

Exercise walk-through

5.7

Public Policy and Economic Growth

AP Macroeconomics

Economic growth

Economic growth = a rise in real
GDP per capita over
time. Two sources:

- more & better **resources** (labour, capital, human capital)
- higher **productivity** – more output per input

Growth = the PPC shifting **outward** and LRAS shifting **right** – the same event.



More capital and productivity raise living standards

Public policy for growth

Governments raise long-run growth by building resources or lifting productivity:

Capital

physical

(roads, machines)

& **human capital**

(schools, health)

Technology

R&D

universities,

patents –

more output per input

Institutions

property rights

honest courts,

good incentives

Each shifts **LRAS** right and the **PPC** outward.

Money Growth and Inflation, continued



More money chasing goods: sustained money growth tends to raise the price level over time

The two Phillips curves, and policy for growth

the short-run Phillips curve

a trade-off: lower unemployment comes with higher inflation

the long-run Phillips curve

vertical at the **natural rate of unemployment**
trade-off in the long run

– no

what shifts SRPC

a change in **expected** inflation, or a supply shock

linking the graphs

a recessionary gap in AD–AS corresponds to a point **up and left** on the SRPC – high unemployment, low inflation

hyperinflation

what sustained excessive money growth produces

long-run growth policy

investment in **infrastructure, human capital and technology**, and secure property rights

Draw the AD–AS and Phillips graphs **side by side** and move both. Every question in this unit checks that the two pictures agree.

Two Phillips curves, one economy

Short-run

The **short-run Phillips curve (SRPC)** slopes down: with expectations fixed, lower unemployment comes with higher inflation.

Long-run

The **long-run Phillips curve (LRPC)** is vertical at the natural rate – no permanent trade-off, whatever inflation is.

Moving between

An AD increase moves *along* the SRPC; when expectations catch up, the SRPC shifts and unemployment returns to the natural rate.

Budget words

A budget **surplus** is revenue above spending; deficits accumulate into the national debt.

SRPC and AD–AS tell the same story twice. Whatever moves one moves the other – say which, in both diagrams.

Exercises 2.1-2.3

2.1 State two policies that promote economic growth.

[2]

2.2 State how research and development raises growth.

[1]

2.3 State one institutional factor important for long-run growth.

[1]

Exercises 2.1-2.3

2.1 State two policies that promote economic growth. [2]

2.1

- any two of: investment in physical capital (infrastructure), investment in human capital (education), support for R&D/technology
-

2.2 State how research and development raises growth. [1]

2.2

- it raises productivity, so more can be produced from the same resources
-

2.3 State one institutional factor important for long-run growth. [1]

2.3

- secure property rights, the rule of law, or good incentives (any one)

Exercises 3.1-3.2

3.1 Investment in human capital means spending on

[1]

☐

A machines and factories

B education and training

C government bonds

D imports

3.2 Which of these promotes long-run growth?

[1]

☐

A weak property rights

B research and development

C high inflation

D trade barriers

Exercises 3.1-3.2

3.1 Investment in human capital means spending on

[1]

- ☐ A machines and factories
B education and training
C government bonds
D imports

3.1 B

- education and training.

3.2 Which of these promotes long-run growth?

[1]

- ☐ A weak property rights
B research and development
C high inflation
D trade barriers

3.2 B

- research and development.

Exercise 3.3 (a)

3.3 A government wants to raise the economy's long-run growth rate.

(a) Name one policy involving **physical** capital.

[1]

Exercise 3.3 (a)

3.3 A government wants to raise the economy's long-run growth rate.

(a) Name one policy involving **physical** capital.

[1]

(a)

- build infrastructure or invest in machines/factories

Exercise 3.3 (b)

3.3 A government wants to raise the economy's long-run growth rate.

(b) Name one policy involving **human** capital.

[1]

Exercise 3.3 (b)

3.3 A government wants to raise the economy's long-run growth rate.

(b) Name one policy involving **human** capital.

[1]

(b)

- fund education or training

Exercise 3.3 (c)

3.3 A government wants to raise the economy's long-run growth rate.

(c) State why secure property rights matter for growth.

[1]

Exercise 3.3 (c)

3.3 A government wants to raise the economy's long-run growth rate.

(c) State why secure property rights matter for growth. [1]

(c)

- they give people the confidence to invest and innovate, knowing they keep the rewards