

## 9 The multiplier – Part 1

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Name: \_\_\_\_\_ Class: \_\_\_\_\_ Date: \_\_\_\_\_

### Vocabulary

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*Write each word three times.*

| English              | Write it 3 times (English) |  |  |
|----------------------|----------------------------|--|--|
| circular flow of in- |                            |  |  |
| come                 |                            |  |  |
| injections           |                            |  |  |
| leakages             |                            |  |  |
| multiplier           |                            |  |  |
| marginal propen-     |                            |  |  |
| sity to consume      |                            |  |  |

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### Recall

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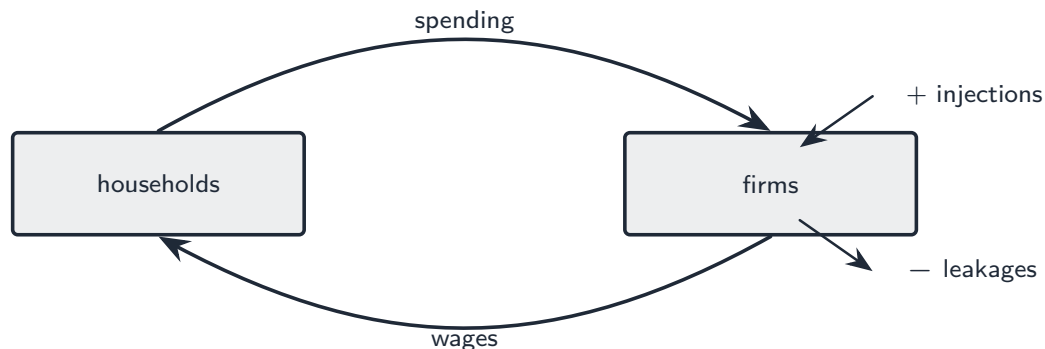
Money moves round the economy between households and firms. New spending can have a surprisingly large effect.

### New ideas

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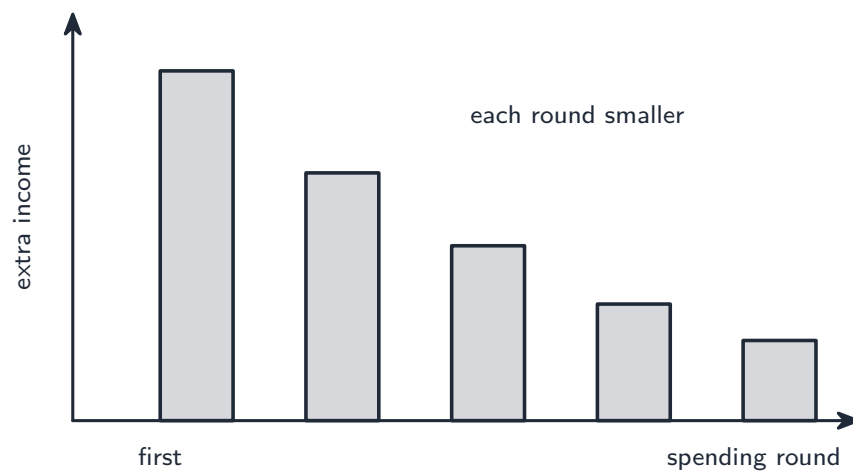
Read these first, then do the Practice.

## ■ 1 The circular flow



The **circular flow of income** shows money passing between households and firms. **injections** add money (investment, government spending, exports); **leakages** take it out (saving, tax, imports).

## ■ 2 The multiplier



The **multiplier** means an injection raises income by *more* than the first amount, because it is spent again and again. How much depends on the **marginal propensity to consume** (MPC) – the fraction of extra income people spend.

*Worked example.* If the MPC is 0.8, the multiplier =  $\frac{1}{1 - 0.8} = 5$ , so a \$10m injection eventually raises income by \$50m.

**Watch out:** a bigger MPC (people spend more of extra income) gives a *bigger* multiplier; more leakages (saving, tax, imports) give a *smaller* one. The multiplier =  $\frac{1}{1 - \text{MPC}}$ .

## Practice

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Try these in order.

**9.1** What does the *circular flow of income* show? [1]

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**9.2** Give one example of an *injection*. [1]

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**9.3** Give one example of a *leakage*. [1]

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**9.4** What does the *multiplier* mean? [1]

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**9.5** If the *MPC* is large (people spend most extra income), is the multiplier large or small? [1]

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**9.6 Challenge.** A government spends \$20m building a road where people spend three-quarters of any extra income ( $MPC = 0.75$ ). Estimate the final rise in income. [2]