

## Homework 5 - Economics 105

Due in class 12/5/03

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At its meeting the end of October, the Federal Reserve FOMC decided not to change interest rates, keeping them at their lowest level for 45 years. However, in his comments, Fed Chairman Greenspan failed to repeat his statement from recent months, that he was “committed to keeping interest rates low for a considerable period.” Some analysts speculate that the Federal Reserve may be beginning to worry more about inflation again, and that the trend over the last 2 years of easing monetary policy will soon come to an end.

Write a short essay (around 500-700 words) arguing whether you think monetary policy should remain loose or begin to tighten. In other words, do you think inflation or unemployment is likely to be the bigger problem for the U.S. economy over the next 6 months to a year. The objective is to apply the analytical tools we have learned in this class to a current policy issue (IS-LM, AS-AD, Phillips curve), and to appreciate the difficulties of policy making (as discussed in chapter 14). You are required to use and cite at least two of the five sources from the list below. The essay must be typewritten, not handwritten.

- 1) First gather some economic statistics for the U.S. over the last year or two. In particular, get data on at least 6 of the following 9 statistics: GDP growth rate, unemployment rate, short-term interest rates (such as 3-month treasury bill rate), inflation rate in the consumer price index, rise in labor costs, labor productivity, growth rate in money (M1), private saving rate and consumer confidence.
  - 2) How could you explain the statistics above in terms of our theories? In particular, which curves have been shifting and what types of shocks have been shifting them?
  - 3) Given that current Federal Reserve actions start to have an effect only 6 months in the future, do you think it should be more concerned about inflation or unemployment?
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### Sources:

- 1) Government Agencies: For current data you could check the websites of the government agencies that collect the statistics. For GDP and related statistics, check the Bureau of Economic Analysis at <http://www.bea.doc.gov>. For inflation and employment statistics, check the Bureau of Labor Statistics at <http://www.bls.gov>.
- 2) You might also read the Federal Reserve's own Beige Book for October or November, which describes the Fed's view of economic conditions:  
<http://www.federalreserve.gov/fomc/beigebook/2003/20031015/default.htm>

The newspapers below are available electronically through:

<http://web.lexis-nexis.com/universe>, accessible via computers on campus.

- 3) Financial Times: British financial newspaper.
- 4) Wall Street Journal
- 5) New York Times