

CHAPTER 2
UNIT-I FISCAL FUNCTIONS: AN OVERVIEW

Questions to be answered bringing in appropriate theoretical rigour.

Application Oriented Questions

Question 1

Elucidate the nature of economic functions performed by the government in the following cases:

- (a) The government initiates a massive programme for eradication of mosquito-borne diseases in coastal areas
- (b) The government of India fixes the prices of 377 essential medicines listed in the National List of Essential Medicine, 2015

Question II

The government decides to levy up to Rs. 20,500 per flight from private airlines on major routes in order to fund an ambitious regional connectivity scheme which seeks to connect small cities by air and to make flying more affordable for the masses. Critically examine the implications of this policy on the airlines market.

Fiscal Policy

Application Oriented Questions

Question I

The government of Country X, an underdeveloped country, having a severe problem of unemployment of labour embarks on a massive development programme. It has recognized the imminent need for boosting up investments to take the country to a higher than average growth trajectory. The following steps were taken by the government:

- i) Invited tenders for a huge net work of highways, solar energy generation, communication systems and computerized systems
- ii) Large number of schools throughout the country
- iii) Research grants for universities and private research institutes
- iv) Announced a number of free health care programmes for all
- v) All citizens assured of social security
- vi) Increase in payments under existing social security schemes

vii) Tax exemption limit raised for individuals, instituted progressive taxes with high marginal rates

Very soon prices started spiraling and there was general unrest among people, especially the poor.

- i) Analyze each of the above measures from a fiscal policy perspective.
- ii) Why did overall prices increase?
- iii) What policies do you suggest to solve the problem of price rise?
- iv) What are the limitations?

Question II

In the above example, suppose that the increase in government spending has been Rs. 5 billion. Assume that the marginal propensity to consume of people is equal to 0.6.

- i) What will be the government spending multiplier?
- ii) What impact would a Rs. 5 billion increase in government expenditure have on equilibrium GDP?