

# Fiscal Policy

# Fiscal Policy

## What is fiscal policy?

- Government changes in spending and taxes that are done to move aggregate demand (AD)

# Fiscal Policy

## How does the government move aggregate demand (AD)?

Aggregate Demand =  $C+I+G+(X-M)$

- G - Government can change its spending
- C – Government can change taxes on consumers
- I – Government can change taxes on business profits

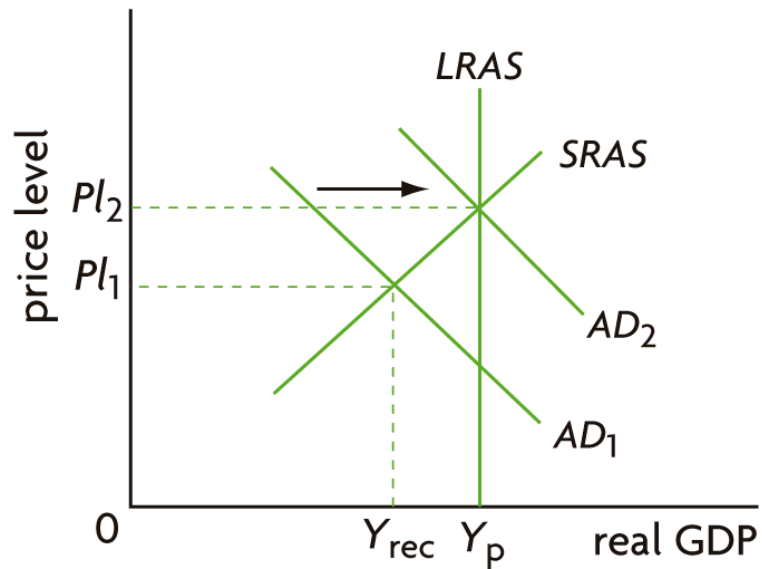
# Expansionary Fiscal Policy

Government actions to move the AD curve to the right and fix a recessionary gap.

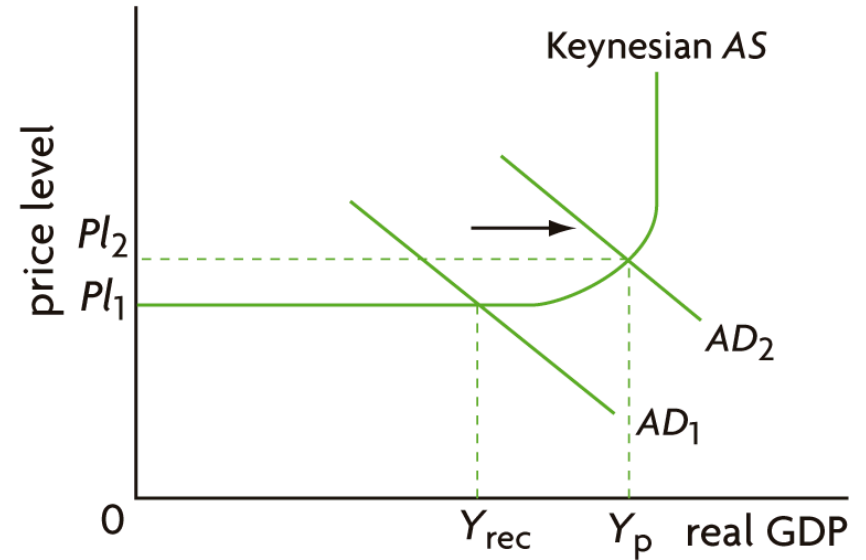
1. Increasing government spending
2. Decreasing taxes
3. Both

# Expansionary Fiscal Policy

(a) The monetarist/new classical model



(b) The Keynesian model



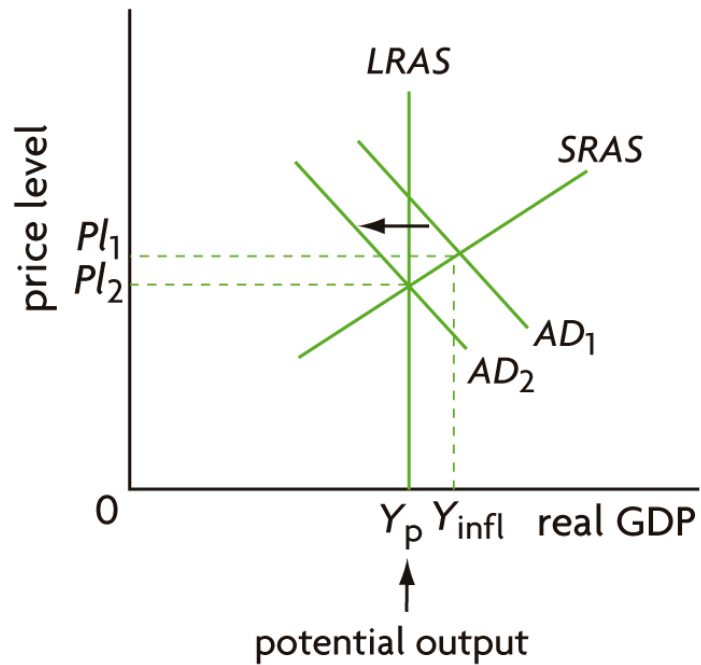
# Contractionary Fiscal Policy

Government actions to move the AD curve to the left and fix an inflationary gap.

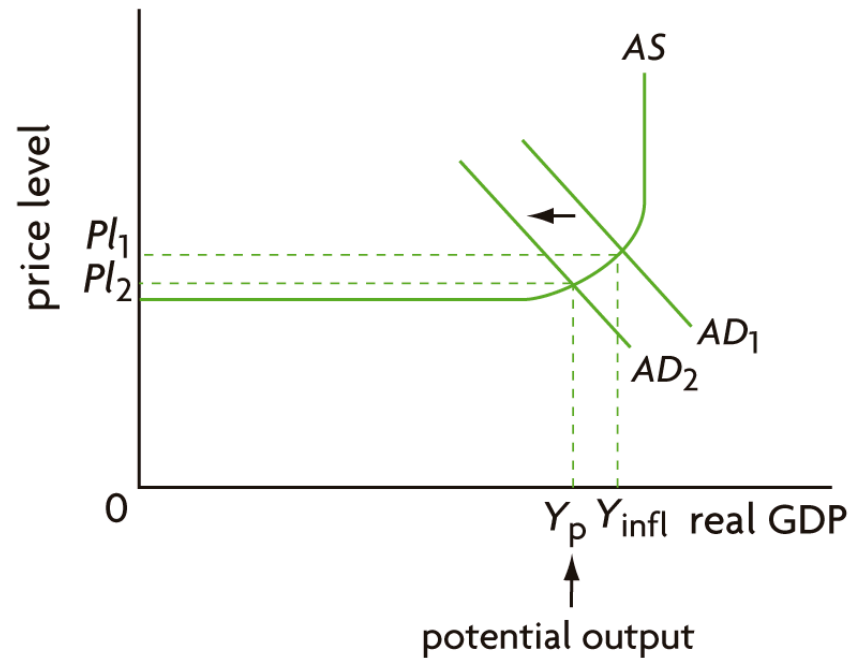
1. Decreasing government spending
2. Increasing taxes
3. Both

# Contractionary Fiscal Policy

(a) The monetarist/new classical model



(b) The Keynesian model



# Not all spending and taxes are the same

## Expansionary Policy

1. Increasing government spending
2. Decreasing taxes
3. Both

## Contractionary Policy

1. Decreasing government spending
2. Increasing taxes
3. Both