

Savings and Investment

Notes

“SAVINGS AND INVESTMENT” TARGETS

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SAVINGS AND INVESTMENT

Savings is important since it provides individuals with future wealth. Macroeconomists, however, view it as the vital tool for financing investment.

1) Savings

A)

B)

C)

2) Investment

A)

B)

C)

SAVINGS-INVESTMENT SPENDING IDENTITY

In our Warm Up activity, we proved that national savings always equals investment in a **closed economy** (an economy with no imports or exports).

1) National Savings

A)

B)

C)

2) Investment

A)

B)

IN AN OPEN ECONOMY

Now let's take a look at saving and investment in an **open economy**, which is one where exports and imports are allowed.

1)

2)

3)

4)

LOANABLE FUNDS MARKET

Savers and borrowers are brought together in various financial markets. For simplicity, economists lump all of them together as the **loanable funds market**.

1) Structure

A)

B)

2) Demand

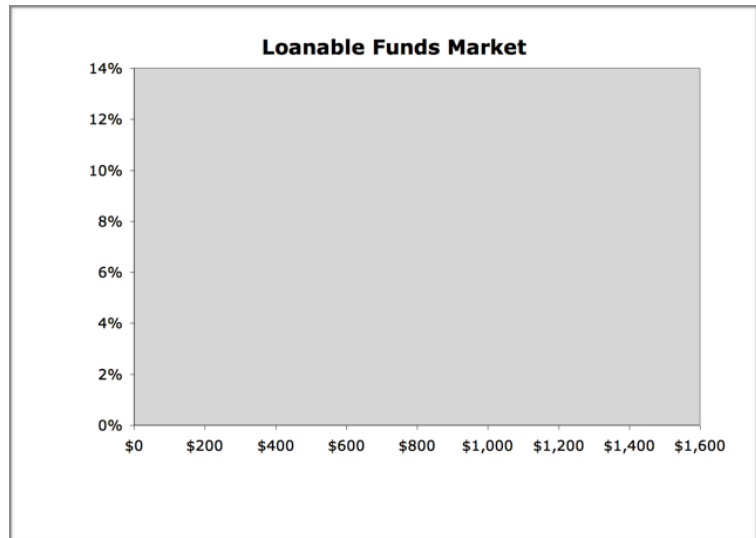
A)

B)

3) Supply

A)

B)



CHANGES IN LOANABLE FUNDS

The supply and demand curves can shift in the market for loanable funds. This affects the quantity and the interest rate.

1) Changes in Demand

A)

B)

C)

2) Changes in Supply

A)

B)

C)

CROWDING OUT

The loanable funds market illustrates how government policies on spending and taxation can have a significant effect on investment and the interest rate.

1) A budget deficit can CROWD OUT private investment.

A)

B)

C)

2) A reduction in taxes can increase investment

A)

B)

