

*A macro FRQ point is a definition plus a direction: name the concept, then say which curve shifts, which way, and what happens to output, the price level or the interest rate. Write each definition below in one sentence, and always finish with “therefore ...”.*

## Measuring the economy

- Gross domestic product** – the market value of all final goods and services produced within a country in a given period
- Real GDP** – GDP valued at base-year prices, so that changes reflect output rather than inflation
- Unemployment rate** – the number unemployed as a percentage of the labour force, where the labour force excludes those not seeking work
- Structural unemployment** – unemployment arising from a mismatch between workers’ skills or location and the jobs available
- Frictional unemployment** – short-term unemployment while workers move between jobs; it exists even at full employment
- Natural rate of unemployment** – the sum of frictional and structural unemployment, the rate at which the economy is at full employment
- Consumer price index** – a measure of the price of a fixed basket of goods relative to a base year, used to calculate inflation
- Real interest rate** – the nominal interest rate minus the inflation rate; it is what determines borrowing and lending decisions

## Aggregate demand and supply

- Aggregate demand** – the total quantity of real output demanded at each price level, equal to consumption plus investment plus government spending plus net exports
- Short-run aggregate supply** – the total output firms will produce at each price level while input prices, especially wages, are fixed
- Long-run aggregate supply** – output at full employment, vertical at potential GDP because in the long run all prices adjust
- Recessionary gap** – the shortfall of equilibrium output below potential GDP, associated with unemployment above the natural rate
- Inflationary gap** – the excess of equilibrium output above potential GDP, which puts upward pressure on wages and prices
- Multiplier** – the factor by which an initial change in spending changes total output, equal to  $1 \div (1 - \text{MPC})$
- Crowding out** – the fall in private investment caused when government borrowing raises the real interest rate

## Money, banking and policy

---

**Money supply** – the total quantity of currency and deposits available in an economy; M1 is currency plus checkable deposits

**Required reserve ratio** – the fraction of deposits a bank must hold rather than lend; its reciprocal is the money multiplier

**Open market operations** – central bank purchases or sales of government bonds, which change bank reserves and so the money supply

**Expansionary monetary policy** – increasing the money supply to lower the nominal interest rate, which raises investment and shifts aggregate demand right

**Fiscal policy** – changes in government spending or taxation used to shift aggregate demand

**Phillips curve** – the short-run inverse relationship between unemployment and inflation; it is vertical in the long run at the natural rate

## The open economy

---

**Balance of trade** – the value of a country's exports minus its imports of goods and services

**Appreciation** – a rise in the value of a currency against another, which makes exports dearer and imports cheaper

**Loanable funds market** – the market in which savers supply and borrowers demand funds, determining the real interest rate