Chapter 29	McConnell, Brue and Flynn 20th

The Aggregate Expenditures Model

In previous chapters we answered in detail two of the most critical questions in macroeconomics: How is an economy's output measured? Why does an economy grow? But we have been relatively general in addressing two other important questions: What determines the level of GDP, given a nation's production capacity? What causes real GDP to rise in one period and to fall in another? To provide more thorough answers to these two questions, we construct the aggregate expenditures model, which has its origins in 1936 in the writings of British economist John Maynard Keynes (pronounced "Caines"). The basic premise of the aggregate expenditures model—also known as the "Keynesian cross" model—is that the amount of goods and services produced and, therefore, the level of employment depend directly on the level of aggregate expenditures (total spending). Businesses will produce only a level of output that they think they can profit-ably sell. They will idle their workers and machinery when there are no markets for their goods and services.