FISCAL AND MONETARY POLICIES

INTRODUCTION.

According to classical economists there is always full employment in the economy. Neither ever rises unemployment nor there is possibility of inflation. Accordingly, they rule out the justification of government intervention in the economic affairs. In other words, they do not realize the need for economic stabilization or fine tuning of the economy. This is the reason, they believed in the operation of market forces and free enterprize system in every field of life except law and order like sectors of the economy.

But during 1930's Great Depression, classcists 'utopia' of full employment was shattered when millions of people were wandering in search of jobs. Then it was J. M. Keynes who advocated for government intervention. In other words, after *Keynesian Revolution* it was realized that state should interfere in economic life. Because the rising unemployment, rising price level, economic backwardness, deficit in BOP and unequal income distribution, etc., could not be removed without the intervention by the government. Therefore, to remove such economic evils or for economic stabilization, two main policies are adopted .

(1) Fiscal policy, (2) Monetary policy.

Here, we discuss fiscal policy, its objectives and its role. Then monetary policy, its objectives and role will be discussed.

FISCAL POLICY

Concept and Definition of Fiscal Policy

Fiscal policy is a policy concerned with Government Revenues and Government Expenditures. According to Prof. Lindhalm, "Fiscal policy is attached with the determination of time, type and procedure to be followed in making Revenues and Government Expenditures".

According to Samuelson, "Fiscal policy is concerned with all those arrangements which are adopted by government to collect the revenue and make the expenditures so that economic stability could be attained/maintained without inflation and deflation". According to M. W. Lee, fiscal policy considers :

(1) Imposition of taxes, (2) Government expenditures,

(3) Public debt, (4) Management of public debt".

It must be remembered that it is the government which manipulates the fiscal policy.

Instruments of Fiscal Policy

(1) Government expenditures (G),

(2) Taxes (T), both direct and indirect,

(3) Deficit financing, i.e., government borrowing and printing of new notes,

(4) Subsidies,

(5) Transfer payments like unemployment allowances, stipends and scholarships

OBJECTIVES / ROLE OF FISCAL POLICY IN ECONOMIC DEVELOPMENT OF PAKISTAN

The most important determinant of economic development in a country is its fiscal policy and its role cannot be denied.

1. **To Increase the Rate of Investment**
   Fiscal policy should be used to encourage some and discourage other forms of investment. In order to raise the rate of investment, government should undertake a policy of planned investment in the public sector which will have the effects of increasing the volume of investment in the private sector.
2. **To Encourage Socially Optimal Investment**
   This policy should encourage the flow of investment into socially desirable channels, investment in transport, communications, river and power development, education, public health, technical training facilities etc. This type of investment leads to external economies and tends to widen the market, raise productivity and reduce the cost of production.
3. **To Increase Level of Employment**
   The state expenditure should be directed towards providing social and economic overheads. Such expenditures create more employment and increase the productive efficiency of the economy in the long-run.
4. **To Promote Economic Stability**
   Fiscal policy plays a crucial role in maintaining economic stability in the face of external and internal forces. Fiscal policy should aim at the diversification of the economy and balanced growth of the various sectors of the economy.
5. **Price Stability**
   The aim of fiscal policy is not only to arrest the inflationary rise in prices but also to maintain some measures of stability in the general price level. The fiscal measures should be adopted to control prices to get the objectives of economic growth and stability.

6. **Equal Distribution of National Income**

   Fiscal policy should increase national income and redistribute it in such a manner that the extreme inequalities of income and wealth are reduced in the economy. The aim of fiscal policy is to remove the inequalities and direct the resources into productive channels for economic development.

7. **To Correct Imbalance of Payments**

   When the imports of a country exceed its exports; it is an adverse balance of payment position and disequilibrium in the balance of payments arises. The imports of a country are discouraged and exports of the country are encouraged by adopting the different instruments of fiscal policy. Then the disequilibrium is corrected.

8. **To Control Trade Cycles**

   A trade cycle has its different phases but the two extreme phases i.e. boom and depression is harmful for an economy. By adopting the tools of fiscal policy, government controls the business cycles.

9. **Protection Policy**

   The home industries are protected through tax and tariff measures and as the production in the country are stimulated and economic growth is accelerated.

10. **High Growth Rate of GDP**

    Fiscal policy influences the gross domestic product through taxation policy by allocating the resources to various sectors of the economy and reduces the cost by eliminating the wastage.

11. **Self-Reliance**

    Self reliance is also an important objective of the fiscal policy. This objective is an important incentive for economic development. This objective can be achieved by effective fiscal policy of import substitution and export led growth.

12. **Decrease Budget Deficit**

    When budget expenditure exceeds its revenues, the gap is called budget deficit. Bringing down budget deficit is also an important objective of the fiscal policy and this objective has a great importance in economic development of a country.