



AE

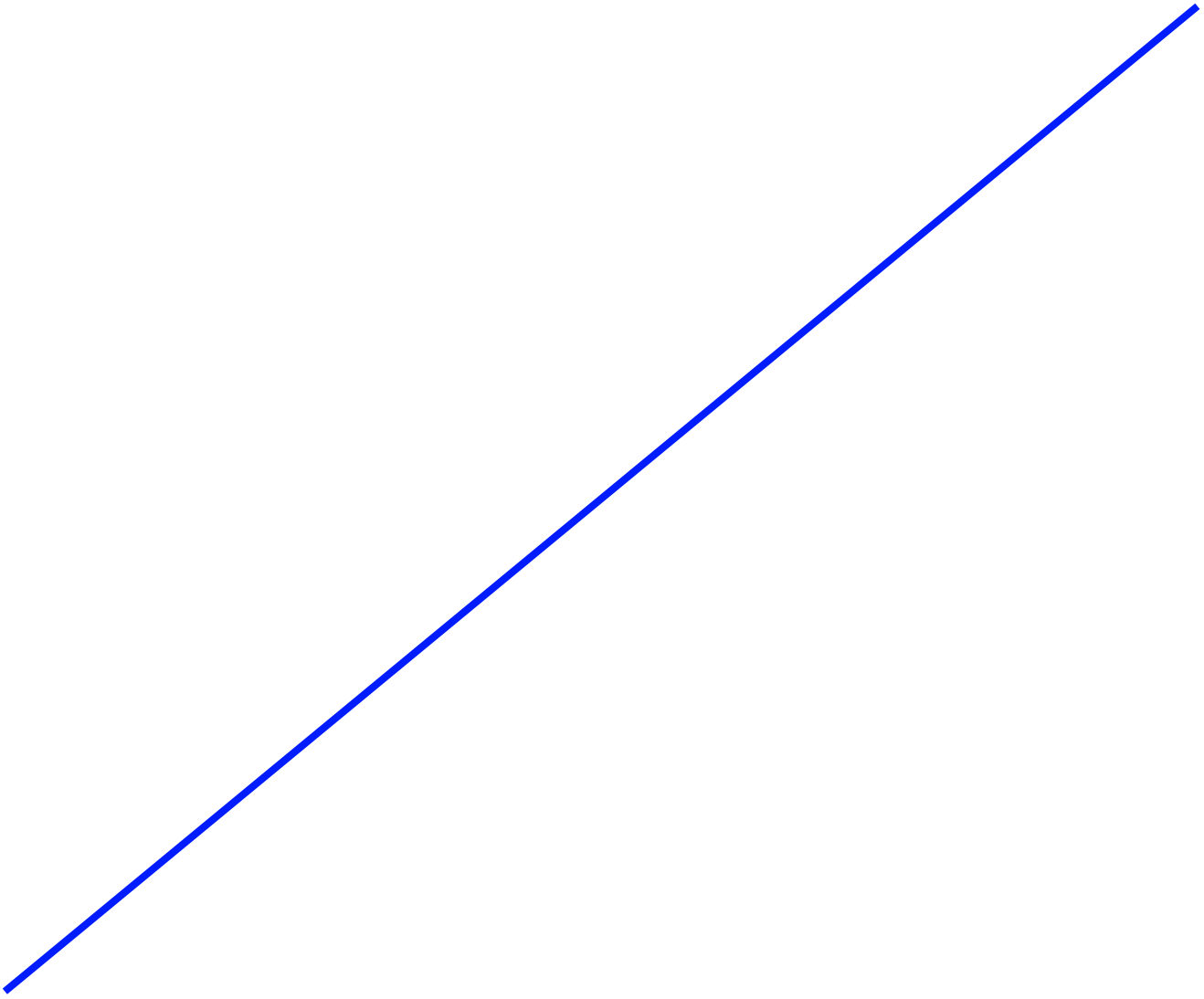




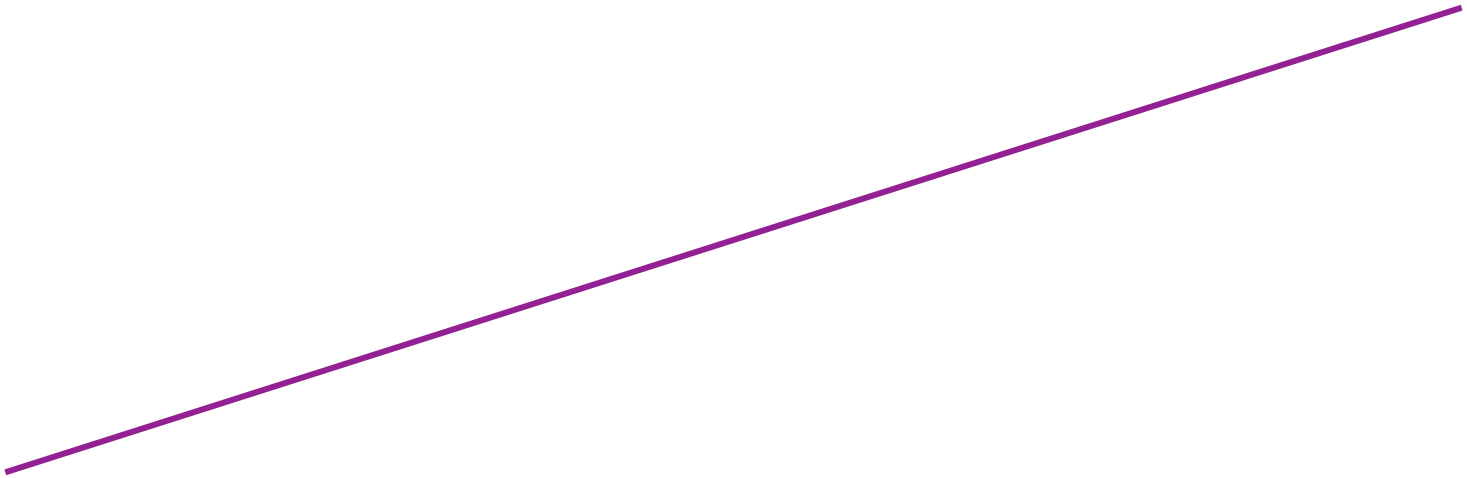
AE

Total  
Production











AE

=

Y\*







No change in  
inventories

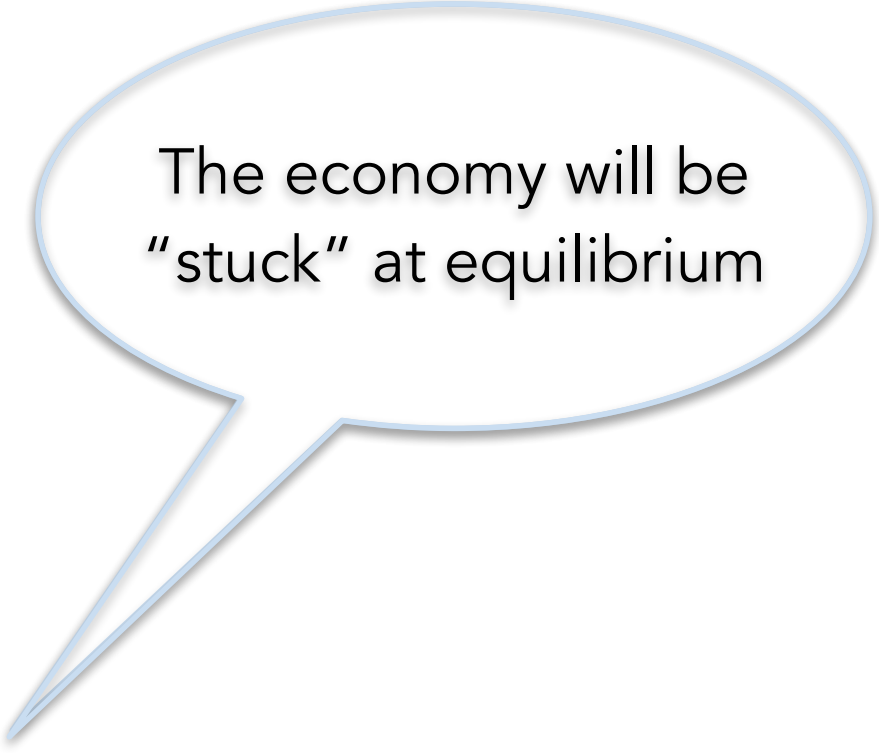
Where the two lines cross:  
Total Production is the  
same as the AE



When firms produce  
 $Y^*$  the economy is at  
equilibrium



Firms will continue to produce  $Y^*$  quarter after quarter...



The economy will be  
"stuck" at equilibrium

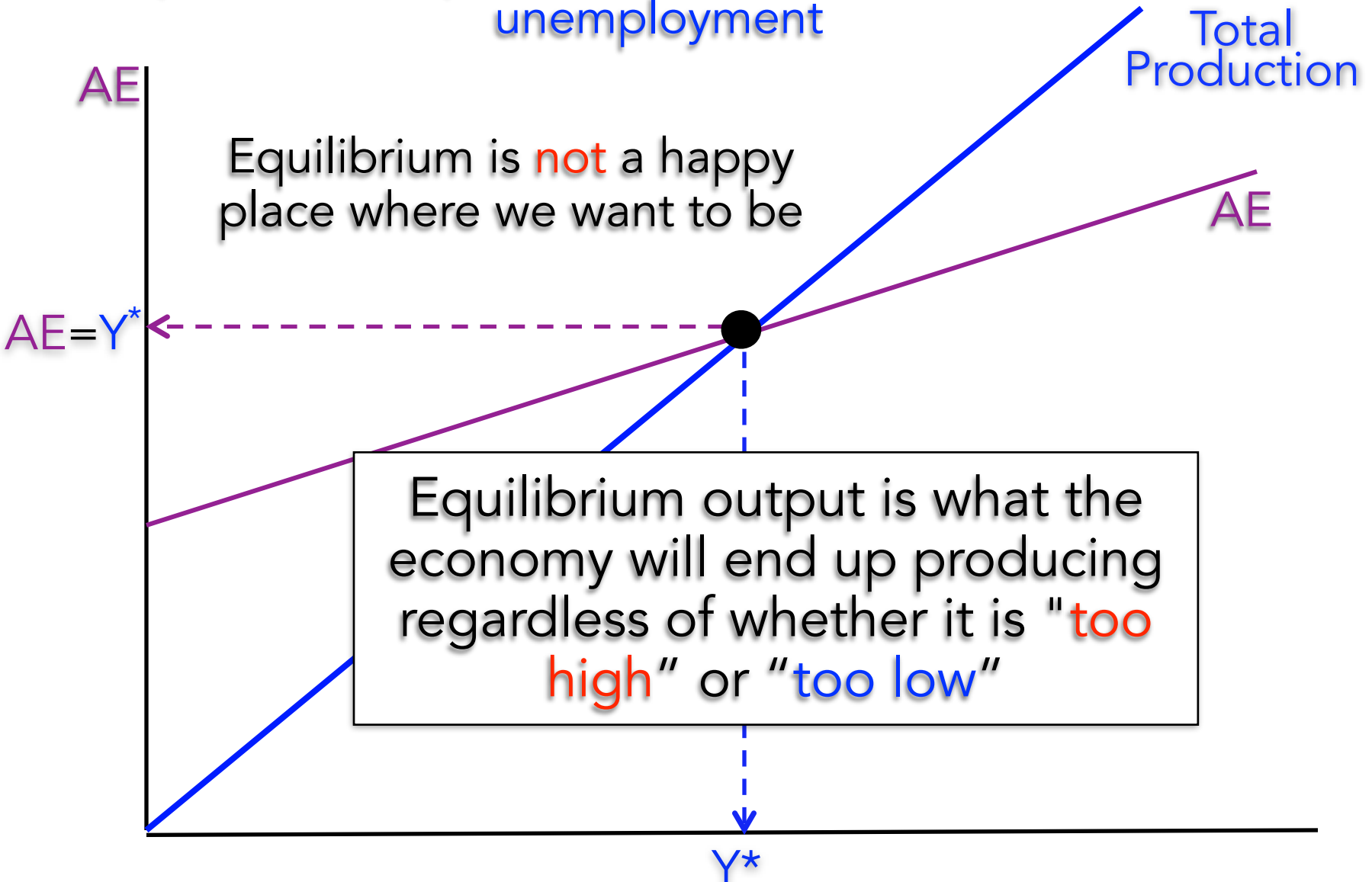
Equilibrium output may be “too low” with massive unemployment

Equilibrium output may be "too high" with rampant  
inflation

Equilibrium is not a happy  
place where we want to be

Equilibrium output is what the economy will end up producing regardless of whether it is "too high" or "too low"

Equilibrium output may be “too low” with massive unemployment



Equilibrium output may be “too high” with rampant inflation

