2.10 Fiscal Policy and the Public Finances: 10-minute Pack

Total Marks

AQA 7136 · Calculators not allowed · about 10 minutes

Name: _____ Date: ____ / ____ / _____

Answer all questions. Full sentences are required for questions worth 4 marks or more. Calculators are not allowed.

1 State the difference between an expansionary fiscal policy and a contractionary fiscal policy, giving one policy instrument for each in a UK context.

(Total for Question 1 is 3 marks)

2 Explain two ways the size of automatic stabilisers determines how much a recession increases a government's budget deficit.

(Total for Question 2 is 5 marks)

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Mark scheme · 2.10 Fiscal Policy and the Public Finances: 10-minute Pack

Question 1

expansionary fiscal policy aims to increase aggregate demand, e.g. higher government spending or tax cuts	**B1**
contractionary fiscal policy aims to reduce aggregate demand, e.g. lower government spending or higher taxes	**B1**
gives one clear instrument for each, e.g. cutting income tax (expansionary) and raising VAT (contractionary)	**B1**

Answer: Expansionary fiscal policy raises AD, for example by cutting income tax or increasing public spending; contractionary fiscal policy reduces AD, for example by raising VAT or cutting public spending.

Question 2

identifies that larger automatic stabilisers (e.g. more progressive tax system or generous welfare) mean tax receipts fall more and benefit payments rise more during a recession	**M1**
developed: thus a larger automatic stabiliser causes a bigger cyclical rise in the deficit because withdrawals and receipts move more strongly with income	**A1**
identifies a second way: larger stabilisers can smooth demand by supporting incomes, reducing the depth of the recession	**M1**
developed: smoothing reduces the fall in tax receipts and limits spending on benefits compared with an economy with weak stabilisers, so the ultimate impact on the deficit may be smaller per unit of GDP shock	**A1**
linking statement: therefore the net effect depends on the size and design of stabilisers and the initial severity of the shock	**B1**

Answer: Bigger automatic stabilisers mean tax receipts fall further and benefit spending rises more in a downturn, increasing the cyclical deficit, but they also cushion demand which can reduce the depth of the recession and so limit the ultimate rise in the deficit.

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