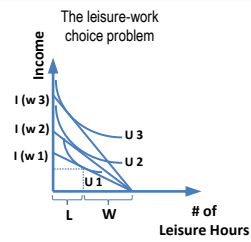
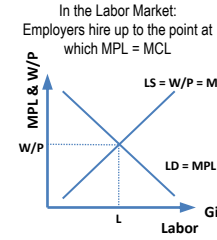
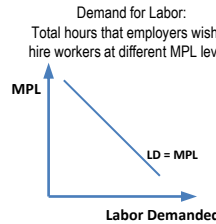
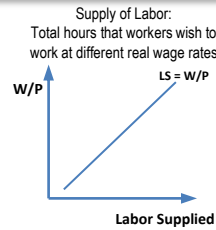
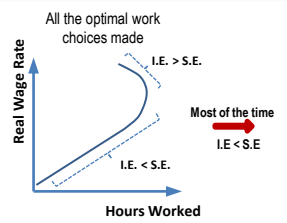


**First Building Blocks / Basic Definitions / Fundamental Ideas**

The Income/Leisure Trade-off

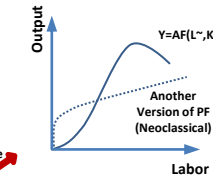


Work-Wage Space

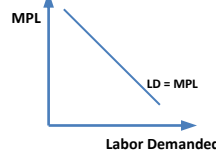
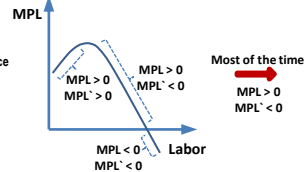


Supply Side

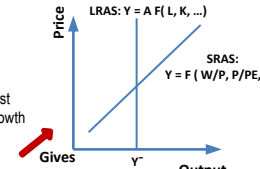
Diminishing Marginal Product of Labor AND Substitutability of L and K



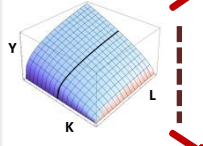
MPL-Input Space



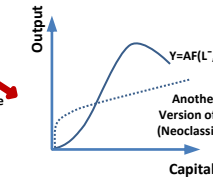
Optimal Capital in Solow Model: The marginal product of capital must equal depreciation plus population growth



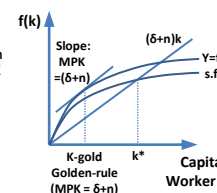
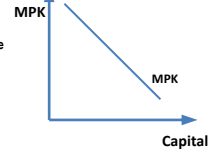
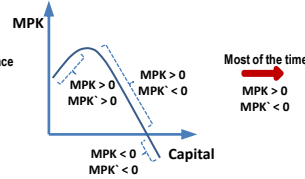
Y-L Space



Diminishing Marginal Product of Labor AND Substitutability of L and K



MPK-Input Space



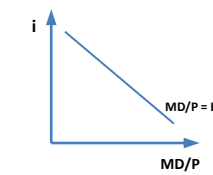
Gives W/P, Gives L, Gives L, Gives SRAS

$MS^- = M0 + M1 + \dots$   
Assumed to be set by the CB

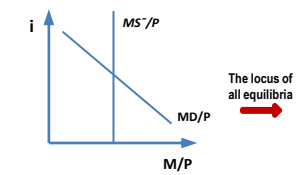
$MD = P \cdot L(Y, i)$   
b/c of three functions of money:  
1- Medium of exchange (Y)  
2- Unit of account (P)  
3- Store of value (i)

Saving - Real Interest rate relationship is an empirical one.

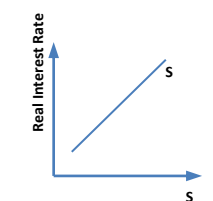
Interest rate is a part of users' cost of capital



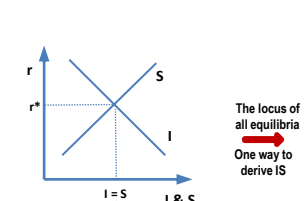
Adding \$MS^-\$ to the diagram



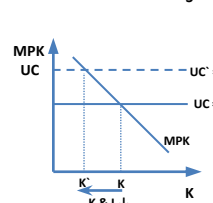
The locus of all equilibria



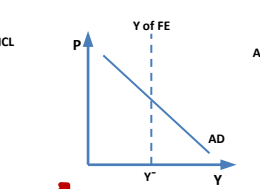
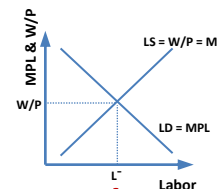
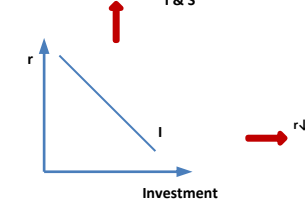
The locus of all equilibria



Another way to derive IS



Keynesian Cross



Demand Side

**LM Curve:**  
The combinations of interest rates and levels of real income for which the money market is in equilibrium  
OR: The set of equilibrium points between the liquidity preferences (or MD) function and the MS function

**IS Curve:**  
The equilibria where total private investment equals total saving  
OR: The locus of all equilibria where total spending equals an economy's total output

A Visual "Big Picture" for the General Equilibrium in the IS/LM/AS/AD Framework in Intermediate Macroeconomics