Macroeconomics: BSc Year One
Components of Basic Models - Introduction

There are three basic macroeconomic models:

- classical
- Keynesian
- monetarist

All three rely on the economics of supply and demand sides. Demand side economics concentrates on what determines consumers' wants; that is, their total and total desired spending. Supply side, however, examines what determines how much is produced.

Demand Side Economics

If we take $q_{i,t}^{d}$ to denote the quantity of the i'th good demanded over time period t, and $p_{i,t}$ to mean the price of the i'th good, the total (or aggregate) nominal demand in the economy can be found by:

$$\sum_{i=1}^{n} p_{i,t} . q_{i,t}^{d}$$

In many cases, however, it is more useful to use aggregate real demand, which uses a base year to keep prices constant:

$$\sum_{i=1}^{n} p_{i,1990} . q_{i,2001}^{d} = y^{d}$$

This excludes effects of price changes, so changes in quantities can be analysed.

Determinants of Aggregate Demand

In general, $y^{d} \equiv c + i + g + x - m$

Where we define:

y^d	the total quantity of domestic goods and services demanded,
c	the total quantity of goods and services which people in the economy wish to purchase for the purpose of immediate consumption (Real Desired Aggregate Consumption Expenditure),
i	the total quantity of goods and services which people in the economy wish to buy not for immediate consumption (Real Desired Aggregate Investment Expenditure),
g	the total expenditure by government on goods and services (Real Desired Aggregate Government Expenditure).

For the moment, we shall assume a closed economy and thus ignore exports (x) and imports (m).