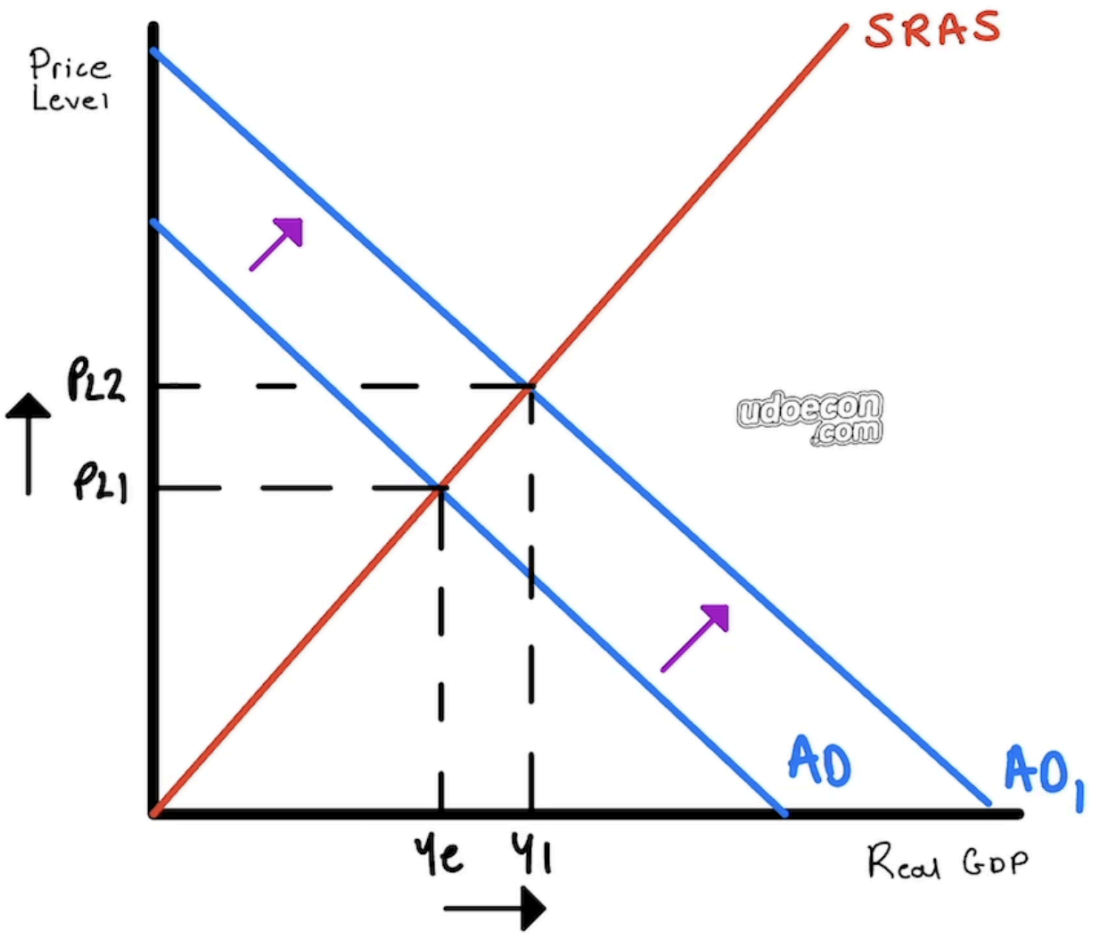
Conflicts and trade-offs between objectives and policies

In an ideal world the government would be able to achieve all macro objectives simultaneously , unfortunately due to trade offs between macro objectives it means that when we achieve one macro objective e.g 2% inflation rate target it can worsen one of our other macro objectives e.g employment.

Economic growth vs low inflation

Economic growth is defined by an increase in real gdp .This is usually driven by increasing **AD** . When AD shifts right (AD→AD1), **real GDP rises** (YE→Y1) but the **price level also rises (PL1→PL2)** , creating **demand-pull inflation**.

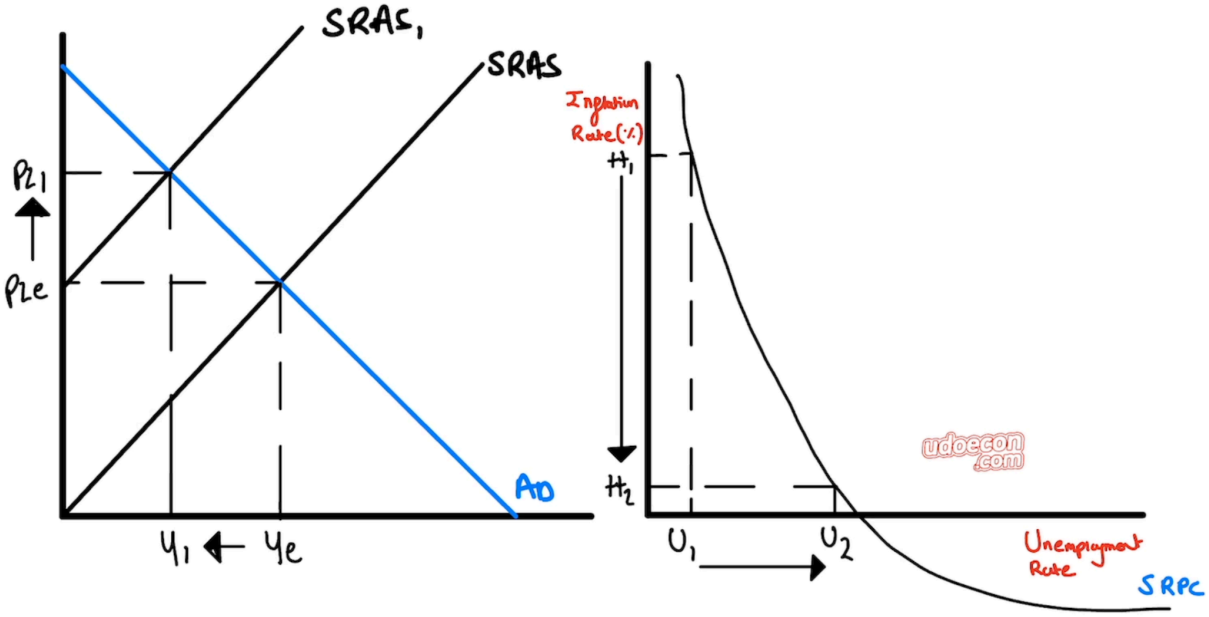


How strong this trade-off is depends on **spare capacity**. If there is high spare capacity (Keynesian LRAS), rising AD can increase output with little upward pressure on prices because unused resources are available. As the economy moves closer to full capacity, resource scarcity pushes prices up more quickly.

Low unemployment vs low inflation

As unemployment falls, workers gain bargaining power because firms find it harder to recruit replacements. This higher bargaining power means workers can negotiate higher wages ,increasing firms' costs and causing a shift of SRAS to SRAS1 causing cost push inflation from PLe to PL1 .

This relationship is shown by the **short-run Phillips curve (SRPC)**: lower unemployment (U1) tends to be associated with higher inflation (TT1), and vice versa .



Economic growth vs current account balance

Economic growth often worsens the current account because higher incomes raise spending on **imports**.

If growth is caused by **AD rising**, the price level tends to rise, which can reduce export competitiveness (exports become relatively more expensive), worsening the current account further.

If growth raises inflation and the central bank responds with higher interest rates, "hot money" inflows can appreciate the currency. Appreciation makes imports cheaper and exports more expensive(think SPICEE), which can widen a current account deficit (the size of the effect depends on PED for exports and imports).

If growth is driven by **LRAS shifting right**, the price level may fall, improving competitiveness and potentially supporting exports, so the trade off may be smaller.

Economic growth vs protecting the environment

Economic growth can damage the environment because higher output and incomes increase resource use (e.g. fossil fuels), pollution, and waste.

But it depends on the type of growth: if growth is driven by green industries e.g UK net zero by 2050 and cleaner technology, environmental harm can be reduced, especially if consumers shift towards sustainable products and away from polluting firms.

Economic growth vs reducing income inequality

Growth can increase inequality if the gains go disproportionately to owners of factors of production (profits, dividends, asset returns) compared with wage growth.

Two common growth drivers can widen inequality:

- **Technological progress**: automation raises productivity and growth but can reduce demand for some workers, while raising wages for high-skill workers (e.g. engineers, coders).

- **Globalisation**: offshoring and international competition can reduce demand in some domestic industries, increasing unemployment in affected areas, while increasing demand in sectors like financial services.

However, inequality is not inevitable. Higher growth can increase tax revenues, funding welfare support and retraining schemes to help workers transition into expanding sectors.

How macro policies can create trade-offs

Monetary policy

Lower interest rates reduce the reward for saving and cut borrowing costs, which tends to raise consumption and investment and shift AD right, increasing growth and employment. But it can also raise inflation.

Lower rates can encourage risk-taking and speculation, potentially creating **asset price bubbles e.g bitcoin**.

Quantitative easing (QE) increases liquidity by buying government bonds with newly created digital money, encouraging lending and investment and boosting AD and growth. But QE can raise asset prices, benefiting asset owners and potentially increasing inequality (e.g. higher house prices make it harder for non-owners to buy).

For example, during covid the UK made £450bn worth of new money , this massively boosted the levels of income inequality within the UK . To put it into some perspective, in 1979 the top 10% of earners took home **21%** of national income , in 2026 the top 10% took **34%** of national income which shows how the income inequality gap has widened .

Fiscal policy

Higher government spending raises AD, supporting growth and employment. However, stronger AD can increase inflation, reduce export competitiveness and worsen the current account, and it may increase the **budget deficit** if not funded by higher taxes.

Supply-side policies

Supply-side policies raise productive capacity (LRAS shifts right). This can increase growth and employment while reducing inflation, and can improve competitiveness.

But there can be distributional trade-offs. Market-based reforms (e.g. deregulation, privatisation, weakening worker bargaining power, tax cuts) may increase inequality, while interventionist supply-side policies (e.g. higher spending on education/healthcare) can worsen the budget balance in the short run.