

NY

=

NT

ΔC

=

ΔY

We know we want Equilibrium GDP to decrease by 2,000:

$$\Delta Y = -2,000$$

Effect on Consumption:

Effect on the Budget Deficit:

$$\Delta \text{Deficit} \equiv \Delta G - \Delta T$$

The Tax Multiplier

$$\left(\frac{-MPC}{1-MPC} \right)$$

$$\left(\frac{-0.8}{1-0.8} \right)$$

$$\left(\frac{-0.8}{0.2} \right)$$

-4

(Tax Multiplier)

$$\Delta C = -2,000$$

$$\Delta \text{Deficit} = 0 - (500) = -500$$

Assume: $MPC = 0.8$

Recessionary Gap:

$$7,000 - 9,000 = -2,000$$

ΔY = -2,000

-2,000 = ΔT

(-4)

$$\Delta T = -2,000/-4$$

$\Delta T = +500$

The Government must increase Taxes by 500
in order to close a 2,000 Inflationary Gap

A 500 increase in Taxes will
decrease the Deficit by 500

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

Recessionary Gap:
 $7,000 - 9,000 = -2,000$

We know we want Equilibrium GDP to decrease by 2,000:

$$\Delta Y = -2,000$$

$$\left(\frac{-MPC}{1-MPC} \right) = \left(\frac{-0.8}{1-0.8} \right) = \left(\frac{-0.8}{0.2} \right) = -4$$

$$\Delta Y = \Delta T \left(\text{Tax Multiplier} \right)$$

Effect on Consumption:

$$\Delta C = -2,000$$

Effect on the Budget Deficit:

$$\Delta T = -2,000 / -4$$

$$\Delta T = +500$$

$$\Delta \text{Deficit} = 0 - (500) = -500$$

The Government must increase Taxes by 500
in order to close a 2,000 Inflationary Gap

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