AQA - A Level Economics

The national and international economy

13.1 Fiscal policy and supply-side policies

Revision Notes

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13.1.1 Fiscal policy

Introduction to fiscal policy

📢 **Fiscal Policy – The Government's Role in Spending & Taxation**

📌 **What is fiscal policy?**
Fiscal policy is how a government uses **spending** 💸 and **taxes** 💰 to influence how much people are buying, selling, and working in the economy (also called *aggregate demand*). It involves:

🚀 **Expansionary Fiscal Policy – Pressing the Gas Pedal**

Used when the economy needs a boost (for example, during a slowdown or recession).

- **How?** Lower taxes 🏷️ or increase government spending 🏗️.
- **Why?** More money in people's pockets → more spending → more jobs → more growth.

Example: Imagine the government builds new high-speed trains 🚄. Construction companies hire more workers, who then spend their wages on food, clothes, and entertainment, giving the whole economy a lift.

🛑 **Contractionary Fiscal Policy – Hitting the Brakes**

Used when the economy is overheating (too much spending, rising prices, or high inflation).

- **How?** Raise taxes 📈 or cut government spending ✂️.
- **Why?** Slows down spending to keep prices under control.

Example: If prices are skyrocketing, the government might increase VAT (sales tax) so people buy less, helping cool down inflation 🔥.

13.1.1 Fiscal policy

Introduction to fiscal policy

📊 **The Government Budget – The Big Annual Money Plan**

The budget is where the government lays out its income and spending for the year.

- **Balanced budget:** Revenue = Spending (break-even).
- **Budget deficit:** Revenue < Spending (spending more than it earns).
- **Budget surplus:** Revenue > Spending (earning more than it spends).

🏢 **When There's a Deficit…**

If the government spends more than it earns, it has to **borrow** 💳.

- This is called *public sector borrowing*, and it adds to the country's *public debt*.
- Think of it like using your credit card for bills, fine occasionally, but too much borrowing can mean trouble later.

🔷 **Example:**

- During the **COVID-19 pandemic**, the UK government **increased spending** on healthcare and furlough schemes to protect jobs.
- If the economy **overheats** (too much demand, causing inflation), the government may **increase taxes** to slow spending.

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Macroeconomic and microeconomic impacts of fiscal policy

📈 **Macroeconomic impacts – The "Big Picture" Effects**

Definition: *Macroeconomics* looks at the economy as a whole, things like inflation, unemployment, and economic growth across the entire country.

Fiscal policy helps governments hit their **big economic goals**:

- 🌱 **Support long-term growth** – Build a stable environment so businesses can plan ahead confidently.
- 🏷 **Keep inflation low and steady** – Avoid prices spiralling up too fast or dropping suddenly.
- 🌎 **Balance imports and exports** – Manage trade so the country isn't overspending abroad.
- 👷 **Maintain low unemployment** – Keep people in jobs and earning wages.
- 📉 **Smooth out the business cycle** – Reduce the extreme "boom and bust" swings in the economy.
- ⚖ **Distribute income fairly** – Use taxes and benefits to reduce big gaps between rich and poor.

Example: If the economy is slowing, the government might cut taxes and boost spending on infrastructure (roads, schools, hospitals) to create jobs and get money flowing again.

Key point: A single fiscal policy decision can send ripples through the entire economy affecting prices, jobs, investment, and trade.

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Macroeconomic and microeconomic impacts of fiscal policy

🛠 **Microeconomic impacts – The "Zoomed-In" Effects**

Definition: *Microeconomics* focuses on individual households, workers, and businesses, basically, the smaller players in the economy.

Fiscal policy can tweak policies like taxes and subsidies to directly affect these smaller units:

- 💸 **Subsidies for industries** → Lower costs for producers (e.g., farmers get subsidies for equipment), making it cheaper to produce goods and encouraging higher output.
- 🚀 **Business tax cuts** → Companies may expand, hire more staff, or take bigger risks on new projects.
- 💼 **Lower income taxes** → Workers keep more of their pay, which can motivate them to work more hours or be more productive.

Example: If the government gives renewable energy companies a subsidy, it can make solar panels cheaper 🌞, increase production, and help more people switch to clean energy.

📌 **In short:**

- **Macroeconomic impact** = steering the whole economy 🚗.
- **Microeconomic impact** = adjusting the controls for individual drivers and passengers.

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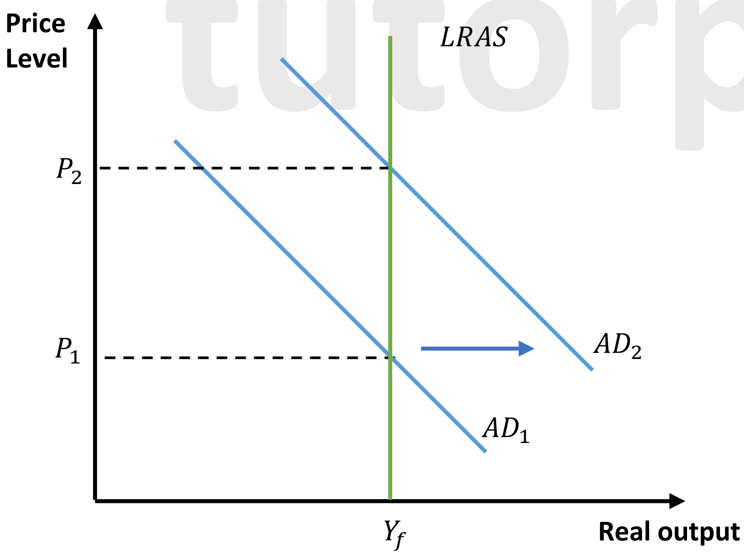
Fiscal policies influence on aggregate demand

Demand-side policies (which focus on **shifting aggregate demand (AD)** through **fiscal and monetary policies**) can help boost economic growth and reduce unemployment. However, they come with challenges, and economists **don't always agree** on their effectiveness.

Classical view

Classical economists argue that **demand-side policies only work in the short run**. They believe that **boosting AD won't increase output** in the long term but will simply cause **inflation (rising prices)**. According to them, economies naturally **correct themselves**, so it's better to focus on **supply-side policies** (like improving education, infrastructure, and business conditions).



13.1.1 Fiscal policy

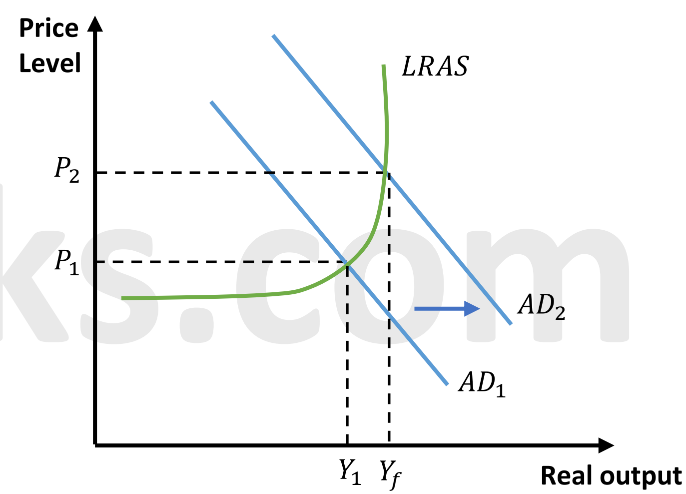
Fiscal policies influence on aggregate demand

Keynesian view

Keynesian economists argue that the **effect of demand-side policies depends on the state of the economy**:

✅ If **unemployment is high**, increasing AD **boosts output and jobs**.

❌ But if the economy is already at **full employment**, increasing AD **only raises inflation** (prices go up, but no extra goods are produced).



Expansionary and Contractionary Demand-Side Policies

Expansionary policies **increase aggregate demand (AD)** to stimulate economic growth. These are used during **recessions** or periods of **slow growth** to **reduce unemployment and encourage spending**. Done through lower interest rates, tax cuts, increased government spending and QE.

Contractionary policies **reduce aggregate demand (AD)** to **control inflation** and prevent the economy from overheating. These are used when **growth is too fast, leading to high inflation and unsustainable demand**.

Fiscal policies influence on aggregate supply

Definition: *Aggregate supply* is the total amount of goods and services an economy can produce at a given time.
When we talk about the **supply-side** of fiscal policy, we mean policies designed to *increase* this productive potential in the long run.

How fiscal policy can help:
Some government spending might seem short-term, but it plants seeds 🌱 for long-term economic growth.

Example:

- 🎓 **Education subsidies** – If the government helps students pay for university or vocational training, it costs money *now* (short-term spending).
- But in the future, those educated workers have higher skills (known as **human capital**), meaning they can work more efficiently, invent new products, and boost overall output 🚀.

Other examples:

- 🏗 **Infrastructure projects** – Building better roads, railways, and internet networks makes it easier for businesses to operate.
- ⚡ **Energy investments** – Funding renewable energy projects can lower future production costs for industries.
- 💊 **Healthcare improvements** – A healthier workforce means fewer sick days and higher productivity.

⏳ **Timeframe:**

- Fiscal policy actions (like setting budgets) are short-term usually planned yearly.
- But their impact on aggregate supply can last *years or decades*.

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Government spending and taxation affects on economic activity

Automatic stabilisers are **built-in government tools** that automatically help smooth out the ups and downs of the economy as it goes through the business cycle (recession, boom, etc) without needing anyone to take action.

✔ **Examples include**:

- **Taxes**: When people earn more in a boom, they pay more in income tax. This takes some money out of the economy and **slows down demand**, stopping the economy from overheating.
- **Welfare benefits**: In a recession, more people lose jobs and automatically qualify for **unemployment benefits**. This puts money in their pockets, **softening the fall in demand**.

These changes happen **without any new laws or decisions;** they just work in the background. This helps keep **Aggregate Demand (AD)** from swinging wildly.

🛠 **Discretionary Fiscal Policy**

This is the government taking the wheel. It's when they **deliberately change taxes or spending** to boost or slow down the economy.

✅ **In short:**

This policy is **planned and chosen** by the government to increase or decrease **Aggregate Demand (AD),** basically how much people, businesses, and the government are spending.

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Government spending and taxation affects on economic activity

✔ **Two types**:

- **Expansionary** (used in recessions): The government **spends more or cuts taxes** to boost economic activity.
- **Deflationary** (used in booms): The government **spends less or raises taxes** to cool things down.

🧠 Example: During the COVID-19 pandemic, governments around the world used discretionary policy by increasing health spending and providing furlough payments to workers.

🧩 **Key Difference?**

- Automatic = works by itself
- Discretionary = needs action by the government

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Types of and reasons for public expenditure

The government doesn't just collect taxes and sit on a pile of money 🏦, it spends that money for lots of important reasons.

Government spending (aka **public expenditure**) makes up a big chunk of **aggregate demand (AD)** which is the total demand for goods and services in the economy.

🧠 **Why Does the Government Spend?**

Government spending helps manage the economy and reach key goals like:

- 🏗 **Economic growth**
- 🔁 **Balanced trade (current account)**
- 💷 **Low and stable inflation**
- 📉 **Low unemployment**

It also supports **fairness** by providing services (like healthcare and education) to people who might not otherwise afford them. On top of that, the government can use spending to fix **market failures**, like building public goods (e.g. streetlights) or reducing pollution.

But not all government spending is the same. It's usually split into three types:

1. 🏗 Capital Expenditure – Long-Term Investment

This is **spending on big projects and equipment** that last a long time. It's like the government investing in the future.

✅ **Examples:**

- Building a new school or hospital
- Upgrading the rail network or road systems
- Buying military jets or NHS ambulances
- Renewable energy projects like offshore wind farms

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Types of and reasons for public expenditure

2. 🧾 Current Expenditure – Everyday Running Costs

This is the **money the government spends regularly** to keep things ticking over; kind of like paying the bills.

✅ **Examples:**

- Salaries of public sector workers (like teachers, NHS staff, or police)
- Fuel for ambulances or fire engines
- Stationery for government offices or medicine and supplies for hospitals

3. 💷 Transfer Payments – Helping People Out

These are payments the government makes **without getting any goods or services back**. They're simply transfers of money from one group to another.

✅ **Examples:**

- Universal Credit or unemployment benefits
- State pensions
- Disability benefits or housing support
- Student grants

👉 No goods or services are exchanged, it's **support, not spending on output**, which is why transfer payments **don't directly contribute to GDP**.

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Direct and indirect taxation

Taxation is **the main way governments collect money** to fund public services like healthcare, education, and infrastructure. Taxes come in **two main types**:

1) Direct Taxes – Charged on Income & Profits

Direct taxes are taken directly from individuals or businesses **based on their income, earnings, or profits**. These taxes **cannot be passed on** to someone else – if you owe them, you **have to pay them!**

✅ **Examples:**
🔷 **Income Tax** – If you earn a salary, a portion is deducted as tax.
🔷 **Corporation Tax** – Businesses pay tax on their profits.
🔷 **Capital Gains Tax** – If you sell a house or shares for a profit, you pay tax on the gain.
🔷 **Inheritance Tax** – A tax on large estates passed down after someone dies.

2) Indirect Taxes – Charged on Spending

Indirect taxes are **charged on goods and services** rather than income. These are collected by **businesses**, which then **pass them on** to the government. **Consumers indirectly pay** these taxes when they buy things.

✅ **Examples:**
🔷 **Value Added Tax (VAT)** – A percentage added to most goods and services (e.g., in the UK, VAT is **20%**).
🔷 **Excise Duties** – Extra taxes on **alcohol, cigarettes, and fuel** (because the government wants to discourage their use).
🔷 **Sugar Tax** – Some countries charge extra on sugary drinks to reduce obesity.
🔷 **Tariffs** – Taxes on imported goods (e.g., if the UK imports American cars, a tariff may be added).

Key Differences:
💰 **Direct tax** = Paid **directly** by individuals & businesses (e.g., income tax).
🛒 **Indirect tax** = Paid **when you buy things** (e.g., VAT on shopping).

Again tax is basically how the government earns its money. It uses this to:

- **Pay for public services** like schools, hospitals, roads, and police.
- **Fix market failure** (e.g. putting extra tax on cigarettes to reduce smoking).
- **Manage the economy** (by changing tax during booms or recessions).
- **Redistribute income:** take more from the rich to help the poor.

Progressive, proportional and regressive taxes

1. 🔼 Progressive Tax

This is when people who earn more **pay a higher percentage** of their income in tax. So, the richer you are, the more tax you pay.

Example: Imagine Amy earns £30,000 and pays 20% in tax, but Ben earns £100,000 and pays 40%. This is what **income tax** in many countries (like the UK) looks like, it's **progressive**.

✅ It's seen as fairer and helps **reduce inequality**.

UK Example (2022):

Income Band	Income Range	Tax Rate
Personal Allowance	Up to £12,500	0%
Basic Rate	£12,501 – £50,000	20%
Higher Rate	£50,001 – £150,000	40%
Additional Rate	Over £150,000	45%

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Progressive, proportional and regressive taxes

🔍 **Worked Example**:
On a £80,000 salary:

- **First £12,500 = 0% tax**
  → You pay **£0**
- **Next £37,500 (from £12,501 to £50,000) = 20% tax**
  → £37,500 × 20% = **£7,500**
- **Final £30,000 (from £50,001 to £80,000) = 40% tax**
  → £30,000 × 40% = **£12,000**
  🧮 Total Tax = £19,500

🎓 **Other countries** like Germany and South Africa also use progressive income taxes to help reduce inequality.

2. 🔽 Regressive Tax

Here, **everyone pays the same rate**, but **poorer people feel the impact more**, because the tax takes up a bigger chunk of their income.

Most **indirect taxes** (like VAT, fuel tax, or alcohol duties) are **regressive**.

Example: VAT (Value Added Tax). Both Sarah (on £20k) and Lucas (on £80k) pay 20% VAT when they buy a phone. But for Sarah, that VAT is a much bigger slice of her income than it is for Lucas.

⚠️ This type of tax can **widen inequality**.

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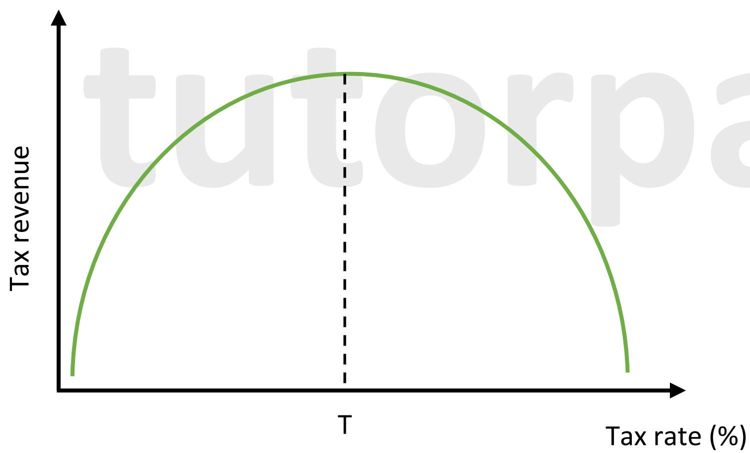
Progressive, proportional and regressive taxes

3. ➖ Proportional Tax (Flat Tax)

This is a system where **everyone pays the same percentage** of their income, no matter how much they earn.

Example: In some countries like Estonia, everyone pays 20% of their income whether they earn £5,000 or £150,000.

📌 It's simple and transparent, but critics say it **doesn't do much to reduce inequality**.



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The merits of different UK taxes

Each tax has its *good points* ✅ and *not-so-good points* ❌.

1 Income Tax

Definition: A tax on the money you earn from work or investments.

✅ **Advantages:**

- **Seen as fair** – You pay based on what you earn; higher earners often pay a bigger share (*progressive tax*).
- **Can reduce inequality** – By taking more from the rich and funding support for the less well-off.
- **Easy for most workers** – Employers take it automatically from wages (PAYE system).

❌ **Disadvantages:**

- **Work disincentive** – Higher taxes might make some people less motivated to work extra hours.
- **Complex rules** – Progressive systems can be tricky to understand.

Example: If you earn £30,000, you might pay less tax per pound earned than someone earning £100,000.

2 VAT (Value Added Tax)

Definition: A tax added to most goods and services you buy.

✅ **Advantages:**

- **No impact on work effort** – It's based on spending, not earnings.
- **Hard to avoid** – Charged at the point of sale.

❌ **Disadvantages:**

- **Regressive** – Takes a bigger percentage of income from low earners, since they spend more of what they earn.
- **Can fuel inflation** – Raising VAT can make prices jump.

Example: Buy a £20 shirt? With VAT, it might cost £24.

13.1.1 Fiscal policy

The merits of different UK taxes

3 **Excise Duties**

Definition: Special taxes on certain goods like alcohol 🍷, cigarettes 🚬, or fuel ⛽.

✅ **Advantages:**

- **Changes behaviour** – Can reduce harmful habits (e.g., smoking less).
- **Generates targeted revenue** – People who use these products pay more.

❌ **Disadvantages:**

- **Job losses risk** – If demand falls, related industries may shrink.
- **Encourages black markets** – People might seek untaxed, illegal alternatives.

Example: A high petrol tax might push people to drive less or switch to electric cars.

4 **Council Tax**

Definition: A local tax based on your home's value, used to fund local services like waste collection 🚛 and libraries 📚.

✅ **Advantages:**

- **Seen as fair locally** – Based on property value, so wealthier homeowners pay more.
- **Funds local needs** – Money stays in the community.

❌ **Disadvantages:**

- **Outdated valuations** – Property value "bands" often don't reflect today's market.
- **Cash-poor homeowners** – People with valuable homes but low incomes may struggle to pay.

Example: Two pensioners in a big old house may pay more than a young professional in a modern flat.

13.1.1 Fiscal policy

The merits of different UK taxes

5 **Corporation Tax**

Definition: A tax on company profits 💼.

✅ **Advantages:**

- **Targets success** – More profitable companies pay more tax.
- **Doesn't hit smaller, struggling firms as hard**.

❌ **Disadvantages:**

- **May deter investment** – High taxes could scare off foreign investors.
- **Encourages avoidance** – Companies may move profits overseas to pay less tax.

Example: If a UK company earns £10 million, a portion of that goes to the government before paying shareholders.

13.1.1 Fiscal policy

Why governments levy taxes

Governments tax for several reasons:

1 **To raise money for public spending**

- The UK government spends around **£800 billion** a year on things like healthcare 🏥, schools 📚, roads 🛣, and defence.
- Most of this comes from taxes, though the government often still needs to borrow more.

Example: Your income tax helps pay for the NHS, just like council tax helps fund your bin collections.

2 **To change economic behaviour**

- Taxes can encourage or discourage certain activities.
- Lower taxes on renewable energy 🌱 could get more people to switch from fossil fuels.
- Higher taxes on petrol ⛽ might push people to use public transport instead.

3 **To discourage harmful products** (*demerit goods*)

- The government often taxes things that are bad for health or society (like tobacco 🚬 or alcohol 🍺) to make them less attractive.
- These are called **excise duties**. Even if people don't stop buying them, the government still earns money from the tax.

13.1.1 Fiscal policy

Why governments levy taxes

4 **To redistribute income**

- Progressive taxes (where richer people pay a higher percentage) help close the gap between the rich and poor.
- This can reduce **relative poverty** and make society fairer.

Example: Someone earning £150k a year pays a higher rate of tax than someone earning £25k, meaning more money goes into public services.

🏷 **Hypothecated Taxes**

Definition: A *hypothecated tax* is money collected for a **specific** purpose, not just added to the general government budget.

- For example, in 1997–2001 the UK Labour government put a special **windfall tax** on certain privatised companies, using the money for job training and employment schemes.
- Governments could also tax industries that cause pollution 🌍 and use that money to clean up the environment.

Pros: It's clear where the money goes, and it directly tackles the problem caused.
Cons: It can tie the government's hands; if tax revenue falls, the funding for that project also drops.

Principles of taxation

Let's be honest, nobody likes paying more tax, so, what makes a tax "good" and fair?

The famous economist **Adam Smith** came up with a set of rules, called the *canons of taxation*, to guide this. Over time, extra principles have been added to keep them relevant today.

The 6 Principles of a Good Tax

1 **Economical** 💷
The cost of collecting the tax should be low compared to the money it brings in.
Example: Income tax is deducted directly from salaries (PAYE), so it's cheaper to collect than chasing millions of small payments.

2 **Equitable** ⚖️
Taxes should be **fair** and based on the ability to pay.

- **Horizontal equity:** People in similar situations should pay the same (e.g., two teachers on £30k should pay equal tax).
- **Vertical equity:** People who earn more should pay more.
  Example: A millionaire pays a higher tax rate than a shop assistant, making it progressive.

3 **Efficient** ⚡
The tax should not cause too many side effects or unintended problems.
Example: A tax that makes companies move abroad would be inefficient because it hurts jobs and growth.

4 **Convenient** 🏢
Paying the tax should be straightforward and not a huge hassle.
Example: Online filing for self-assessment makes it easier than sending paper forms in the post.

13.1.1 Fiscal policy

Principles of taxation

5 **Certain** 📏
People should know roughly how much tax they'll owe and when it's due, no nasty surprises.
Example: VAT is clearly stated on receipts, so you know it's already included in the price.

6 **Flexible** 🔄
The tax system should be able to adapt when the economy changes.
Example: Governments can adjust fuel duty in response to oil price changes to help consumers.

In short:
A "good" tax is **fair, clear, cheap to collect, easy to pay, doesn't cause chaos, and can adapt when needed**.

13.1.1 Fiscal policy

The budget balance and the national debt

Definition: The **government budget** is a yearly plan showing how much money the government expects to bring in (revenue) and how much it plans to spend (expenditure).
It can be in one of three states:

📏 Balanced Budget

Government revenue = Government spending
Like earning £2,000 a month and spending exactly £2,000, no savings, no debt.

📉 Budget Deficit

Government revenue < Government spending
The government spends more than it earns, so it has to borrow the difference.
Example: You earn £2,000 a month but spend £2,200, so you put £200 on your credit card.

📈 Budget Surplus

Government revenue > Government spending
The government earns more than it spends, so it can save or pay off debt.
Example: You earn £2,000 but only spend £1,800, so you have £200 left over.

🏢 What Happens When There's a Deficit?

When the government has a **budget deficit**, it has to borrow money, this is called **public sector borrowing**.
That borrowing gets added to the **national debt;** the total amount the government owes from past borrowing (plus interest).

13.1.1 Fiscal policy

The budget balance and the national debt

📚 Keynesian View

Economist John Maynard Keynes argued that during tough economic times, governments *should* run a deficit to boost spending and help the economy grow.
Example: Building new hospitals or roads during a recession can create jobs and encourage businesses to invest.

⚠️ The Downside

More debt means future generations will have to help pay it off through taxes, a bit like giving your kids your old credit card bill.

In short:

- **Balanced budget** = Even.
- **Deficit** = Spending more than you earn → Borrowing → More debt.
- **Surplus** = Earning more than you spend → Savings or debt repayment.

Cyclical and structural deficits

🔄 Cyclical Deficits – Temporary Budget Gaps

These happen when the economy hits a rough patch like a recession.

- **Why?** When people earn less and businesses make smaller profits, the government collects **less tax**.
- At the same time, **government spending goes up** (e.g. more people claim unemployment benefits).
- This gap between spending and income is a **cyclical deficit** and the good news is, it usually **fixes itself** as the economy recovers.

🛍️ **Example**: During COVID-19 lockdowns, the UK government collected less VAT and income tax but had to increase spending on furlough and support; a classic cyclical deficit.

🧱 Structural Deficits – Built-In Budget Problems

These are long-term deficits that **don't go away**, even when the economy is doing well and everyone's working.

- They exist because the **government's spending permanently exceeds its revenue**.
- These deficits are **harder to fix** often caused by things like poor tax systems, inefficient public services, or a culture of **tax avoidance** (where people and firms legally dodge paying their fair share).

🏗️ **Example**: A country spends a huge amount on defence, healthcare, or pensions every year but doesn't collect enough tax, this creates a structural deficit.

📊 Actual Deficit = Structural Deficit + Cyclical Deficit

Think of the actual deficit as the full picture:

- The **structural deficit** is permanent unless policy changes.
- The **cyclical deficit** comes and goes with the economy.

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The consequences of budget deficits and surpluses

Definition:

- A **budget deficit** is when the government spends more than it earns in revenue.
- A **budget surplus** is when the government earns more than it spends.

Both can have big effects on the economy and it's important to figure out whether the economy is *causing* the change in the budget or the budget change is *causing* changes in the economy.

🚀 Economic Growth

- A **budget deficit** often means the government is using *expansionary fiscal policy* (spending more or taxing less) to increase **aggregate demand,** boosting short-term economic growth.
- A **budget surplus** usually means *contractionary policy;* taking demand out of the economy, which can slow growth.
- Growth itself also affects the budget: slower growth means less tax revenue and higher welfare payments, while faster growth means the opposite.

Example: During a recession, the government might spend billions on infrastructure projects 🛤️ to create jobs and boost demand, even if it pushes the budget into deficit.

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13.1.1 Fiscal policy

The consequences of budget deficits and surpluses

Typical Mistake:
A budget deficit isn't always bad; it could be a sign of a struggling economy **or** a deliberate move to boost growth. Always check the wider economic indicators 📈 before jumping to conclusions.

👷 Unemployment

- Higher government spending (and a larger deficit) can create more jobs because businesses see more demand and hire more workers.
- However, some economists believe that over the long run, unemployment will return to its "natural rate" no matter what fiscal policy does.

Example: A temporary public works programme might cut unemployment sharply, but when it ends, jobless rates may climb again.

💸 Inflation

- **Demand-pull inflation** happens when there's too much demand chasing too few goods and prices rise.
- Expansionary fiscal policy (bigger deficits) can cause this if the economy is already near full capacity.
- A surplus (through higher taxes or lower spending) can help slow down inflation.

Example: If wages and spending are already high, a tax cut could cause prices in shops 🛒 to rise quickly.

In short:

- Deficit → Can boost growth and cut unemployment but risks inflation and higher debt.
- Surplus → Can reduce inflation and debt but risks slowing growth and raising unemployment.

13.1.1 Fiscal policy

The significance of the size of the national debt

Definition:

- **Budget deficit** → When the government spends more than it earns.
- **National debt** → The total amount the government owes from all past borrowing, plus interest.

When there's a budget deficit, the government has to borrow money; this is called **public sector borrowing**.
Every time it borrows, the amount gets added to the national debt.

Example: During the Covid-19 pandemic 🦠, the UK government borrowed heavily to fund furlough schemes, healthcare spending, and business support, causing the national debt to grow significantly.

📊 Debt-to-GDP Ratio

Definition: The **Debt-to-GDP ratio** compares a country's total debt to the size of its economy (GDP = Gross Domestic Product, or the total value of everything produced in the country in a year).
It's like comparing your credit card debt to your yearly salary; it shows whether your debt is manageable or risky.

- **High ratio** → More vulnerable, as a bigger share of the country's income would be needed to pay off debt.
- **Low ratio** → More breathing space for borrowing if needed.

Example: If the UK's GDP is £2.5 trillion and its debt is £2.5 trillion, the Debt-to-GDP ratio is 100%, meaning the country owes as much as it produces in a year.

The significance of the size of the national debt

The size of a country's **fiscal deficit** (when spending is more than income in a year) and **national debt** (the total of all past deficits) can seriously affect how the economy performs, especially in the long term.

Why it matters?

💳 **1. Interest Rates**

When a government borrows a lot of money, it can push up **interest rates** which is the cost of borrowing. Think of it like this: the more people want to borrow money, the more expensive it becomes to do so. If the government is also borrowing a lot, this might lead to **higher interest rates** for everyone else too. This can discourage investment by businesses and slow down the economy.

However, sometimes governments borrow from overseas or during periods when businesses aren't investing much anyway, in those cases, interest rates might stay low.

🔁 **2. Servicing the National Debt**

Paying back debt isn't free, the government has to pay **interest** on what it owes. "Servicing the debt" just means paying back the **interest** on what the country owes. For example, the UK spends around **£100 billion a year** just on these interest payments, that's a lot, but it's still small compared to the total size of the economy (**GDP**). This money could have been spent elsewhere, like on healthcare or education, so it's called an **opportunity cost**.

13.1.1 Fiscal policy

The significance of the size of the national debt

📈 **3. Inflation Worries**

A high level of debt can be tempting to "inflate away". **Inflation** means prices rise and money loses value. This can make it easier for governments to repay debt with "cheaper" money, but it also reduces your **purchasing power** (what you can buy with your money).

So while it might help the government, it makes life more expensive for everyone else.

💳 **4. Credit Ratings**

Governments get **credit ratings** (like AAA, AA… to D.) based on how likely they are to pay back debt. A high level of debt might make lenders nervous and lead to a **lower rating**, which means the government will be charged **higher interest rates** when borrowing more money. But it's not just about the size of the debt, history and political stability matter too.

🌍💵 **5. Foreign Direct Investment (FDI) and Foreign Currency**

If a country owes **external debt** (money borrowed from abroad), it must repay it in foreign currency (e.g., US dollars). If it doesn't have enough, it may try to attract **FDI** (money coming in from international businesses investing in the country).

This can lead to: Selling assets or offering incentives to foreign companies just to get enough dollars to repay debt, which may or may not be a good long-term strategy.

13.1.1 Fiscal policy

The significance of the size of the national debt

📃 6. Primary Deficit vs. Budget Deficit

- The **budget deficit** is how much more the government spends than it earns in a year.
- The **primary deficit** is the same but **excludes** interest payments on previous debt.

Running a budget deficit now means future generations may have to pay more tax. But if today's deficit is used for things like building roads, schools or hospitals (called **capital expenditure**), then future generations might benefit making it more justifiable.

🚪 7. Crowding out

Definition: *Crowding out* happens when government borrowing makes it harder or more expensive for businesses and households to borrow money.

How it works:

1 **Government borrows** 💰
When the government needs money, it sells **bonds** (IOUs, also called treasury bills) to investors often to people or institutions who want a safe place to put their savings.

2 **More demand for savings = higher interest rates** 📈
Selling bonds increases the competition for available savings. Investors want a good return, so interest rates rise.

3 **Borrowing becomes pricier for everyone else** 🏦
When interest rates go up, businesses and consumers find loans more expensive.

- Firms might delay building new factories 🏭.
- Households might skip buying a home 🏠 or a car 🚗.

4 **Result: Lower spending in the economy** 📉
With less borrowing, **aggregate demand** (total spending in the economy) can fall, slowing economic growth.

Example:
Imagine there's only one big swimming pool of savings. The government jumps in and takes a large share to fund projects. This leaves less "water" for everyone else, and those who want to swim (borrow) now have to pay a higher fee (interest) to get in.

13.1.1 Fiscal policy

The Office for Budget Responsibility

Definition:
The **Office for Budget Responsibility** (OBR) is an independent body created by the UK government in **2010** to give unbiased, expert analysis of the government's finances.
The idea was to make it harder for politicians to change fiscal policy (government spending & tax plans) just for political gain rather than because it's the *right* economic choice.

📋 Main Functions of the OBR

1 **Economic forecasting** 📈

- Predicts the future state of the UK economy, with a special focus on the government's income and spending.
- *Example:* Estimating how Brexit or rising energy prices will affect tax revenues and borrowing over the next five years.

2 **Evaluating fiscal policy** 🧐

- Checks whether the government is meeting its own targets for borrowing, debt, and spending.
- *Example:* If the government promised to cut the deficit by 2025, the OBR assesses if they're on track.

3 **Sustainability analysis** 🔮

- Looks at whether the government's current financial path is sustainable in the long term.
- *Example:* Will pension and healthcare costs for an ageing population overwhelm the budget in 20 years?

4 **Assessing fiscal risks** ⚠️

- Identifies threats to the government's finances, such as recessions, pandemics, or rising interest rates.

5 **Tax and welfare cost analysis** 🧾

- Works out how much new policies will cost or raise.
- *Example:* Calculating the cost of increasing Universal Credit or cutting fuel duty.

13.1.2 Supply-side policies

Supply-side policies and supply-side improvements

Supply-side policies are all about making an economy better at producing things in the long run. Imagine giving the economy a “productivity upgrade” like installing faster machinery, smarter workers, and smoother processes so more goods and services can be made.

Economists call this pushing out the **long-run aggregate supply (LRAS),** basically, the economy’s maximum output if everything is running efficiently. Supply-side policies try to push this limit further out.

There are **two main flavours**:

- 🏗️ **Interventionist policies** – where the government jumps in to help directly.
- 🏪 **Free market policies** – where the government steps back, letting businesses and competition do the heavy lifting.

Supply-side Policy vs. Supply-side Improvements

- **Supply-side Policy** → The *rules and support systems* set by the government to make production easier (like building a new highway (capital) or funding coding bootcamps (labour)).
- **Supply-side Improvements** → The *upgrades and innovations* businesses make themselves (like a bakery buying a bigger oven or a delivery company switching to electric vans 🚐⚡).

13.1.2 Supply-side policies

Supply-side policies and supply-side improvements

🎯 **Objective**

- **Policy:** Create an environment where the *whole economy* can grow steadily and compete internationally 🌍.
- **Improvements:** Make individual firms or industries more efficient, higher quality, and more competitive 💥.

Examples

- **Policy:**
  - Cutting business taxes 💰 so firms invest more.
  - Building faster internet across the country 🌐.
  - Funding renewable energy projects 🌱⚡.
  - Paying for more nurses and doctors to improve healthcare 🏥.
- **Improvements:**
  - A car company switching to AI-powered assembly lines 🚗🤖.
  - A farm using drones to monitor crops 🚁🌾.
  - A cafe launching a slick online ordering app 📱☕.

13.1.2 Supply-side policies

Supply-side policies to improvement the economy

Supply-side policies = policies designed to make the economy more productive ⚙️.
These policies shift the **long-run aggregate supply (LRAS)** curve outward 📈 → meaning the economy can produce *more stuff* with the same resources. Let's see how this plays out…

💷 Effect on GDP

GDP (Gross Domestic Product) = the total value of goods and services produced in a country.

When supply-side policies are successful, the economy can produce *more output*, meaning higher GDP.

- Example: If the UK builds faster internet nationwide 🌐, businesses can operate more efficiently → boosting production and GDP.
- But remember: GDP growth also needs **aggregate demand (AD)** (the demand for goods/services) to rise, or else that new capacity goes unused.

🧑‍🏭 Effect on Unemployment

Supply-side policies can reduce unemployment in lots of ways:

- **Lower income taxes** → working becomes more rewarding, so more people choose jobs over staying home.
- **Better education and training** → people gain skills for modern jobs (e.g. coding bootcamps for tech jobs 💻).
- **Deregulation (removing business red tape)** → easier to start businesses, more competition, more jobs.
- **Reduced welfare traps** → discourages long-term unemployment by making work more attractive.
- **Infrastructure investment** → new transport links (like HS2 🚄) can attract businesses and jobs and make it easier for people to commute.

13.1.2 Supply-side policies

Supply-side policies to improvement the economy

📉 Effect on Inflation

Inflation = the rate at which prices rise.

Supply-side policies can help lower inflation by making production cheaper and more efficient:

- 🏭 **More capacity** → the economy can handle more demand without prices spiking.
- 🆚 **More competition** → harder for firms to keep prices high, as customers can switch to cheaper alternatives.
- 💼 **Union reforms** → less upward pressure on wages, meaning lower cost-push inflation.
- Example: Cheaper renewable energy ☀️ reduces production costs, lowering prices in the long run.

🌍 Effect on Balance of Payments (Current Account)

Balance of payments = a record of trade (exports vs imports).

Supply-side policies can make exports more competitive:

- 📉 **Lower costs** → UK goods/services become cheaper abroad → more exports.
- 👷 **Skilled workforce** → better quality products = more global demand.
- 🏫 **Investment in education/training** → creates innovation → e.g. world-class UK tech exports 💻.
- Example: If UK firms produce high-quality green tech 🌱⚡, demand abroad increases, improving the trade balance.

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13.1.2 Supply-side policies

Supply-side policies and the natural rate of unemployment

The **natural rate of unemployment** is the level of unemployment that exists even when the economy is doing well. It happens because of things like:

- **Frictional unemployment**: when people are between jobs (e.g., a teacher quits and takes a few months to find another school).
- **Structural unemployment**: when workers don't have the right skills for new industries (e.g., a coal miner struggling to find work in a renewable energy economy).

✅ **Supply-side policies** can help reduce this "natural" level of unemployment by making the job market work more smoothly:

- 💰 **Lower taxes on income** → gives people more incentive to actually work rather than stay out of the workforce.
- 🎓 **Better education & training** → helps workers gain skills to switch careers or adapt to new industries.
- 🔬 **Research & development subsidies** → can create brand-new industries (think AI, green tech) that provide fresh jobs.
- ⚖️ **Less generous unemployment benefits** → encourages people to take jobs sooner instead of waiting for the perfect one.
- 🚌 **Improved infrastructure (like transport & broadband)** → makes it easier for people to move to where jobs are.

If unemployment falls, the country's **national income** rises, meaning more money in the economy, stronger growth, and less risk of inflation getting out of control.

📍 In the UK, the natural rate of unemployment is around **5%** (a few people will *always* be between jobs). In some EU countries, it's higher.

Supply-side policies don't magically "fix" unemployment. Instead, they create the right *conditions* (like better training and lower barriers) so that other policies can help reduce it.

13.1.2 Supply-side policies

Free market supply-side policies

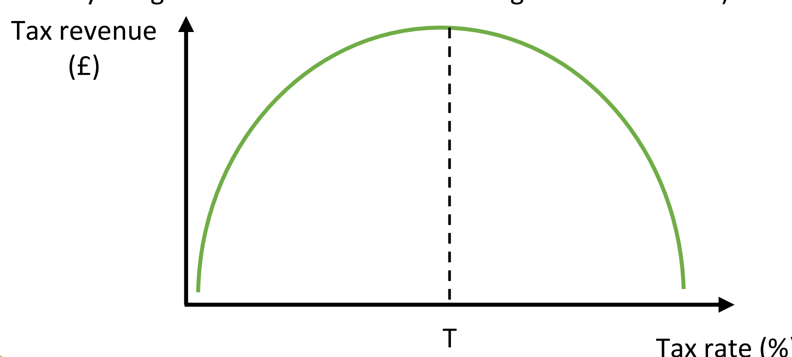
Free market supply-side policies are all about *removing barriers* that stop the economy from working smoothly and efficiently. Think of it as "decluttering" the economy so businesses, workers, and consumers can perform at their best. These policies usually focus on:

- Cutting **taxes** 💰
- Reforming the **labour market** 👷
- Reducing **government control** (privatisation & deregulation) 🏭

💰 Income Tax Cuts & Work Incentives

- **Income tax** = the percentage of your wages the government takes to fund public services.
- Lower taxes mean workers keep more of what they earn → making work more attractive.
- This can encourage people to work longer hours or even enter the workforce if they weren't working before.

📊 *Example:* The **Laffer Curve** is a cool little economic theory that shows how changes in **tax rates** can affect **government revenue** (that's the money the government collects from things like income tax).



13.1.2 Supply-side policies

Free market supply-side policies

🧠 **The Big Idea:**

- When tax rates go up, the government **earns more**, right?
- Well... only **up to a point.**
- At **0 % tax** the government collects **£0** (obvious).
- At **100 % tax** nobody would bother to earn (or they'd hide the money), so revenue is **£0** again.
- Somewhere in the middle there's a **sweet spot T** where revenue is *maximised*.

⚡ But caution: if taxes are already low, cutting them further may not change behaviour much. For example, dropping from 20% to 19% probably won't make someone suddenly work double hours.

Why does revenue fall after point T?

- **Lower incentive to work** – people skip overtime, turn down promotions, or leave the workforce.
- **Tax avoidance / evasion** – clever accountants or illegal hiding reduce the declared tax base.
- **Offshore shift** – high earners or mobile firms may move profits (or themselves) to lower-tax countries.

⚡ **Real-World Context**

- Over the past 30 years, the UK has gradually shifted taxes from **direct taxes** (like income tax) towards **indirect taxes** (like VAT on goods and services).
- There's also been an increase in **tax-free allowances** (the amount you can earn before paying tax), which helps low-paid workers.

13.1.2 Supply-side policies

Free market supply-side policies

🛠️ **Reduction in Trade Union Power**

- **Trade unions** are groups of workers banding together to negotiate better pay and working conditions.
- If unions have too much power, they may push wages above what businesses can afford, leading to fewer jobs.
- Reducing their influence could lower costs for businesses, encouraging them to hire more staff.

🏢 **Cutting Unemployment Benefits**

- If benefits (money given to people out of work) are very generous, people may not feel pressure to find jobs quickly.
- Reducing benefits creates stronger incentives to seek work.
- Downside: it could also increase poverty and inequality if people struggle to cope.

👷 **Less Labour Protection**

- **Labour protection** = rules like paid holidays, sick pay, maternity leave, and limits on working hours.
- These protect workers, but they also raise costs for businesses.
- Reducing protections could lower hiring costs, encouraging firms to take on more workers. But this might make jobs more insecure or stressful for workers.

⏳ **Zero-Hour Contracts**

- A **zero-hour contract** means workers aren't guaranteed any hours; they only work when the employer needs them.
- This gives businesses flexibility and can help reduce unemployment.
- However, it makes income less predictable for workers.

13.1.2 Supply-side policies

Free market supply-side policies

🏭 **Privatisation**

When the government owns a company (like a railway or a broadcaster), it might scare off private competitors because the government firm has deep pockets and advantages.
Privatisation means selling these companies to private owners, making the market more open and competitive.

Example:
In the 1980s, the UK government **privatised British Telecom (BT),** before that, telecoms were a government monopoly. After privatisation, lots of new companies entered the market (like Vodafone), giving customers more choice and better prices.

⭐ **Advantages of privatisation:**

- **More competition**: Firms now have to fight for customers! This cuts **X-inefficiency** (when businesses get lazy and wasteful) and usually means **lower prices** and **better quality** for everyone.
- **Boosts government cash**: Selling companies brings in money straight away, helping reduce the **Public Sector Net Cash Requirement (PSNCR).** Basically, the government's need to borrow money.
- **Less political interference**: Firms don't have to stress about changing their plans every time a new government gets elected. They can **invest with more confidence** in the long term.

⚡ **Disadvantages of privatisation:**

- **Natural monopolies become risky**: In industries like water and electricity, where it's impractical to have loads of competitors, a private monopoly could exploit customers. Some say the government should stay in charge here.
- **Some industries are too important**: Services like **hospitals, electricity, and public transport** are vital to society. Leaving them purely to private profit-seeking companies could be risky.
- **Externalities and inequality**: Private companies might not think about the broader impacts (like pollution), and poorer people might end up worse off.

13.1.2 Supply-side policies

Free market supply-side policies

📉 **Minimum Wage Changes**

The UK Government sometimes **steps into the labour market** to make things fairer and to **protect workers from being underpaid or exploited**.

Maximum Wage:

- A maximum wage is when the government sets a limit on how much someone can be paid.
- It would be **below the natural market wage.**
- **Example:** In some European football leagues, there have been talks about **salary caps** to stop players from earning millions every year.
- The goal is to **reduce income inequality** and **make pay fairer** across workers.
- But in real life, maximum wages are **very rare** because they can cause talented people to move abroad.

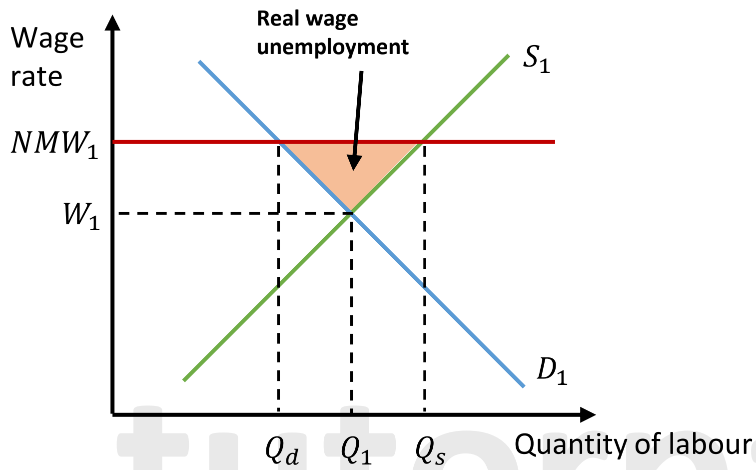
Minimum Wage:

- A minimum wage is a **legal rule** saying employers cannot pay workers less than a certain amount.
- It is set **above the market wage** to make sure people get a fair basic income.
- In the UK, the minimum wage changes **depending on your age**.

13.1.2 Supply-side policies

Free market supply-side policies

Understanding the diagram



Let's say we are looking at the market for **baristas** in coffee shops:

- At the start, the market wage is W_1, where the number of baristas needed by cafes matches the number willing to work.
- Then the government sets a **new national minimum wage** at $\boldsymbol{NMW_1}$ (higher than W_1).

What happens after that?

- **More people want to be baristas** because the pay is better (supply rises from Q_1 to Q_s).
- **Cafes want to hire fewer baristas** because the new wage is more expensive (demand falls from Q_1 to Q_d).
- Result: **More people are looking for jobs than there are jobs available,** this is **real wage unemployment**.

At wage $\boldsymbol{NMW_1}$, the gap between Q_d and Q_s shows how many baristas are now unemployed despite wanting to work.

13.1.2 Supply-side policies

Free market supply-side policies

Arguments for the National Minimum Wage

- **Reducing poverty**: A minimum wage helps lift the lowest earners above the poverty line, making sure they have enough income to cover basics like food, shelter, and heating. For example, in New Zealand, introducing a minimum wage boost helped thousands avoid falling into severe hardship.
- **Reducing gender wage gaps**: Since women are often overrepresented in lower-paid roles (think childcare workers or shop assistants), a decent minimum wage helps narrow the income gap between men and women.
- **Fairness**: Everyone deserves a fair wage that reflects their effort and prevents exploitation, especially in sectors like cleaning or hospitality where low pay was common before minimum wage laws came in.
- **Avoiding the "unemployment trap"**: If people earn more working than they would on welfare benefits, they are more motivated to find and keep a job. This helps reduce long-term unemployment. In places like Canada, stronger minimum wages have been linked to increased workforce participation.

Arguments against the National Minimum Wage

- **Risk of job losses**: If wages are pushed up too high, some businesses might cut jobs to save money, or even close down. For example, some small cafes in the USA closed after a sudden hike in minimum wages.
- **Higher costs for businesses**: Companies may face bigger wage bills, leading them to raise prices. This could make everything from burgers to haircuts more expensive.
- **Ignoring regional differences**: A single national wage might not fit everywhere. Living costs in London are way higher than in rural Wales, for instance. A flat minimum wage could either be too low in expensive cities or too high in cheaper areas, affecting jobs unevenly.

13.1.2 Supply-side policies

Free market supply-side policies

Again, free market supply-side policies are designed to let the economy "run free" by reducing government interference, think tax cuts, deregulation, and privatisation. These policies aim to make businesses more efficient and competitive.

But like everything in economics, there are both **upsides** and **downsides.**

🌟 **Advantages**

- **No big strain on government spending**
    - Because the government isn't funding lots of projects directly, taxpayers' money doesn't have to cover huge costs.
    - Instead, the private sector invests.
    - Example: If a railway is privatised, the company (not the government) pays for upgrades and maintenance.
- **Better use of resources (resource allocation)**
    - *Definition:* Resource allocation = how an economy decides to use its workers, money, and materials.
    - Free markets encourage businesses to be efficient because they have to compete.
    - Example: If one company wastes too much on admin, a rival offering cheaper prices will win more customers.

13.1.2 Supply-side policies

Free market supply-side policies

🚨 **Disadvantages**

- **Time lags** ⏳
    - It takes *years* for these policies to show real benefits.
    - Example: Cutting taxes today doesn't mean workers instantly produce more; the effect builds slowly.
- **Equity problems (fairness issues)**
    - *Definition:* Equity = fairness in how income and opportunities are shared.
    - Reforms may mean lower wages or less protection for some workers.
    - Example: Deregulation might allow firms to cut staff benefits, making income inequality worse.
- **Environmental costs** 🌍
    - Big projects can harm nature.
    - Example: Building a hydroelectric dam boosts energy supply but can flood habitats and damage ecosystems.
- **Vested interests (powerful groups influencing outcomes)**
    - Sometimes policies don't work as planned because big players get special treatment.
    - Example: In privatisations, politically connected firms may scoop up government assets "on the cheap," instead of genuine competition creating efficiency.

13.1.2 Supply-side policies

Interventionist supply-side policies

Unlike free-market policies (which let businesses "do their thing"), **interventionist supply-side policies** are where the **government steps in directly** to help boost the economy. They aim to increase both **aggregate supply** (the economy's productive capacity) and sometimes **aggregate demand** (overall spending in the economy).

The catch? They often take longer to show results than quick fixes like tax cuts. But the long-term benefits can be huge. 🚀

🎓 Education

Education reform + investment = a smarter, more adaptable workforce.

- **Reducing occupational immobility** (👉 *definition:* when workers struggle to switch between different types of jobs).
  - Example: If a coal miner retrains as a software coder, they can move into new industries instead of being stuck unemployed.
- **Boosting productivity** — better-educated workers are usually more efficient, so the whole economy produces more.
  - Example: Investing in STEM education in schools can fuel growth in tech industries.

🛠 Training

Training is like education's best friend; it helps workers stay sharp and adaptable.

Ways governments can support training:

- **Directly:** e.g. welfare recipients might get benefits only if they complete job training.
- **Indirectly:** e.g. offering tax breaks to companies that invest in employee training.

Example: A government might subsidise apprenticeships in renewable energy to prepare workers for the green economy 🌱.

13.1.2 Supply-side policies

Interventionist supply-side policies

🔬 Research and Development (R&D) Subsidies

R&D = research + innovation 💡

When businesses (or universities) do research, they can invent better tech or new ways of working, which boosts productivity.

- The government can give **grants** (free money for research) or **tax breaks** (companies pay less tax if they invest in R&D).
- Example: UK grants for green technology have supported innovations like offshore wind turbines.

🏭 Industrial Policy

This is when governments give the business world a little "nudge" through **rules, laws, and incentives**.

- Could involve changing labour laws (like trade union reforms).
- Could mean laws to encourage business start-ups or help small businesses compete.
- Example: South Korea's government heavily supported car and tech industries in the 20th century → now they've got Hyundai and Samsung.

💡 **Exam Tip:** Supply-side policies are often sneaky, they cross over with lots of other topics (like education, unemployment, growth). Always make those links in your answers for extra marks ✨.

13.1.2 Supply-side policies

Interventionist supply-side policies

Interventionist supply-side policies are when the **government directly invests in or supports industries and infrastructure** to boost the economy's productive capacity. Think of it as the government stepping in as the "coach" rather than just letting the "players" (businesses) figure it out themselves.

Here are the **pros and cons** ⬇️

✅ **Advantages**

- **Direct support for key industries** 🏭
  - Giving subsidies (government financial help) to important industries can boost growth, reduce unemployment, and even help exports.
  - Example: If the government funds green energy projects (like solar or wind farms), it creates jobs, reduces reliance on imported fuel, and can make the country a leader in renewable exports. 🌍⚡
- **Better living standards** 🏘️
  - Big investments in infrastructure (roads, schools, hospitals, broadband internet) make everyday life easier, healthier, and more productive.
  - Example: Expanding public transport means people spend less time stuck in traffic 🚊 → more time for work, family, or leisure.

13.1.2 Supply-side policies

Interventionist supply-side policies

❌ **Disadvantages**

- **Time lags ⏳ + political changes ⚖️**
  - These policies often take **years (or decades)** to show results.
  - Plus, if a new government comes into power, they may cancel or cut funding for projects, making them less effective.
  - Example: The UK's **High Speed Rail project (HS2)** has been scaled back and delayed multiple times due to political and budget shifts.
- **High costs** 💸
  - These projects are **expensive** and usually paid for by higher taxes or government borrowing (which adds to national debt).
  - Example: Building new airports, highways, or high-speed rail can cost billions; money that might otherwise be used for healthcare or education.

13.1.2 Supply-side policies

Other strengths and weaknesses of supply-side policies

✅ **Strengths of Supply-Side Policies** 🚀

- ✓ **Lower Prices for Consumers** 🛒 – More efficient production reduces **costs**, leading to **lower average price levels** (helping fight inflation).
- ✓ **Faster Economic Growth** 📈 – By making businesses **more efficient** and workers **more skilled**, supply-side policies **increase the economy's long-term growth rate**.
- ✓ **Lower Unemployment** 👩‍💼 – Policies like **education investment** and **labour market reforms** help **get more people into work**.
- ✓ **Better Infrastructure** 🏗️ – Government investment in **transport, energy, and digital infrastructure** improves **quality of life** and **supports economic growth**.
- ✓ **Boosting International Trade** 🌍 – When a country becomes **more productive**, its goods and services become **cheaper and more competitive abroad**, increasing **net exports**.

🔷 **Example:** In **Singapore**, government investment in **education and digital infrastructure** has helped create a **highly skilled workforce**, attracting **foreign investment** and boosting long-term growth.

13.1.2 Supply-side policies

Other strengths and weaknesses of supply-side policies

❌ **Weaknesses of Supply-Side Policies** ⚠️

- ❌ **Income Inequality Increases** 💰⚖️ – Labour market reforms, such as **weakening trade unions or reducing minimum wages**, can **lower worker pay**, benefiting businesses but **worsening income inequality**.
- ❌ **High Costs** 💸 – Policies like **building infrastructure** and **improving education** require **huge government spending**, leading to **budget deficits**.
- ❌ **Slow to Show Results** ⏳ – Supply-side policies take **years** to fully impact the economy. Governments **spend money now** but may **not see benefits for decades**.
- ❌ **Changes in Government** 🏛️ – Different political parties have **different priorities**. If one government **starts a major infrastructure project**, the next might **cancel or change it**, making policies **less effective**.

Please see the '13.2 Fiscal policy and supply-side policies Worked Examples' pack for exam style questions.

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