

Chapter - 6

Unit - 2

Demand for Consumer Goods by Household

Demand for Investment Goods by Business Firm

Demand by Government for Goods & Factor Services

Foreign Trade / Net exports
[eXpost - iMpost]

Types of economy situation

Situation

Autonomous Consumption (a)

Proportionate Consumption [Yd · b]

disposable income mpc

Consumption Function [C]

$$C = a + Yd \cdot b$$

Average propensity to consume = APC = C/Y

Marginal propensity to consume = MPC = $b = \frac{\Delta C}{\Delta Y} = 1 - MPS$

Average propensity to Save = APS = S/Y

Marginal propensity to Save = MPS = $\frac{\Delta S}{\Delta Y} = 1 - MPC$

2
Sector Model

3
Sector Model

4
Sector Model

✓

✓

✓

✓

✓

✓

✗

✓

✓

✗

✗

✓

closed

closed

Open

Myth

Reality

Reality

✓

✓

✓

✓

✓

✓

✓

✓

✓

✓

✓

✓

Ex ante Demand / Expenditure

Ex ante Supply / Income

Equilibrium Income (Y)

Equilibrium Position

Investment Multiplier [K]
without Tax rate

with Tax rate

Tax Function [T]

$$T = \bar{T} + Y \cdot t$$

Lumpsum Tax
Income
Tax rate

Disposable Income [Y_d]

2
Sector Model

$$C + I$$

$$C + S$$

$$Y = C + S$$

$$I = S$$

$$K = \frac{1}{1-b}$$

X

X

$$Y_d = Y$$

∴ No Tax

3
Sector Model

$$C + I + G$$

$$C + S + T$$

$$Y = C + I + G$$

$$I + G = S + T$$

$$K = \frac{1}{1-b}$$

$$K = \frac{1}{1-b(1-t)}$$

✓

$$\begin{aligned}
 Y_d &= Y - T + TR \quad \text{--- Transfer receipts} \\
 &= Y - (\bar{T} + Y \cdot t) + TR \\
 &= Y - \bar{T} - Y \cdot t + TR
 \end{aligned}$$

4
Sector Model

$$C + I + G + (X - M)$$

$$C + S + T$$

$$Y = C + I + G + (X - M)$$

$$I + G + (X - M) = S + T$$

$$K = \frac{1}{1-b+m}$$

$$K = \frac{1}{1-b(1-t)+m}$$

[Also known as Foreign Trade Multiplier]

✓

Impost Function (m)

$$m = \bar{m} + Y \cdot m$$

\bar{m} → autonomous imposts
 Y → income
 m → MPM

Marginal Propensity to impost (m)

2 Sectors Model

X

3 Sectors Model

X

4 Sectors Model

✓

X

X

$$m = \frac{\Delta m}{\Delta Y}$$