Illustrating the Demand for Loans

Some Illustrations

People Become More Optimistic About the Future

People Become More Optimistic About the Future

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A Temporary Reduction in Income

The net demand curve shifts to the right. Interest rates rise

People reduce consumption by less than the drop in income, shifting the demand for loans to the right.
A Temporary Reduction in Income

There may be a reduction in investment, shifting the demand to the left.

If the net effect is a left shift, interest rates will fall.

Why Do We Care?

Two Extensions

• Government Demands
  – The government almost never spends exactly what it takes in. Its transactions affect the supply and demand for loans.

• The World Market
  – International lending is around $300 billion per year; international borrowing runs about $500 billion per year. We cannot neglect the international sector.

Two Extensions

End

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