

# MACROECONOMICS CONCEPTS

1. <b>2 Causes of Inflation</b>	<ul style="list-style-type: none"> <li>- Demand-pull (excess AD)</li> <li>- Cost-push (increased cost of production)</li> </ul>	11. <b>AS Curve</b>	<ul style="list-style-type: none"> <li>- Planned output at any given price level</li> <li>- The total quantity of output supplied in an economy over a period of time</li> <li>- Dependent on quantities of factors of production</li> <li>- Flexible depending on ST &amp; LT effects</li> <li>- Influenced by skills of workforce, efficiency &amp; quantity of capital, cost of raw materials and cost of workforce</li> </ul>
2. <b>Actual growth</b>	<ul style="list-style-type: none"> <li>- The annual percentage increase (or decrease) in output</li> </ul>	12. <b>Automatic stabilisers definition</b>	<ul style="list-style-type: none"> <li>- Automatic stabilisers help to reduce the volatility of the business cycle</li> <li>- Taxes rise to avoid boom, benefits rise to avoid recession</li> <li>- If used, could reduce amplitude of cycle by 20% say OECD</li> </ul>
3. <b>Actual Growth (economic growth)</b>	<ul style="list-style-type: none"> <li>- The annual percentage increase in output</li> </ul>	13. <b>Average propensity to consume (APC)</b>	<ul style="list-style-type: none"> <li>- Ratio of consumption to income (proportion of income you spend)</li> </ul>
4. <b>AD Curve Definition</b>	<ul style="list-style-type: none"> <li>- Relationship between level of AD and overall price level over a period of time</li> <li>- Price is an average of all goods and services in an economy</li> </ul>	14. <b>Balance of Payments</b>	<ul style="list-style-type: none"> <li>- Capital account + current account</li> </ul>
5. <b>AD curve shifting</b>	<ul style="list-style-type: none"> <li>- When RNI increases whilst remaining at current price level</li> <li>- Caused by changes (e.g taxes) effecting C, I, G or X-M</li> <li>- Any changes that increase components of AD (assuming CP) will shift curve right</li> </ul>	15. <b>Balance of Payments</b>	<ul style="list-style-type: none"> <li>- Current Account: the trade in goods and of services (exports/imports), income flows (profits, dividends/interest), current transfers (grants/subsidies)</li> <li>- Capital Account: sale and purchase of capital assets and non-produced or non-financial assets</li> <li>- Financial Account: Trade in financial assets</li> <li>- Net Errors and Omissions</li> </ul>
6. <b>Advantages of a current account deficit</b>	<ul style="list-style-type: none"> <li>- ST boost to living standards (buy more better quality imports)</li> <li>- Cyclical - depends on time period</li> <li>- Deficit due to increased demand for imported capital goods which would increase productivity in UK in LT</li> <li>- HOWEVER: CA surpluses not always good sign (e.g. Germany &amp; Japan recessions), capital flows have to be able to finance the current account deficit</li> </ul>	16. <b>Balance of Payments Definition</b>	<ul style="list-style-type: none"> <li>- Measures the economic transactions between UK residents and the rest of the world</li> <li>- Trade in goods</li> <li>- Trade in services</li> <li>- Income flows from investments (Example of a positive flow)</li> <li>- Financial flows - shares, loans</li> <li>- Foreign aid (Example of a negative flow)</li> </ul>
7. <b>Aggregate Demand</b>	<ul style="list-style-type: none"> <li>- Sum of all expenditure in economy over period of time</li> <li>- <math>AD = C + I + G + (X-M)</math></li> </ul>	17. <b>Balancing the current account</b>	<ul style="list-style-type: none"> <li>- I.e. deficit in current account = surplus in capital account in order to balance the BOP</li> <li>- Attract foreign investment</li> <li>- Government running down official reserves of foreign currency</li> <li>- High IRs leading to ST banking flows (Hot money flows)</li> </ul>
8. <b>Aggregate Demand</b>	<ul style="list-style-type: none"> <li>- Sum of all expenditure in economy over a period of time</li> <li>- <math>AD = C+I+G+(X-M)</math></li> </ul>		
9. <b>Aims of fiscal policy</b>	<ul style="list-style-type: none"> <li>- Equity (inter-generational equity - each generation pays the same level)</li> <li>- Funding government spending (generate tax revenues to avoid borrowing and debt)</li> <li>- Benefits (benefits meet cost - only gain if you pay the cost)</li> <li>- Macroeconomic stability (smooth path of AD over economic cycle - smooth peaks and troughs)</li> </ul>		
10. <b>APC vs MPC</b>	<ul style="list-style-type: none"> <li>- Income rises, APC falls</li> <li>- MPC lower than APC</li> <li>- Lower incomes have higher MPC than higher earners (rich already have everything)</li> </ul>		

18. <b>Barriers to growth</b>	<ul style="list-style-type: none"> <li>- Trade barriers (embargoes, high tariffs, quotas)</li> <li>- Decreased confidence (consumers mainly)</li> <li>- Exchange rates (SPICED)</li> <li>- Unemployment (unemployed resources = spare capacity)</li> <li>- Lack of credit (banks less likely to lend, increased IRs)</li> <li>- High interest rates (less loans)</li> <li>- Crowding out effect (more reliable public sector spending crowds out less reliable private sector spending)</li> <li>- High taxes (reduces consumption &amp; investment)</li> </ul>	23. <b>Causes of cost-push inflation</b>	<ul style="list-style-type: none"> <li>- External shocks (commodity price changes - oil)</li> <li>- Depreciation in the exchange rate (M more expensive - withdrawal)</li> <li>- Acceleration in wages (only in SR - wages often follow prices)</li> <li>- Increased inflationary expectations (inflation expected to continue - workers demand higher wages)</li> </ul>
19. <b>Benefits of growth</b>	<ul style="list-style-type: none"> <li>- Increased standard of living (gov spends more on infrastructure improvements)</li> <li>- Increased employment (growth &gt; investment &gt; capital increase &gt; excess workforce (derived demand - increase in one thing leads to an increase in another)</li> <li>- Increased investment at home and abroad (ACCELERATOR EFFECT)</li> <li>- Increased income (bonuses &amp; matching inflation)</li> <li>- Sustainable growth (increased spending on env issues, greenbelt, recycling, nature policies)</li> <li>- Increase in Gov revenue (fiscal dividend/taxes)</li> <li>- Increase in confidence (business &amp; consumer)</li> <li>- Trickle down effect (rich get richer creating more opportunities for poor, rich get richer, pay more tax increasing benefits to poor)</li> </ul>	24. <b>Causes of demand-pull inflation</b>	<ul style="list-style-type: none"> <li>- Depreciation of exchange rate (increases price of M)</li> <li>- Reduction in indirect or direct taxation (inc. disposable income)</li> <li>- Rapid growth of money supply as a result of increased lending from banks (inc. spending)</li> <li>- Rising consumer confidence (wealth effect)</li> <li>- Increase in rate of growth of house prices</li> <li>- Strong economic growth in trading partners (inc. UK exports - injection)</li> </ul>
20. <b>Boosting AD by running a budget deficit</b>	<ul style="list-style-type: none"> <li>- Running a larger budget deficit (higher gov spending or reduced taxation) - example of counter-cyclical demand management</li> <li>- Multiplier effect (growth and employment increases)</li> <li>- Some of gov spending may be self-financing if the economy experiences an upturn</li> </ul>	25. <b>Causes of growth - AD</b>	<ul style="list-style-type: none"> <li>- Increase in consumer confidence</li> <li>- Increase in business confidence</li> <li>- Increase in consumption</li> <li>- Increase in investment</li> <li>- Increase in Gov spending (G)</li> <li>- Increase in exports</li> <li>- Increase in employment (higher incomes - C)</li> <li>- Reduced interest rates (increases borrowing - C)</li> <li>- Decrease in exchange rate (increases X)</li> </ul>
21. <b>The Business Cycle</b>	<ul style="list-style-type: none"> <li>- Fluctuations in actual growth</li> <li>- Never 100% efficient due to unemployment, low productivity etc</li> <li>- Output gap is difference between potential and actual</li> <li>- Trend output is the average from which the GDP fluctuates around</li> <li>- LEDCs (lower GDP) have a steeper trend output than MEDCs (higher GDP)</li> </ul>	26. <b>Causes of growth - AS</b>	<ul style="list-style-type: none"> <li>- Increase in productivity</li> <li>- Increase in labour market flexibility (occupational mobility)</li> <li>- Increase in migration (larger workforce)</li> <li>- Increase in competition (within workforce = increase productivity)</li> <li>- Increase in capital stock (increased potential)</li> </ul>
22. <b>Capital account</b>	<ul style="list-style-type: none"> <li>Capital flows</li> <li>- Direct investments (factories, mergers and acquisitions)</li> <li>- Financial investment - savings in stocks and bonds</li> <li>- Currency trading</li> </ul>	27. <b>Causes of Inflation</b>	<ul style="list-style-type: none"> <li>- Demand Pull: Increase in demand leads to firms increasing prices to take advantage and maximise profit. Causes an increase in AD (aggregate demand)</li> <li>- Cost Push: Increase in the costs (labour, raw materials, imported costs etc) of producing a product are pushed on to the consumer pushing up prices to maintain profits. Causes an increase in AS (aggregate supply)</li> </ul>
		28. <b>Causes of Unemployment (supply side)</b>	<ul style="list-style-type: none"> <li>- Occupational: when employment is available but people are not willing to look for jobs, don't have the skills</li> <li>- Geographical: inability to move from one area to another</li> <li>- Imperfect info about job opportunities</li> <li>- Real wages too high</li> </ul>

29. **Circular flow of income**
- Where supply = demand determines price of something
  - Factors: Tax, Investment, Savings, Spending
  - Withdrawals/Leakages (net saving, net taxes, import expenditure)
  - Injections (Investment, government expenditure, export expenditure)
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30. **Claimant Count**
- Those claiming job seekers allowance (must show evidence)
  - 18-65 years old
  - Have to prove you are looking for work
  - Stigma attached - people would feel embarrassed if they had to sign up leading it to become even more inaccurate
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31. **Claimant Count**
- Claiming job seekers allowance
  - 18-65 years old
  - Have to prove that you are looking for work
  - Stigma attached - doesn't fully reflect unemployed
- 
32. **Classical AS Curve (LRAS)**
- LRAS is totally inelastic (vertical)
  - Believe markets will clear so firms will produce to the maximum capacity of the economy whatever the rate of inflation/price level
  - There will be no unemployed resources (max capacity)
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33. **Consequences/costs of inflation**
- Money loses its value (confidence decreases as value of savings decreases - saving rate lower than inflation rate)
  - Wage-price spiral (prices inc., wages demanded inc. - spirals out of control)
  - Consumers and businesses on fixed incomes lose out because their real income falls (poor bargaining position)
  - Inflation writes off debts
  - Lower capital investment (business planning disrupted)
  - Unemployment
  - High IRs - stagnation leading to recession
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34. **Consumer Price Index (CPI)**
- Measurement of Inflation
  - Basket of 700 goods from a survey of 7000 households
  - Monthly
  - Weighted average (sum of price x weight) / (sum of weights)
  - Basket is updated
  - Doesn't include mortgage

35. **Consumption**
- Largest component of AD
  - Most important in determining disposable income
  - APC (average propensity to consume): proportion of income that you spend (ratio of C to income)
  - MPC (marginal propensity to consume): proportion of an income increase that you spend (proportion of income increase devoted to C)
  - As income rises, APC falls (people already have enough so don't spend as much)
  - Lower income households have higher MPC than richer households
  - Benefits capped to reduce C
  - High inflation means spending decisions are brought forward so C increases (opposite for deflation)
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36. **Consumption Definition**
- Disposable income minus tax and adding on any transfer payments (benefits)
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37. **Cost-push inflation definition**
- When the cost of production is increasing
  - Firms have to offload cost on to price (best done when the market price is inelastic)

38. **Cost-push inflation diagram (Classical view)**

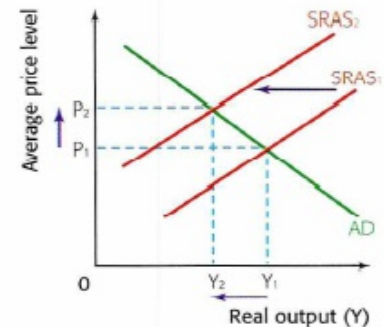


Figure 18.3 Cost-push inflation

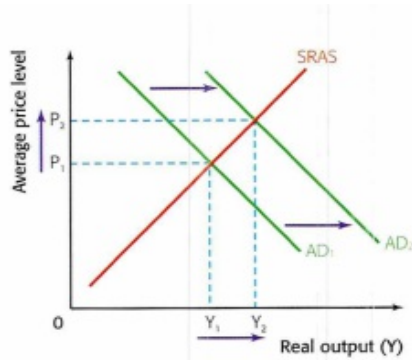
- LRAS would be a straight line at Y1

39. **Cost-push inflation diagram (Keynesian view)**

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40. <b>Costs of growth</b>	<ul style="list-style-type: none"> <li>- Not all income distributed evenly (rich own the factors of production)</li> <li>- Wealth in the hands of a few (growth increases the value of assets mainly held by rich)</li> <li>- Trickle down effect doesn't always work (tax avoidance)</li> <li>- Corruption may limit redistribution effects (regimes keep money rather than giving to people) (Nepitism = jobs kept within family members etc)</li> <li>- Growth could be spent on weapons which don't directly benefit the population (e.g. Syria)</li> <li>- Negative externalities (env damage from more factories, waste, overproduction, transport, use of scarce resources)</li> </ul>	45. <b>Costs of Unemployment to the economy</b>	<ul style="list-style-type: none"> <li>- Lower tax revenues - VAT (less disposable income), Cooperation tax (decrease in profits) and Income tax (less people are working)</li> <li>(government have less money leading to loans which are unsustainable)</li> <li>- Higher benefit payments (job seeker allowance, income support and pensions)</li> <li>- Social Costs (crime, family breakdowns, regional decay)</li> <li>- Opportunity Cost of potential output (what they could have produced - larger output gap)</li> </ul>
41. <b>Costs of inflation</b>	<ul style="list-style-type: none"> <li>- Menu costs: changing prices of goods</li> <li>- Wealth costs: affects those on fixed incomes redirecting wealth to those in bargaining positions or those with physical assets</li> <li>- Planning costs: businesses uncertain about the future price changes aren't as likely to invest impacting economic growth</li> <li>- Fall in Competitiveness: inflation at a higher rate in one country means it is less competitive and affects the balance of payments</li> <li>- Social Instability: In extreme cases, confidence in the currency is nul so production and exchange stalls leading to food riots, stealing and riots</li> </ul>	46. <b>Costs of Unemployment to the individual</b>	<ul style="list-style-type: none"> <li>- De-skilling (structural unemployment)</li> <li>- Loss of self-esteem</li> <li>- Lower Income (reducing purchasing power and lower standard of living)</li> <li>- Effects on family unit</li> <li>- Increase in stress related illnesses and mental breakdown (E.g. 3,000 suicides from the benefits being cut)</li> </ul>
42. <b>Costs of Unemployment on businesses</b>	<ul style="list-style-type: none"> <li>- Negative multiplier effect</li> <li>- Fall in demand for goods and services as incomes fall</li> <li>- Fall in demand for businesses further down supply chain</li> <li>- Quantity of labour decreases</li> <li> </li> <li>- +ve: bigger pool of surplus labour, less pressure to pay higher wages, reduced trade union/strike power</li> </ul>	47. <b>CPI</b>	<ul style="list-style-type: none"> <li>- Consumer Price Index</li> <li>- Average price of a bundle of 700 goods and services measured at different points in time from a sample of 7000 households</li> <li>- Each household completes a living costs and food survey</li> <li>- Each good is weighted so that the ones which we purchase more of are worth more in the overall calculation</li> </ul>
43. <b>Costs of Unemployment on government</b>	<ul style="list-style-type: none"> <li>- Increased spending on unemployment benefits (OC)</li> <li>- Fall in tax revenues from spending</li> <li>- Fall in corporation tax - less profits</li> <li>- May lead to more gov borrowing (budget deficit)</li> </ul>	48. <b>Current account</b>	<ol style="list-style-type: none"> <li>1) Trade in goods</li> <li>2) Trade in services</li> <li>3) Net flow of investment income</li> <li>4) Transfers of money</li> </ol>
44. <b>Costs of Unemployment on individual</b>	<ul style="list-style-type: none"> <li>- Loss of income</li> <li>- Fall in living standards</li> <li>- Health risks</li> <li>- Social alienation</li> <li>- Loss of marketable skills</li> </ul>	49. <b>Cyclical/demand deficit unemployment</b>	<ul style="list-style-type: none"> <li>- Fall in AD relative to potential GDP leading to a loss of RNO, employment</li> <li>- Labour is a derived demand - AD falls therefore labour falls</li> </ul>
		50. <b>Definition of money</b>	<ul style="list-style-type: none"> <li>- M0 to M4</li> <li>- Narrow money M0</li> <li>- Broad money M4</li> <li>- Near money</li> <li>- A rise in any might cause a rise in AD</li> </ul>
		51. <b>Delay in unemployment (lagged indicator)</b>	<ul style="list-style-type: none"> <li>- Unemployment is a lagged indicator</li> <li>- Expensive to pay off contracts</li> <li>- Cost of rehiring &amp; training is expensive</li> <li>- Cut wages to pay off debt</li> </ul>
		52. <b>Demand for money (MD)</b>	<ul style="list-style-type: none"> <li>- The amount people wish to hold as cash as opposed to other assets</li> </ul>
		53. <b>Demand-pull inflation definition</b>	<ul style="list-style-type: none"> <li>- When there is excess AD (positive output gap)</li> <li>- Firms raise prices to make the most of high demand</li> <li>- Mainly in Boom phase</li> </ul>

**54. Demand-pull inflation diagram (classical view)**



- LRAS would be a straight line at  $Y_1$

**55. Demand-pull inflation diagram (Keynesian view)**

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**56. Demand-side factors considered by the MPC (eval)**

- Real GDP growth (growth means inflation)
- Estimate of output gap (if negative = deflation)
- AD components (C, G & X-M etc)
- House prices (wealth effect)
- Unemployment
- Money & credit data
- Business and consumer confidence

**57. Demand side factors effecting GDP (mainly SR)**

- Changes in business confidence
- Changes in consumer confidence
- Changes in any component of AD
- Changes effecting UK's trading partners
- UK monetary and fiscal policy (IRs and taxes)

**58. Disposable income**

- Income minus tax, adding on any benefits (transfer payments - payments which are received in exchange for nothing)

**59. Economic Growth**

- The country can produce more
- Incomes rise increasing spending power
- Increased consumer spending power encourages firms to produce more

**60. Economic Growth Definition**

- AS: expansion of the productive capacity of an economy
- AD: increase in total value of goods and services produced in an economy in any given year

**61. Effects of fall in exports on economy**

- AD falls as X falls
- Negative multiplier
- Slowdown/recession
- Reduced profits
- Reduced producer confidence (could lead to reduced capital investment)
- Unemployment (jobs & plants/resources)
- Tax revenues decrease (less G, AD falls)
- Might worsen regional inequality (some regions more reliant on exports)

**62. Effects on Investment (4 things)**

- Firms invest past profits but at an OC
- Increase of productive capacity (Capital stock is prod. plant and machinery)
- Interest rates rise: 1) Cost of borrowing inc. (puts off investment) 2) OC of investing past profits inc. (as profits could be saved in interest bearing account)
- Inflation: high inflation (boom) = uncertainty = discourages investment

**63. Evaluation of fiscal policy**

- Depends on which rate of income tax is changed (MPC increases for poor)
- Range of goods covered by VAT
- Changing rules about how tax is paid
- Recognition lags and policy time lags (takes time to recognise, implement and have an effect)
- Imperfect information (may stimulate a bubble - overstimulate demand)
- Crowding out (increase in government spending means private firms have to raise cost of borrowing therefore reducing private investment)

**64. Expenditure switching (to make exports more competitive)**

- Depreciation of the exchange rate - decreases price of exports (eval: depends on elasticity & may end up reducing BOP)
- Reducing relative inflation - exports appear cheaper/imports more expensive
- Campaigns ("buy British")
- Structural change - Supply-side reforms to raise productivity and lower unit labour costs
- Subsidies to businesses - increases R & D + infrastructure

**65. Factors considered when manipulating IRs**

- Strength of AD (too much demand = demand pull inflation, too little = recession/deflation)
- Housing market (prices too strong = demand pull inflation, weak could lead to recession - 2009)
- Labour market (wage spirals? If so, IRs rise to discourage firms from raising wages above inflation levels)
- Inflation from overseas (import costs - e.g. oil)
- Trends in the exchange rates (SPICED)

**66. Factors effecting SRAS**

- Skills of workforce
- Efficiency of capital
- Quantity of capital
- Cost of raw materials
- Cost of workforce

**67. Factors effecting trade**

- Exchange rates (SPICED)
- Inflation (High inflation = less competitive)
- Income (High UK income = more imports, high foreign income = more exports)
- Investment (increases productivity increasing exports but could also reduce exports because the cost may be passed onto the consumer)



68. <b>Factors effecting trade (4 things)</b>	<ul style="list-style-type: none"> <li>- Exchange Rates (inc. means exports less competitive - appear more expensive) SPICED</li> <li>- Inflation (inc. inflation means red. competitiveness)</li> <li>- Income (disposable income inc. leads to more imports)</li> <li>- Investment (inc. investment means better quality goods but more expensive)</li> </ul>	77. <b>GDP (National income, national output or aggregate demand)</b>	<ul style="list-style-type: none"> <li>- Total value of all goods and services produced in a year</li> <li>- Primary (agriculture), secondary (manufacturing) and tertiary (services) sectors</li> <li>- Real GDP is adjusted for inflation</li> <li>- Nominal GDP has not been adjusted for inflation</li> <li>- Value = price x quantity</li> </ul>
69. <b>Factors on Consumption (4 things)</b>	<ul style="list-style-type: none"> <li>- Wealth of households (property, shares)</li> <li>- Wealth effect on consumption (more wealth, confidence, consumption)</li> <li>- Inflation brings consumption (spending decisions) forward</li> <li>- Interest rates rise 1) Cost of borrowing inc. 2) Benefits of saving inc. 3) Value of assets may rise</li> </ul>	78. <b>Government Expenditure</b>	<ul style="list-style-type: none"> <li>- All Gov. spending</li> <li>- Budget Deficit: Gov spends more than it receives</li> <li>- Budget Surplus: Gov receives more than it spends</li> </ul>
70. <b>Factors shifting AS right (increasing productive capacity)</b>	<ul style="list-style-type: none"> <li>- Migration</li> <li>- Technology advances</li> <li>- Capital goods</li> <li>- More resources (land)</li> <li>- (Think factors of production)</li> </ul>	79. <b>Government Expenditure (E)</b>	<ul style="list-style-type: none"> <li>- Budget Deficit: when government spends more than it receives (taxes)</li> <li>- Budget Surplus: when the government spends less than it receives</li> <li>- Government spending = autonomous (acts independently within AD)</li> </ul>
71. <b>Falling Unemployment leads to...</b>	<ul style="list-style-type: none"> <li>- Circular flow of income grows</li> <li>- Positive multiplier</li> <li>- Increase in demand for M</li> <li>- Higher tax revenues</li> <li>- Inflation</li> </ul>	80. <b>Growth effecting Welfare</b>	<ul style="list-style-type: none"> <li>- Increased growth means government can supply more welfare</li> <li>- Pensions</li> <li>- Benefits (sickness, disability)</li> <li>- Support (maternity, holidays)</li> <li>- Housing</li> <li>- Infrastructure (homes for elderly)</li> <li>- Funded by taxes</li> </ul>
72. <b>Fiscal policy definition</b>	<ul style="list-style-type: none"> <li>- Influencing the level of economic activity through manipulation of government income and expenditure (shifting AD)</li> </ul>	81. <b>How IRs effect asset prices</b>	<ul style="list-style-type: none"> <li>- Higher interest rates increase return on savings in banks - discourages investment in alternatives such as property or shares</li> <li>- Wealth effect: if demand for assets fall, the asset holders lose out and therefore spending confidence</li> <li>- Vice Versa</li> </ul>
73. <b>Fiscal policy diagram</b>	...	82. <b>How IRs effect cash flow (amount of cash consumers have available)</b>	<ul style="list-style-type: none"> <li>- Increases the amount of money savers have from interest-bearing accounts or building societies</li> <li>- Increases the amount people who take out loans have to pay back</li> <li>- Vice Versa</li> </ul>
74. <b>Fiscal policy effects on AS (in LT)</b>	<ul style="list-style-type: none"> <li>- Influences AD in ST but AS in LT</li> <li>- Education and health (productivity + capacity increases)</li> <li>- Poverty reduction (Increased benefits)</li> <li>- Welfare reform (decreased benefits)</li> <li>- Investment (capital goods increase)</li> </ul>	83. <b>How IRs effect exchange rates</b>	<ul style="list-style-type: none"> <li>- Hot money flows: if IRs in UK increase compared to other countries, attracts foreign investors (strengthens the £)</li> <li>- Can be influenced by speculation that might not actually happen</li> <li>- Vice Versa</li> </ul>
75. <b>Frictional Unemployment</b>	<ul style="list-style-type: none"> <li>- Unemployment between jobs</li> <li>- Includes new and returning entrants (e.g. starting a family)</li> <li>- Information flows decrease unemployed time</li> <li>- Effected by incentives (min wage) and disincentives (benefits) to look for work</li> <li>- Good for economy because pool of workers keeps wage inflation down</li> </ul>	84. <b>How IRs effect spending and saving decisions</b>	<ul style="list-style-type: none"> <li>- Attractiveness of spending today compared to tomorrow</li> <li>- Inc. leads to saving more attractive and borrowing less attractive (reduces C &amp; I)</li> <li>- Vice Versa</li> </ul>
76. <b>GDP</b>	<ul style="list-style-type: none"> <li>- The total value of output of goods and services produced in the UK in a year</li> <li>- Can be used to measure national income, national output and AD</li> <li>- GDP per capita = GDP per head</li> <li>- GNP is all money earned including UK businesses abroad</li> </ul>		

85. <b>How LRAS works</b>	1) AD curve shifts right (inc. C) 2) SRAS shifts left (workers demand higher wages) 3) AD shifts left (prices increase to pay for higher wages) 4) SRAS shifts right (wages cut due to decreased C)	93. <b>Inflation</b>	- The sustained increase in the general price level over a period of time - Measures your purchasing power so if inflation increases, prices increase meaning you have less purchasing power - Doesn't fall (deflation) - Disinflation is the decrease in inflation - Affects the outcome of economic decision making. If it's anticipated, changes in prices can accommodate the changes in prices, if un-anticipated, it can cause shocks and problems arise
86. <b>How to reduce expenditure</b>	- Increase direct taxes - Increase IRs - Higher import tariffs - Decrease benefits - All could have a negative impact on AD	94. <b>Inflation Definition</b>	- A sustained increase in the general/average price level of a country - Government target is 2% +/-1
87. <b>Hyperinflation</b>	- Ridiculously high demand for cash - Money becomes worthless - Same effect of collapse of consumer and business confidence in a recession - Savings become worthless	95. <b>Inflation in a recession</b>	- Low inflation/deflation - Prices fall to attract C - Exchange rate decreases in recession
88. <b>ILO</b>	- Out of work for 4 weeks, ready to start in 2 - Face to face interview then phone survey of 60,000 households (regional issues) - 16 to 65 year olds - Takes into account students looking for part time work (not wholly accurate)	96. <b>An injection</b>	- Exports - Goods and services sold abroad with funds coming into UK - Raises AD
89. <b>ILO (International Labour Organisation)</b>	- Out of work for 4 weeks, ready to return in 2 - Face to face interview then phone survey of 60,000 households - 16 to 65 year olds - Published once a month so is out of date - 60,000 people is only a small proportion of the UK pop and also people could lie as it is a survey	97. <b>Interest Rates</b>	- Direct and indirect effect on C - If IRs increase, borrowing (C) decreases - less affordable - IRs increase, C decreases - more beneficial to save - IRs increase, value of assets may rise so more money to spend increasing C
90. <b>Impacts of IR changes</b>	- Effects different industries & sectors - Elasticity of demand (e.g. food sector) - Trading sector (exchange rates) - Regional economies - Impacts/benefits savers/borrowers	98. <b>Interest Rates on AD</b>	- Prices low, IRs tend to be low - IRs tend to follow price level - Therefore a rise in price level/IRs = decreased AD
91. <b>Importance of exports</b>	- Boosts GDP (30% of UK GDP) - UK 2nd largest exporter of services - Jobs created down the line - Regional economies (some regions more dependent than others on exports) - Injection of AD	99. <b>Interest Rate Transmission mechanism</b>	- The process by which a change in interest rates feeds through to AD - Individuals, firms (unemployment), mortgages, savings, exchange rates (SIMFER)
92. <b>Increasing economic growth</b>	- Firms increasing capital goods by building more factories and machinery (LT) - Government or firms spending more on education or training (LT) - Spending on infrastructure (ST) - Firms investing in research and development (new tech) (ST) - Government subsidies and banks investing in firms	100. <b>Investment Definition</b>	- Expenditure undertaken by firms to add to capital stock
		101. <b>Investment (I)</b>	- Expenditure undertaken by firms to add to capital stock (machinery and plants) - Increases economy's productive capacity - Firms can use past profits to invest - an opportunity cost - If IRs increase, borrow decreases so investment may be put off - If IRs increase, investment using past profits may increase because they can be put into a high interest bearing account - Amount invested depends on the expected return (point on business cycle - best at upturn) - High inflation = uncertainty = discourages investment

102. <b>Keynesian AS Curve</b>	<ul style="list-style-type: none"> <li>- Curve = SRAS</li> <li>- Vertical line = LRAS</li> <li>- Flat line = recession (price level stays same even though RNO is increasing)</li> <li>- Unemployment is distance between horizontal and vertical parts on the curve</li> </ul>	110. <b>Monetary policy definition</b>	<ul style="list-style-type: none"> <li>- Attempts to influence the level of economic activity (AD) through changes to the amount of money in circulation and the price of money</li> <li>- IRs &amp; Quantitative easing</li> <li>- Used to control inflation (+2%)</li> <li>- Official rate ('base rate') set by the B of E influences the structure of other IRs</li> <li>- Eval: has little effect on LRAS, fiscal policy also has an impact, changes in rates depend on anticipation, confidence &amp; the world economy</li> </ul>
103. <b>Length of time for IRs to have an impact</b>	<ul style="list-style-type: none"> <li>- A change in the official Bank Rate takes about 2 years to have its full impact on inflation (due to fixed wages, contracts, credit cards, fixed IRs)</li> <li>- Exchange rate changes have instant effects on C</li> <li>- Mortgages and savings take longer to have an effect on C</li> </ul>	111. <b>Monetary policy diagram</b>	<ul style="list-style-type: none"> <li>- Manipulates AD only meaning only inflation is affected and nothing else</li> </ul>
104. <b>Limitations of CPI</b>	<ul style="list-style-type: none"> <li>- Not accurate representation of whole economy (doesn't take into account top and bottom 4% - however this does remove abnormalities)</li> <li>- An average (people's spending habits different - vegetarians)</li> <li>- Doesn't include mortgage payments</li> </ul>	112. <b>The Multiplier</b>	<ul style="list-style-type: none"> <li>- The ratio of the change in real income to the amount of expenditure (spend £1bil on HS2 and get £5bil back in increased productivity, trade, communication etc)</li> <li>- Greater return on investment (ROI) (positive multiplier)</li> <li>- Depends on the size of the withdrawals and leakages (how much of increased income is saved, spent on imports or taxed)</li> </ul>
105. <b>Limitations of manipulating IRs (eval)</b>	<ul style="list-style-type: none"> <li>- Time lags (IRs always take 18-24mths to have an impact - not have effect in ST) doesn't directly determine inflation</li> <li>- Fixed rate mortgages</li> <li>- Rented property owners see no impact</li> <li>- Credit-card lenders may not change rates immediately</li> <li>- If businesses are running with spare capacity, a fall in rates may not lead to increased capital investment)</li> <li>- Many sources of capital funding are on fixed rates</li> <li>- Lower IRs cause saver's disposable incomes to fall</li> </ul>	113. <b>The Multiplier Effect Definition</b>	<ul style="list-style-type: none"> <li>- Equilibrium output changes by more than the original increase in expenditure</li> <li>- E.g. Gov Exp leads to improvements which then lead to other improvements (e.g. income boost) more than the original expenditure</li> </ul>
106. <b>Loose monetary policy</b>	<ul style="list-style-type: none"> <li>- When IRs are low to encourage spending (e.g. when inflation is below target)</li> </ul>	114. <b>Multiplier effect definition</b>	<ul style="list-style-type: none"> <li>- When the change in AD is greater than the autonomous change which brought it about</li> </ul>
107. <b>Macroeconomic costs of unemployment</b>	<ul style="list-style-type: none"> <li>- Loss of output (inside PPF)</li> <li>- Market failure (labour not efficiently allocated)</li> <li>- Labour leaves force permanently - LT (fall in potential GDP)</li> <li>- Increase in inequality</li> </ul>	115. <b>Nominal Growth</b>	<ul style="list-style-type: none"> <li>- Growth in output not including any adjustment for price changes expressed as 'current prices' (price at time of measurement)</li> </ul>
108. <b>Marginal propensity to consume (MPC)</b>	<ul style="list-style-type: none"> <li>- Proportion of income increase spent on Consumption (proportion of pay increase you spend)</li> </ul>	116. <b>Nominal Growth (economic growth)</b>	<ul style="list-style-type: none"> <li>- The growth in output not including any adjustment for price changes (inflation) expressed as 'current prices'</li> <li>- The price used is the price at the time of the measurement</li> </ul>
109. <b>Measure of Economic Performance</b>	<ul style="list-style-type: none"> <li>- Inflation</li> <li>- Unemployment</li> <li>- Growth (GDP)</li> <li>- Balance of Payments</li> <li>- Sustainable Growth</li> <li>- Income Equality</li> </ul>	117. <b>Nominal Value</b>	<ul style="list-style-type: none"> <li>NOMINAL = Real + inflation</li> <li>- Doesn't include inflation in its value</li> <li>- Based on current prices</li> </ul>
		118. <b>Opportunity cost of growth</b>	<ul style="list-style-type: none"> <li>- Depends on the type of country (level of development)</li> <li>- Necessity of generating growth by using resources (scarce resources)</li> <li>- Makes population poorer in SR because there are less consumer goods available at first</li> <li>- Sacrifice vs Gain</li> </ul>
		119. <b>Policies to reduce trade gap</b>	<ul style="list-style-type: none"> <li>- Self-correcting - Cyclical (as demand falls, imports fall)</li> <li>- Lower exchange rate (time lag and doesn't work if inelastic)</li> <li>- Above can be done by:               <ol style="list-style-type: none"> <li>1) Expenditure-reduction (reducing AD)</li> <li>2) Expenditure-switching (changing the UK's relative prices)</li> </ol> </li> </ul>



120. <b>Policies to reduce unemployment (demand side)</b>	<ul style="list-style-type: none"> <li>- Lower IRs</li> <li>- Lower direct taxes</li> <li>- Gov spending on infrastructure/projects (direct employment)</li> <li>- Employment subsidies (New Deal)</li> <li>- Incentives to encourage foreign investment in UK (create high skilled jobs)</li> </ul>	131. <b>Real wage unemployment</b>	<ul style="list-style-type: none"> <li>- Real wages above market eqm (wages are too high so market can't clear - excess supply of labour e.g. national min wage in regional areas)</li> <li>- Causes: trade unions (drive wages above FM level), rise in min wage (labour shedding in labour intensive industries), globalisation (good cheaper elsewhere)</li> </ul>
121. <b>Policies to reduce unemployment (supply side)</b>	<ul style="list-style-type: none"> <li>- Increased spending on education and training</li> <li>- Increase info on job vacancies</li> <li>- Changes to tax and benefits - incentives to look for work</li> <li>- Reduce trade union powwe</li> </ul>	132. <b>Reasons for a trade deficit (demand side) - mainly ST</b>	<ul style="list-style-type: none"> <li>- Stronger economy than trading partners (e.g. euro zone countries still in recession)</li> <li>- High marginal propensity to import due to lack of domestic substitutes &amp; high levels of borrowing (need to import)</li> <li>- Strong exchange rate</li> </ul>
122. <b>Potential benefits of Unemployment</b>	<ul style="list-style-type: none"> <li>- There is now an excess in supply of labour</li> <li>- Downward pressure on labour - people are willing to do a job whatever the salary is like (benefits capital owners)</li> <li>- Businesses gain by paying out less wages</li> <li>- Productivity may also rise as workers are scared of losing their jobs</li> </ul>	133. <b>Reasons for a trade deficit (supply side/structural) - mainly LT</b>	<ul style="list-style-type: none"> <li>- Insufficient capacity from producers (LT = deindustrialisation)</li> <li>- Inadequate non-price competitiveness (quality) - research and development gap + lack of investment on innovation and design</li> <li>- Changing comparative advantage in the global economy (emergence of lower cost competition - China)</li> </ul>
123. <b>Potential growth</b>	<ul style="list-style-type: none"> <li>- The overall capacity of the economy if it used all of its resources 100% efficiently</li> </ul>	134. <b>Reasons for low inflation</b>	<ul style="list-style-type: none"> <li>- Low cost-push pressures (wage demands, shocks, expectation, improved tech)</li> <li>- Low demand-pull pressures (recession, greater competitive pressure in many industries)</li> <li>- Strong pound</li> <li>- Expectations of inflation fallen</li> </ul>
124. <b>Potential Growth (economic growth)</b>	<ul style="list-style-type: none"> <li>- The overall capacity of the economy (how much it could produce if it used all of its resources)</li> </ul>	135. <b>RPI</b>	<ul style="list-style-type: none"> <li>- Retail Price Index</li> <li>- Used prior to CPI</li> <li>- Includes mortgage interest payments which the CPI doesn't</li> <li>- More useful on a national scale but CPI is used when comparing to other countries</li> <li>- May fall in comparison to the CPI for instance due to a fall in interest rates</li> </ul>
125. <b>Problems of a persistent trade 'payments deficit'</b>	<ul style="list-style-type: none"> <li>- Structural weakness - sign of LT loss of competitiveness within the international markets (manufacturing + exports low)</li> <li>- Unbalanced economy - more M than X (high consumer spending vs low industrial sector)</li> <li>- Unemployment</li> <li>- Loss of output</li> <li>- Cost push inflation - lower exchange rate (M more expensive = inflation) eval: current low oil prices</li> </ul>	136. <b>Seasonal Unemployment</b>	<ul style="list-style-type: none"> <li>- Seasonal changes in labour demand/employment</li> <li>- Only effects certain industries so doesn't effect whole economy</li> </ul>
126. <b>Production Factors</b>	<ul style="list-style-type: none"> <li>- Land</li> <li>- Labour</li> <li>- Capital</li> </ul>	137. <b>Shifts in AD</b>	<ul style="list-style-type: none"> <li>- Caused when RNI rises but price level stays the same</li> <li>- Inc. national income - economic growth</li> </ul>
127. <b>Purchasing power of income on AD</b>	<ul style="list-style-type: none"> <li>- Prices low, purchasing power is high (you can do more with income)</li> <li>- Low prices indicate high levels of income</li> <li>- Assuming ceteris paribus, suggests inc. C and leading to increasing national income</li> </ul>	138. <b>SRAS Curve Definition</b>	<ul style="list-style-type: none"> <li>- The total production of goods and services available in an economy at different price levels while some resources produced are fixed</li> <li>- Upward sloping</li> <li>- When prices increase, employees will naturally work harder increasing RNO</li> </ul>
128. <b>Real Growth</b>	<ul style="list-style-type: none"> <li>- Growth in GDP taking into account changes of the price level expressed as 'constant prices'</li> </ul>	139. <b>SRAS &amp; LRAS</b>	<ul style="list-style-type: none"> <li>- Classical LRAS curve (vertical/completely inelastic because in the LR, markets will clear meaning no unemployed resources meaning whatever inflation, LRAS will remain the same)</li> <li>- Keynesian curve (flat bit = SRAS, steep bit = LRAS)</li> </ul>
129. <b>Real Growth (economic growth)</b>	<ul style="list-style-type: none"> <li>- Growth in output including adjustments (inflation) to take into account the price level expressed as 'constant prices'</li> </ul>		
130. <b>Real value</b>	<ul style="list-style-type: none"> <li>REAL = Nominal - inflation</li> <li>- Takes into account the changes of prices of goods due to inflation</li> <li>- Based on changing prices over time</li> </ul>		

140. <b>Structural Unemployment</b>	<ul style="list-style-type: none"> <li>- Due to changes in focus of economy</li> <li>- Mismatch of skills</li> <li>- Involuntary unemployment</li> <li>- Occupational immobility (major cause)</li> <li>- Long-term unemployment</li> <li>- Regional decay</li> <li>- To reduce it, keep people in education</li> </ul>	148. <b>Supply side policy definition</b>	<ul style="list-style-type: none"> <li>- Intention to shift AS curve right increasing the LT productive capacity of the economy with minimal impact in ST</li> <li>- Impact productivity and efficiency by opening up markets</li> </ul>
141. <b>Supply of money (MS)</b>	<ul style="list-style-type: none"> <li>- The amount of money in circulation in the economy</li> </ul>	149. <b>Tight monetary policy</b>	<ul style="list-style-type: none"> <li>- When IRs are high to restrict spending (e.g. when inflation is above target)</li> </ul>
142. <b>Supply-side factors considered by the MPC (eval)</b>	<ul style="list-style-type: none"> <li>- Wages and earnings</li> <li>- Unit labour costs (cost of labour)</li> <li>- Labour shortages</li> <li>- Import prices</li> <li>- Commodity prices</li> </ul>	150. <b>Trade in Goods and Services</b>	<ul style="list-style-type: none"> <li>- Exports: injections that raise AD (goods and services sold abroad)</li> <li>- Imports: withdrawals that lower AD (goods and services bought abroad)</li> </ul>
143. <b>Supply side factors effecting GDP (mainly LR)</b>	<ul style="list-style-type: none"> <li>- Size of population</li> <li>- Productivity increase</li> <li>- Investment</li> <li>- Increasing potential (capital goods)</li> </ul>	151. <b>Trade in oil</b>	<ul style="list-style-type: none"> <li>- UK was importer until 1970s (North Sea oil turned UK into an exporter)</li> <li>- Early high surpluses in 80s diminish as NS oil decreases</li> <li>- UK is now a net importer again</li> </ul>
144. <b>Supply side government policies - Education &amp; training</b>	<ul style="list-style-type: none"> <li>- Reform of 14-19 education</li> <li>- Apprenticeships</li> <li>- Expansion of vocational qualifications</li> <li>- Expansion of university access</li> </ul>	152. <b>Trade on AD</b>	<ul style="list-style-type: none"> <li>- Assuming Ceteris Paribus, when UK prices low compared to foreign countries = more competitive</li> <li>- Opposite of SPICED</li> <li>- Therefore national income rises (AD rises)</li> </ul>
145. <b>Supply side government policies - Incentives and technology</b>	<ul style="list-style-type: none"> <li>- Cutting corporation tax</li> <li>- Subsidies to develop new technology - investment</li> <li>- Regional policies to encourage enterprise, investment, location , expansion</li> <li>- Privatisation</li> </ul>	153. <b>Types of tradeable goods</b>	<ul style="list-style-type: none"> <li>- Consumer durables (household goods, motor vehicles, PCs)</li> <li>- Capital goods / technology / software</li> <li>- Commodities (oil and other fuels)</li> <li>- Components &amp; basic raw materials</li> <li>- Foodstuffs and beverages</li> </ul>
146. <b>Supply side government policies - Labour market</b>	<ul style="list-style-type: none"> <li>- Deregulation (remove 'red tape' restrictions and bureaucracy)</li> <li>- Reduce trade union power (less strikes - productivity inc., reduced bargaining power - productivity inc./dec., working conditions fall - demotivation)</li> <li>- Flexible labour markets (0 hour contracts - reduces firm's costs, may reduce AD because unstable income)</li> <li>- Contracts (ST contracts promote fear of sack, may reduce incentive to work)</li> <li>- Terms and conditions (performance incentives - company car etc)</li> <li>- Pay</li> </ul>	154. <b>Types of tradeable services</b>	<ul style="list-style-type: none"> <li>- Tourism &amp; travel (inc. civil aviation)</li> <li>- Insurance and business consultancy services</li> <li>- Banking and accountancy services</li> <li>- Data processing &amp; other information services</li> <li>- Music &amp; entertainment</li> <li>- Shipping</li> </ul>
147. <b>Supply side government policies - Tax &amp; welfare reform</b>	<ul style="list-style-type: none"> <li>- More strict benefit regime (application: £3,500 disability benefit decrease)</li> <li>- Reduce income tax (incentive to work - gap between workers and non widens, increase labour supply, however real incomes may fall AD falls)</li> <li>- Increase min wage (incentive to work)</li> <li>- Increase retirement (increase productive capacity, decrease pension payments, however less work for students)</li> <li>- 'New Deal' scheme (help young into jobs)</li> <li>- Decrease min wage</li> </ul>	155. <b>Types of Unemployment</b>	<ul style="list-style-type: none"> <li>- Frictional Unemployment: ST unemployment between jobs</li> <li>- Demand Deficient/Cyclical Unemployment: When in a recession, demand decreases meaning labour is derived leading to unemployment</li> <li>- Technological Unemployment: Changes in technology lead to people put out of a job</li> <li>- Seasonal Unemployment: Caused by the seasonal nature of some types of employment</li> <li>- Real Wage or Classical Unemployment: wage levels too high for firm to afford (above the market clearing level)</li> <li>- Structural Unemployment: LT unemployment caused by changes in the structure of industry in the economy (skills mismatch, closing down mines to invest in services, closing down call centres to other countries where labour is cheaper)</li> </ul>
		156. <b>UK Performance</b>	<ul style="list-style-type: none"> <li>- Recession is two consecutive periods of negative economic growth</li> </ul>

157. <b>Unemployment</b>	<ul style="list-style-type: none"> <li>- The number of people of working age out of a job</li> <li>- Problems: defining working age, housewives/husbands, disabled, survery</li> <li>- Measured from the Claimant Count and ILO</li> </ul>
158. <b>Unemployment definition</b>	<ul style="list-style-type: none"> <li>- People able, available and willing to find work actively seeking work - but not employed</li> <li>- Claimant Count</li> <li>- Labour Force Survey (ILO)</li> </ul>
159. <b>Unemployment Diagram</b>	<ul style="list-style-type: none"> <li>- AD shifts left</li> <li>- Unemployment is the distance between Y and Y1</li> </ul>
160. <b>Wealth Effect</b>	<ul style="list-style-type: none"> <li>- Dependent on the wealth of households (property, shares)</li> <li>- If wealth increases, confidence increases because households have more money to fall back on, this means that consumers will spend more increasing C</li> </ul>
161. <b>What determines size of multiplier</b>	<ul style="list-style-type: none"> <li>- Size of withdrawals &amp; leakages</li> <li>- How much of increased income is saved</li> <li>- How much is spent on imports</li> <li>- How much of inc income is taxed</li> </ul>
162. <b>What fiscal policy effects</b>	<ul style="list-style-type: none"> <li>- AD (taxes)</li> <li>- Unemployment</li> <li>- BOP</li> <li>- Inflation</li> <li>- Economic growth</li> </ul>
163. <b>What GDP misses</b>	<ul style="list-style-type: none"> <li>- Self-sufficiency (don't sell or buy goods)</li> <li>- Doesn't include any subtractions (harmful substances, pollution, environment degradation)</li> <li>- Doesn't include informal/black economy (subsistence farming, cash in hand, bartering &amp; illegal activities)</li> </ul>
164. <b>Why a AD curve goes from left to right</b>	<ul style="list-style-type: none"> <li>- Purchasing power (low prices = high pp = high levels of income therefore meaning increased consumption and assuming CP, increases AD increasing RNI)</li> <li>- Interest rates (low prices = low IRs, if prices rise, so do IRs, discouraging borrowing therefore spending decreasing consumption/investment/competitiveness)</li> <li>- Trade (low UK prices = more competitive, more exports meaning higher national incomes)</li> </ul>
165. <b>A withdrawal</b>	<ul style="list-style-type: none"> <li>- Imports</li> <li>- Goods and services bought abroad with an outflow of funds from UK</li> <li>- Reduces AD</li> </ul>