

## Budget Module Self-Test

### Unit 2: Introducing the Budget

#### 1. Does it matter if governments have high budget deficits?

A budget deficit is defined as the excess of government's total expenditure over total revenue. The deficit to Gross Domestic Product (GDP) ratio is used to indicate the share of national income that will have to be used to finance the deficit.

Deficit changes are not necessarily the result of a shift in fiscal policy, but can also reflect the business cycle. Consistently growing deficits, however, can however:

- put upward pressure on interest rates so as to 'crowd out' private investment
- reduce funds for important services as the government will have to put aside a proportion of funds to service its stock of debt
- create inflationary pressures (some governments have resorted to 'printing money' in order to meet debt servicing obligations. This policy is often called "quantitative easing". The policy was used in Japan in the 1990s in a bid to avoid economic stagnation and some govts are reportedly considering such measures today if falling interest rates do not stimulate struggling economies)
- force future generations to make sacrifices for us to spend money today. This problem is exacerbated when borrowed funds are not invested productively.

#### 2. List some of the main sources of government revenue. Which of these are important in your country?

You should have included in your answer:

- Direct taxes: Tax paid directly to government, e.g. a tax imposed on the income of individuals or companies.
- Indirect taxes: Tax paid to 2nd party, e.g. shop owners, who pass it on to the government. Value added tax & custom duties.
- User charges for certain services.
- Foreign aid
- Income from investments or commercial activities (privatization?).

### **3. How does the budget in your own country compare to the principles of good budgeting?**

World Bank (1998) defines the principles of good budgeting as:

- Comprehensiveness: Covers all fiscal operations
- Predictability: Certainty by agencies about spending allocations in medium term to plan ahead.
- Contestability: No item should have an automatic claim to funding.
- Transparency: Accurate, timely, reliable & comprehensive information.
- Periodicity: Should cover a fixed time, & follow a clear schedule.

How the budget in your own country meets these principles of good budgeting will be discussed further in the e-discussion.

### **4. Are fiscal discipline, allocative efficiency and operational efficiency the only objectives of budgeting?**

- Fiscal discipline: Budget totals should be the result of explicit, enforced decisions; they should not merely accommodate spending demands.
- Allocative efficiency: Expenditures should be based on government priorities and on effectiveness of public programs.
- Operational efficiency: Agencies should produce goods and services at a cost that achieves ongoing efficiency gains.

Schick (2003) reports that performance budgeting has becoming increasingly important in recent decades. This is where the budget presents information on what departments have done or expect to do with the money provided to them; in its strictest form a budget may explicitly link each increment in resources to an increment in outputs or other results.

Budgets may also consider different impacts on men and women. So-called gender budget initiatives can also propose the adoption of budgets with explicit gender-related goals. The aim is to incorporate awareness of gender into the process of formulating the country's budget in the first place (McGee 2007: 15). This can also apply, of course, to other disadvantaged groups in society.

Other considerations could also include conflict prevention/resolution.