Econ 522

September 20, 2017

Money Supply & Inflation

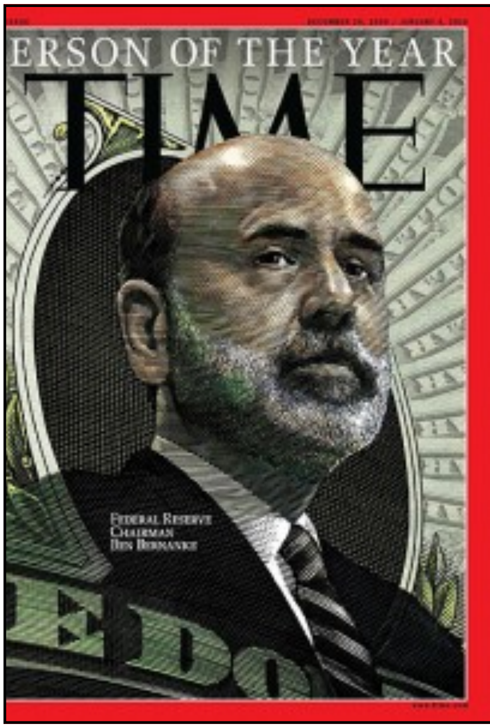
A Question

Expansionary Monetary Policy

- Following the Great Recession, the Fed has maintained strongly expansionary monetary policy (i.e., increasing money supply).
  - Low (basically zero real) interest rates
  - Bond / asset purchases & repurchases
  - Large excess reserves (balances unconstrained by required reserve ratios, having the potential to be loaned out)

Inflation Threat

- In Chapter 5, we learned that in our long run model, increasing money supply growth in excess of output growth leads to inflation.
- Thus far, inflation has remained low and largely below the Fed's target, but with expansionary monetary policy, there's a possibility of inflation.



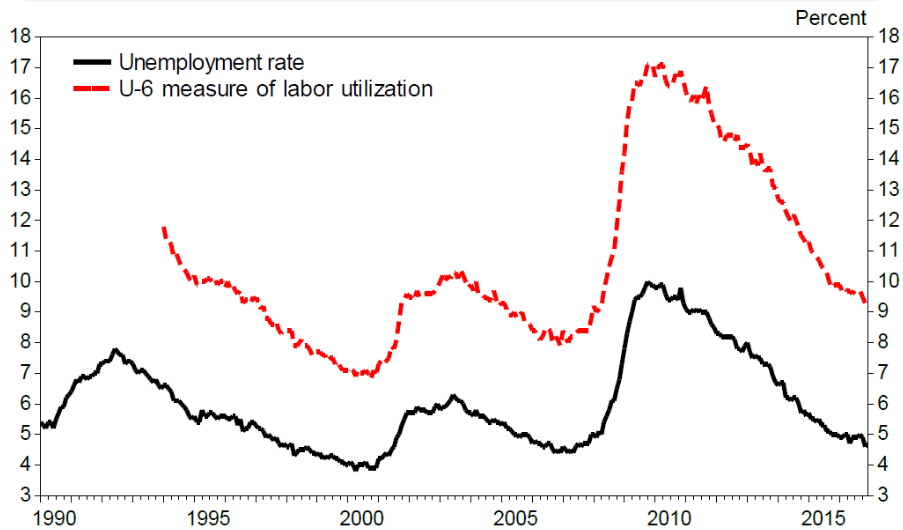
The Question:

Why do this?

Is there a reason the Fed may have been willing to risk potential inflation (less price stability)? Or an alternative policy goal that was being pursued? A more pressing concern?

Is it a policy goal that fits well in the classical model we have studied thus far (Chapters 3-5)? Which variables would be implicated?

Figure 1
Labor Utilization



Source: Bureau of Labor Statistics

January 19, 2017 Board of Governors of the Federal Reserve System 1