Automatic Stabilizers

Building Fiscal Policies Into Institutions

- Economists have attempted to create built-in fiscal policies.
- *Automatic stabilizers* – any government program or policy that counteracts the business cycle without any new government action.

Building Fiscal Policies Into Institutions

- Automatic stabilizers include welfare payments, unemployment insurance, and the income tax system.

How Automatic Stabilizers Work

- When the economy is in a recession, the unemployment rate rises.
- Unemployment insurance automatically is paid out to the unemployed, offsetting some of the fall in income.

How Automatic Stabilizers Work

- Government spending increase without an explicit act by the government.
- When incomes increase, government spending declines automatically.

How Automatic Stabilizers Work

- When the economy expands, tax revenues rise, slowing the economy.
- When the economy contracts, tax revenues decline, providing stimulus to the economy.

The Automatic Stabilizers

- The automatic stabilizers protect us from the extremes of the business cycle
  - Personal Income and Payroll Taxes
    - During recessions, tax receipts decline
    - During inflations, tax receipts rise
  - Personal Savings
    - During recessions, saving declines
    - During prosperity, saving rises

12-27

The Automatic Stabilizers

- The automatic stabilizers protect us from the extremes of the business cycle
  - Credit Availability
    - Credit availability helps get us through recessions
  - Unemployment Compensation
    - During recessions more people collect unemployment benefits

12-28

The Automatic Stabilizers

- The automatic stabilizers protect us from the extremes of the business cycle
  - The Corporate Profits Tax
    - During recessions, corporations pay much less corporate income taxes
  - Other Transfer Payments
    - Welfare (or public assistance) payments, Medicaid payments, and food stamps rise during recessions

12-29