

Macroeconomic Policies

Money and Monetary Policy

NADZIRAH ZAINORDIN

MSc QS [Heriot-Watt, UK], BSc (Hons) QS [IUCTT, Msia]

- *Fiscal Policy**
- *Monetary policy**
- *Supply Side policy**

Monetary Policy

- * Attempts to **influence the level of economic activity** (the **amount of buying and selling** in the economy) through changes to **the amount of money in circulation and the price of money** – short-term interest rates.
- * Interest rates the key area of Monetary Policy

Monetary Policy... cont'd

- * Short-term interest rates set by Bank Negara Malaysia;
- * ***Basis of Monetary Policy is that there is a long run relationship between the amount of money and inflation;***
- * Monetary policy looks also into:-
 - * **Demand for Money** – the amount people wish to ***hold as cash*** as opposed to other assets
 - * **The Supply of Money** – the amount of money in ***circulation*** in the economy

1. Monetary Policy

- The Classical Quantity Theory of Money:
 - **$MV = PY$**
 - (where M = the money stock, V = velocity of circulation, P = price level and Y = level of national income
 - Velocity?



Velocity of Circulation

- *The number of times annually that money on average is spent on goods and services that make up GDP.

2. Supply Side Policy

- * Incentives
- * Education and Training
- * Investment
- * Technology Improvements
- * Productivity/Efficiency

Supply Side Policy

- * Intention is to shift the *aggregate supply* curve to the right, increasing the long term productive capacity of the economy;
- * Tend to be long-term policies;
- * Arguments about how effective they are – e.g. lowering taxes increases incentives, reducing welfare dependency increases the urge to find work

Aggregate Supply and Demand

demand

- The total level of spending in the economy

supply

- The total amount of output in the economy

Supply Side Policy

- Policies aim to **influence productivity and efficiency of the economy;**
- Key feature – open up markets and de-regulate to improve efficiency in the working of markets and the allocation of resources

Supply Side Policy

- * Main areas of policy:
 - * **Labour Market** – reduce barriers to free market, reduce bureaucracy and ‘red tape’
Short term contracts
 - * Flexible working arrangements
 - * Hiring and firing
 - * Contracts, terms and conditions, pay

Supply Side Policy

- * Education and Training:
 - * National Qualifications framework
 - logical set of qualifications
 - * Expansion of vocational qualifications
 - * Expansion of university access

Supply Side Policy

- * Incentives and technology:
 - * Tax reform to encourage incentives and entrepreneurial spirit
 - * Incentives to develop new technology – investment
 - * Drive to embracing ‘knowledge driven economy’
 - * Regional policies to encourage enterprise, investment, location, expansion

Fiscal Policy

- * Influencing the *level of economic activity* through *manipulation of government income and expenditure*
- * Influence Aggregate Demand –
 - * Tax regime influences consumption (C) and investment (I)
 - * Government Spending (G)
- * Influences key economic objectives
- * **Acts as an ‘automatic stabiliser’**
 - * **BUT:**

Fiscal Policy

- * Also used *to influence non-economic objectives and provide framework for supply side policy;*
- * e.g. education and health, poverty reduction, welfare reform, investment, regional policies, promotion of enterprise, etc.

Fiscal Policy

Government Expenditure

- Social Security
- Law and Order
- Emergency Services
- Health
- Education
- Defence
- Foreign Aid
- Environment
- Agriculture
- Industry
- Transport
- Regions
- Culture, Media and Sport