

**CLASS 1**

TOPIC	<i>Economic Policy Concepts</i>
<p><b>LEARNING CONTENT - DETAILED CHARACTERISTICS</b></p>	<p>This topic introduces the concept and the methodology of economic policy. We focus on the objectives of economic policy (such as improving the population’s standard of living, promoting sustainable growth, achieving full employment, maintaining price stability, reaching a fair distribution of income and alleviating poverty) considering that some of them are contradictory. We also discuss the instruments of the economic policy which is a combination of the instruments of fiscal policy (such as the levels of public expenditure and taxes) and monetary policy – the setting of official interest rates, quantitative easing and forward guidance that consists in communicating about future monetary policy to guide market expectations. We consider that institutions directly affect the effectiveness of policy instruments – they are made up of formal constraints (rules, laws, and constitutions), informal constraints (norms of behaviour, conventions, and self-imposed code of conduct) and their enforcement characteristics. We make students aware of the two study approaches in the field of economic policy: positive approach – one takes the point of view of an outside observer and aims to determine the channels through which public decisions affect private behaviour and outcomes – and the normative approach when one examines which set of decisions can best serve explicit public policy purposes, such as reducing employment, improving the standard of living, or safeguarding the environment. We discuss the three functions of economic policy: allocation policies (that cover public interventions aiming to affect the quantity or the quality of the factors available for production (capital, unskilled and skilled labour, technology, land) and their sectoral or regional distribution); stabilization policies consider that management of the government budget can stabilize the economy and monetary policy by affecting interest rates also alters households’ and firms’ intertemporal decisions; redistribution policies that are designed to correct the primary distribution of income. Key issues are what policymakers do, why politicians may depart from the general interest, and who should decide – politicians or technocrats. We present the criteria to guide decisions to assign specific responsibilities to technocratic bodies. The main dimensions of the economic policy are discussed.</p>

<b>KEY WORDS</b>	Public intervention, economic policy, fiscal policy, monetary policy, positive approach, normative approach, allocation policies, stabilization policies, redistribution policies, general interest, politicians, policymakers, technocrats.	
<b>SUGGESTED TOOLS</b>	Power-point presentation Reading and interpreting tables Real-world personal observation Interactive and group discussions A personal study plan	
<b>TIPS / METHODOLOGICAL REMARKS</b>  (if applicable)	Learning-by-doing and case studies activities. The focus is on the interpreting of economic policy facts and real-world problems.	
<b>IMPLEMENTATION OF THE CLASSES</b>	<b>STEP 1</b>	The lecturer discusses that economic policy examines the role of government in the economy and important issues such as: What are the economic functions of government, and what should they be? How should the government finance the services it provides? What kinds of government programs should confront the problems of poverty, unemployment, and pollution? What problems does government involvement create?
	<b>STEP 2</b>	The relationship between the objectives and instruments of the economic policy is presented. The lecturer focuses on differences between fiscal and monetary policy as regards their goals and instruments. Real-world examples are given. The positive and normative approaches of analyzing economic policy are discussed.
	<b>STEP 3</b>	The three functions of economic policy (allocation, stabilization, and redistribution policies) are presented considering direct and indirect effects of three public policies: reduction in income tax; increase in government expenditures and increase in social transfers. Specific terms (such as crowding out effect, inactivity trap, and income inequality) are stressed. See work card 1.
	<b>STEP 4</b>	A discussion on the key aspects and main dimensions of economic policy is provided. The focus is what policymakers do and why politicians may depart from the general interest.

	<b>STEP 5</b>	The role of institutions in the economic policy framework is discussed. The criteria to guide economic policy decisions and indicators for effective economic policy implementation are presented. A case study is considered. See work card 2.
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### ADDITIONAL MATERIAL 1 (WORK CARD, PICTURE, RECORDING, QUIZZ, PRESENTATION, ASSIGNMENTS)

#### WORK CARD 1 – ECONOMIC POLICY CONCEPTS

Consider the direct and indirect effects of three public policies in the table below and answer the following questions:

	<i>Allocation</i>	<i>Stabilization</i>	<i>Redistribution</i>
<b>Reduction in income tax</b>	+ Increase in labour supply	+ Increase in demand for goods	+ Increase in inequalities
<b>Increase in government expenditures</b>	+/- Depends on the content of expenditure and on the possibility of crowding out private expenditure	+ By hypotheses	+/- Depends on the content of expenditure
<b>Increase in social transfers</b>	- Risk of inactivity trap	+ Increase in the demand for goods	+ Reduction in inequalities

1. How the three public policies – allocation, stabilization, and redistribution policies – may be distinguished? What do you think about the time perspective as regards their formulation and implementation?
2. What are the instruments of fiscal policy? Which of them is most powerful following the effects considered in the table?
3. What is the crowding out effect? Why is this effect associated with the fiscal policy? Why allocation and redistribution effect of the increase in government expenditures may be positive and negative?
4. What is the inactivity trap? Is this situation valid for your country? Give some examples.

- How can the government support the reduction in inequalities? What is your opinion – is public intervention in the economy desired or not? What are the economic consequences of active and passive economic policies?

## ADDITIONAL MATERIAL 2 (WORK CARD, PICTURE, RECORDING, QUIZZ, PRESENTATION, ASSIGNMENTS)

### WORK CARD 2 – ECONOMIC POLICY CONCEPTS

Watch the video *The importance of institutions* and take part in the discussion:

<https://www.youtube.com/watch?v=wdKBfXRpNsk>



Share your thoughts as regards:

- Situations that policymakers engage in policies that are not optimal from an intertemporal point of view;
- A political business cycle behaviour of the policymakers;
- Divisions between regions or between ethnic or social groups when economic policy making is considered;
- Technocratic and political decisions that impact economic and social processes;
- Climate change and long-run effects of economic policy.