

## Macroeconomics

Read Topic 7, 8, 9: Lessons 1-3

Gross National Product (GNP)

total market value of all goods and services produced by all people of a given state in one year

Three guidelines

items produced at home are excluded

only final new products are counting

to insure no double counting

adjust for inflation

GNP deflator

money GNP vs. real GNP

select a base year

Gross Domestic Product (GDP)

total market value of all goods and services produced in a given state in one year

Other Measures

Net National Product

GNP minus depreciation

National Income

Net National Product minus indirect business taxes

Personal Income

National Income minus:

Undistributed corporate profits

Corporate Income tax

Social Security contributions

**plus** government pay outs

Uses of GNP

economic comparisons over time

doesn't necessarily indicate improvement or decline in society

comparisons between countries

different lifestyles can warp numbers

What determines GNP?

level of total spending determines GNP

business supply will meet demand

spending comes from three sectors

consumption

money spent by consumers for their needs

2/3 of all spending

income is determining factor

expectations affect spending decisions

taxes also affect spending decisions

investment

money spent on capital goods

Factors

availability of investment opportunities

cost and availability of funds  
rate of return

government spending  
20% of all spending

#### Equilibrium GNP

total demand equals total supply  
no growth or decline in GNP

#### Recession

six straight months of declining GNP  
prolonged recession(2yrs) is a depression

#### Economic Growth

increase in GNP over time  
causes increase in standard of living

#### Determinants

availability of natural resources  
supply and quality of capital goods  
supply and quality of labor  
education

#### Labor Productivity

the amount produced per unit of labor  
environmental concerns may outweigh growth issues

#### Business Cycles

Peak  
Recession  
Trough  
Recovery

#### Unemployment

##### Measurements

employed  
unemployed  
not in the labor force

##### Problems with measurements

people quit and drop out of system  
part time work is counted as employed  
people in wrong line of work counted as employed

##### Types

frictional  
people naturally switching jobs  
cyclical  
insufficient aggregate demand  
such as during recession  
business lays off workers  
structural  
job openings don't match skills of unemployed  
technological unemployment  
seasonal

job is only available part of the year

#### Costs

individuals and families have little or no income  
labor is wasted and production is less than maximum

#### Inflation

a decline in purchasing power of currency

#### Measurement

consumer price index

Dept. of Labor tracks prices of 400 basic items

percentage increase is the percentage of inflation

#### Types

##### Demand – Pull Inflation

aggregate demand exceeds potential GNP

demand for goods rises, therefore prices rise

##### Cost – Push Inflation

when production costs rise to cause increase in price

wage – push inflation

when labor costs rise

#### Effects

fixed income people are hurt worse

income doesn't rise to match higher prices

reduces value of savings

banks usually don't match inflation

long-term lending rates rise

makes investment more difficult

hyperinflation (more than 100%)

makes business planning very difficult

people heavily in debt actually benefit

wage and price controls can be tried to control inflation

#### Public Finance

government expenditures and revenues at all levels of government

#### Government expenditures

gov. spending has risen drastically in the last seventy years

#### Why?

increase demand for collective goods and services

schools, defense, highways, urbanization

income security

Social Security, Medicare

#### Taxes

the way government collects revenue

#### Principles

the benefit principle

people who benefit from spending should pay

highway construction-gas tax

not very practical, not all people can pay

the ability to pay principle  
those with money should pay  
progressive income tax  
doesn't distribute gross burden equally

#### Classes

proportional tax  
AKA "flat tax"  
percentage remains the same with all incomes  
progressive tax  
same as our federal income tax  
percentage increases as income increases  
regressive tax  
sales tax  
percentage decreases as income increases

#### Fiscal Policy

##### Origins

classical economics  
policies of Adam Smith  
Great Depression causes concern and questions  
Keynesian economics  
John Maynard Keynes  
1936 – publishes *The General Theory of Employment, Interest, and Money*  
theorizes that government should get involved in economy  
should spend during recessions  
stimulates economy  
should raise taxes during expansion  
pays off debt, prevents inflation  
the objective of fiscal policy is to control business cycles  
possible?  
excessive government spending causes inflation  
lack of spending causes unemployment  
Automatic Fiscal stabilizers  
Government spending  
payouts automatically rise/fall during recession/growth  
welfare, unemployment, food stamps  
Tax collections  
when people make less, they fall into lower tax brackets  
when people make more, they rise into high tax brackets  
Discretionary Fiscal spending  
additional actions that the government can take  
increase spending on public works  
raise taxes to slow down inflation  
Fiscal Spending in Practice  
classic economics until Great Depression

Keynesian economics from WWII until 1980

Supply-Side Economics

cut taxes and revenues will rise  
smaller piece of larger pie  
Laffer Curve  
Reaganomics

did it work?

tax revenues tripled from 1980-92  
spending increased even more  
defense and entitlements  
massive federal debt

Balancing the Budget

Annually balanced budget  
never have any debt or surplus  
constitutional amendment?

Cyclically balanced budget

Keynesian economics  
surplus in expansion  
debt in recession  
balance in between  
realistic?

Full Employment Balanced Budget

balance the budget only during times of full employment  
estimate budget for full employment  
adjust tax rates to fit  
count on automatic stabilizers to fix problems

Deficits and the National Debt

Deficit- yearly debt

national debt – aggregate total owed by government