Macroeconomics Topics

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|  |  | Beginning(REVISE PRIORITY)Can you… | Developing(REVISE)NEED FOR 3-5Can you…  | Mastery HL CONTENT (REVISE IF TARGET 6/7)Can you… |
| **The level of overall economic activity**  | Economic activity | * Identify the four factors of production and their respective payments (rent, wages, interest and profits) and explain how these constitute the income flow in the model.
* Explain how the size of the circular flow will change depending on the relative size of injections and leakages.
* Distinguish between GDP and GNP/GNI as measures of economic activity.
* Distinguish between the nominal value of GDP and GNP/GNI and the real value of GDP and GNP/GNI.
* Distinguish between total GDP and GNP/GNI and per capita GDP and GNP/GNI.
* Explain, using a business cycle diagram, how economies typically tend to go through a cyclical pattern
* Distinguish between a decrease in GDP and a decrease in GDP growth.
 | * Describe, using a diagram, the circular flow of income between households and firms in a closed economy with no government.
* Outline how the income flow is numerically equivalent to the expenditure flow and the value of output flow.
* Describe, using a diagram, the circular flow of income in an open economy with government and financial markets, referring to leakages/withdrawals (savings, taxes and import expenditure) and injections (investment, government expenditure and export revenue).
* Examine the output approach, the income approach and the expenditure approach when measuring national income.
* Evaluate the use of national income statistics, including their use for making comparisons over time and between countries and their use for drawing conclusions about standards of living.
* Explain the meaning and significance of 'green GDP', a measure of GDP that accounts for environmental destruction.
* Explain the long-term growth trend in the business cycle diagram as the potential output of the economy.
 | * Calculate nominal GDP from sets of national income data, using the expenditure approach.
* Calculate GNP/GNI from data.
* Calculate real GDP, using a price deflator.
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| Measures of economic activity |
| Calculation of GDP (HL) |
| The business cycle |
| **Aggregate demand and aggregate supply**  | AD and the AD curve | * Distinguish between the microeconomic concept of demand for a product and the macroeconomic concept of aggregate demand.
* Construct an aggregate demand (AD) curve.
* Explain why the AD curve has a negative slope.
* Describe consumption, investment, government spending and net exports as the components of aggregate demand.
* Explain, using a diagram, the determination of short-run equilibrium, using the SRAS curve.
* Examine, using diagrams, the impacts of changes in short-run equilibrium.
* Explain, using a diagram, the determination of long-run equilibrium, indicating that long-run equilibrium occurs at the full employment level of output.
* Examine why, in the monetarist/new classical approach, although there may be short-term fluctuations in output, the economy will always return to the full employment level of output in the long run.
* Describe the term aggregate supply.
* Explain, using a diagram, why the short-run aggregate supply (SRAS) curve is upward sloping.
 | * Explain how the AD curve can be shifted by changes in consumption, investment, government spending and net exports.
* Explain, using a diagram, how the SRAS curve can shift due to factors including changes in resource prices, changes in business taxes and supply shocks.
* Explain, using a diagram, that the monetarist/new classical model of the long-run aggregate supply (LRAS) curve is vertical at the level of potential output (full employment output) because aggregate supply, in the long run, is independent of the price level.
* Explain, using a diagram, that the Keynesian model of the aggregate supply (AS) curve has three sections because of 'wage/price' downward inflexibility and different levels of spare capacity in the economy.
* Explain, using the two models above, how factors leading to changes in the quantity/quality of factors of production (including improvements in efficiency, new technology, reductions in unemployment and institutional changes) can shift the AS curve over the long term.
* Examine why, in the monetarist/new classical approach, although there may be short-term fluctuations in output, the economy will always return to the full employment level of output in the long run.
* Examine, using diagrams, the impact of changes in the long-run equilibrium.
* Explain, using the Keynesian AD/AS diagram, that the economy may be in equilibrium at any level of real output where AD intersects AS.
* Explain, using a diagram, that if the economy is in equilibrium at a level of real output below the full employment level of output, then there is a deflationary (recessionary) gap.
* Discuss why, in contrast to the monetarist/new classical model, the economy can remain stuck in a deflationary (recessionary) gap in the Keynesian model.
* Explain, using a diagram, that if aggregate demand increases in the vertical section of the AS curve, there is an inflationary gap.
* Discuss why, in contrast to the monetarist/new classical model, increases in aggregate demand in the Keynesian AD/AS model need not be inflationary, unless the economy is operating close to, or at, the level of full employment.
 | * Explain, with reference to the concepts of leakages (withdrawals) and injections, the nature and importance of the Keynesian multiplier.
* Calculate the multiplier using either of the following formulas:

11−MPC1MPS+MPT+MPM* Use the multiplier to calculate the effect on GDP of a change in an injection in investment, government spending or exports.
* Draw a Keynesian AD/AS diagram to show the impact of the multiplier.
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| SRAS and short-run equilibrium in the AD-AS model |
| Long-run aggregate supply and long-run equilibrium in the monetarist/new classical model  |
| Aggregate supply and equilibrium in the Keynesian model  |
| Shifting aggregate supply curves over the long term  |
| Illustrating the monetarist/new classical and Keynesian models  |
| The Keynesian multiplier (higher level topic)   |
| Understanding aggregate demand and the multiplier in terms of the Keynesian cross  model (supplementary material, recommended for higher level)   |
| **Macroeconomic objectives I: Low unemployment, low and stable rate of inflation** | Low unemployment  | * Define the term unemployment.
* Explain how the unemployment rate is calculated.
* Distinguish between inflation, disinflation and deflation.
* Explain how inflation and deflation are typically measured by calculating a consumer price index (CPI).
* Discuss the possible consequences of deflation.
* ​Explain demand-pull inflation.
* Explain cost-push inflation.
 | * Calculate the unemployment rate from a set of data.
* Explain the difficulties in measuring unemployment, including the existence of hidden unemployment, the existence of underemployment, and the fact that it is an average and therefore ignores regional, ethnic, age and gender disparities.
* Discuss possible economic consequences of unemployment.
* Discuss possible personal and social consequences of unemployment.
* Describe, using examples, the meaning of frictional, structural, seasonal and cyclical (demand-deficient) unemployment.
* Distinguish between the causes of frictional, structural, seasonal and cyclical (demand-deficient) unemployment.
* Explain, using a diagram, how cyclical unemployment is caused by a fall in aggregate demand.
* Explain, using a diagram, how structural unemployment is caused by changes in the demand for particular labour skills, changes in the geographical location of industries, and labour market rigidities.
* Evaluate government policies to deal with the different types of unemployment.
* Explain how different income earners may experience a different rate of inflation when their pattern of consumption is not accurately reflected by the CPI.
* Explain how inflation figures may not accurately reflect changes in consumption patterns and the quality of the products purchased.
* Explain how economists measure a core/underlying rate of inflation.
* Explain how a producer price index measuring changes in the prices of factors of production may be useful in predicting future inflation.
* Construct a weighted price index, using a set of data.
* Calculate the inflation rate from a set of data.
* Discuss the possible consequences of a high inflation rate.
* Explain, using a diagram, how the short-run Phillips curve may shift outwards, resulting in stagflation (caused by a decrease in SRAS due to factors including supply shocks).
* Discuss, using a short-run Phillips curve diagram, the view that there is a possible trade-off between the unemployment rate and the inflation rate in the short run.
* Discuss, using a diagram, the view that there is a long-run Phillips curve that is vertical at the natural rate of unemployment, and therefore there is no trade-off between the unemployment rate and the inflation rate in the long run.
* Explain how the natural rate of unemployment is the rate of unemployment that exists when the economy is producing at the full employment level of output.
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| Low and stable rate of inflation |
| Topics on Inflation (HL) |
| **Macroeconomic objectives II: Economic growth and equity in the distribution of income**  | Economic growth   | * Define economic growth as an increase in real GDP.
* Calculate the rate of economic growth from a set of data.
* Explain, using a production possibilities curve (PPC), economic growth as an increase in actual output.
* Explain the difference between equity in the distribution of income and equality in the distribution of income.
* Explain how, due to unequal ownership of factors of production, the market system may not result in an equitable distribution of income.
 | * Explain, using a PPC diagram, economic growth as an increase in production possibilities.
* Explain, using an LRAS diagram, economic growth as an increase in potential output.
* Evaluate the view that increased investment is essential for achieving economic growth.
* Evaluate the view that improved productivity is essential for achieving economic growth.
* Discuss the possible consequences of economic growth.
* Analyse data on relative income shares of given percentages of the population, including deciles and quintiles.
* Draw a Lorenz curve and explain its significance.
* Explain how the Gini coefficient is derived and interpreted.
* Distinguish between absolute and relative poverty.
* Explain possible causes of poverty.
* Explain possible consequences of poverty.
* Distinguish between direct and indirect taxes as a mechanism to redistribute income.
* Distinguish between progressive, regressive and proportional taxation, providing examples of each.
* Calculate the marginal rate of tax and the average rate of tax from a set of data.
* Explain how governments undertake expenditures to provide directly, or to subsidise, a variety of socially desirable goods and services, thereby making them available to those on low incomes.
* Explain the term transfer payments and provide examples.
* Evaluate government policies to promote equity.
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| Equity in the distribution of income   |
| **Demand-side and supply-side policies**  | Introduction to demand-side policies   | * Explain that the government earns revenue primarily from taxes (direct and indirect), as well as from the sale of goods and services and the sale of state-owned (government-owned) enterprises.
* Explain that government spending can be classified into current expenditures, capital expenditures and transfer payments, providing examples of each.
* Distinguish between a budget deficit, a budget surplus and a balanced budget.
* Explain the relationship between budget deficits/surpluses and public (government) debt.
* Explain how changes in the level of government expenditure and/or taxes can influence the level of aggregate demand in an economy.
* Explain the mechanism through which expansionary fiscal policy can help an economy close a deflationary (recessionary) gap.
* Construct a diagram to show the potential effects of expansionary fiscal policy, outlining the importance of the shape of the AS curve.
* Explain the mechanism through which contractionary fiscal policy can help an economy close an inflationary gap.
* Construct a diagram to show the potential effects of contractionary fiscal policy, outlining the importance of the shape of the AS curve. ​​
* Explain how factors including the progressive tax system and unemployment benefits, which are influenced by the level of economic activity and national income, automatically help stabilise short-term fluctuations.
* Evaluate the view that fiscal policy can be used to promote long-term economic growth (increases in potential output), indirectly by creating an economic environment that is favourable to private investment and directly through government spending on physical capital goods and human capital formation, as well as provision of incentives for firms to invest.
* Evaluate the effectiveness of fiscal policy.
* Describe the role of central banks as regulators of commercial banks and bankers to governments.
* Explain that central banks are usually made responsible for interest rates and exchange rates in order to achieve macroeconomic objectives.
* Explain how supply-side policies aim at positively affecting the production side of an economy by improving the institutional framework and the capacity to produce (that is, by changing the quantity and/or quality of factors of production).
 | * Explain, using a demand and supply of money diagram, how equilibrium interest rates are determined, outlining the role of the central bank in influencing the supply of money.
* Explain how changes in interest rates can influence the level of aggregate demand in an economy.
* Explain the mechanism through which an easy (expansionary) monetary policy can help an economy close a deflationary (recessionary) gap.
* Construct a diagram to show the potential effects of an easy (expansionary) monetary policy, outlining the importance of the shape of the AS curve.
* Explain the mechanism through which a tight (contractionary) monetary policy can help an economy close an inflationary gap.
* Construct a diagram to show the potential effects of a tight (contractionary) monetary policy, outlining the importance of the shape of the AS curve.
* Explain how central banks of certain countries, rather than focusing on the maintenance of both full employment and a low rate of inflation, are guided in their monetary policy by the objective to achieve an explicit or implicit inflation rate target.
* Evaluate the effectiveness of monetary policy through consideration of factors, including the independence of the central bank, the ability to adjust interest rates incrementally, the ability to implement changes in interest rates relatively quickly, time lags, limited effectiveness in increasing aggregate demand if the economy is in deep recession and conflict among government economic objectives.
* State how supply-side policies may be market-based or interventionist, and that in either case they aim to shift the LRAScurve to the right, achieving growth in potential output.
* Explain how investment in education and training will raise the levels of human capital and have a short-term impact on aggregate demand, but more importantly will increase LRAS.
* Explain how policies that encourage research and development will have a short-term impact on aggregate demand, but more importantly will result in new technologies and increase LRAS.
* Explain how increased and improved infrastructure will have a short-term impact on aggregate demand but, more importantly, will increase LRAS.
* Explain how targeting specific industries through policies including tax cuts, tax allowances and subsidised lending promotes growth in key areas of the economy and will have a short-term impact on aggregate demand but, more importantly, will increase LRAS.
* Explain how factors including deregulation, privatisation, trade liberalisation and anti-monopoly regulation are used to encourage competition.
* Explain how factors including reducing the power of labour unions, reducing unemployment benefits and abolishing minimum wages are used to make the labour market more flexible (more responsive to supply and demand).
* Explain how factors including cuts in personal income tax are used to increase the incentive to work, and how cuts in business tax and capital gains tax are used to increase the incentive to invest.
* Evaluate the effectiveness of supply-side policies through consideration of factors including time lags, the ability to create employment, the ability to reduce inflationary pressure, the impact on economic growth, the impact on the government budget, the effect on equity, and the effect on the environment.
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| Fiscal policy |
| Monetary policy |
| Supply-side policy |
| Government policies to deal with inflation and unemployment |