

Does the US economy has a self correcting mechanism?

YES

- When there is “too little spending”-Firms unable to sell all their production-

• The **con**my **ex**periences **an** **re****ce****si****on****ary** **gap**.

- Wages decrease, AS shifts right, prices decrease
increasing AD.

BUT

During Recessions, wages do not easily fall...

Firms prefer to fire unskilled workers and keep skilled workers at the same pay (Job security increase productivity, reduces cost of inexperience and training)

- Recessionary gaps take longer because wages and prices do easily not fall

- Self correcting mechanism operates only weakly to cure recessions

- There is an argument to be made in favor of stabilization policies during recessions

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