

- And the MPC value remains constant across different income values for different individuals. in short run.
- Average propensity (APC) to consume falls as income rises.

$$APC = \frac{C}{Y} = \frac{a}{Y} + b \quad \text{Hence, } APC > MPC.$$

$APC = \frac{\text{Total consumption in a particular time period}}{\text{Income}}$

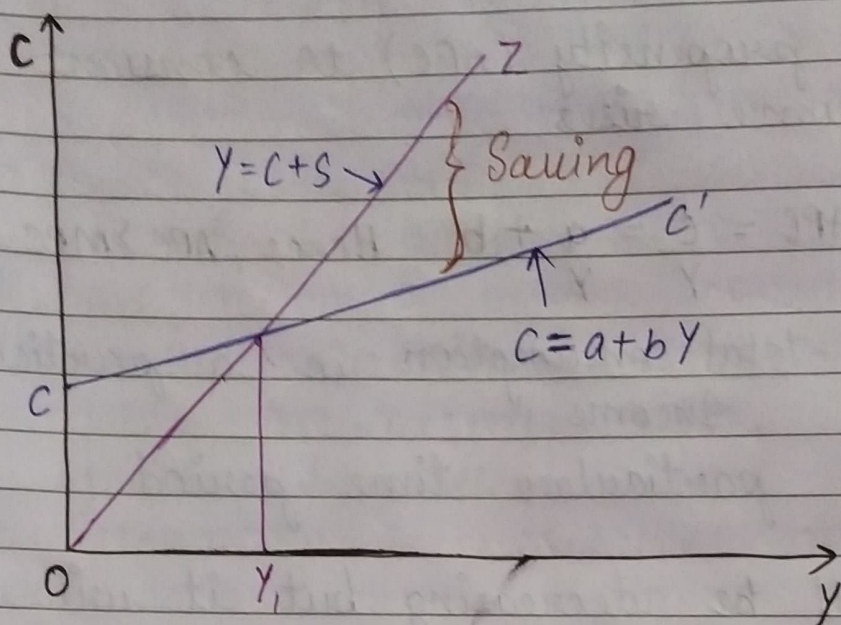
- APC will be decreasing but it will always be greater than MPC.
as $APC = \frac{a}{Y} + MPC.$
- The fraction of the income consumed will decrease with the increase in income.
- Income is the primary determinant of consumption and the interest rate does not have an important role.

Example.

Y	0	10	20	30	40	50
C	10	15	20	25	30	35
S	-10	-5	0	5	10	15

$$MPC = \frac{1}{2}$$

$$C = 10 + 0.5Y.$$



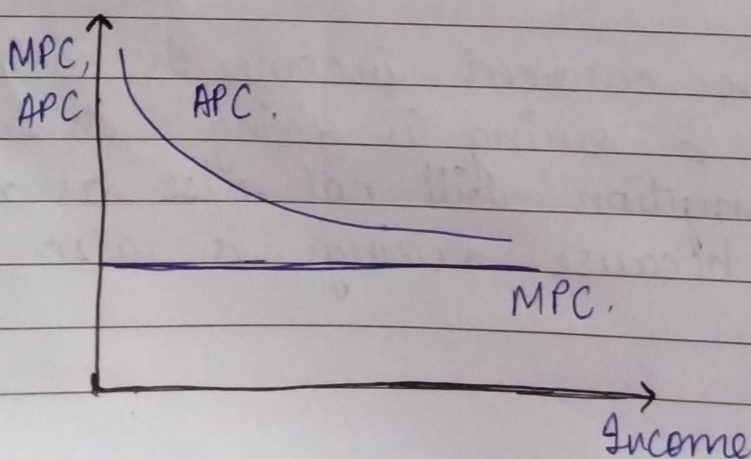
- $C \rightarrow$ autonomous consumption i.e. consumption at 0 income.
- Income is a flow which is generated only when the resources are employed. when more resources are employed, more income is generated.
- If the current income is zero then it doesn't mean that the ~~the~~ income was zero previously as well. The autonomous consumption is the consumption which is independent of income. It comes from dissavings. i.e. they might use their past savings ~~for~~ which were made when income was not zero.

- Another source can be borrowing money. They could ~~be~~ borrow from the bank, friends or relatives. ~~This~~ This is a short run behaviour.
~~In the short run~~
- If this continues in the long run i.e. income remains zero then consumption will ultimately become zero as the consumer will not even have the opportunity to borrow.
- While in the short run, if income becomes zero, then also consumption have some +ve value.
- But when the income is zero, then the consumer would spend only on the basic needs, \therefore it can be met by the options available in the short run.
- Saving funcⁿ is a counter part of the consumption funcⁿ. If one is known other can be found.
- ~~Saving~~ As ~~inc~~ current income is rising, consumption & saving is rising. \therefore As income rises, consumption will not rise as much as income because savings is also rising.

at $Y = Y_1$

$Y = C$ (Break-even point)

- $MPC = 1/2$ \therefore half of the increase in income is spent & half is saved. MPS (Marginal propensity to save) will also be the same.
- The fraction of income consumed decreases as income rises. i.e. APC decreases as income rises.
- As the income rises, the economy will become more & more ~~prosperous~~ prosperous. therefore the fraction of income utilised will ~~become~~ decrease.
- i.e. APC will decrease & APS will increase.
- Unless saving = investment, the economy will face deficiency in demand given supply leading to recession.



- Unless all that is saved is invested, the economy will experience leakages.
- Prosperous economy is bound to face stagnation.
- When the income level rises so much, then the people build greater tendency to save, ~~the dem cons~~
- The ~~consumption~~ needs of all the individuals have been fulfilled. The economy will face stagnation.
- As the income rises, the fraction of income consumed decreases. As the people would have already fulfilled all their needs of consumer durables & other products, therefore, there will be a ~~very~~ very large tendency of the people to save their money.
- Unless saving = investment, the economy is bound to face recession.
- Deficiency of demand arises from the difference between income & consumption which is saving. ∴ unless saving is channelised towards productive investment, the country will face recession.

- In the long run, APC may become equal to MPC.

* Saving funcⁿ:

$$S = Y - C = Y - a - bY.$$

$$S = -a + (1-b)Y$$

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Thus $MPS = 1-b$.

$$APS = \frac{-a}{Y} + (1-b)$$

Hence $MPS > APS$.

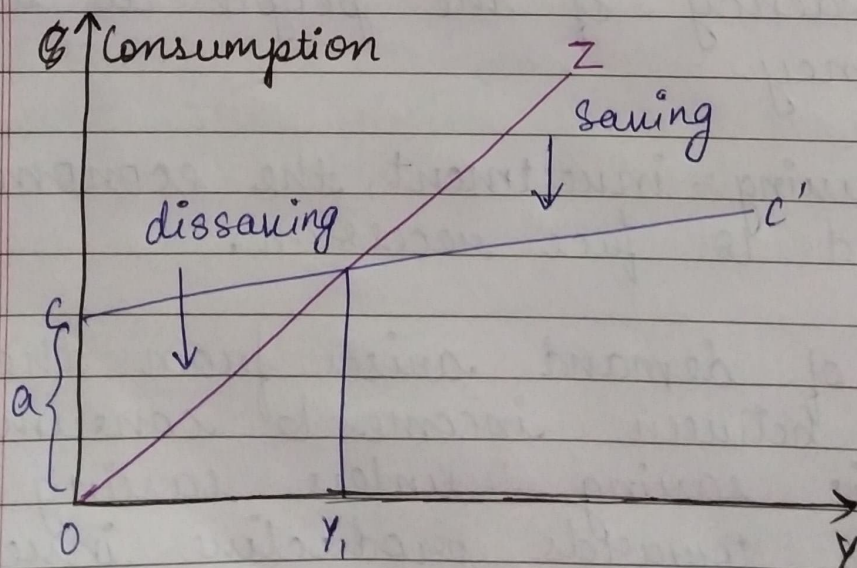
$$MPC + MPS = 1$$

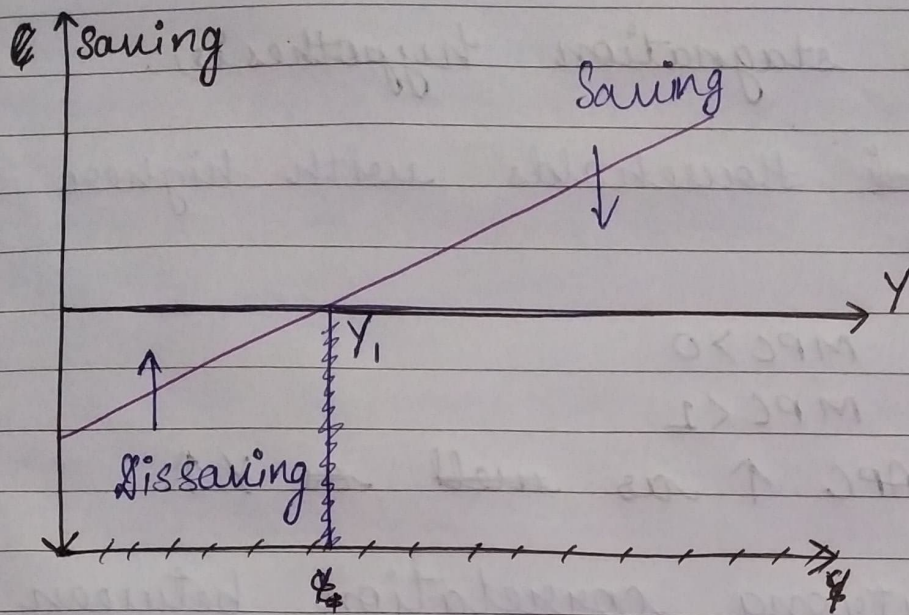
$$APC + APS = 1$$

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$$MPS > APS$$

$$0 < 1-b < 1 \quad \text{where } 1-b = MPS.$$





* Implications :

- As an economy prospers, income goes up ~~as~~ and so does the savings rate (APS).
- Thus prosperity leads to stagnation.

* Reasons :

- As Y goes up, APC goes down & APS goes up. Thus, consumption expenditure falls leading to fall in AD.
- Savings do not ~~lead~~ lead to ~~investment~~ investment as the opportunities for investment may ~~not~~ not be favourable.
- This leads to increase in inventory, fall in production & then to stagnation.

(Secular stagnation hypothesis).

- ~~Household~~ Households with higher incomes:

$$MPC > 0$$

$$MPC < 1$$

APC \uparrow as ~~well~~ ~~as~~ $Y \uparrow$.

- Very strong correlation between income & consumption
 \Rightarrow Income seemed to be the main determinant of ~~the~~ consumption.