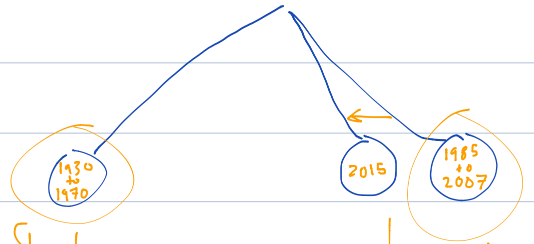
The Major Emphases of Macroeconomics



Short run — Long run

Business Cycle Theory — Growth Theory

Recessions and Expansions — Development

Aggregate Demand and Aggregate Supply Model "AD-AS Model"

Aggregate = Total

real GDP = Y

Aggregate Demand: Demand for all final goods and services Spending

Aggregate Supply: Supply of all final goods and services producing

Aggregate Demand

Demand for GDP from all Sources

4 Pieces of AD:

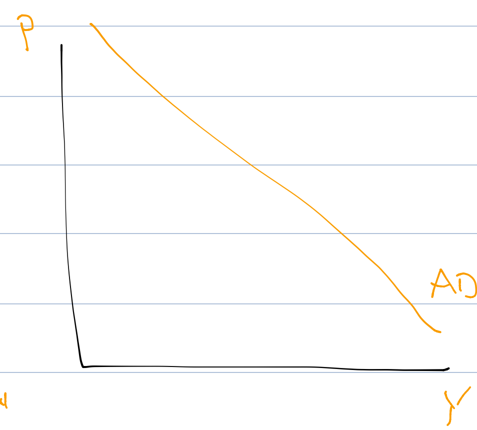
C Consumption

I Investments

G Government Spending

NX Net Exports (imports - exports)

$AD = C + I + G + NX$



capital

P = Price Level

Y = real GDP

Slope of AD curve is negative

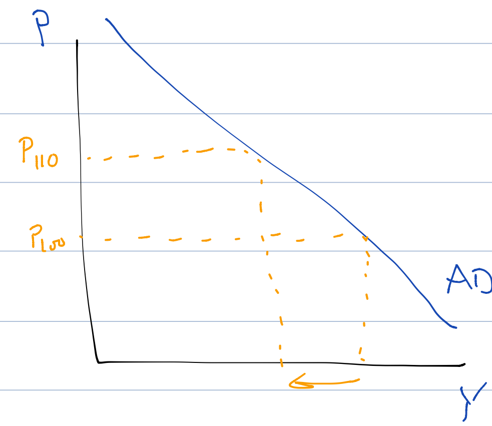
Three Reasons why Slope is Negative

1. Wealth Effect

Price level increases reduce the real value of wealth and this reduces the quantity of AD

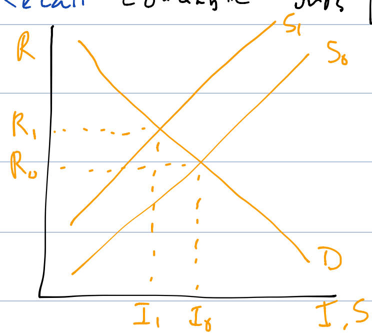
*This is caused by a change in P

$AD = C + I + G + NX$



2. Interest Rate Effect

Recall: Loanable Funds Market



Summary:

A. $\uparrow P \rightarrow \downarrow$ Real wealth

B. $\downarrow$ real wealth $\rightarrow \downarrow$ savings

C. $\downarrow$ Savings $\rightarrow$

D.

3. International Trade Effect

$P = P_{US}$

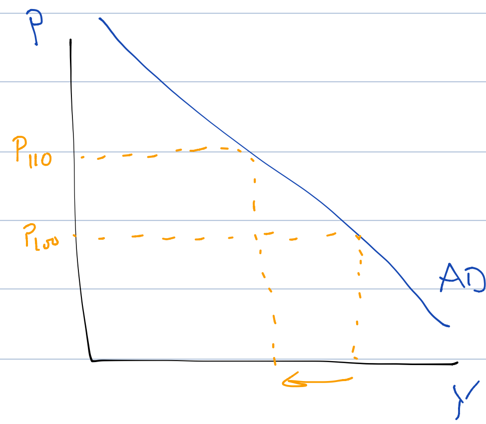
$P_{US} \uparrow \rightarrow \left. \begin{array}{l} \downarrow \text{exports} \\ \uparrow \text{imports} \end{array} \right\} \downarrow NX$

$AD = |C + | I + G + NX|$

Summary

Why does AD slope down?

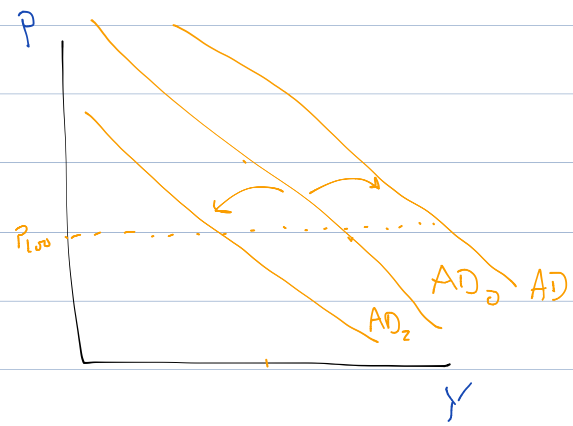
1. Wealth Effect
2. Interest Rate Effect
3. International Trade Effect



AD Shifts

Five Factors that Shift AD

1. Real Wealth (+)
2. Expected Income (+)
   Consumer Confidence!
3. Expected Future Price (+)
4. Foreign Income (+)
5. Value of the Dollar



(Value of Dollar) ↑ → { ↑ imports, ↓ exports } ↓ NX