CONCEPT: AVERAGE AND MARGINAL PROPENSITIES TO CONSUME AND SAVE

● There are two things that can be done with disposable income: ______________ and ______________

☐ ***Average Propensity to Consume*** – the fraction of total income that is used for consumption

$$APC = \frac{Consumption}{Income}$$

☐ ***Average Propensity to Save*** – the fraction of total income that is used for savings

$$APS = \frac{Saving}{Income}$$

☐ ***Marginal Propensity to Consume*** – the amount by which consumption changes when income increases

$$MPC = \frac{\Delta\, Consumption}{\Delta\, Income}$$

☐ ***Marginal Propensity to Save*** – the amount by which saving changes when income increases

$$MPS = \frac{\Delta\, Saving}{\Delta\, Income}$$

PRACTICE: If the Keynesian consumption function is C = 10 + 0.8 Yd then, when disposable income is $1000, what is the average propensity to consume?

a) $0.8
b) $800
c) $810
d) $0.81
e) Cannot be determined

PRACTICE: If the Keynesian consumption function is C = 10 + 0.8 Yd then, when disposable income is $1000, what is the marginal propensity to save?

a) 0.8
b) 0.81
c) 0.19
d) 0.2
e) Cannot be determined