

Fiscal Policy

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Introduction

- **Major events of the economy: Growth, employment...etc.**
- **What is fiscal policy?**
 - The word fiscal has been derived from the French/ Latin word '*fisc*' which means treasury
 - So fiscal policy means policy of treasury
- **Who manages the treasury of the country?**
- Government

Introduction

- Government's actions affecting its receipts and expenditure
- Macro policy measures taken by the government in order to adjust its spending levels along with tax rates
- **Two major instruments-tax rate and public expenditure**
- Fiscal policy deals with the taxation and expenditure decisions of the government

Objectives

- Full employment
- Price stability
- Accelerating the rate of economic development
- Equitable distribution of income and wealth
- Economic stability
- Capital formation and growth
- Encouraging investment
- Balance of payments
- Balanced regional development

Full Employment

- Avoid unemployment and to achieve a state of near full employment
- The State should spend sufficiently on social and economic overheads-will create more employment opportunities
- A properly planned public sector investment will not only expand income, output and employment but will also step up effective demand
- Private investment can also be encouraged - tax holidays, concessions, cheap loans, subsidies etc.

Price Stability

- Economic growth and Stability are joint objectives for developing countries
- Economic stability-Inflation-contractionary fiscal policy (raising taxes and reducing spending)
- Economic stability-economic slump- expansionary fiscal policy (cuts taxes to spur economic growth)

Economic Growth

- Accelerate the rate of economic growth
- Fiscal measures like taxation, public borrowing and deficit financing should be used

Optimum allocation of Resources

- Allocation of resources across different sectors and occupations
- To gear the economy, government can push the growth of social infrastructure
- Public expenditure, subsidies and incentives can favourably influence the allocation of resources

Equitable distribution of income and wealth

- Focus on low income groups through public investment
- Well-planned public expenditure through human capital
- Highly progressive tax policy
- Luxurious items subject to heavy taxation

Economic Stability

- Promote economic stability in the face of short run international cyclical fluctuations
- Maintaining economic stability in the face of internal and external forces
- For example – in the period of boom export and import duties should be imposed to minimise the impact of international fluctuations
- During recession- government should undertake public works programme through deficit financing

Capital formation and growth

- Fiscal policy stimulates investment –that lead to capital formation
- Fiscal policy must be designed in two ways-
 - by expanding investment in public and private enterprises
 - By diverting resources from socially less desirable to more desirable investment channels

To encourage Investment

- Aims to accelerate the rate of investment in the public as well as private sectors of the economy
- Fiscal policy should encourage public investment in the first instance- that will effect in increasing volume of investment in private sector

Balance of Payments

- Export Promotion
- Import substitutions

Balanced Regional Development

- Higher Public expenditure in less developed regions
- Provision of aid and other assistance to regions which are less economically developed.