**Discuss five areas of conflict in the objectives of monetary policy.**

Monetary policyis a policy which affects money supply growth. It can be used to affect inflation and employment. Objectives of monetary policy are to achieve full employment and price stability. Monetary policy consists of the manipulation of bank reserves of financial systems through alteration in the *discount rate, open market sales and purchase of securities, and changes in reserve requirements*.By controlling monetary reserve, the central bank affects the money supply and\or interest rates, which can change private consumption and investments expenditure (aggregate demand) and thus employment, output and price. Monetary policy may be termed discretionary policies. That is, policies require direct intervention by fiscal authority and the central bank. However there are various areas of conflict in the objectives of monetary policies.

* Some economists believe that discretionary policies would work to solve economic problems, while other economists are in serious doubts about the ability of discretionary controls to solve national economic problem. They argue that the economic equilibrium of the economy if displaced would return automatically to full employment in a competitive system by market adjustment in prices, wages, and interest rates. Classical view or neoclassical view argue that in a competitive market system, prices, wages and interest rates would automatically adjust to restore the economy back to full employment level. They advocate for minimum government intervention, since employing discretion in fiscal and monetary affairs might compound problems rather Than curing them.
* When the economy is at full employment level.

The aggregate supply of goods and services would not be responsive to increase in the aggregate demand. The aggregate supply curve would be vertical (perfectly inelastic) .As a result, an increase in the aggregate demand owing to expansionary monetary policy would be inflationary.(i.e. higher price)



*Long run aggregate supply*



* In case the economy is not at full employment

In a case where the economy is responsive to increase in aggregate demand, economy is not at full employment level, and is responsive to policy changes. At the point of wide spread unemployment, increase in aggregate demand would not only create additional output but would cause inflation as well. A trade off would exist, in other words, between changes in the level of output and employment and changes in the level of prices.



An expansionary policy that increases AD leads to increase in levels of output from  to  and prices from  to .In other words, the level of employment at is higher than. Associated with high employment level is higher price level or some level of inflation

* The classical economists saw no role for monetary policy due to the crowding out effect.

**The’ crowding out’ effect**

Suppose there is unemployment in the economy and the government attempts to increase the level of national income by increasing government spending on public goods (such as roads, dams) or on public services (such as education) than it receives in tax collection. The government when faced with a budget deficit has two choices in financing it. Print money through the central bank or Borrow by selling bonds to the general public. If the government printed money and used it to purchase goods and services, then it would be increasing the money supply, and this would be considered monetary policy and not fiscal policy. But crowding out results from the selling of new government bonds by the treasury to finance the government deficit. The treasury in order to coax the public into buying government bonds rather than bonds issued by private business lowers the price of government bonds, which would concurrently increase the interest rate on those bonds.