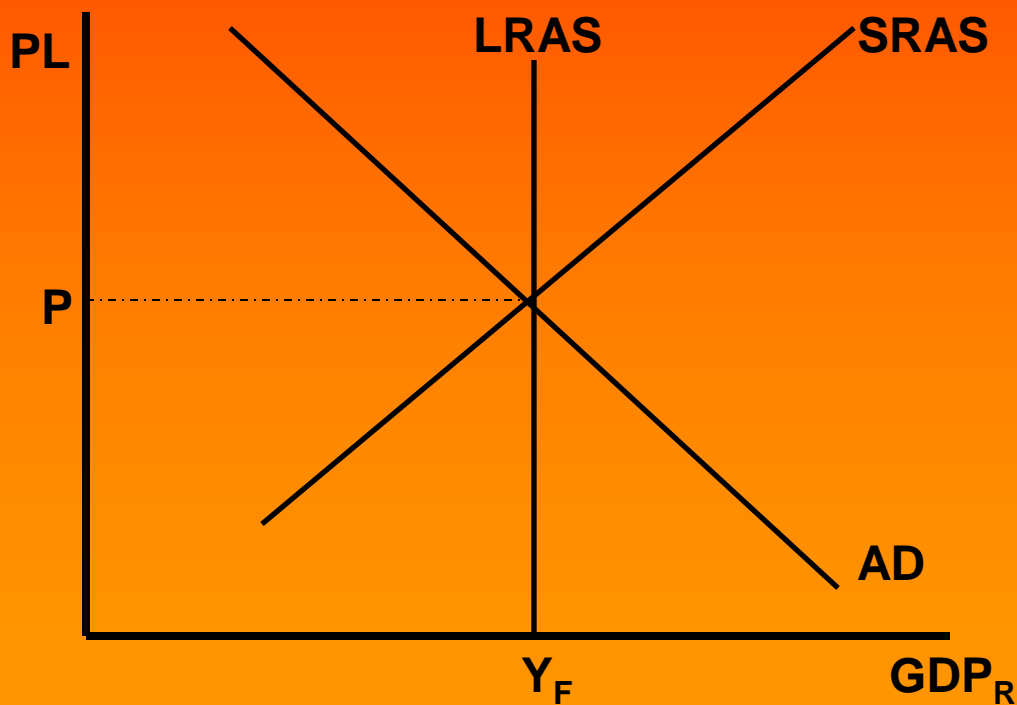


# AP Macroeconomics

## The AS/AD Model

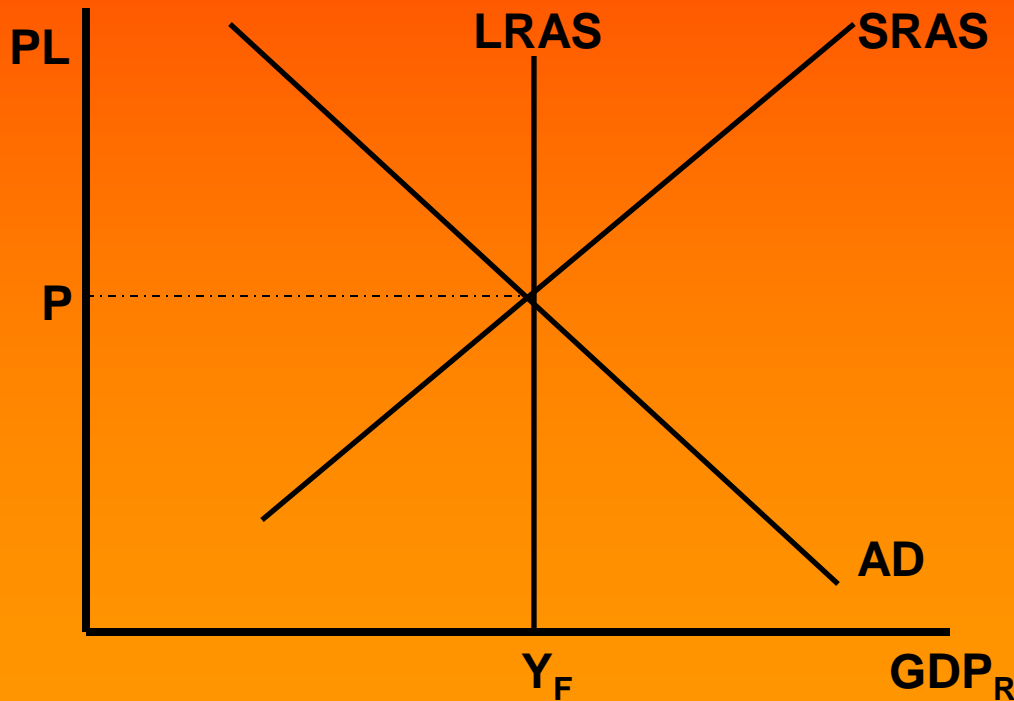
# The AS/AD Model

- The equilibrium of AS & AD determines current output ( $GDP_R$ ) and the price level (PL)



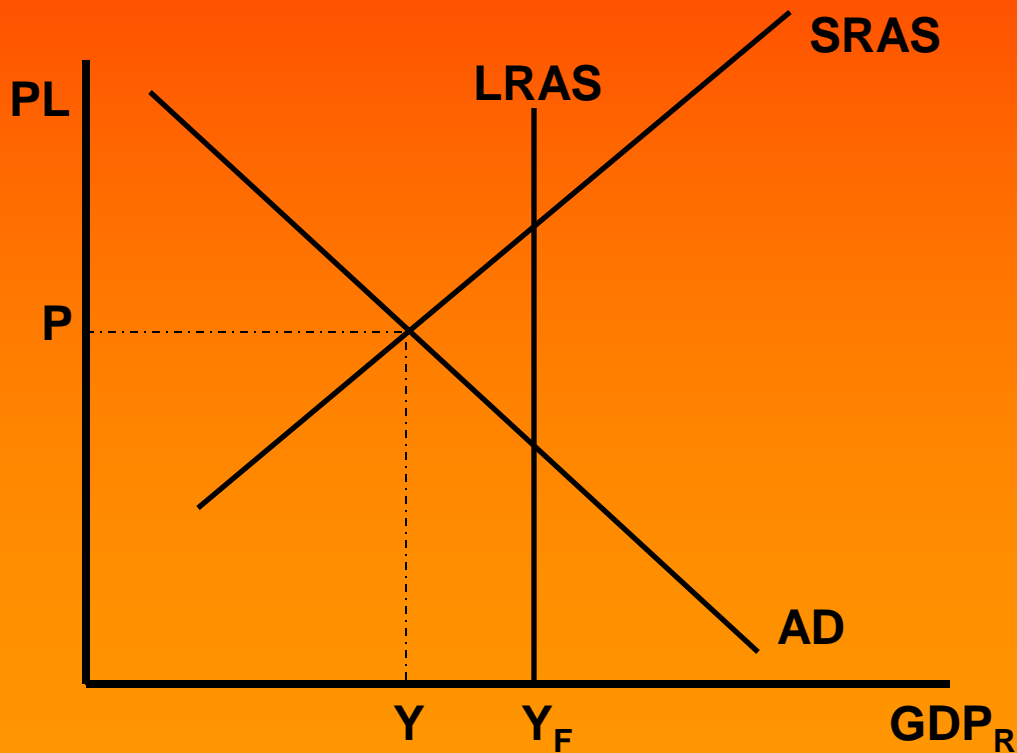
# Full Employment

- Full Employment equilibrium exists where AD intersects SRAS & LRAS at the same point.



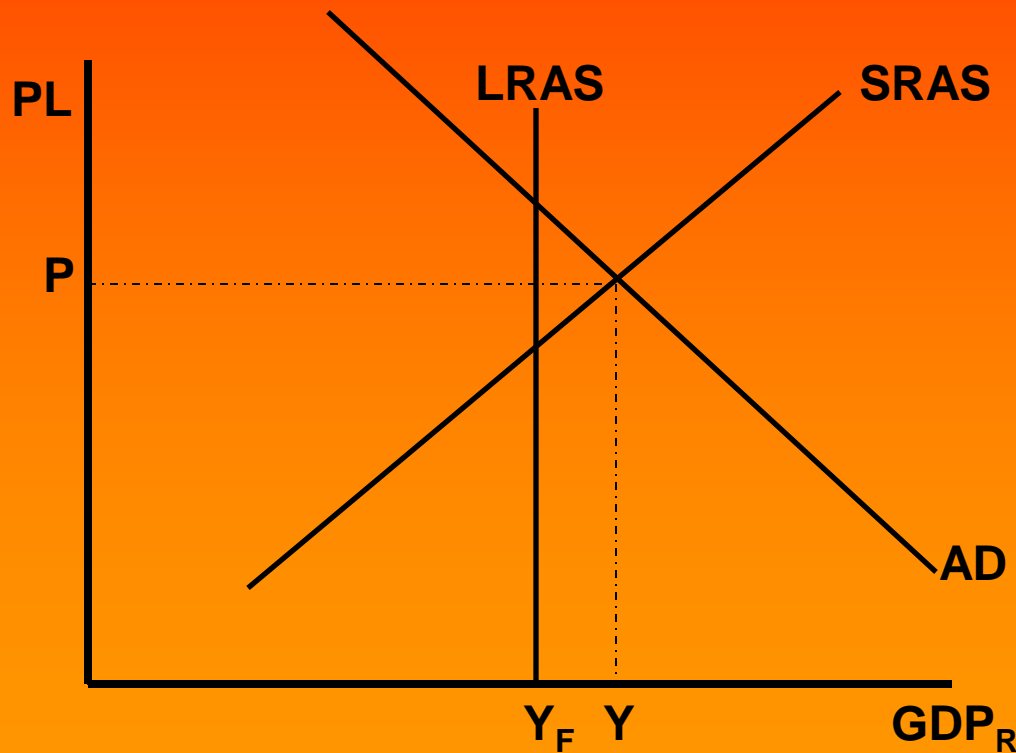
# Recessionary Gap

- A recessionary gap exists when equilibrium occurs below full employment output.



# Inflationary Gap

- An inflationary gap exists when equilibrium occurs beyond full employment output.



# Changes ( $\Delta$ ) in AD

- $\Delta$  Consumption (C)

- $C \uparrow \therefore AD \rightarrow \therefore GDP_R \uparrow \ \& \ PL \uparrow \therefore U\% \downarrow \ \& \ \pi\% \uparrow$

- $C \downarrow \therefore AD \leftarrow \therefore GDP_R \downarrow \ \& \ PL \downarrow \therefore U\% \uparrow \ \& \ \pi\% \downarrow$

- $\Delta$  Gross Private Investment ( $I_G$ )

- $I_G \uparrow \therefore AD \rightarrow \therefore GDP_R \uparrow \ \& \ PL \uparrow \therefore U\% \downarrow \ \& \ \pi\% \uparrow$

- $I_G \downarrow \therefore AD \leftarrow \therefore GDP_R \downarrow \ \& \ PL \downarrow \therefore U\% \uparrow \ \& \ \pi\% \downarrow$

- $\Delta$  Government Spending (G)

- $G \uparrow \therefore AD \rightarrow \therefore GDP_R \uparrow \ \& \ PL \uparrow \therefore U\% \downarrow \ \& \ \pi\% \uparrow$

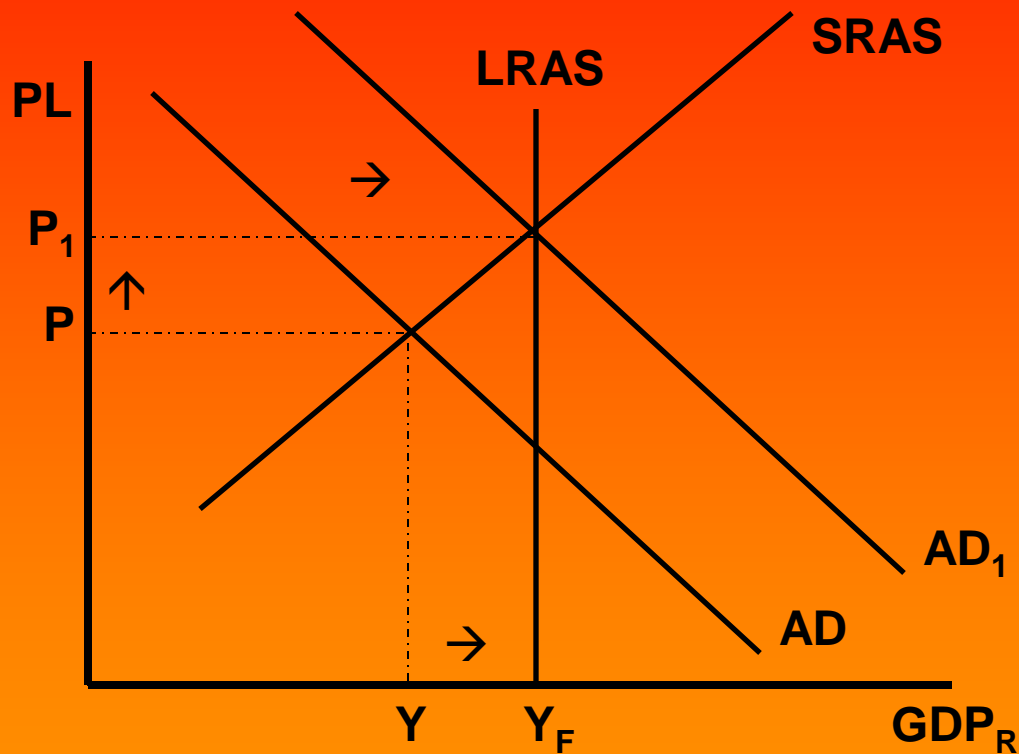
- $G \downarrow \therefore AD \leftarrow \therefore GDP_R \downarrow \ \& \ PL \downarrow \therefore U\% \uparrow \ \& \ \pi\% \downarrow$

- $\Delta$  Net Exports ( $X_N$ )

- $X_N \uparrow \therefore AD \rightarrow \therefore GDP_R \uparrow \ \& \ PL \uparrow \therefore U\% \downarrow \ \& \ \pi\% \uparrow$

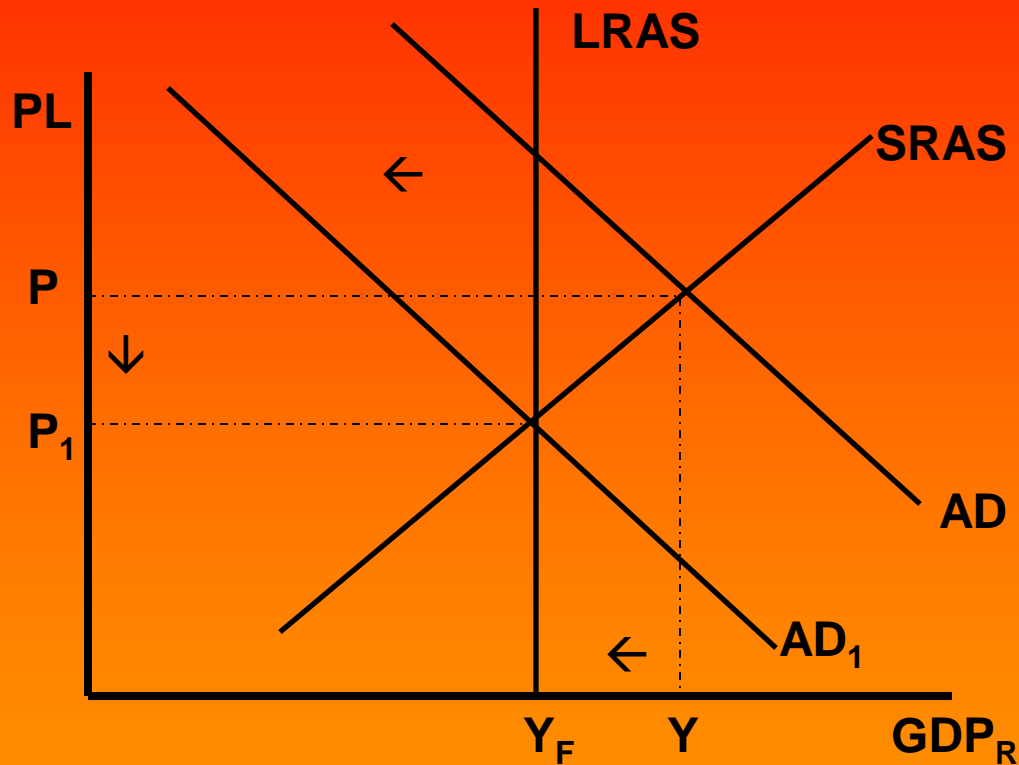
- $X_N \downarrow \therefore AD \leftarrow \therefore GDP_R \downarrow \ \& \ PL \downarrow \therefore U\% \uparrow \ \& \ \pi\% \downarrow$

# Increase in AD



$C \uparrow, I_G \uparrow, G \uparrow$  and/or  $X_N \uparrow \therefore AD \rightarrow \therefore GDP_R \uparrow \text{ \& } PL \uparrow \therefore u\% \downarrow \text{ \& } \pi\% \uparrow$

# Decrease in AD



$C \downarrow, I_G \downarrow, G \downarrow$  and/or  $X_N \downarrow \therefore AD \leftarrow \therefore GDP_R \downarrow \ \& \ PL \downarrow \therefore u\% \uparrow \ \& \ \pi\% \downarrow$



# Changes ( $\Delta$ ) in SRAS

- $\Delta$  Input Prices

- Input Prices  $\downarrow$   $\therefore$  SRAS  $\rightarrow$   $\therefore$   $GDP_R \uparrow$  &  $PL \downarrow$   $\therefore$   $u\% \downarrow$  &  $\pi\% \downarrow$
- Input Prices  $\uparrow$   $\therefore$  SRAS  $\leftarrow$   $\therefore$   $GDP_R \downarrow$  &  $PL \uparrow$   $\therefore$   $u\% \uparrow$  &  $\pi\% \uparrow$

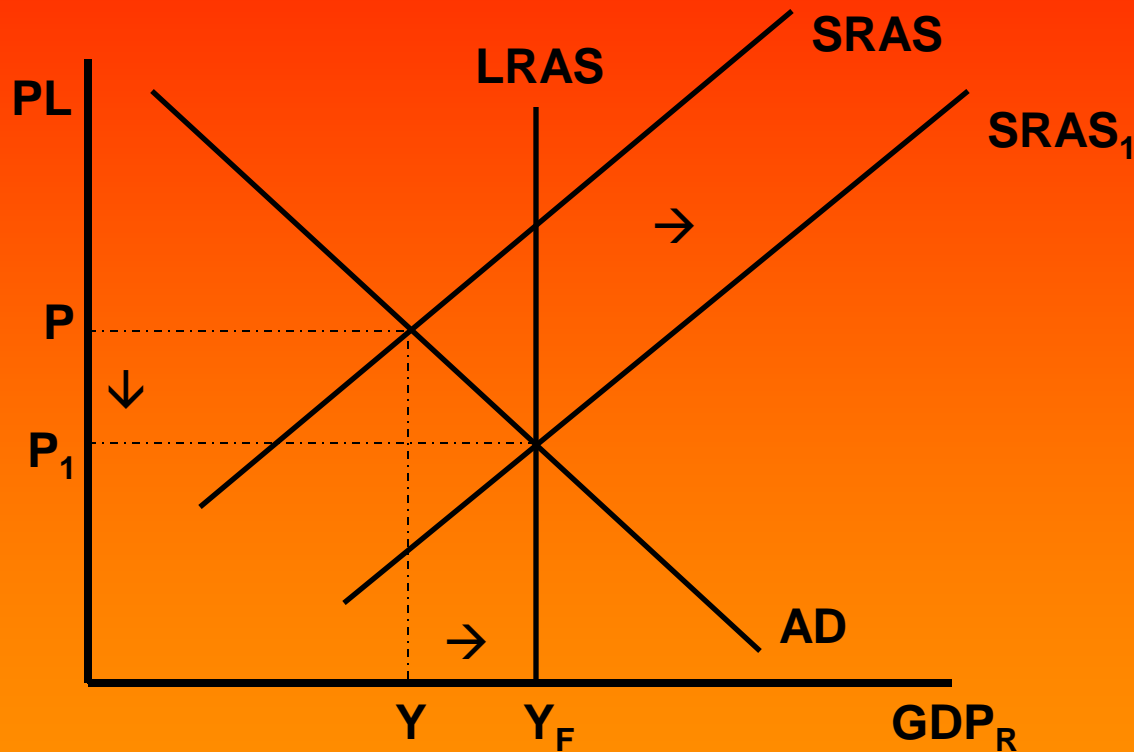
- $\Delta$  Productivity

- Productivity  $\uparrow$   $\therefore$  SRAS  $\rightarrow$   $\therefore$   $GDP_R \uparrow$  &  $PL \downarrow$   $\therefore$   $u\% \downarrow$  &  $\pi\% \downarrow$
- Productivity  $\downarrow$   $\therefore$  SRAS  $\leftarrow$   $\therefore$   $GDP_R \downarrow$  &  $PL \uparrow$   $\therefore$   $u\% \uparrow$  &  $\pi\% \uparrow$

- $\Delta$  Legal-Institutional Environment

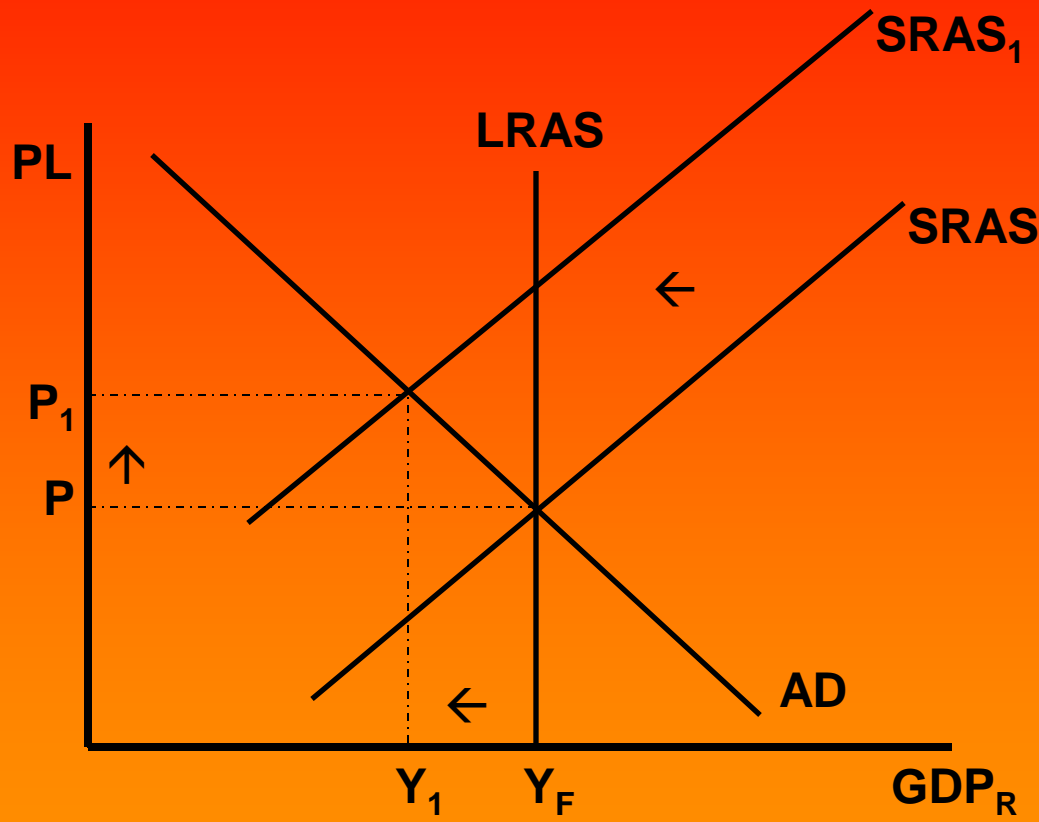
- Deregulation  $\therefore$  SRAS  $\rightarrow$   $\therefore$   $GDP_R \uparrow$  &  $PL \downarrow$   $\therefore$   $u\% \downarrow$  &  $\pi\% \downarrow$
- Regulation  $\therefore$  SRAS  $\leftarrow$   $\therefore$   $GDP_R \downarrow$  &  $PL \uparrow$   $\therefore$   $u\% \uparrow$  &  $\pi\% \uparrow$

# Increase in SRAS



Input Prices  $\downarrow$ , Productivity  $\uparrow$ , and/or Deregulation  
 $\therefore$  SRAS  $\rightarrow$   $\therefore$   $GDP_R \uparrow$  &  $PL \downarrow$   $\therefore$   $u\% \downarrow$  &  $\pi\% \downarrow$

# Decrease in SRAS



Input Prices  $\uparrow$ , Productivity  $\downarrow$ , and/or Regulation  
 $\therefore SRAS \leftarrow \therefore GDP_R \downarrow$  &  $PL \uparrow \therefore u\% \uparrow$  &  $\pi\% \uparrow$

# AS / AD Summary

- $\Delta C$ ,  $\Delta I_G$ ,  $\Delta G$ , and/or  $\Delta X_N = \Delta AD$ 
  - $AD \rightarrow \therefore GDP_R \uparrow \ \& \ PL \uparrow \ \therefore u\% \downarrow \ \& \ \pi\% \uparrow$
  - $AD \leftarrow \therefore GDP_R \downarrow \ \& \ PL \downarrow \ \therefore u\% \uparrow \ \& \ \pi\% \downarrow$
- $\Delta$  Input Prices,  $\Delta$  Productivity, and/or  $\Delta$  Regulation =  $\Delta$  SRAS
  - $SRAS \rightarrow \therefore GDP_R \uparrow \ \& \ PL \downarrow \ \therefore u\% \downarrow \ \& \ \pi\% \downarrow$
  - $SRAS \leftarrow \therefore GDP_R \downarrow \ \& \ PL \uparrow \ \therefore u\% \uparrow \ \& \ \pi\% \uparrow$
- The AS/AD Model is the most important graph in AP Macroeconomics.
- KNOW IT!!!