

**Is the economy experiencing an
Inflationary or a Recessionary Gap?**

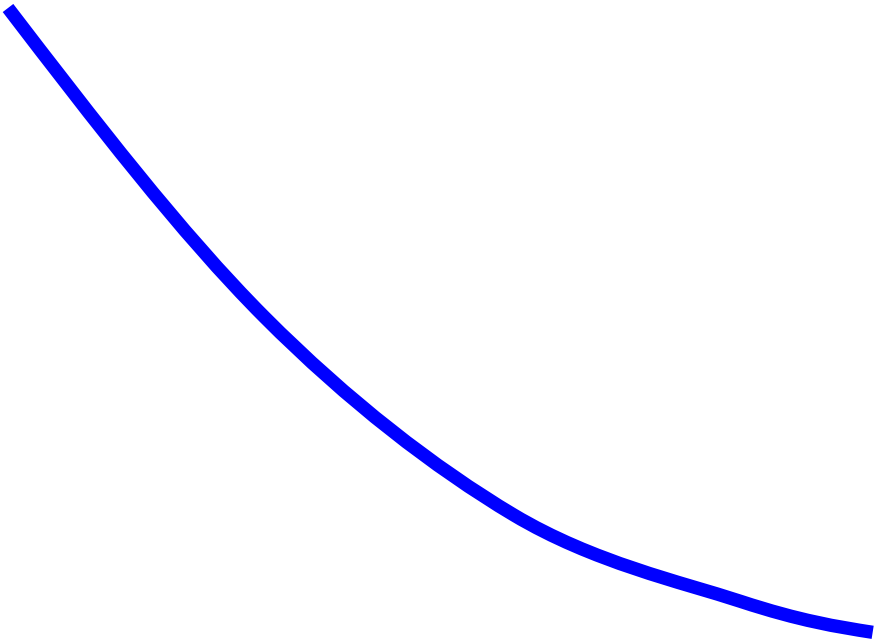
To close the gap we need to increase?

Or Decrease AE and AD?

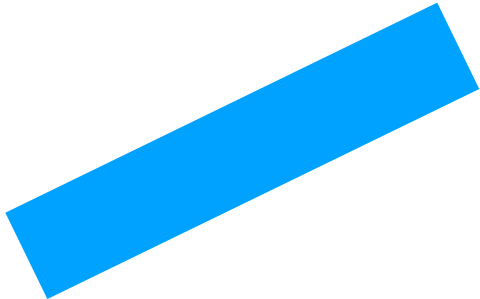
**Increase Taxes (Decrease
Transfers)**

**Decrease Government
Spending**

Increase Interest Rates



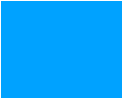




Potential

GDP















Fiscal Policy

Monetary Policy



Potential

GDP



Decrease

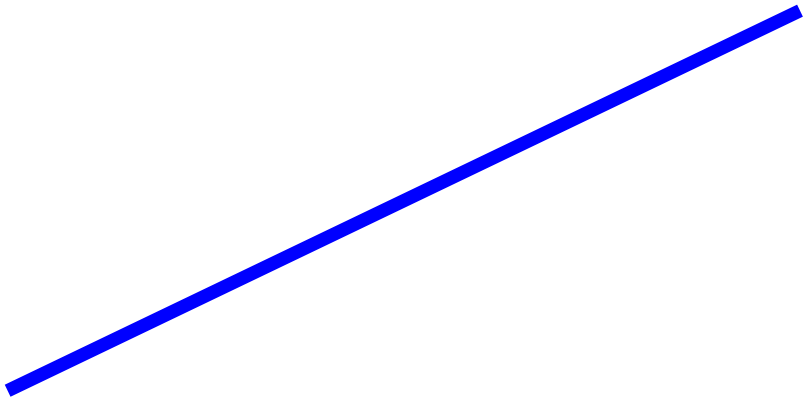
AE



Decrease
AD











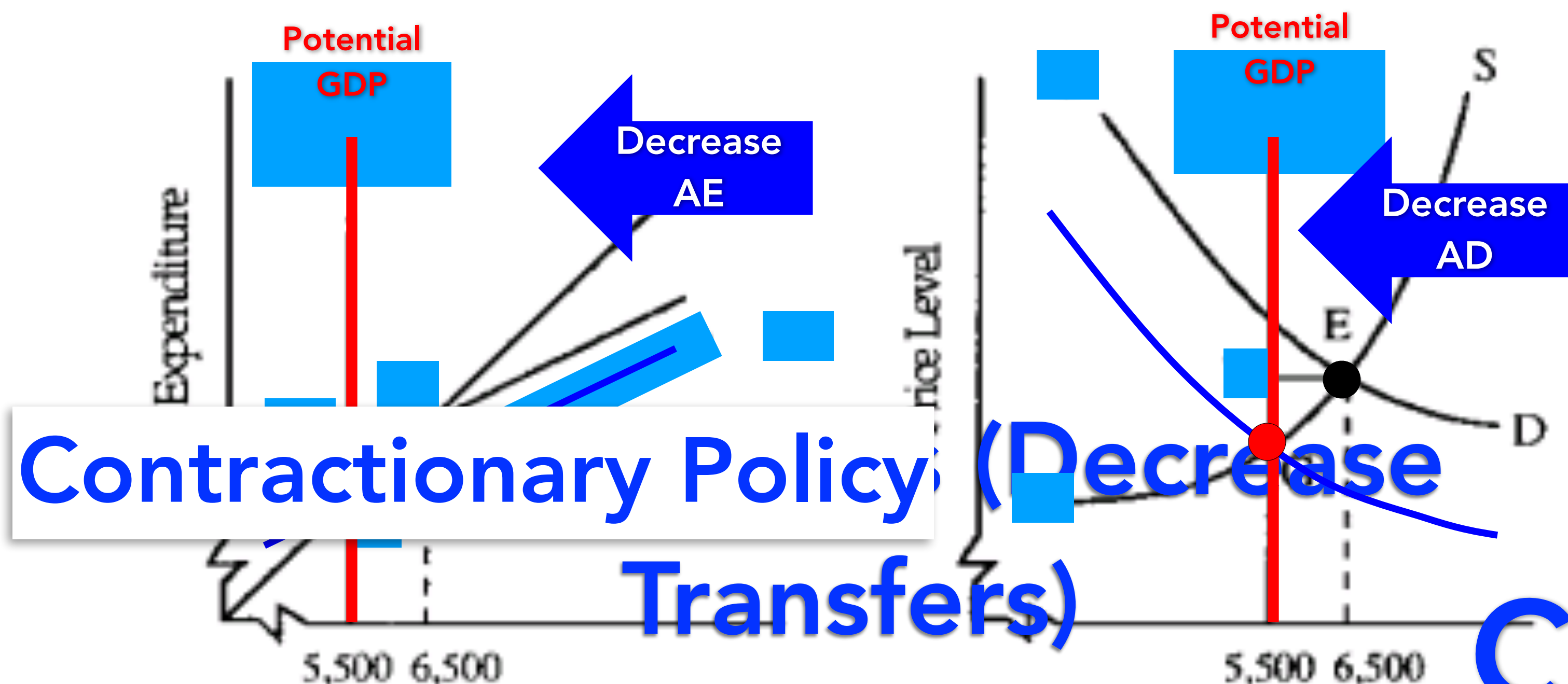
C



G



Contractionary Policy



Contractionary Policy (Decrease Transfers)

Fiscal Policy: Decrease Government Spending
Monetary Policy: Increase Interest Rates

Stabilization policies are
not needed