



Living with a Single Monetary Policy



But what is...?

Monetary Policy is the domain of central banks like the ECB and the US Federal Reserve. By setting interest rates, central banks can influence borrowing and saving decisions by consumers and firms. This is a powerful economic policy tool.

Inflation is a general rise in the prices of goods and services in an economy. Deflation occurs when there is a general fall in prices.

Fiscal Policy is the domain of national governments in the euro area. Fiscal policy refers to government spending and taxation.

ECB The European Central Bank is responsible for setting monetary policy for the euro area.

The euro area is unique in that it is a currency union without a corresponding fiscal union. Sharing a single currency helps the single market by lowering transaction costs and preventing competitive devaluations. But EMU also means that countries cannot always depend on monetary policy to help them adjust to shocks, and the appropriate policy stance for one country might be inappropriate in another.

- ① How does raising or lowering interest rates impact the economy? What is meant by the saying “one size fits all” with respect to the monetary policy in the euro area?
- ② What policy tools does a country give up when it joins a monetary union? What benefits do they gain in return?
- ③ What is a business cycle? Do the countries in the euro area tend to share the same business cycles?
- ④ What are the consequences of a euro area member country having higher inflation or slower GDP growth than the euro area average? What tools can policy makers use to manage growth and inflation?
- ⑤ What is the mandate of the ECB? How does it compare with the Federal Reserve’s mandate in the US?
- ⑥ Is the euro area an optimal currency area?
- ⑦ What is price stability? Why might high inflation be a problem for an economy? What about deflation, or falling prices?
- ⑧ What problems have arisen for your chosen country as a result of it having to live under the single monetary policy set by the ECB? What could be done to address these problems?
- ⑨ Can a monetary union function properly without fiscal union?
- ⑩ What unconventional policy tools has the ECB deployed over the past several years? Why have these tools been deployed?