Types of Monetary Policy

#1-Expansionary Monetary Policy:

The expansionary monetary policy is adopted when the economy is in a recession, and the unemployment is the problem. The expansion policy is undertaken with an aim to increase the aggregate demand by cutting the interest rates and increasing the supply of money in the economy. The money supply can be increased by buying the government bonds, lowering the interest rates and the reserve ratio. By doing so, the consumer spending increases, the private sector borrowings increases, unemployment reduces and the overall economy grows. Expansionary policy is also called as "easy monetary policy".

#2 – Contractionary Monetary Policy:

The contractionary monetary policy is one of the most used monetary policies because it helps reduce the inflation rate. Contractionary monetary policy is taken by the authorities when the inflation rate is sky-high and the central bank needs to do something immediately. The main tools of this policy are interest rates and security options. When the central bank adopts a contractionary monetary policy, it tries to raise the interest rates of the bank so the people keep their money in banks to avail of higher interest rates. This will result in less money in the hands of people and as a result, the inflation rate will reduce. Secondly, the central bank also sells off securities in the open market so that the public would be more interested to buy more securities which will result in the same i.e. lowering the inflation rate.

Thus, these are the monetary policies applied by the monetary authority to control the inflationary or recessionary pressures in the economy.