Two Policy Paths

Compare who acts, what changes, and why it matters.

GE.5.2 "Differentiate between monetary policy and fiscal policies."

NAME _____ DATE _____

1 READ AND MARK

Read it twice

YOUR JOB In paragraphs 2 and 3, underline each policy action. Write F beside an action you think is fiscal policy or M beside an action you think is monetary policy.

A Shipping Town and Two Policy Paths

1 When the economy slows or prices rise too quickly, leaders have more than one way to respond. Fiscal policy changes the federal government's taxes or spending. Congress passes tax and spending laws, and the president signs or vetoes them. Monetary policy works through the nation's money and credit conditions. The Federal Reserve, often called the Fed, makes these decisions independently of Congress's day-to-day votes. Its tools include changing a key short-term interest rate and buying or selling government securities. Both kinds of policy can affect jobs and prices, but they use different decision makers and different tools.

2 Imagine a shipping town where many residents have lost work because fewer goods are moving through its port. Lawmakers approve federal money to repair aging docks, and the president signs the bill. Contractors hire workers, and those workers may spend their pay at nearby businesses. In another year, Congress passes a temporary reduction in federal payroll taxes, which the president signs. Workers then keep more of each paycheck, while federal tax revenue falls. Neither choice guarantees a certain number of new jobs. To identify the kind of policy, focus on who made the choice and what changed.

3 Now picture two decisions made at different times by the Fed. When prices are climbing rapidly, Fed officials raise their key short-term interest rate. Borrowing often becomes more expensive, which can cool spending, though the effects take time. Later, during a downturn, the Fed buys government securities from financial institutions. This purchase adds funds to the banking system and can put downward pressure on interest rates, encouraging borrowing. These moves do not require Congress to pass a new tax or spending law. Look at the tool and decision maker, not just the hoped-for effect on the economy.

2 ANSWER WITH EVIDENCE

Use the passage

1. How do the dock repair decision and the Fed's rate increase differ in policy type and tool?

2. How do the payroll tax reduction and the Fed's securities purchase differ in policy type and tool?

3. The dock repairs and payroll tax reduction use different tools. Why are both the same kind of policy?

4. The Fed raises a rate in one situation and buys securities in another. Why are both the same kind of policy?

3 YOUR TURN

Your own words

Your region has rising unemployment. Write a brief advice note proposing one federal fiscal action and one Fed monetary action. Name who would make each decision, explain how each could affect employment, and state one key difference between the actions.

ANSWER KEY

Two Policy Paths

PART 1 · READ AND MARK

In paragraphs 2 and 3, underline each policy action. Write F beside an action you think is fiscal policy or M beside an action you think is monetary policy. Accept any marking that follows this job and points at the right text.

PART 2 · ANSWERS

#	QUESTION	ANSWER
1	How do the dock repair decision and the Fed's rate increase differ in policy type and tool?	**The dock repairs are fiscal policy because they change federal spending through a law. The rate increase is monetary policy because the Fed changes a key interest rate.**
2	How do the payroll tax reduction and the Fed's securities purchase differ in policy type and tool?	**The payroll tax reduction is fiscal policy because it changes federal taxes. The securities purchase is monetary policy because the Fed uses a transaction to affect funds in the banking system and interest rates.**
3	The dock repairs and payroll tax reduction use different tools. Why are both the same kind of policy?	**Both are fiscal policy: one changes federal spending, and the other changes federal taxes through laws passed by Congress and signed by the president.**
4	The Fed raises a rate in one situation and buys securities in another. Why are both the same kind of policy?	**Both are monetary policy because the Fed makes the decisions to influence money and credit conditions, rather than changing federal taxes or spending.**

PART 3 · YOUR TURN (SAMPLE ANSWER)

Congress could pass a temporary increase in federal funding for job training, and the president could sign it. The spending could pay instructors and help unemployed workers qualify for openings. The Fed could lower its key short-term interest rate, which might make business loans cheaper and support hiring. The first action changes federal spending through a law; the second changes credit conditions through a Fed decision.

Accept other plausible federal tax or spending changes and Fed actions if the student identifies the correct decision maker and explains a possible effect on employment. For the marking job, students should label the dock repairs and payroll tax reduction F, and the rate increase and securities purchase M.