

DISCUSSION QUESTION

Name:

Instructor:

Course:

Do you think most people who identify as “laissez-faire” economists would agree or disagree with the following statements? If most would disagree, explain why.

- a) We should eliminate all government agencies, including the Department of Defense.

- b) State run government agencies are generally inefficient.

- c) We should limit the government's ability to use taxes and subsidies to influence market prices.

- d) The efficient government tax rate is zero, so we should always reduce taxes, regardless of the impact to society.

PEER GROUP PROBLEM SOLVING

Name:

Instructor:

Course:

Suppose someone were to say the following, “The U.S. is a democracy, which means that all policies that influence citizens should be determined by freely elected representatives. Although the Federal Reserve Bank makes policy decisions regarding interest rates and inflation that affect all citizens, its members are not elected, they are appointed. This is inherently undemocratic. Like the President and all Congressional representatives, all members of the Federal Reserve should be elected.”

- a) Do you agree or disagree with this individual's opinion? Explain why.
- b) How would making members of the Federal Reserve subject to elections impact their monetary policy decision making? Would they be more or less likely to come to a consensus? Would they be more or less biased? Explain.

IN-CLASS EXPERIMENT / ACTIVE EXERCISE

Have students form groups of four or six. Half of the group will be identified as Keynesian economists and the other half will represent Classical economists.

Each group is presented with a macroeconomic problem, or a series of problems. The problems should be straightforward, like “Suppose unemployment increases to 10%” or “Suppose inflation increases to 10%.”

The Keynesian economists and the Classical economists in each group should try to explain what policy or action (if any) they suggest should be done to address the problem. After each side explains their policy choice, have the other half explain the potential pitfalls associated with the group’s suggestions.

As a final variant, each group can remove their preset identities and explain which side they agree with and why.

SOLUTIONS AND INSTRUCTOR NOTES

Discussion Question

Do you think most people who identify as “laissez faire” economists would agree or disagree with the following statements? If most would disagree, explain why.

- a) We should eliminate all government agencies, including the Department of Defense.

Most would disagree. There is a key difference between wanting no market interference by the government and wanting no government in general. Most laissez-faire economists see the government as necessary in the provision of certain public goods, including national defense.

- b) State run government agencies are generally inefficient.

Most would agree.

- c) We should limit the government's ability to use taxes and subsidies to influence market prices.

Most would agree.

- d) The efficient government tax rate is zero; we should always reduce taxes, regardless of the impact to society.

Most would disagree. Although most laissez faire economists are in favor of lower taxes they recognize that some taxes are necessary in order for the economy and a civilized society to function.

Peer Group Problem Solving

Suppose someone were to say the following, “The U.S. is a democracy, which means that all policies that influence citizens should be determined by freely elected representatives. Although the Federal Reserve Bank makes policy decisions regarding interest rates and inflation that affect all citizens, its members are not elected, they are appointed. This is inherently undemocratic. Like the President and all Congressional representatives, all members of the Federal Reserve should be elected.”

- a) Do you agree or disagree with this individual's opinion? Explain why.

Both agreement and disagreement is valid for this question. However, it is worth pointing out that many influential policymakers are appointed, not elected. For example, all members of the Supreme Court and all heads of government agencies are appointed. If an individual agrees with this opinion, must they also believe that all members of the Supreme Court and all heads of government agencies should also be elected to their positions?

In addition, instructors should emphasize the need for independence in monetary policy decision making. Subjecting Federal Reserve Board members to election makes it more likely that policymakers take a short-run view when constructing monetary policy. Political independence is necessary to ensure policymaker's interests are aligned with long-run outcomes, even if these may be politically unpopular in the short run.

- b) How would making members of the Federal Reserve subject to elections impact their monetary policy decision making? Would they be more or less likely to come to a consensus? Would they be more or less biased? Explain.

One can use fiscal policy as a basis for comparison for the likely effects of subjecting monetary policymakers to elected positions. It is more difficult to reach consensus in fiscal policy due to the political bargaining process, impact of interest groups, and the need to tailor policy to short-run voter demands. As a result of these factors, fiscal policy has an expansionary bias, as evidenced by the \$17 trillion dollar national debt, and a persistent pattern of annual budget deficits. If monetary policymakers were subject to the will of the voters, they would be more inclined to make decisions based on what will get them elected or re-elected, rather than what is best for the economy in the long-run.

In-Class Experiment / Active Exercise

Have students form groups of four or six. Half of the group will be identified as Keynesian economists and the other half will represent Classical economists.

Each group is presented with a macroeconomic problem, or a series of problems. The problems should be straightforward, like "Suppose unemployment increases to 10%" or "Suppose inflation increases to 10%."

The Keynesian economists and the Classical economists in each group should try to explain what policy or action (if any) they suggest should be done to address the problem. After each side explains their policy choice, have the other half explain the potential pitfalls associated with the group's suggestions.

As a final variant, each group can remove their preset identities and explain which side they agree with and why.

The Keynesian/Classical identities of the students should be determined randomly; have students select from a hat or have the two/three tallest represent the Keynesians (because Keynes was tall) and two/three shortest represent the Classical economists (because Milton Friedman was short).

The exact policy proposals and explanations of the groups aren't the most important part of this exercise.

For more in-class experiment and active learning ideas, visit www.econedactive.com.