Chapter 12

Government objectives and policies

1. Government Spending

: Government spending is used to provide a range of pubic services. For example, Health care, education, defence, care for the elderly, child protection, policing etc.

2. How can governments affect business Activity ?

: The government can affect business activity in a number of ways. It can

- Change the law
- Influence the rate of interest and exchange rates in the economy
- Change levels of government expenditure and taxation
- Introduce policies that have a direct impact on businesses such as giving subsidies to farmers

2.1 Infrastructure provision

: This includes building schools, hospitals, roads, railway system.

Benefits

- Private firms are likely to get most of work.
- More employment

2.2 Legislation

: Government is to provide a legal framework in which businesses can operate and ensure that vulnerable groups are protected.

2.2.1 Consumer protection

: Without government regulation, some firms may exploit consumers by using anti-competitive practices (attempt by firms to prevent or restrict competition)

2.2.2 Competition policy

: Governments should try to promote competition.

- Encourage the growth of small firms
- Lower barriers to entry

2.2.3 Environmental legislation

: If businesses fail to comply with environmental laws they may be fined or force.

2.2.4 Trade policy

: Governments can use trade barriers to restrict trade

- Tariffs : a tax on imports, which makes then more expensive
- Quota : A physical limit on the amount allowed into the country
- Subsidy : the giving of financial support, such as grants or tax breaks, to exporters or domestic producers that face fierce competition from imports
- Administrative barriers : the use of strict health and safety or environmental regulations and specifications to make importing more awkward.

3. Effects of interest rates on businesses

3.1 When the interest rate rises, cost of borrowing will increase.

3.2 The purchase of capital goods funded by borrowing is discouraged because it is more expensive.

3.3 Higher interest rate usually mean that demand in the economy falls. This is because consumers are less willing to borrow money to fund spending.

4. Effects if interest on consumer spending

4.1 House-owners with mortgages will be affected negatively when interest rates rise.

: Consumers need to pay interest

: less disposable income (income after taxes and bills)

: less ability to spend on goods and services

: less aggregate demand

4.2 Savers will be hit if interest rates are low

: less income on saving

: less spending on goods and services