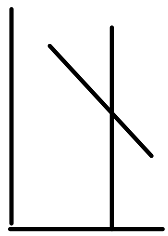
What is the market
for loanable funds?

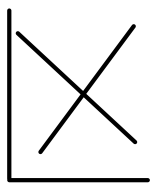
graph that displays the supply of
and demand for loanable funds.

money market
graph=nominal interest
rate (expected)



real=nom-inflation

loanable funds graph=real interest
rate



What's the difference?

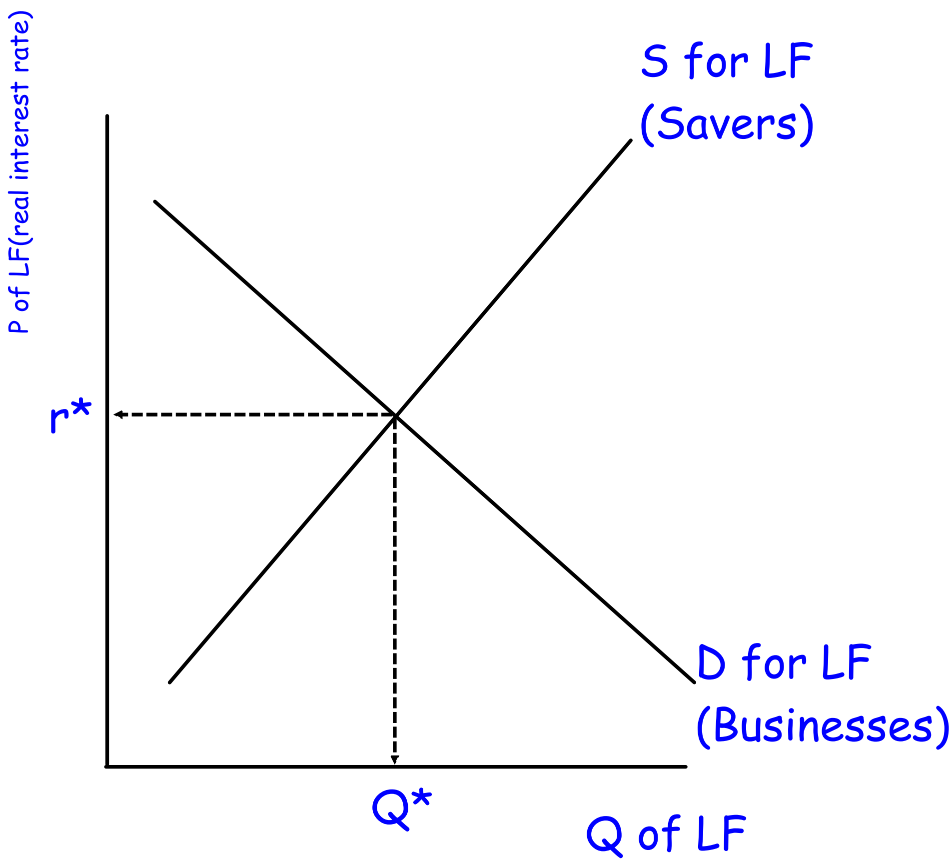
how do businesses decide if they are going to borrow money?

rate of return=rev-cost/cost*100

a project will cost 10M, generate revenue of 12M, what is the rate of return?

12-10/10*100=20% return

If interest rates are lower than 20%, then business will borrow

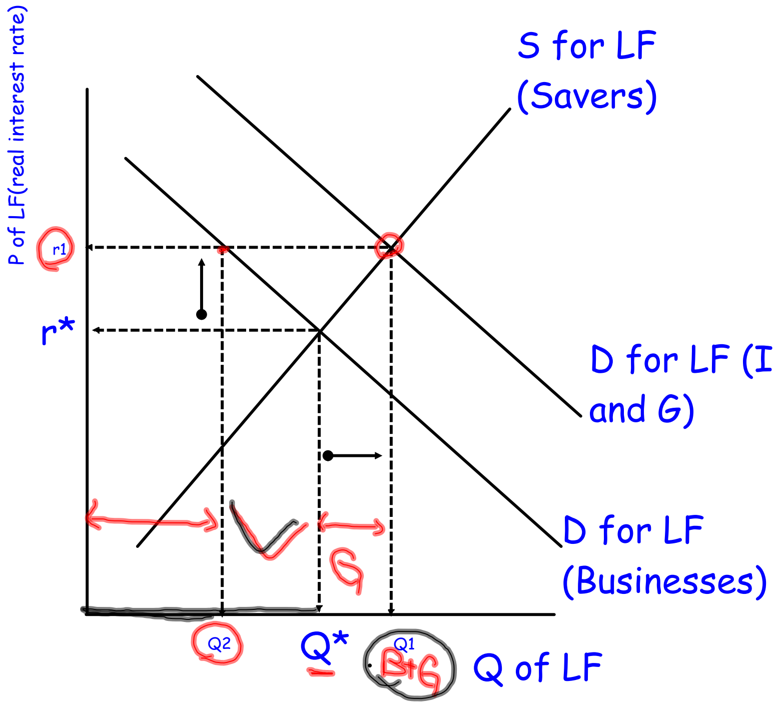


What shifts D for LF?

Changes in the predicted rate of return by businesses

What shifts D for LF?

Government borrowing:
if G borrows along with I, D for LF increases



G has increased the interest rate. As a result some businesses will decide not to borrow. This is called, crowding out.

What is the amount of crowding out that occurs in this graph?

What shifts the S of LF?

changes in the behaviors of savers
consumer confidence means less saving (S decreases)

consumer unease means more saving (S increases)

What shifts the S of LF?

Changes in Capital Inflows:

people who want to save in the US from other countries (belief that dollar is safe)

More money into country (S increases)

Less money into country (S decreases)

real interest rate=nominal interest rate-inflation

nominal interest rate=real interest rate+inflation

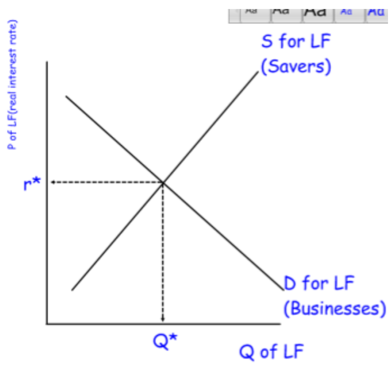
Fisher Effect: the expected real interest rate is unaffected by the change in expected future inflation

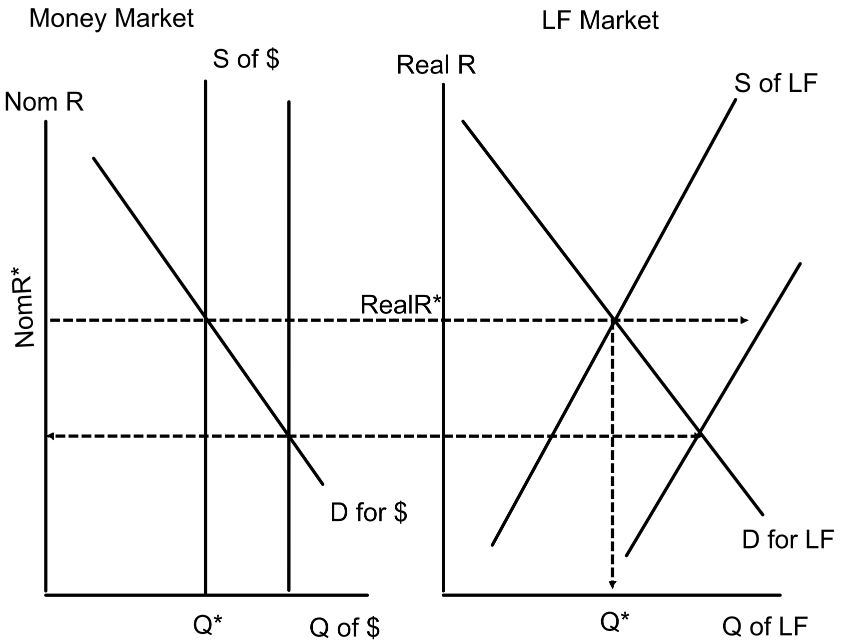
"As long as inflation is expected, it's built into the nominal rate"

savings-investment spending identity

total savings=total investment spending

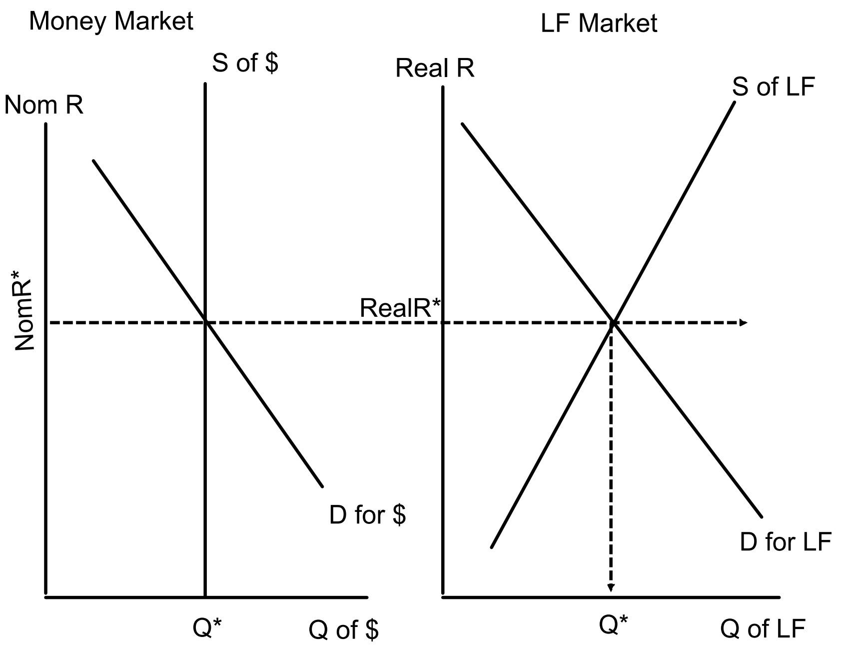
This is equilibrium on the LF Graph





When Fed increases MS, ir fall, real GDP rises. As RGDP rises, s of lf increases.

What happens when changes occur?



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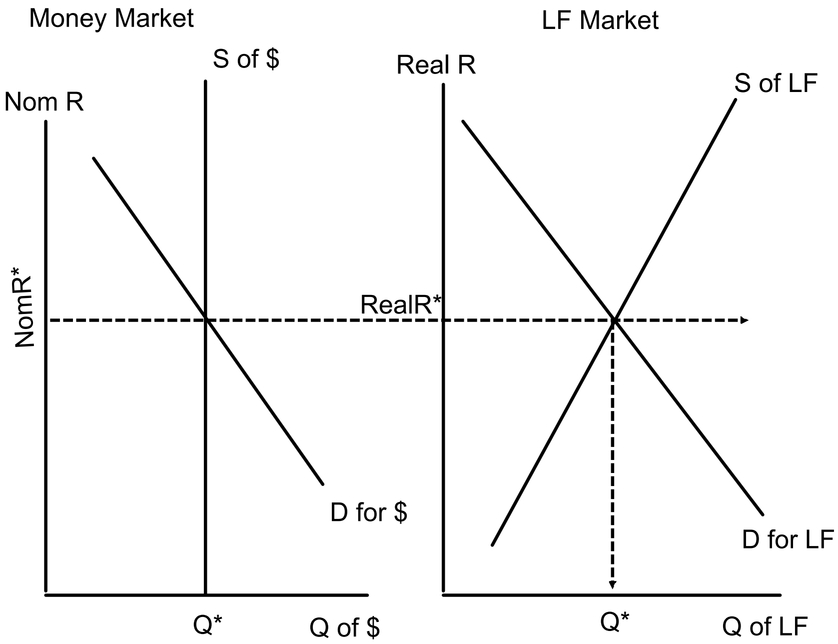

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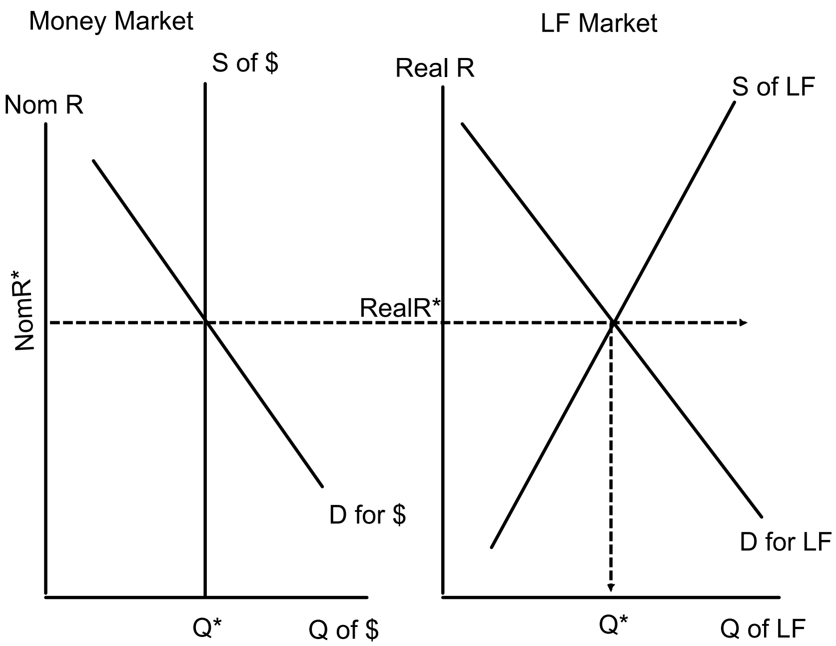

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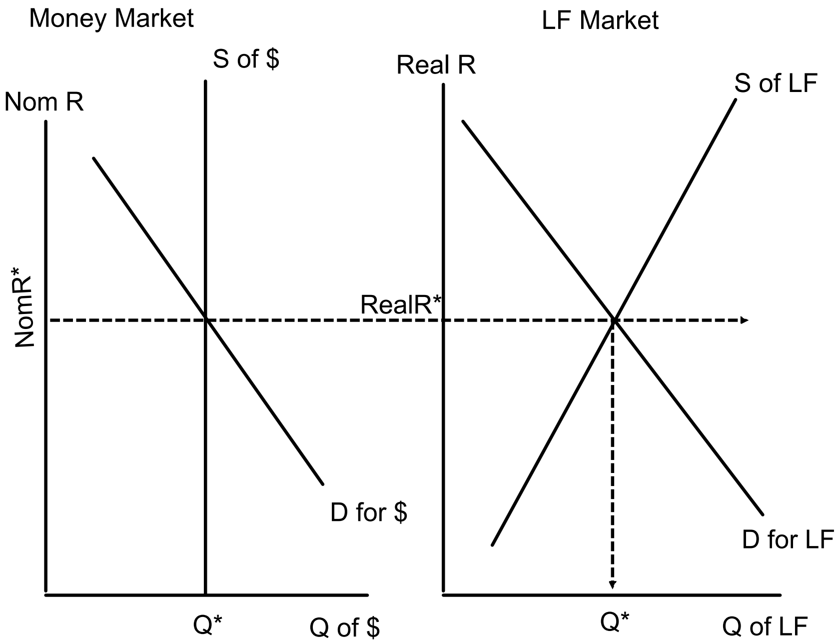

What happens when changes occur?