Who Steers Money?

Compare central banks through two bakeries' decisions

GE.5.1 "Explain the role of the Federal Reserve in the U.S. economy, as well as the functions of its counterparts in other countries."

NAME _____ DATE _____

1 READ AND MARK

Read it twice

YOUR JOB Underline how the Fed can affect borrowing, circle two other Fed jobs, and draw a line from each named central bank to the place or currency it serves to compare their roles.

An Oven, a Loan, and a Central Bank

1. Imagine a bakery in Ohio deciding whether to borrow for a new oven. The Federal Reserve, or Fed, does not set the bakery's loan rate. Instead, its Federal Open Market Committee sets a target range for the federal funds rate, the rate banks charge each other for overnight loans. The Fed uses tools such as interest paid on bank reserves to help keep that rate in its target range. Changes in borrowing costs can affect spending, jobs, and prices. The Fed aims for maximum employment and stable prices, so its decisions reach far beyond banks.

2. The Fed also supervises certain banks to check whether they manage risks and follow banking rules. It runs payment systems that help banks move money, including payments businesses make to suppliers. When eligible banks face a sudden shortage of cash, the Fed can provide short-term loans against acceptable collateral. These jobs matter even when the Fed does not change its interest-rate target: safe banks and reliable payments help people use money with confidence. The Fed is not Congress. Congress and the president make federal tax and spending decisions, while the Fed carries out monetary policy.

3. Now consider a bakery in France and one in Britain. France uses the euro, so the European Central Bank, or ECB, sets policy interest rates for the euro area rather than for France alone. It works with national central banks and directly supervises significant banks in participating countries. Britain uses the pound. The Bank of England sets its own policy rate for the United Kingdom and helps keep its financial system stable. Its Prudential Regulation Authority, which is part of the Bank, supervises banks and other firms. All three central banks influence borrowing and support financial stability, but their currencies and jurisdictions differ.

2 ANSWER WITH EVIDENCE

Use the passage

1. How could a Fed decision about the federal funds rate affect the Ohio bakery's oven purchase, even though the Fed does not set the bakery's loan rate?

2. Explain how two Fed jobs other than setting an interest-rate target help the U.S. economy.

3. How do the areas served by the ECB and the Bank of England differ, and what monetary-policy decision does each make?

4. Compare the Fed's and the ECB's roles in bank supervision. How does this work differ from setting interest rates?

3 YOUR TURN

Your own words

Prices are rising as a U.S. bakery and a French bakery each plan to borrow for a new oven. Write an advisory note explaining a possible rate decision by each bakery's central bank, how those decisions could affect the bakeries, and why the banks serve different areas; then explain one separate Fed function that could help if bank payments were delayed.

Who Steers Money?

PART 1 · READ AND MARK

Underline how the Fed can affect borrowing, circle two other Fed jobs, and draw a line from each named central bank to the place or currency it serves to compare their roles. Accept any marking that follows this job and points at the right text.

PART 2 · ANSWERS

#	QUESTION	ANSWER
1	How could a Fed decision about the federal funds rate affect the Ohio bakery's oven purchase, even though the Fed does not set the bakery's loan rate?	**A change in the Fed's target can affect borrowing costs. If the bakery's loan becomes more expensive, it might delay buying the oven.**
2	Explain how two Fed jobs other than setting an interest-rate target help the U.S. economy.	**Supervising certain banks helps them manage risks and follow rules. Running payment systems helps banks move money reliably. Also accept short-term lending to eligible banks facing a cash shortage.**
3	How do the areas served by the ECB and the Bank of England differ, and what monetary-policy decision does each make?	**The ECB sets policy interest rates for the euro area, which includes France. The Bank of England sets its policy rate for the United Kingdom.**
4	Compare the Fed's and the ECB's roles in bank supervision. How does this work differ from setting interest rates?	**The Fed supervises certain banks, while the ECB directly supervises significant banks in participating countries. Supervision checks banks rather than changing a policy rate to influence borrowing.**

PART 3 · YOUR TURN (SAMPLE ANSWER)

The Fed could raise its target range for the federal funds rate, and the ECB could raise its policy interest rates. If loans become more expensive, both bakeries might delay buying ovens, which could ease pressure on prices. The Fed serves the United States, while the ECB serves the euro area, including France. If bank payments were delayed, the Fed's payment systems could help U.S. banks move money reliably.

Accept other well-supported descriptions of how higher borrowing costs might affect a bakery. Rate changes influence loan costs but do not determine a particular bakery's loan rate.