

## **QUESTION #1**

The government plays a big part in the stability of the United States economy. This is normally accomplished in one of two ways – either by Monetary Policy or Fiscal Policy.

Monetary Policy “refers to the actions the Federal Reserve System (Fed) takes to manage the money supply and interest rates to pursue its macroeconomic policy objectives”.

As a way to provide loans to banks that were suffering a large amount of withdrawals Congress passed the Federal Reserve Act in 1913 (Dibie, 2009, p. 291). After the Great Depression the Fed was challenged to promote a well-functioning economy by pursuing four main monetary policy goals:

1. Price stability
2. High employment
3. Economic growth
4. Stability of financial markets and institutions

In his analysis What Operating Procedures Should Be Adopted to Maintain Price Stability?—Practical Issues, Charles Freedman quoted former Fed Chairman Alan Greenspan’s definition of price stability as “a rate of inflation so low that it has virtually no influence on economic behavior”.

Price stability is critical in that as prices rise the purchasing power of the individual is reduced. The value of money is reduced and people tend to buy less. As an example; the recent and rapid instability of fuel prices caused many people to change their driving habits and purchase less fuel. Furthermore, businesses like retailers, delivery services, and just about anyone else who relied heavily on vehicle transport, of their products, seen their profits greatly

reduced. Ultimately, the increased cost of service was passed on to the customer who seen their purchasing power greatly reduced. So when Mr. Greenspan's definition is considered; price stability is critical in providing the American people peace of mind and confidence in the economic well-being of the nation.

The second goal of the Fed is keeping the unemployment rate low. It is reasonable to believe that a low unemployment rate makes for a healthy economy; given the fact for people to purchase goods and services they must have a stable income. Second, high unemployment means more people are collecting an unemployment payment which over the long run is a drain on resources. Finally, high unemployment reduces the confidence people have in the economy and ultimately affects their purchase of goods and services, especially if they fear the loss of their job.

The question is how far government should go in trying to affect the employment rate. In his article The Role of Monetary Policy: Where Does Unemployment Fit In? , Donald Brash states "It is clear that we were asking monetary policy to do things it could not. Stimulating activity worked for short periods in the sense of increasing both output and employment. Ultimately, however, the only enduring result was high inflation".

As for the third goal there are differing opinions as to whether the Fed can directly affect economic growth. It is generally believed that Congress and the President can better affect economic growth by using tools such as changing the tax laws to increase the return to saving and investing. However, the Fed may indirectly affect economic growth with its ability to impact price stability and high employment (Dibie, 2009, p. 292). It is reasonable to believe that when prices are stable and there is high employment people will have more confidence in the economy

and will purchase more goods and services therefore having a positive effect on economic growth.

Finally, a stable financial system is critical for a healthy economy. Unless, you live in another world it would be difficult not to see the impact the current unstable financial system has on our recent economic situation. If creditors lack the funds or desire to loan money then borrowers will lack the resources necessary to build products, invest in new ventures, and hire employees. The Fed will use Monetary Policy as a way to ensure stability in the financial system.

According to Richard Lehne the Fed manages the monetary policy by altering the supply of money and adjusting the interest rates. When inflation is high the Fed will reduce the supply of money and conversely when unemployment begins to rise they may increase the amount of money as a way to encourage spending and higher a rate of employment.

There are three main monetary policy tools used by the Fed. First of all they require a certain portion of deposits be held by banks in an effort to maintain stability of the banking system. In this way they can control the money supply as needed. Second, is control over the rate of interest that banks must pay to borrow money, which in turn either encourages or discourages the loaning of money to its customers, once again affecting the supply of money in the economy. Third is the buying or selling of Treasury Department's interest-bearing bonds in the open market (Richard Lehne, 2006, p. 210).

Aside from using a monetary policy approach the other economic approach used by the government is fiscal policy. Richard Lehne describes fiscal policy as the "use of the national government's taxing and spending authority to influence the country's economy" (Richard Lehne, 2006, p. 202). During the last few years we have seen examples of fiscal policy with the tax rebates given during President Bush's term as a way to encourage spending. Most recently

current President Obama worked with Congress to produce a \$787 billion spending package as a way to reduce the high unemployment rate by encouraging business to either keep current employees and/or hire additional employees.

During a course lecture Dr. Dible stated the use of fiscal policy depended on the state of the economy. Government will use either an Expansionary Fiscal Policy or Contractionary Fiscal Policy. When government wants to increase the amount of money in the economy they will use an expansionary policy which will involve an increase in government spending or a decrease in taxes. As a way to reduce the supply of money in the economy they will increase taxes and reduce government spending.

Furthermore, according to David Weil's interpretation of fiscal policy "the most immediate impact of fiscal policy is to change the aggregate demand for goods and services". He goes on to say fiscal policy is an important tool for managing the economy because of its ability to affect the gross domestic product, exchange rate, and trade balance.

Economist differ on which economic policy approach is the best to use, however, according to Richard Lehne the use of monetary policy is the most widely accepted means of managing the economy because of its flexibility, ease of deployment, and more immediate impact.

As explained by Dr. Dible in class no one has a silver bullet that will work every time and in every situation. The economy of the United States is a living, breathing and ever changing economy. Therefore, government from time to time must intervene by using past successes and failures to determine which approach is the right approach. The use of one tool may cause a change in a different aspect of the economy; such as an attempt to create a lower unemployment rate may result in a higher inflation rate.

Therefore, government must seek a balance when using either policy and constantly be aware of the every changing economic environment. Once thing is for sure -- the use of both monetary and fiscal policy is critical in maintaining a vibrant and healthy economy.

## **QUESTION #2**

In answering this question I would like to point out there are many important issues discussed by Mr. Lehne's in his book. Perhaps one of the most important topics is covered in Chapter 10 under *Business and Economic Policy*, specifically Fiscal and Monetary Policy. It is very important for any public manager or Chief Executive Officer (CEO) to understand the impact these policies have on the economy and their business. However, since I covered this topic extensively in question one I will not go into detail here, only to say this is a critical area of study for all CEO's. So I have instead identified four main issues that I feel are important for public managers who are studying managerial economics and they are as follows:

1. Corporate Public Affairs Programs
2. Regulatory Policy
3. Technology Policy
4. Business as Social Actor

### **Corporate Public Affairs Programs:**

In today's world for a company to be successful they must have the ability to interact with the public in a positive way. If they are to be successful in selling their product or service the customer must have confidence in their company. Moreover, the company must have the ability to express their point of view on issues that will have both a direct and indirect impact on the business.

A quote by English Bishop Jeremy Taylor perfectly describes ignorance, “it is impossible to make people understand their ignorance; for it requires knowledge to perceive it and therefore he that can perceive it hath it not” (The Quote Page [TQP], 2007). In other words if customers are ignorant about a company or its product they may be less likely to buy from them. It is for this reason that a successful company will have in place a reliable corporate public affairs program which will have the following four elements as listed in Mr. Lehne’s book (Richard Lehne, 2006, p. 78):

1. Issues management -- Describes the process by which a company can identify, evaluate and respond to social and political issues.
2. Government relations -- Is the idea of maintaining representatives who work with the government on both Federal and State levels in an effort to relay the companies opinions on pending proposals.
3. Public communications – Is the way the company provides information about the company to the public, stakeholders, and key shareholders.
4. Community affairs – Includes such things as charitable support, employee involvement programs, and community activities.

It has been said that “a corporate public affairs department is a window into the organization for increasing transparency, legitimacy, and trust between the firm and its environment” (Dunn & Griffin, 2004).

Most businesses recognized the need to build trust and confidence with the public after the corporate corruption revealed in companies such as Enron, Tyco, and WorldCom. It is therefore critical that a business, no matter what size, has some type of corporate public affairs program.

**Regulatory Policy:**

According to Richard Lehne government regulation has been called “a distinctively American approach to balancing public and private interests” (Richard Lehne, 2006, p. 223). In other words it is a way to make sure private interest is respectable of the public when it comes to how they operate.

Regulations come about for many reason such as; a way to deal with a problem, failure, issue of fair competition, or potential danger to the public. In Johan den Hertog’s abstract General Theories of Regulations he list two prominent regulation theories; public interest theories of regulation and private interest theories of regulation. In the public interest theories of regulation Mr. Hertog describes how regulation is used to affect the “best possible allocation of scarce resources for individual and collective goods”. He goes on to say that “regulation can improve the allocation by facilitating, maintaining, or imitating market operation” (Hertog, 225).

In his private interest theory Mr. Hertog states it is generally assumed that “in the course of time, regulation will come to serve the interest of the branch of industry involved” (Hertog, 235).

Over the last century there is little doubt that government regulations have grown exponentially with nearly every aspect of our lives being regulated in some fashion. No matter which regulation theory applies it is very important for public managers to be educated on how regulations may affect their business. Regulations can cost businesses thousands and even millions of dollars depending on the type of business and what regulations apply to them. CEO’s must have a good understanding of current regulations and stay updated on proposed new regulations so they can have a voice in the process.

**Technology Policies:**

A company's ability to contend with its competitors is critical in determining whether there is a profit and ultimately survival. Therefore, it is imperative that a business has an updated plan or technology policy in place to ensure they are providing the best possible product or service. Richard Lehne states in his book American Political Economy in Comparative Perspective that "new technologies generate efficiencies that spread throughout an economy and produce strategic advantages for a firm or country over its competitors" (Richard Lehne, 2006, p. 270).

Although it is important for a company to maintain a competitive edge when it comes to technology it is equally important that they balance the money they spend on research and development(R&D) with the profits that are generated by new technology. Companies must be smarter in their spending when it comes to R&D according to Jaruzelski, Dehoff, & Bordia (2006) in their article Smart Spenders: The Global Innovation 1000, it is not always the highest spenders who are producing the greatest profit. In fact their research shows that of the largest 500 companies their median R&D spending was only 3.5 percent of their sales in 2005 where conversely 500 of the smaller companies spent 7.6 percent of their sales on R&D during the same period.

Therefore, it is important for a public manager who is entrusted with running a business to be aware of the balance they must have when it comes to R&D spending. Furthermore, in an effort to maintain a competitive edge they must be sure to keep their company updated when it comes to technology, but at the same time be aware of balancing what they are spending with the profits they receive in return.

**Business as Social Actor:**

In Richard Lehne's book he identifies three objectives of business-related policies; to accomplish broad societal goals, to protect society from business, and to safeguard workers (Richard Lehne, 2006, p. 299).

It has been greatly misunderstood what makes people happy in their job. If you asked you may get the response more money. However, Maslow's Theory of Hierarchy proves the opposite is really true. The bases of the theory is that people have five basic needs; physiological, safety, belonging, esteem, and self-actualization. Once a person has satisfied the most basic need of things such as air, water, and sleep then they will move to the next need and so forth. If employees are motivated by the drive to fulfill unsatisfied needs then it is important for managers to understand what those needs are if they are to get the most from their workers (NetMBA Business Knowledge Center [NBKC], 2007).

A successful manager and business is one which recognizes the social needs of their employees beyond a salary. Such things as health care, retirement programs, and day care. Furthermore, it is important for a manager to make his/her employees feel as though they are important and part of the family, to challenge them, and give them encouragement to realize their potential.

Government also pays a part in this social policy as a protector of the public against bad business practice and policy. They require certain professionals to have licenses, create safeguards to protect our food and provide us with safe medicine. Moreover, they ensure businesses have safety measures in place to protect us from dangers such as the chemical gas disaster which occurred in Bhopal, India in the early 1980's that killed thousands of people.

Furthermore, government, business, and employees should work together to create policies to protect workers and make for a better working environment which meets the safety need referred to in Maslow's Theory.

To be competitive, businesses must have motivated employees who enjoy coming to work and who care about the quality of the product or service they provide. It is important that managers ensure social policies are in place to make sure their employees are satisfying their unfulfilled needs. Finally, as a successful manager and socially responsible business, it is important to make sure the company is attentive to the needs of community in which they operate and live. A company which is active in the community; cares about the impact they have on the environment; and who treats their employees as family will have the trust of their customers.

**Conclusion:**

I have identified what I believe are four very important issues that a manager must be knowledgeable of -- if he/she is to be successful. First of all it is important to make sure the customers are familiar with your company and for the company representatives to have a voice when it comes to important issues, which may have either a direct or indirect affect. Second, is awareness of the regulations that currently exist and to have input on those that are being proposed. Third, is maintaining a balance when it comes to money spent on R&D and technology upgrades. A business must maintain a competitive edge but at the same time ensure they make a profit.

Finally, it is important to take care of company employees. The employees are the backbone of any business and it extremely important to make sure they are fulfilling their unsatisfied needs if they are to be motivated in doing their job. As a final thought, material things such as brick and mortar, equipment, and machines can be replaced, however, employees are

scarce resources that must be handled just right if a business is to be successful. Therefore, I believe the four points that have been listed in this paper are important to all public managers who are studying managerial economics.

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