

Economics theories

1. Keynesian economics is the theory that focus on spending in the economy which is effect directly to number of output and inflation rate. And keynesian economics is Demand-side while classical economics is supply-side. Furthermore, this theory support government to increase theirs spending to boost economy.

2. In 1929, economy was dramatically growth in United states. Every sector were boom whether stock market, bank and others sector. But when people loan and invested in high number, and then crash due to stock market. So, it caused high bad debt in economy. Most bank have many people withdraw money and caused bank run because bank doesn't have enough money to pay back to customers. After that FED (Central bank of United states) failed to solve this problem.

3. When money supply in economy is higher, interest rate must be high to slow down economy, but in this case they kept interest rate low and economy were crash. Most people suggests that government should do nothing and market will return to natural equilibrium by itself due to classical economics theory that market is perfect.

4. The great depression from keynes's perspective, he thinking that market is not perfect, and not natural return to equilibrium. Moreover, number of output is low while unemployment rate was high and investors not invest to push economy up during recession or depression. Thus, customers confidence have effect directly to economy in this situation. On the other hand, he think that government should take action when economy is growth of temporary slow down by using fiscal and monetary policy to stabilize an economy.

5. There are many solutions to solve depression as follows: using fiscal and monetary policy to slow down economy. So, both policies are very effective in short run because in the great depression economy was growing to fast and lead to crash in economy. Moreover, there are advantage and disadvantage of both policies.

6. Fiscal policy have an advantages and disadvantages to use it. Especially, the most important idea of this policy is "Multiplier effect". So, Multiplier is related to MPC with a concept one spending is becomes income of another person in cycle and also money multiplier is a system of fractional reserve banking. And to stimulate economic growth by increasing government spending and reduce taxes can boost aggregate demand, consumption and income. Moreover, it will create economic growth and reduce externalities.

7. On the other hand, disadvantage of fiscal policy is when we use both expansionary or contractionary to boost or slow down economy it might have some conflict of the purpose in policy. For example, If the government wants to raise more money to increase its spending and stimulate economic growth, government can issue bonds to the public. Since government bonds offer benefits to buyers, and buyers will buy them heavily. Furthermore, it can create budget deficits and tax will burden in import and export.

8. One of Keynes's ideas is that government intervention is part of Keynesian economics. In other words, monetary policy also has advantages and disadvantages. This policy can boost the short-run economy and it can make the market return to equilibrium and stabilize more quickly. Mainly, the interest rate is easy to control and it will cause a small inflation rate.

9. Conversely, the effect from policy might have a time lag. When we use policy it takes time, about a month or a year, and this will not affect the long-run economy. Similarly, the interest rate is the most important tool of monetary policy. But when we lower the interest rate to 0, after that it will not have much effect in the economy anymore.

10. Classical economics believed that when people save more money, investment will increase and it is a sufficient condition. But from Keynes's perspective, he believes that savers and investors are not the same group because the reasons for saving and investing are different. Moreover, saving is a direct function of national income while investment is an indirect function of interest rates.

11. Accordingly, saving and economic growth are related. An increase in saving relative to its demand would lower the interest rate and increase borrowing for investment or production. In this case, economic growth would take place along with lower interest rates. On the other hand, an increase in saving would raise the interest rate and increase the number of savers. Economic growth will proceed along with higher interest rates.

12. The paradox of thrift is a theory that an increase in saving leads to a decrease in aggregate expenditure because people have lower income. Therefore, it will cause a decrease in output and finally it leads to a decrease in economic growth.