ECO 202 Project Template
Economic Summary Report

Table of Contents

Introduction

For the benefit of the incoming administration, I submit this report to document, analyze, and interpret the macroeconomic policy decisions I made as the chief economic policy advisor of Econland. The purpose of this document is to further our national prosperity by deepening our understanding of the relationship between macroeconomic policies and their consequences for our citizens. The report includes a thorough accounting of the major fiscal and monetary policy decisions made over each of the seven years of my term, as well as an explanation of the underlying rationales for those decisions and the resulting impacts of those policies.

Table 3: Economic Environment, Decisions, and Results

	Year 0	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7
Global Economic Growth Forecast	2.4	2.4	2.6	2.2	2.0	1.7	1.9	2.2
Consumer Confidence Index	100.0	100.0	101.8	101.8	100.3	100.3	100.2	99.6
Interest Rate %	3.0	3.5	4.0	4.5	5.0	5.0	5.0	5.0
Income Tax Rate %	24.0	24.0	24.0	24.0	24.0	26.0	26.0	26.0
Corporate Tax Rate %	30.0	30.0	30.0	30.0	30.0	32.0	32.0	32.0
Government Expenditure US$ (in billions)	30.0	32.0	34.0	36.0	38.0	38.0	36.0	34.0
Real GDP Growth %	2.5	3.7	2.7	2.6	2.5	-0.8	-0.9	-0.4
Unemployment Rate %	5.0	4.5	4.5	4.9	5.0	6.3	7.7	7.6
Inflation Rate %	2.0	1.5	1.8	1.4	0.3	0.2	-1.9	-4.0
Budget Surplus (Deficit) as % of GDP	-3.0	-3.4	-3.9	-4.5	-5.4	-3.4	-2.5	-2.1

Table 1.1

The table above summarizes the macroeconomic climate of Econland over my term. I chose the stagnation scenario. As chief economic policy advisor of Econland I did my best to not to make drastic changes as the economy was doing generally well. I paid close attention to interest rates and government expenditures and tried to keep the economy growing steadily. My overall approval rating was 63, yet the consumer confidence index averaged 100.5.

Fiscal Policy: Taxation

Table 1: Real GDP and Its Components

	Year 0	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7
Consumption	55.0	60.2	62.9	65.3	66.4	64.3	62.0	57.2
Government Expenditure	30.0	32.0	34.0	36.0	38.0	38.0	36.0	34.0
Investment	15.0	15.1	15.5	15.8	15.5	15.0	14.4	13.7
Exports	25.0	25.5	26.2	26.9	27.5	28.2	28.8	29.3
Imports	25.0	27.5	28.6	29.6	30.0	28.8	27.7	25.7
Nominal GDP	100.0	105.2	109.9	114.3	117.4	116.7	113.5	108.6
Real GDP	100.0	103.7	106.4	109.2	111.9	111.0	110.0	109.5

Table 2.1

Government policies have a large impact on overall consumption and investments, as well as government purchases and net exports; all of which reflect Gross Domestic Product (GDP). The intent of my taxation policies was to support growth through consumer spending, keeping in mind government expenditure and its effect on inflation and consumption.

I opted not to change income or corporate tax much. Income tax stayed at 24% until year five when I increased it to 26%, while corporate tax stayed at 30% until year five when I increased it to 32%. With reasonable income and corporate tax rates, higher production would ensue. Keeping it at a

consistent rate allowed for safe steady growth, whereas lowering these rates could have a negative impact on job creation and income since it raises the deficit. To this point as well, when income and corporate taxes were raised in year five, there was a subsequent fall in GDP.

Between 2020 and 2021, President Joe Biden proposed the Build Back Better Plan. “CBO estimated that the cost of Build Back Better would increase federal deficits by $3 trillion over the next 10 years if certain provisions were to be made permanent,” (“2022 Tax Policy Outlook: Managing Constant Change,” 2022). Deficit spending, whether through tax cuts or government expenditure increases, can sometimes have a positive impact on the economy, (Mankiw, 2021). One of the main controversies with this plan though is the crowding out effect. Crowding out occurs when “government spending fails to increase overall aggregate demand because higher government spending causes an equivalent fall in private sector spending and investment,” (“Crowding Out,” 2019). Increases in interest rates causes investments to fall, which leads to lower production rates and thus, lower economic growth. During my seven-year term as chief economic policy advisor, my tax policy decisions aimed at steadily increasing government expenditures to not cause any major economic fluctuations. The Tax effect on the GDP for Econland is shown in the table above. Less taxation allowed for more economic growth since tax policies effect investment and savings, as well as the overall money supply, (Mankiw, 2021).

Fiscal Policy: Government Expenditure

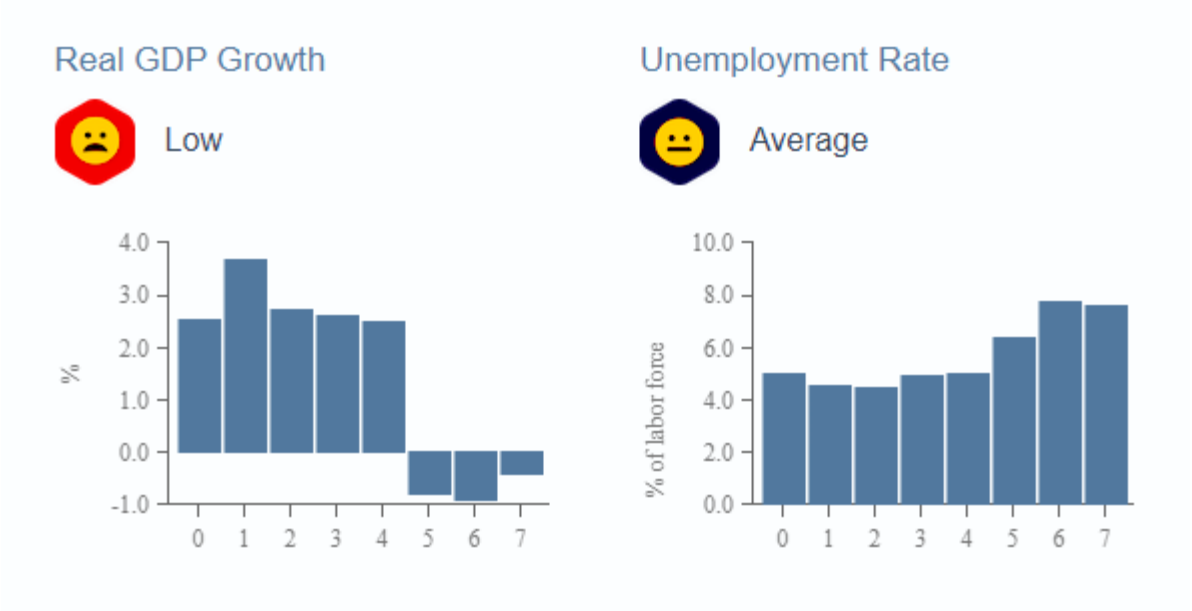

Figure 3.1

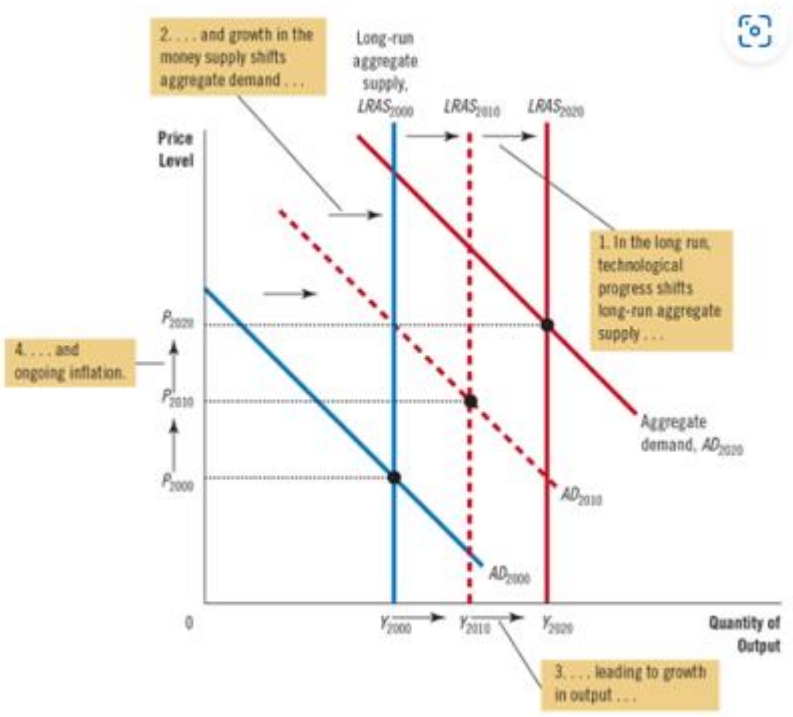

Figure 3.2

The intent of my fiscal policy decisions in response to the given economic climate were based around government spending and interest rates. During the fifth year, investments began to fall along with the global economic growth forecast. In response to this, I lowered government spending in year six and seven in attempt to promote productivity.

My fiscal policy decisions that were most successful when government spending and interest rates were kept at a steady increase. However, as I mentioned previously, investments began to fall in the fifth year. I attempted to combat this by lowering government spending and increasing income and corporate taxes minorly. By doing so, consumption, the largest component of GDP, fell. (Mankiw, 2021). The falling investments contributed to a lower level of productivity and higher level of unemployment. Overall economic growth took a hit, otherwise heeding a negative outcome – at least in the short-term. Fiscal policy decisions reflect GDP and unemployment specifically in long run, (Mankiw, 2021).

In the long run, with prices low and unemployment high, the costs of production decreases overtime and workers become obliged to accept lower wages. This causes the aggregate supply curve to shift to the right as the unemployment rate decreases. As employees return to work, the level of production increases, which causes price levels to increase as well, as seen above in Figure 3.2.

Monetary Policies

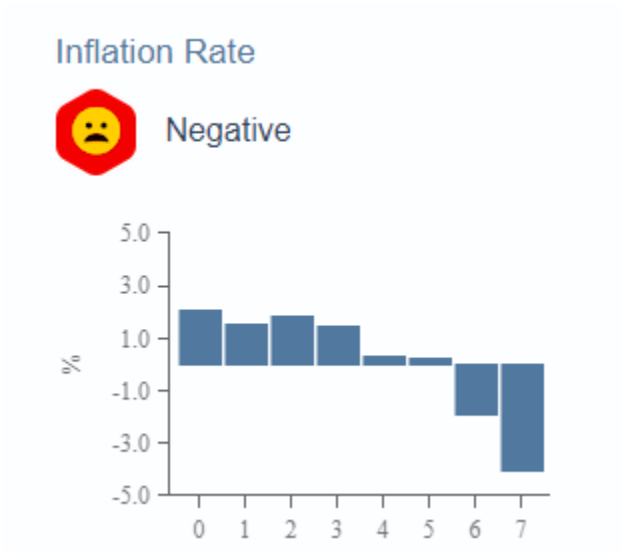

Figure 4.1

Changes in interest rates can have either positive or negative macroeconomic effects. Throughout my seven-year term, interest rates increased steadily from 3.0% to 5.0%, where they remained from years four through seven. By not changing the interest rates for the last three years of my term, inflation went from low to negative – meaning deflation occurred, as shown in Figure 4.1. Deflation caused consumption to fall quite rapidly, until it reached the all-time low of 57.2. With lower consumption came lower demand, which simultaneously caused a decrease in investments. This demonstrates the validity of macroeconomic models, in part because it shows that steadily increasing interest rates overtime can yield a positive economic outlook. When I stalled investment rate increases, my economy stalled as well.

President Joe Biden's Build Back Better Plan enacts significant corporate, international, and individual tax changes through additional federal funding during a time in which inflation is already at a 40-year high, ("2022 Tax Policy Outlook: Managing Constant Change," 2022). The difference in the impact of the monetary policies that I put in place, and the ones President Joe Biden put in place, are that I decided to keep government spending controlled to some level. Where my monetary policies led to deflation, President Joe Biden's monetary policies have led to significant inflation. These are both great examples that demonstrate the validity of macroeconomic models in that higher government spending leads to inflation, whereas lower government spending can lead to less production, higher unemployment, and overall, less spending – creating deflation.

Global Context

Openness to trade leads to higher consumer variety, lower product prices, and an increase in consumer surplus. A closed economy is self-sufficient and there is no international trade. In an open economy, there are numerous interactions with other countries to buy and sell goods. Because of this, an open economy's expenditure will not always equal its output, (Mankiw, 2021). In an open economy, fiscal policy is effective in its ability to alter the level of output. Along with net exports and controlled exchange rates, the overall economy is influenced through fiscal policies. On the other hand, expansionary fiscal policies in a closed economy leads to increased government expenditures, reduced taxes, and reduced interest rates. With no net exports, one factor of GDP is omitted, which can

negatively impact the overall GDP, (Mankiw, 2021). Fixed exchange rates increase government expenditure and output levels, causing a downward pressure on domestic currency, (Mankiw, 2021). Flexible exchange rates, however, increase the money supply which reduces interest rates and increases investment and consumption throughout the economy.

Conclusions

Macroeconomics provides an understanding of the economy as a whole. It allows individuals from various backgrounds important insight into the factors that directly impact the economy, including unemployment, income, and inflation. The macroeconomic models also served as clear interpretations of how various economic policies can affect an economy. The simulations also provided a global economic outlook for each year by summarizing the results of each year's decisions. My economic policy decisions throughout the course of the simulations mostly produced the anticipated results. However, I struggled with making policy decisions based on a stagnant economy. I had initially expected lower government spending to keep inflation at bay without compromising production. After the fact, I realized I should have kept government spending at a steady increase to keep production levels increasing.

Consumer confidence reflects the overall health of an economy. While my overall approval rating was 63, the consumer confidence index stayed consistent (around 100) until year seven, when it dropped to 99.6. Consumption is a factor of GDP because when consumers are confident about government policy decisions, they will continue to spend money which increases GDP and leads to an overall healthier and more productive economy. This is very relevant to making successful policy decisions because it provides the level of consumers' confidence in regard to the health of the economy, (Mankiw, 2021).

References

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