

Story 2 : Can the FED Control Inflation and Maintain Full Employment

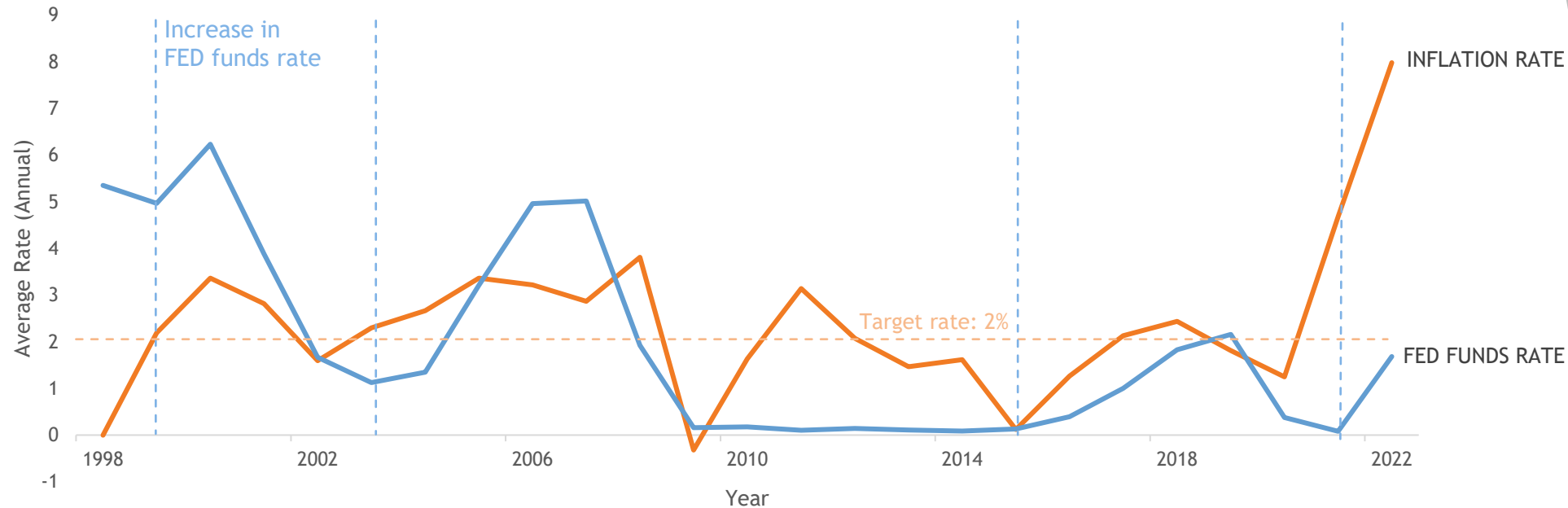
By: Shoshana Farber

Objective:

- ▶ The Federal Reserve's mandate from Congress is to control inflation and to maintain low unemployment. These seem to be contradictory objectives.
- ▶ Has the FED been able to fulfill the mandate given to it by Congress?

Federal Funds vs. Inflation (1998-2022)

The Federal Reserve adjusts the FED funds rate based on rising inflation

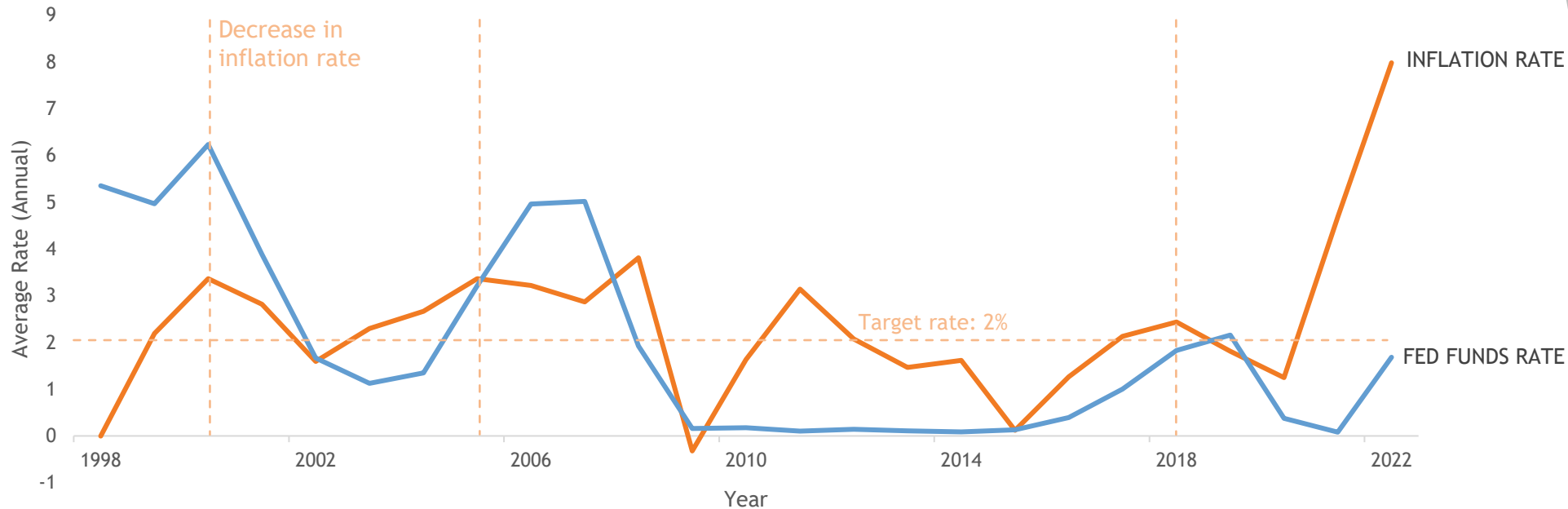


- ▶ Increases in FED funds rates typically lag behind increases in inflation as the Federal Reserve increases interest rates to battle rising inflation
- ▶ The Federal Reserve strives to maintain an inflation rate of about 2%*

*Based on the Federal Reserve's FOMC statement as of September 20th, 2023 ([link](#))

Federal Funds vs. Inflation (1998-2022)

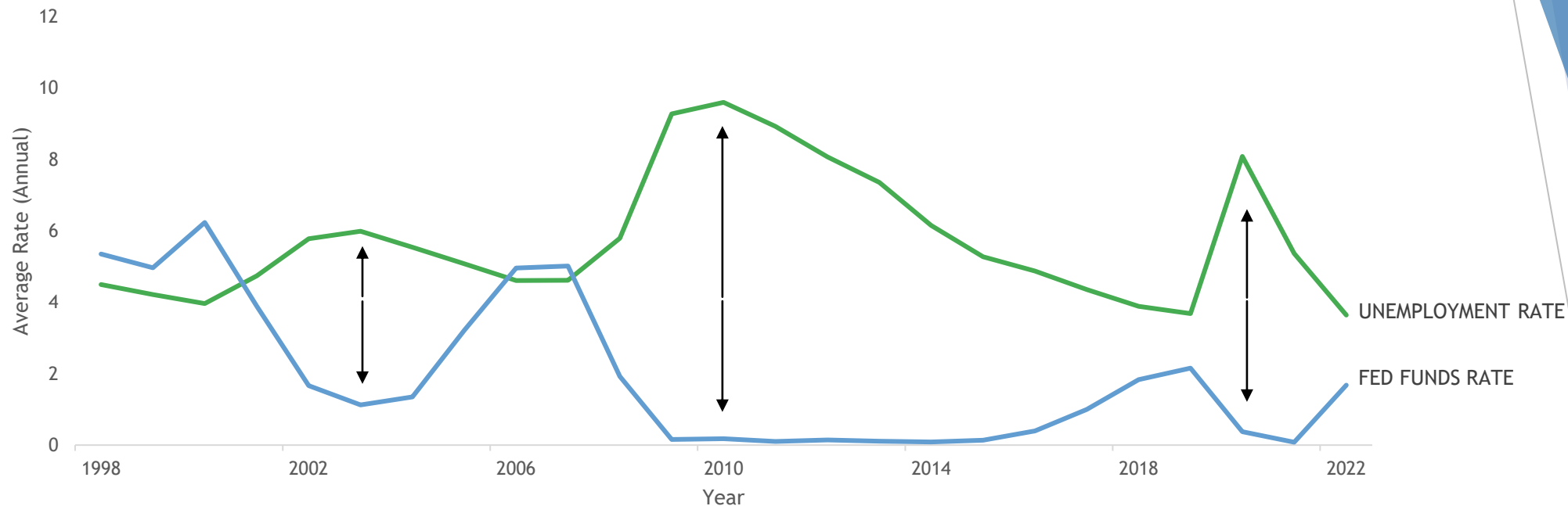
Inflation rates respond to increases in FED funds rate



- ▶ Increased federal interest rates discourage borrowing and slow down economic growth which leads to less inflationary pressure
- ▶ For the most part, inflation rates have been centered around the FED's target rate of 2%

Federal Funds vs. Unemployment (1998-2022)

The FED funds rate moves to counteract high unemployment

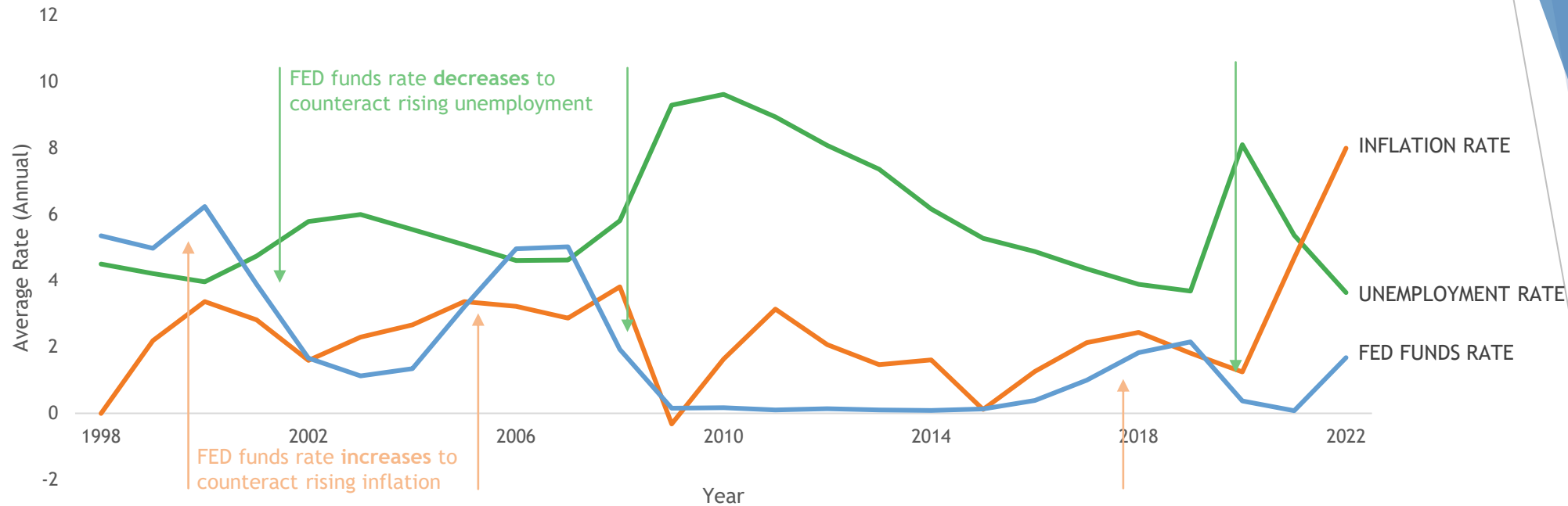


- ▶ The Federal Reserve attempts to counteract high unemployment rates by decreasing interest rates which encourages borrowing thereby stimulating the economy and leading to increased hiring*

*It is important to note that unemployment is influenced by various factors beyond monetary policy, such as technological advancement, demographics, global economic conditions, and structural aspects of the labor market

The Federal Reserve's Mandate: A Balancing Act

The FED tries to battle rising inflation and unemployment simultaneously



- The Federal Reserve has been given a difficult job by Congress, as they must attempt to address rising inflation and rising unemployment rates at the same time

Has the FED been able to fulfill the mandate given to it by Congress?

- ▶ The Federal Reserve has generally been successful in maintaining their target inflation rate of about 2% by raising interest rates in reaction to rises in inflation rates.
- ▶ The inverse relationship between unemployment rates and FED funds rates indicates that the Federal Reserve is using monetary policy to influence unemployment rates.
- ▶ The Federal Reserve's mandate is an extremely hard one and requires many trade-offs. Increases in interest rates to curb rising inflation can also result in less economic growth and fewer job opportunities. Conversely, decreases in interest rates to accommodate for greater job growth lend to greater stimulus of the economy and increases in inflationary pressure.

Data Sources:

- ▶ The Consumer Price Index (CPI) (Bureau of Labor Statistics)
- ▶ The FED Funds Rate (FRED) (Federal Reserve Board)
- ▶ Unemployment Rate (Bureau of Labor Statistics)