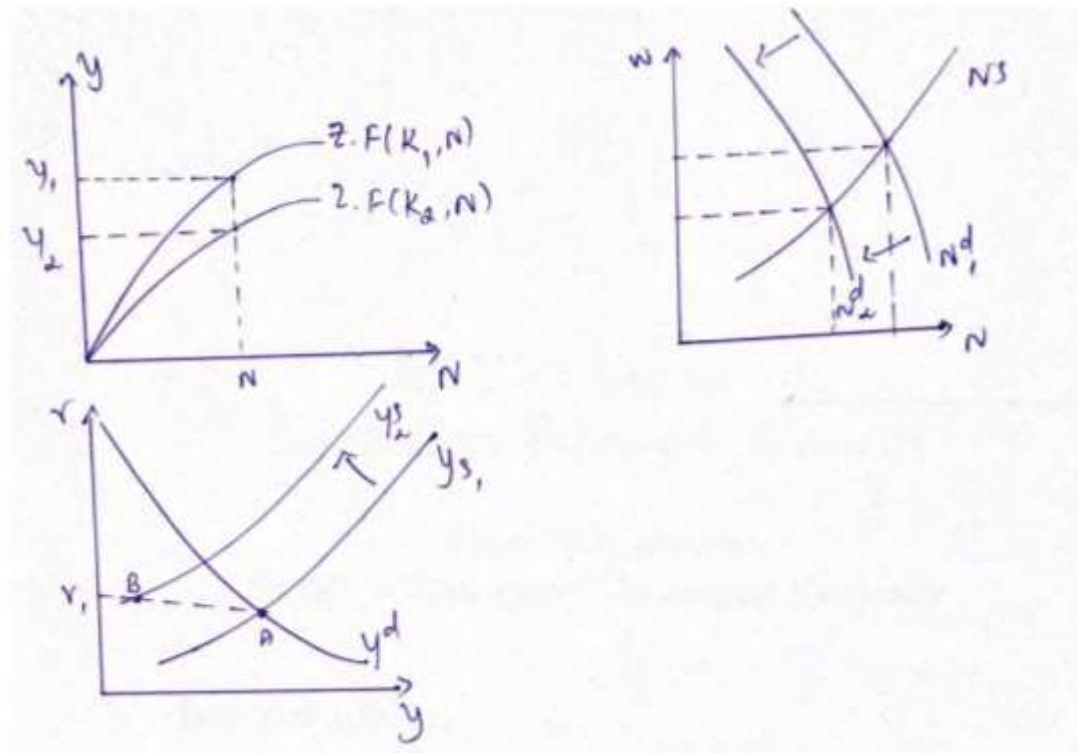
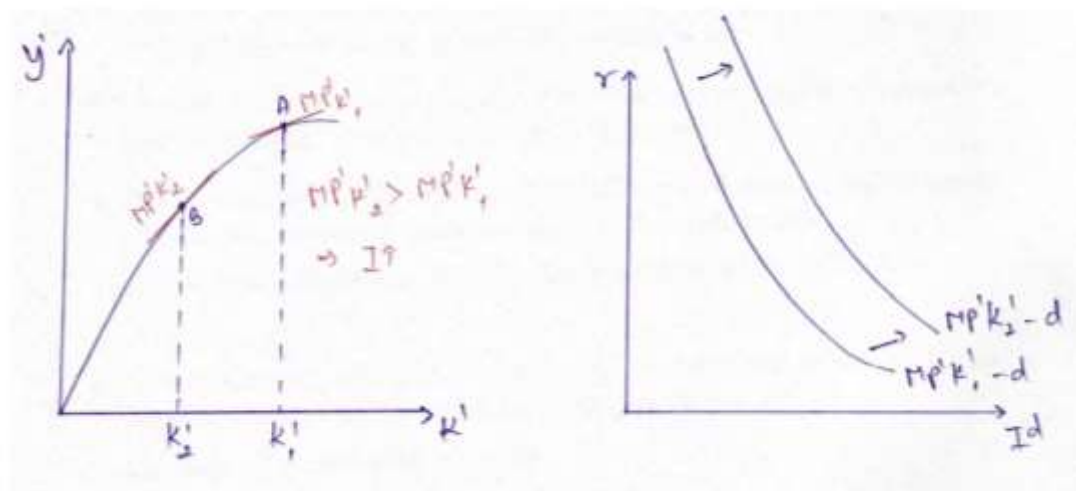


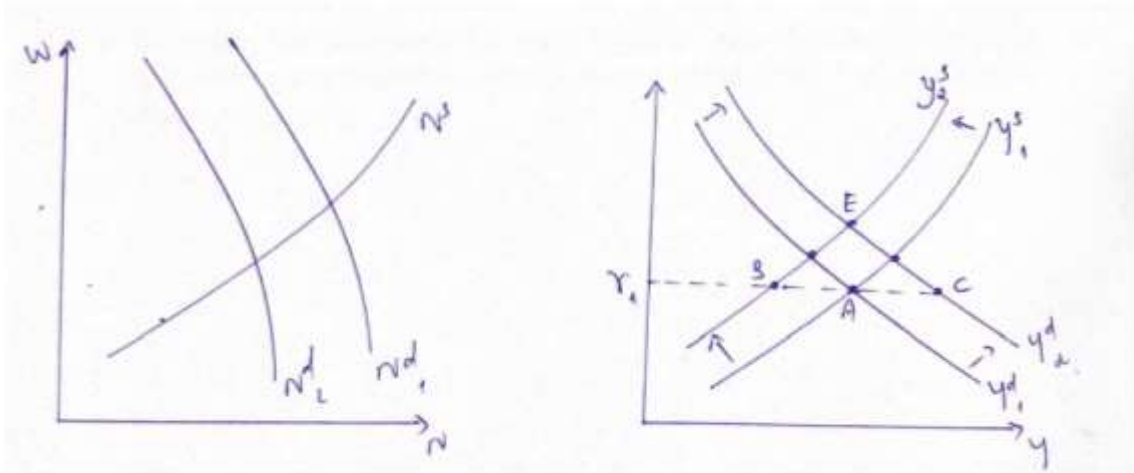
Effect of Vietnam War on American Capital Stock

In March 1965, the U.S. President Mr. Johnson made a decision to fully support the republic of south Vietnam in fighting the north. This caused a decrease in Current capital stock of the U.S. as the factory production were shift from consumer to military. It means that there will be more production for military than for the consumer.

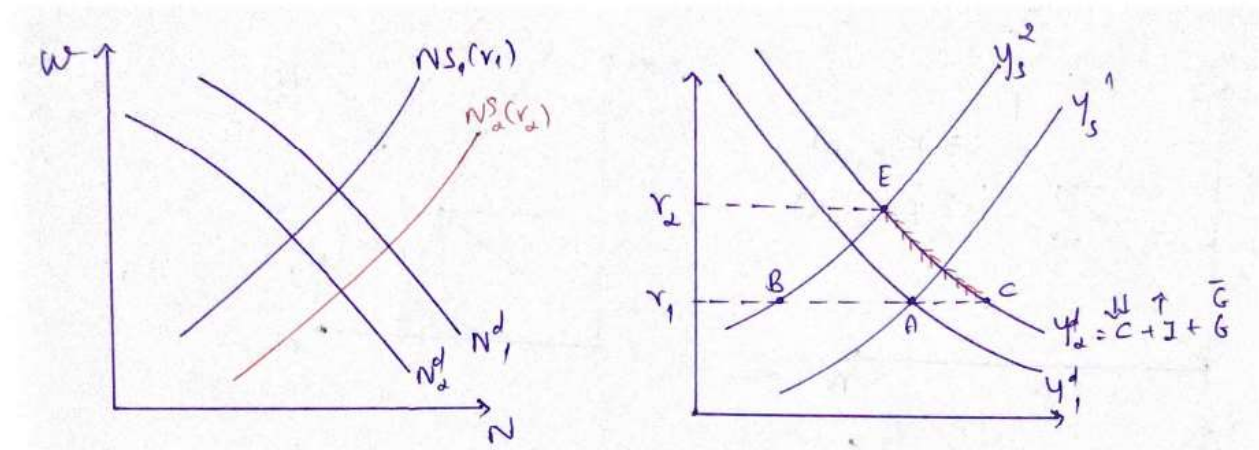


Currently there will be lower capital stock with the same labor which cause a drop in MPN. This will lead to lower demand for labor from firm. Labor demand curve will shift to the left. Therefore, there will be lower output supply. Output supply curve shift to the left.

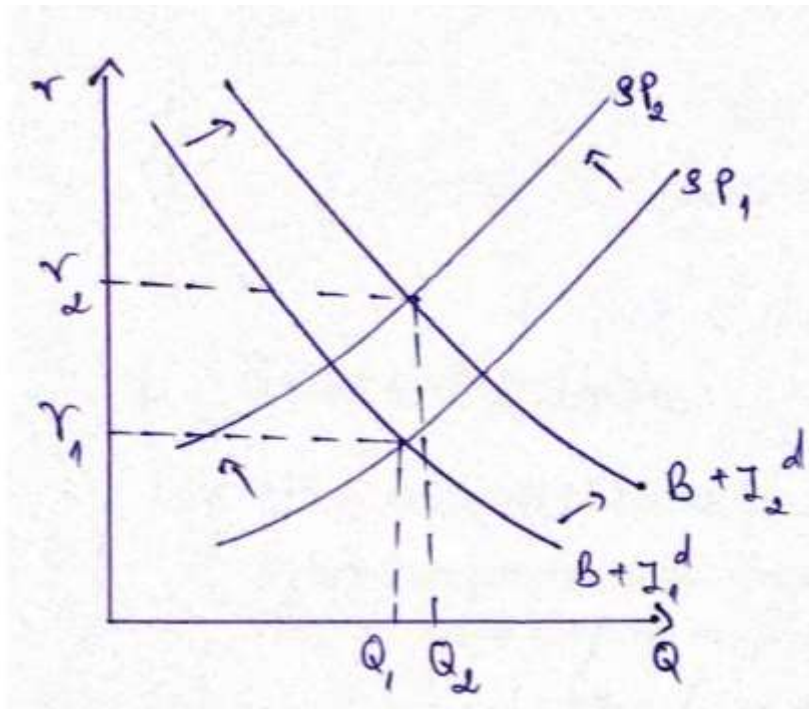




Moreover, the lower current capital stock (K) lead to smaller future capital stock (K'). we now have higher future Marginal propensity of future capital ($MP'K'$). Therefore, investment also increases that lead to a shift in investment demand curve to the right. As investment shift, thus output demand also shift to the right with higher interest rate.



With higher interest rate, people tend to reduce more leisure, cut down their consumption and invest less. Thus, labor supply increase. these lead labor supply to shift to the right. Real wage is now decrease which we have a movement along the output supply curve. Investors to invest because of higher interest rate. However, with higher future marginal propensity of future capital. Therefore, it raises investment.



In credit market, as consumption drop less than the aggregate output, we have the consumption smoothing as there will be less credit supply. Additionally, investment demand increase which shift the curve to the right. Therefore, we now have higher interest rate.

Reference

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