

Supply-Side Policy

GCE A-LEVEL & IB ECONOMICS

Supply-side Policies

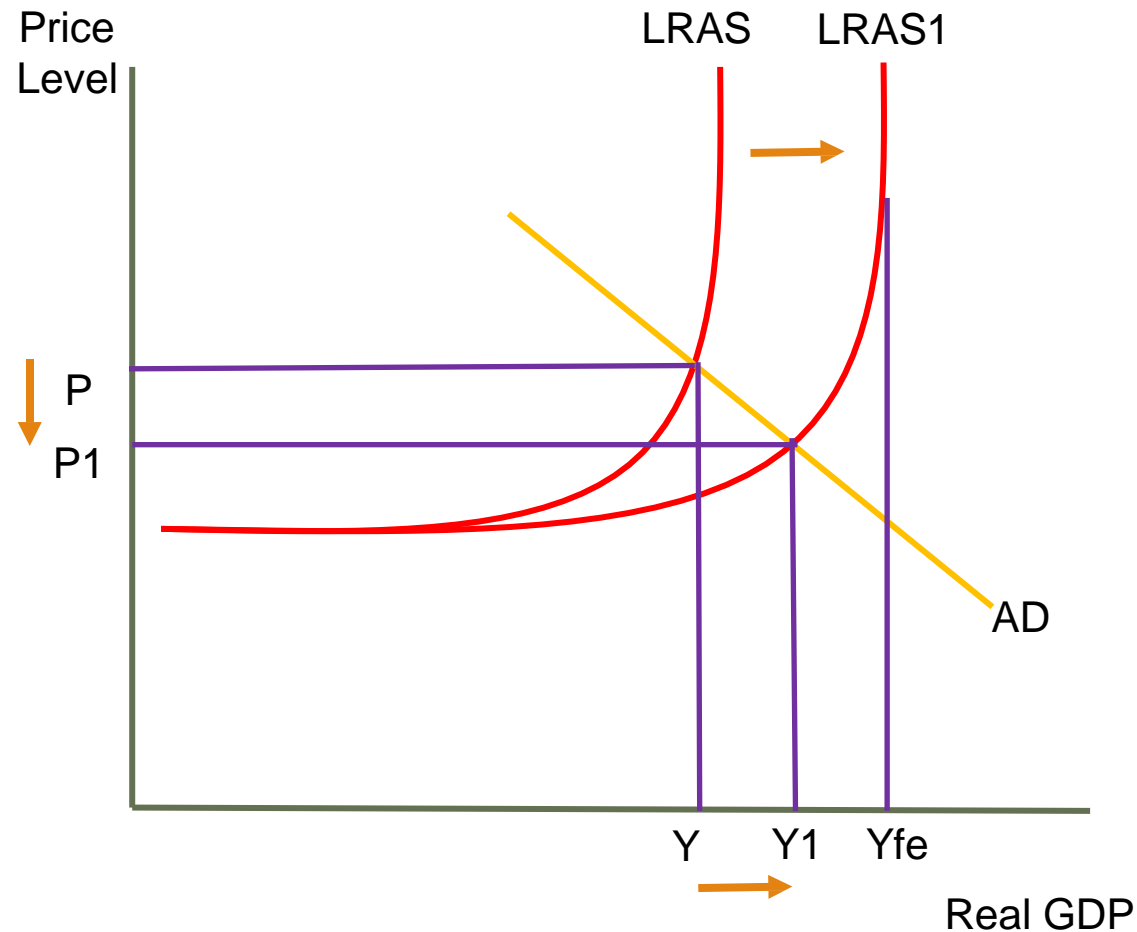
- Market-Based Supply-Side Policy
- Interventionist Supply-Side Policy
- AD/AS Diagrams to illustrate Supply-Side Policies
- Evaluating Supply-Side Policies

Supply-Side Policies

Supply-side policies aim to increase the **aggregate supply** of the economy by increasing economic **productivity** or improving **market efficiency**.

An increase in the productive capacity of the economy (LRAS) will **decrease price level** (inflationary pressures) in the economy and cause **economic growth**.

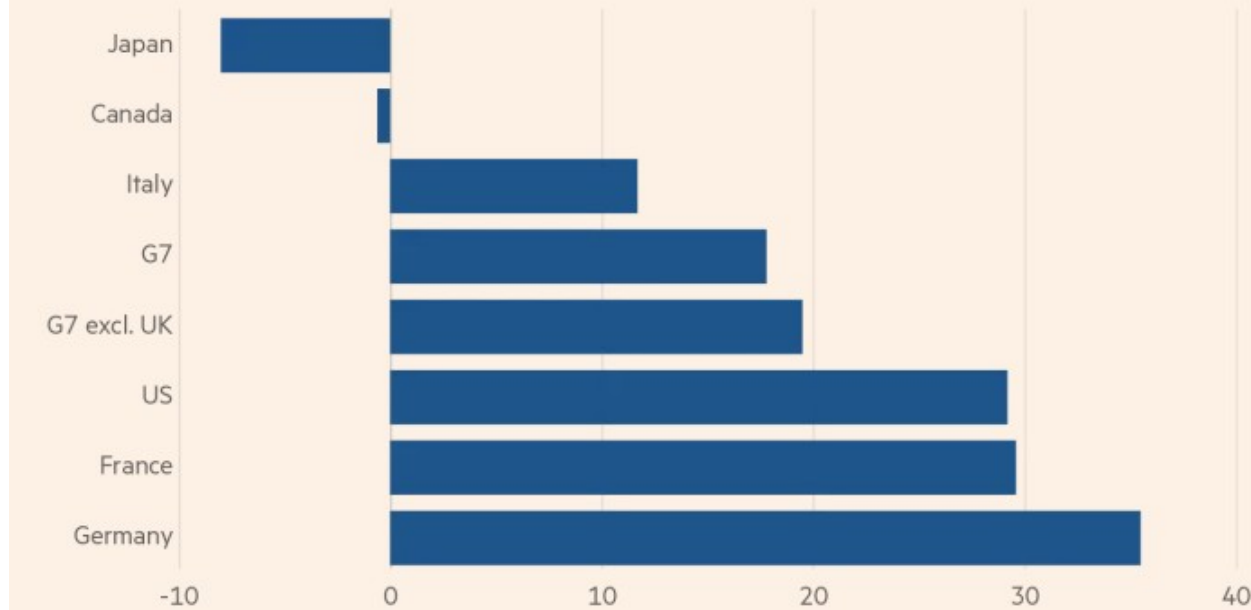
This also corresponds to an increase in real GDP and a shift outward of the PPF.



UK's Productivity Crisis

UK productivity levels are weaker than several other large economies

GDP per hour worked, 2016 (% above/below UK level)*



*GDP is in current prices, at purchasing power parity

Source: ONS

© FT

***“The average German worker produces more in four days than a British equivalent does in five”
Telegraph, 2018***

UK's Productivity Crisis



If the UK is high tech, why is productivity growth slow? Economists weigh in

A new survey of leading economists explores causes and policy options to improve business productivity, writes Ethan Ilzetzki



“There have been two broad categories of explanations for the productivity slowdown. The first focuses on supply-side factors. This category includes employee skills, with the UK among the worst in Europe in terms of mismatch between skills and field of employment, sluggish investment in research and development (R&D), and global factors, including increases in market power. One study suggests greater labour market flexibility in the UK than in other major economies as an explanation.”

“More than half of respondents (63%) propose investments in human capital, such as education and job retraining, as a policy solution.” (ie. **Supply side policy**)

Improving Factors of Production



Land



Labour



Capital



Enterprise

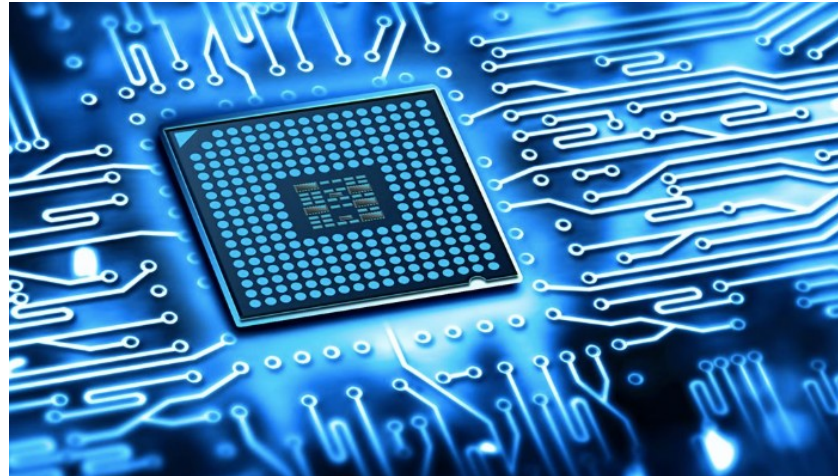
Image source: Tutor2u

A big focus of supply-side policies is to improve **factors of production** to increase productive capacity.

Interventionist Supply-side Policy

Supply-side policies aiming to improve **infrastructure**, **labour** and **technology** through government investment to boost economic productivity.

Fundamentally, these policies involve government **investment** to improve our factors of production.



Types of Infrastructure

Infrastructure are fundamental facilities and systems that help provide basic needs for an **economy** to function.

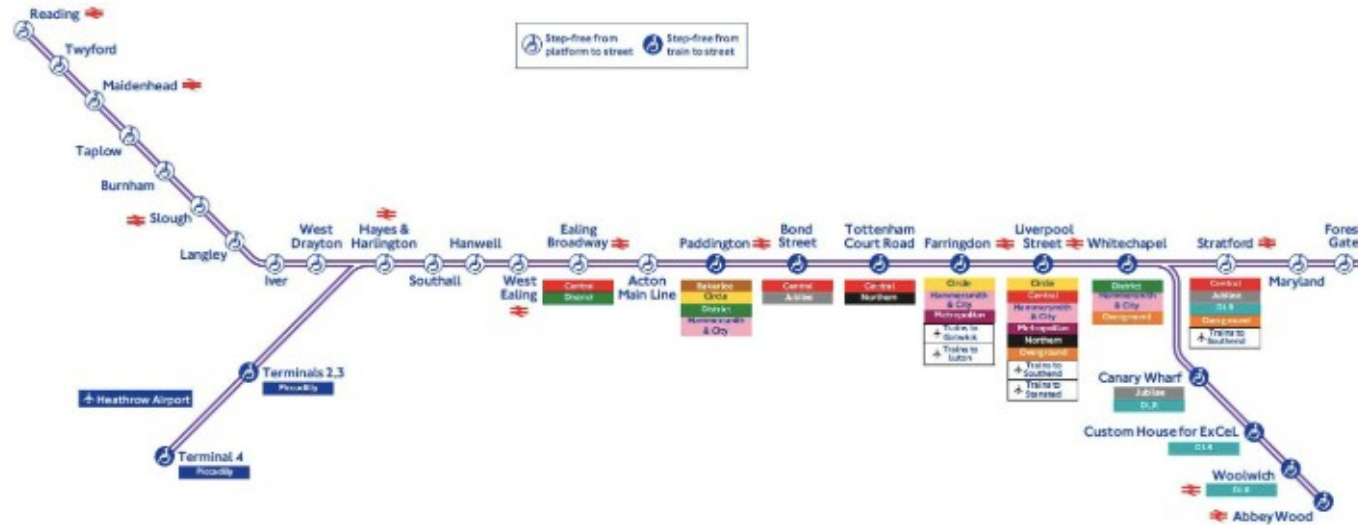
They tend to be publicly owned, provided or subsidized, and is a type of **capital** that helps us produce goods and services.



Utilities, Transportation, Telecommunications

Interventionist Supply-side Policy

Elizabeth line map



“The new railway will bring an extra 1.5 million people to within 45 minutes of Central London”

MAYOR OF LONDON

Investment in Infrastructure

- Better transportation, telecommunications and energy provision increases firm productivity and reduces cost to produce
- New business opportunities allow more companies be set-up in various industries (e.g. manufacturing/logistics companies)

Interventionist Supply-side Policy

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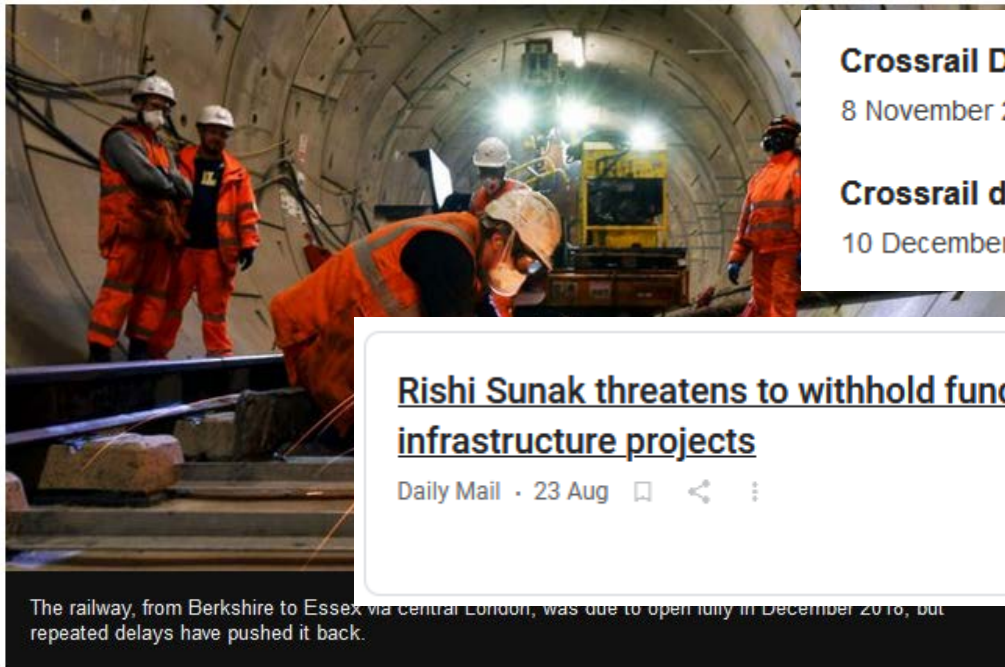
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Crossrail needs extra £450m and delayed until 2022

🕒 21 August 2020 | 📄 794

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Crossrail Delay: Line will not open until 2021 as costs increase

8 November 2019

Crossrail delay: £1.4bn bailout as autumn 2019 launch delayed

10 December 2018

Rishi Sunak threatens to withhold funding for poorly thought out infrastructure projects

Daily Mail · 23 Aug 📄 🔄 ⋮



The railway, from Berkshire to Essex via central London, was due to open fully in December 2016, but repeated delays have pushed it back.

Interventionist Supply-side Policy



Note that some investments may **increase AD** slightly in the short term before **shifting AS**, due to higher government spending and investment.

HS2 rail project work begins with pledge of 22,000 jobs

4 September 2020 1251



The Prime Minister visited an HS2 construction site on Friday



News story

Transport Secretary launches new Acceleration Unit to speed up transport infrastructure projects and build back better from COVID-19

New unit will boost the delivery times of major transport projects as new funding is announced.

- £1.1 million investment for Network Rail to develop short-term plans to relieve overcrowding at London Liverpool Street station
- £6.4 million scheme to build a new second footbridge serving all 4 platforms at St Albans City station...

Interventionist Supply-side Policy



24 July 2020 — Press release

UK aid funding available for innovative energy projects

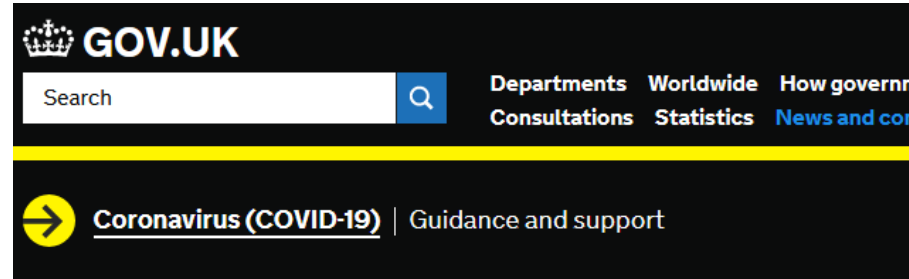
The UK's innovation agency, Innovate UK, is offering £20m of UK aid funding to develop and demonstrate innovative solutions for clean, affordable and secure energy access in sub-Saharan Africa, South Asia or South East Asia.



15 May 2020 — Guidance

Access coronavirus business innovation support package

Detail on how businesses can access the scheme providing continuity grants, loans for existing award holders and additional business advisory support services.



[Home](#) > [Coronavirus \(COVID-19\)](#) > [Health and wellbeing during coronavirus](#)

Press release

£20 million for ambitious technologies to build UK resilience following coronavirus outbreak

Businesses to help boost the UK's resilience to the long-term impact of coronavirus and similar future situations as a result of £20 million government funding.

Investment in Technology

- More efficient capital machinery can be used to produce more goods and increase output
- Technology tend to generate positive production externalities and spark further innovation

Interventionist Supply-side Policy

Guidance

Introduction of T Levels

Updated 4 September 2020

Contents

[T Levels: what they are](#)

[When they will start](#)

[How T Levels will work with
other qualifications](#)

[How T Levels have been
developed](#)

[Structure of a T Level](#)

[Industry placements](#)

T Levels: what they are

T Levels are new courses which follow GCSEs and are equivalent to 3 A levels. These 2-year courses, which launched September 2020, have been developed in collaboration with employers and businesses so that the content meets the needs of industry and prepares students for work, further training or study.

T Levels offer students a mixture of classroom learning and 'on-the-job' experience during an industry placement of at least 315 hours (approximately 45 days).

T-levels 'uniquely narrow' compared to technical courses in high performing countries, claims think tank

News



Investment in Human Capital

- Better education and labour training will increase the skills and productivity of workers
- Furthermore, training reduces occupational immobility, thus increasing labour demand, employment and output.

Market-Based Supply-side Policy

Supply-side policies that reduce government **involvement** in the free market to increase market efficiency. This is possibly done by providing **incentives** or encouraging **market competition**.

For example, by **reducing income tax**, it would mean...

Individuals more incentivized to work -> Higher supply of labour -> Bigger labour force -> Increase Factors of production -> Increase in AS and potential output (GDP)

Market-Based Supply-side Policy

M Mirror.co.uk

British Airways holidaymakers facing half-term hell as workers warn of strike action

British Airways workers say they're set to vote on strike action in the coming months, in a move that could spell havoc for half-term ...
2 weeks ago



“Unions say staff are being disposed of as cheaply and as quickly as possible”

G The Guardian

Civil servants' union will consider strike action over back-to-office plans

US edition · UK edition · Australian edition · International edition · The Guardian - Back to home. Support The Guardian. Available for everyone
...
12 hours ago



Labour market reforms

- Reduce unemployment benefits and power of labour unions to increase labour market mobility and size of labour force

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London Underground drivers vote to strike over pay

12 March 2020

London tube strikes

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Market-Based Supply-side Policy

REGIONAL GROWTH AND LOCAL GOVERNMENT GRANTS

WRITTEN BY TOWN CENTRE BID - PUBLISHED IN NEWS



Incentive related policies

- Reduce income, corporation and capital gains tax to increase incentive to work, produce goods/services and invest in new capital

Industrial/regional policies and Investment Grants

- Promote growth in key industries by tax cuts/allowances or subsidized lending to increase LRAS

Market-Based Supply-side Policy



Coronavirus: Key workers are clapped and cheered, but what are they paid?

By Ben Butcher
BBC News

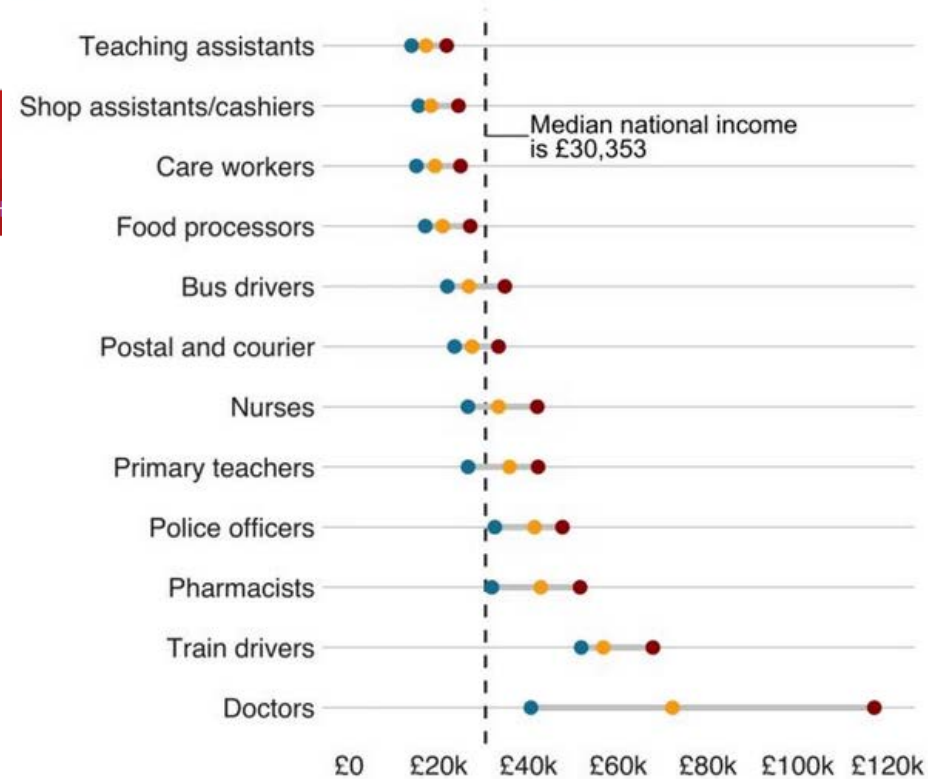
🕒 21 April 2020 | 📄



How much do 'key workers' earn?

Lowest and highest brackets of income for full-time employees
Salary in £ thousands


● Lowest 20% earn under this ● Median ● Highest 20% earn over this







Source: Office for National Statistics

Market-Based Supply-side Policy



Policies encouraging (free-market) competition



 THE WORLD BANK | **DOING BUSINESS** Measuring Business Regulations

ENGLISH | 

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Select Rankings by Region  Select Rankings by Income 

Economy	Starting a Business	Dealing with Construction Permits	Getting Electricity	Registering Property	Getting Credit	Protecting Minority Investors	Paying Taxes
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- Deregulation can reduce barriers to entry into markets, reducing market power and allow more firms to enter and compete. AS will increase with more firms producing goods and services in various markets.

Economy	Ease of Doing Business Rank 
New Zealand	1
Singapore	2
Hong Kong SAR, China	3
Denmark	4
Korea, Rep.	5
United States	6
Georgia	7
United Kingdom	8

Market-Based Supply-side Policy

Policies encouraging (free-market) competition

- Privatization can reduce public-sector inefficiencies. Privatizing firms giving companies a profit incentive to keep costs low, raise productivity and compete in the free market. This will increase supply and market efficiency.

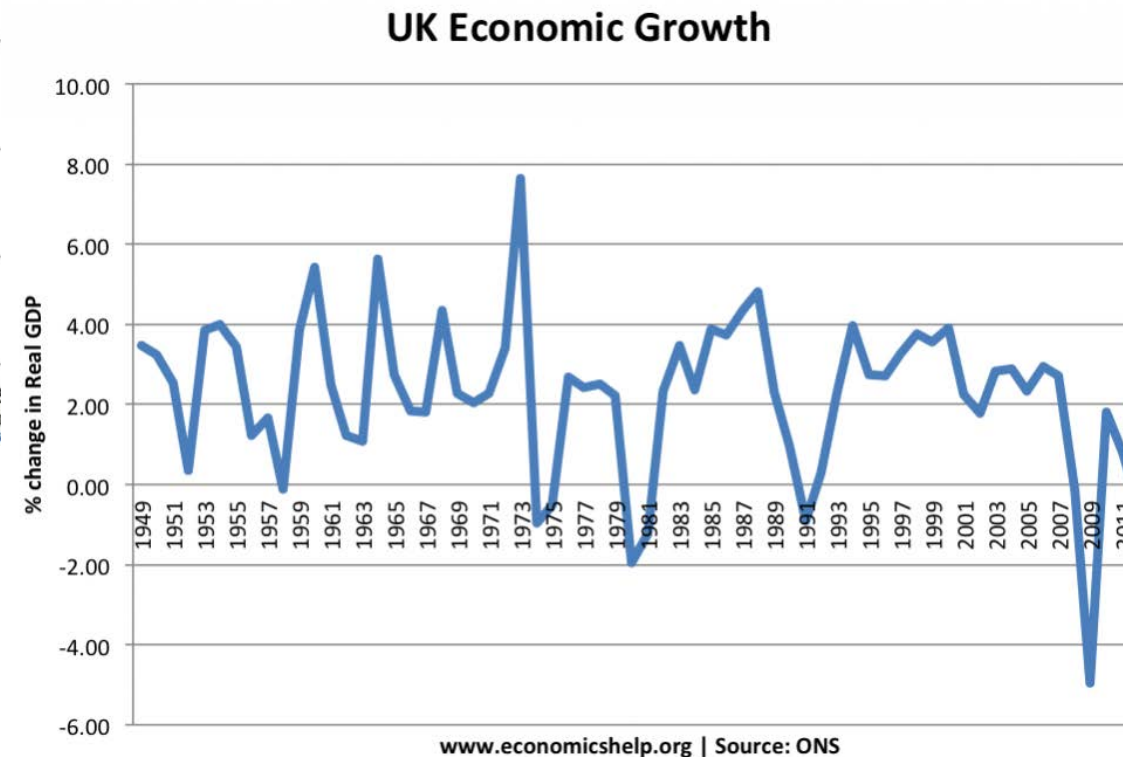
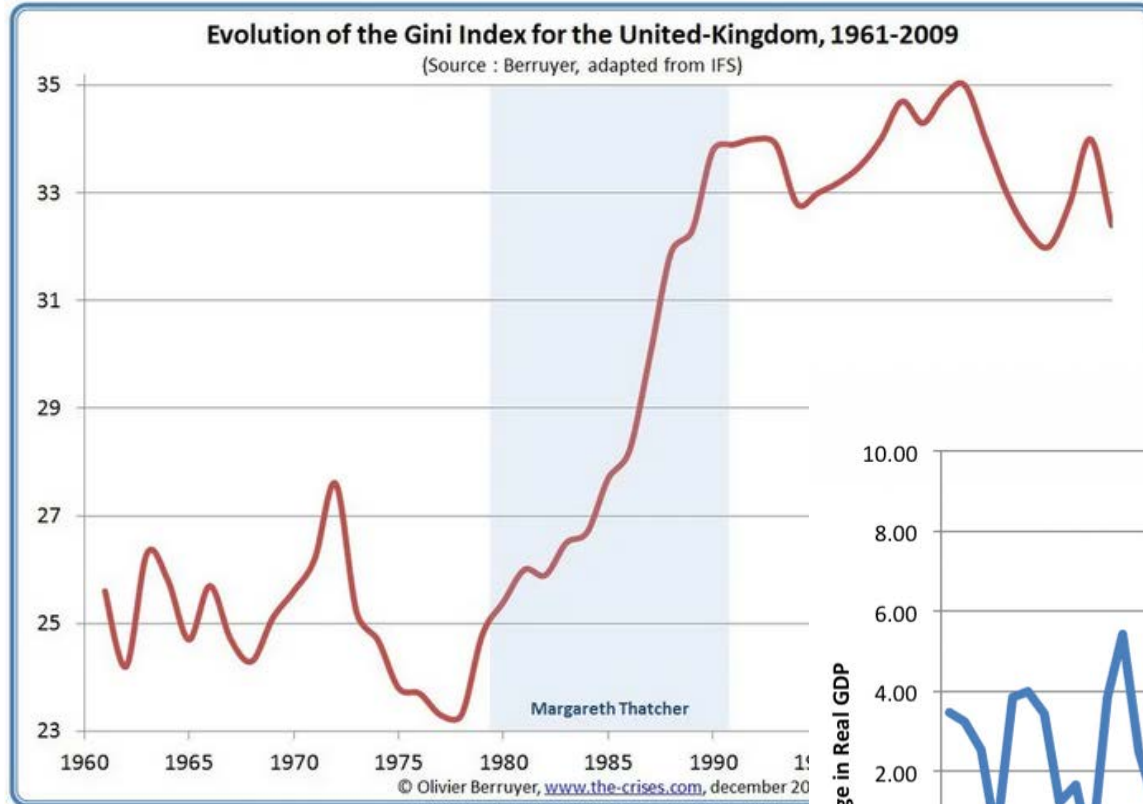
What Didn't Margaret Thatcher Sell?



Supply-Side Policy Problems

- Time lag
 - Investments to increase productivity can take years (e.g. education/training), although incentive-based policies may work faster (e.g. tax cuts)
- Effects on Equity
 - Capital gains and income tax are progressive, meaning tax cuts are likely to benefit the wealthy more. Furthermore the fall in government revenue and welfare support will also affect disadvantaged households, making the distribution of income less equitable.
- Exploitation of Workers
 - By reducing/removing min. wage, labour union power and worker rights can easily lead to exploitation of workers by firms, even though more of them may be employed.
- Diminishes Government Budget
 - Investment in human capital, technology and infrastructure combined with tax cuts & subsidies will reduce the government budget significantly. Meaning some spending now must be given up.

Supply-Side Policy Problems



Supply-Side Policy Advantages

- Increases Real GDP with Limited Trade-off
 - Compared to demand-side policies, supply-side policies are disinflationary but increases output.
- Reduces Natural Unemployment Rate
 - Labour market reforms reduce frictional unemployment, and investment in human capital reduces structural unemployment. This decreases the long run natural unemployment rate.
- Improves International Competitiveness & Current Account
 - By investing in productivity through technology, human capital & infrastructure, this will reduce production costs and make domestic producers more competitive. This can potentially have a positive impact on the current account.
- Long Term Solution/Impact
 - Supply-side policies have a positive effect on the economy in the long run by addressing structural issues, rather than temporary output boosts in demand-side policy

Evaluating Supply-Side Policy

- Gov. Budget & Opportunity Cost
 - Any government spending that needs to be given up for investing (e.g. infrastructure) should be considered. It may also be unwise to invest if the government is in significant debt.
- Current Distribution of Income / Equity
 - If income inequality is high, then the government may consider other policies
- Timeframe
 - Given investment in capital or particular industries may take years, timing should be an important consideration as the investment may become obsolete by completion.
- Extent of Market Failure
 - Effectiveness of market-based policies depends on the level of inefficiency in the market caused by labour unions, labour legislation and monopolies.