

# Economy and Politics

The global economy is shaped not only by markets and supply and demand, but also by government decisions, political ideologies, and international relations, all of which influence and shape growth, development, stability, and inequality<sup>1</sup>. This field is referred to by scholars as political economy<sup>2</sup>.

Governments intervene through various policies that include systems like taxes and public spending. Combined with the implementation of economic reforms and amendments, such as interest rates, the government's objective is to stabilize markets, correct failures, and reduce inequality. However, if carried out recklessly, interventions carry many risks that can all have detrimental effects. Subsidies and bailouts can promote inefficient industries, prevent resources from being used productively, and create moral hazard, encouraging risky behavior<sup>3</sup>.

Various political systems and ideologies can shape these interventions differently, with capitalist economies prioritizing market efficiency, socialist systems emphasizing redistribution, and authoritarian regimes sometimes pursuing rapid growth at the expense of equity<sup>4</sup>.

On a global scale, political actions can disrupt supply chains, affect exchange rates, and threaten financial stability, while international alliances, trade agreements, and sanctions can amplify or mitigate these effects. Economic downturns often reinforce political instability, which in turn can exacerbate crises, creating a cycle of uncertainty, as seen during the 2008 financial crisis.



Government intervention in the global economy has, in some way or another, an effect on either the world economy, national economy, the world markets or even some SMEs, otherwise known as small and medium enterprises.

In many cases, government intervention is positive and required. Political intervention can often bring several benefits, including equality. In a free market, significant inequality and poverty are common. An intervention can bring along with it “basic security net – unemployment benefit, minimum income for those who are sick and disabled.”<sup>5</sup> This helps the general population by increasing net welfare and aids individuals to rid themselves of terrible poverty.

Beyond income redistribution, the government can also influence consumer shift behaviour. If the general public were to increase the consumption of demerit goods like drugs, alcohol and prostitution, a significant increase in personal costs and

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<sup>1</sup> Role of Government Intervention | CARI Journals

[https://carijournals.org/journals/IJECOP/article/view/1763?srsId=AfmBOopS0Q2h\\_YFuuSDNoTdCoLgdA6BUj1wzCq\\_9aF5OkIV3nSOqoT\\_t](https://carijournals.org/journals/IJECOP/article/view/1763?srsId=AfmBOopS0Q2h_YFuuSDNoTdCoLgdA6BUj1wzCq_9aF5OkIV3nSOqoT_t)

<sup>2</sup> International Political Economy | Thomas Oatley

<https://www.taylorfrancis.com/books/mono/10.4324/9781003276524/international-political-economy-thomas-oatley>

<sup>3</sup> Moral Hazard and Bailouts | IMF

<https://www.imf.org/external/pubs/ft/wp/1999/wp99106.pdf>

<sup>4</sup> Economic Systems and Political Implications | Fiveable

<https://fiveable.me/introduction-comparative-politics/unit-12/economic-systems-political-implications/study-guide/1pk0kZDILN0uk2sr>

<sup>5</sup> Political Instability and Economic growth | ScienceDirect

<https://www.sciencedirect.com/science/article/pii/S0176268024000880>

significant social costs, such as crime, would be seen. The government would attempt to combat this with what is known as a “Fiscal Policy”<sup>6</sup>.

If the government were to intervene and manage to pinpoint what the more damaging goods for the national population are, action in the form of higher tax, advertising campaigns and behavioural economics, (for example, making cigarettes difficult to buy with unappealing packets)<sup>7</sup> would be taken.

Moreover, the government would equally employ what is known as “monetary policy”, which is the “action that a country's central bank or government can take to influence how much money is in the economy and how much it costs to borrow<sup>8</sup>” (Monetary Policy, Bank of England, 2026).

Monetary policy interest rates are the benchmark rates set by central banks, like the Bank of England for the UK, to control inflation, stimulate economic growth, and manage credit, with higher rates cooling an overheating economy and lower rates encouraging borrowing and spending. For example, the Bank of England's current base rate is 3.75% following several cuts in 2025, but further adjustments depend on inflation trends, with predictions saying a plateauing or slight decrease is in store.

In rarer and more urgent scenarios, as a last line of defense, another used method is quantitative easing. As per the definition of the Bank of England, “quantitative easing, abbreviated to QE, is an unconventional monetary policy where central banks, like the Bank of England or Federal Reserve, create new digital money to purchase government bonds and other financial assets<sup>9</sup>”.

The government’s aim with these implementations is to amend market failures, promote equity, and foster stability.

These amendments help, firstly, reduce major unemployment. Through the installations of job centres, the government “handles many responsibilities [...], reducing the burden on employers<sup>10</sup>”.

They also help the smoothing of economic cycles, primarily through the “counter-cyclical fiscal and monetary policies designed to manage aggregate demand.<sup>11</sup>”. However, with such an extensive amount of additional bureaucracy, government aid can create long-term dependency and inefficiency in resource allocation. As explained by the UK parliament, “Long-term welfare benefits can reduce work incentives by creating a "poverty trap" where the financial gain from employment is minimal or non-existent compared to remaining on benefits, [...] described as the ‘benefit trap’<sup>12</sup>”.



<sup>6</sup> Fiscal Policy : Taking and Giving Away | IMF

<https://www.imf.org/en/publications/fandd/issues/series/back-to-basics/fiscal-policy>

<sup>7</sup> Pros and Cons of Government Intervention | Economicshelp

<https://www.economicshelp.org/blog/151818/economics/pros-and-cons-of-government-intervention/>

<sup>8</sup> Monetary Policy | Bank of England

<https://www.bankofengland.co.uk/monetary-policy>

<sup>9</sup> IEO evaluation of the Bank of England’s approach to quantitative easing, section 1.1 | Bank of England

<https://www.bankofengland.co.uk/independent-evaluation-office/ieo-report-january-2021/ieo-evaluation-of-the-bank-of-englands-approach-to-quantitative-easing>

<sup>10</sup> Keep Britain Working Review: Discovery | Gov.uk

<https://www.gov.uk/government/publications/keep-britain-working-review-discovery>

<sup>11</sup> Monetary Policy | IMF

<https://www.imf.org/en/publications/fandd/issues/series/back-to-basics/monetary-policy>

<sup>12</sup> Welfare Reform and Work Bill | UK Parliament

<https://hansard.parliament.uk/commons/2016-02-23/debates/1602234900001/WelfareReformAndWorkBill>

This effect is particularly pronounced when combined with high tax rates on low earnings and the withdrawal of non-cash benefits like housing support.”<sup>13</sup>

Furthermore, in many cases, the solution is worse than the outcome. As the Sphere-Ed paper “Market Failure versus Government Failure” explains, “Market failure occurs when free markets inefficiently allocate resources due to externalities, monopoly power, or public goods, failing to maximize social welfare. Conversely, government failure arises when intervention to correct these issues—such as taxes, subsidies, or regulations—creates deeper inefficiencies, higher costs, or perverse incentives, often making the situation worse than the original market outcome”<sup>14</sup>.

Just as a poorly maintained machine will fail, political programs with misallocated resources can worsen the problems they were meant to solve.



In conclusion, even though markets and supply and demand are still at the center of all economic activities, political interventions, government policies, and international relations are equally important in influencing economic outcomes. Through fiscal and monetary policies, international alliances, and, at times, drastic measures, governments try to correct market failures, maintain stability, and reduce inequality in society, especially during times of crisis in the economy. Various political ideologies play an equally important role in influencing policies and outcomes, thus affecting the overall performance of economies. In addition, with globalisation, there is an international ripple effect with domestic policies, thus influencing global markets and economies as well. Even with the best intentions, without careful balance, government interventions risk reinforcing the very issues they aim to resolve, and inefficiencies and even government failures could occur in the long run.

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<sup>13</sup>Universal Credit implementation: meeting the needs of vulnerable claimants | House of Commons Work and Pensions Committee  
<https://publications.parliament.uk/pa/cm201213/cmselect/cmworpen/576/57609.htm>

<sup>14</sup>Market Failure versus Government Failure | Sphere-ed  
<https://www.sphere-ed.org/lesson/market-failure-versus-government-failure>