

## The principle of effective demand

The base of Keynesian employment theory is the law of effective demand. According to Keynesian employment theory "The level of the employment depends on the effective demand in the Capitalistic economy."

if the effective demand is decreased then the employment level is decreased and vice-versa.

According to Keynes "The point where Aggregate Supply function cross the Aggregate demand function is called the value of aggregate demand (It is also called effective demand)"

Thus, effective demand is determined by Aggregate supply function (~~Receipts~~ <sup>Cost</sup>) and Aggregate demand function (Receipt).

Aggregate demand function  $\Rightarrow$  Aggregate demand function is the schedule of the various amounts of money which the entrepreneurs in the

in an economy expect from the sale of their outputs at varying level of employment.

Aggregate Supply function  $\Rightarrow$  ASf is a Schedule of the various amount of money which the entrepreneurs in an economy must receive from the sale of output at varying level of employment.

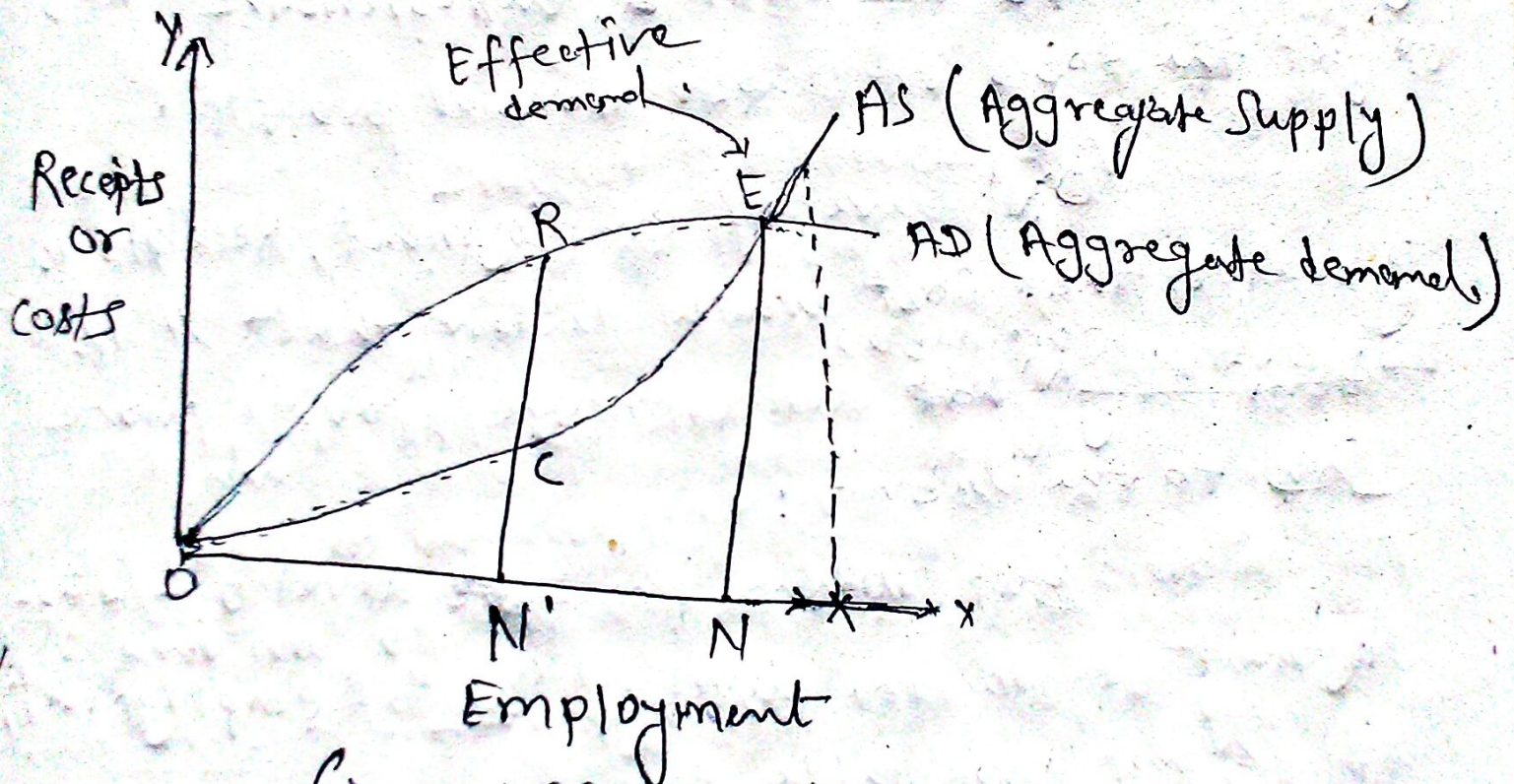


Fig :- Effective demand

The above figure describe the effective demand, in which AD is the Aggregate demand function and AS is the Aggregate Supply function. Level of employment denotes x-axis and Receipts or Cost denotes the y-axis.

AS and AD curve is crossed each other on the point E that is the point of effective demand where "ON" labor in employment.

The entrepreneur has the max<sup>m</sup> expectation to profit at the point of effective demand like point E.  
Any other <sup>point</sup> Except the point E, entrepreneur has to get the loss or Super normal profits.

"ON" level of employment, Receipts is greater than Cost which declare that it is <sup>(profitable)</sup> ~~beneficial~~ that entrepreneur <sup>will</sup> provide more Job to the labor.

But, when the ~~low~~ level of employment leads the level of "ON" of employment, it is not profitable to entrepreneur due to Cost is greater than receipts.

Thus, the point of the effective demand indicates the real level of employment  
Keyens said that  
~~Keyens~~ Aggregate Supply function is constant

in both determinants of effective demand due to it depends upon technique used in production, raw materials, machines etc. which are not changeable in short run. "

So, in the economy, Aggregate demand function plays the important role to determine the level of employment.

According to Keynes " - Aggregate demand function depends on Consumption function and Investment function.