Source : www.thehindu.com Date : 2018-11-01

WHAT'S CROWDING OUT EFFECT IN ECONOMICS

Relevant for: Indian Economy | Topic: Government Budgeting incl. Fiscal Deficit

This refers to a phenomenon where increased borrowing by the government to meet its spending needs causes a decrease in the quantity of funds that is available to meet the investment needs of the private sector. Some have argued that the diversion of investment funds away from the private sector adversely affects economic growth. Others, however, believe that government spending does not always lead to a crowding out of private investment in the economy. They instead argue that government demand for funds can compensate for the lack of private demand for funds during economic depressions, thus helping to prop up aggregate demand.

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