

# Federal reserve paper

Literature, Russian Literature



Monetary Policy The Federal Reserve System is the Central Bank in the United States abbreviated as FED. The FED has various functions which include managing the money and credit supply in United States. It operates at the centre of the financial system of the United States. The FED also keeps business running in the nation through supply of currency, coins, and services payments such as check clearing and electronic funds transfer (Solow & Taylor, 2008). The paper will look at the U. S Federal Reserves monetary policy in detail addressing various issues. Purpose and function of money Money has three main functions and these are medium of exchange, store of value and unit of account. Money as a medium of exchange means that it can be used to pay for goods and services. Instead of a transaction between goods and other goods, goods can be exchanged for money. As a store of value, money holds a value today and it will hold the same value at a later date in future. Money as a unit of account means that the value of goods as well as services is quoted in a manner that is standard. It allows for a meaningful interpretation of costs, prices and profits hence an entity is able to monitor its performance. Management of a Nation's monetary system by Central Bank The central Bank is in place to implement the monetary policy chosen for a country. It achieves this through establishment of the form of currency the nation may have, whether gold-backed currency, fiat currency, currency union or currency board. When a nation has its own currency in place, the currency has to be standardized by the Central Bank. The Central Bank is in a position to use currency from another country directly in a currency union or indirectly through a currency board. Nations with fiat money, the monetary policies by the Central Bank are used for their

targets in interest rates. The Central Bank is also able to manage the monetary system in a country through activities like interest rates management, set up of reserve requirements, and as a lender of last resort in instances where a bank is undergoing insolvency or in a financial crisis.

Direction of recent monetary policy in the U. S As a result of recession, there is a new direction taken in the monetary policy by the United States. The nation had undergone a deep recession after which a new monetary policy had to be formulated in order for the nation to fully recover and avoid such conditions in future. There are also other economic indications which have impacted the direction of the monetary policy. These indicators include inflation, employment and unemployment, real GDP, and Federal Reserve.

The stated direction of the monetary policy in the United States is towards a monetary policy that will protect the country from inflation, increase the rate of employment, increase the nations GDP The Federal Reserve is important for the continued progress towards a maximum employment and stability of prices. A highly accommodative monetary policy remains the most appropriate tool to achieve all this (Solow & Taylor, 2008). Actions towards the outlined direction of the monetary policy The monetary policy being formulated is in terms of money and credit cost as opposed to their supply. The Federal Reserve conducts monetary policy through focusing on money and credit cost proxied by the interest rates. The particular target is a short term interest rate referred to as federal funds rate. This federal fund rate is determined within private markets particularly for overnight reserves of the depository institutions. Depository institutions calculate the reserves they want to hold against the reserve liabilities they have. Interest rates in the

market are known as federal funds rates, which are used by the FED to conduct the monetary policy. If FED wishes to create an expansion of money and credit, the target will be lowered hence encouraging lending activities and demand in the economy. Conversely incase the FED wishes to reduce money and credit it raises target and removes reserves from depository institutions to accomplish this. These actions lead to economic growth within the United States and reduction of uncertainties (Solow & Taylor, 2008).

Effects of monetary policy The monetary policy plays an important role in the financial and economic decisions made in a nation. This policy affects the economic production within country. Economic growth in a country is achieved through an enhancement in the investment of capital like better machinery. Low interest rates means that organizations and people can loan money for investment. When it comes to repaying the loans they do so with low interest rates. Lowering interest rates through the monetary policy leads to increase in economic growth. On the other hand an increase in the interest rates in high economic growth is used to protect the economy from overheating (Solow & Taylor, 2008). Monetary policy also affects employment in that people are involuntarily unemployed in instances where there is a rise in wage-goods compared to the money-wage. People who are willing to work under current money-wage as well as its aggregate demand would be more compared to employment opportunities available. This leads to a decrease employment since the employment positions are not sufficient for those who are willing to fill them. Reference Solow, R. M & Taylor, J. B. (2008). Inflation, unemployment, and monetary policy. Cambridge, Mass: MIT Press.