





Because  $\sigma < 1$  . Say's Law is broken

( supply does not create its own demand entirely)

→ only a fraction  $\sigma < 1$  of supply becomes demand

MPS

→ we have a proper concept of aggregate demand.

Why is Say's Law broken? Because  $\sigma < 1$ ,

which is because  $X < \infty$  (finite), which

is because real wealth enters the utility function

$$\left[ \text{recall } u(c, m) = \underbrace{\frac{X}{1+X}}_{=1 \text{ if } X=\infty} c^{\frac{1}{1+X}} + \underbrace{\frac{1}{1+X}}_{=0 \text{ if } X=\infty} \left( \frac{m}{P} \right)^{\frac{1}{1+X}} \right]$$

To break Say's Law: household must value something else than consumption → here it's real wealth.

From aggregate demand analysis:

$$| y = \sigma(x) [ y^s(x) + M/P ]$$

$\sigma(r)$  : Marginal propensity to spend (MPS)  
decreasing w/  $r$

$y_f^s(r)$  : aggregate supply = real income  
increasing w/  $r$

→ Two counteracting forces, hard to know  
whether output  $y$  increases or decreases w/  
tightness