination of decrease in government spending and increase in personal income taxes and/or business taxes.

Instruments of Fiscal Policy

- **Government Expenditure** : Generates income and also effect of multiplier.
- **Taxes** : Determine the size of the disposable income of public.
- **Budget** : A widely used tool to stimulate or contract aggregate demand.
- **Public Debt**: Public Borrowing and Debt Repayment system.

Fiscal Policy For Long Term Economic Growth

- A well designed tax policy that rewards innovation and entrepreneurship, without discouraging incentives will promote private businesses who wish to invest and thereby help the economy grow.

Fiscal Policy For Inequalities of Income & Wealth

- A progressive direct tax system
- Indirect taxes can be differential
- A carefully planned policy of expenditure

Fiscal Policy Limitation

- In respect of choice of appropriate policy
- Recognition lag
- Decision lag
- Implementation lag
- Impact lag