2.6.3 Supply-side policies

a) *Distinction between market-based and interventionist methods*
b) *Market-based and interventionist policies: o to increase incentives*
  - *to promote competition*
  - *to reform the labour market*
  - *to improve skills and quality of the labour force*
  - *to improve infrastructure*

c) *Use of AD/AS diagrams to illustrate supply-side policies*
d) *Strengths and weaknesses of supply-side policies*

- Supply-side policies: Supply Side Policies are policies aimed at increasing Aggregate Supply (AS) or expand the productive potential, a shift from left to right. Successful policies lower the natural rate of unemployment.
- Supply-side policies concern the government creating the right conditions to allow market forces to create growth instead of the government creating growth directly. They aim to make an economy more robust and flexible
- Aims of supply-side policies:
  - Improving incentives for work and investment
  - Improve productivity
  - Improve occupational and geographical mobility of labour to reduce unemployment
  - Increase R&D spending
  - Promote more competition
  - Encourage the start-up of new businesses
- Causes of low productivity in the UK:
  - Low rate of capital investment
  - Banking crisis affected lending and borrowing is slowing
  - Slowing rates of innovation
  - Persistent skills shortages
  - Relatively low level of competition
  - Low AD and high spare capacity
- Advantages of higher productivity:
  - Lower unit costs leading to lower prices or higher profits
  - Improved competitiveness and trade performance
  - Higher wages can be afforded by firms
  - Economic growth
- Market-based methods: aim to increase efficiency by removing things which interfere with the free market. They include tax cuts, privatization, deregulation, and policies to increase labour market flexibility
- Interventionist supply-side policies: they are usually aimed at correcting market failure. They include government spending on education, subsidies for research and development, funding for improvements to infrastructure and international policy
- Types of supply side policies:
  - Cutting corporation tax so firms have a strong incentive to produce more
  - Removing regulations and other restrictions that are preventing firms from growing e.g. removing restrictions on mergers

    - Encouraging investment by forcing banks to lend money, or by easing the credit situation (QE), or even cutting the interest rate
    - Increasing competition in markets. By deregulation, privatisation and contracting services out. Note that this might conflict with deregulation and allowing more monopolies.
    - Privatising or subsidising industries e.g. Royal mail
    - Improving the labour market by increasing educational standards
    - Productivity might increase by spending on the NHS. For example, waiting lists are shorter, and people can get back to work more promptly
    - Improved incentives for workers by cutting income tax rates and cutting benefits for out-of-work members of the labour force
    - Improving infrastructure, e.g. the transport system and internet coverage
    - Introducing measures to make exports cheaper, such as cutting income tax rates and cutting benefits for out-of-work members of the labour force
    - Trade liberalisation: removing barriers and allowing goods and capital to flow more freely between countries
- An incentive is a factor that makes the labour resource more effective. It might be harder, or more profits if businesses are run successfully
- Infrastructure is the capital assets that enable resource to move and be moved forward
- Supply-side policies shift the LRAS curve to the right
- Strengths of supply-side policies:
    - Increasing the trend growth rate makes it easier for government to achieve its macroeconomic objectives, with fewer conflicts between objectives
    - More flexible to demand and supply shocks
    - Improvement in competitiveness
- Weaknesses of supply-side policies:
    - The effects are generally microeconomic i.e. on individual workers, firms or markets
    - It can take a long time to see results, so they don't provide immediate effects
    - There can be unintended consequences e.g. deregulation can lead to excessive risk-taking
    - Supply-side policies can be unpopular, and there are also concerns about whether they are equitable