

Keynes' perspective on Great Depression.

Great Depression is when the economy is stuck at high unemployment rate and low output. From the idea of Neoclassical that the economy can return to equilibrium by itself (without government intervention) or when price decrease wage will decrease and employers will hire more labors (back to full employment), this cannot solve Great Depression because in Great Depression wage will not decrease and this will make a deflationary gap for a long time so Keynes rejects this idea and presents his perspective. His perspective is during the Great Depression, people lose their confidence and aggregate demand cannot increase to go back to full employment and this will remain for a very long period of time which makes wage and price downward inflexibility and this can solve by increasing demand or encourage people to spend their money.

Possible solutions to Great Depression.

As I already said before that to solve Great depression, we can do by increasing demand or encourage people to spend their money, and to do this government should increase their spending and reduce tax. For increasing government expenditure for example construct a road, this can make more employment and when people get a job they will have money for spending and this can increase demand. For another way, decreasing tax, this will make people want to consume more after that producer want to produce more and have to hire more labor so output will increase and economic will be more developing.

Pros and cons of monetary policy

Pros: Monetary policy can decrease interest rates to encourage borrowing and lending. This make firms employ more labor and have more output. Conversely, Neoclassical idea believe that interest rates are not affect unemployment rate.

Cons: This can make zero bound problem. As interest rate approach zero, stimulating the economy by reducing interest rate will not effective anymore because people will do not want to deposit money but they will keep money in cash or buy bond instead.

Pros and cons of fiscal policy

Pros: Fiscal policy can stimulate economy by an injection of government spending. This will make people spending more money. So, this will be raising marginal propensity to consume to effect full employment and increasing economic growth.

Cons: This Keynesian model is misrepresented the relationship between savings investment and economic growth. Also, most of economist accept that fiscal stimulus is far less effective than the original multiplier model suggests.

What is Keynesian economics?

Keynesian economics is economic concept that prevent economic slumps and optimal economic performance achieved and can solve economic problems by using Fiscal and Monetary policy. This will focus on demand side which influencing aggregate demand through activist stabilization and economic intervention by government. Also focusing on output and inflation. This concept is rejection from Neoclassic ideas that economy can work by itself (without government intervention) and can use invisible hand to solve economic problems.

Keynes' perspective on saving and economic growth

Saving and Economic growth have an opposite relationship which is when people saving more money economic growth will decreasing. This is because saving money make a leakage in economy or money is going out from the economy so people will consume less then producer will decrease their production and decrease hiring labor so this will increase unemployment rate and decrease economic growth.

Phillips Curve on saving and economic growth

When price level increase, economic growth will be reducing. This is because price level increasing make an inflation so if price level keep increasing every year, inflation rate also keep increasing every year. This make people consume less because product is expensive and they save their money. After that firms will reduce production and decreasing employ labor so this increasing unemployment rate and decreasing economic growth.

Depreciation on saving and economic growth

When depreciation increase and saving rate is stay the same, bank will have lower money for firms to loan. At the same time, firms should loaning money to pay depreciation if not, it will make production rates and output decreasing so this will make an excess demand or price increasing because products are not enough with consumer needs. In short, when depreciation increase, the average per capita increase but saving and investment is still the same so this make steady state growth rate of total output decrease and also increase inflation rate.

Liquidity Trap on saving and economic growth

Liquidity trap is when interest rate reducing a lot so people want to keep money only for spending and not for buy bond. This make no effect in interest rate in the market so output in the market will increasing in lower rate because IS curve will have a very high slope so it will make firms reduce production and hire labor so output will be decreasing and then economic growth will be down.

Solow Growth Model on saving and economic growth

- When developed and developing countries are developing their technology they both have to pay depreciation in the same rate. Then in finally, developing country can develop to be the same level or surpass the developed country. This is because average per capita of developing country are less than developed country so this attracts investor to invest in this country so developing country can develop to be a developed country for example China.
- Also, Saving rate is not effect economic growth. This is because in long run if economy is always steady state, people will get more wage but output is stay the same so economy growth will stay the same.