Role of Government

IGCSE

Role of Government in Mixed Economy

Government in mixed economies having following responsibilities: Provide Public goods like roads, parks, defense, street lights.

Provide necessary goods and services to citizens which are not public goods but are important for citizens' welfare like education and health care

Role of Government in Mixed Economy

To ensure fair income distribution through taxing the rich people and providing income support to poor people through programs like unemployment benefits etc.

Macroeconomic Objectives

Governments in all countries pursue macroeconomic objectives. Any objective that relates to the entire economy is macroeconomic objective. These include:

1. High economic growth (rate of increase of GDP)
2. Low and stable rate of inflation
3. Low unemployment
4. Stable Balance of Payments
5. Stable Exchange Rate

High Growth Rate

Rate of increase of GDP (gross domestic product – the total value of all goods and services produced in an economy) is governments primary objective.

5 % growth rate refers to that national income is increasing at 5 percent each year. For instance if last year a country's GDP was Rs 100 million this year it would be Rs 105 million.

High Growth Rate

The higher the growth rate the better it is because it means that the country's total income is increasing at a faster rate.

Low and Stable Inflation

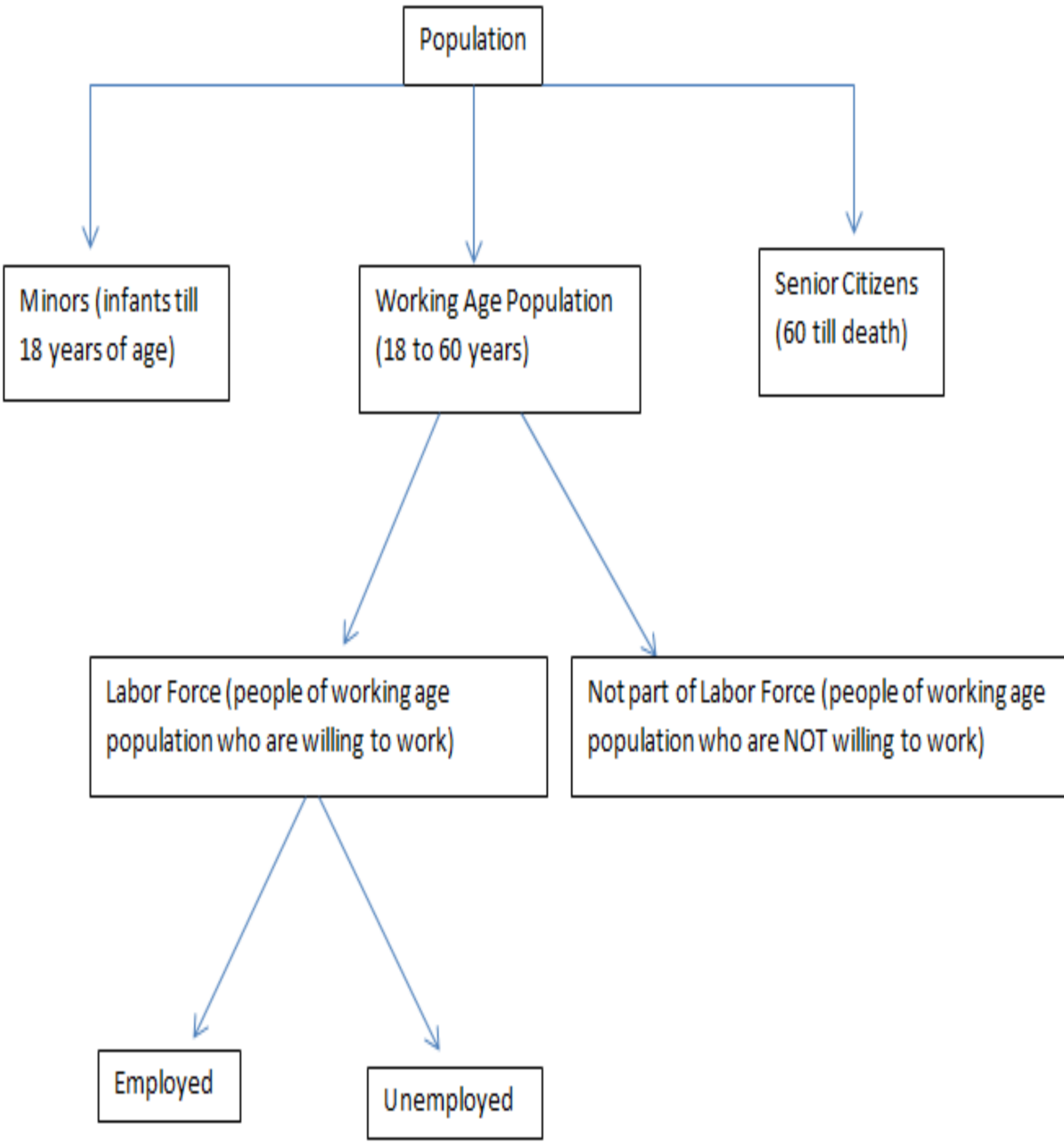
The inflation refers to rise in general price level. It estimates the increase in cost of living. 10 percent inflation means that products' prices are on average 10 percent higher this year.

Low and stable inflation is desirable since it does not erode consumers' purchasing power like high inflation rate.

Low and Stable Inflation

Secondly low rate of inflation encourages investment since slight increase in goods' prices increase producers' profits incentivizing them to increase their output.

Low Unemployment



Low Unemployment

People who are able and willing to work but are unable to find job are defined as unemployed.

Low unemployment is important for achieving high economic growth rate. Unless not all or majority of people are willing to work are working there will not be high output.

There are different reasons for unemployment which require different strategies.

Stable Balance of Payments

Balance of Payments (BOP) is an official documents that records all of an economy's international transactions during certain time period.

BOP surplus means that value of exports were greater than imports and BOP deficit means that import value was greater than export revenue.

Stable BOP means that export and import value balance each other over time.

Stable Exchange Rate

Exchange Rate is value of once currency in terms of another. How many rupees would buy one dollar and vice versa refers to exchange rate.

Stronger exchange rate of rupees (or appreciate of exchange rate) refers to few units of our currency buying more units of foreign currency and vice versa.

Macroeconomic Policies

Any government has following 3 macroeconomic policies available to achieve its macroeconomic objectives:

1. Fiscal Policy
2. Monetary Policy
3. Supply Side Policies

Fiscal Policy

Fiscal Policy relates to government revenue collected through taxation and government spending.

Budget Surplus refers to situation when government revenue is greater than government expenditure.

Budget deficit refers to a situation when government expenditure is greater than government revenue.

Monetary Policy

Monetary Policy refers to interest rates and is **independently set** by the central bank.

Interest rates being the cost of borrowing affect the level of economic activity in the country. Lower interest rates encourage investment and consumption since the cost of borrowing is low and vice versa.

Supply Side Policies

Supply-side policies are government attempts to increase **productivity** and increase **efficiency** in the economy. If successful, they will shift aggregate supply (AS) to the right and enable higher economic growth in the long-run.