



# Soochow University International Programs

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2021 SCUIP Winter Session I  
ECON202



# Lecture 1: Introduction to Macroeconomics

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ECON202: Macroeconomics  
Soochow University



# Know Your Instructor

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- Instructor: Dr. Lei Pan
- Position: Lecturer (Assistant Professor) in Economics
- Institution: School of Accounting, Economics and Finance, Curtin University, Australia
- Office Hour: Tuesday 11:00am – 12:00pm
- More info: [www.leipan.org](http://www.leipan.org)



# Assessments

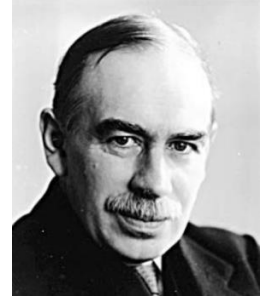
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- Attendance and participation: 10%
- Quizzes: (i) Four in total (5% for each quiz)  
(ii) 20 minutes completing time  
(iii) Quiz time (refer to syllabus)
- Weekly discussion: 10%  
**Note: The first week's discussion has been rescheduled to Thursday.**
- Mid-term exam: 30%, **Friday of Week 2**
- Final exam: 30%, **Friday of Week 4**

# History of Macroeconomics

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- John Maynard Keynes
- Background: The Great Depression of the 1930s
- Challenge the ideas of neoclassical economics (i.e. free markets)
- Famous book: The General Theory of Employment, Interest and Money



# What Macroeconomics is About?

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- **Macroeconomics** is the study of the structure and performance of national economies and of the policies that governments use to try to affect economic performance.



# Common Issues Addressed by Macroeconomists

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- What determines a nation's **long-run economic growth**?
- What causes a nation's **economic activity to fluctuate**?
- What causes **unemployment**?
- What causes **prices to rise**?
- How does being a part of **a global economic system** affect nation's economies?
- Can **government policies** be used to improve economic performance?



# Long-Run Economic Growth

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- Rich countries have experienced extended periods of rapid economic growth.
- Poor countries either have never experienced them or economic growth was offset by economic decline.



# Increased Output

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- **Total output** is increasing because of increasing population, i.e. the number of available workers.

Note: Empirical literature, however, does not provide a clear answer.

- Increasing **average labour productivity**: the amount of output produced per unit of labour input.

# Rates of Growth of Output

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- Rates of growth of output (or output per worker) are determined by:
  - (i) rates of saving and investment
  - (ii) rates of technological change
  - (iii) rates of change in other factors

# Business Cycles

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- **Business cycles** are short-run contractions and expansions of economic activity.



# Recessions

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- Recession is the downward phase of a business cycle when national output is falling or growing slowly.
  - Hard times for many people
  - A major political concern
- The current COVID-19 global pandemic is the second most volatile period in the human history since the 1930s Great Depression.

# Unemployment

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- Recessions are usually accompanied by high **unemployment**: the number of people who are available for work and are actively seeking it but cannot find jobs.

# Inflation

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- When prices of most goods and services are rising over time it is **inflation**. When they are falling it is **deflation**.
- The **inflation rate** is the percentage increase in the average level of prices.

# Effects of Inflation

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- When the inflation rate reaches an extremely high level the economy tends to function poorly. The purchasing power of money erodes quickly, which forces people to spend their money as soon as they receive it.

# The International Economy

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- An economy which has extensive trading and financial relationships with other national economies is an **open economy**. An economy with no relationship is a **closed economy** (autarky).
- International trade and borrowing relationships can transmit business cycles from country to country.



# Exports and Imports

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- US exports are goods and services produced in US and consumed abroad.
- US imports are goods and services produced abroad and consumed in US.



# Trade Imbalances

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- Trade imbalances (trade surplus and deficit) affect output and employment.
  - **Trade surplus**: exports exceed imports
  - **Trade deficit**: imports exceed exports

# The Exchange Rate

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- The trade balance is affected by the **exchange rate**: the amount of US dollars that can be purchased with a unit of foreign currency.



# Macroeconomic Policy

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- A country's economic performance depends on:
  - natural and human resources
  - capital stock
  - technology
  - economic choices made by citizens
  - **macroeconomics policies** of the government

# Macroeconomic Policy (Cont'd)

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- Macroeconomic policies:
  - **Fiscal policy**: government spending and taxation at different government levels.
  - **Monetary policy**: the central bank's control of short-term interest rates and the money supply.

# Budget Deficits

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- The economy is affected when there are large **budget deficits**: the excess of government spending over tax collection.

# Aggregation

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- Macroeconomists ignore distinctions between individual product markets and focus on national totals.
- The process of summing individual economic variables to obtain economywide totals is called **aggregation**.

# What Macroeconomists Do?

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- Macroeconomic forecasting
- Macroeconomic analysis
- Macroeconomic research
- Data development



# Macroeconomic Forecasting

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- **Macroeconomic forecasting** – prediction of future economic trends – has some success in the **short run**. In the **long run** too many factors are highly uncertain.
- Keynes: “In the long run, we are all dead.”

# Macroeconomic Analysis

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- **Macroeconomic analysis** – analysing and interpreting events as they happen – helps both private sector and public policymaking.

# Macroeconomic Research

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- **Macroeconomic research** – trying to understand the structure of the economy in general – forms the basis for macroeconomic analysis and forecasting.



# Economic Theory

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- **Economic theory**: a set of ideas about the economy to be organized in a logical framework.
- **Economic model**: a simplified description of some aspects of the economy.

# Developing and Testing a Theory

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- State the research question.
- Make provisional assumptions.
- Work out the implications of the theory.
- Conduct an **empirical analysis**.
- Evaluate the results.

# Data Development

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- Macroeconomists use data to assess the state of the economy, make forecasts, analyse policy alternatives, and test theories.
- Providers of data must:
  - Decide what types of data should be collected based on who is expected to use the data and how.
  - Ensure the measures of economic activity correspond to economic concepts.
  - Guarantee the confidentiality of data.

# Why Macroeconomists Disagree

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- A **positive analysis** examines the economic consequences of an economic policy, but it does not address its desirability.
- A **normative analysis** tries to determine whether a certain economic policy **should** be used.

# Why Macroeconomists Disagree (Cont'd)

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- Economists can disagree on normative issues because of differences in values.
- Economists disagree on positive issues because of different school of thought.





# The Classical Approach

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- The invisible hand of Economics: General welfare will be maximized (not the distribution of wealth) if:
  - there are free markets
  - individuals act in their own best interest
- To maintain markets' **equilibrium** – the quantities demanded and supplied are equal:
  - Markets must function without interventions.
  - Wages and prices should be flexible.
- Thus, according to the classical approach, the government should have a limited role in the economy.

# The Keynesian Approach

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- Keynes (1936) assumed that wages and process adjust slowly.
- Thus, markets could be out of equilibrium for long periods of time and unemployment can persist.
- Therefore, according to the Keynesian approach, governments can take actions to alleviate unemployment.
- The government can purchase goods and services, thus increasing the demand for output and reducing unemployment.
- Newly generated incomes would be spent and would raise employment even further.

# Evolution of the Classical-Keynesian Debate

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- After **stagnation** – high unemployment and high inflation – of the 1970s, a modernized classical approach reappeared.
- Substantial communication and crosspollination is taking place between the classical and the Keynesian approaches.

# Unified Approach to Macroeconomics

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- Individuals, firms and the government interact in goods, asset and labour markets.
- The macroeconomic analysis is based on the analysis of individual behaviour (i.e. microeconomic foundations of macroeconomics).



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