Lesson 10: Macro Policy w/ AD/AS

Contents

1 Two Objectives

1. Stabilizing Economic Activity (Y -> y^p)
2. Low and Stable Inflation (π -> π^T)

1.1 Stabilizing Economic Activity (Fed and Governement)

How do we aim to stabilize economic activity? We want to aim for maximum employment also known as the natural rate of unemployment. This is done both throught monetary and fiscal policy. Monetary policy (MP) changes $\Delta \bar{r}$ and fiscal policy changes taxes (ΔT) and government spending (ΔG).

1.2 Low and Stable Inflation

To achieve low and stable inflation the fed aims for an inflation target π^T. The Fed wants to achieve this goal, because higher inflation and higher variation in inflation leads to difficult planning for business and decreases the growth rate of the economy (g_y).

2 Central Bank Mandates

There are two types of Mandates:

1. Dual Mandate
2. Hierarchial Mandate

2.1 Dual Mandate

In a dual mandate, each objective is equally important.

1. Maximum employment ($u = u_n$).
   - Those who prioritize this are called doves.
2. Price Stability ($\pi = \pi^T$)
   - Those who prioritize this are called hawks.

2.2   Hierarchial Mandate

In this type of mandate the central bank is required to focus on price stability above all other mandates.
(ECB, BOC, BOE, RB of NZ)