

**Economic Growth**  
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**BSC IV - Spring 2023**

**Assignment 5**

**Group 6:** Summarize *Chapter 20: The Employment Function and Chapter 19: Appendix - Professor Pigou's 'Theory of Unemployment'* from the book "The General Theory of Employment, Interest, and Money" by John Maynard Keynes.

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In Chapter 20 of "The General Theory of Employment, Interest, and Money" by John Maynard Keynes discusses the employment function. According to Keynes, employment is determined by the intersection of aggregate demand and aggregate supply in the labor market. The employment function represents the relationship between the level of employment and the level of income in the economy.

Keynes argues that there are two main determinants of the employment function: the marginal propensity to consume (MPC) and the marginal efficiency of capital (MEC). The MPC represents the proportion of additional income that individuals spend on consumption, while the MEC represents the expected return on investment in new capital equipment.

The employment function is derived from the investment function, which represents the relationship between investment and the interest rate. According to Keynes, the interest rate is determined by the supply and demand for money. When the interest rate is low, investment is high, and employment increases. When the interest rate is high, investment is low, and unemployment increases.

Keynes argued that the employment function is unstable and subject to fluctuations due to changes in the MPC and the MEC. He also suggests that government intervention is necessary to stabilize the economy and maintain full employment. He proposes a policy of deficit spending during times of recession to increase aggregate demand and stimulate employment.

In Chapter 19's Appendix, Keynes presents an overview of Professor Pigou's "Theory of Unemployment." Pigou believed that unemployment was caused by a mismatch between the

supply and demand for labor. According to Pigou, wages should adjust to balance the supply and demand for labor, leading to full employment in the long run.

Keynes criticizes Pigou's theory, arguing that wages are sticky and do not adjust quickly enough to changes in the labor market. He also suggests that unemployment can be caused by a deficiency in aggregate demand, rather than a mismatch between supply and demand. Keynes argued that government intervention is necessary to stimulate demand and maintain full employment. Overall, Keynes emphasizes the importance of understanding the employment function and the role of government intervention in stabilizing the economy and maintaining full employment