EC1506 Essay

I will approach this question from a Malthusian point of view.

Through methods of substitution (Parkin et al, 2011;538), we find that I = S + (T-G) + (M-X), where I is investment, S is savings, T is taxes, G is government expenditure, M is imports and X is exports. Therefore, “Investment is financed by household savings, the government budget surplus and borrowing from the rest of the world” (Parkin et al, 2011; 538). However, this identity takes into account stock building (inventory accumulation), which does not increase the actual investment into machinery and the likes. Stock building can then lead to a recession due to unconsumed products, and eventually lay-offs, non profitability and inefficiency. In this situation, firms must get rid of excess products and correlate their supply with changed demands. Fortunately, use of lean production helps decrease these effects. Proper forecasting the demand for goods and services also helps to reduce accumulating inventory.

If firms do not change according to demand and simply lower output, real GDP falls and price levels increase (Parkin et al,2011;618).

As I chose the Malthusian point of view, I will look at the Malthusian trap. As the labour force grows with population, there are diminishing returns to output.

The catchphrase from Say’s law of supply creates its own demand is very relevant in this situation.

We can also use the following to correlate saving and investment:

Y = total expenditure = total income

Bibliography

Parkin, M., Powell, M. and Matthews, K. (2011) *Economics*. 8th edn. Harlow, England: Addison-Wesley.