Supply-side Economic Policies

AS Economics Presentation

2005

Key supply side concepts

- Aggregate supply
- Incentives for people and businesses
- Productivity
- The economy's productive potential
- Capital Investment
- Research and development
- Product and Process Innovation
- Skills / Human Capital
- Competitive markets / market deregulation
- Long run economic growth
- Non-inflationary growth

What are Supply-Side Policies?

- Supply-side policies are designed to:
  - Improve incentives for people to get new jobs
  - Increase the productivity of labour and capital inputs
  - Increase the occupational and geographical mobility of labour to reduce unemployment
  - Increase the level of capital investment and research and development spending by firms
  - Stimulate inflows of overseas capital investment
  - Increase business efficiency by promoting more competition within and between markets
  - Stimulate a faster pace of invention and innovation throughout the economy
  - Provide a platform for sustained non-inflationary growth of an economy

What are Supply-Side Policies?

- The aims of supply side policies are to
  - (1) Improve the efficiency of market forces
  - (2) Contribute to a higher level of productive potential (long run aggregate supply)
  - (3) Create the conditions for rising living standards
- Key point:
  - Supply side policies focus on the long run
  - There are often few “quick fixes” to structural economic weaknesses

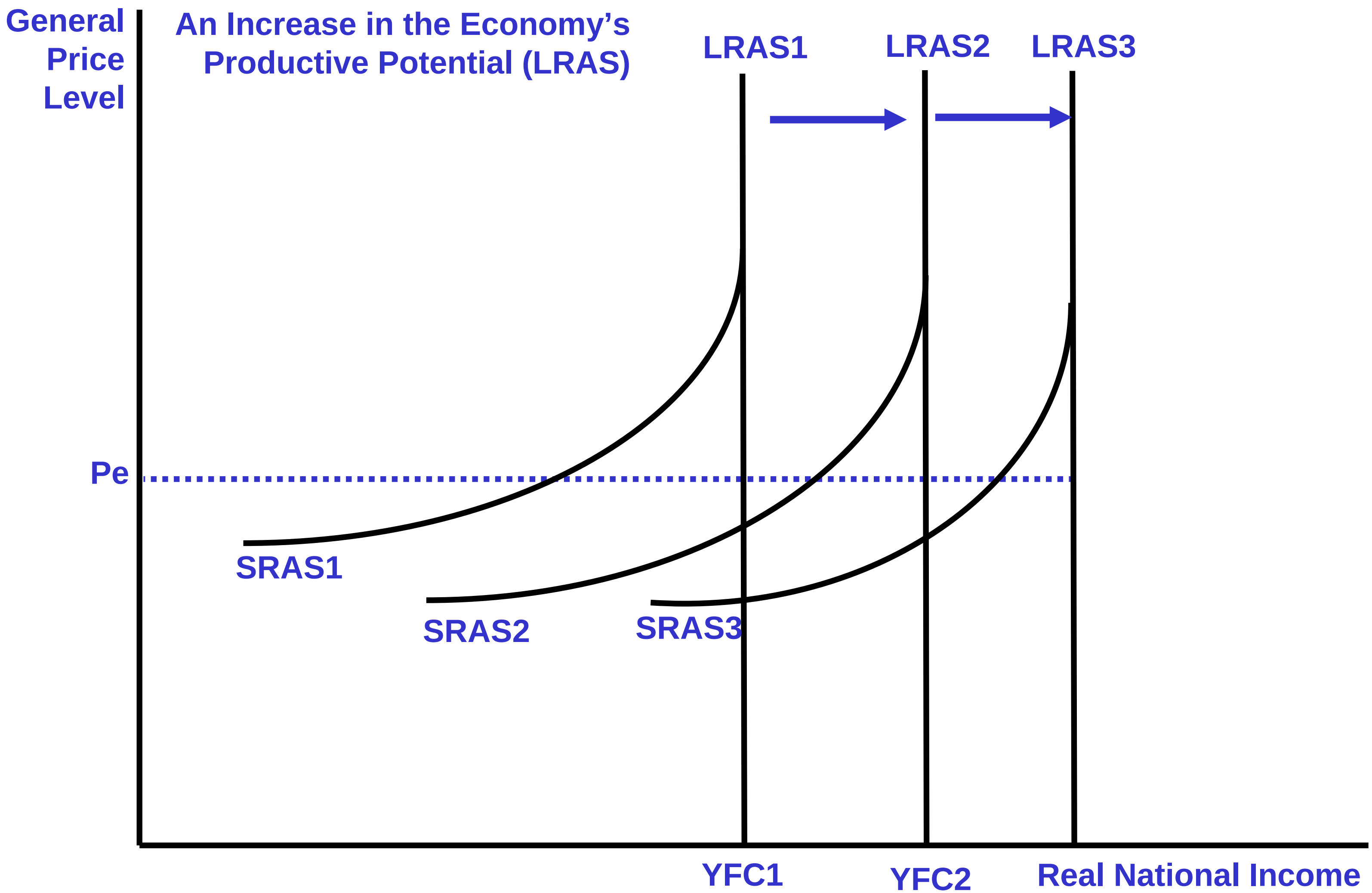
Different Perspectives on the Supply-Side (1)

- Neo-Liberal “Classical” Economists
  - Critical of “big government”!
  - Believe in the power of free markets
  - Supply-side should be “liberated” by a reduction in government spending
  - Taxation should be as low as possible to create incentives for people to work harder
  - Economic reforms should include reducing the power of trade unions

Different Perspectives on the Supply-Side (2)

- The Interventionist Approach
  - Direct state investment is required in education, training & other key public services
  - Intervention to correct for market failure may help to boost the supply side of an economy in the long run
  - Reforms to the public services
  - Tax incentives for business investment and innovation
  - Strong regional policy to help deprived areas of the economy

Increasing Productive Potential



Supply Side Reforms for Product Markets (1)

- Many of the supply-side policies mentioned below were first introduced by the Conservative government from 1979 – 1997
- But the Labour party is also keen on such policies!
- Privatisation – i.e. a transfer of ownership from the state (government) to the private sector
- Deregulation "opening up" of markets - allowing for more competition
- Toughening up of competition policy – for example investigation and prosecution of anti-competitive practices

Supply Side Reforms to Product Markets (2)

- A commitment to free international trade
- Encourage entrepreneurship and new business start-ups
- Policies to encourage increased investment including foreign direct investment into UK product markets
- Measures to increase price flexibility

Deregulation of markets (1)

Postal services opened to competition in 2006

Should the UK gambling industry be deregulated?

Deregulation of markets (2)

Has bus deregulation improved services and lowered prices for consumers?

Taxis are heavily regulated – could the market be opened up?

Privatisation

- Between 1980 and 2001 many former state-owned and state-managed businesses were transferred into the private sector
  - British Gas
  - British Telecom
  - British Airways
  - British Steel
  - British Aerospace
  - Regional water companies
  - Electricity generators and distributors, and the Railways
- Privatization was designed to break up state monopolies and create more competition

Measures to increase price flexibility

- Reductions in government set prices
  - E.g. abolition of rent controls
  - Elimination of minimum wages
  - Reductions in government subsidies e.g. farm support
  - Freedom of utility businesses to set their own prices

Supply Side Reforms to the Labour Market

- Supply side reforms to the labour market are designed to improve the quality and quantity of the supply of labour available to the economy
- They seek to make the British labour market more flexible so that it is better able to match the labour force to demands placed upon it
- In the last two decades, the UK labour market has undoubtedly become more flexible, mirroring developments in the United States

Labour Market Reforms

- Reforms to employment laws
  - Reduction of many trade union protections
  - Measures encouraging the expansion of short term contracts and part time labour
- Increased investment in education and training
  - Real terms increases in state funding of education
  - Tax relief for businesses running training schemes
  - Subsidies to encourage firms to employ the long-term unemployed under the New Deal Scheme
- Reforms to the tax and benefit system
  - Reductions in rates of income tax for lower income tax payers
  - Reforms to the system of welfare benefits

Building a flexible labour market

- Expansion of flexible employment contracts
  - Short term contracts
  - Increase in part time employment
  - Variable hours
  - Easier for businesses to change the size of their workforce or the number of hours worked
- Flexible pay arrangements
  - Performance-related pay
  - Share options schemes
- Incentives for employer-based training
  - Modern apprenticeships
  - National Vocational Qualifications Framework

The importance of supply-side policies

Provides the platform for long term growth

More productivity - better living standards

Allows the economy to grow without inflation

Long term importance of supply-side policies for the British economy

More competition - lower prices – gains in welfare

Makes the UK more competitive in global markets

Increased tax revenues to fund state spending

A stronger supply-side

- On the right tracks
- “There has been a remarkable structural improvement in the British economy. This began under Margaret Thatcher and has largely been maintained under Tony Blair.
- Deregulation, privatization, reductions in trade union power and reform of unemployment benefits have transformed the business environment.”
- Ed Crooks, Economics editor of the Financial Times. June 2004