

## "Fiscal Policy: Components & Objectives"

For 6th Semester  
Economics (Major)  
Paper - 6.1

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Fiscal Policy consists of steps and measures which the government takes both on the revenue and expenditure sides of its budget.

Components: — The four main components of fiscal policy are i) Expenditure, budget reform ii) Revenue (particularly tax revenue) mobilization iii) Deficit Containment/financing and iv) Determining fiscal transfers from higher to lower levels of government.

So the key elements of fiscal policy are government spending and taxation. In times of a recession, the government can increase spending/reduce taxes to stimulate consumption and push towards economic growth. Similarly, when the economy is booming, the Govt. can raise taxes to curb spending. Expansionary fiscal policy, designed to stimulate the economy, is most often used during a recession. Contractionary fiscal policy is

used to slow down economic growth, such as when inflation is growing too rapidly.

### Objectives:—

The objective of Fiscal policy is to maintain the condition of full employment, economic stability and to stabilize the rate of growth. For the developing countries the main purpose of the fiscal policy is to quicken the rate of capital formation and investments for the purpose of development and growth. Whereas in developed countries, the main objective of the fiscal policy is to maintain stability. Although the long-run goal of any fiscal policy is to maintain stabilization by moderating short-run fluctuations.

The fiscal policy is designed to achieve certain objective in general.

#### 1) Development by effective Mobilisation of Resources:—

The principal objective of fiscal

Policy is to ensure rapid economic growth and development. This objective can be achieved by mobilisation of financial resources. The financial resources can be mobilised by:—

Taxation:— Through effective fiscal policies, the government aims to mobilise resources by way of direct taxes as well as indirect taxes.

Public Savings:— The resources can be mobilised through Public Savings by reducing Govt. expenditure and increasing surpluses of public sector enterprises.

Private Savings:— Through effective fiscal measures such as tax benefits, the Govt. can raise resources from private sector and households. Resources can be mobilised through Govt. borrowings by ways of treasury bills, issue of Govt. bonds, etc., loans from domestic and foreign parties and by deficit financing.

2) Efficient allocation of Financial Resources:— Financial resources

are allocated for Development activities which includes expenditure on railways, infrastructure, etc. While Non-development Activities includes expenditure on defence, interest payments, subsidies etc. Fiscal Policy should ensure that the resources are allocated for generation of goods and services which are socially desirable.

### 3) Reduction in inequalities of income and wealth:

Fiscal Policy aims at achieving equity or social justice by reducing inequalities of income among different sections of the society. For example, the direct taxes such as income tax are charged more on the rich people as compared to lower income groups. Indirect taxes are also more in the case of semi-luxury and luxury items, which are mostly consumed by the upper middle class and the upper class. The government invests a significant proportion of its tax revenue in the implementation of poverty alleviation programmes to improve the conditions of poor people in society.

#### 4) To stabilize the Price Level:—

One of the main objective of fiscal Policy is to control inflation and stabilize Price. Therefore, the government always aims to control the inflation by reducing fiscal deficits, introducing tax savings schemes, productive use of financial resources, etc.

#### 5) Employment Generation:—

An important objective of fiscal Policy is to create conditions of full employment and provide with rising standards of living. Specific fiscal measures help in increasing the level of employment. Public expenditure on labour-intensive public works like construction of roads, flyovers, bridges, etc, helps in creating employment opportunities. Lower taxes and duties on small-scale industrial (SSI) units encourage more investment and consequently generates more employment.

#### 6) Balanced Regional Development:—

Fiscal policy helps in promoting

development of backward regions. There are various incentives from the government for setting up projects in backward areas such as Cash Subsidy, Concession in taxes and duties in the form of tax holidays, Finance at Concessional interest rates, etc. Government aims to achieve balanced development of the Country by making investment in setting up industries and providing infrastructural facilities in the backward regions.

#### F) To maintain equilibrium in the balance of payments :-

Fiscal policy attempts to encourage more exports by way of fiscal measures like exemption of income tax on export earnings, exemption of central excise duties and Customs, exemption of Sales tax and octroi, etc.

The foreign exchange is also conserved by providing fiscal benefits to import substitute industries, imposing Customs duties on imports etc.

The foreign exchange earned by way of exports and saved by way of

import substitutes helps to solve balance of payments problem. In this way adverse balance of payment can be corrected either by imposing duties on imports or by giving subsidies to export.

### 8) Capital formation :-

In order to increase the rate of capital formation, the fiscal policy must be efficiently designed to encourage savings and discourage or reduce spending. Increase in the rate of capital formation helps to accelerate the rate of economic growth.

### 9) Increasing National Income :-

The fiscal policy aims to increase the national income of a country. This is because fiscal policy facilitates the capital formation. This results in economic growth, which in turn increases the GDP, per capita income and national income of the country.

Fiscal policy of India always has two objectives, namely improving

the growth performance of the economy  
and ensuring social justice to the people.

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