Difference between Fiscal policy and Monetary policy

Fiscal policy

- Sets taxes
    - Raising taxes reduces spending in the economy and reducing taxes increases it.
    - Low rates of tax gives businesses more profit
    - Direct taxation
        - Raising income tax reduces consumer spending and raising business taxes reduces economic output
    - Indirect taxation
        - Short term increase in VAT causes inflation because prices increases, whereas in longer term causes deflation because of decrease in customer spending and prices have to fall to meet drop in demand
- Sets Government spending
    - On social services, health, education
    - Changing government spending on welfare benefits has a quick impact on economy cos people who receive benefits will instantly has more or less money available
    - Govt spending on infrastructure has slower effect on economy
- Its abt balance between tax and spending

Fiscal policy	When it's done	How it's done	Change in government borrowing	The effect it has
Expansionary fiscal policy	Economic slowdown/ high unemployment	Cutting taxes and/or raising spending	Govt borrowing increases	Demand for goods and services increases
Contractionary fiscal policy	Production at 100% capacity/ risk of high inflation	Raising taxes and/or cutting spending	Govt borrowing decreases	Demand for goods and services decreases

Monetary policy

- Controls interest rate by tweaking the interest rate to control inflation and exchange rates
- When interest rates are high, foreign investors want to save money in UK banks. They buy British pounds which boosts demand for currency and makes exchange rate go up affecting imports/exports.
- When interest rates low, investors prefer to invest abroad so they sell pounds and exchange rate falls
- Interest rates are set by bank of England, not by the government
- Monetary policy aims to:
    - Control inflation
    - Control overall rate of economic growth
    - Manage unemployment levels
    - Influence foreign exchange rates