

Lecture 20 Fiscal Policy II

Demand Side Fiscal Policy

- Keynesian roots
- Countercyclical

Critiques of Keynesian Fiscal Policy

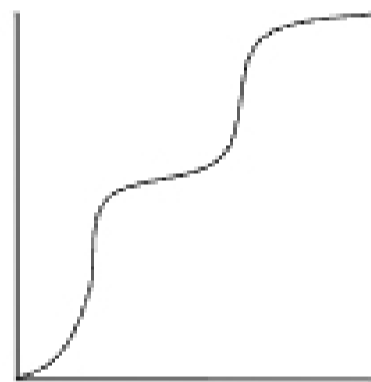
- Lags
- Crowding-out

Supply Side Fiscal Policy

- Examples
- Tax rates and tax revenues
- 1980s experiment

Demand Side Fiscal Policy

Countercyclical: smooth out the business cycle



Lags:

recognition

implementation (pass both houses of congress and get president to agree)

impaction (stimulus, gov policy to actually work through the economy)

Keynesian answer

automatic stabilizers

A Progressive income taxes

B Corporate profit taxes

C Unemployment insurance

D Welfare payments

AB change T

CD Change G

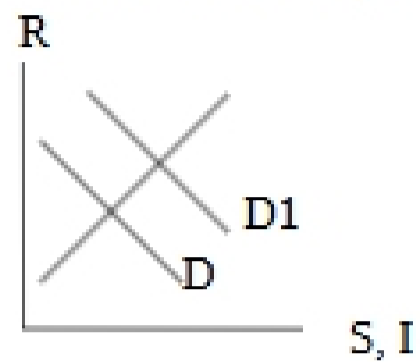
Crowding out

Government spending crowds out private spending

G increase c, I decrease

2012: Balanced budget

2013 G increase by \$100 billion: no new taxes



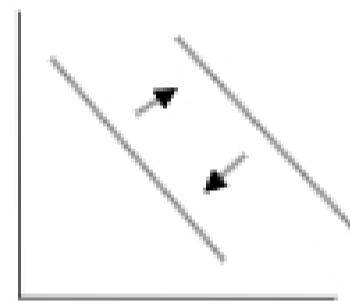
2012	2013
s=200	250
i=200	150

net changes

G+100

I-50

Does Keynesian Fiscal Policy work?



Answer:

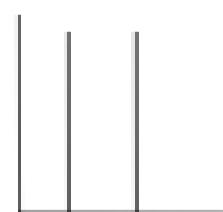
Much debate among economists

Little debate among politicians

Supply Side Fiscal Policy

Demand vs Supply

Spending Producing



Supply Side: Sample Proposals

Tax credits for research and development

Education subsidies

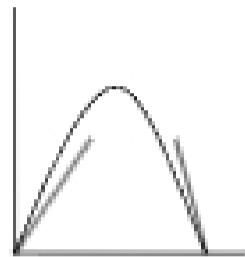
Lower corporate profit taxes

Lower marginal tax rates

Tax Rates and tax revenue

The math:

Income tax revenue



Laffer curve:

Incentives affect behavior: higher tax rate reduces incentives for production

Tax rates and Tax Revenue

1980s experiment

All tax rates fell: total revenue fell

top 1 percent paid 40 percent of tax