

T



C





S

e

a

R

e

C



S

S





n



y

G

a

p

W





h



u





n





e

a

S



n

g



h



D















h

e

g



V



n

m



n



m

u

S



n

C





a

S



b





h

G



V



m

e

n



S

p



n

d



n

g

a

n

d

T

a





S

b

y



h

e

S

a

m



a

m



u

n



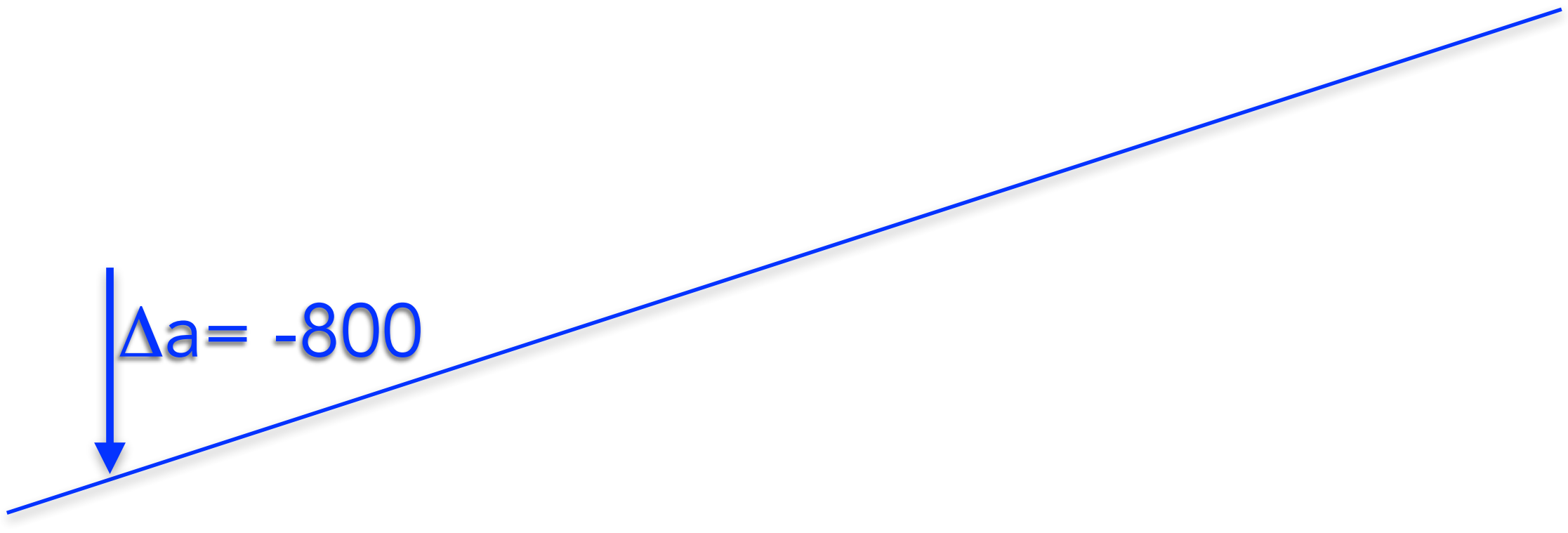
The Government must increase both Taxes and Government Spending by 1,000 in order to close a 1,000 Recessionary Gap

If taxes increase by 1,000, Disposable Income decrease by 1,000 and Consumption decrease by $1,000 \times \text{MPC} = -1,000 \times 0.8 = -800$
 $\Delta a = -800$ The AE line shifts down by 800

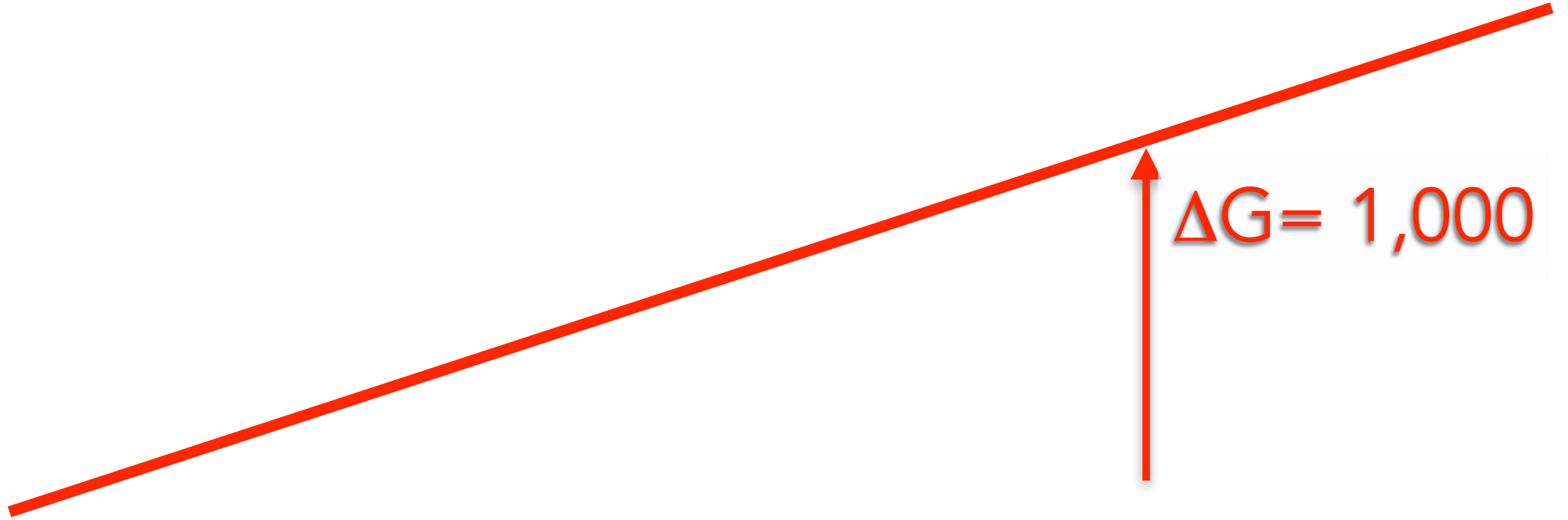
If Government Spending increase by 1,000

$\Delta G = 1,000$, the AE line shifts up by 1,000

The net effect of increasing G and T by 1,000 is a net increase of 200: the AE line shifts up by 200



$\Delta a = -800$





To close a Recessionary Gap
without increasing the Deficit the government
must **increase both** Government Spending and
Taxes by the **same** amount

To close a Recessionary Gap

without increasing the Deficit the government must **increase both** Government Spending and Taxes by the **same** amount

The Government must increase both Taxes and Government Spending by **1,000** in order to close a **1,000** Recessionary Gap

If taxes increase by 1,000, Disposable Income decrease by **1,000** and Consumption decrease by $1,000 \times \text{MPC} = -1,000 \times 0.8 = -800$
 $\Delta a = -800$ The AE line shifts down by 800

If Government Spending increase by **1,000**
 $\Delta G = 1,000$, the AE line shifts up by 1,000

The net effect of increasing G and T by 1,000 is a **net increase** of **200**: the AE line shifts up by 200

