Macroeconomics: BSc Year One

Components of Basic Models - Government

Government Expenditure

g is the volume of goods which the government wishes to buy, not including expenditure on social services (for example). *g* is assumed to be exogenous, compared to *c* and *i* which are endogenous – that is, the determination of *g* occurs outside the model, not within it.. This is because it is hard to theorise on how governments will act, and the ultimate aim of macroeconomics is to work out how the rest of the economy will alter with any changes in *g*.

There *are* theories on government behaviour (such as public choice theory), because government is, after all, simply a collection of individuals who have personal aims (getting re-elected or promoted). It can be predicted that government spending will vary around elections, and will tend to become excessively large, as economic performance influences elections considerably.

Any item of government expenditure is likely to be small in relation to the total, but individuals will be affected a lot by these items, and will lobby for it to be increased; there would be little opposition to this (tax would hardly rise at all), so the government will be biased towards agreeing to expenditure, leading to excessively large amounts.

For the purposes of our model, we will set:

$$g = \bar{g}$$

where the bar indicates exogeneity.