Macroeconomics

Introduction The current financial crisis wrecking havoc in the US, just as it is in many other parts of the globe, have raised concerns that pertainto a number of issues, some of which are serious and indeed require policy interventions. One of the serious issues is related with the question of regulating the interest rates in accordance with the trends in the money and capital markets. Hence it is the mission of Federal Reserve Bank (Fed) to keep the economy on a proper and healthy track by controlling and maintaining inflation and employment in a balanced way. When the economy falls into recession or deflation, Fed normally cuts the interest rates and takes suitable policies to maintain the low interest rates. The intention is to give incentive to people and businesses to borrow and spend more and thus to sustain the economy. But when the economy shows the signs of inflation and fast economic growth, Fed will raise the interest rates and keep high interest rates. This will cause the borrowing become costlier and lead to slow spending and economic growth.

The Present Situation

Here the situation needs special attention of policy makers as the economy shows the signs of deflation in some districts and inflationary trends in other districts. The states of New York and San Francisco districts shows the trends of price deflation while all other districts believe that inflation may be at hand. The groups of policy makers as well as media who fear the future outbreak of inflation believe that the Fed's decision to keep interest rates near zero and pump the economy with credits will lead to the spread of inflation in the near future.

But among the policy makers of Fed, a substantial wing believes that the already low rate of inflation will again be slow due to the unsolved real estate problems in majority of the districts. It can be pointed out that dwindling rate of inflation is an evidence of the excess capacity and need to sustain the economy with lower interest rates.

The inflation is always danger, but deflation is more danger. Hence, Fed's decision whether to keep the lower interest rate so as to widen the spending or to increase the interest rate in order to tighten the economy, is a crucial question at this stage. Though there are some trends of inflation Fed will decide to keep the lower interest and loosen the monetary policy.

Continued low rate of inflation has strengthened the hands of officials in Federal Reserve who are in the belief that there should not be tightened monetary policy.

The recent meeting of Fed has decided to follow the lower interest rate as there is no any fear of inflation in the near future.

(http://articles. latimes. com/2010/apr/07/business/la-fi-fed-dissent7-2010apr07).

Hence in this present situation it is better to keep the lower interest rate and raise the short-term interest rate whenever the situation arises. At present inflation cannot be seen as an immediate threat to the economy, instead soft inflation will boost the economy up.

Reference:

1. http://articles. latimes. com/2010/apr/07/business/la-fi-fed-dissent7-2010apr07