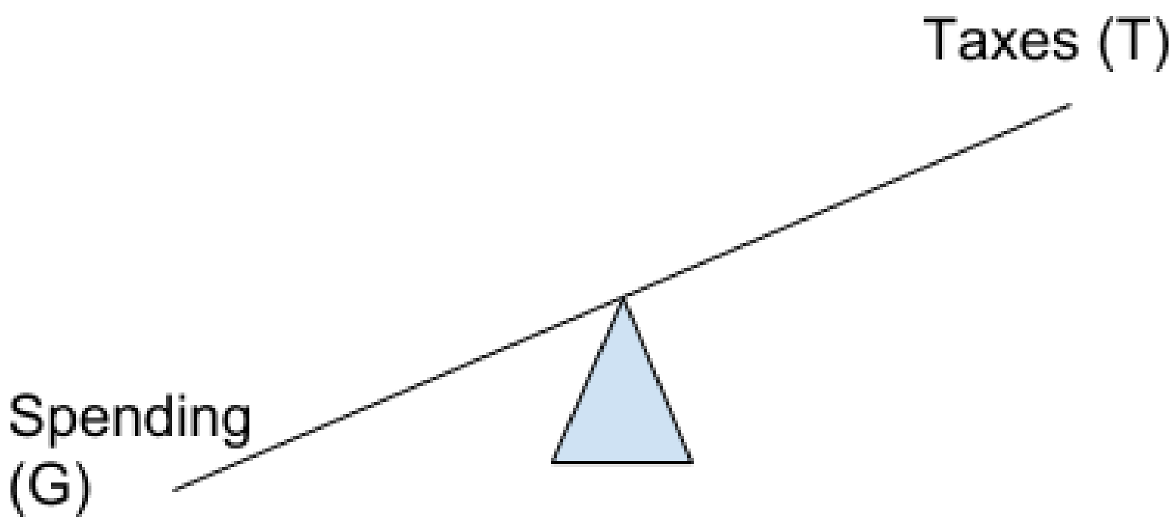
Government Budgets

When governments are preparing their annual budget, they consider revenue (from taxes) and expenditures (government spending). Their budget choices will depend on where the economy is in the business cycle, as well as their political perspective.

Budget (B) = Taxes (T) - Government spending (G)

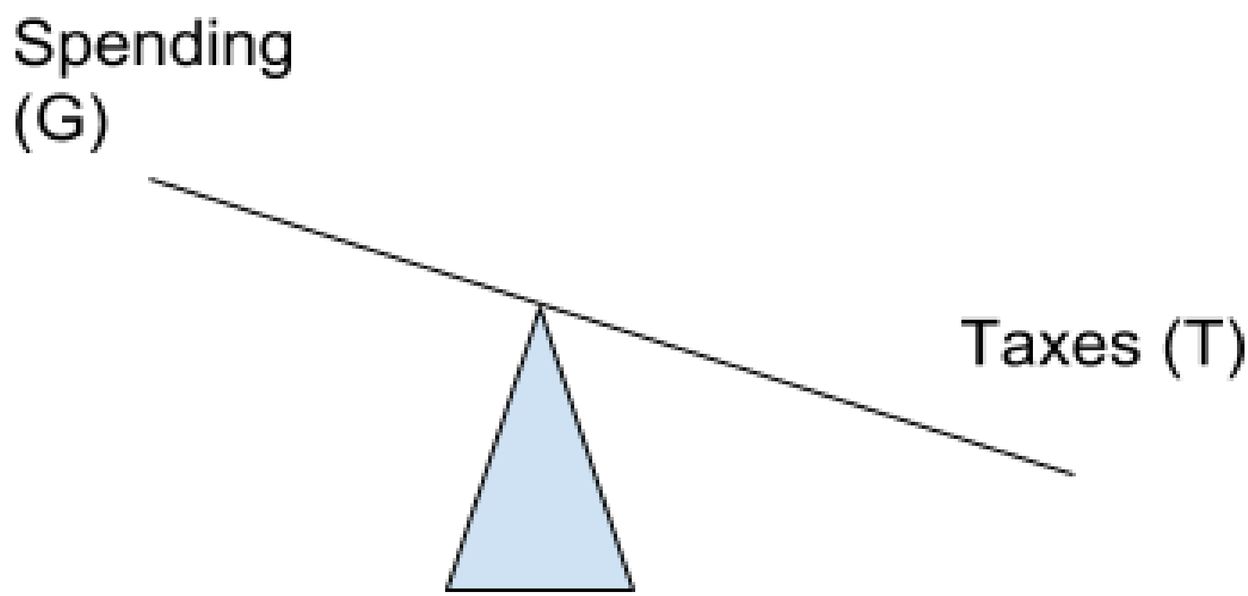
Deficit Budget

When **G >T,** the budget is in deficit. This is referred to as an Expansionary fiscal policy because the government is trying to expand the economy through spending.



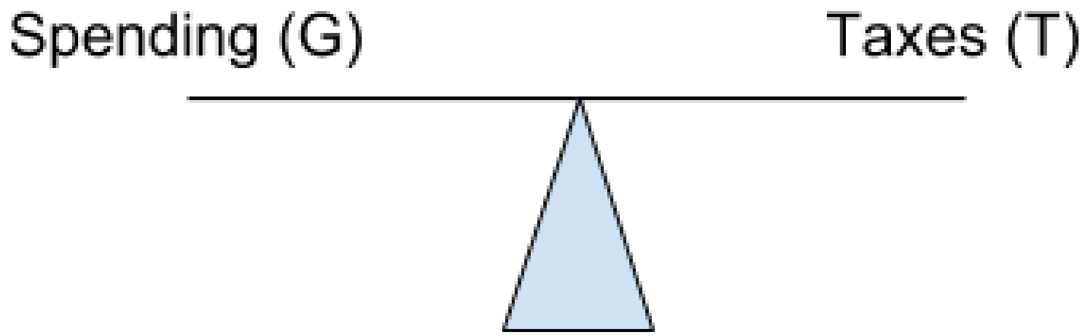
Surplus Budget

When **G < T,** the budget is in surplus. This is referred to as a contractionary fiscal policy because the government is trying to slow down the economy through reduced disposable income leading to less spending.



Balanced Budget

G = T



Keynes said, instead of balancing the budget every year (T=G) that the government should balance the budget over the business cycle.