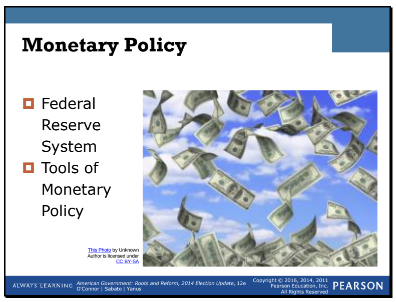
Slide 1

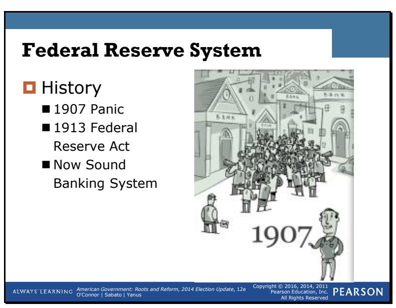
The Federal Reserve and U. S. monetary policy aren't always understood by the general public, but their effects can be felt by everyone with a credit card, savings account, with a stock portfolio, a car loan, or a house loan.

Slide 2



Economic stability isn't just about fiscal policy. Monetary policy helps stabilize the economy by regulating the nation's supply of money and influencing interest rates. Most monetary policy is handled by the Federal Reserve System, or the Fed, as it's known. In this section we will talk about the Fed and the tools it uses in regulating the money supply.

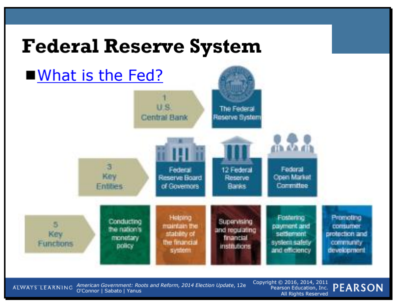
Slide 3



Before the Federal Reserve was founded, the nation was plagued with financial crises. At times, these crises led to "panics" in which people raced to their banks to withdraw their deposits. The failure of one bank often had a domino effect, in which customers of other banks rushed to withdraw funds from their own banks even if those banks were not in danger of failing. Banks needed a source of emergency reserves to prevent the panics and resulting runs from driving them out of business.

A particularly severe panic in 1907 resulted in bank runs that wreaked havoc on the fragile banking system and ultimately led Congress in 1913 to write the Federal Reserve Act. The Federal Reserve System, initially created to address these banking panics, is now charged with several broader responsibilities, including fostering a sound banking system and a healthy economy.

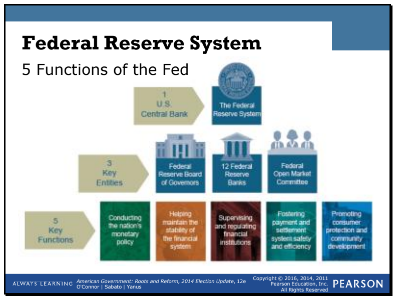
Slide 4



In 2013, the Federal Reserve System celebrated its 100th anniversary. The Fed is made up of the Federal Reserve Board, the Federal Open Market Committee, 12 federal reserve banks, member banks and the Board of Governors.

The Fed operates under a dual mandate: to control inflation and to limit unemployment. Sometime those two missions can conflict with each other. Government stimulation to increase employment levels, for example, can lead to inflation and higher prices for goods and services. The Fed has responded to economic crises with monetary policy tools to increase employment in the short term, only to have to deal with debt and inflation later.

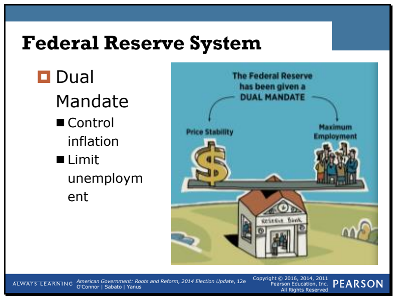
Slide 5



It performs five general functions to promote the effective operation of the U.S. economy and, more generally, the public interest.

1. The Federal Reserve conducts the nation's monetary policy to promote maximum employment, stable prices, and moderate long-term interest rates in the U.S. economy;
2. It promotes the stability of the financial system and seeks to minimize and contain systemic risks through active monitoring and engagement in the U.S. and abroad;
3. It promotes the safety and soundness of individual financial institutions and monitors their impact on the financial system as a whole;
4. It fosters payment and settlement system safety and efficiency through services to the banking industry and the U.S. government that facilitate U.S.-dollar transactions and payments; and
5. It promotes consumer protection and community development through consumer-focused supervision and examination, research and analysis of emerging consumer issues and trends, community economic development activities, and the administration of consumer laws and regulations.

Slide 6



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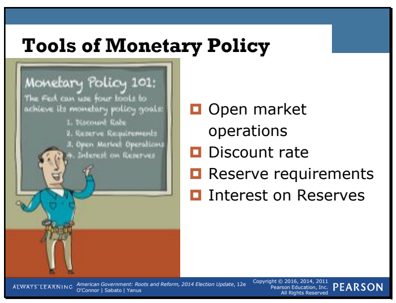
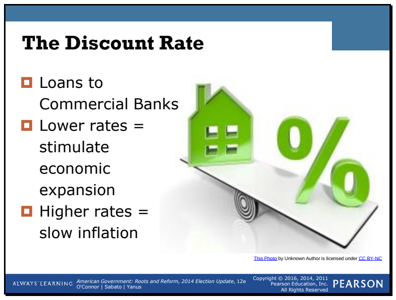


So, how does the Fed regulate the money supply? It has three key tools to do its job. The first is **open market operations**, which are the buying and selling of government securities. When banks buy long-term government bonds, they make payments to the Fed, which reduces the amount of money available for loans. On the other hand, banks have more money available to loan to businesses and individuals when the Fed buys the securities back.

The second key tool the Fed uses is the **discount rate**, which is the rate of interest at which the Fed lends money to member banks. Lowering the discount rate encourages banks to lend more money, which can expand the economy.

The Fed can also adjust the **reserve requirements**, which is the portion of deposits that member banks must retain on hand. The more banks must keep on hand, the less they have available for lending.
Interest on reserves is paid on excess reserves held at Reserve Banks. Lower the interest and banks will be more likely to give loans for businesses.

Slide 8



The **discount rate** is the interest rate Reserve Banks charge commercial banks for short-term loans. Lowering the discount rate is expansionary because the discount rate influences other interest rates. Lower rates encourage lending and spending by consumers and businesses. Likewise, raising the discount rate is contractionary because the discount rate influences other interest rates.

Slide 9