

● 27 Aggregate Demand

● 28 Aggregate Supply



● **29** The AD-AS Model



# The AS-AD Model

- The **AS-AD model** uses the AS curve and the AD curve together to analyze economic fluctuations.

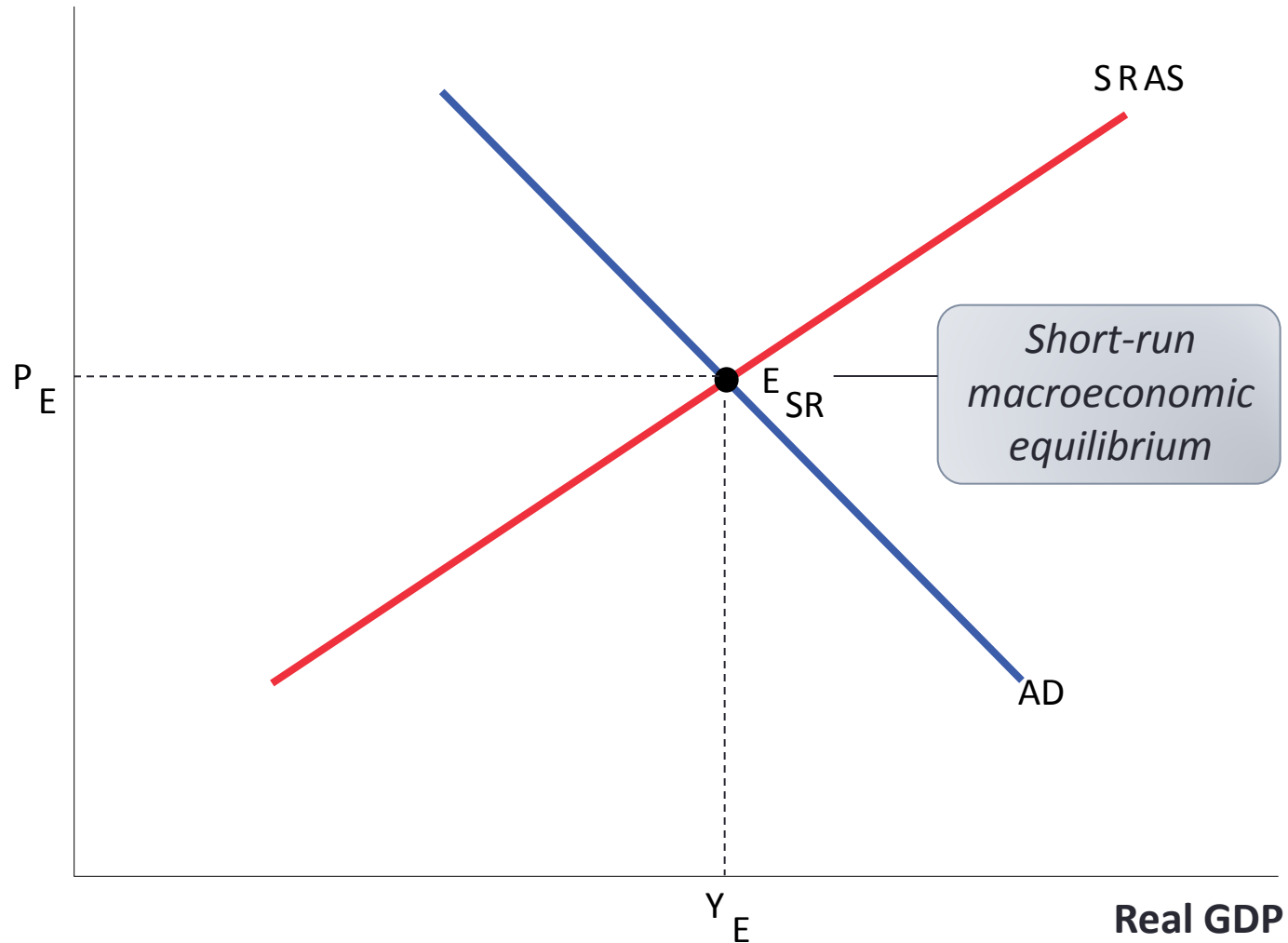


# Short-Run Macroeconomic Equilibrium

- The economy is in **short-run macroeconomic equilibrium** when the quantity of aggregate output supplied is equal to the quantity demanded.
- The **short-run equilibrium aggregate price level** is the aggregate price level in the short-run macroeconomic equilibrium.
- **Short-run equilibrium aggregate output** is the quantity of aggregate output produced in the short-run macroeconomic equilibrium.

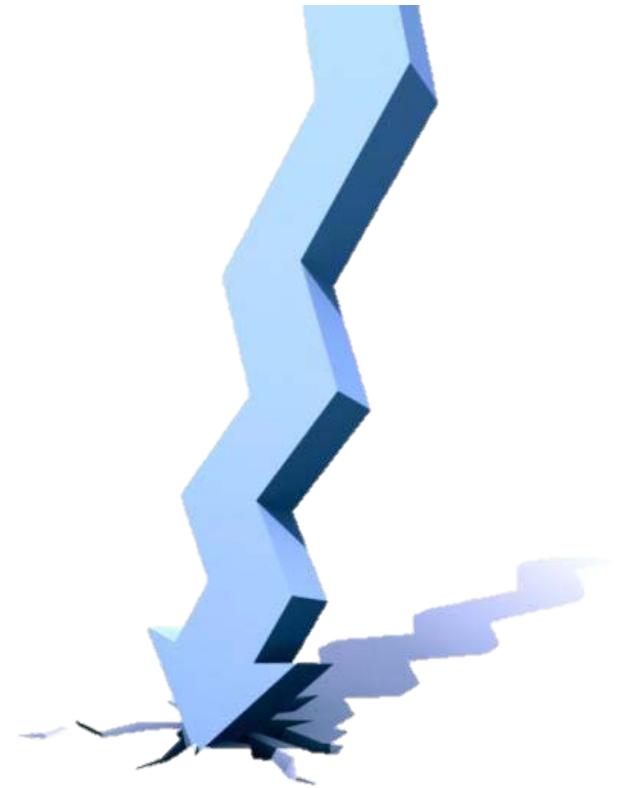
# The AS–AD Model

Aggregate price level



# Macroeconomic Shocks

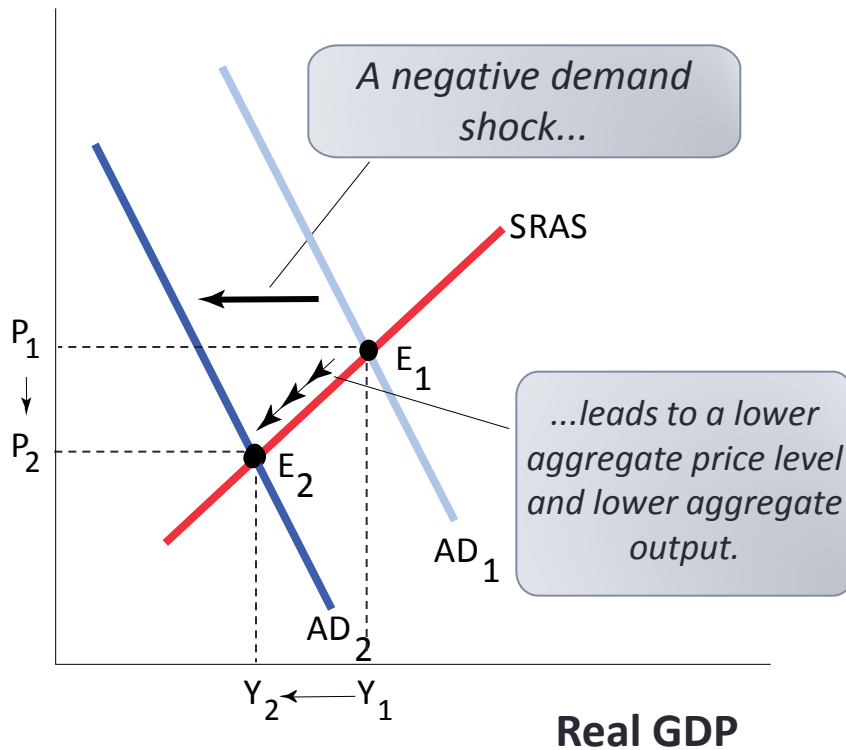
- If a demand or supply shock hits the economy, **AD** or **AS** shifts and moves the economy to a new equilibrium.



# Demand Shocks

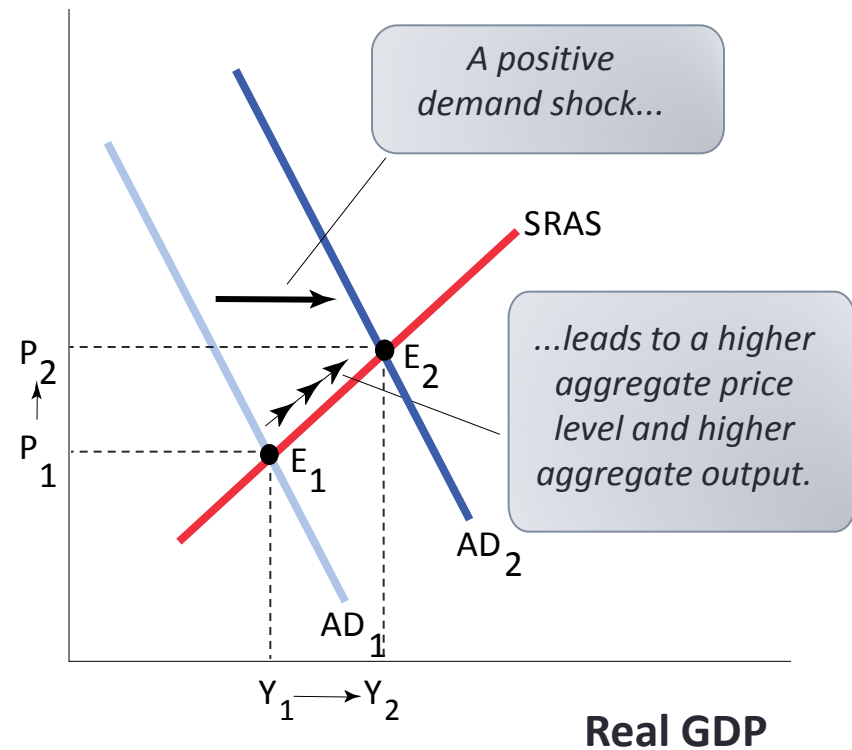
(a) A Negative Demand Shock

Aggregate price level



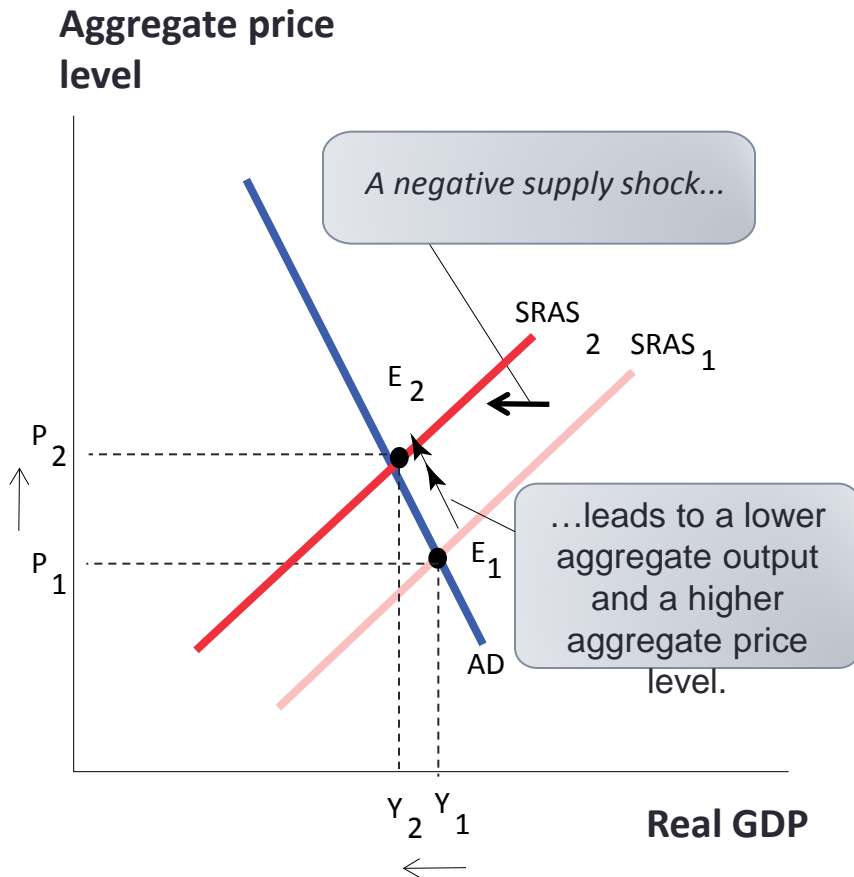
(b) A Positive Demand Shock

Aggregate price level

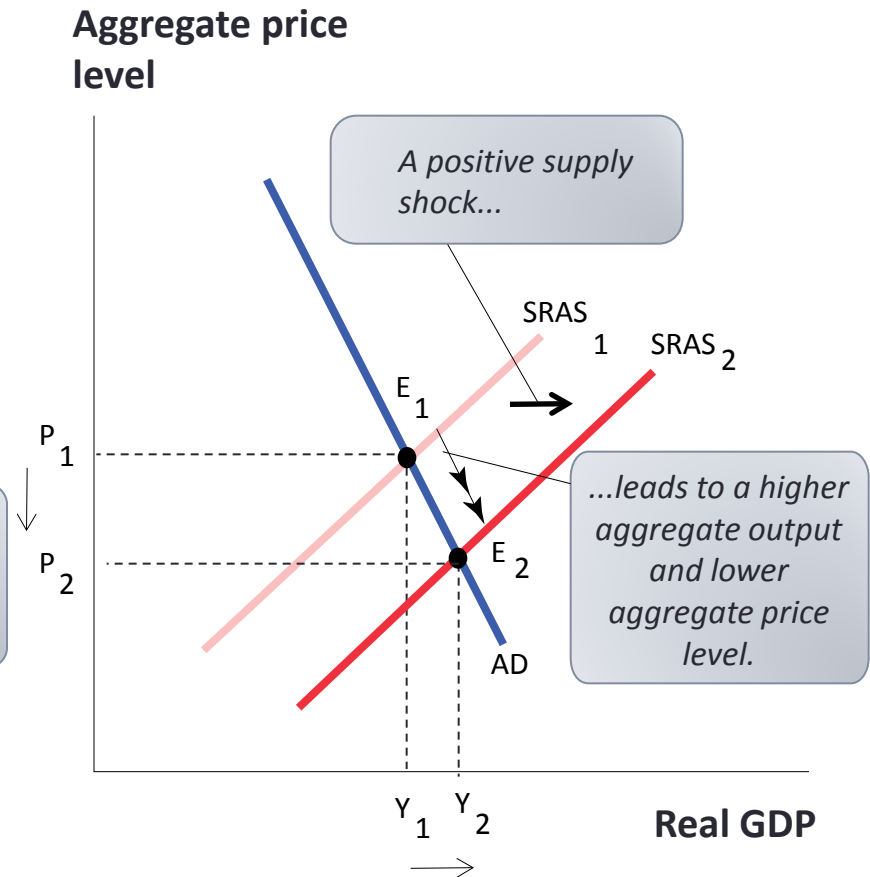


# Supply Shocks

(a) A Negative Supply Shock



(b) A Positive Supply Shock

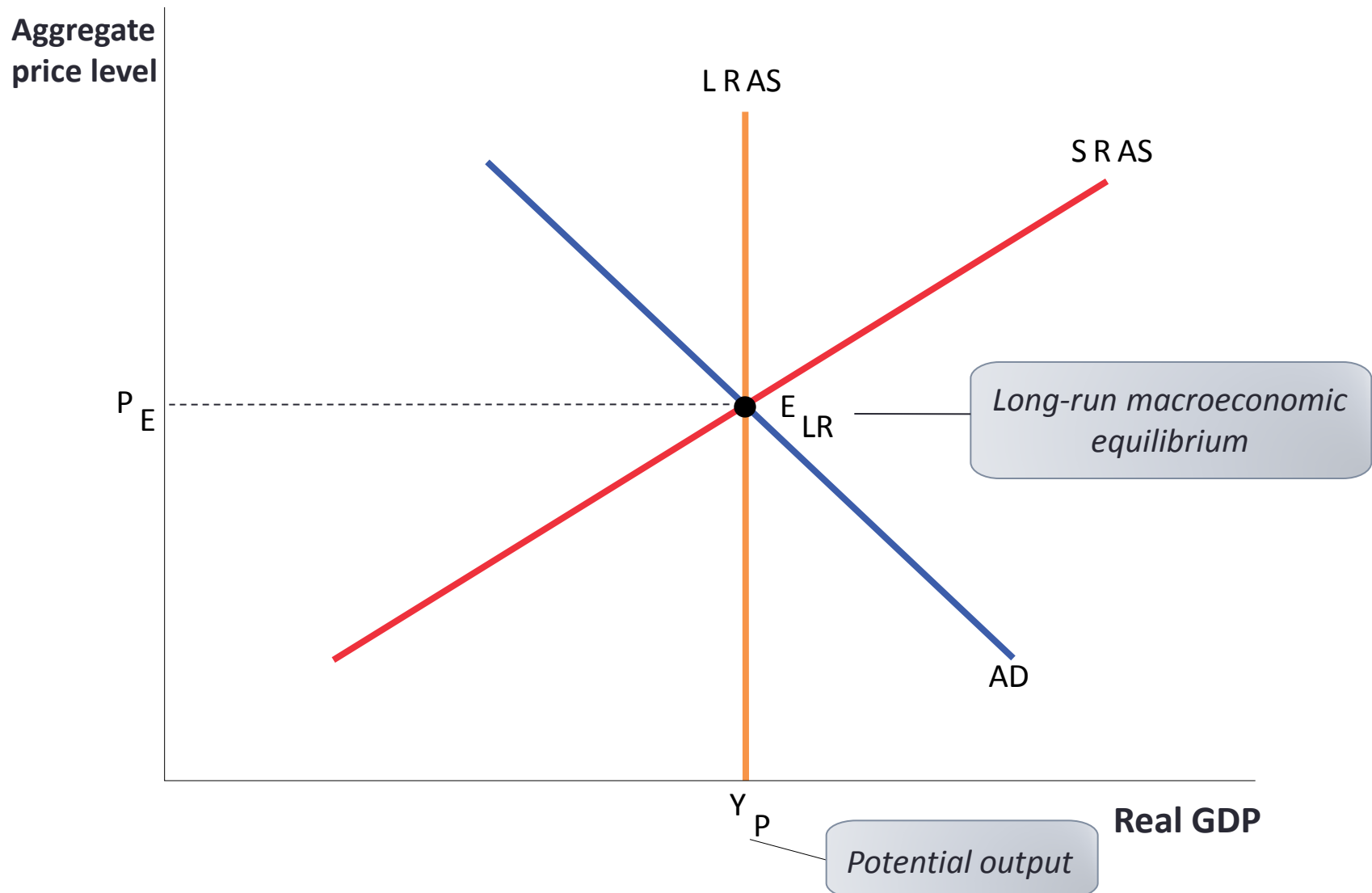


# Long-Run Macroeconomic Equilibrium

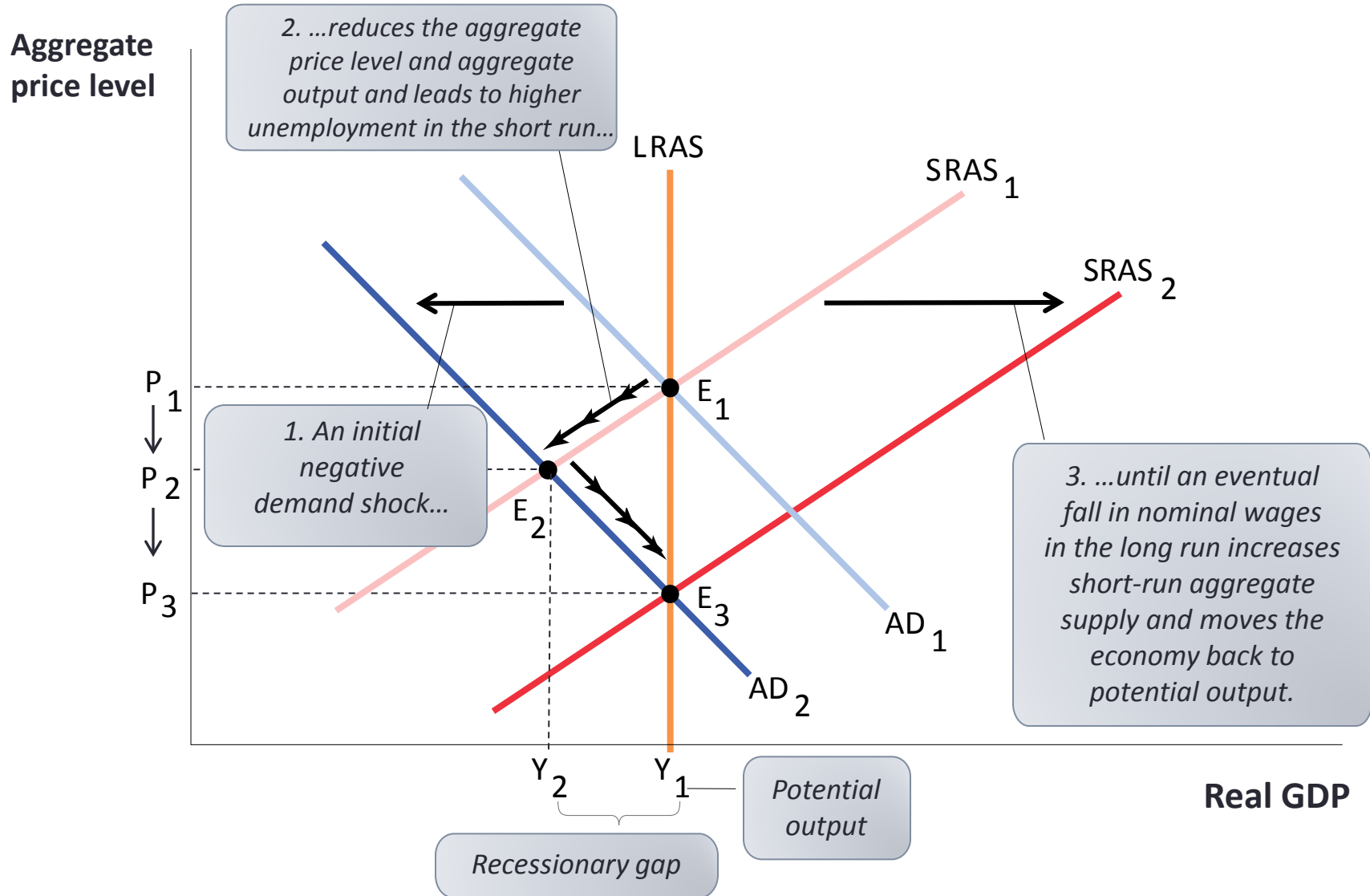
- The economy is in **long-run macroeconomic equilibrium** when the point of short-run macroeconomic equilibrium is on the long-run aggregate supply curve.



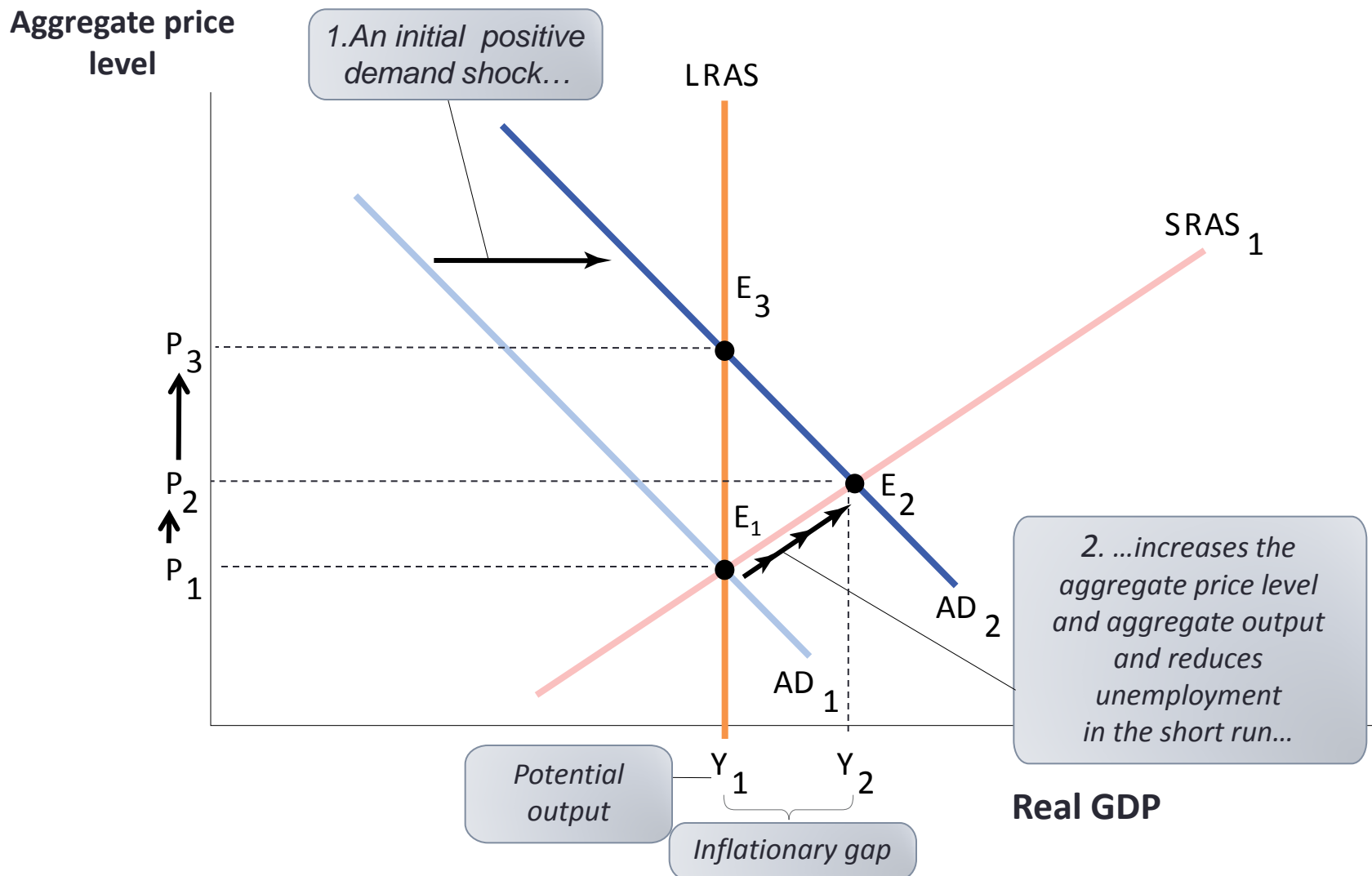
# Long-Run Macroeconomic Equilibrium



# SR vs LR Effects of a Negative Demand Shock



# SR vs LR Effects of a Positive Demand Shock



# Long-Run Macroeconomic Equilibrium

- The economy is **self-correcting** when shocks to AD affect aggregate output in the short run, but not the long run.
- **Stabilization policy** is the use of government policy to reduce the severity of recessions and rein in excessively strong expansions.
- If policy makers react quickly to a fall in aggregate demand, they can use monetary or fiscal policy to shift the AD curve back to the right.
- Unlike demand shocks, there are no government policies that can easily react to shocks an AS shock.