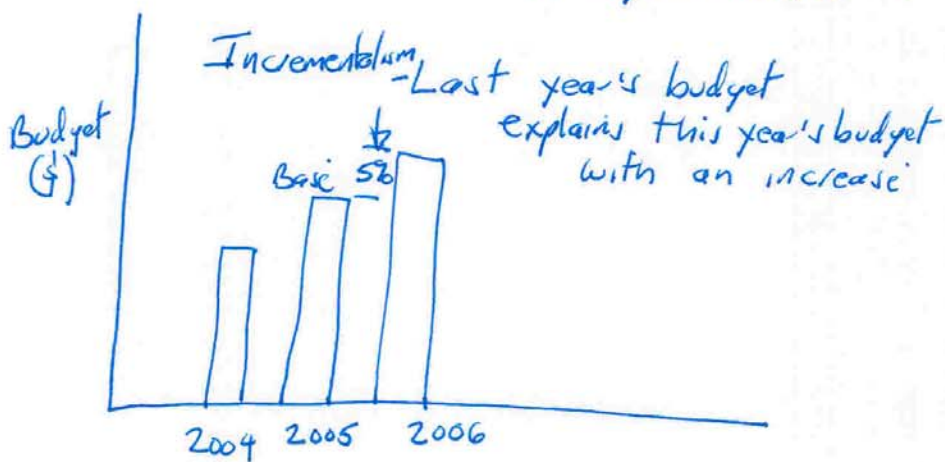


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## Ch. 7 Economic Policy Incrementalism and Economic Policy

- Fiscal Years
- Calendar Year (City of Newark)
  - Federal (Oct. 1 - Sep. 30)
  - State, University (July 1 - June 30)



- Economic policy ought to be rational
- growth in economic output
  - standard of living
  - full employment
  - stable prices, low inflation

## Economic Theories

2/

For homework, print out statistics for following indicators since 1970:

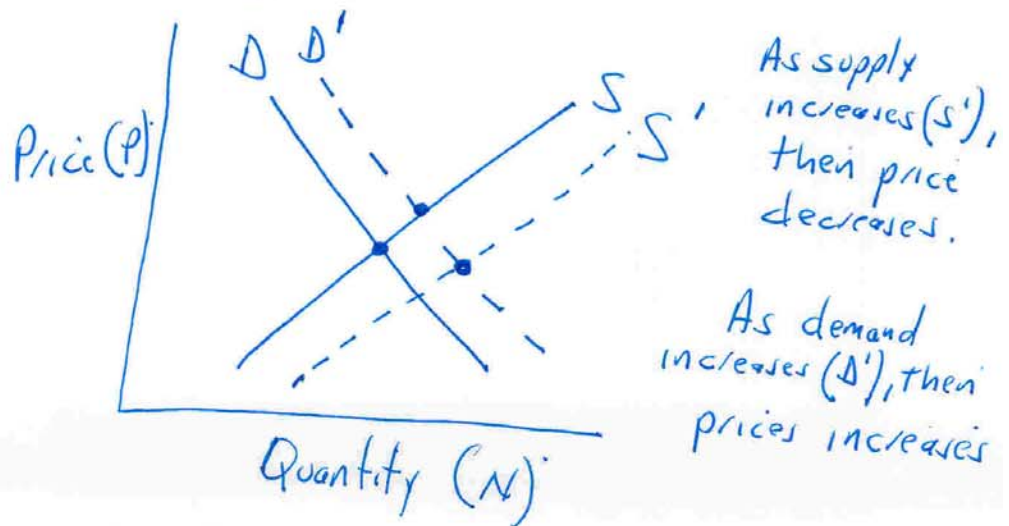
- inflation
- employment rate
- oil
- stock

### ① Classical Economic Theory

- Self adjusting
- employment
- productivity
- wages

If demand  $\uparrow$  and inventory  $\uparrow$ ,  
then prices will  $\downarrow$

Law of Supply and Demand



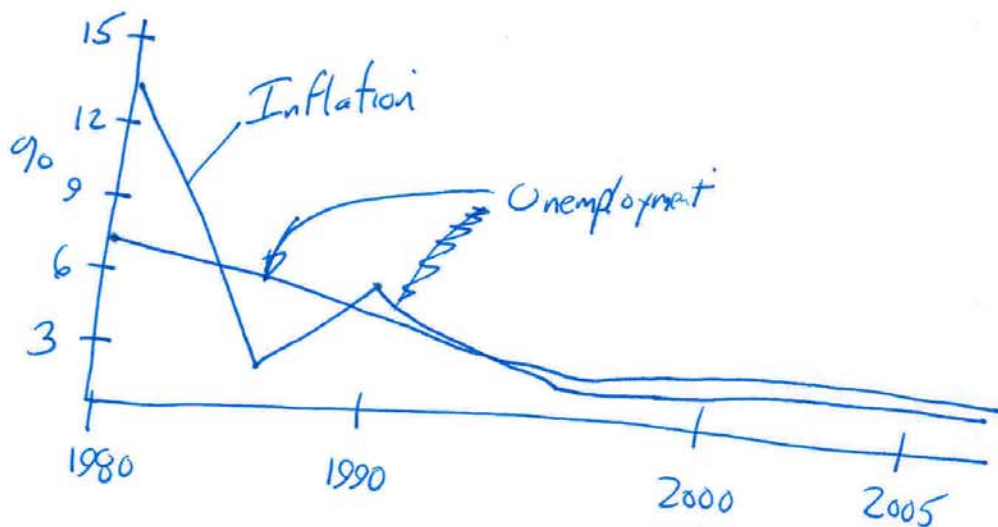
## ② Keynesian Theory

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The depression of the 1930's shattered classical theory. Unemployment ranged from 18% - 25%.

If the gov't spends more money during economic recession, it will lower taxes, and in turn the public will have more money to spend.

Fig. 7-2



If the inflation rate increases, then interest rate increases, resulting in slow economic growth.

Low inflation rates contributed to the nation's booming economy in the late '90s.

The economy would be worse in the 4/ early 2000's if inflation were not so low.

The individual banks borrow from the 12 Federal Reserve Banks. ~~which~~ The Federal Reserve lends out money at discount rates usually 2% above the inflation rate. The individual banks then lend money to the public at a rate 2% higher than the discount rate. This difference is called float.

• Federal Reserve lends <sup>to</sup> banks at 3%, then individual bank lends ~~for~~ money at 5%.

Incremental Table 7-1

1959	<u>Fed. Spending</u>
	92.1 Billion
2005	2.4 Trillion

Supplemental Appropriations for war in Iraq  
= 87B

### ③ Supply-side Economics

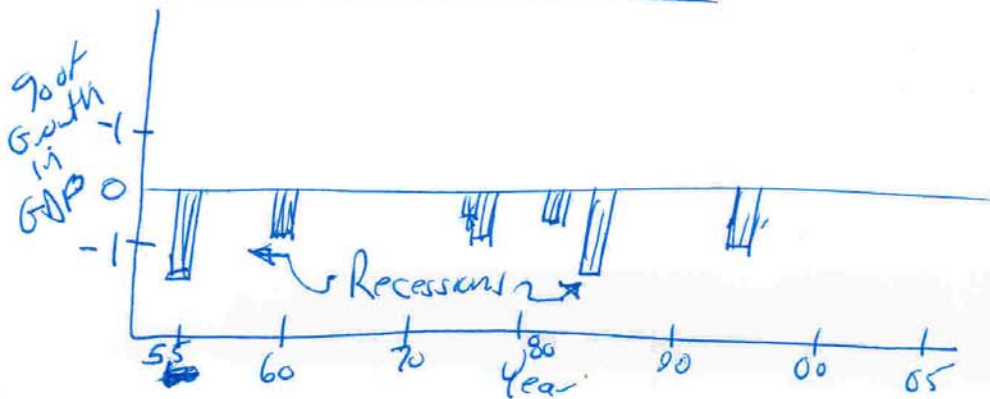
⑤

- Increase the overall supply of goods
- Reduce inflation
- Based on the free market.
- Gov't is the problem; Gov't taxing is the problem.
- Reagan tried to achieve:
  - cut spending
  - reduce income taxes
  - slowed the growth of regulations

Actually Ronald Reagan's policies resulted in increase in spending and large annual budget deficits.

The recession of the early 1980's resulted in Clinton's election.

Fig. 7-1 Economic Growth



In 2001 George W. Bush initiated tax reductions (6)

- In late 1990's, the stock boom bubble burst.
- Large spending after 9/11 returned the federal budget to annual deficits.

(4) Monetary Economics - All of the money in circulation is a measure of the economy.

The fed increases supply of money from banks which in turn increases money in circulation.

Fig. 7-4 Changing Fed. Budget Priorities

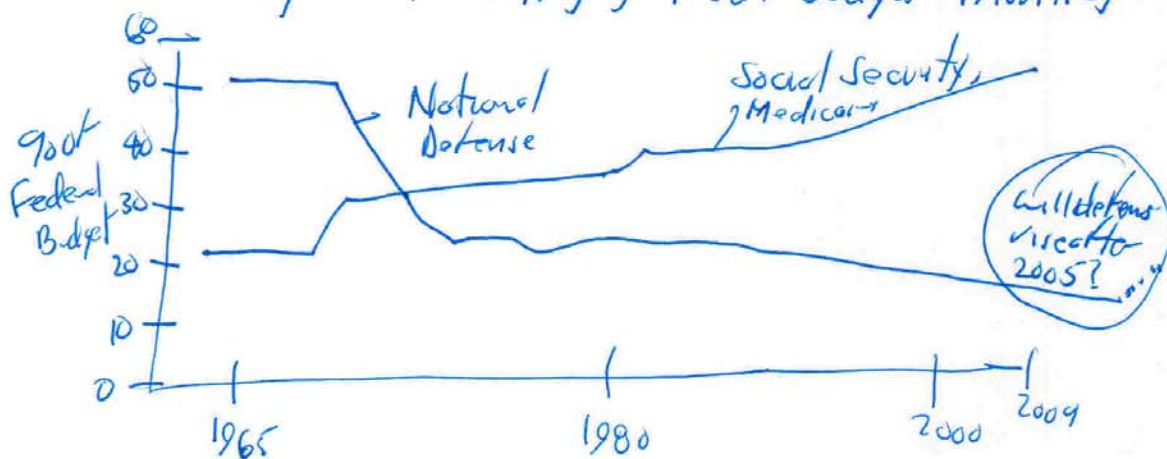


Fig. 7-5 Annual Federal Deficits & Surpluses

(7)

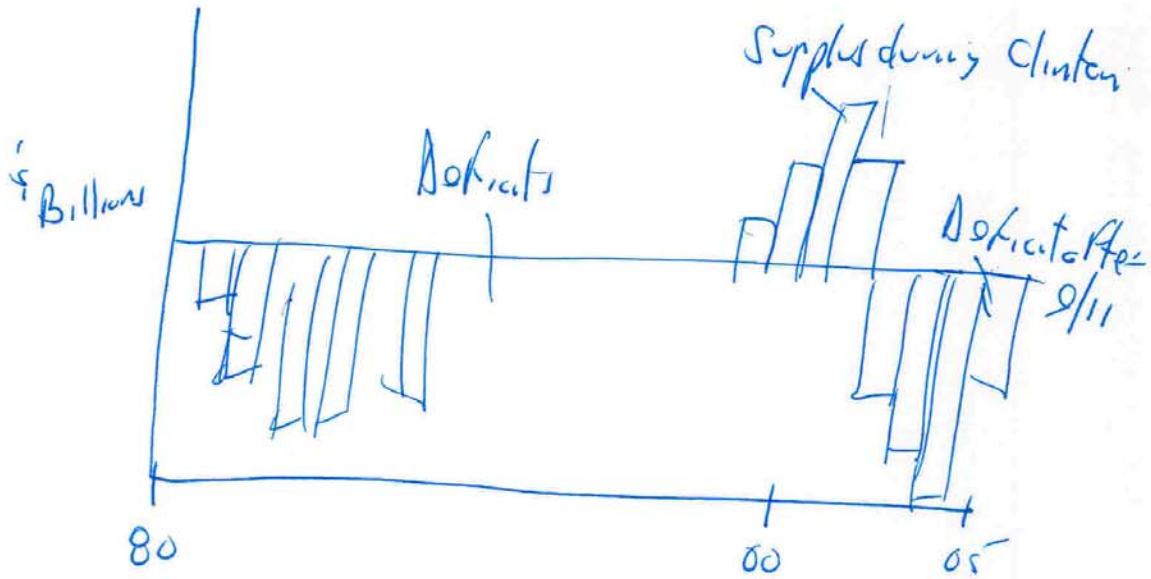


Fig. 7-6 Federal Budget Process

OMB Introduces President's Budget Jan.  
 House / Senate Budget Committee May

Appropriations Committees

Presidential Signs or Vetoes. - The line item  
 veto is unconstitutional. The President  
 must sign the whole bill or veto it.

Resolutions / shutdowns by Oct 1, the beginning of the  
 Fiscal Year.

## Entitlements

8/

Almost Half of all Federal spending are entitlements such as social security, welfare, medicare, etc.

Fig. 7-3 Federal Budget

