Standard 20 : Monetary and Fiscal Policy

Students will understand that:
Federal government budgetary policy and the Federal Reserve System's monetary policy influence the overall levels of employment, output, and prices.

Students will be able to use this knowledge to:
Anticipate the impact of federal government and Federal Reserve System macroeconomic policy decisions on themselves and others.

The U.S. federal government's taxation and spending policies, and the Federal Reserve System's monetary policies affect the nation's overall levels of employment, output, and prices. However, many government taxation and spending activities are undertaken for other reasons, as well. Government expenditures for national defense, human services, and other purposes are made to meet specific objectives and not primarily because of their fiscal policy effects. Other important objectives must be merged with the goals of full employment, price stability, and economic growth. Therefore, government programs may have contradictory effects upon employment and inflation. Understanding these effects is complicated also by the time lags that occur before action taken pursuant to a specific policy begins to affect overall levels of employment, output, and prices.

In spite of these difficulties, policy makers and the general public continue to examine and debate the overall stabilization effects of public policy actions, because the consequences are so important. Citizens should understand the role of conflicting objectives and the limitations on the effectiveness of economic stabilization policies in order to develop realistic expectations about what can be accomplished with taxation, spending, and monetary policies.

Benchmarks

Grade 12

At the completion of Grade 12, students will know the Grade 4 and Grade 8 benchmarks for this standard, and also that:	At the completion of Grade 12, students will use this knowledge to:
Fiscal policies are decisions to change spending and tax levels by the federal government. These decisions are adopted to influence national levels of output, employment, and prices.	Identify historical examples of fiscal policies and explain whether these policies were adopted to influence levels of output, employment, prices, or all three.
In the short run, increasing federal spending and/or reducing taxes can promote more employment and output, but these policies also put upward pressure on the price level	Outline the fiscal policies they would recommend to correct each of the following: (1) rising unemployment and (2) rising inflation. Explain each

and interest rates. Decreased federal spending and/or increased taxes tend to lower price levels and interest rates, but they reduce employment and output levels in the short run.	recommendation.
n the long run, the interest-rate effects of fiscal policies lead to changes in private investment spending by businesses and individuals that partially, if not entirely, offset the output and employment effects of fiscal policy.	Explain why an additional $2 billion of federal spending on highways, financed by federal government borrowing, can reduce private investment spending in the economy in the long run.
The federal government's annual budget is balanced when its revenues from taxes and user fees equal its expenditures. The government runs a budget deficit when its expenditures exceed its revenues. The government runs a surplus when its revenues exceed its expenditures.	Determine whether the budget is in surplus, in deficit, or is balanced, and whether the effect upon the economy is contractionary, expansionary, or neutral if the government receives $800 billion in taxes and (1) government spending is $800 billion; (2) government spending is $900 billion; (3) government spending is $700 billion.
When the government runs a budget deficit, it must borrow from individuals, corporation, or financial institutions to finance that deficit.	Explain that the federal debt is financed through the sale of government securities and identify the percentage of debt owed to foreigners.
The national debt is the total amount of money the federal government owes. This is the accumulated sum of its annual deficits and surpluses. The government pays interest on the money it borrows to finance the national debt.	Explain the difference between the budget deficit and national debt. Then determine how long it would take to pay off all of the national debt at the current rate of GDP if all GDP were devoted to that purpose.
In the long-run, inflation results from increases in a nation's money supply that exceed increases in its output of goods and services.	Explain why inflation occurs after participating in two rounds of an auction where the number of goods available remains constant, but the money in circulation increases in round two.
Monetary policies are decisions by the Federal Reserve System that lead to changes in the supply of money and the availability of credit. Changes in the money supply can influence overall levels of spending, employment, and prices in the economy by inducing changes in interest rates charged for credit, and by affecting	Write an article for the business section of the local newspaper explaining what monetary policy is and how changes in monetary policy affect the money supply and interest rates. Using this information, advise a teenager about taking out a car loan and his/her opportunities for obtaining summer employment in the construction

the levels of personal and business investment spending.	trade when the Federal Reserve is contracting the money supply.
The major monetary policy tool that the Federal Reserve System uses is open market purchases or sales of government securities. Other policy tools used by the Federal Reserve System include increasing or decreasing the discount rate charged on loans it makes to commercial banks and raising or lowering reserve requirements for commercial banks.	Play the roles of members of the Federal Open Market Committee and decide for each of the headlines below whether they would recommend an expansionary policy or a contractionary policy and whether government securities should be purchased or sold. Newspaper headlines: Unemployment Rate Soars New Housing Starts Rise CPI Rises for Third Consecutive Month