

Introduction to Macroeconomics

Introduction to Macroeconomics – Study Notes

1. What Is Macroeconomics?

- **Definition:** The branch of economics that examines the behavior and performance of an economy as a whole.
 - **Scope:** National income, output, unemployment, inflation, fiscal and monetary policy, economic growth, and international trade.
 - **Contrast with Microeconomics:**
 - *Micro* ? individual households, firms, markets.
 - *Macro* ? aggregate aggregates (GDP, price level, total employment).
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2. Core Objectives of Macroeconomic Analysis

Objective	Typical Question	Key Indicator
Economic Growth	How does an economy become richer over time?	Real GDP, GDP per capita, productivity
Price Stability	How can inflation be kept low and predictable?	Consumer Price Index (CPI), GDP deflator
Full Employment	What level of labor utilization is sustainable?	Unemployment rate, labor force participation
Balance of Payments	How does a country manage its international transactions?	Current account, trade balance, exchange rate
Fiscal & Monetary Stability	How should government and central banks intervene?	Budget deficit/surplus, interest rates, money supply

3. Fundamental Concepts & Variables

Concept	Description	Typical Measurement
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Gross Domestic Product (GDP)	Total market value of all final goods & services produced within a country in a given period.	Nominal GDP, Real GDP (inflation-adjusted)
Aggregate Demand (AD)	Total spending on domestic output at each price level.	$(AD = C + I + G + (X-M))$
Aggregate Supply (AS)	Total output firms are willing to produce at each price level.	Short-run AS (SRAS) vs. Long-run AS (LRAS)
Inflation	Sustained rise in the general price level.	CPI, PCE price index
Unemployment	Share of labor force that is jobless but actively seeking work.	Frictional, structural, cyclical, natural rate
Fiscal Policy	Government's use of spending and taxation to influence the economy.	Expansionary vs. contractionary
Monetary Policy	Central bank's control of money supply and interest rates.	Open market operations, discount rate, reserve requirements
Exchange Rate	Price of one currency in terms of another.	Nominal vs. real exchange rate

4. The Circular Flow of Income

1. **Households** supply factors of production (labor, capital) & receive **factor incomes** (wages, rent, profit).
2. **Firms** use these factors to produce goods/services & sell them & receive **revenue**.
3. **Government** collects taxes, provides public goods, and makes transfers.
4. **Foreign sector** engages in imports/exports, affecting net exports.

Diagram tip: Draw two circles (households & firms) with arrows for goods/services and factor payments; add government and foreign sector boxes linked to both circles.

5. Key Macroeconomic Models

5.1 Classical Model

- **Assumptions:** Prices and wages are flexible; markets clear instantly.

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- **Implication:** Economy always operates at full employment; policy has limited short-run effect.

5.2 Keynesian Model

- **Assumptions:** Prices/wages sticky in the short run; aggregate demand determines output.
- **Policy Insight:** Active fiscal and monetary policy can stabilize output and employment.