Chapter 5: Introduction to Macroeconomics

Week 2

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1 The Roots of Macroeconomics

2 Macroeconomics Concerns

3 Government in economy
Figure 1: Macroeconomics

This book is about **Macroeconomics**...

...which looks at issues that affect the economy of an entire country...

I see inflation, unemployment, the business cycle, economic growth, free trade...
Questions

- what is the difference between Classical econ and Keynesian econ? (2011Mid1 M6; 2012Mid1 M8)
- What is sticky price vs. flexible price? (2012Mid1 M8; 2011Mid1 M15)
- What is fine tuning? (2010Mid1 M36 Page 219)
- What is stagflation?
Classicals v.s. Keynesians

Just as in the history of music and art there has been classicalism vs romanticism with each dominating for a period of time. In economics, Classical School and Keynesian School also alternate to dominate Macroeconomics.
Keynes vs Hayek

The rival of a century: Friedrich Hayek (1899-1992) vs John Keynes (1883-1946)
According to ___________ economists, the economy is self-correcting.

A command system
B Keynesian
C Classical
D Marxist

Back
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A. command system
B. Keynesian
C. Classical
D. Marxist

Back
According to John Maynard Keynes
A an excess supply of labor would drive down wages to a new equilibrium level.
B unemployment could not persist.
C there is no role for government in the economy.
D government could intervene in the economy and affect the level of output and employment.
According to John Maynard Keynes

A. an excess supply of labor would drive down wages to a new equilibrium level. Flexible price assumption

B. unemployment could not persist. Sticky wage may lead to persistent unemployment

C. there is no role for government in the economy.

D. government could intervene in the economy and affect the level of output and employment.

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1 The Roots of Macroeconomics

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Questions

- What is Macroeconomics concerned with? (2011Mid1 M6; 2012Mid1 M8)
- What is business cycle? (2012Mid1 M6; 2012 Mid I M9; 2010Mid1 M16)
Price Level Stability

Figure 2: what has caused the fluctuation in price level?
Figure 3: We all hope economy is going to be like this
Price Level Stability

Figure 4: But sometimes it may be like this
Price Level Stability

Figure 5: Then this is going to happen
Macroeconomics is concerned with
A price level stability
B economic growth
C unemployment.
D all of these.

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Macroeconomics Concerns

2012 Mid I M7 Page 192

Macroeconomics is concerned with

A. price level stability
B. economic growth
C. unemployment.
D. all of these.

Back
Business Cycle

Figure 6: US economy in Business Cycle
Business Cycle

Figure 7: Business Cycle

- Peak
- Trough
- Recovery
- Boom
- Trend
- Contraction
- Expansion
- Time
- Real GDP
If the economy is in the **expansionary** phase of the business cycle, then

A  the rate of change in economic activity is negative.
B  there is no change in the level of economic activity.
C  the level of economic activity is negative.
D  the rate of change in economic activity is positive.
If the economy is in the **expansionary** phase of the business cycle, then

A. the rate of change in economic activity is negative.

B. there is no change in the level of economic activity.

C. the level of economic activity is negative.

D. the rate of change in economic activity is positive.
Business Cycle

In a business cycle

A. the period from a trough to a peak is called an expansion.
B. output increases and unemployment decreases in a contraction.
C. output and employment fall during an expansion.
D. the trend growth line is negative sloping.
E. the peak of a new business cycle is lower than the peak of the previous business cycle.

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Questions

- What is Fiscal Policy concerned with? (2011Mid1 M9 2010Mid1 M1)
- What is Monetary Policy concerned with?
- What is Supply Side policy? (2011Mid1 M7)
- Can you locate the three markets in Circular Flow Diagram?
The Roots of Macroeconomics

Macroeconomics Concerns

Government in economy

Government Role in Economy

Figure 8: Huge US Government Debt
Figure 9: How much money do we need?
Figure 10: Less Tax; Less Government Spending; Industry Degregulation

"IF YOU CUT TAXES ON THE RICH, THEY'LL INVEST THAT MONEY AND CREATE JOBS FOR EVERYONE!"
Supply Side Policy

2011Mid 1 M7 Page 204

__________ would advocate a policy of government reducing corporate profit taxes to encourage investment.

A  Classical economists
B  Keynesian economists
C  Marxist economists
D  Supply-side economists

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Fiscal Policy

2011 Mid I M9 Page 204;
Fiscal Policies are concerned with policies regarding __________ and __________

A income; saving
B taxes; expenditures
C revenues; earnings
D money supply; money demand

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2010Mid1 E1
Where are the goods-services, labor and money markets?
(Note: Transfer Payment refers to redistribution of income which include financial aid, social security, health care etc.)