Fiscal and Monetary Policy

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When the fiscal and monetary policymakers use their respective tools to push the economy in the same direction, policies are said to be "coordinated." Depending on the degree of independence of the monetary authority, in some instances, the monetary authority may *not* accommodate fiscal policy changes. For example, when President Reagan instituted a tax cut in the United States (expansionary fiscal policy), the Federal Reserve tightened monetary policy because it feared inflation. Similarly, in Germany during the Reunification after the fall of the Berlin Wall in November 1989, the central bank and the German government enacted countervailing policies.

Table 1 summarizes the tools at the disposal of fiscal and monetary policymakers.

Table 1

	Policy Tool	**Expansionary**	**Contractionary**
Monetary	1. Open Market Operations	Buy T-Bills	Sell T-Bills
	2. Discount Rate	Decrease	Increase
	3. Required Reserve Ratio	Decrease	Increase
Fiscal	1. G (purchases of goods and services by the government)	Increase	Decrease
	2. Transfers	Increase	Decrease
	3. Taxes	Decrease	Increase