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The Government must decrease both Taxes
and Government Spending by 2,000 in order
to close a 2,000 Inflationary Gap

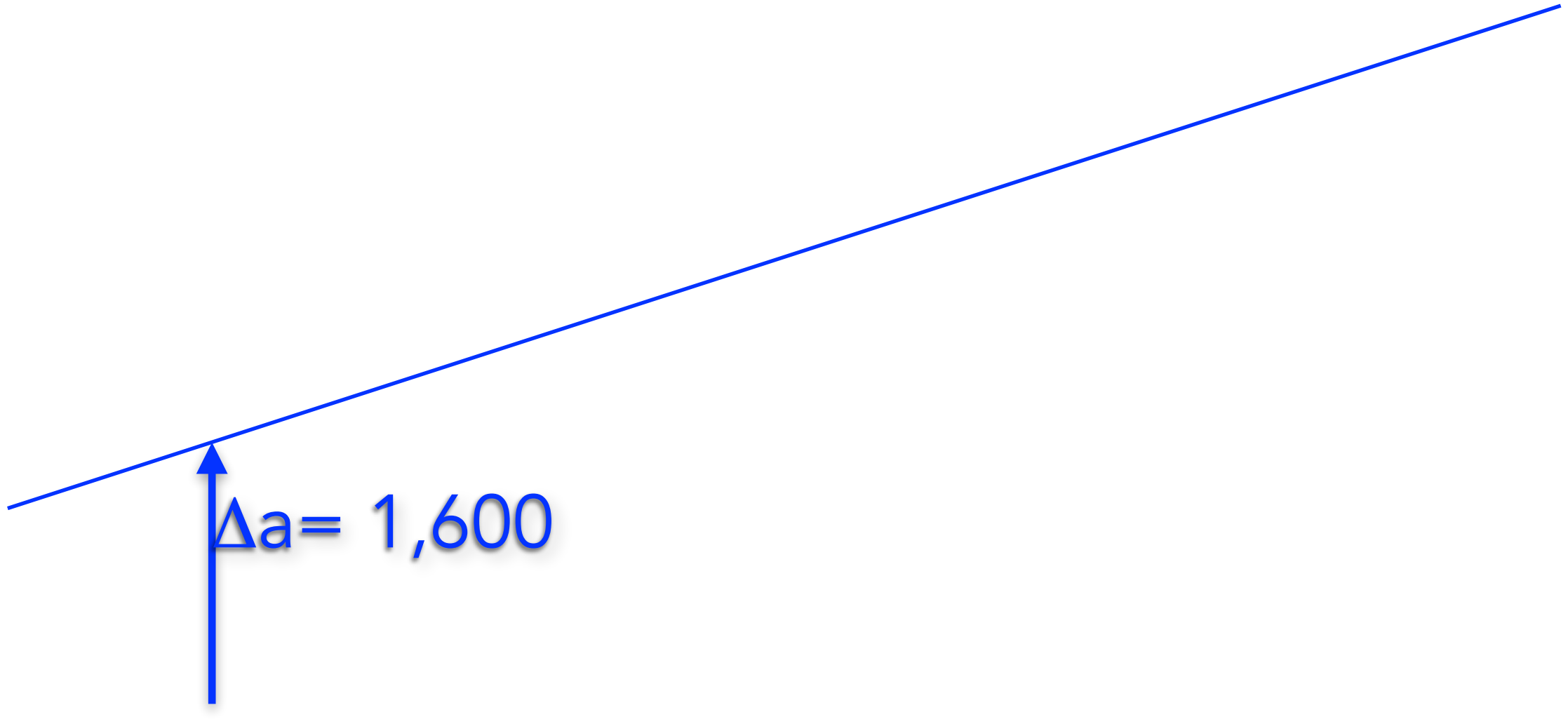
If taxes decrease by 2,000, Disposable Income increase by 2,000 and Consumption increase by

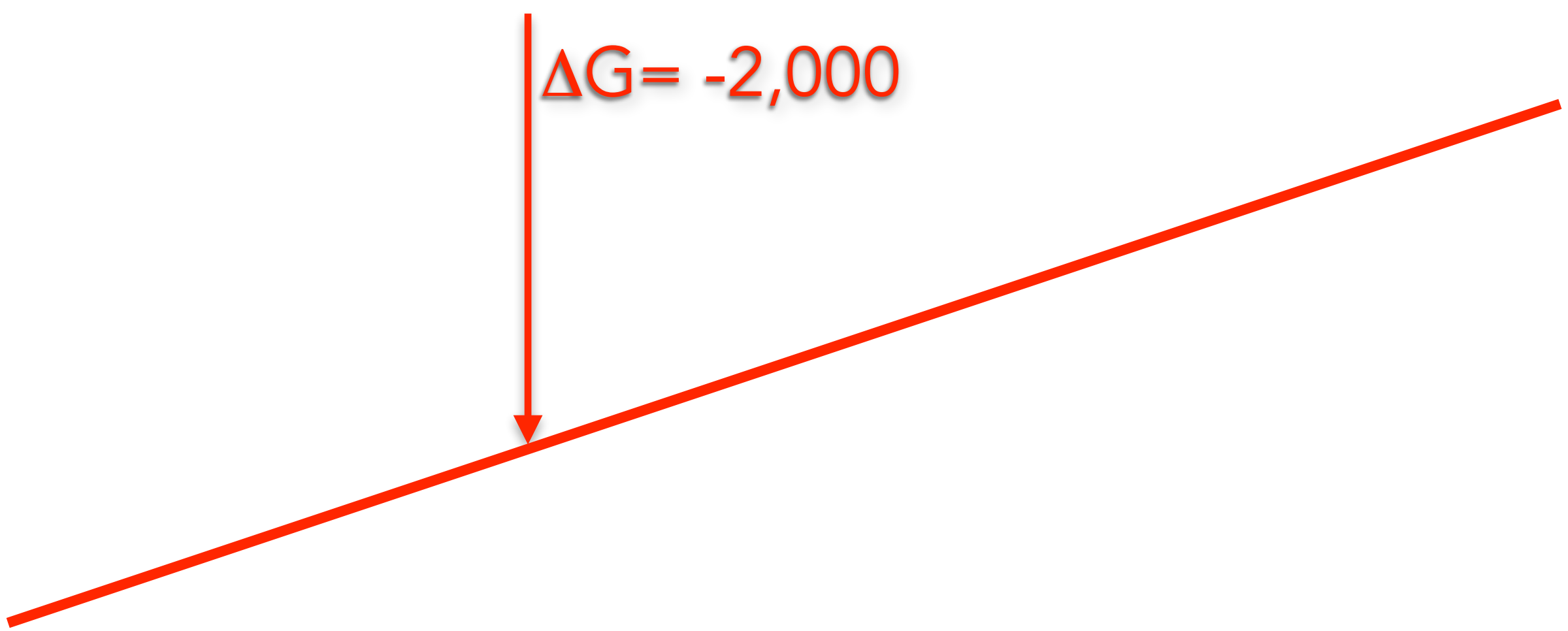
$$2,000 \times \text{MPC} = 2,000 \times 0.8 = 1,600$$

$\Delta a = +1,600$ The AE line shifts up by 1600

If Government Spending decrease by 2,000
 $\Delta G = -2,000$, the AE line shifts down by 2,000

The net effect of decreasing G and T by 2,000 is a net decrease of 400: the AE line shifts down by 400





A diagram showing a red line sloping upwards from left to right. A vertical red arrow points downwards from the top of the line to the line itself. To the right of the arrow, the text $\Delta G = -2,000$ is written in red.

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



A diagram illustrating a downward shift of a line. A solid magenta line slopes upward from left to right. A second, dashed magenta line is parallel to and below the first. A vertical magenta arrow points from the first line down to the second. To the right of the arrow, the text $\Delta AE = -400$ is written in magenta.

$\Delta AE = -400$



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without increasing the Deficit
the government must **decrease**
both Government Spending and
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