CAN THE FED CONTROL INFLATION AND MAINTAIN FULL EMPLOYMENT?

Story 2

Data 608

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HAS THE FED FULFILLED ITS DUAL MANDATE?

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The Federal Reserve's **dual mandate** from Congress is to control inflation and to maintain low unemployment.

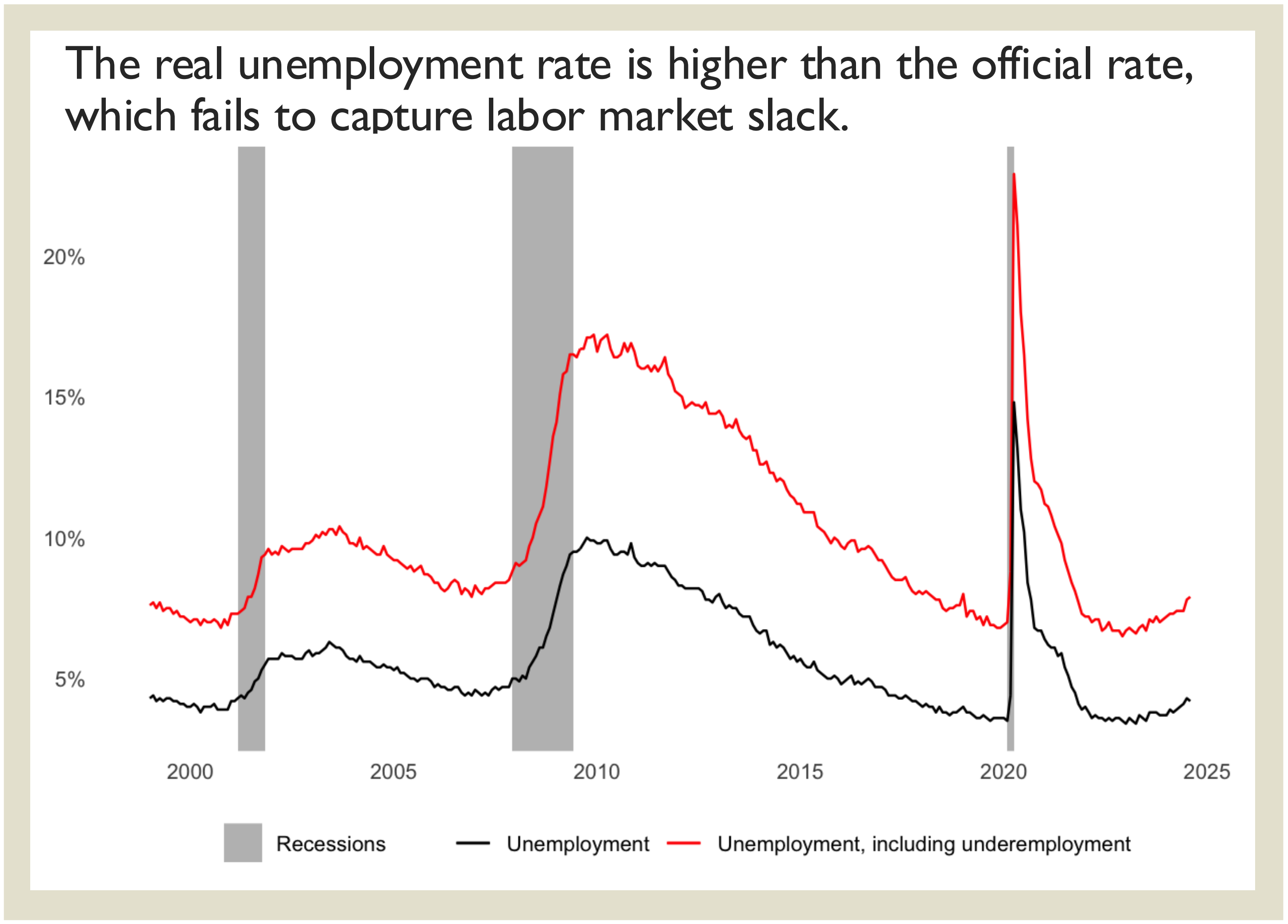
The **federal funds rate** is the average interest rates at which banks trade federal funds with each other.

The Fed can **raise interest rates** to slow the economy and **bring inflation down**.

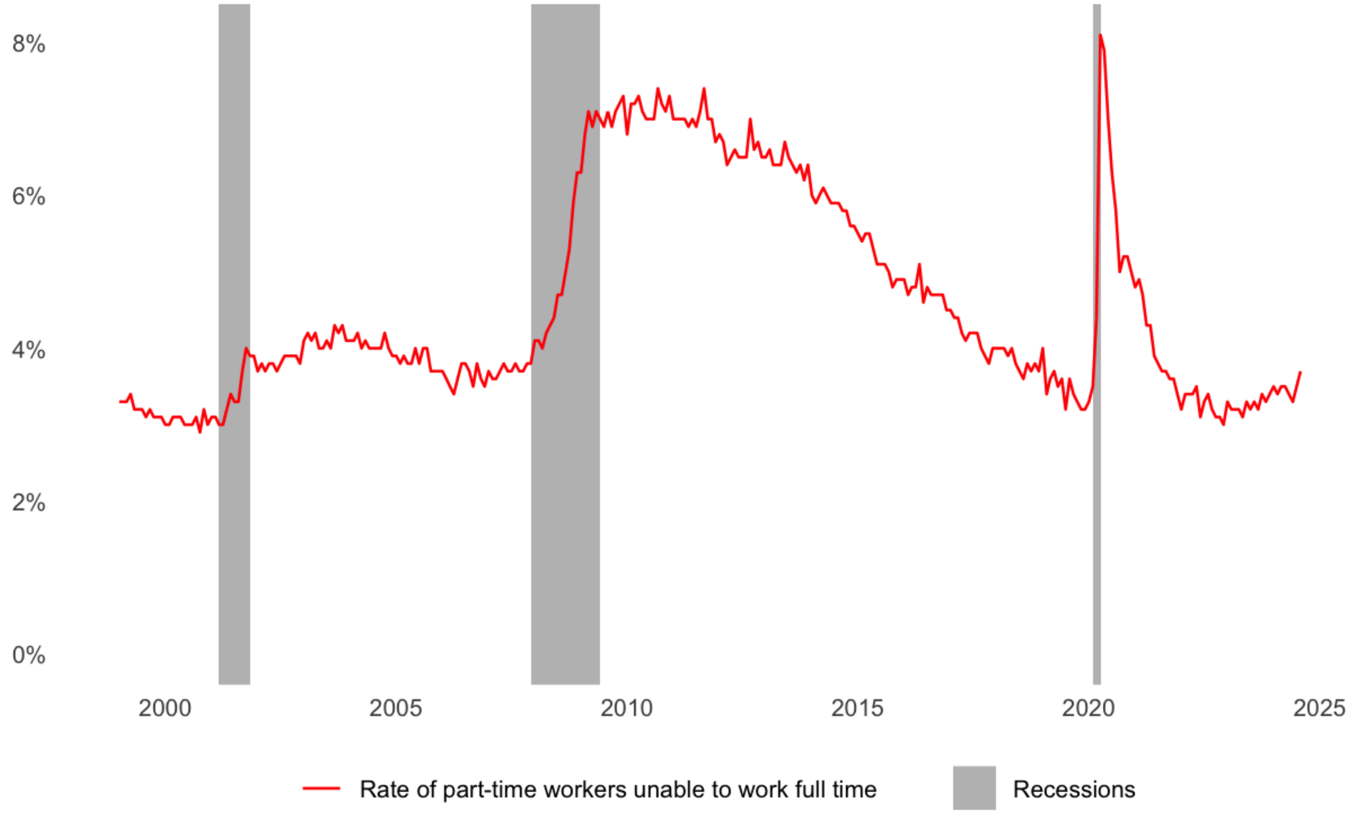
The Fed can **lower interest rates** to make it cheaper for businesses to borrow money, which can **lead to more hiring** and higher wages.

This broader employment measure, U6, includes the underutilized **part-time workers who would prefer to work full time**, as well as **individuals who are too discouraged to try to find work**.

The Fed **does not take underemployment into account** when adjusting the Federal Funds Rate.

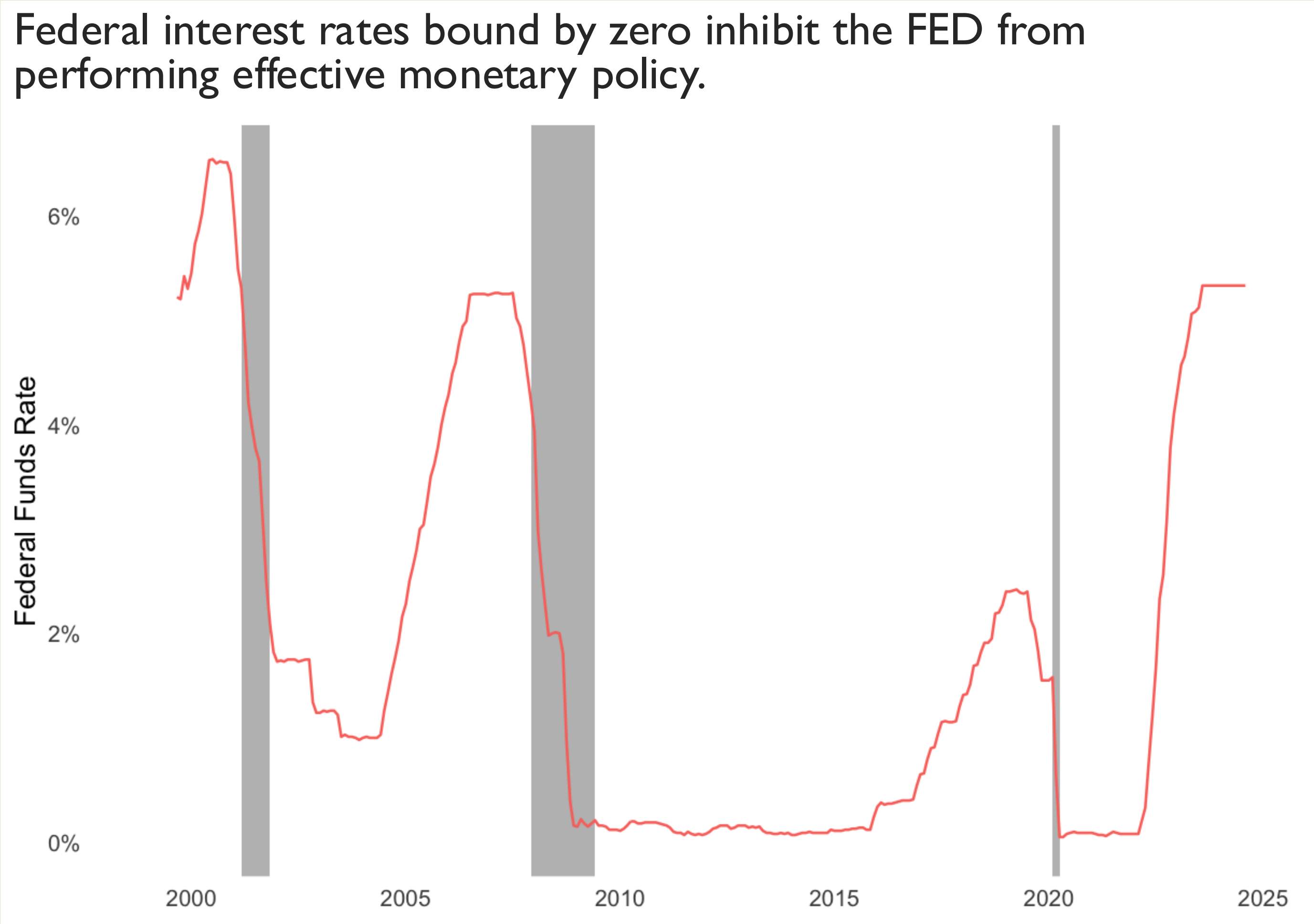


The FED was unable to keep underemployment low, especially after the Great Recession.

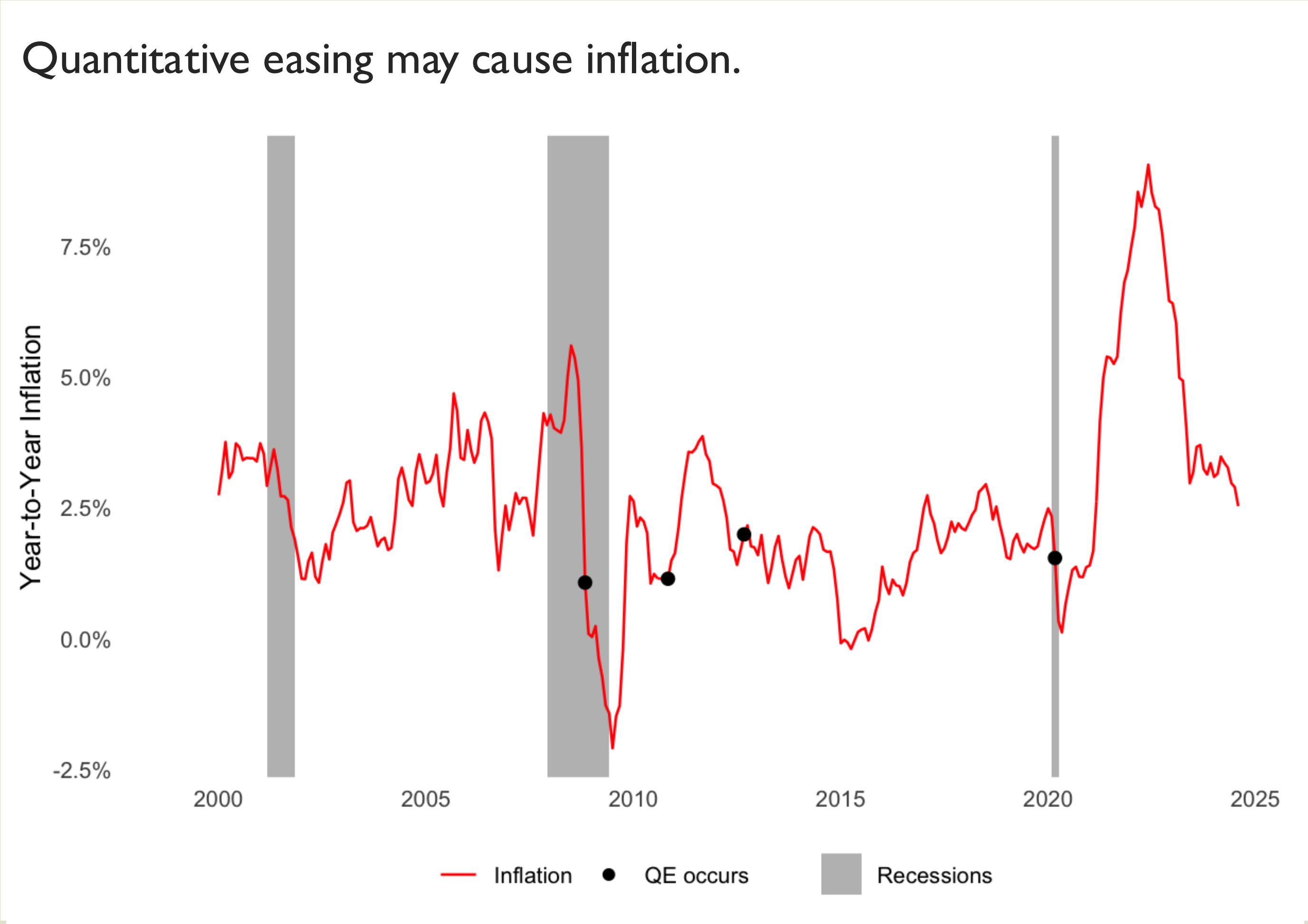


Underemployment spiked during recessions and remained elevated long after (breached pre-crisis level of 4% at the end of 2017).

Could the FED have lowered rates further to combat unemployment?



- No, the Fed could not have lowered interest rates further to combat persistent unemployment and underemployment.
  - Monetary policy becomes ineffective in stimulating the economy when rates approach zero (a **liquidity trap**).
- The Fed raised rates in 2015 before underemployment had fully recovered.



- **Quantitative easing (QE)** is a novel monetary policy tool.
- With rates already low, the Fed injected trillions into the economy by buying assets.
- QE mainly inflated asset prices as banks invested in the stock market.

CONCLUSION

No, the FED has fulfilled its dual mandate.

- It was unable to keep unemployment low and neglected persistent underemployment when deciding to raise rates again.
- When federal interest rates were already low, injecting money into the economy using QE caused inflation without significantly reducing unemployment.

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