<u>Report on how two Government Policies are used to influence the chances of success</u>

Fiscal Policy or Monetary Policy

Table of Contents

Introduction

The government has many tools they can go about using to try and help their nation's economy economically prosper. However, some of the major policies that the government uses are fiscal policy and monetary policy. The fiscal policy is the government collects from the general public to help run the government. The fiscal policy is what the government helps do to stimulate the economy by either cutting taxes or increasing taxes. The fiscal policy the government also goes about doing it by spending, spending on the military, unemployed people, government salaries, government buildings, military spending, etc. This is called the government expenditures. Monetary policy is what the central bank done to either help stimulate the in un employment or economic growth. The monetary policy goes about stimulation the economy by changing the levels of interest the central bank has (Semmler et al., 2021).

The goal of this essay is to delve into the aspects of running economies using fiscal and monetary policies by the government of UK and its implications on policy objectives. It will be important to try and comprehend how the policies work by going in depth on the two policies and the instruments involved in ensuring that these policies are achieved. Two main policy objectives will be concentrated on and these will be analysed in the Export led growth and sustain economic growth. Looking at how fiscal policy and monetary policy can be used to help economy immunise itself from the economic problem and the implication to the society where both policies are applied (Ahmad & Satrovic, 2023).

Policies and Theories

Fiscal and monetary policies are two of the most commonly used macroeconomic tools to help run the economy of the United Kingdom. The monetary policy and the fiscal policy.

Fiscal Policy

When the economy is weak or in a recession, fiscal policy can be used to try to increase aggregate demand and therefore output. An expansionary fiscal policy will typically involve government spending increasing and taxes decreasing (Larch et al., 2021). Money is put into the hands of consumers through a tax cut, this is likely to lead to an increase in aggregate demand (AD) but the multiplier effect will mean that real GDP will increase significantly more. Government spending will also increase from welfare payments and infrastructure projects and this will also create growth in the economy (Bilbiie et al., 2021).

Oppositely, in times of overheating or high inflation, the government would at times want to cool down the economy by implementing contractionary fiscal policies. This is evident when the government decides to raise taxes. The main purpose is to raise tax to reduce disposable income of the population thus reducing consumer spending as well. Reducing expenditure on non-essential projects and programs which the government believes would be helping the raise of disposable income and demand, theoretically assumed as inflationary (Lenoël & Young, 2020).

One specific example of the use of discretionary fiscal policy took place during the great recession when the UK government implemented expansionary fiscal policy by cutting tax and increasing spending on public infrastructure. This was done in an attempt to boost economic growth and prevent the UK economy from slipping into a deep recession, during periods of high inflation the government have implemented a policy of austerity to reduce government borrowing and curb inflationary pressures (Bonam et al., 2020).

Monetary Policy

Monetary policy is implemented by the UK's central bank, the Bank of England. It is said. Alternatively, if inflation becomes a problem and the economy is expanding too quickly, the central bank may raise interest rates to slow down the economy and cool off inflation. Higher interest rates make borrowing money more expensive which should cause people to spend less, and investment to decrease, thereby slowing the rate of economic growth and reducing inflation (Cesa-Bianchi et al., 2020).

Take, for instance, the actions of the Bank of England in the many years after financial crisis. In the aftermath of the financial crisis, the Bank of England implemented a policy of Quantitative Easing and cut interest rates to unprecedented lows in order to help stimulate the recovery in the UK. Conversely, in the more recent years when inflationary pressures began to grow, the Bank of England has gradually started to increase interest rates to try and maintain price stability and to avoid inflation getting too out of control (De Marco et al., 2021).

Fiscal and monetary policy are two important tools in the United Kingdom's economic toolbox. They are both important the management of the rate of inflation, aggregate demand, economic growth, unemployment, balance of payments, and the distribution of wealth and income. Monetary policy uses the tools of interest rates and interest rate creation, provided the banks co-operate to make deposits and loans. Fiscal policy can be used to affect national spending, national saving and national borrowing, the effects of inflation and the supply side of the national economy. Both monetary and fiscal policy makers aim to lower unemployment and inflation and to encourage economic growth by altering the conditions in which people in the economy live their lives (Bernanke, 2020). Both forms of policy have similar objectives: assists in the management of the cash flow of the economy of the United Kingdom to control the level of prices or inflation. Government operates the fiscal policy and the Bank of England operates the monetary policy. The recent objectives of the government through the fiscal policy were to improve economic growth, support the level of employment in the economy and reduce inflation.

Economic growth, employment and inflation have all been influenced by the Bank of England working through the monetary policy. The influence of the two types of policy is indirect. Each policy tries to influence the economic behaviour of individuals and institutions in the United Kingdom. The combined activity of the whole population of the United Kingdom is therefore steered by individuals who are knowingly or, unknowingly acting as if there were engaged in the economic activity of the entire population of the United Kingdom. The objective of the fiscal policy is to improve economic performance (Christophers, 2019).

Current or Historic Relevant Data

For the past ten years the UK has been through its share of economic high and lows that included the aftershocks of the global financial crisis to the uncertainties of Brexit, and the unprecedented challenges of the Covid-19 pandemic. Throughout these fluctuations the UK managed to survive and overcame with some tough resilient days of higher and lower that were definitely not to be taken lying.

Economic Growth

The UK government has the job of seeking to achieve economic growth as it will enhance peoples' standard of living e.g. with improved education, pensions and welfare benefits which will also overtime reduce poverty. Improved employment opportunities throughout the economy also help improve living standards by offering higher incomes and greater job security. There are several policies a government can adopt to promote economic growth including monetary and fiscal policy. These manage activity in the economy. Monetary policy is the demand side economic policy implemented by the Bank of England. It involves using interest rates and other monetary tools to control the level of aggregate demand in the economy. Fiscal policy involves the use of the government spending and taxation to influence the level of aggregate demand in the economy (Corlet Walker et al., 2021).

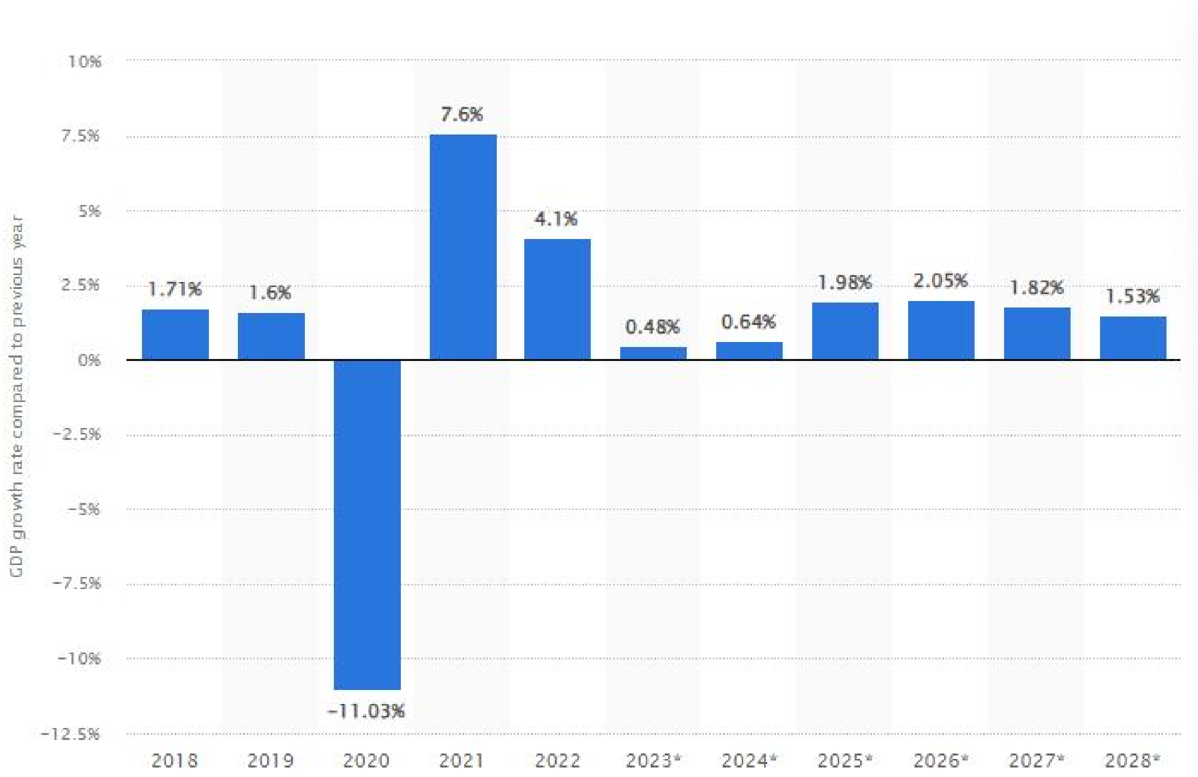

Figure 1 ***gross domestic product (GDP) growth rate from 2018 to 2028***

Fiscal Policy for Economic Growth

Fiscal policy is an extremely important tool that the governmental has at its disposal to stimulate economic growth. By strategically allocating resources to promote productive activities, it can lead to the desired economic expansion. The government may spend more on infrastructure, healthcare and education for instance and this will clearly generate jobs in the public sector and also generate demand for goods and services which ultimately leads to increased capital formation and productivity. Additionally, fiscal policy may be employed to grant tax incentives and credits to corporations and individuals thereby lifting the burden associated with tax payment. In so doing, there will be a likely increase in business activities and hence and improved investment climate for SMEs, large corporates and foreign investors (Avlijas et al., 2021).

Monetary Policy for Economic Growth

Another important element of economic policy is monetary policy. This includes anything having to do with money and banks. A major role that banks play in economic growth is the influence they have through interest rates and the amount of money in the economy. During times of economic slowdowns or recession, central banks adopt an expansionary monetary policy approach to attempt to influence borrowing and spending. Thus, lowering interest rates and pumping money into the financial system such as quantitative easing central banks believe that they can make money cheaper to borrow and invest and of course result in greater economic activity. Monetary policy can also promote economic growth when it manages to keep prices stable. A primary goal of central banks it to control inflation at a moderate level within a given price range. It is important to have stable low inflation because when prices are lower and stable people have better confidence is the economy and therefore spend and invest more money (Chugunov et al., 2021).

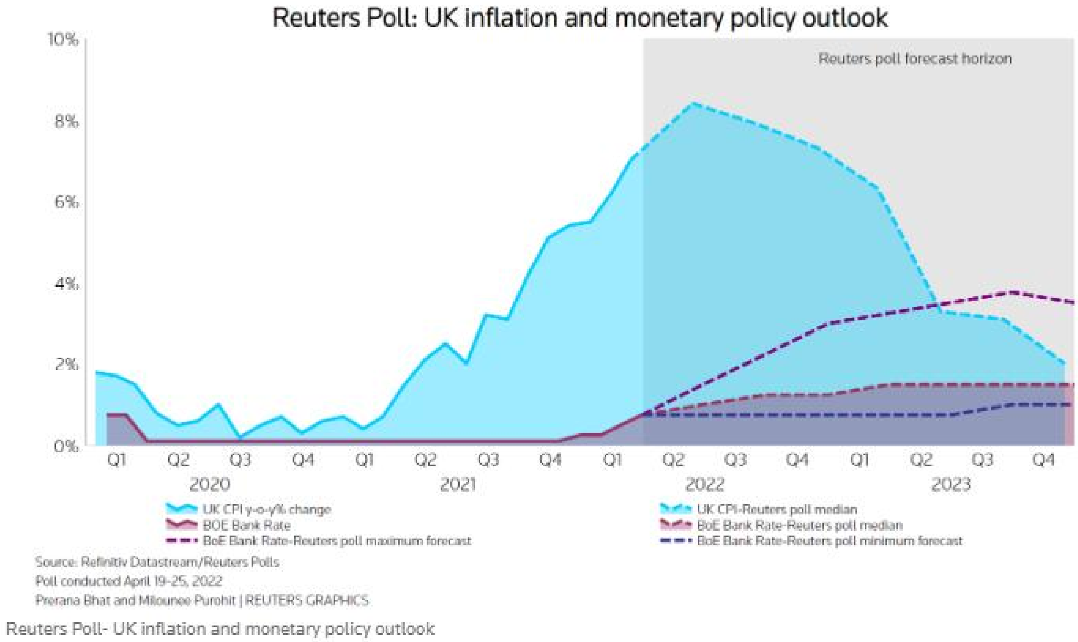

Figure 2 UK Inflation and Monetary Policy Outlook

Price Stability (Low Inflation)

Price stability is what most citizens, households and businesses in economies with low and stable inflation presume in their plans and behaviours, and it is a very important factor for growth of the whole economies and the global economic growth. If the inflation rates are too high then it may distort the decisions of people one of the problems are that current holders or owners of money can keep the money, so they do not make investment into other sectors of the economies. By keeping too much money, its purchasing power, however, decreases, so, at the end, its real value decreases. The real value of money and other financial assets does not depend on the nominal or face value, but also the inflation rate. If high inflation rates persist, then it is not profitable to keep money in private funds or in banks, so the holders of large cash funds would try to find a way to spend them (Forbes et al., 2019).

	Average 1998–2007	Average 2010–19	2022	2023	2024	2025	2026
Bank Rate (c)	5.0	0.5	2.8	5.3 (5.8)	5.1 (5.9)	4.5 (5)	4.2
Sterling effective exchange rate (d)	100	82	78	81 (82)	80 (81)	80 (81)	79
Oil prices (e)	39	77	89	90 (79)	81 (75)	77 (72)	74
Gas prices (f)	29	52	201	118 (113)	142 (139)	117 (114)	99
Nominal government expenditure (g)	7¼	2¼	4	6¼ (4)	¾ (3)	1¾ (1½)	2½

Sources: Bank of England, Bloomberg Finance L.P., Office for Budget Responsibility (OBR), ONS, Refinitiv Eikon from LSEG and Bank calculations.

Figure 3 UK Price Estimation Low Inflation

Fiscal Policy for Price Stability

Fiscal policy indirectly contributes to price stability also by ensuring a stable macroeconomic environment which will enable a country to have low inflation. This can be achieved by maintaining sound fiscal discipline, avoiding over- borrowing by government and implement prudent fiscal measures that can prevent fiscal imbalances that can fuel inflationary pressures. Also Fiscal policy helps to promote efficiency of public spending and investment which would minimise the cost push factors of inflation (Batten et al., 2020).

Monetary Policy for Price Stability

Monetary policy is used to target inflation rates by adjusting interest rates and changing the money supply. Central banks can use contractionary monetary policies to slow down the economy when inflation rates are high. This is done by increasing interest rates so that consumers are discouraged to borrow and spend money. This will thus lead to a decrease in demand-pull inflation rates. Expansionary monetary policies are used when inflation rates are low and deflationary effects can happen. These policies are used to stimulate economic opportunities and prevent prolonged stagnated growth (Svensson, 2020).

For example, in times of economic recovery, the government may pursue expansionary fiscal policy through a reduction in taxes or an increase in government spending. The Bank of England would cooperate with these policies by pursuing expansionary monetary policy; likely involving a cut in interest rates.

A fiscal policy which has been used to improve UK growth and stability was when after the global financial crisis of 2008-2009, the UK government initiated expansionary fiscal tactics with the purpose of stimulating the economy. The fiscal measures which were utilised was the governments' tax reductions and an increase in the amount of public sector expenditure, for example, the implementation of welfare programs for the public and the funding of infrastructure projects. These were just some of the instances of expansionary fiscal measures implemented by the government with the main motive to spend more money in order to encourage economic prosperity by rejuvenating the consumer and business sector (Adedoyin & Zakari, 2020).

The Bank of England has used a number of monetary policy measures to try and achieve the objectives of the government. During the period following the global economic crisis the Bank of England has used unconventional monetary policy measures including quantitively easing. This policy is exactly what it says on the tin. It is when the Bank of England wants to take out of the economy then they will buy assets, ultimately increasing liquidity in the market. To do this they buy bonds i.e. gilts or corporate ones to increase liquidity. When they were buying the amounts were usually up to £200bn of assets. These measures were to help stimulate lending and borrowing as well as investing. It helps a lot of stuff. Above all things, it is there to help support asset prices in the hope that it would promote economic recovery (Papadamou et al., 2020).

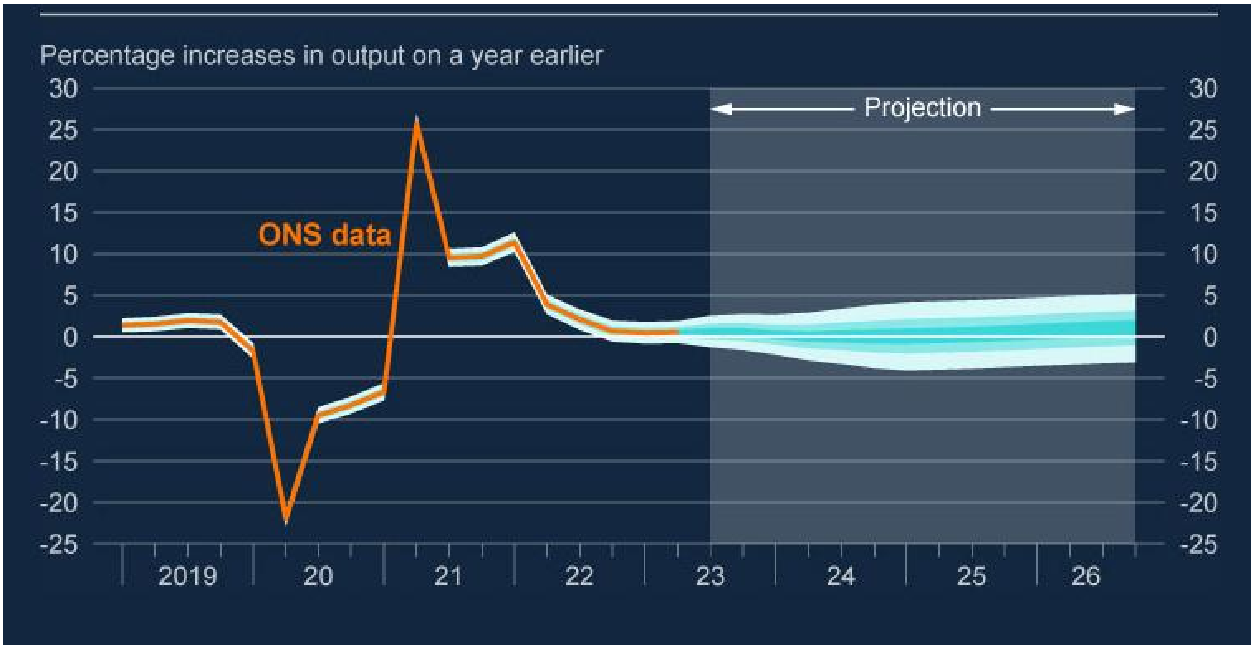

Figure 4 ***GDP growth projection based on market interest rate expectations, ONS Data***

Policies and Theories Can Be Applied and Their Expected Effects

Fiscal and monetary policies are some of the main devices that governments and/ or central bank have to implement policies in their countries for example to speed up the growth of their economy and improve the life of the people. These policies may also target other variables including increased employment, stable prices and decreased inflation. These policies may be effective or not according to some factors will be discussed below.

Global Economic Conditions

Global economic conditions form one of the important considerations that determines the effectiveness of fiscal policy and monetary policy. The world is economically interdependent, therefore, any changes that occur at the global level such as changes in the global economic trends or the way the world trades will ultimately have an effect on individuals that rely on the global economy. For example, if the global economy is in a state of depression and one country hurries to implement an expansionary fiscal policy, chances are, even if the fiscal policy has positive effects on the expenditure patterns of the country, the impact won't be long-lived because some countries may be engaging in very harsh fiscal, or even monetary policies. The goal is therefore to say that if one country suffers from an economic trouble that is not their own doing, they would rather weather it out accept the pain that it comes along with, but if it is as a result of their own makings, then they will sit down and think of policies that are built to save the situation (Römer, 2020).

Policy Coordination

The coordination between fiscal and monetary authorities really matters for the successful implementation of the policies. Conflicting policies or lack of coordination between government's fiscal policy measures and central bank's monetary policies may result into sub optimal situation. For example, if the fiscal policy of the government is to stimulate the economic growth through increased government spending while monetary policy of the central bank is trying to control inflation by raising interest rate then the mix of objectives may result into conflict and the overall effect of the policies may become uncertain. In order to make the macroeconomic management more effective, the policy maker must do coordination among their actions for consistency and coherence in the approach (Son & Enstroem, 2020).

Expectations and Confidence

Confidence and expectations of economic agents when it comes to fiscal and monetary agencies are one of the most important things that should be considered when we talk about how effective fiscal and monetary policy is going to be. The expectations that people have on things like inflation, fiscal policy changes that might occur in the future and the general status of the economy shall influence the behavior and thus, the decisions of the households, corporate bodies as well as the financial markets. If one would expect cuts in tax imposition or increments on government purchases in the future, it could mean that you as a person would shift behavior and the households would end up responding to this thus the changes in the above policy influencing total expenditure coming from the households. The cooperate investment may as well depend on the confidence that the firms have towards the economy as the general future of the country as well. For instances, the financial agencies may think that the government to be has very many distortions to be flexible in its own regulations on the market (Publications et al., 2020).

Structural Factors

The effectiveness of fiscal and monetary policies also depends on the structural characteristics of the economy. For example, labor market flexibility, regulatory environment, productivity levels etc, highly influence how these policies impact the economy. In instances whereby rigid labor markets are in place and regulatory framework is stringent, fiscal stimulus measures aiming to increase employment may be least effective due to regulatory constraints and or labor frictions. Similarly, if even after governmental spending has been increased or monetary stimulus leveled, the productivity levels in the economy are low, the economy could fail to sustainably absorb such stimulus. Therefore, policy makers should also consider the structure their economies before designing and implementing fiscal and monetary policies (Studies, 2021).

Conclusion

In conclusion, there are a number of instruments and policy frameworks which relate to each level of the government (macroeconomic) increasing or reducing the aggregate demand at a time will undoubtedly affect the output levels, economic growth, and the process of economic activity; consequently, expense will be vomit or increase. In this case, there are two strongly effective instruments available to the government fiscal and monetary policy. It is important to underline the fact that the effectiveness of both policies is vastly depending on the domestic or international economic stability. Again, the policy coordination is also important because a gulf between two policies can be share the economy and no intended consequences to get. In addition to that, expectation is important elements interpreted by working people and players in the economy while government exercising the respective policy tools. If the country has high expectation for instance increasing interest rate for further analysis, it may have the positive output on the economic development out unions of the state. Finally, it’s firstly to consider the implication of monetary and fiscal and monetary policy before applying them because if the economy of a country is savers, it will be influenced for the decision you are going to initiate.

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