

3.8 Fiscal Policy

Name: _____ Class: _____ Date: _____

Total: 8 marks

Objective

Build the skills to answer exam questions on **fiscal policy**.

You must be able to:

- define **fiscal policy** 财政政策 as government spending and taxes
- distinguish **expansionary** 扩张性 from **contractionary** 紧缩性 fiscal policy
- apply the **spending** and **tax multipliers** to estimate the change in output
- relate a fiscal choice to closing a recessionary or inflationary gap

1 Worked examples

Study these first. Each one shows the method for a question type used later.

■ Fiscal policy

The government's use of **spending** and **taxes** to influence aggregate demand.

■ Expansionary vs contractionary

- **Expansionary** (more spending or lower taxes) → AD **right**; used to close a **recessionary** gap.
- **Contractionary** (less spending or higher taxes) → AD **left**; used to close an **inflationary** gap.

■ Sizing the policy

Use the spending multiplier: the spending change needed = $\frac{\text{output gap}}{\text{multiplier}}$.

2 Practice

2.1 Define fiscal policy. [1]

2.2 State the type of fiscal policy used to close a recessionary gap. [1]

2.3 State the effect of expansionary fiscal policy on AD. [1]

3 Exam-style questions

3.1 Expansionary fiscal policy involves [1]

- A cutting government spending
 - B raising taxes
 - C increasing government spending
 - D raising interest rates
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3.2 To fight high inflation, the government should use _____ fiscal policy. [1]

- A expansionary
 - B contractionary
 - C monetary
 - D no
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3.3 An economy is in a recessionary gap of \$100 billion, with $MPC = 0.8$.

(a) Name a fiscal tool that could close it. [1]

(b) State the effect on AD. [1]

(c) Find the rise in government spending needed. [1]

4 Go further

- work through the **3.8 Fiscal Policy** lesson on the **Learn** page;
- read the **National Income and Price Determination** section of the AP Macroeconomics handout on the **Know** page.

Solutions

2.1 the government's use of spending and taxes to influence the economy.

2.2 expansionary fiscal policy.

2.3 it increases (shifts right) AD.

3.1 C.

3.2 B.

3.3 (a) increase government spending (or cut taxes). (b) AD shifts right. (c) multiplier $= \frac{1}{1 - 0.8} = 5$, so spending $= \frac{100}{5} = \$20$ billion.