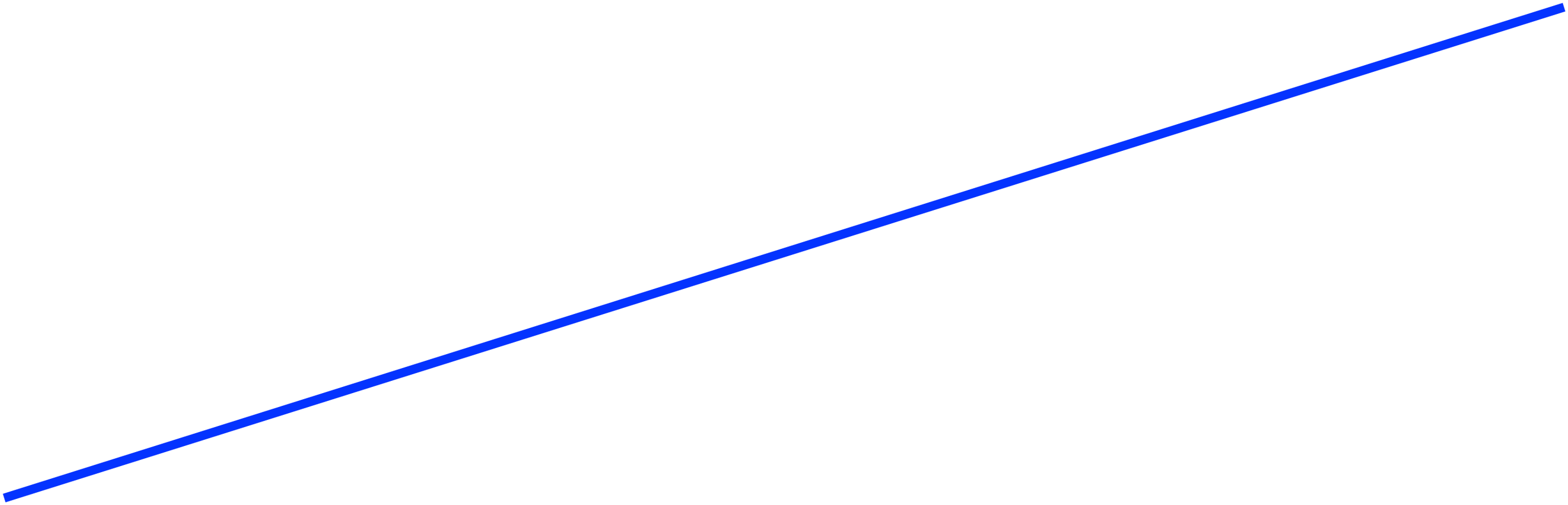
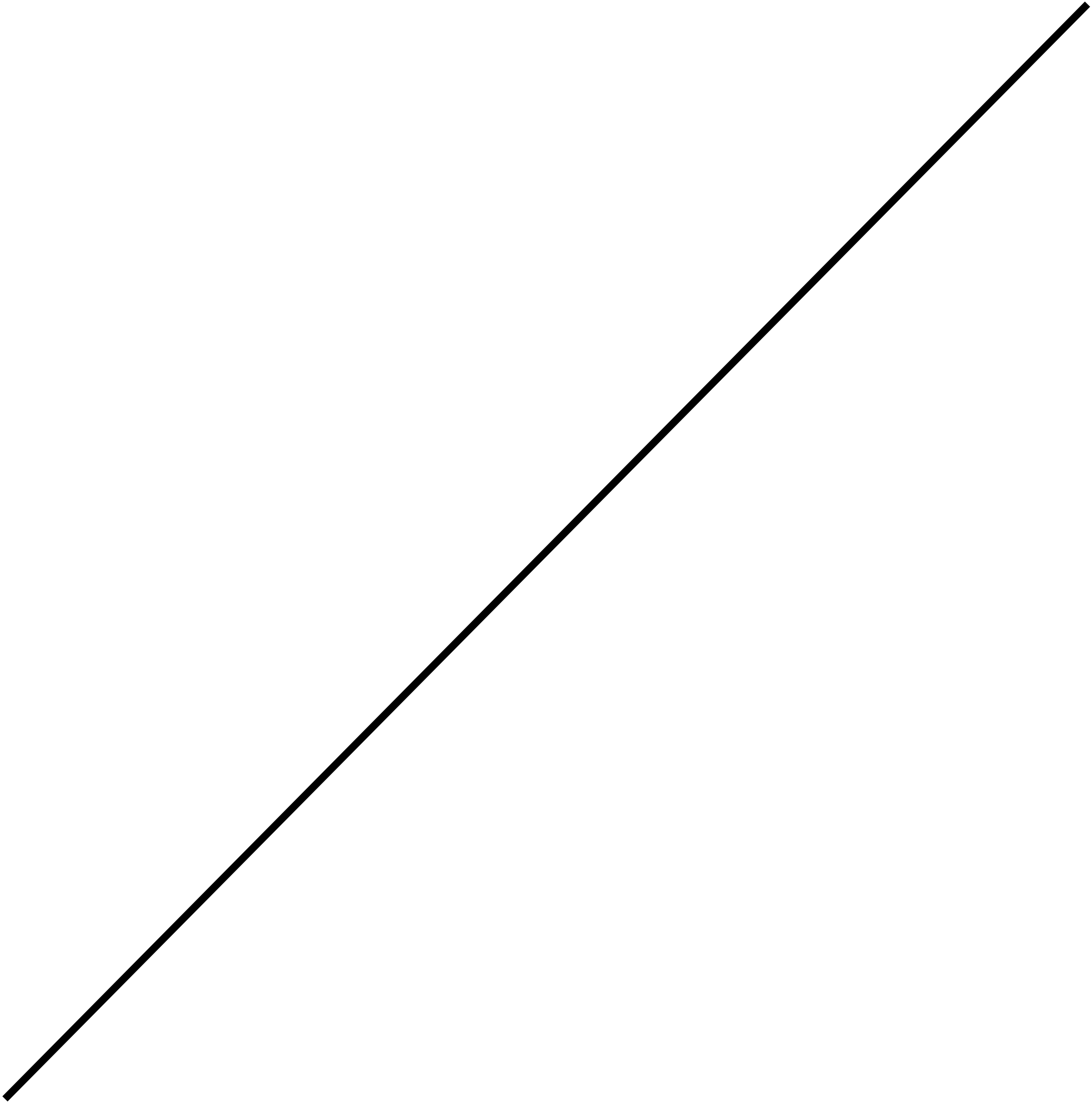
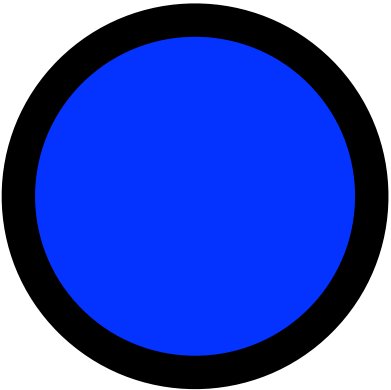


Equilibrium GDP: 9,000



Equilibrium

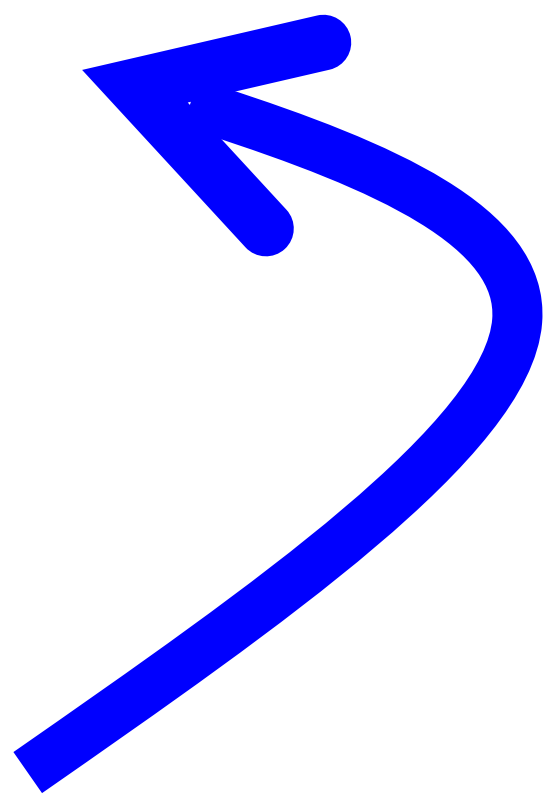


AE0

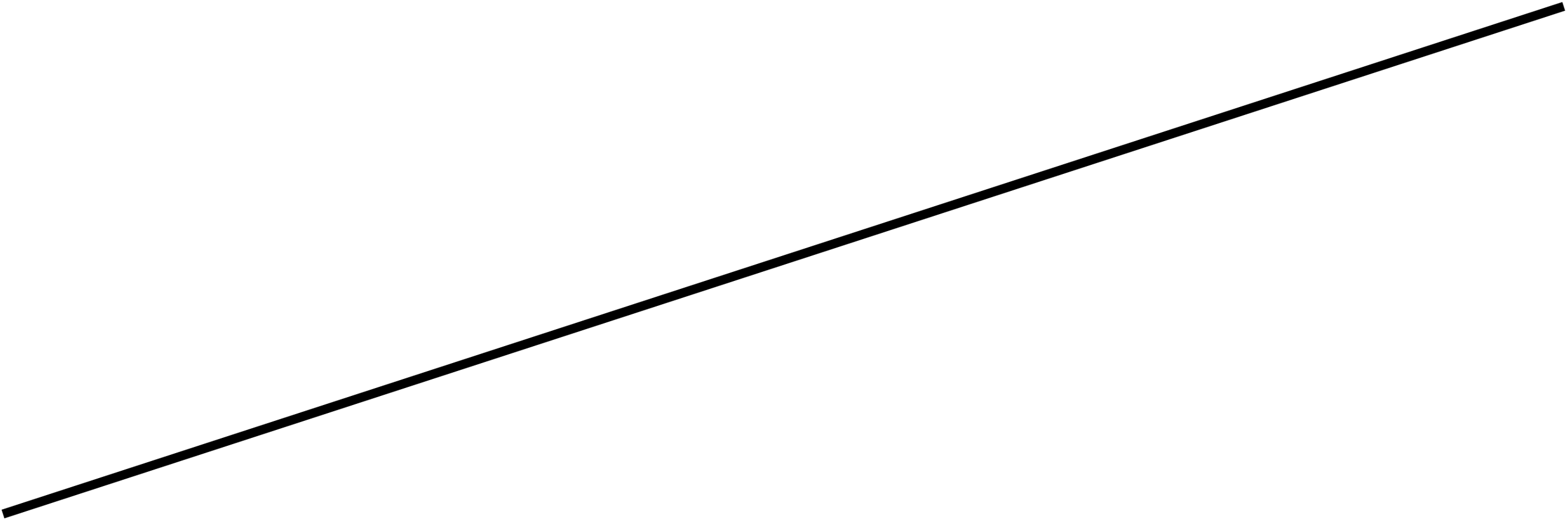
Potential GDP

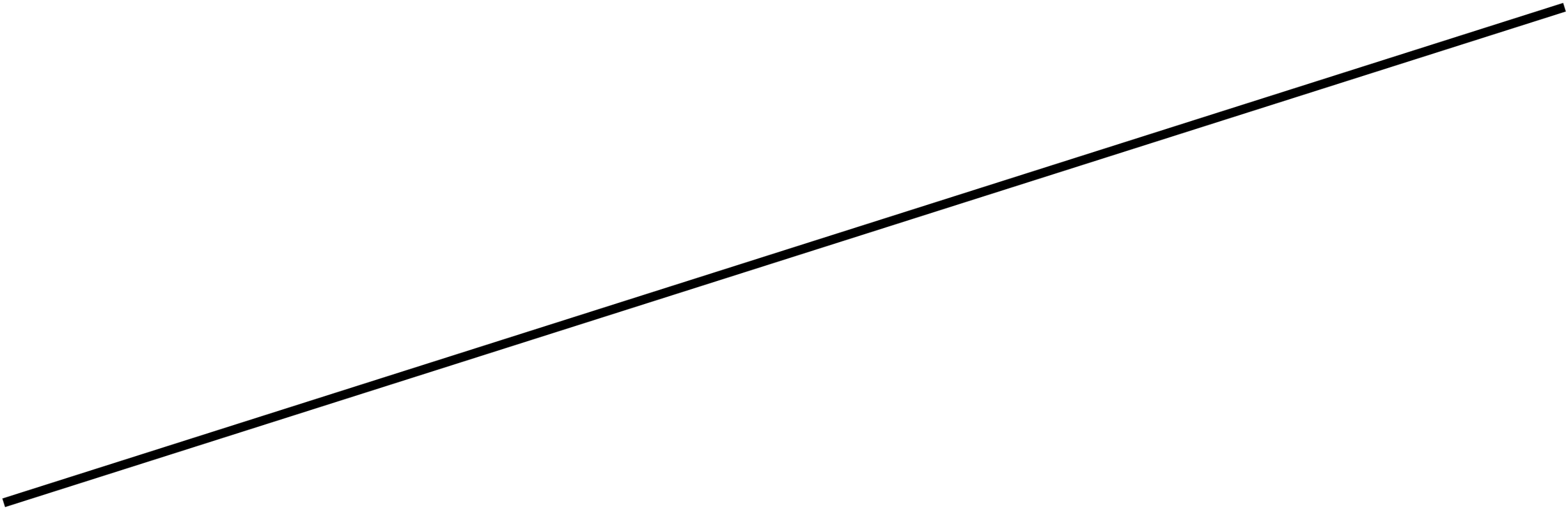
Potential

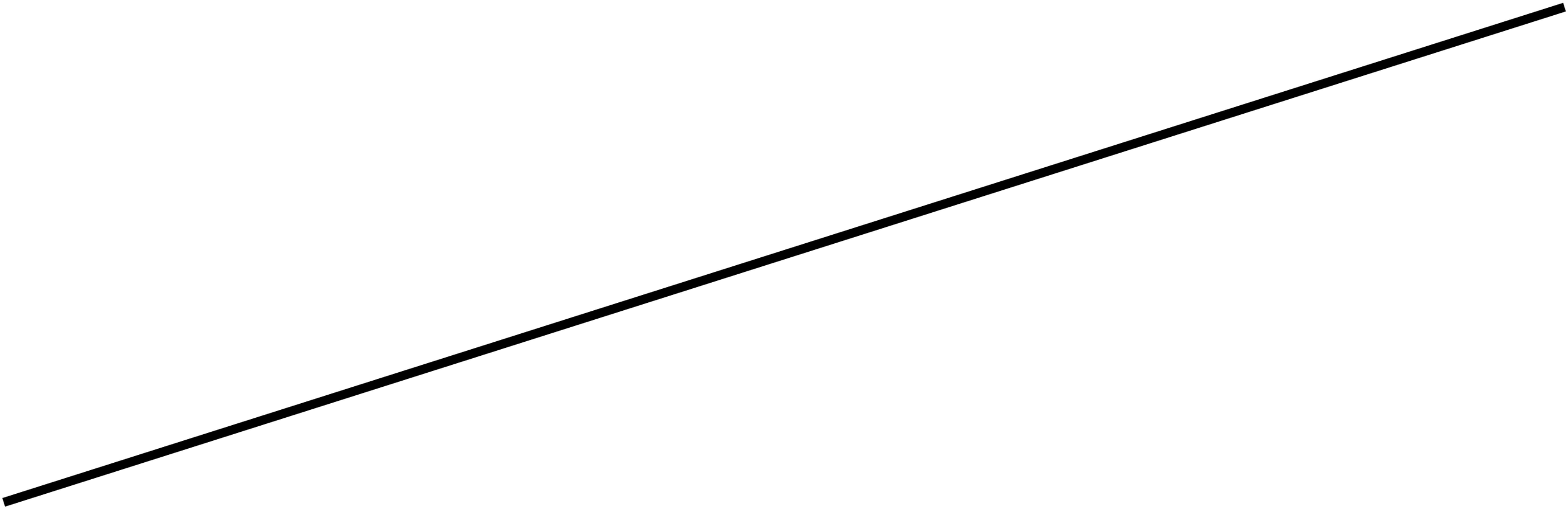
GDP : 7,000



45º



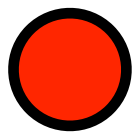




AE1

To eliminate an Inflationary gap, AE must fall

Equilibrium =



Government Policy

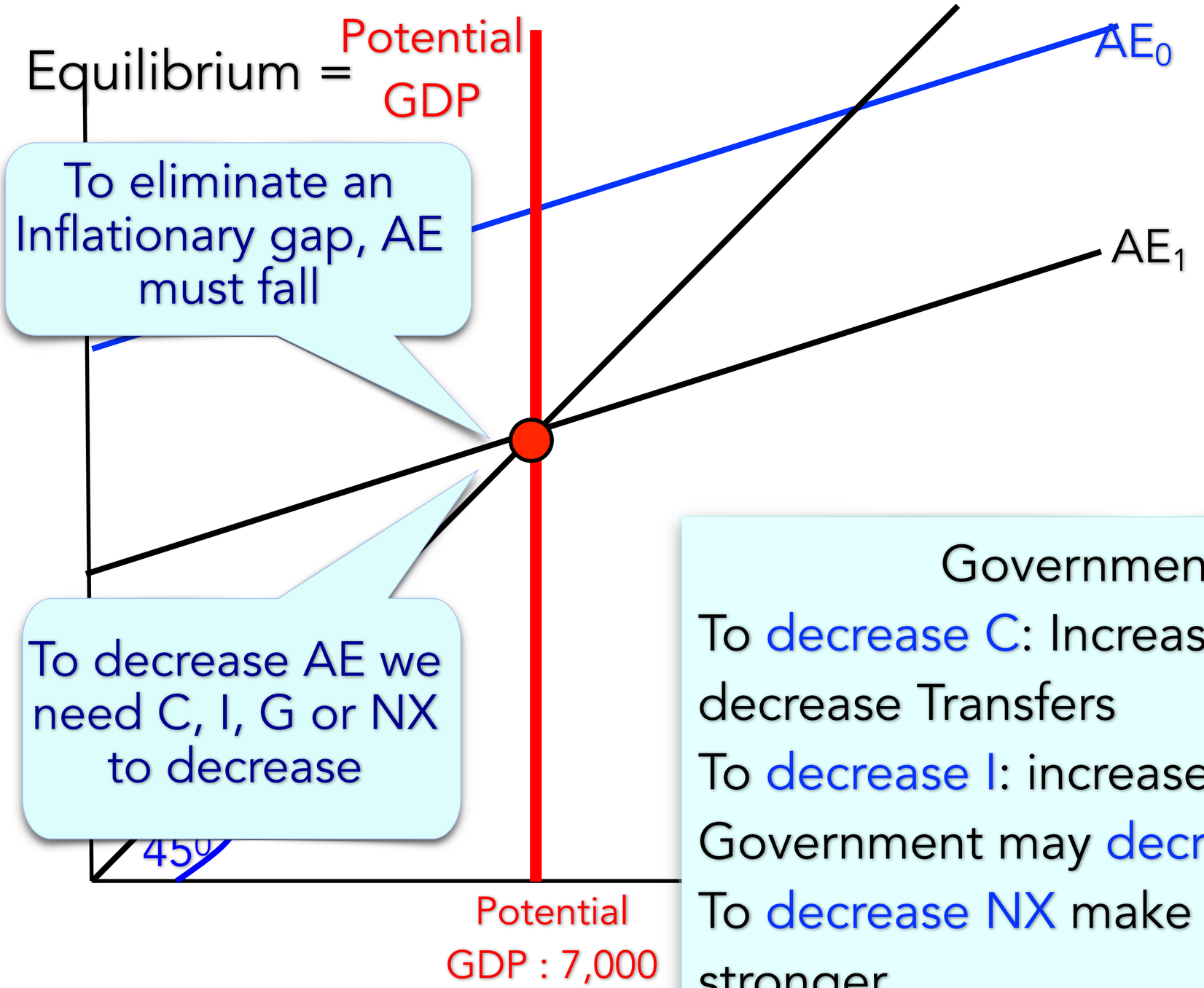
To decrease C: Increase Taxes or decrease Transfers

To decrease I: increase interest rates

Government may decrease spending or

To decrease NX make the dollar stronger

To decrease AE we need C, I, G or NX to decrease



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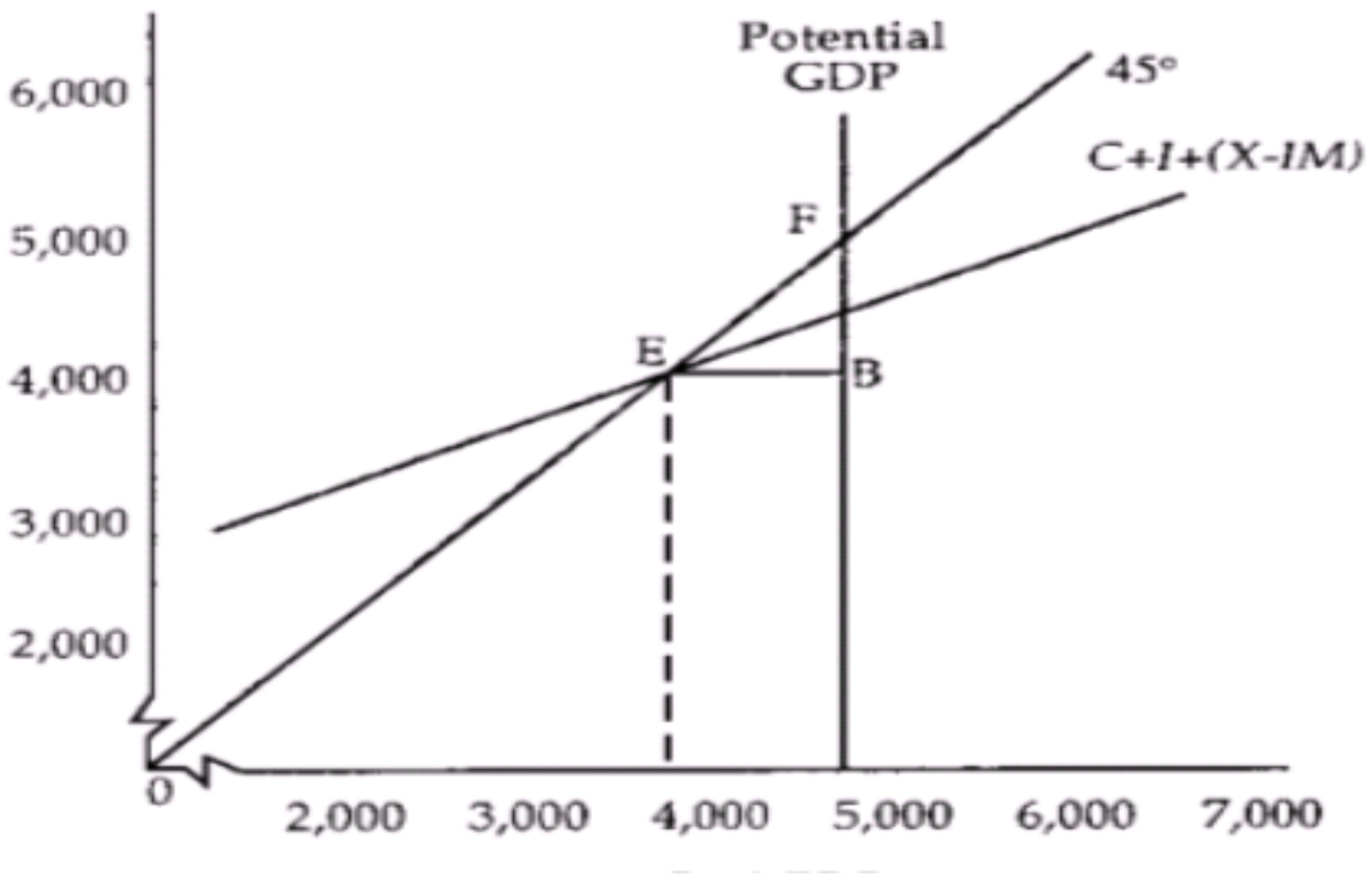
Potential
GDP
45°
C+I+(X-IM)
F
E
B
6,000
5,000
4,000
3,000
2,000
0
2,000
3,000
4,000
5,000
6,000
7,000