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What is Aggregate Demand

- **Aggregate Demand** = a metric of overall demand for *all* goods
  - You can think of it as a **demand schedule** of all the goods and services people are willing to purchase at different price levels
    - The same relation applies
      - Increasing price yields lower quantity demanded
      - Decreasing price yields higher quantity demanded
  - A useful way of looking at it is that aggregate demand is *really* just real GDP
    - This actually makes sense, because it is basically just the market value of all goods at any given time

$$AD = C + I + G + \Sigma X$$

    - where C is consumer spending, I is investment, G is government spending, and ΣX is net exports
- You can construct a demand curve using **price level(PL)** and **Real GDP** just like with price and quantity demanded

Why is the Aggregate Demand Curve Downward-Sloping?

1. **Wealth Effect** = a change in price level changes the purchasing power of a dollar, and thus the quantity of transactions changes
   - Increasing price yields lower "GDP demanded"
   - Decreasing price yields higher "GDP demanded"
2. **Interest-Rate Effect** = a change in price level changes interest rates that lenders charge
   - If price level increases, the lend is more risky, so a higher interest rate is charged
   - If price level decreases, the lend is less risky, so a lower interest rate can be charged
3. **Foreign Trade Effect** = a change in domestic price level invokes a kind of substitution effect wherein foreign goods are bought more or less
   - If domestic price level increases, GDP demanded(which doesn't include foreign production) will decrease because consumers are purchasing foreign goods
   - If domestic price level decreases, GDP demanded(which includes domestic production) will increase because consumers are purchasing more domestic goods

Shifters of Aggregate Demand

1. Change in consumer spending
    - Can be caused by many things
        1. Change in disposable income of consumers
        2. Expectations about future economic growth or contraction
            - If people are fearful of a recession, they won't spend as much
        3. Consumer debt
        4. Changes in consumer taxes
2. Change in investment spending
    - Can be caused by many things
        1. Change in interest rates
        2. Expectations about future demand trends
            - If a new industry pops up and shows potential for growth, investment will increase
        3. Changes in labor productivity or automation
            - If productivity(output vs input ratio) increases, companies will invest to take advantage of that
        4. Changes in business taxes
3. Change in government spending
    - Is only caused by a change in government expenditures
        - *e.g.* Buying more drones to bomb Libya with
4. Change in net exports
    - Can be caused by many things
        1. Change in exchange rates
            - If the USD->Euro exchange rate changes, the purchasing power of each respective currency changes, and net exports change
        2. Change in domestic economic well-being
            - Generally, countries with high GDP-per-capita spend more on foreign goods