

10.17: Assignment- The Income-Expenditure Model

Suppose the economy is operating at potential GDP, something like was the case for the U.S. in mid-2018. The unemployment rate has reached historic lows, suggesting that the economy is at full employment. Now suppose that due to an economic slowdown in Europe, U.S. export sales decline. Use the income-expenditure model to analyze the impact this decrease in export expenditures will have on U.S. GDP and employment. Show graphically and explain your economic reasoning.

To make this more concrete, here are some specific numbers to work with. Suppose potential GDP occurs where $Y = \$10,000$ billion. Suppose that the marginal propensity to consume is 0.75. If we assume that both taxes and imports are given then the simple expenditure multiplier formula applies. Suppose exports fall by \$100 billion. Use the multiplier formula to estimate the change in GDP. Suppose further that for every one percentage point that GDP falls below potential, the unemployment rate will rise by half of one percentage point. How much then will the unemployment rate rise due to the decrease in exports?

Rubric

Criteria	Not Evident	Developing	Proficient	Distinguished	Weight
Use the income-expenditure model to analyze this problem graphically, showing the initial and final equilibrium points. Label appropriately.					4
Correctly explain the economic reasoning about what happens to GDP and employment, and most importantly, why.					4
Use the simple expenditure multiplier formula to correctly compute the change in GDP.					4
Converting the change in GDP to percent, use the information provided to estimate the effect of the change in GDP on the unemployment rate (in percent).					4
Write up your analysis using correct language, explaining all your work					4
					Total: 20

CC licensed content, Original

- Assignment: The Income-Expenditure Model. **Authored by:** Steven Greenlaw and Lumen Learning. **License:** [CC BY: Attribution](#)

10.17: Assignment- The Income-Expenditure Model is shared under a [not declared](#) license and was authored, remixed, and/or curated by LibreTexts.