

AE_0

Y_0

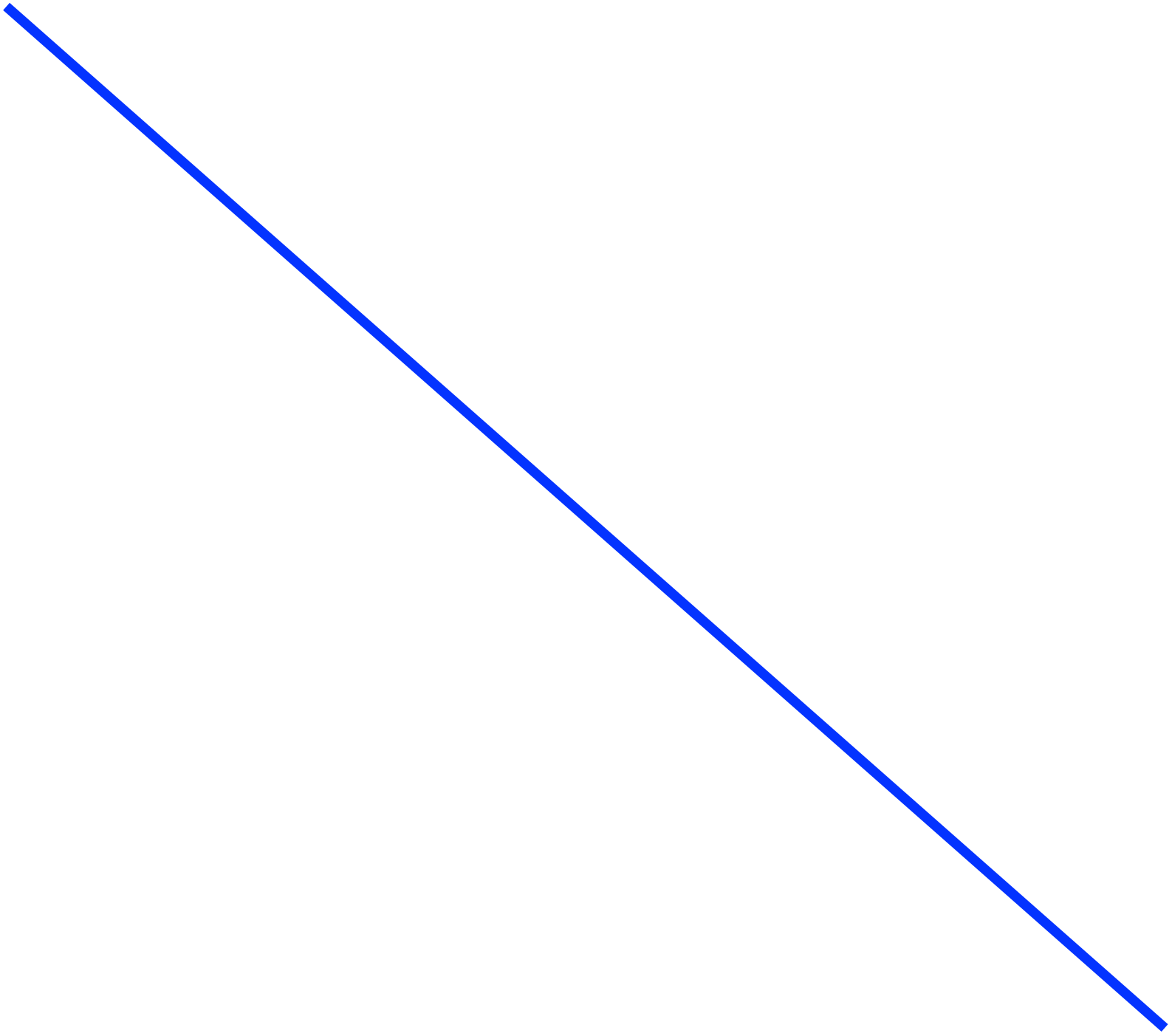
At Potential GDP



Price Level
(CPI)







AD₀

PO

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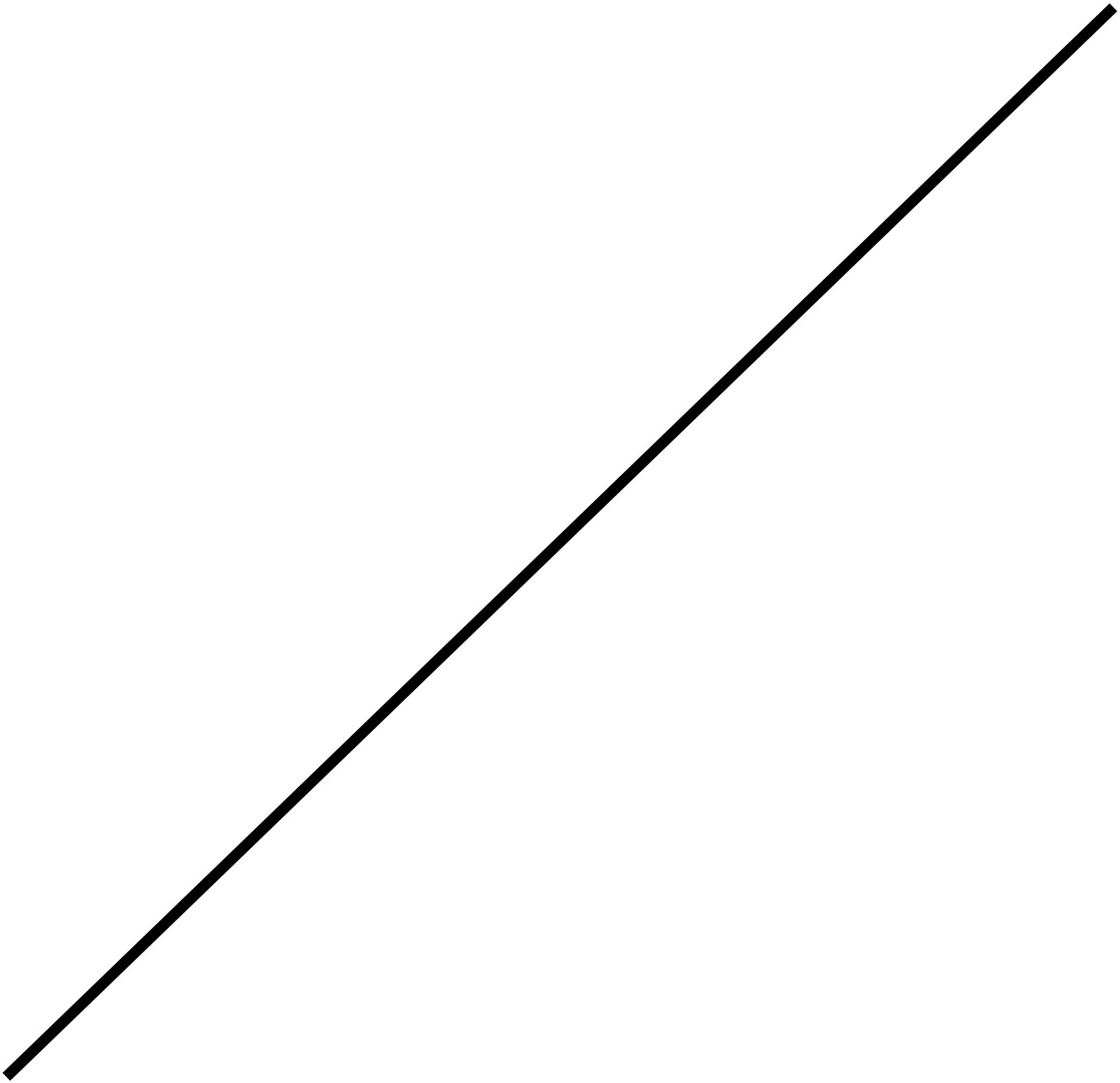
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AS₀



GDP₀



At Potential GDP

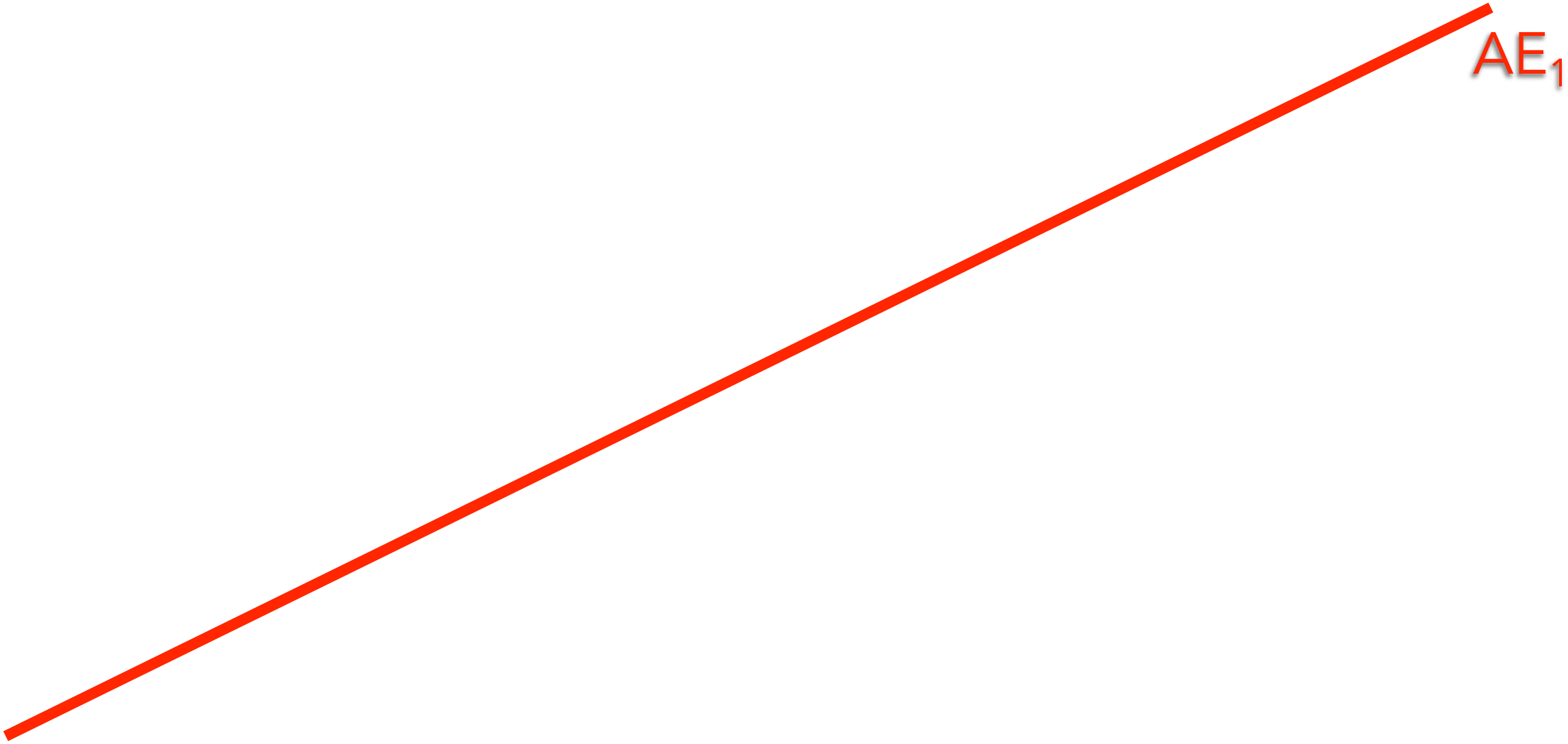


Recessionary Gap



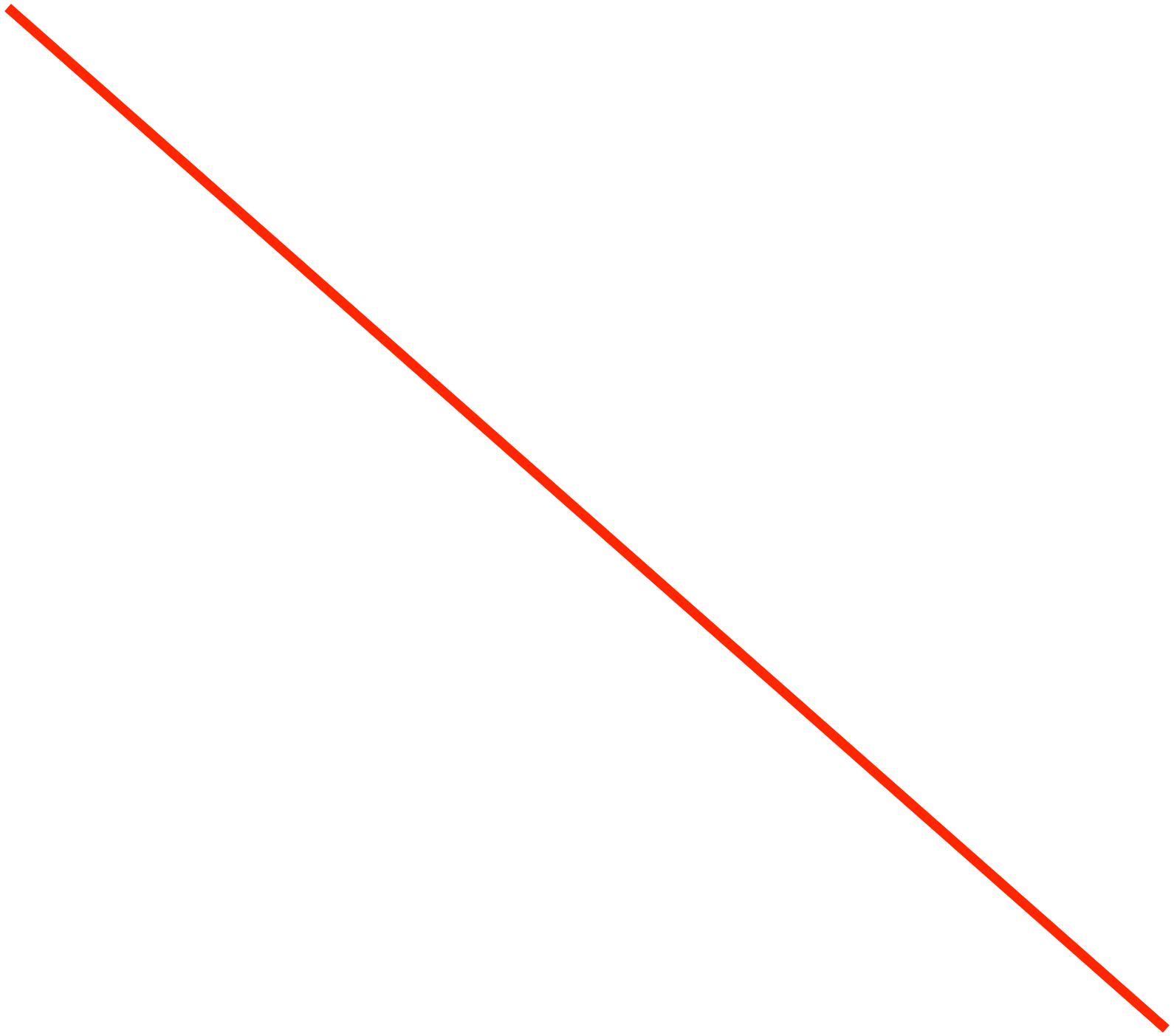
Recessionary Gap





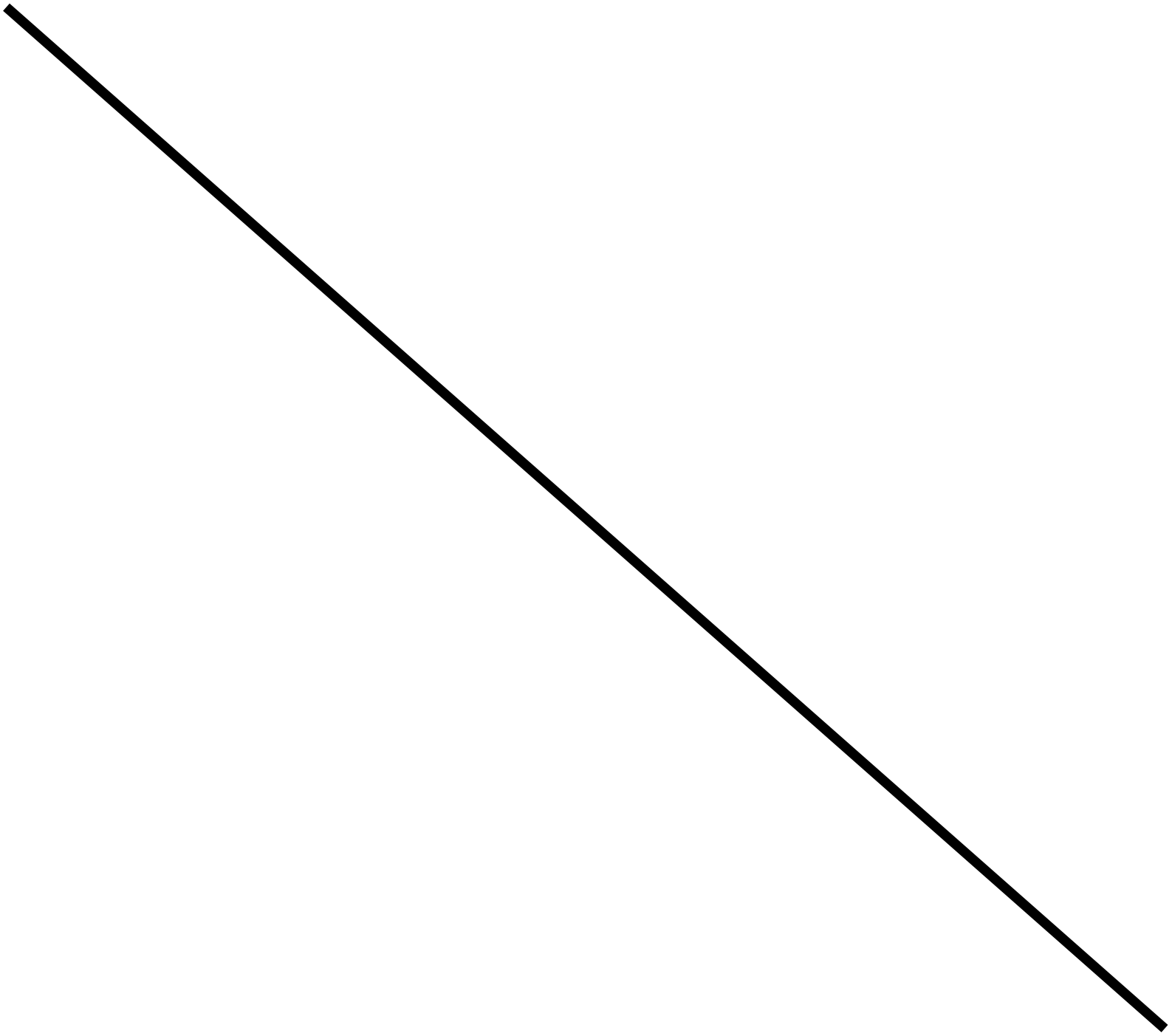
Increase in AD





AD₁

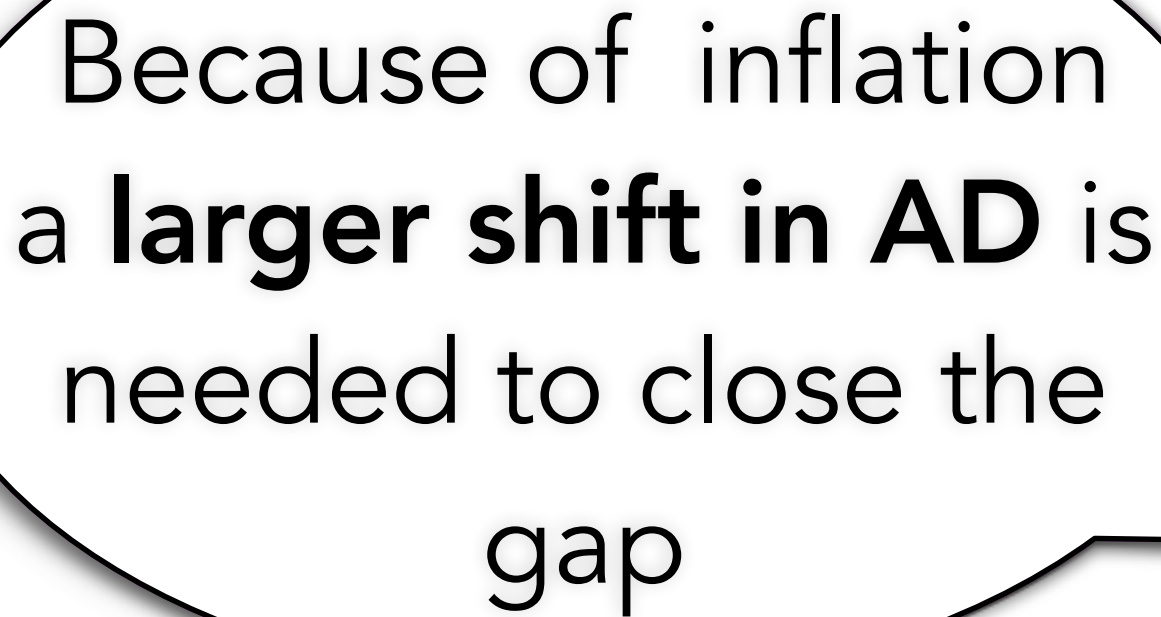
Inflation **reduces** the size of the multiplier



AD₂





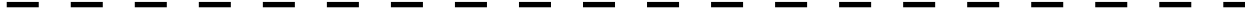


Because of inflation
a **larger shift in AD** is
needed to close the
gap

P₁ - - - - -

GDP₁

P₂



GDP₂

Inflation **reduces** the size of the multiplier

Because of inflation
a **larger shift in AD** is
needed to close the
gap

