

ECONOMICS

for South African students

Macroeconomics

**Basic concepts,
relationships and issues**

Introduction

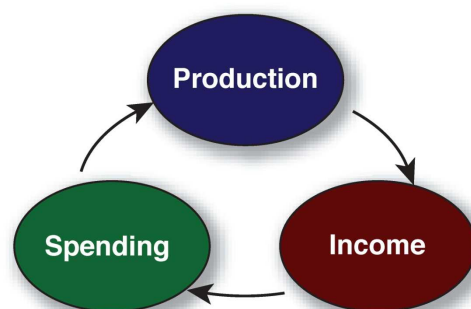
- **Economics:** science of household management
- Unlimited wants, limited means: scarcity
- Scarcity necessitates choice
- Every choice entails opportunity cost
- **Opportunity cost**
 - best alternative forgone
 - examples

- **Microeconomics and macroeconomics**
 - **Microeconomics:**
 - focus on detail
 - microscope
 - examples
 - **Macroeconomics:**
 - deals with whole economy
 - examples

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Major flows in the economy

- **Production → income → spending/expenditure**



Production, income and spending

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- **Production:**
 - factors of production
 - natural resources (land)
 - labour
 - capital
 - entrepreneurship

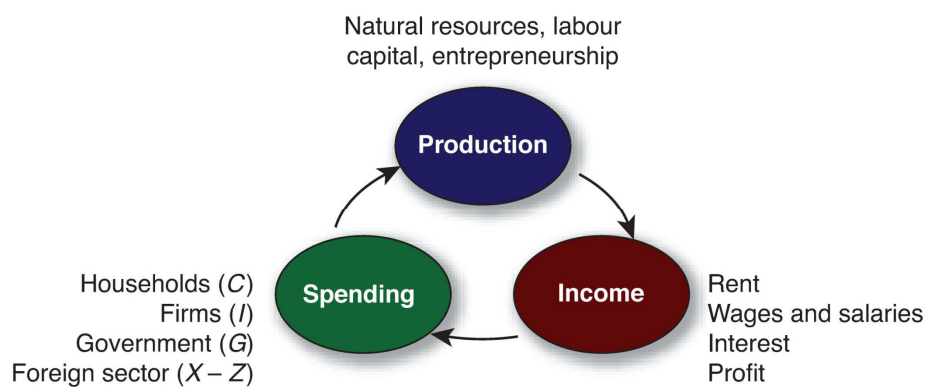
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- **Income:**
 - Flipside of production
 - Reward of the factors of production
 - rent (natural resources)
 - wages and salaries (labour)
 - interest (capital)
 - profit (entrepreneurship)

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- **Spending:** expenditure by all sectors of the economy
 - consumption expenditure by households (C)
 - investment (capital) expenditure by firms (I)
 - government spending (G)
 - exports (X) minus imports (Z)

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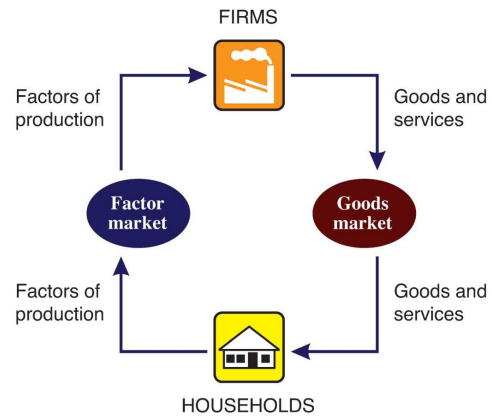
The different components of production, income and spending

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Circular flows

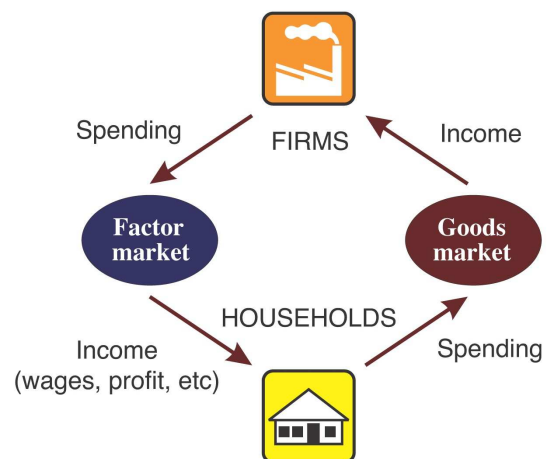
- *Goods market and factor market*
- *Circular flow of goods and services*

The circular flow of goods and services



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- *Circular flow of income and spending (opposite direction to goods and services)*



The circular flow of income and spending

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- ***Injections into (or additions to) circular flow of income and spending***
 - investment spending/capital formation
 - government spending on goods and services
 - exports

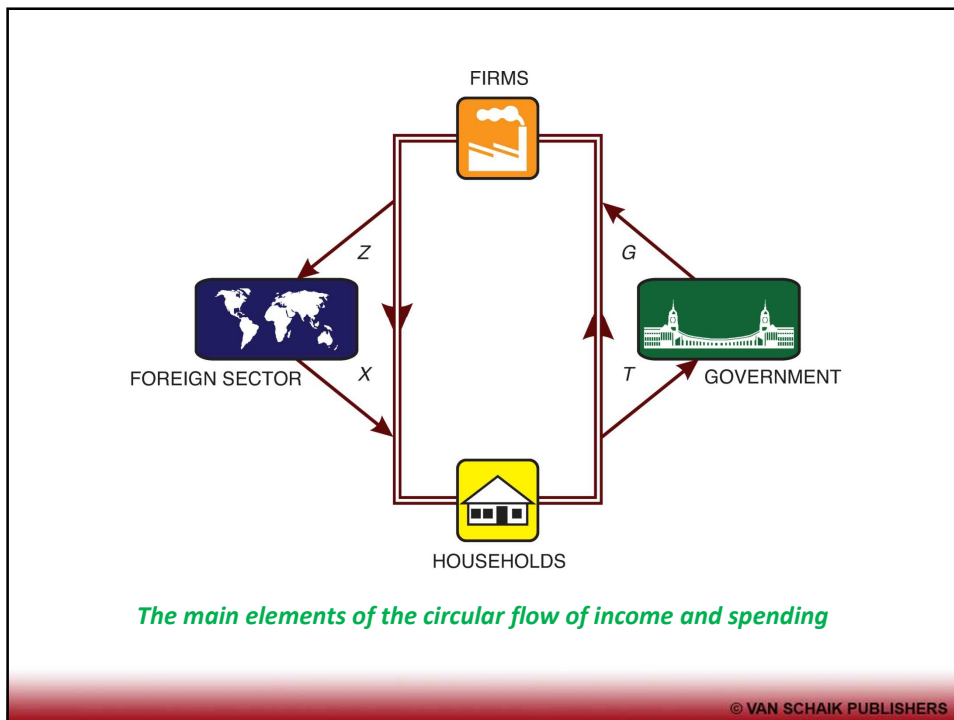
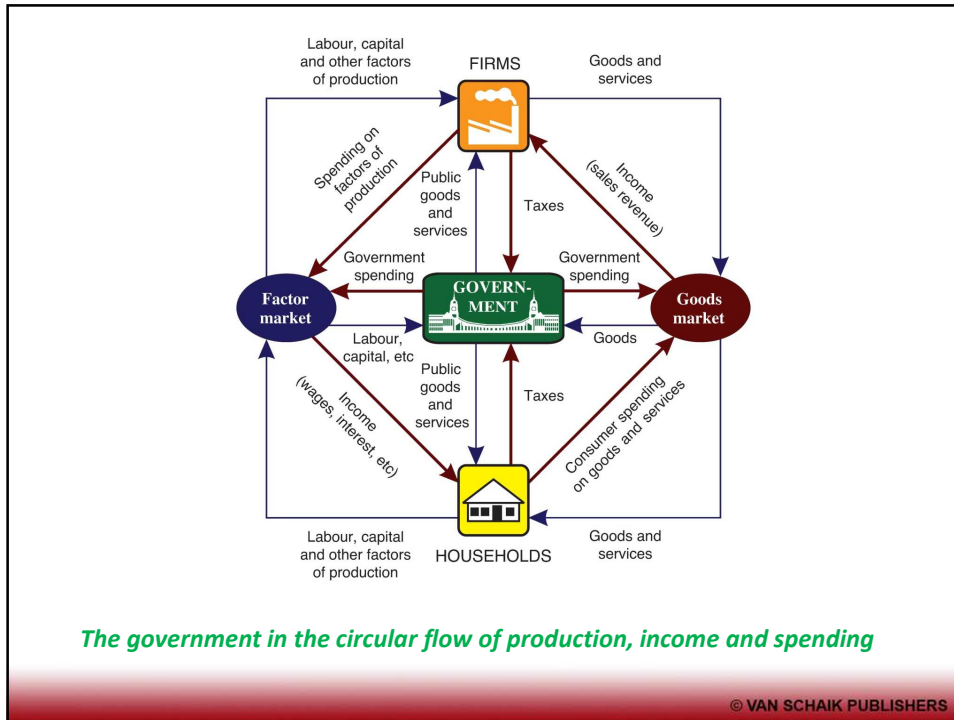
- ***Withdrawals or leakages from the circular flow***
 - saving
 - taxes
 - imports

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- ***Note that capital goods (capital as factor of production) are tangible***

- ***Investment refers to purchase of capital goods***

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Macroeconomic theory

Simplification, abstraction, model

Purposes

- explanation
- prediction
- policy

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Macroeconomic policy

Objectives

- economic growth
- full employment/low unemployment
- price stability/low inflation
- balance of payments stability/external stability
- equitable/socially acceptable distribution of income

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Instruments

- monetary policy
- fiscal policy
- other policies

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Things to watch out for

Fallacy of composition

- whole is more than the sum of the parts
- what is true for single part not necessarily true for the whole
- examples

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Do not confuse correlation with causation

➤ examples

Do not confuse levels with rates of change

➤ examples