PFL Academy

Chapter 53: Fiscal and Monetary Policy

Student Activity Packet

THE CHALLENGE

In 2008, the stock market crashed 40%, major banks failed, and unemployment doubled to 10%. The Federal Reserve cut interest rates to nearly 0% and bought $4 trillion in bonds. Congress passed $1.5 trillion in stimulus and bailouts. In 2022, inflation hit 8.5%—the highest in 40 years. The Fed raised rates from 0% to 5.5%, and Congress debated whether to spend less.

How do these policies affect YOUR ability to buy a home, find a job, or save for the future? When do they help you, and when do they hurt?

Learning Objectives

- Explain fiscal policy tools: government spending, taxation, and budget deficits.
- Explain monetary policy tools: Federal Reserve interest rates and money supply.
- Analyze how these policies affect employment, inflation, and your personal finances.
- Evaluate trade-offs between fighting recession and controlling inflation.

CORE CONCEPTS

Term	Definition
Fiscal Policy	Government's use of spending and taxation to influence the economy (controlled by Congress).
Monetary Policy	Federal Reserve's management of interest rates and money supply to influence the economy.
Federal Funds Rate	Interest rate banks charge each other; influences all other rates (mortgages, car loans, credit cards).
Expansionary Policy	Stimulating the economy: increase spending, cut taxes, or lower interest rates (used in recession).
Contractionary Policy	Cooling the economy: decrease spending, raise taxes, or raise interest rates (used against inflation).

Background: The economy naturally cycles through expansion and recession. Government uses **fiscal policy** (spending/taxes) and **monetary policy** (interest rates) to smooth these cycles. During recessions, stimulating policies create jobs but may cause inflation and debt. During high inflation, cooling policies reduce prices but may cause unemployment. Understanding these trade-offs helps you make better financial decisions and evaluate policy proposals.

APPLY IT

PART A: POLICY RESPONSE ANALYSIS

For each economic situation, identify the appropriate policy response.

Scenario 1: Deep Recession

Unemployment: 9.5%, Inflation: 1.2%, GDP Growth: -3.0%. Businesses are closing, consumer confidence is collapsing, and your state's unemployment rate is at 11%.

Fiscal Policy: ________________________ (expansionary / contractionary / neutral)

Monetary Policy: ________________________ (expansionary / contractionary / neutral)

Specific Actions: ____

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Scenario 2: High Inflation

Unemployment: 3.5%, Inflation: 8.0%, GDP Growth: 4.5%. Prices are rising rapidly, workers are demanding higher wages, and your savings are losing purchasing power.

Fiscal Policy: ________________________ (expansionary / contractionary / neutral)

Monetary Policy: ________________________ (expansionary / contractionary / neutral)

Specific Actions: ____

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Scenario 3: Stable Economy

Unemployment: 4.2%, Inflation: 2.0%, GDP Growth: 2.5%. Economy is healthy and balanced. No significant concerns.

Fiscal Policy: ________________________ (expansionary / contractionary / neutral)

Monetary Policy: ________________________ (expansionary / contractionary / neutral)

Why maintain? ____

Hint: *Expansionary = stimulate economy (lower rates, increase spending). Contractionary = cool economy (raise rates, reduce spending).*

PART B: INTEREST RATES AND PERSONAL FINANCES

Calculate how interest rate changes affect your major financial decisions.

Purchase	Low Rates (3%)	High Rates (7%)	Monthly Difference
$300,000 Mortgage (30 yr)	$1,265/mo	$1,996/mo	
$25,000 Car Loan (5 yr)	$449/mo	$495/mo	
$10,000 Savings (annual interest)	$300/yr	$700/yr	

4. If you're buying a home, would you prefer high or low interest rates? How much would you save monthly at 3% vs. 7%?

5. If you're a saver with $10,000 in savings, would you prefer high or low rates? How much more would you earn at 7% vs. 3%?

6. As a young person, are you more likely to be a net borrower or net saver? How does this affect whether high rates help or hurt you?

PART C: POLICY TRADE-OFFS

7. The 2020 COVID stimulus sent $2,000 checks to most Americans. Analyze this policy:

Benefits	Costs

Worth it? ______________________ (Yes / No / Partially)

8. The Fed raised rates from 0% to 5.5% in 2022-2023 to fight inflation. Who benefits and who is harmed by this decision?

CHECK YOUR UNDERSTANDING

1. The Federal Reserve primarily controls the economy by adjusting:

- ☐ A. Tax rates
- ☐ B. Government spending
- ☐ C. Interest rates
- ☐ D. Minimum wage

2. Explain why the Fed might raise interest rates even though it makes borrowing more expensive for families.

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3. Calculation: During a recession, Congress passes a $500 billion infrastructure bill. If the spending multiplier is 1.5, what is the total impact on GDP?

Show your work:

Answer: $____________ billion total GDP impact

4. Why might expansionary fiscal and monetary policy during a recession lead to inflation later?

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5. Reflection: You're planning to buy your first home in 3 years. How does knowing about monetary policy help you time this purchase? What would you watch for?

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