



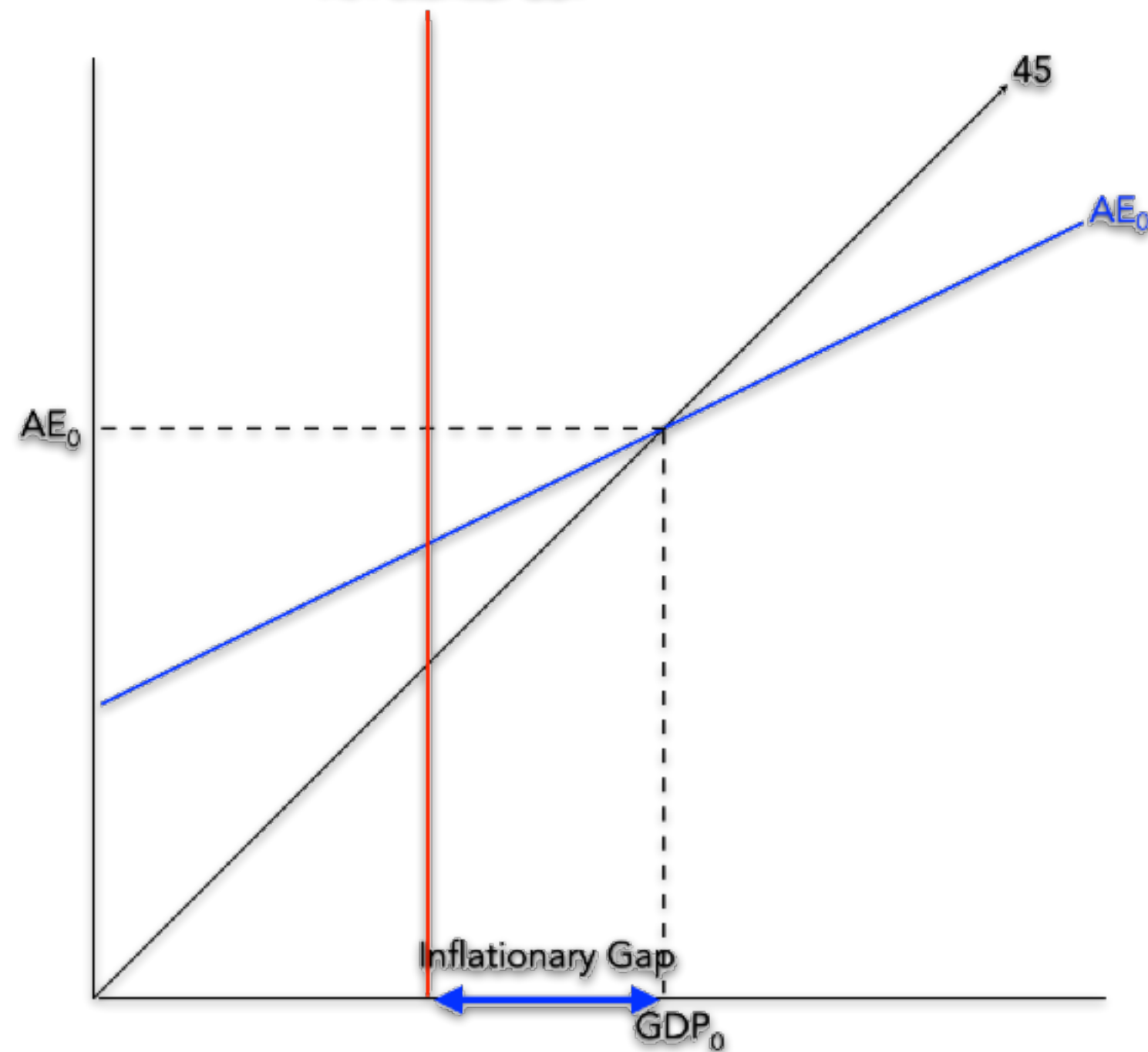
To close an **Inflationary** Gap, Aggregate Expenditures and Aggregate Demand must  
decrease

1. Increase Taxes and/or Decrease Transfers to decrease Consumption

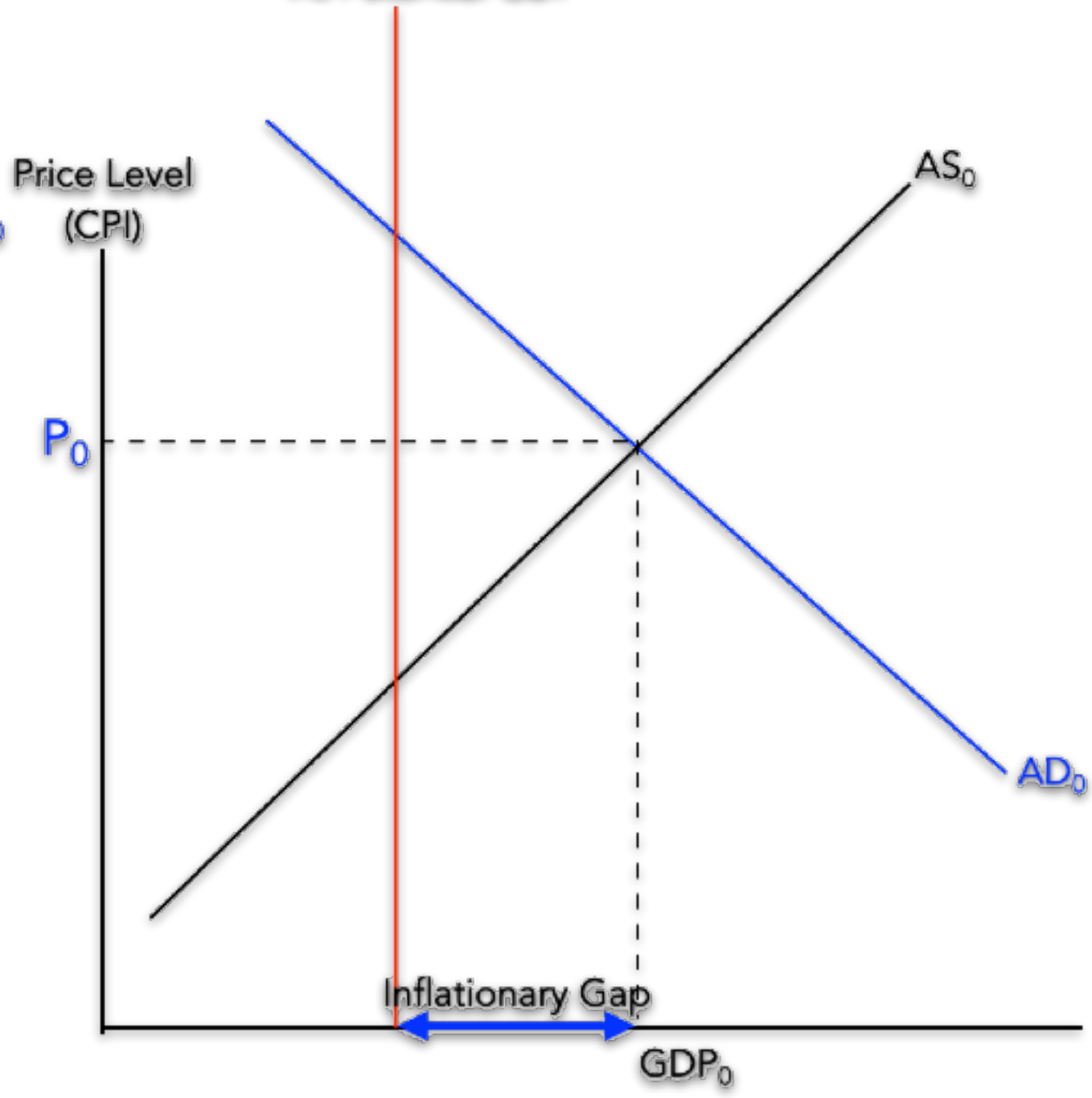
2. Decrease Government Spending

Contractary Policy

At Potential GDP



At Potential GDP

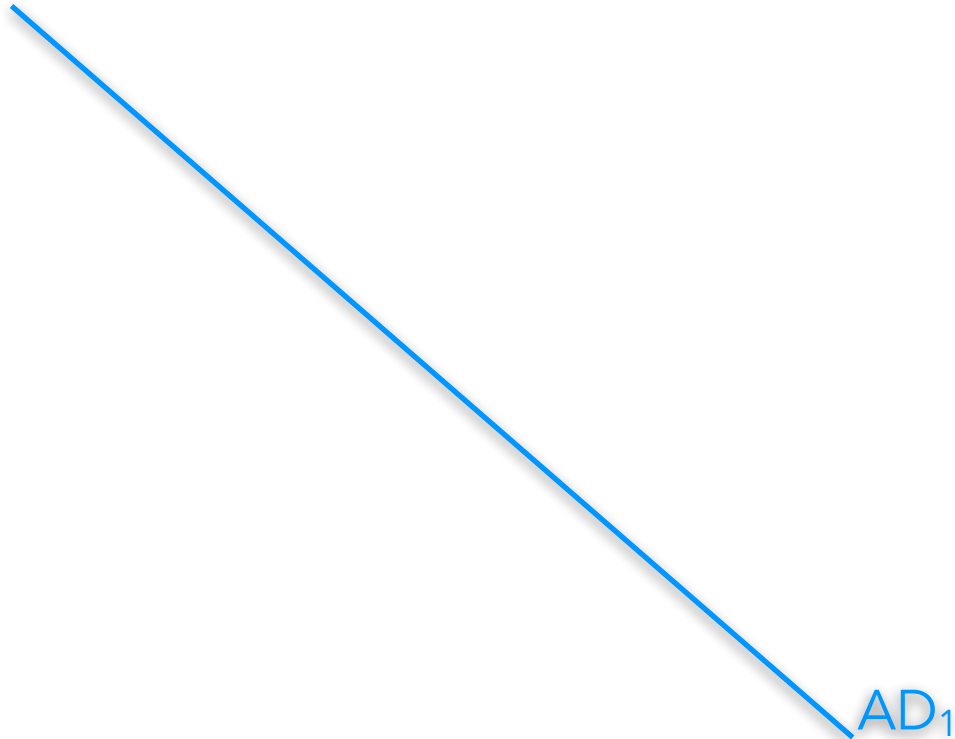


3. **Sell bonds** to **decrease** the Money Supply and cause an **increase** in all interest rates to reduce Investment spending

Contractionary Fiscal Policy



Contractionary Monetary Policy



$AE_1$

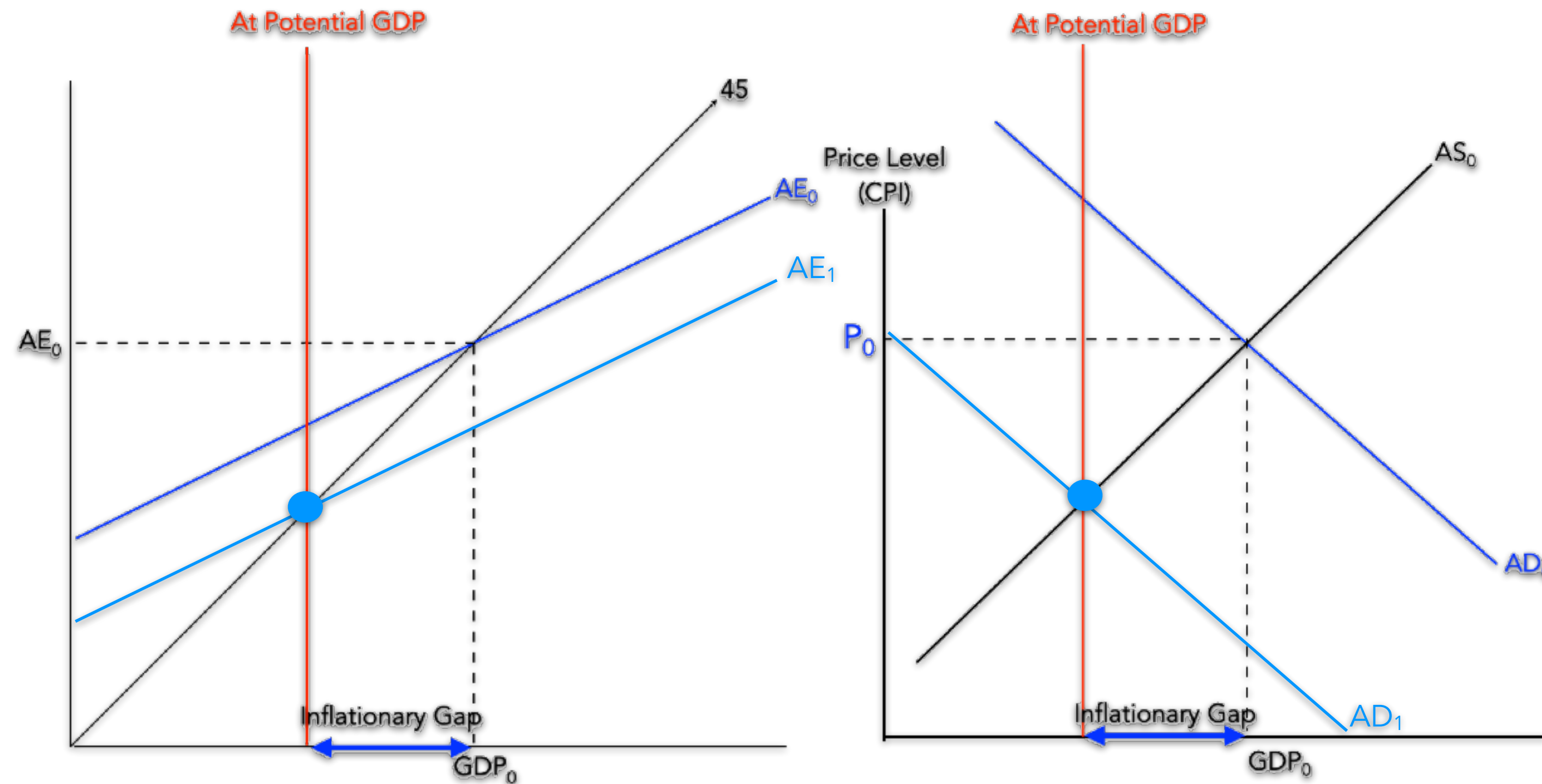
A solid blue line with a positive slope, starting from the bottom-left and extending towards the top-right. The line is straight and has a consistent upward angle.





3. Increase interest rates to decrease investment

# Contractionary Policy



To close an **Inflationary** Gap, Aggregate Expenditures and Aggregate Demand must decrease

1. **Increase** Taxes and/or Decrease Transfers to decrease Consumption
2. **Decrease** Government Spending

Contractionary Fiscal Policy

3. **Sell bonds** to **decrease** the Money Supply and cause an **increase** in all interest rates to reduce Investment spending

Contractionary Monetary Policy

# Monetary Policy Tools

## 1. Open Market Operations