

Consultancy to Develop and Implement a  
Macroeconomic Model for Lesotho (DIMMoL)

## Macro-Econom(etr)ic Modelling

### Part 4

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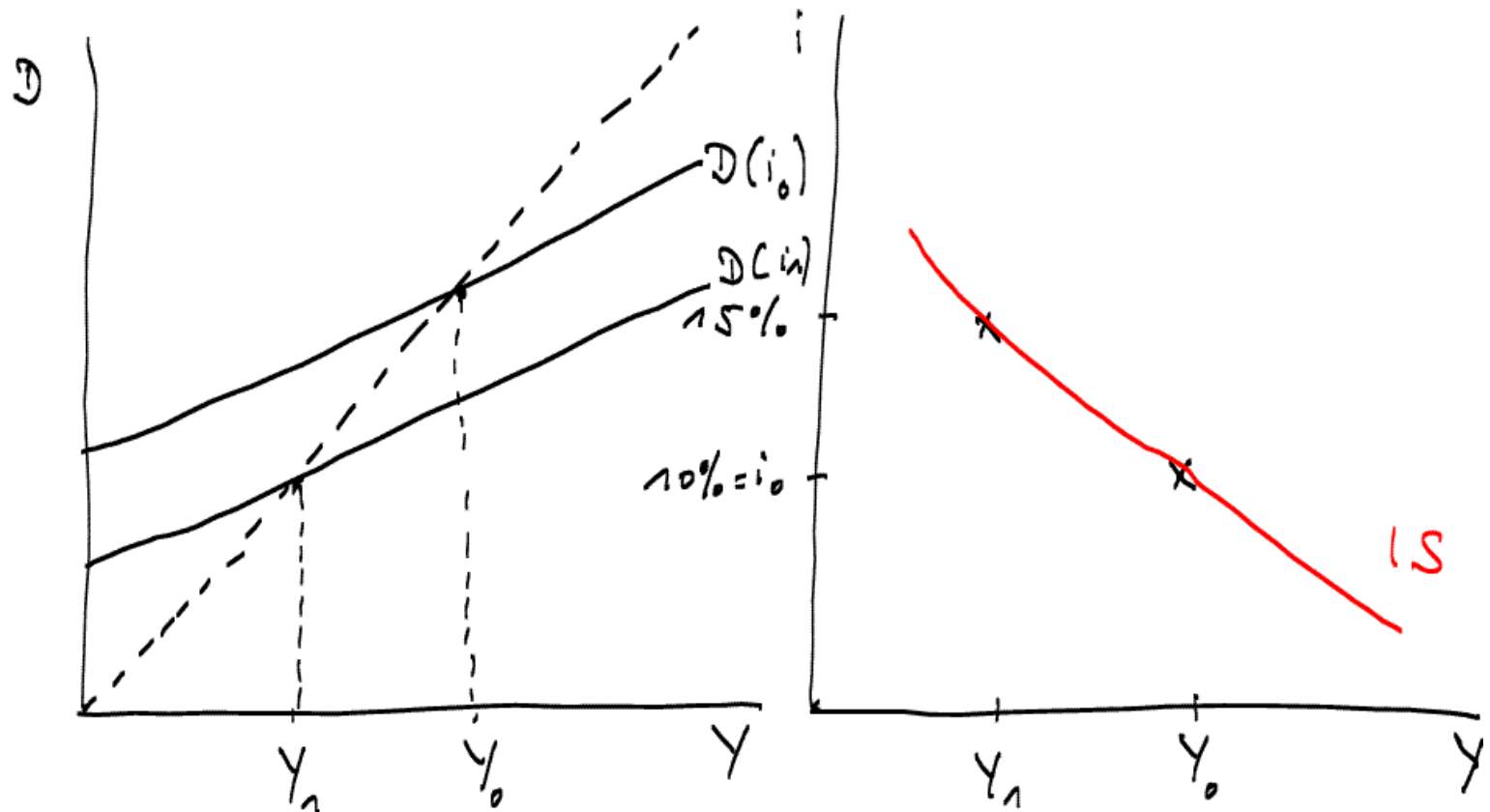
# Course program

- Introduction
- Outline of macroeconom(etr)ic models
- **Macroeconomic framework (cont.)**
- Econometric methodology
- Applied econometrics with EViews
- Lesotho case studies

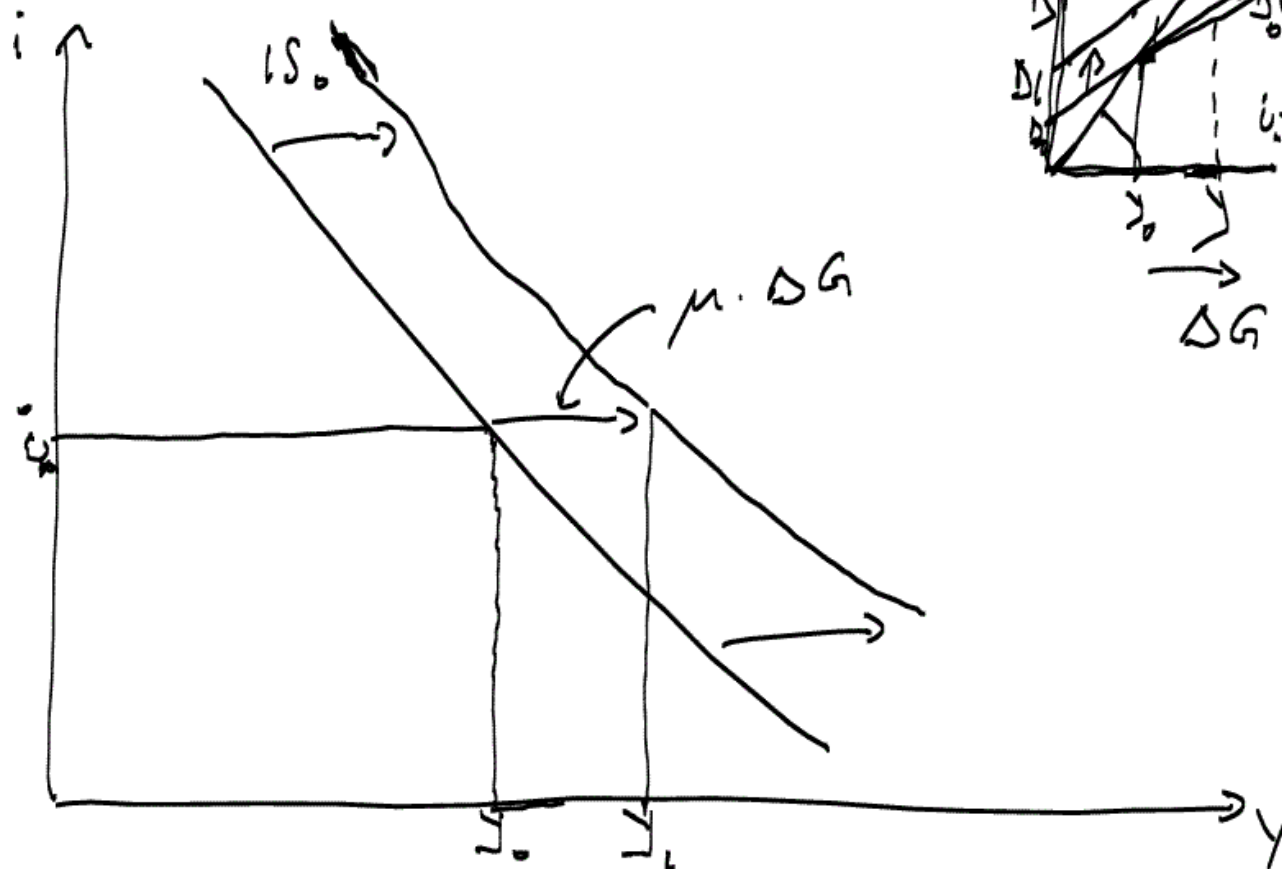
## **Income-expenditure model: Main points**

- Production follows demand  
(no limiting supply-side factors)
- Exogenous prices
  - goods market
  - interest rate
  - wage rate
  - exchange rate
- Multiplier effect depends on
  - marginal propensity to consume (+)
  - marginal tax rate (-)
  - marginal import rate (-)
- Income expansion reduces trade surplus

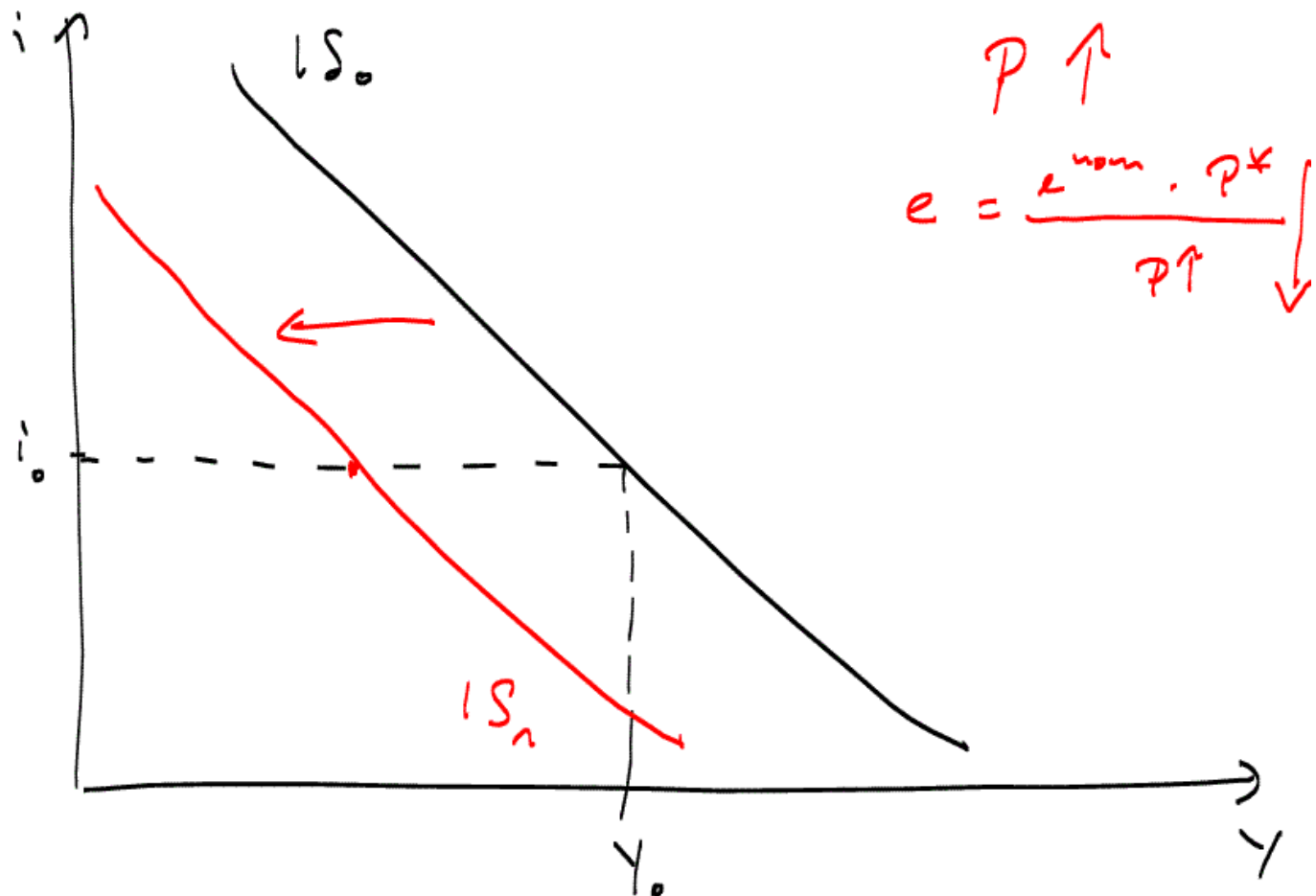
# IS-curve: Construction



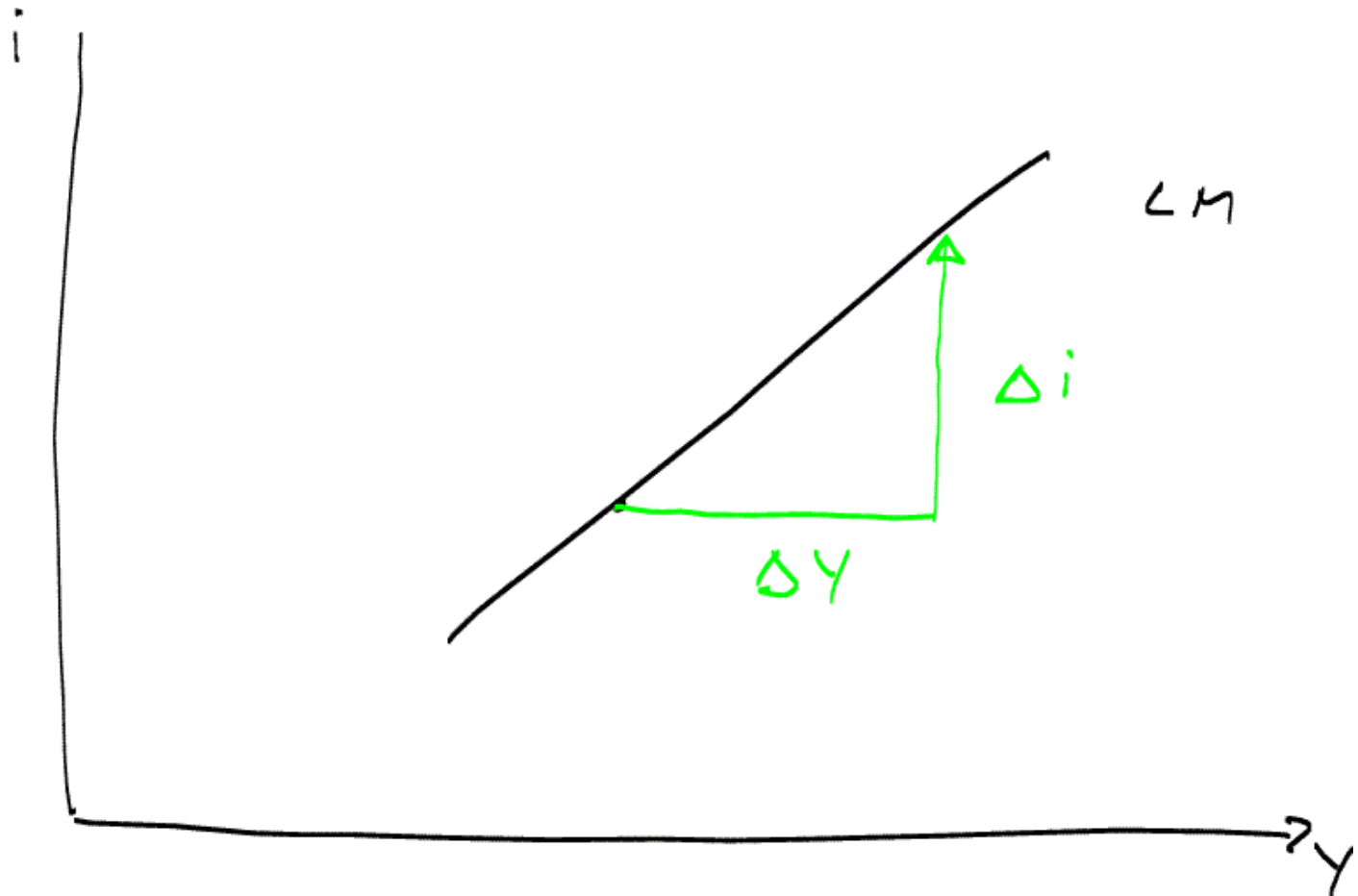
# IS-curve: Response to fiscal policy



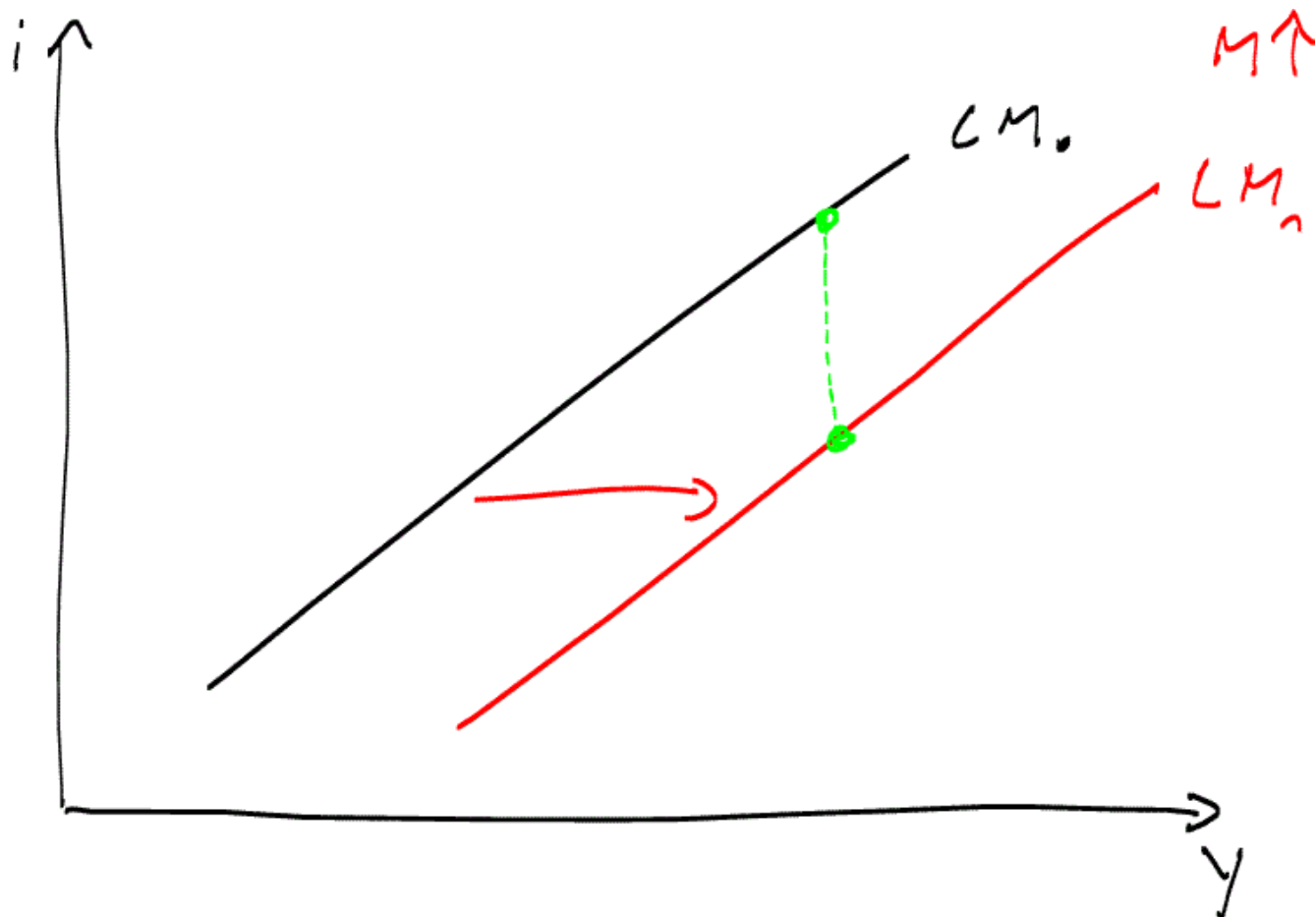
## IS-curve: Response to price movements



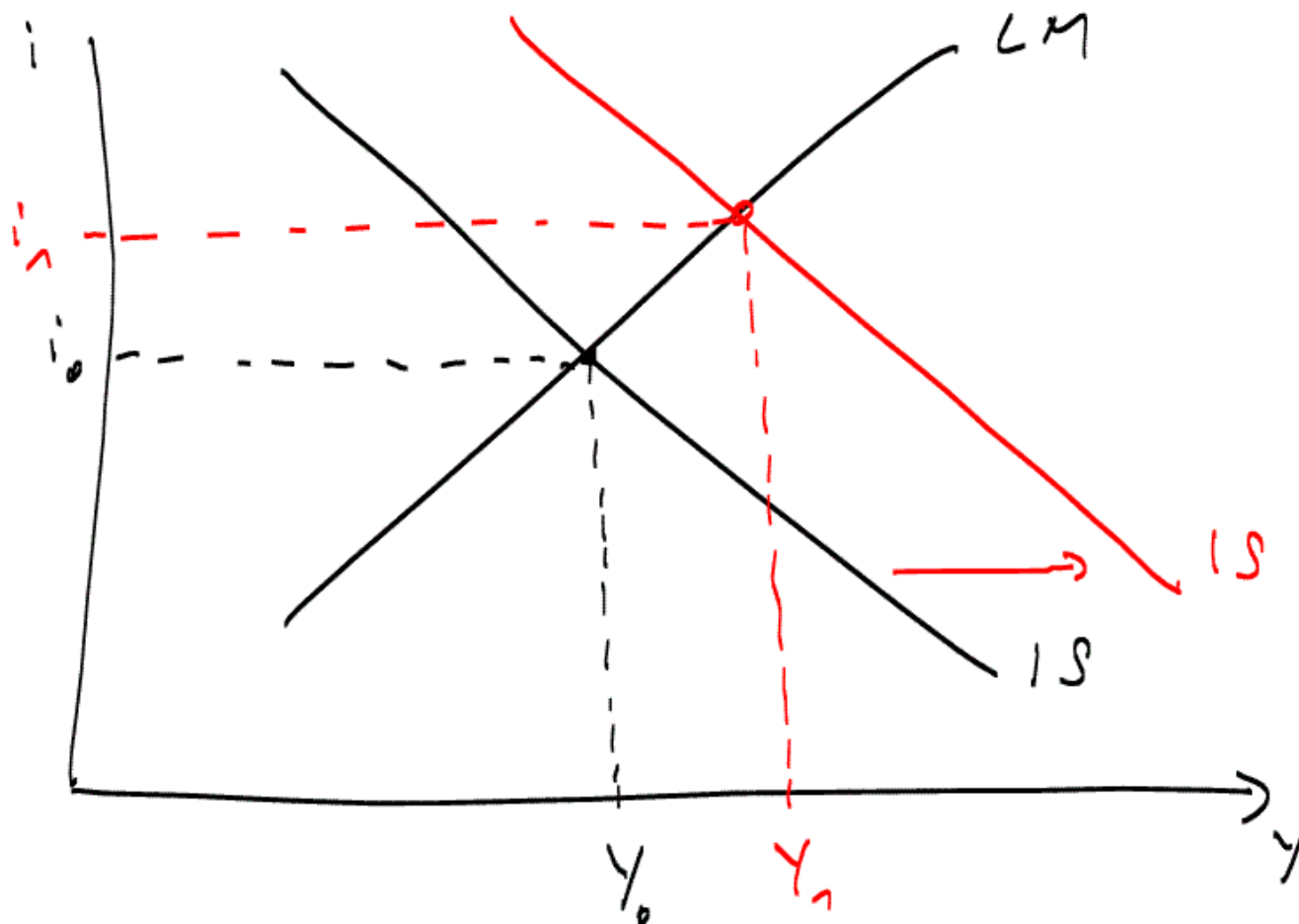
## LM-curve: Discussion



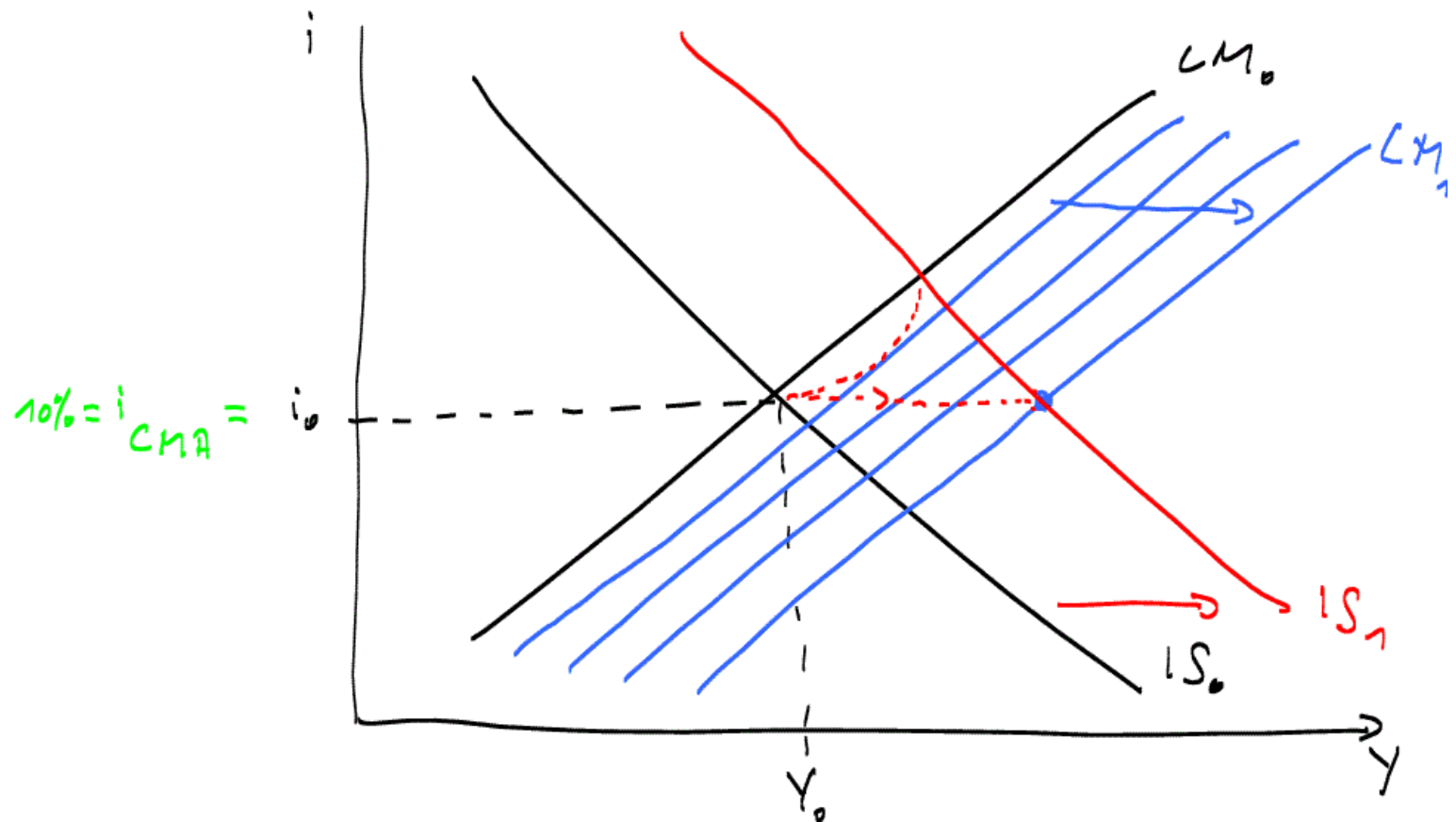
## LM-curve: Response to monetary policy



## IS-LM: Simultaneous equilibrium



# IS-LM: Dynamics within a currency union 1



## IS-LM: Dynamics within a currency union 2

- Starting point: Equilibrium ( $i = i_{CMA}$ )
- Increase in public spending ( $\Delta G > 0$ )
- Output expansion (multiplier process starts)
- Tendency for the interest rate to increase
- Arbitrage induces financial capital inflows
- Money supply increases according to inflowing capital
- Higher quantity of money keeps interest rate near to the initial level ( $i = i_{CMA}$ )