c. Economy-Wide Interactions

3 principles

a. One person's spending is another person's income

A cut in business spending leads to layoffs or pay cuts; incomes fall, spending by consumers fall

b. Overall Spending Sometimes Gets Out of Line With the Economy's Productive Capacity

- collapse of consumer and business spending, a crisis in the banking industry & other factors ⇒ a plunge in overall spending ⇒ high unemployment during the Great Depression of the 1930s
- Overall spending may not match what the economy can produce

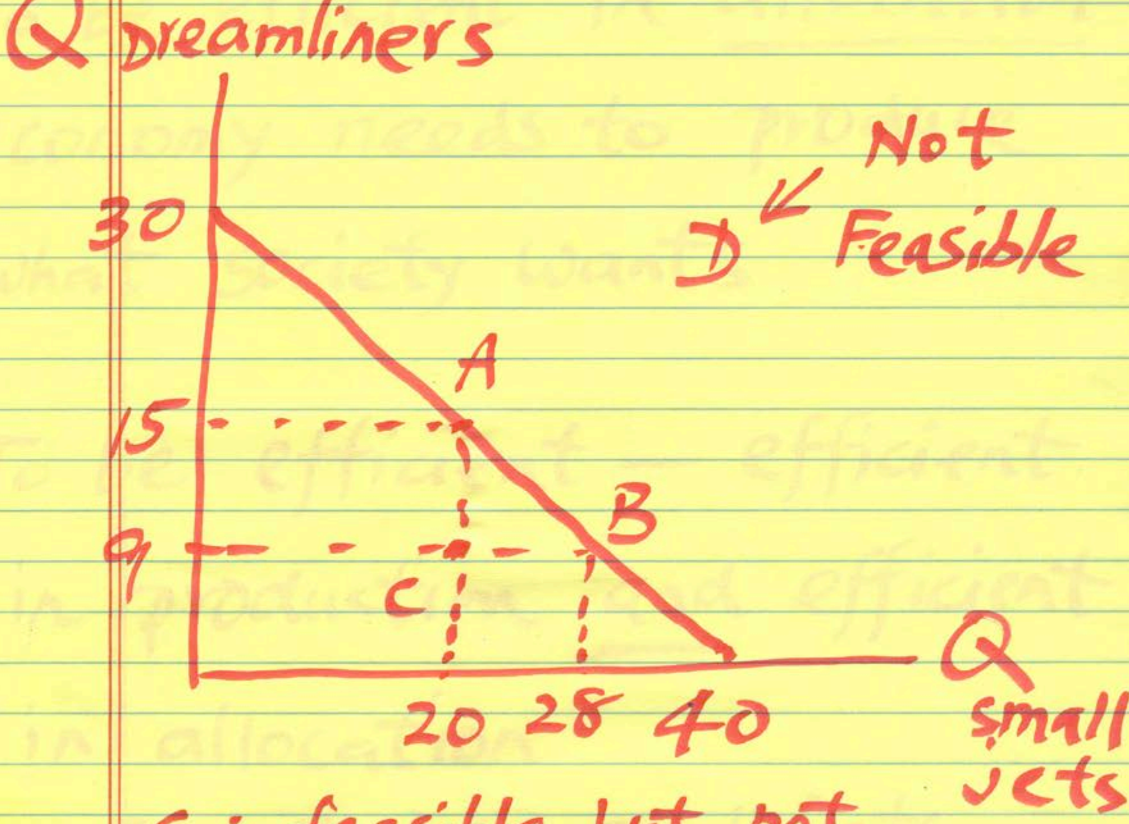
c. Government Policies can change spending

- increase in infractrure spending
- increase in spending on education
- tax cuts

all can increase national spending

Ch 2

Production Possibility Frontier (PPF)



C : feasible but not efficient

A, B efficient in production

CH 5

Society may want A or B

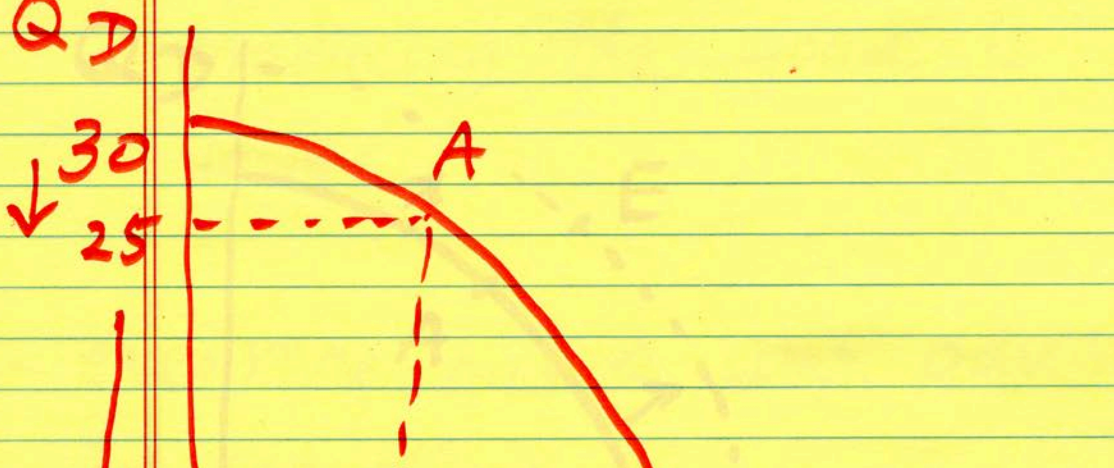
To be efficient in <u>allocation</u> economy needs to produce what society wants

To be efficient — efficient in production <u>and</u> efficient in allocation

A → B 8 more small jets
6 fewer Dreamliners

opportunity cost of a small jet
= 6/8 or 3/4 Dreamliners

<u>Increasing opportunity cost</u>

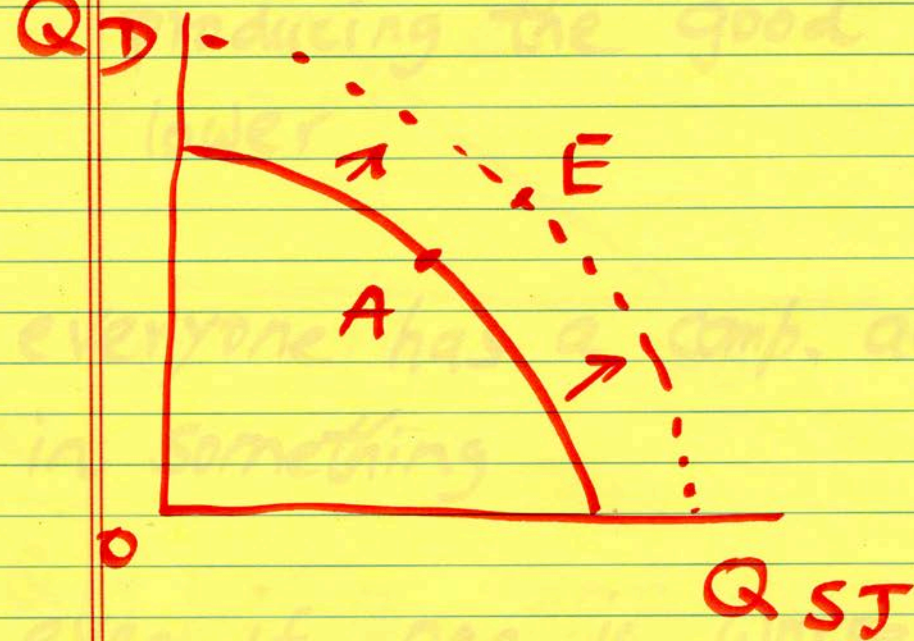


First 20 small jets, give up 5 Dreamliners

For next 20 small jets, give up 25 Dreamliners

Why?

Economic Growth



Due to

a.) increase in factors of production — land, labor, physical capital, human capital

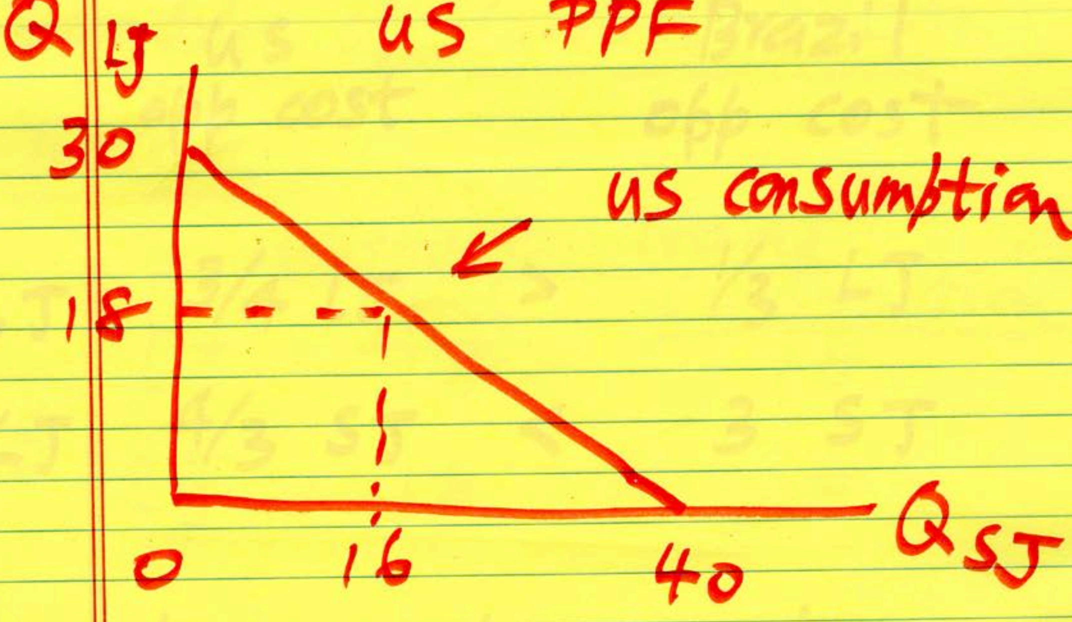
b.) technology improvement

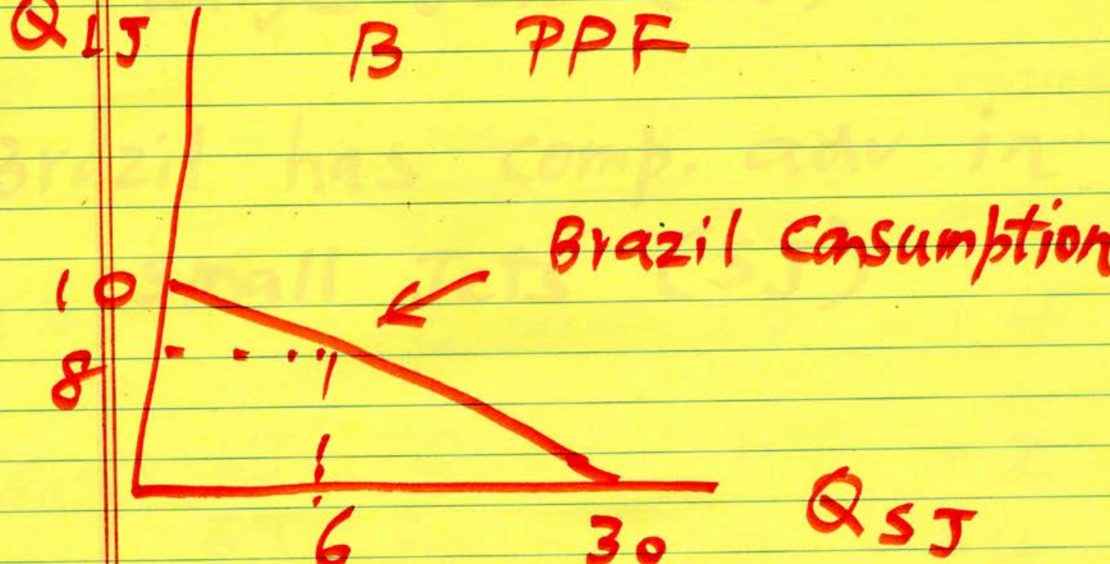
Comparative advantage

- opportunity cost of producing the good is lower.

- everyone has a comp. adv in something

- even if one is worse in everything


Q LJ
US PPF
30
US consumption
18
0
16
40
QSJ


QLJ
B PPF
Brazil Consumption
10
8
6
30
QSJ

	US opp cost		Brazil opp cost
1 SJ	$\frac{3}{4}$ LJ	>	$\frac{1}{3}$ LJ
1 LJ	$\frac{4}{3}$ SJ	<	3 SJ

US has comp. adv in Large Jets (LJ)

Brazil has comp. adv in Small Jets (SJ)