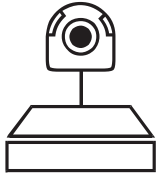
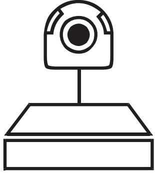


Unit 6, Lesson 37
Visual 1

KEYNESIAN THEORY

- Recessions and depressions can occur because of too little aggregate demand for goods and services.
- Inflation can occur because of too much aggregate demand for goods and services.
- Government can influence macroeconomic activity by influencing aggregate demand through fiscal and monetary policies.
- Fiscal policy (changes in government spending and taxes) is more powerful than monetary policy (changes in the money supply and interest rates).
- Monetary policy affects investment spending through interest rates.



Unit 6, Lesson 37
Visual 2

New Classical Theory

- The government's power to influence the macro-economy is limited and often ineffective.
- Consumers, business leaders, and investors are intelligent decision makers and take the effects of government policies into account in deciding on their behavior.
- People's actions often offset the effects of government fiscal and monetary policies.
- Monetarists believe the government should increase the money supply 3 to 5 percent a year and do no more.
- Rational Expectations theorists emphasize the role of forward-looking expectations in affecting economic growth, inflation and unemployment.
- Monetary and fiscal policies affect expectations and have unanticipated secondary effects that make these policies ineffective.