

KOFA HIGH SCHOOL SOCIAL SCIENCES DEPARTMENT

AP ECONOMICS

**STUDY GUIDE # 19 - FEDERAL RESERVE AND
MONETARY POLICY**



CHAPTER LEARNING OBJECTIVES

- 1. STUDENTS WILL BE ABLE TO IDENTIFY WHO OWNS THE FEDERAL RESERVE SYSTEM AND ITS STRUCTURE**
- 2. STUDENTS WILL BE ABLE TO DESCRIBE THE STRUCTURE OF THE FEDERAL BOARD OF GOVERNORS AND THE 12 FED DISTRICTS**
- 3. STUDENTS WILL BE ABLE TO DESCRIBE AND EXPLAIN THE ROLES OF THE FEDERAL ADVISORY COUNCIL AND THE FEDERAL OPEN MARKET COMMITTEE**
- 4. STUDENTS WILL BE ABLE TO IDENTIFY AND EXPLAIN THE FUNCTIONS OF THE FEDERAL RESERVE BANK IN SERVING THE GOVERNMENT OF THE UNITED STATES, SERVING AND REGULATING MEMBER BANKS, AND REGULATING THE MONEY SUPPLY**
- 5. STUDENTS WILL BE ABLE TO EXPLAIN THE DIFFERENCE BETWEEN FISCAL AND MONETARY POLICY**
- 6. STUDENTS WILL BE ABLE TO IDENTIFY AND EXPLAIN THE TOOLS FOR MANAGING MONETARY POLICY**
- 7. STUDENTS WILL BE ABLE TO EXPLAIN THE CONCEPT BEHIND THE PHILOSOPHY OF MONETARISM, EASY MONEY POLICIES, AND TIGHT MONEY POLICIES**

STRUCTURE OF THE FEDERAL RESERVE SYSTEM - 5 FACTS :

1.

1.

2.

3.



2.

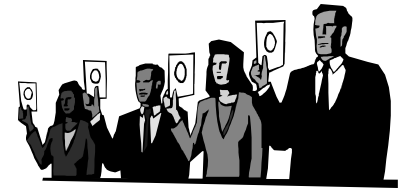
1.

2.

3.

4.

5.



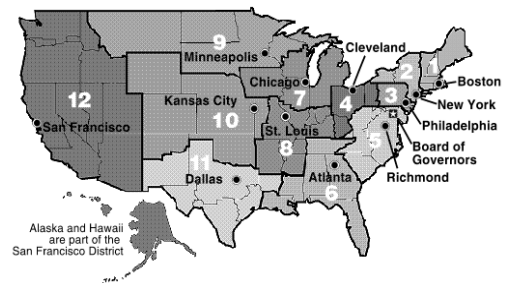
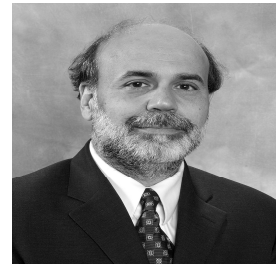
WHO IS CHAIRMAN OF THE FEDERAL RESERVE AND SECRETARY OF THE TREASURY ?

3.

1.

2.

3.



4. **" FEDERAL ADVISORY COUNCIL (FAC) "** -

5. **" FEDERAL OPEN MARKET COMMITTEE (FOMC) "** -

1.

2.

3.



WHAT ARE THE 4 FUNCTIONS OF THE FEDERAL RESERVE SYSTEM ?

1.

1.

2.

3.



2.

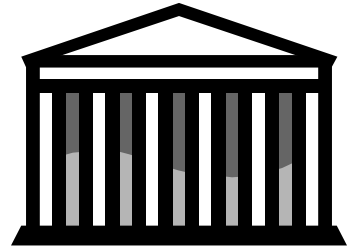
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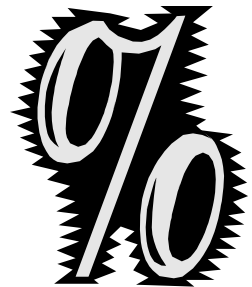
4.

5.



1. “DISCOUNT RATE” -

2. “FUNDS RATE” -



3.

1.

2.

1.

2.

3.

4.

1.

2.

3.

4.



MONETARY POLICY

WHAT IS THE DIFFERENCE BETWEEN FISCAL AND MONETARY POLICY ?

1. **FISCAL POLICY -**

2. “ MONETARY POLICY ” -

WHAT ARE THE 4 TOOLS THE FED HAS FOR MANAGING MONETARY POLICY ?

1.

1.

2.

3.

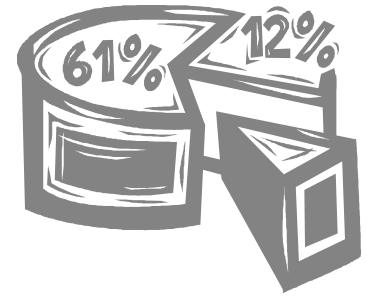
2. “ RESERVE REQUIREMENTS ” -

1.

2.



3.



1. “ PRIME RATE ” -

2.

WHY DOES THE FED LIKE TO USE THE DISCOUNT RATE AS A MONETARY TOOL RATHER THAN THE RESERVE REQUIREMENT ?

4. “ OPEN MARKET OPERATIONS ” -



1.

2.



WHY DOES THE FED LIKE TO USE THE OPEN MARKET OPERATIONS TOOL THE MOST ?

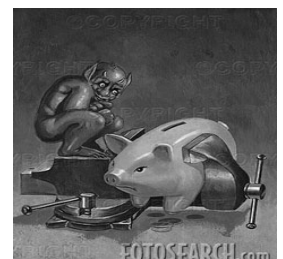
WHAT ARE THE 3 FUNDAMENTAL BELIEFS OF MONETARY POLICY ?

1. “ MONETARISM ” -

2. “ EXPANSIONARY MONEY POLICY ” -

WHY IT WOULD BE USED ?

3. “ CONTRACTIONARY MONEY POLICY ” -



WHY IT WOULD BE USED ?

SUCCESS IN COORDINATION MONETARY AND FISCAL POLICIES IS A MATTER OF TIMING > KNOWING WHEN AND HOW TO ACT > THERE ARE 3 THINGS TO CONSIDER :

1. “ INSIDE LAGS ” -

1.

2.

2. “ OUTSIDE LAGS ” -

3.

ILLUSTRATING THE IMPACT OF THE MONEY SUPPLY ON AGGREGATE SUPPLY AND DEMAND

THE MONEY MARKET CHART

THIS CHART IS USED FOR TWO THINGS :

1.

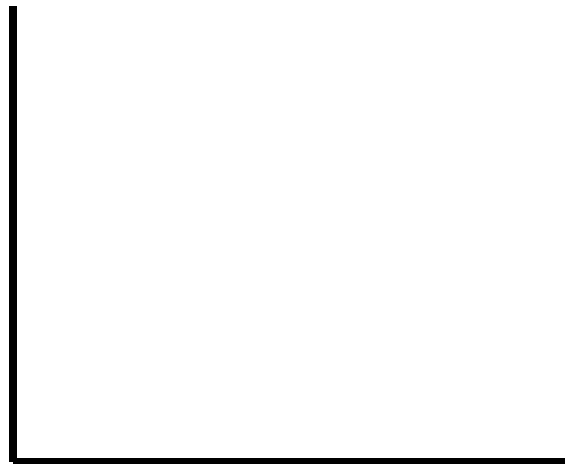
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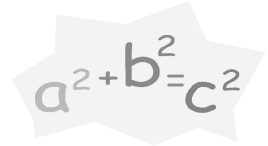
3.

THREE IMPORTANT NOTES ABOUT THE “ RESERVE REQUIREMENT ” :

1.

2.

3. **IT DRIVES THE “ MONEY MULTIPLIER ” -**



1.

2.

3.

MONETARY POLICY EXAMPLES :

RESERVE RATE REDUCTION TO SPEED UP THE ECONOMY :



DISCOUNT RATE REDUCTION TO SPEED UP THE ECONOMY



OPEN MARKET OPERATIONS TO SPEED UP THE ECONOMY



THE EFFECT THE ↓RR, ↓DR, AND / OR THE PURCHASE OF BONDS WOULD HAVE ON DEMAND AND THEREFORE GDP



CAUTION ! BE ABLE TO RECOGNIZE THE SUBTLE DIFFERENCE BETWEEN AN “INCREASE ” IN THE MONEY SUPPLY , VERSUS THE “TOTAL ” MONEY SUPPLY EXAMPLE :

WHAT HAPPENS WHEN A LARGE FOREIGN DEPOSITOR COMES INTO THE COUNTRY ?

BE ABLE TO DISTINGUISH BETWEEN THE MONEY SUPPLY AND MONEY STOCK :

M1

M2

M3

ILLUSTRATING EFFECTS OF COMBINED FISCAL AND MONETARY POLICY ON INTEREST RATES

AS GOVERNMENT



THE "FLIP" SIDE OF THE COIN IS



THE LONG TERM EFFECTS ARE REFLECTED IN THE LOANABLE FUNDS MARKET :



AP EXAM TIP !!!!

WHEN

WHEN

THE FEDERAL RESERVE WILL LIKELY



**HOWEVER , NOTE THAT ANY HIGHER INTEREST RATES WILL CAUSE THE
“ CROWDING OUT EFFECT ” -**



ADVANCED CONCEPTS RELATING TO MONETARY TOPICS

“ MONETARY NEUTRALITY ” -

A DEBATABLE

TO UNDERSTAND

“ NOMINAL VARIABLE ” -

“ REAL VARIABLE ” -

THE KEY TO

NOMINAL VARIABLES ARE

REAL VARIABLES ARE

THE FISHER EFFECT

FIRST , IT IS A FACT

SECOND , BASED ON THE

THIRD , THE “ FISHER EFFECT ” -