5 Government macroeconomic policy – Part 2 — Answers

Answers

5.1 The central bank runs monetary policy; its main tool is the interest rate.

5.2 (a) borrowing becomes dearer, so people borrow and spend less; (b) aggregate demand falls.

5.3 To raise the economy's productive capacity (shift long-run aggregate supply to the right), raising growth without inflation.

5.4 Market-based: cut income tax / privatisation / deregulation. Interventionist: spending on training / infrastructure. (One of each.)

5.5 (a) demand-side; (b) supply-side.

5.6 Supply-side policy shifts long-run aggregate supply to the *right*, so the economy can produce *more* output while the price level *falls* — raising growth and easing inflation together. The drawback is that it is *slow*: measures like training, education and infrastructure take years to pay off.