

ECO202Y - Lecture 1

- ❖ Macroeconomics is the study of economics at the national level
- ❖ Macroeconomics = aggregate economic activity, what is happening to the change of prices in the aggregate economy
- ❖ Macro is the study of the structure of the economy - how things are actually interrelated with one another, the dynamic adjustments of the economy**
- ❖ Dynamic adjustments - how does the economy move from equilibrium position to another, what are the economic forces that are causing that movement to take place?
- ❖ Macro - performance of the economy - good or bad? Government policies related to how that national economic performance is unfolding - kinds of government policies
- ❖ Endogenous variables - dependent variables - this what the model is going to try to explain
- ❖ Exogenous variables - independent variables - explanatory variables
- ❖ Exogenous variables explain endogenous variables
- ❖ We also have constants and parameters - the coefficients that are in the equation (not variables!)
- ❖ If you cannot get any data on your exogenous variable, you need to eliminate it
- ❖ In Macro, there are three very important variables: GDP (or aggregate economic activity), unemployment, and inflation
- ❖ Real GDP = measure of the quantity of production taking place in the economy
- ❖ Real GDP fluctuates around its long term trend - the fluctuations are called business cycles
- ❖ When the economy is growing = expansion
- ❖ When the economy is shrinking = contraction
- ❖ Unemployment rate = % of the labour force who is out of work and is actively seeking to find work
- ❖ Recession = unemployment rate increases
- ❖ Expansion = unemployment rate decreases (but it decreases at a much lower rate than it increased)
- ❖ Inflation = measure of how rapidly is the overall price changing
- ❖ Two things are related to inflation = deflation & hyperinflation
- ❖ Deflation = when prices are dropping (deflation is not a good thing)
- ❖ Hyperinflation = when prices are rising very rapidly (about 50% per month)
- ❖ Our models should be able to explain the three important variables
- ❖ Macroeconomic policies = use the economic models that we develop to try to use government policies to help to produce better economic outcomes
- ❖ When we think about macroeconomic policies affecting better outcomes, the implications are:
- ❖ Why are richer countries richer and poor countries poorer and how can macro help?
- ❖ How has China managed been able to grow so rapidly and can their policies be applied to other developing countries?
- ❖ How much do savings matter? Short-run saving and long-run savings
- ❖ Do budget deficits matter? => How and how much budget deficit matter?

- ❖ Budget deficit = difference between how much tax revenue the government receives and its expenditures
- ❖ Budget Deficit = Expenditure > Tax revenue received
- ❖ Fiscal policy = the government decision about how to spend and how to receive in taxes
- ❖ How costly is to reduce inflation? What is the cost of inflation on an economy?
- ❖ If there is a cost related with inflation, then it has been found to be related to a country's Central Bank
- ❖ When the Central Bank conducts its policies (called Monetary Policies) (because
- ❖ Central Bank can almost always influence changing growth rate of the money supply. The growth rate of the money supply can be direct or indirect:
 - ❖ Direct method: by changing money supply or
 - ❖ Indirect method: by changing interest rates
- ❖ What causes financial crisis? Can they be made less severe and can they be made to happen less often?
- ❖ Financial Crisis = severe disruption of the financial markets - the movement of financial capital around the economy
- ❖ Asset prices typically fall quite significantly (stock market prices, prices of housing)
- ❖ Theoretically we know how monetary and fiscal policies should be used to help stabilize the economy, but can we implement the right solution at the right time to fix the right problem? Activist & non-activist debate
- ❖ Should macroeconomic policies be discretionary based or rules based?
- ❖ Are trade imbalances a big danger? Are they an economic problem, how big of a problem are they, and for whom are they a big problem?
- ❖ Ex. For USA, the trade deficits are a big problem because they are going to into a deeper and deeper debt to the Chinese
- ❖ For China, the problem is that they are lending more and more money to the Americans
- ❖ Trade imbalance = difference between exports and imports
- ❖ Trade balances = also represent international lending and borrowing activities