

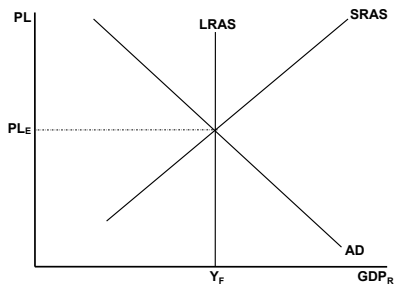
THE AD/AS MODEL

Coach Burnett
AP Macroeconomics

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THE AD/AS MODEL

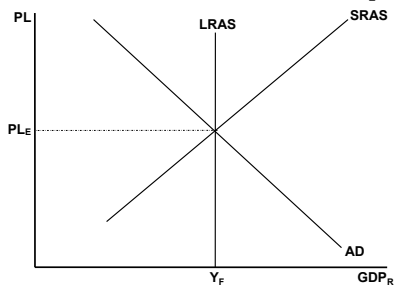
- The equilibrium of AD & AS determines current output (GDP_R) and the price level (PL)



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FULL EMPLOYMENT

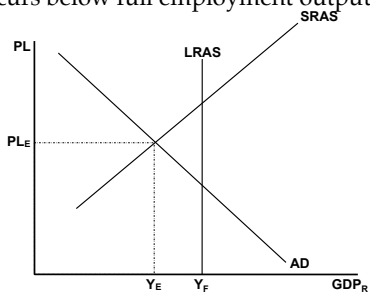
- Full Employment equilibrium exists where AD intersects SRAS & LRAS at the same point.



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RECESSIONARY GAP

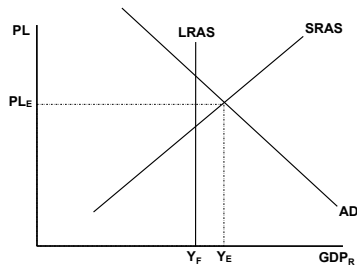
- A recessionary gap exists when equilibrium occurs below full employment output.



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INFLATIONARY GAP

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



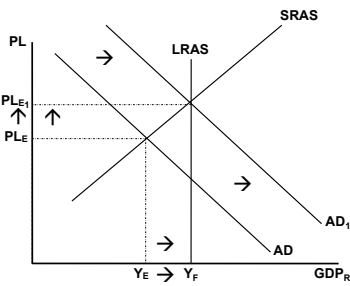
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CHANGES IN AD (ΔAD)

- Δ Consumption (C)
 - $C \uparrow \therefore AD \rightarrow \therefore GDP_R \uparrow$ & $PL \uparrow \therefore u\% \downarrow$ & $\pi\% \uparrow$
 - $C \downarrow \therefore AD \leftarrow \therefore GDP_R \downarrow$ & $PL \downarrow \therefore u\% \uparrow$ & $\pi\% \downarrow$
- Δ Gross Private Investment (I_G)
 - $I_G \uparrow \therefore AD \rightarrow \therefore GDP_R \uparrow$ & $PL \uparrow \therefore u\% \downarrow$ & $\pi\% \uparrow$
 - $I_G \downarrow \therefore AD \leftarrow \therefore GDP_R \downarrow$ & $PL \downarrow \therefore u\% \uparrow$ & $\pi\% \downarrow$
- Δ Government Spending (G)
 - $G \uparrow \therefore AD \rightarrow \therefore GDP_R \uparrow$ & $PL \uparrow \therefore u\% \downarrow$ & $\pi\% \uparrow$
 - $G \downarrow \therefore AD \leftarrow \therefore GDP_R \downarrow$ & $PL \downarrow \therefore u\% \uparrow$ & $\pi\% \downarrow$
- Δ Net Exports (X_N)
 - $X_N \uparrow \therefore AD \rightarrow \therefore GDP_R \uparrow$ & $PL \uparrow \therefore u\% \downarrow$ & $\pi\% \uparrow$
 - $X_N \downarrow \therefore AD \leftarrow \therefore GDP_R \downarrow$ & $PL \downarrow \therefore u\% \uparrow$ & $\pi\% \downarrow$

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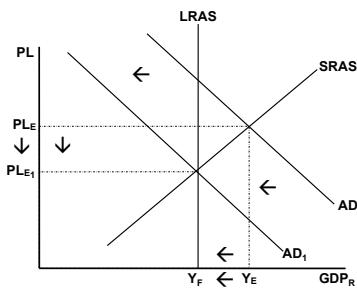
INCREASE IN AD



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

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DECREASE IN AD



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

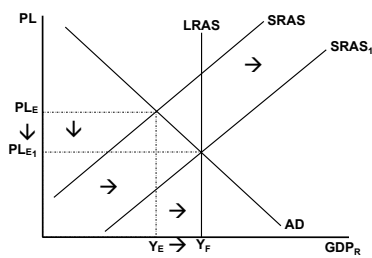
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CHANGES IN SRAS (Δ SRAS)

- Δ Input Prices
 - Input Prices \downarrow : SRAS \rightarrow : $\text{GDP}_R \uparrow$ & $\text{PL} \downarrow$: $u\% \downarrow$ & $\pi\% \downarrow$
 - Input Prices \uparrow : SRAS \leftarrow : $\text{GDP}_R \downarrow$ & $\text{PL} \uparrow$: $u\% \uparrow$ & $\pi\% \uparrow$
- Δ Productivity
 - Productivity \uparrow : SRAS \rightarrow : $\text{GDP}_R \uparrow$ & $\text{PL} \downarrow$: $u\% \downarrow$ & $\pi\% \downarrow$
 - Productivity \downarrow : SRAS \leftarrow : $\text{GDP}_R \downarrow$ & $\text{PL} \uparrow$: $u\% \uparrow$ & $\pi\% \uparrow$
- Δ Legal-Institutional Environment
 - Deregulation : SRAS \rightarrow : $\text{GDP}_R \uparrow$ & $\text{PL} \downarrow$: $u\% \downarrow$ & $\pi\% \downarrow$
 - Regulation : SRAS \leftarrow : $\text{GDP}_R \downarrow$ & $\text{PL} \uparrow$: $u\% \uparrow$ & $\pi\% \uparrow$

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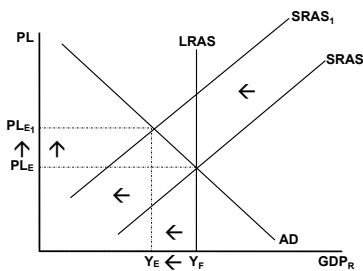
INCREASE IN SRAS



Input Prices \downarrow , Productivity \uparrow , and/or Deregulation
 : SRAS \rightarrow : $\text{GDP}_R \uparrow$ & $\text{PL} \downarrow$: $u\% \downarrow$ & $\pi\% \downarrow$

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DECREASE IN SRAS



Input Prices \uparrow , Productivity \downarrow , and/or Regulation
 : SRAS \leftarrow : $\text{GDP}_R \downarrow$ & $\text{PL} \uparrow$: $u\% \uparrow$ & $\pi\% \uparrow$

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AD/AS SUMMARY

- ΔC , ΔI_C , ΔG , and/or $\Delta X_N = \Delta$ AD
 - AD \rightarrow : $\text{GDP}_R \uparrow$ & $\text{PL} \downarrow$: $u\% \downarrow$ & $\pi\% \uparrow$
 - AD \leftarrow : $\text{GDP}_R \downarrow$ & $\text{PL} \downarrow$: $u\% \uparrow$ & $\pi\% \downarrow$
- Δ Input Prices, Δ Productivity, and/or Δ Regulation = Δ SRAS
 - SRAS \rightarrow : $\text{GDP}_R \uparrow$ & $\text{PL} \downarrow$: $u\% \downarrow$ & $\pi\% \downarrow$
 - SRAS \leftarrow : $\text{GDP}_R \downarrow$ & $\text{PL} \uparrow$: $u\% \uparrow$ & $\pi\% \uparrow$

The AD/AS Model is the most important graph in AP Macroeconomics.

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