**Brady Kondek** **3.05 The Fed and Monetary Policy**

# The Fed and Monetary Policy

*Analysis and Comparison to Fiscal Policy*

**Step 1:** Analyze each scenario. Answer the questions in complete sentences.

<table>
<tr><td rowspan="3">Scenario A<br><br>College graduates are moving back in with family in record numbers. They are waiting longer than previous generations to buy homes and start families. Data show downward trends in new home building, mortgage applications, and the birthrate. Multiple markets are complaining of falling demand. A national supplier of home goods permanently shut down. The media is calling babies born today part of the “baby bust generation.” Economists predict future school closings and labor shortages.</td>
<td>Would the Fed address the scenario with expansionary or contractionary policy? Explain.<br><br>The Federal Reserve would respond with expansionary policy, in an effort to help increase the tanking economy seen in this scenario. This downward trend is most likely due to the economy being week, as well as an excessive amount of supply. This type of policy helps to strengthen the weak economy, helping to increase demand.</td></tr>
<tr><td>What is a specific monetary action the Fed might use in this scenario? Identify the tool and how the Fed would use it. Explain how this would address the scenario.<br><br>Lowering interest rates would help by encouraging more people to take out loans. More people are going to take out a loan when the rates are lower, as they will be paying back less than if they were higher. Because of this, the demand would increase significantly.</td></tr>
<tr><td>What is a specific fiscal action that Congress might use in this scenario?<br><br>Reducing taxes would allow more money to be in the people’s hands. With more money at their disposal, they would be more willing to spend towards a new home; as opposed to not having as much money. More people buying homes equals increase in housing demand.</td></tr>
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<tr><td>Scenario B<br><br>Reports of price increases for everyday goods begin to dominate the news. People are complaining that their wages and salaries are not keeping pace with the cost of living. Most people being interviewed have</td>
<td>Would the Fed address the scenario with expansionary or contractionary policy? Explain.<br><br>In this case, the Federal Reserve would respond through contractionary policy. The main problem here is that inflation is occurring, which is driving prices up; because there is too much money in circulation. Adopting this kind of policy would aid in lowering that money supply.</td></tr>
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<td rowspan="2">jobs, and the national unemployment rate is low. However, many commonly remark that they are looking for second jobs or jobs that pay more because basics like food and clothing cost them so much more than a year ago.</td>
<td>What is a specific monetary action the Fed might use in this scenario? Identify the tool and how the Fed would use it. Explain how this would address the scenario.<br><br>A specific action they may take, through monetary policy, would be selling government bonds. Through selling them, they would be receiving that money; therefore lowering the amount of money in circulation. By lowering the money supply in this case, the value of money would increase.</td>
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<td>What is a specific fiscal action that Congress might use in this scenario?<br><br>Reducing federal spending, as well as increasing taxes. As taxes are higher, people are paying more for them. Through more income that is received by the government, this also help to balance out the amount of money in circulation.</td>
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<td rowspan="3">Scenario C<br><br>The media report that an “epidemic of the jobless” has emerged. Major corporations and small businesses alike are laying off workers. People are out of work in record numbers and struggling to find jobs. Some admit that they have given up looking. Housing foreclosures are increasing, while banks say they lack the funds to approve new loan applications or to adjust existing loans. Requests for unemployment, housing, and nutrition assistance are at record highs. Charity organizations are not receiving enough donations to meet the growing need in their communities. Credit card companies say the average debt balance is climbing while repayments are falling behind.</td>
<td>Would the Fed address the scenario with expansionary or contractionary policy? Explain.<br><br>The Federal Reserve would respond with expansionary policy. Due to the fact that the economy is sinking here, they need it to go up. Expansionary policy would increase economic activity and demand, helping to boost the economy.</td>
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<td>What is a specific monetary action the Fed might use in this scenario? Identify the tool and how the Fed would use it. Explain how this would address the scenario.<br><br>Specifically, the Federal Reserve may lower interest rates if they choose to go with monetary policy. By them doing this, people pay less money in interest; therefore having more money that they are able to spend. With more money to spend, there would be more economic activity; helping the economy to improve upwards.</td>
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<td>What is a specific fiscal action that Congress might use in this scenario?<br><br>Through fiscal policy, the Federal Reserve would most likely issue out stimulus checks. This as well would increase the amount of money in people’s pockets, helping to increase economic activity. The difference here is instead of people saving money on interest, the government is actually giving them money.</td>
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**Step 2:** Which type of policy, fiscal or monetary, do you think is more effective in today's U.S. economy? Explain your perspective, referencing an event from within the past 10 years. Write at least one complete paragraph.

Out of the two, monetary policy is the most effective option. The big key difference between them is the fact that monetary policy is much easier to implement; as fiscal policy has to go through the government (which can take a while), while monetary can go through the bank. During the pandemic, the Federal Reserve lowered the federal funds rate, in an effort to increase available money and expand the economy as much as possible during the time.