**Federal Expenditure and Deficits**

What is the difference between deficits and debt?

Distinguish between stocks and flows. Why are deficits considered a flow concept?

Why is the opportunity cost of producing government goods/services partially a function of the way the goods/services are financed?

Explain the rationale for deficit financing government production of goods such as roads and bridges.

Explain the rationale for tax financing the extension of hours at the Smithsonian.

Market for loanable funds:

interest rate

S

government

i2

i1

D+G

L2

L1

D

L3

loanable funds

Explain why the supply curve for loanable funds is positively sloped.

The model implies that government borrows at the same interest rates as non-government borrowers. What is unrealistic about this assumption?

In the model, does government borrowing increase interest rates?

Without government, what is the total amount of loanable funds transacted in the market?

In the model, does government borrowing (G) increase the total pool of loanable funds transacted in the capital market?

How do we know L2-L3 is the total amount government borrows?

How much does private borrowing decrease when government demands funds in the market? Why is this called crowding out?

If the supply curve for loanable funds were horizontal, would crowding out occur?