<u>Day 29</u>

- Aggregate Expenditures Model
    - Explanation for why level of economic activity changes
- In a private, closed economy
    - All business by citizens
    - Level of GDP would equal consumption + Investment and equilibrium would gravitate there
    - Spending = GDP
    - Investment independent of GDP and this is always the same; illustrated by parallel
- When investment spending goes up and down, the line shifts up and down; equilibrium changes
    - Reason for the business cycle
- What happens in the open economy?
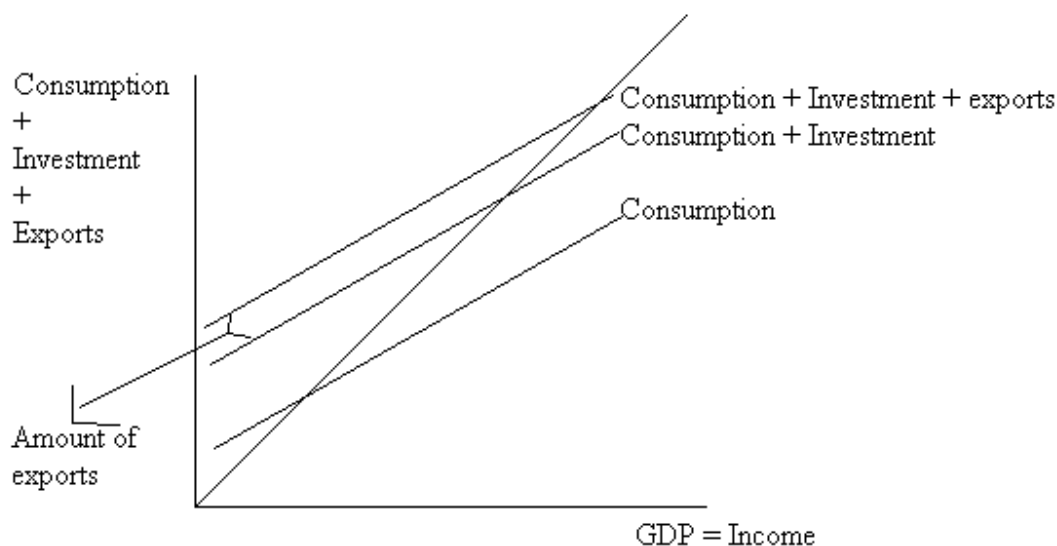
- What about imports; shift line down
    - Exports – Imports = Net exports
    - If the net exports are positive, line shifts up
    - If negative, the line shifts down
- If exports = Imports Xn = 0

Y	C	Ig	Xn	S
100	100	25	0	-25
150	125	25	0	0
200	125	25	0	25
250	175	25	0	50

- What determined net exports? (3 things)
    - Exchange rates (What it costs to get currency from another country)
        - Value of the dollar ↑ Xn ↓

- Value of the dollar ↓ Xn ↑
  - o Prosperity of the world
    - Tariffs and trade restrictions
  - o Net exports small, but still influence

<u>Day 30</u>

- When government spends the consumption line goes up, when tax it goes down, but less government spending is not dollar to dollar to dollar because people spend

Notes From The Book:

APC = Consumption/Income

APS = Saving/Income

MPC = Change in Consumption/Change in Income

MPS = Change in Savings/Change in Income

Non-Income Determinants of Consumption and Saving

- Wealth
- Expectations
- Taxation
- Household Debt

Both Consumption spending and saving rise when disposable income increases; both fall when disposable income decreases

The APC is the fraction of any specific level of disposable income that is spent on consumer goods

The APS is the fraction of any specific level of disposable income that is saved

APC falls and APS rises as disposable income increases

MPC is the fraction of the change in disposable income that is consumed; slope of consumption schedule

MPS is the fraction of change in disposable income that is saved; slope of savings schedule

Increases in investment demand are shown as rightword shifts in the investment demand curve; decreases in investment demand are shown as leftword shifts in the investment schedule

A specific investment will be undertaken if the rate of return exceeds the real interest rate

The investment demand curve shows by total monetary amounts that will be invested by an economy at various possible real interest rates

The investment demand curve shifts when changes occur in (a) the cost of acquiring, operating, and maintaining capital (b) business taxes (c) technology (d) the stock of capital goods on hand, and (d) business expectations

In a private closed economy, equilibrium GDP occurs where aggregate expenditures equal real domestic output ($C + I_g$ =GDP)

At equilibrium GDP, saving equals planned investment ($S = I_g$)

At equilibrium GDP, unplanned changes in inventories are zero

Actual investment consists of planned and unplanned investment plus unplanned changes in inventory and is always equal to saving in a private closed economy

CH 10

Multiplier = Change in real GDP/Initial change in spending

Multiplier = 1/MPS or 1/(1-MPC)

The multiplier effect reveals that an initial change in spending can cause magnified changes in domestic income and output. The multiplier is the factor by which the initial change is magnified: Multiplier = Change in real GDP/Initial change in spending

The higher the marginal propensity to consume (the lower the marginal propensity to save), the larger the simple multiplier: Multiplier = 1/MPS

Positive Net Exports Increase Aggregate Expenditures relative to the closed economy and increase equilibrium GDP

Negative net exports decrease aggregate expenditures relative to the closed economy and reduce equilibrium GDP

In the open economy, U.S. net exports and therefore aggregate expenditures and equilibrium GDP can be affected by the changes in prosperity abroad, changes in tariffs, and changes in exchange rates.

Government purchases shift the aggregate expenditures schedule upward and raise the equilibrium GDP

Taxes reduce disposable income, lower consumption spending and saving, shift the aggregate expenditures schedule downward, and reduce the equilibrium GDP

The balanced-Budget multiplier is 1

A recessionary gap is the amount by which an economy's aggregate expenditures schedule must shift upward to achieve the full-employment GDP; the inflationary gap is the amount by which the economy's

aggregate expenditures schedule must shift downward to eliminate demand-pull inflation and still achieve the full-employment GDP

Limitations of the Keynesian Model

- Doesn't show price-level changes
- Ignores premature demand-pull inflation
- Bars real GDP beyond the full-employment level of output
- Does not deal with cost-push inflation

Day 31
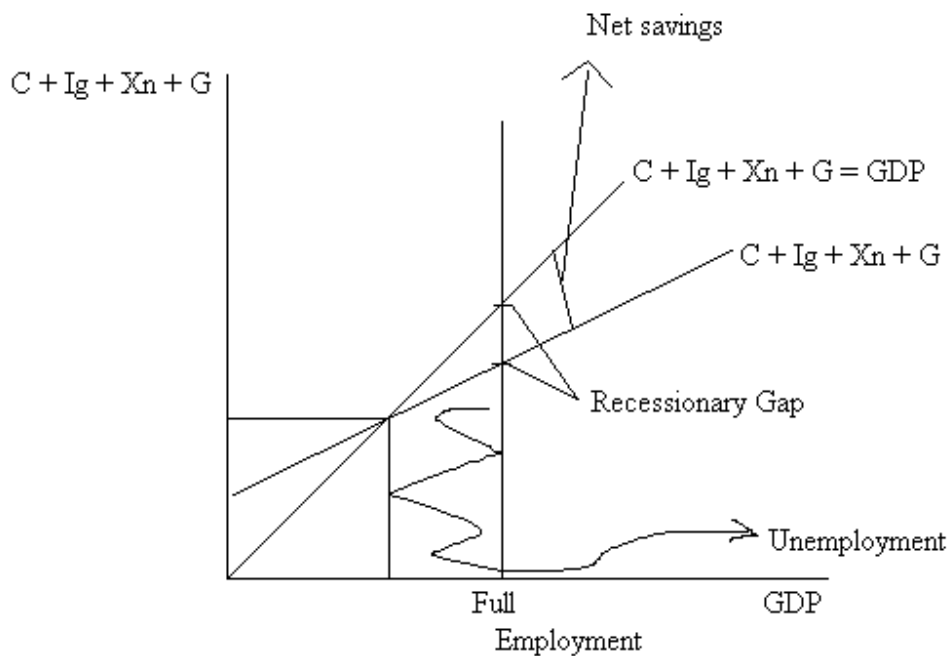
- Equilibrium, spending = output
  - What would equilibrium be without government?
  - Government controls disposable income
  - Not all taxes spent with consumption
- For full employment, value of production must be higher, say if equilibrium were 490, it would be 510
  - Consumers want to spend 505?
  - Net savings, inventory up
  - Production goes down
  - Unemployment due to lack of spending
  - Wages and prices are sticky down
    - In the long run according to Keynes, all are dead

- - We need to <u>stimulate</u> spending
- Multiplier effect
- Effect of people wanting to buy more: Inflation
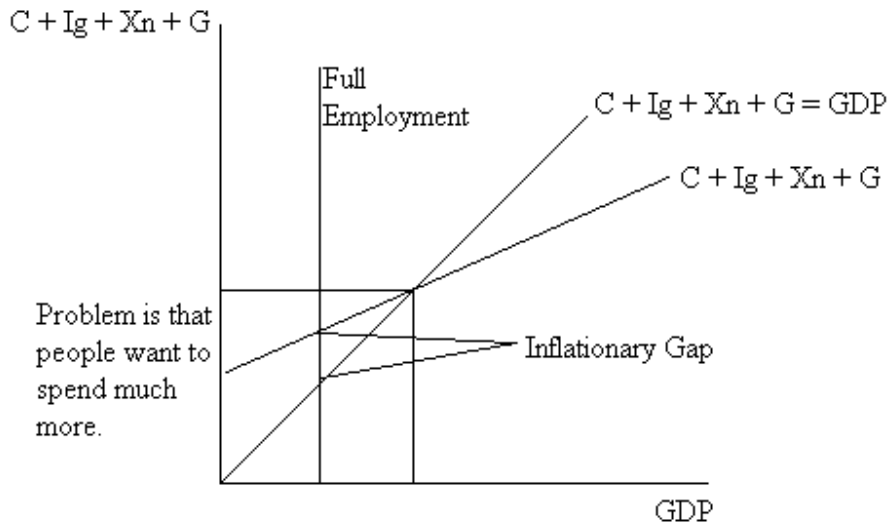
- Multiplier effect
- Effect of people wanting to buy more = Inflation
- Business spending manipulated by the government
  - o Interest rates
- Savings + Taxes + Imports = Investment + Gov't + Exports
- S + T + M = Ig + G + X
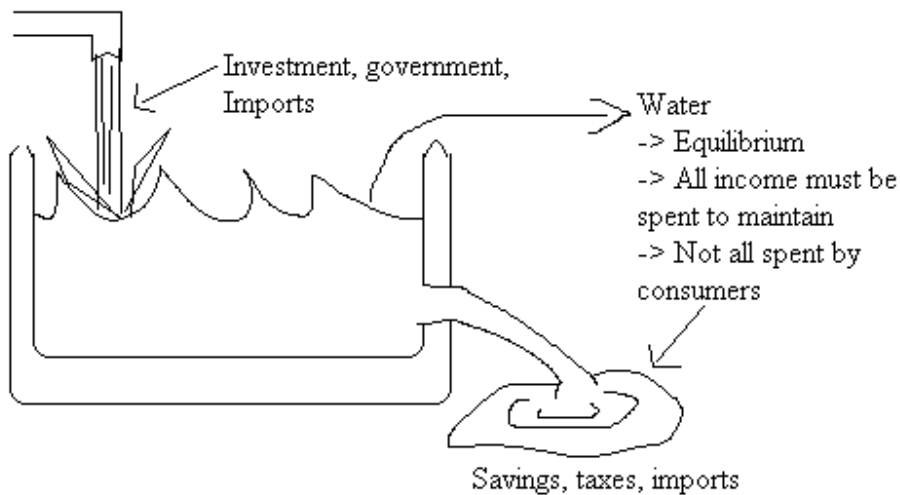
- (I know you love my artistic rendition ^_^)
- @ Equilibrium, amount going out = amount going in

I was absent for the next few days… I copied some notes, but from someone whose notes aren't really the same style so… o.O yeah, here they are

- Savings + Taxes + Imports > Ig + G + X goes to the right
- S + T + Imports < Ig + G + X net dissavings
- Marginal propensity to consume - % of additional income spent
  - MPC - MPS = 100% of additional income
- 1/(1-MPC) = m (Multiplier)
- Propensity = Tendency
- APC = Total income consumed
- MPC – For change, additional income consumed
- MPC – Slope of function line rise/run = Spending/Income
- MPC = Consumption change/ Income change
- Balanced budget multiplier is always 1