MACRO

IV. Consumption, Saving, Investment and the Multiplier

Consumption

Disposable income

Saving

Autonomous consumption

Marginal propensity to consume

Marginal propensity to save

Determinants of consumption and saving

- Wealth
- Expectations
- Household debt
- Taxes and transfers
- Real Interest Rates

Investment

Decision to invest

Interest rate v. expected rate of return

Investment demand

Loanable funds market

Supply of loanable funds

Demand for loanable funds

Multiplier Effect

Spending multiplier (Ig, G or Xn influencing C)

= 1/ mps
= 1/ (1-mpc)
= change in GDP / change in spending

Tax multiplier = mpc / mps

Why is the spending multiplier more robust than the tax cut multiplier?

The balanced budget multiplier = spending multiplier – tax cut multiplier

V. Aggregate Demand and Aggregate Supply

<u>Aggregate demand-</u>

Components of aggregate demand

The shape of AD

Interest rate effect

Wealth effect

Foreign sector substitution effect

Changes in AD

Consumption

Investment

Government spending

Taxes and transfers

Net exports

Foreign incomes

Consumer tastes

Exchange rates

Aggregate supply-

Macroeconomic short run

Short-run aggregate supply

Macroeconomic long run

Long run aggregate supply

Shifts in Aggregate Supply

Short-run shifts

Input prices

Tax policies

Legal environment

Political or environmental phenomena

Long-run shifts

Availability of resources

Technology and productivity

Policy incentives

Macroeconomic Equilibrium

Macro equilibrium graph

GDP and Price level

Recessionary and inflationary gaps

Shifts in AD

Graphing the multiplier

Shifting AS

-Stagflation

Supply shocks

The Trade-off between inflation and unemployment

Changes in AD in the intermediate range

The Phillips Curve

Movement of the Phillips curve

The long-run Phillips curve

Expected inflation, actual inflation the natural rate of unemployment, and the long-run Phillips Curve