

3.2 Multipliers

Name: _____ Class: _____ Date: _____

Total: 11 marks**KEY WORDS** marginal propensity to consume 边际消费倾向 • to save (mps) 边际储蓄倾向

Objective

Build the skills to answer exam questions on **multipliers**.**You must be able to:**

- define the **marginal propensity to consume (MPC)** 边际消费倾向 and **to save (MPS)** 边际储蓄倾向, with $MPC + MPS = 1$
- calculate the **spending multiplier** $\frac{1}{1 - MPC} = \frac{1}{MPS}$
- explain why the **tax multiplier** is smaller in magnitude
- find the change in equilibrium real GDP from an initial change in spending or taxes

1 Worked examples

Study these first. Each one shows the method for a question type used later.

■ MPC and MPS

MPC is the fraction of extra income **spent**; MPS is the fraction **saved**; $MPC + MPS = 1$.

■ The spending multiplier

$$\text{multiplier} = \frac{1}{1 - MPC} = \frac{1}{MPS}.$$

A higher MPC gives a larger multiplier.

■ Change in GDP

 $\Delta GDP = \text{multiplier} \times (\text{initial change in spending})$. With $MPC = 0.8$, the multiplier is $\frac{1}{0.2} = 5$.

2 Practice

2.1 If $MPC = 0.75$, find the MPS. [1]

2.2 Find the spending multiplier when $MPC = 0.8$. [2]

2.3 Using that multiplier, find the change in GDP from \$10 billion of new spending. [2]

3 Exam-style questions

3.1 The spending multiplier is [1]

- A** $\frac{1}{1 - MPC}$
- B** $1 - MPC$
- C** MPC
- D** $\frac{MPC}{MPS}$

3.2 The tax multiplier is _____ the spending multiplier. [1]

- A** larger than
- B** smaller in magnitude than
- C** exactly equal to
- D** unrelated to

3.3 An economy has $MPC = 0.9$.

(a) Find the spending multiplier.

[2]

(b) Find the change in GDP from a \$5 billion rise in government spending.

[2]

Solutions

2.1 $MPS = 1 - 0.75 = 0.25$.

2.2 $\frac{1}{1 - 0.8} = \frac{1}{0.2} = 5$.

2.3 $\Delta GDP = 5 \times 10 = \50 billion.

3.1 A.

3.2 B.

3.3 (a) $\frac{1}{1 - 0.9} = \frac{1}{0.1} = 10$. (b) $\Delta GDP = 10 \times 5 = \50 billion.