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A

Actual investment: the sum of planned and unplanned investment over a specified time period.

Actual saving: the level of saving achieved by households, based on the incomes they receive and the MPS.

Adaptive expectations theory: assumes that people form their expectations of future inflation on the basis of previous and present rates of inflation, and only gradually change their expectations as experience unfolds; thus expectations are backwards-looking, suggesting that continuous forecasting errors will be made.

Adjustable-peg system of exchange rates: system by which members of the IMF were obligated to define their monetary units in terms of gold (or US dollars), establishing par rates of exchange between the currencies of all other members, and to keep their exchange rates within 1 per cent of these par values.

Aggregate: a collection of specific economic units that are treated as if they were one unit.

Aggregate demand curve: represents the amount of goods and services—real GDP—that will be purchased at each possible price level.

Aggregate expenditures: the sum of expenditures on consumption (C), investment (I), government purchases (G) and net exports (NX).

Aggregate expenditures – output approach to income determination: the model that uses the relationship between aggregate expenditures and output to determine the equilibrium level of national income.

Aggregate supply curve: indicates the level of real domestic output that will be produced at each possible price level.

Aggregate supply shocks: sudden changes in one or more of the determinants of supply (for example, the OPEC oil shocks) leading to rapid changes in supply conditions affecting real GDP, the price level and employment.

Allocative efficiency: occurs when all available resources are devoted to the combination of goods most wanted by society.

Asset demand for money: the demand for money as a financial asset and store of wealth.

Assets: items of economic and financial value.

Average propensity to consume (APC): the fraction, or percentage, of any given total income that is consumed.

Average propensity to save (APS): the fraction, or percentage, of any total income that is saved.

B

Balance of payments account: a statement recording all the transactions that take place between a country's residents (including individuals, businesses and government units) and the residents of all foreign nations.

Balance of trade: the difference between a country's merchandise (goods) exports and its merchandise imports.

Balance sheet: a statement of assets and claims that summarises the financial position of a firm at a point in time.

Balanced-budget multiplier: the multiplier showing the amount by which equilibrium output is increased, following the use of a discretionary fiscal policy that neither increases nor decreases the budget deficit (because of equal increases in both government spending and taxes).

Bartering: the exchange of one good or service for another good or service.

Base year: the year containing the reference price level and output, relative to which price levels or outputs in other periods are judged.

Basic social capital: public infrastructure and utilities (e.g. roads, railways, schools, hospitals, housing, power stations).

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Break-even income: the level of income at which consumption expenditure exactly equals households' income.

Broad money: M_3 plus the borrowings from the private sector of non-bank financial institutions (NBFIs) less holdings of currency and bank deposits by the NBFIs.

Business cycle: the recurrent, somewhat cyclical, increases and decreases in the level or rate of growth in economic activity that typify the pattern of progress of our economy's real GDP over time.

C

Capital: all the manufactured aids to production used to produce goods and services and distribute them to the final consumer without directly satisfying human wants.

Capital account balance: the sum of net capital transfers (migrants' transfers and aid flow related to capital formation) and net sales of patents, copyrights, trademarks, franchises and embassy land (non-produced, non-financial assets).

Capital adequacy: the ability to make claims against shareholders sufficient to cover losses should the bank be liquidated. Currently, the banks are required to maintain financial capital equivalent to 8 per cent of their risk-weighted assets.

Capital flight: large-scale outflows of investment funds from the LDCs to the comparative safety of banks and other financial centres of the EACs to prevent seizure, or the erosion of value through inflation or depreciation of the currency.

Capital–output ratio: the ratio or relationship between net increases in the size and value of the capital stock (net investment) and sustainable increases in real GDP (capacity output).

Cash rate: the 'price'—interest rate—charged for exchange settlement funds.

Classical theory of employment: the view that underspending in a capitalist economy was highly unlikely, and that where this did happen the price system, through rapid adjustment of all prices (including interest rates and wages), would act to ensure the rapid return to full employment.

Closed economy assumption: the assumption that both the product and financial markets of the economy are fully isolated from the rest of the world.

Commodity terms of trade: the rate at which one commodity can be exchanged for another expressed in physical units of each commodity.

Comparative advantage: the ability to produce a commodity at relatively low opportunity cost in terms of the amount of the alternative commodity forgone.

Complementary goods: goods that are used in conjunction with each other; there is an indirect relationship between the price of one good and the demand for another.

Complex multiplier: the multiplier that arises when all leakages (saving, taxes and imports) are taken into account. It is represented by $1/[1 - MPC(1 - MPT) + MPM]$ or $1/[MPT + MPS(1 - MPT) + MPM]$.

Consumer price index (CPI): measures the price level of a 'market basket' of a variety of consumer goods and services that are purchased by a 'typical' family.

Consumption schedule: a schedule of the income–consumption relationship. The schedule shows the various amounts households plan or intend to consume at various possible levels of disposable income, which might conceivably prevail at some specific point in time.

Contractionary fiscal policy: discretionary budgetary policy that decreases government spending, increases taxes, or combines these actions, to reduce or eliminate inflationary pressures in the economy.

Cost ratio: the rate, due to movements in resources between sectors, at which the production of additional units of one commodity reduces the production of another; the opportunity cost of production.

Cost-push inflation: inflation associated purely with shifts in aggregate supply, due to cost factors, along a stable aggregate demand curve; often explained in terms of the market power of unions and businesses.

Currency (coins and notes): the coin and note components of the money supply.

Current account balance: the sum of the goods and services balance, income balance and current transfers balances.

Current transfers balance: net transfers, both public and private, from the rest of the world to Australians, including net pensions paid to/from Australia and net remittances to/from relatives abroad.

Cyclical peak: that point of the business cycle where economic activity has reached a temporary maximum.

Cyclical unemployment: unemployment caused by the business cycle—that is, by a deficiency in aggregate demand or total spending.

Cyclically adjusted budget deficit: indicates what the budget deficit (or surplus) would be if the economy were to operate at potential output throughout the year.

D

Debt crisis: an inability to service existing debt obligations and to attract further debt which has resulted from a convergence of forces, and which has had serious adverse effects on the ability of some developing economies to improve their rates of economic growth.

Demand-pull inflation: inflation associated purely with shifts in aggregate demand, resulting from changes in the components of aggregate expenditures, along a stable short-run aggregate supply curve. The economy attempts to spend beyond its capacity to produce—beyond its 'potential' level of output.

Dependent variable: variable which changes as a consequence of a change in some other (independent) variable; the 'effect' or outcome.

Deposit, credit or monetary multiplier: the reciprocal of the required reserve ratio, showing the maximum number of new dollars of deposits that can be created for a single dollar of excess reserves.

Depreciation: the annual charge that estimates the amount of capital equipment used up in each year's production.

Depression: a severe and prolonged recession.

Devaluation: an increase in the number of units of the domestic currency required to purchase a unit of foreign currency under the fixed or pegged exchange rate systems.

Direct relationship: where the values of two related variables change in the same direction.

Discouraged workers: workers who, after unsuccessfully seeking employment for a time, become discouraged and drop out of the labour force but would return if a suitable job prospect arose; often termed the 'hidden unemployed'.

Discretionary fiscal policy: the deliberate manipulation of taxes and spending by government for the purpose of altering real GDP and employment, controlling inflation and stimulating economic growth.

Disguised unemployment: unemployment that is not recognised, or measured, because the individuals concerned are currently 'employed', although they are underemployed and contribute little or nothing to total output.

Disinflation: reductions in, or elimination of, the rate of inflation.

Double counting: the separate inclusion of intermediate consumption in the value of final goods and services. The value of final goods and services includes any intermediate consumption required during the production process.

E

Easy monetary policy: RBA actions designed to reduce the cash rate, lowering the cost of, and increasing the availability of, bank credit in order to expand spending and real GDP.

Economic growth: increases in real GDP or real GDP per capita that occur over the long term.

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Economic resources: all the natural, human and manufactured resources that go into the production of goods and services.

Economically advanced countries (EACs): those of the world's nations with a high income per capita.

Economics: is concerned with the efficient use of limited productive resources for the purpose of attaining the maximum satisfaction of our material wants.

Efficiency: the result of using or administering scarce resources to produce the maximum amount of desired goods and services, thereby achieving the greatest possible fulfilment of society's wants.

Entrepreneurial ability: the human resource which combines the other resources to produce a product, make non-routine decisions, innovate, and bear risk.

Entrepreneurial class: the group in the community willing to bear risks, accumulate capital and provide the organisational requisites for economic growth, in return for incomes in the form of profit.

Equation of exchange: the basic equation of the monetarist school, given as $MV = PQ$ where M is the supply of money, V is the velocity of money (that is, the number of times per year the average dollar is spent on final goods and services), P is the price level, and Q is the level of real domestic output.

Equilibrium output: the level of total output that exists when the flow of income created by the production of the output gives rise to a level of total expenditures sufficient to clear the product market of that output.

Exchange controls: government rationing of the supply of foreign exchange among importers, with the objective of restricting imports to the amount of foreign exchange earned by exports.

Exchange rate: the price of a unit of one currency expressed in units of another currency.

Exchange rate appreciation: a reduction in the number of units of a country's currency required to purchase a single unit of some foreign currency.

Exchange rate depreciation: an increase in the number of units of a country's currency required to purchase a single unit of some foreign currency.

Exchange rate overshooting: the process by which adjustments in the exchange rate in the short term exceed those consistent with longer-term equilibrium because of differences in the speed of adjustment between asset market prices and product market prices.

Exchange settlement accounts: accounts kept by banks with the Reserve Bank to settle debts owing to other banks which arise as a result of the exchange of cheques, and to provide funds on which to draw additional notes and coin.

Excise taxes: a specific levy per physical unit usually placed on alcohol, tobacco and petroleum products.

Expansionary fiscal policy: the use of increased government spending and/or lower taxes, thereby increasing the government budget deficit, to stimulate economic activity and move the economy out of recession or depression.

Expenditure approach to GDP: measures GDP as the sum of all the expenditures involved in taking that total output off the market.

External balance: a level of the current account consistent with the maintenance of existing (or growing) levels of consumption, employment and national output over the long term.

F

Fiat money: money that draws its value from government decree, not through backing by precious metals or other valued commodities.

Final goods and services: goods and services that are being purchased for final use and are not to be subject to further processing, manufacturing or resale.

Financial account balance: the net flows of funds associated with direct investment in shares and

portfolio investment via shares and institutional loans, financial derivatives, other investment, and changes in the value of reserve assets.

Fixed (or pegged) exchange rates: exchange rates for which the values are determined by government decision.

Floating exchange rates: exchange rates for which the values are determined by the unimpeded forces of supply and demand.

Foreign-purchases effect: a rise in our domestic price level increases our imports and reduces our exports, thereby reducing net exports.

Free on board (fob): valuation of exports and imports is that for the actual goods and excludes insurance and freight costs.

Frictional unemployment: the level of unemployment associated with the efficient movement of workers between jobs (e.g. because they are switching jobs voluntarily; experiencing lay-offs due to seasonality; seeking labour market entry for the first time). Allows for the movement of labour from low-productivity to higher-productivity areas.

Full employment: a situation of labour market balance consistent with output at the economy's potential output level; cyclical unemployment is absent; the employment of all available resources.

Full production: the maximum amount of goods and services that can be produced from the employed resources of an economy.

Fundamental objective of monetary policy: the objective of assisting the economy to achieve a full-employment, non-inflationary level of total output.

G

Gains from trade: increases in consumption of goods and services allowed through the efficient allocation of resources and international exchange.

GDP gap: the amount by which the actual level of GDP falls short of the potential level of GDP.

Gold standard: a system under which the value of a nation's monetary unit was backed by gold rather than fiat.

Goods and services balance: the net difference between value of exports and imports of current goods and services.

Goods and services tax (GST): a form of value-added tax, where tax is added at each sale point in the production and distribution chain associated with the product. However, tax credits provided to business for any GST they have paid on the goods and services they use effectively means that the tax is paid only at the final point of sale.

Government purchases of goods and services (*G*): the sum of government final consumption expenditure, government gross fixed capital expenditure, and the increase in stocks of authorities.

Gross domestic product (GDP): the total market value of all final goods and services produced in the economy during a specific period.

Gross private investment (*I*): private gross fixed capital expenditure *plus* increases in stocks.

Growth economics: the area of economics concerned with the analysis of the patterns of long-term trends in an economy's productive capacity and the factors that influence and may alter these trends.

H

Human capital: the embodiment of productive capacity in the labour force; investment in people.

Hyperinflation: sustained, very rapid increase in the level of prices (very high inflation), leading to rapid erosion in the value of the monetary unit.

I

Implicit price deflator (IPD): a broadly based measure of the average level of prices in the economy, based on consumer goods and services, investment goods, goods and services purchased by government, and goods and services exported and imported.

Income approach to GDP: measures GDP as the sum of the incomes derived or created from the production of the GDP.

Income balance: net interest, dividend payments and reinvested earnings, plus net payments made to employed workers located outside their official country.

Incomes policies: government intervention in the labour and product markets, which is designed to constrain both nominal incomes and prices paid in order to influence real incomes.

Independent goods: goods that are not related at all, so that a change in the price of one good will have negligible impact on the demand for the other.

Independent variable: variable which causes a change in some other (dependent) variable.

Indirect taxes: excise taxes, licence fees and customs duties. Businesses treat these taxes as costs of production and therefore add them to the prices of their products.

Inferior goods: commodities whose demand varies inversely with money income.

Inflationary expectations: expectations about the likely future path and rate of increase of the general level of prices.

Inflationary gap: the amount by which aggregate spending exceeds that required to achieve the full-employment level of GDP. This excess of aggregate expenditures produces an inflationary impact on the economy.

Injection: that component of spending that is not related to consumption spending by households, representing a supplement or addition to the income–expenditures stream (e.g. investment expenditure by businesses).

Interest-rate effect: as the price level rises, so do nominal interest rates; rising interest rates cause reductions in certain kinds of consumption and, most importantly, investment spending.

Intermediate consumption: the cost of intermediate goods and services.

Intermediate goods and services: goods and services that are subject to further processing, manufacturing or resale.

International monetary reserves: stocks of foreign monies owned by a particular government.

Inverse relationship: where the values of two related variables move in opposite directions.

Investment: the process of producing and accumulating capital goods.

Investment demand schedule: a schedule of the investment – interest rate relationship. The schedule shows the cumulative level of investment demanded at various possible levels of the interest rate, which might conceivably prevail at some specific point in time.

K

Keynesian economics: the body of theory refined and extended from the economics of Keynes. The schools of thought associated with this body of theory view the capitalist economy as inherently unstable and likely to achieve equilibrium with considerable unemployment or severe inflation, rather than a sustainable full-employment level of output.

Keynesian equation: the basic formulation of the aggregate expenditures basis for GDP ($C + I + G + NX = GDP$) showing that, in equilibrium, aggregate expenditures equal GDP.

L

Labour: a broad term the economist uses for all human physical and mental talents (excluding entrepreneurial ability) that can be used in producing goods and services.

Labour- (land-, capital-) intensive commodity: a commodity in which the production process uses relatively large amounts of the labour (land, capital) resource compared with the average rate at which this resource is combined with others in the economy's production process.

Labour productivity: real output per worker per hour.

Land: an economic resource which includes all the natural resources that go into the production of goods and services.

Land reform: the reform of current systems of ownership and tenure so as to improve the efficiency of allocation of land used for agricultural production.

Law of demand: the inverse relationship between the price and the quantity demanded of a good or service during some period of time.

Law of diminishing returns: as successive equal increments of one resource (e.g. labour) are added to a fixed resource (e.g. land), beyond some point the resulting increases in total output (marginal products) will diminish in size.

Law of one price: when converted to a common currency value through the exchange rate, the price of identical goods should be the same across national boundaries.

Law of supply: the direct relationship between the price and the quantity supplied of a good or service during some period of time.

LDC debt crisis: an inability to service existing debt obligations and to attract further debt which resulted from a convergence of forces during the 1970s and 1980s, and which has had serious adverse effects on the ability of the LDCs to improve their rates of economic growth.

Leakage: that part of income paid to households that is not consumed by households, representing a withdrawal or diversion of potential spending from the income–expenditures stream (e.g. savings).

Leakages–injections approach to income determination: the model that uses the required relationship between leakages from, and injections back into, the expenditure flow to determine the equilibrium level of national income.

Legal tender: an acceptable form of payment for debt owed.

Least developed countries (LDCs): those of the world's nations that have low per capita incomes; that is, they are less developed in their ability to provide incomes and economic consumption for their population.

Liabilities: the financial claims of non-owners (creditors) against the firm's assets.

Lump-sum tax: a tax that collects the same amount of tax revenue, the lump sum, at each level of GDP.

M

M_3: the sum of currency (coins and notes), current (or demand) deposits in banks on which cheques can be drawn, and non-current deposits in banks (e.g. savings).

Macroeconomic stability: the simultaneous existence of full employment, price-level stability, and external balance.

Macroeconomics: is concerned either with the economy as a whole or with the basic subdivisions or aggregates that make up the economy.

Malthus's thesis: given diminishing returns, persistent and substantial population growth will force and maintain the standard of living close to the subsistence level.

Managed floating exchange rates: the system where central banks buy and sell foreign exchange to smooth out short-run or day-to-day fluctuations in rates to encourage international trade and finance, while allowing for trend or long-term exchange rate flexibility to correct fundamental payments disequilibria.

Marginal propensity to consume (MPC): the ratio of the change in consumption to the change in income that brought about the consumption change. The MPC thus represents the fraction of each additional (or marginal) dollar of income that will be used for consumption expenditures.

Marginal propensity to save (MPS): the ratio of the change in saving to the change in income that brought about the saving change. The MPS thus represents the fraction of each additional (or marginal) dollar of income that will be directed to saving.

Market: a mechanism or arrangement that brings buyers ('demanders') and sellers ('suppliers') of a good or service in contact with one another.

Material wants: the desires of consumers to obtain and use various goods and services that give utility.

Microeconomics: is concerned with specific economic units and a detailed consideration of the behaviour of these individual units.

Monetary approach: looks at the relationship between the domestic money supply, the domestic demand for money, and the exchange rate.

Monetary base or high-powered money: the net *monetary* liabilities of the government to the non-bank public and the banks in the form of currency held by the public, currency held by the banks, and banks' demand deposits with the Reserve Bank of Australia.

Monetary policy: influencing the economy's interest rates and credit availability to assist in stabilising real GDP, employment and the price level.

Monetary rule: the rule that the money supply be expanded each year at the same rate as GDP.

Money: any item which is generally acceptable to buyers and sellers for facilitating the exchange of goods and services.

Money as a medium of exchange: money is usable for buying and selling goods and services.

Money as a store of value: the role of money as a form in which to store wealth, due to its liquidity and convenience.

Money as a unit of account: the use of the monetary unit as a yardstick for measuring the relative worth of heterogeneous goods and resources.

Multiplier: the ratio of a change in equilibrium GDP to the original change in investment spending (or other autonomous spending) that caused that change in real GDP.

Multiplier effect: the result that a change in investment spending (or other autonomous spending) gives rise to a larger change in the output–income level.

N

Natural rate hypothesis: the suggestion that there is a unique level of unemployment around which observed unemployment will fluctuate, but that the economy will tend towards at any point in time.

Natural rate of unemployment: the sum of the rates of frictional and structural unemployment.

Net export effect: the impact of interest-rate-induced changes in the level of the exchange rate, and thus net exports, following changes in fiscal policy. The net export effect reduces the effectiveness of fiscal policy.

Net exports: the difference between the value of exports and imports ($X - M$).

Net private investment: additions to the level of the economy's stock of investment goods made by non-government enterprises.

Net worth: the financial claims of the owners of a firm against the firm's assets.

New classical economics: the school of thought most closely associated with the use of the RET position, which shares the classical school's belief in the highly competitive markets underlying the economy's operation.

New International Economic Order (NIEO): a new structure for the relationship between the LDCs and the EACs which would see a lower level of exploitation of the situation of the LDCs by the EACs and a recognition of the LDCs as equal partners in the world's economic and political institutions.

Nominal GDP: money GDP; GDP measured at current prices; GDP measured at dollars of the period.

Nominal income: the number of dollars received as wages, rent, interest or profits.

Nominal interest rate: the percentage increase in money that the lender receives from the borrower.

Non-bank financial institutions (NBFIs): permanent building societies, credit cooperatives, money market corporations (merchant banks), pastoral finance companies, finance companies, general financiers and cash management trusts.

Non-discretionary fiscal policy: built-in stabilisers that tend to increase the government's deficit (or reduce its surplus) during a recession and to increase its surplus (or reduce its deficit) during inflationary periods without requiring explicit action by policy makers.

Non-financial investment: the accumulation of capital by transferring surplus agricultural labour to the improvement of agricultural facilities or to the construction of basic social capital.

Non-productive transactions: transactions where no production of goods or services occurs. This includes purely financial transactions and second-hand sales.

Normal goods: commodities whose demand varies directly with money income; also known as superior goods.

O

Okun's law: the quantified relationship between the unemployment rate and the GDP gap.

Open-economy multiplier: recognises that imports represent a leakage from the aggregate expenditures – income flow. The simple open-economy multiplier is given by $1/(MPS + MPM)$ where MPM is the marginal propensity to import.

Open-market operations (OMOs): the buying and selling of government securities by the RBA in the cash or short-term money market.

Opportunity cost: the amount of other products that must be forgone or sacrificed to obtain a unit of any product.

P

Paradox of thrift: the paradox that if society attempts to save more, it may end up actually saving the same amount or even less, as a result of the multiple decline in the equilibrium GDP caused by the withdrawal of aggregate expenditures.

Participation rate: those in the specified labour force group expressed as the percentage of the civilian population aged 15 and over in that specified group.

Personal consumption expenditures (*C*): expenditures by households on durable consumer goods, non-durable consumer goods, and services.

Phillips curve: an inverse relationship, suggestive of a trade-off between inflation and the unemployment rate, apparent in some of the empirical work of economists in the late 1950s and 1960s.

Planned investment: the level of investment, including inventory investment, that businesses plan to make within the specified period.

Planned saving: the level of savings that households intend to achieve over a specified period.

Portfolio balance approach (PBA): looks at changes in exchange rates resulting from shifts in investors' holdings of assets. These shifts occur in response to changes in the relative real returns, both available and expected, on assets in each country.

Post-hoc fallacy: a hazard in economic reasoning in which the assumption is made that simply because one event precedes another, the first event is the cause of the second.

Potential output: the real level of domestic output that is associated with the natural rate of unemployment.

Preferential tariff treatment: a system whereby the EACs place a lower rate of tariff on exports from LDCs than that applied to imports from other EACs, with the objective of stimulating the industrial growth of the LDCs.

Price-level surprises: unanticipated changes in the price level, which allow deviations from long-run supply to occur.

Price–wage flexibility: the assumption that all prices, including wages and interest rates, are flexible and will rapidly adjust to remove disequilibria.

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Price–wage inflexibility: the assumption that all prices, including wages and interest rates, are inflexible, especially over the short term, and do not adjust to remove disequilibria over this period.

Prime assets ratio (PAR): the proportion of banks' total liabilities (not including shareholders' funds) that must be held in highly liquid form. This includes currency, deposits with the Reserve Bank, and government securities. The PAR reflects both negotiations with the Australian Regulation Authority (APRA) and prudent banking practice.

Principle of comparative advantage: that nations should specialise in the production of those goods and services in which they have a comparative advantage, allowing an increase in consumption possibilities through trade and specialisation.

Private economy assumption: the assumption that there is no explicit contribution by government to either the product or financial markets.

Productive efficiency: occurs when goods or services are produced using the lowest cost production methods.

Productivity: the relationship between real output and the quantity of inputs used to produce it, often measured as average real output per unit of input.

Profit-push inflation: inflation brought about by big businesses through its power to adjust or administer price increases that are neither initiated nor justified by increases in wage costs.

Public debt: the total accumulation of the federal government's total deficits and surpluses that have occurred over time.

Purchasing power parity: suggests that the purchasing power of different currencies should be the same when converted to a common currency value through the exchange rate.

R

Rapid rural–urban migration: the rapid transfer of rural labour to urban centres; often precipitated by a substantial urban–rural wage differential, which, because of the lack of actual job opportunities in urban areas, leads to substantial increases in unemployment rates.

Ratchet effect: the result of the tendency for prices of both products and resources to be individually 'sticky' or inflexible in a downward direction, leading to a loss in downward flexibility of the general level of prices.

Rate of capital accumulation: the rate at which net investment, or additions to the capital stock, occurs.

Rational behaviour: behaviour that involves decisions and actions by individuals in order to achieve the greatest satisfaction or maximum fulfilment of their goals.

Rational expectations theory (RET): businesses, consumers and workers understand the economy and use this knowledge to assess the anticipated effects of current economic policies on the future of the economy and to make decisions that best further their own self-interests.

Real GDP: GDP at constant prices; GDP figures that have been inflated or deflated to account for changes in the price level.

Real income: the amount of goods and services that can be purchased with money income.

Real interest rate: the percentage increase in purchasing power that a lender receives from a borrower in exchange for the borrower's use of the lender's fund.

Real-balances effect: at a higher price level the real value or purchasing power of the accumulated financial assets held by the public falls; the fall in real wealth of the public leads to a reduction in consumption expenditures. (Also referred to as the wealth effect.)

Recession: a period where rates of growth in output and employment both decline to low or negative levels.

Recessionary gap: the amount by which aggregate expenditures fall short of that required to generate the full-employment level of GDP. This deficiency of aggregate expenditures produces a contractionary or depressing impact on the economy.

Recovery: the phase of the business cycle where the economy's levels of output and employment expand towards the full-employment or capacity level.

Repurchase agreement (repo or RP): agreement detailing the price, timing and conditions under which the banks and the RBA may exchange government securities.

Required reserve ratio: the ratio of reserves to deposits required to meet official liquidity requirements and additional requirements determined by normal banking practice.

Revaluation: a reduction in the number of units of the domestic currency required to purchase a unit of foreign currency under the fixed or pegged exchange rate systems.

S

Saving schedule: a schedule of the income–saving relationship. The schedule shows the various amounts households plan or intend to save at various possible levels of disposable income, which might conceivably prevail at some specific point in time.

Say's law: this law states that the very act of producing goods generates an amount of income exactly equal to the value of the goods produced. Thus the production of any output automatically provides the incomes required to take that output off the market—supply creates its own demand.

Seasonal variations in business activity: regular fluctuations in the tempo of business activity that are independent of the business cycle, and that occur particularly in the retail industry (e.g. the pre-Christmas buying rush).

Secular trend: the average (or trend) rate of expansion or contraction of an economy over the long term (e.g. 25, 50, 100 years).

Simple multiplier: the multiplier based on the private, closed model of the economy, where the 1/MPS formulation reflects only the leakage of saving.

Special drawing rights (SDRs): bookkeeping entries at the IMF, available to IMF members in proportion to their IMF quotas, that may be used to settle payments deficits or satisfy reserve needs in place of foreign exchange or gold.

Stabilisation fund: supplies of both foreign and domestic monies and gold held with the central bank or treasury for the purpose of intervention in the foreign exchange market to maintain the par value of the exchange rate.

Stagflation: the simultaneous experience of both high and increasing unemployment and inflation.

Strikes: a form of industrial action by which employees withdraw some or all of their labour.

Structural unemployment: unemployment resulting from mismatches in the skills and geographic location of labour due to changes in the composition of the total demand for labour, which in turn have been caused by changes in consumer demand and in technology.

Subsidies: payments to businesses to encourage production of a particular commodity or use of a particular resource (effectively negative indirect taxes).

Substitute goods: goods that can be used in place of another good; there is a direct relationship between the price of one good and the demand for another.

Supply-side shocks: rising product prices caused by increases in the costs of raw materials, inputs or energy.

T

Terms of trade: the ratio of the average price of the goods and services exported by a country to the average price of its imports.

Tight monetary policy: RBA actions designed to increase the cash rate, increasing the cost of, and reducing the availability of, bank credit in order to constrain spending and reduce inflationary pressures.

Token money: money for which the intrinsic value of the commodity used to hold the monetary unit (e.g. a coin or note) is less than the recorded value of the money.

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Trade-weighted index: an index of the 'average' exchange rate, comprised of a basket of currencies of Australia's major trading partners weighted to reflect their relative importance in our total trade.

Trading possibilities line: a line showing the rate at which one commodity can be exchanged for another during international trade. The slope reflects the international commodity terms of trade.

Transactions demand for money: the demand for money as a medium of exchange.

Trough: a period where output and employment growth 'bottom out' at their lowest levels.

U

Underemployed: part-time employees who want to work more hours but are unable to do so. This may be because of their inability to find suitable full-time work (or additional hours), or the imposition of short hours due to a temporary slack in consumer demand.

Unplanned investment: unintended changes in the level of business inventories.

Utility: the economist's term for pleasure or satisfaction.

V

Value added: the market value of a firm's output less the value of its intermediate consumption.

Vault cash or till money: currency held by a bank to meet customers' currency needs.

Vicious circle of underdevelopment: low per capita incomes are associated with limited ability or incentive to save, and low levels of demand; limited available resources and lack of demand reduce incentives for investment in real or human capital; a lack of investment in real and human capital means that labour productivity is low; output per person is real income per person, so per capita income is low; and so on.

W

Wage–price inflationary spiral: a continuous cycle of money-wage and price rises that feed on each other.

Wage-push inflation: cost-push inflation initiated through wage increases obtained by unions.

World Bank Group: the International Bank for Reconstruction and Development (IBRD), the International Development Association (IDA), the International Finance Corporation (IFC) and two other agencies.