Answer on Question #40630 - Economics - Macroeconomics

Disinflation is a decrease in the rate of inflation – a slowdown in the rate of increase of the general price level of goods and services in a nation's gross domestic product over time. It is the opposite of reflation. Disinflation occurs when the increase in the "consumer price level" slows down from the previous period when the prices were rising. Disinflation is said to be caused by a slowdown in the rate of increase of a country's money supply. In some cases, it could also be caused by an economic recession. If, for example, businesses decide to refrain from increasing their prices in the interest of gaining more customers during a period of economic struggle, then disinflation is taking place. This is very bad for business, because businesses are forced to absorb costs and compromise profit just to get their products moving. In this case, disinflation is taken as a negative sign, but in cases of hyperinflation, such an occurrence may be a welcome development.

The great moderation refers to a period of economic stability characterised by low inflation, positive economic growth, and the belief that the boom and bust cycle had been overcome. In retrospect, economists look back on the great moderation in a different light because although inflation was low, there was great volatility in financial markets and asset prices. For example, in the UK, the great moderation is considered to be the period 1993-2007 because the UK had a classic boom and bust in late 1980s and early 1990s. The great moderation had various aspects.

- Low inflation. The most prominent feature of the great moderation was persistently low inflation.

- Stable growth. With low inflation, we avoided the boom and bust cycles. The UK had their longest period of economic expansion on record 1992-2007. Apart from a minor dip in 2001, the US economy grew strongly during 1986-2006.

- The end of uncertainty and greater risk taking. The benign macro economic situation encouraged investment in both capital and financial investments. During the 1980s and 1990s, there was a period of financial deregulation which encouraged a growth in complex financial derivatives, such as credit default swaps.

- Rising asset prices. Asset prices, especially houses, saw a rapid growth in prices.

Full employment, in macroeconomics, is the level of employment rates where there is no cyclical or deficient-demand unemployment. It is defined by the majority of mainstream economists as being an acceptable level of unemployment somewhere above 0%. The discrepancy from 0% arises due to non-cyclical types of unemployment. Unemployment above 0% is seen as necessary to control inflation, to keep inflation from accelerating, i.e., from rising from year to year

It was argued that the governments tended to make poor decisions about monetary policy. In particular they tended to be influenced by short term political considerations. Before an election, the temptation is for a government to cut interest rates. This increases economic growth, reduces unemployment and increases the political support of the party. However, this expansionary monetary policy may lead to inflation and boom and bust economic cycles. Therefore arguably, it is better to take monetary policy out of government's hands. People have more confidence in the Central Bank, therefore this helps to reduce inflationary expectations. In turn this makes inflation easier to keep low. Central bank independence does not necessarily require completely giving up discretion. In a sense, dependence may interfere with a central bank's discretion by requiring a central bank to accommodate fiscal policy. Such an accommodation, however, is the result of the fiscal authorities' enforcing their discretionary urges on a potentially resistant central bank. Likewise, while an independent central bank is free to use discretion, it is assumed to be less likely to exploit this freedom.