

SPD College, Garhwa

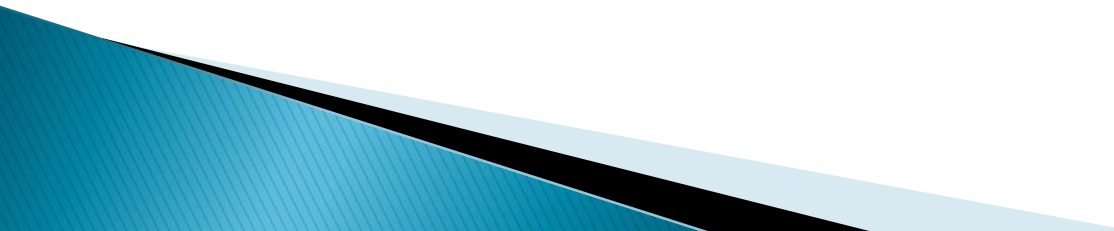
Department of Economics

Presentation on:

Determination of Income & Employment: JM Keynes
(UG NEP: MJ-2)

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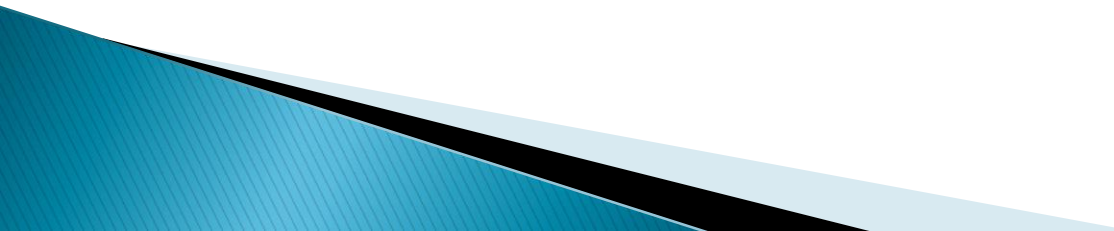
Main Points of the topic

- ❑ **Introduction**
 - ❑ **Assumptions**
 - ❑ **Explanation of the theory**
 - ❑ **Diagrammatic Representation**
 - ❑ **Components of the theory**
 - ❑ **Conclusion**
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Introduction

JM Keynes, in his renowned book 'The General Theory of Employment, Interest and Money – 1936' has explained modern theory of employment. In this theory Keynes has explained various components on which the volume of employment depends in the economy, causes of unemployment and remedies to increase or generate employment.

Assumptions of the theory

- ▶ Theory is based 'Short-run' in which the technique of production is constant.
 - ▶ Perfect competition is exists in factor and commodity markets.
 - ▶ Diminishing returns implies in agriculture.
 - ▶ Closed and Capitalistic economy
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Explanation of the Theory

- ▶ According to JM Keynes the total volume of employment depends on effective demand, it depends on:
 - Demand for Consumption Goods
 - Demand for Investment Goods

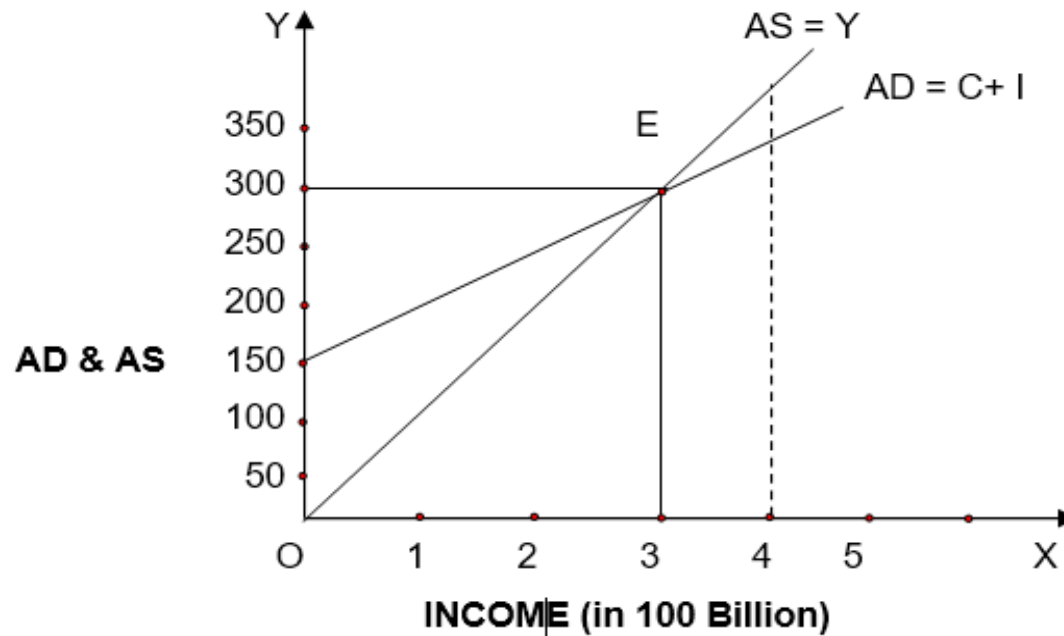
i.e. $ED = C + I$
- In an economy, the main cause of unemployment is reduction of effective demand. When income is increased in society, expenditure cannot increase in proportion to income, then a gap between income and expenditure created. This gap should be fulfilled by investment. But, investment does not increase as per requirement then unemployment comes.
- Determination of Effective Demand depends on two components: ADF and ASF

Explanation by Table

Level of Income (Y)	Aggregate Demand (AD = C + I)	Aggregate Supply (AS = Y = C + S)	Remarks
0	150	0	} AD > AS
100	200	100	
200	250	200	} AD = AS
<u>300</u>	<u>300</u>	<u>300</u>	
400	350	400	} AD < AS
500	400	500	
600	450	600	

This schedule shows that determination of equilibrium income level occurs at the point where the Aggregate Demand Schedule is equal to the Aggregate Supply Schedule in the economy.

Diagrammatic Representation



Explanation of the diagram

In the diagram, the point E is equilibrium point where aggregate demand and aggregate supply both are equal to each other. But, if income is increased to 400 billion, then $AD < AS$, this shows disequilibrium in the economy. In this situation the problem of over production of commodities and services will be occurred which will carry the economy towards unemployment as well as deflationary situations.

Components of Aggregate Demand (AD):

According to JM Keynes aggregate demand in an economy depends on two factors:

- consumption expenditure
- Investment expenditure
- i.e. $AD = C + I$

because aggregate demand is equal to aggregate expenditure in an economy.

Components of Aggregate Supply (AS)

According to JM Keynes aggregate supply in an economy is equivalent to flow/production of commodities and services during an accounting year. It depends on two factors:

- Consumption
- Saving
- i.e. $AS = C + S$

Conclusion

According to JM Keynes, aggregate supply remains constant in short-run, therefore aggregate demand plays vital role to determine income and employment in an economy. It is necessary to increase aggregate demand for generating employment in the economy.

----- The End -----



Thanks for watching

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