The fiscal and monetary policy and economic fluctuations

Finance

The fiscal and monetary policy and economic fluctuations The fiscal and monetary policy and economic fluctuations The U. S is the world's largest economy with an average 16. 6% of global GDP. It has a mixed economy and has enjoyed uninterrupted economic growth and falling unemployment with a progressive decline in inflation, interest rates and high levels of research and capital investment for the past five years.

The inflation rate has gradually increased from an average value of -0. 2 to 1. 7 for the past five years. This has resulted because of the change in value of goods' production costs and appreciation of the currency (Jaeger, 1999). The rate of unemployment for the past years has also depreciated slowly and steadily, this is as a result of the 10 million jobs created for the last five years.

Interest-rate targets are a vital tool when dealing with variables like inflation and unemployment. Adjustments on the rates are made to keep inflation within a target range so as to ensure economic growth and therefore safeguarding economic momentum. The key reasons for changing interest rates are; to give the economy a short run boost so as to lower interest rates. And to make up for a loss as a result of the interest being subjected to taxation this is achieved by increasing the interest rates

Demand side policies and Supply side policies are two strategies that create economic growth by encouraging people to spend money (Mikek, 2000). These strategies base on fiscal policy that is a general term referring to the federal government tax and spending policies. And monetary policies that refer to the actions of the central bank to achieve macroeconomic objectives like; full employment, stable economic growth and price stability.

Demand side policies basing on fiscal policy decreases unemployment by helping to increase economic growth rate and aggregate demand (Siu, 2004). With a higher level of the demand and a high economic growth, the level of bankruptcy in firms will go down leading to fewer job losses. Nevertheless, demand for workers will increase thereby lowering demand deficient unemployment. Demand side policies play a role in increasing economic growth rate. However, if the economy is already stable, a further increase in AD will cause inflation and therefore increase in interest rates. Demand side policies based on the monetary policy involves cutting interest rates that lead to decrease in the cost of borrowing and also encouraging people to spend and invest. This increases both GDP and AD thereby reducing demand deficient unemployment (Mikek, 2000). Lower interest rates reduce saving incentives, and mortgage interest payments, therefore, increasing consumers' disposable income.

Supply side policies aim to reduce unemployment caused by supply side factors which; gives long-term skills to unemployed to enable them find jobs in developing industries(Siu, 2004). This is accomplished by, Improving geographical mobility by giving tax breaks to firms that are set up in depressed areas, and also providing assistance to unemployed workers moving to areas with high employment.

In conclusion to that, supply-side policies can help reduce inflation by reducing costs and increasing productivity. For example, deregulation and privatization can help reduce costs nevertheless, controlling interest rates is most significant in controlling inflation. However, supply-side policies can take an extended period.

References

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