Deficits

How we finance a deficit

A budget deficit can occur when federal expenditures which include the spending of final goods and transfer payments, or the limit placed for tax revenues has been surpassed.

1. Borrowing (Issuing bonds)
2. Taxes
3. Printing Currency

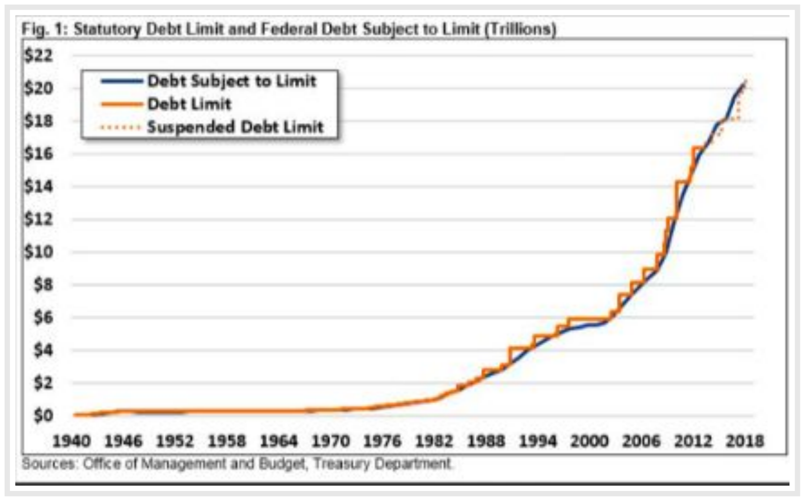
The items listed above our all ways that we contribute to the budget deficit and finance the government to pay off the deficit.

Dangers in financing a deficit

- “Deficit financing is inherently inflationary. Since deficit financing raises aggregate expenditure and, hence, increases aggregate demand, the danger of inflation looms large” (Muley, 2016).
- Ex. The government is trying to pay off a $2.1 million Clean Water Act for restoring habitats back to their natural state, getting rid of pollutants. If they are loaned the money from the federal reserve or a foreign country. An issue might be that the creditor notices it is taking the US abnormally long to pay off that amount and decide to raise the interest rate. This would not help the deficit because inflation would come into play.

Are there federal limits on deficits?

• The deficit is in fact limited by the debt ceiling. When the deficit reaches the debt ceiling, the government must raise the ceiling or cut spending somewhere. According to Economics for Today (Tucker, 2019), the government raises the ceiling, and it causes a very heated debate over the issue.



Are deficits the effect of Keynesian Economics? Why or why not?

- Deficits are in fact the effect of Keynesian Economics because the government intervenes and spends tax dollars that it does not have in times of downturns in the economy. This is in effort to stimulate the economy.

Upsides and downsides of deficits

Upsides- If there is high employment levels or a tax increase, it could transform the budget deficit into a surplus such as in the 1990’s.

- Allows the government to organize what generations will pay taxes over time
- In Keynesian Theory, a budget deficit will cause automatic stabilizers to fall into place

Downsides- Crowds out the private sector, in turn causing that sector to have substantially lower funds and lack the ability to invest.

-High interest rates

-Inflation

References

- Muley, R. (2016, January 29). Deficit financing: Meaning, effects and advantages. Retrieved April 11, 2021, from https://www.economicsdiscussion.net/public-finance/deficit-financing/deficit-financing-meaning-effects-and-advantages/17460
- Tucker, I. B. (2019). *Economics for today*. Boston, MA: Cengage Learning.