**Taxation and government spending**

In addition to economic change, businesses can be affected by economic policy decisions taken by government. If worried about inflation, a government could decide to increase income tax. This would take spending power out of the pockets of consumers, softening the upward pressure on prices, but cutting demand for the products and services produced by businesses. What might be right for the economy as a whole could be damaging for individual businesses.

Why would any government take actions that could damage businesses and therefore threaten jobs? The answer is simple: because ministers may believe that short-term pain may be necessary for long-term gain. This might be correct, but it will be no consolation to any business squeezed out of business by an unexpected tax rise.

The other main weapon government can use to achieve its policy goals is to change the level of government (known as 'public') spending. At present, public spending generates just over 40 per cent of the British economy. Private consumers (you and me) mainly generate the rest. The government spends huge sums on the health service, defence, roads and much else. If the government was concerned about rising prices, it could consider cutting back on its own spending. This would reduce the income of businesses involved in education, road-building, and so on. They, in turn, may have to make redundancies, thereby dampening down consumer spending, which should help to keep prices from rising so sharply.

'The last thing you want to do is raise taxes in the middle of the recession.'

Barack Obama, US President

It follows, therefore, that sensible businesspeople keep an eye on government activity. Years ago, the government announced its tax and spending plans in the Spring Budget, which was always kept secret until the government announced it. Today, an 'Autumn Statement' announces, six months in advance, the government's public spending plans. This ensures that firms can anticipate the tax decisions that will be announced in the spring.

Table 45.4 shows how a government could use its power over taxation and spending to tackle different economic problems.

