

AD-AS model 4 (equilibria)

AS = Aggregate supply
 PL = Price level
 LRAS = Long-run AS

AD = Aggregate demand = $C + I + G + (X - M)$
 rGDP = real gross domestic product
 SRAS = Short-run AS

1 Equilibria

11 Long-run equilibrium	12 Short-run equilibrium
Three variables (LRAS, SRAS, AD) meet at point A.	Only two variables (SRAS, AD) meet at point B.

2 Example I: Shift of the AD curve to the right (due to a rise in consumption)

21 Short-run equilibrium

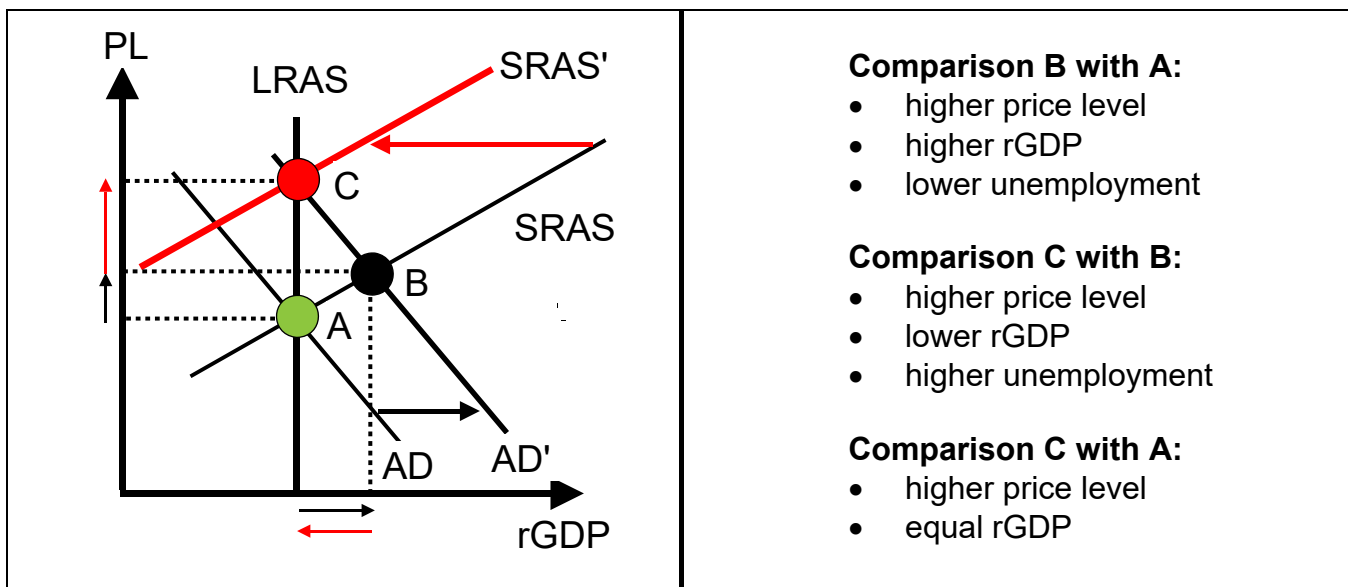
	<p>Comparison B with A:</p> <ul style="list-style-type: none"> • higher price level • higher rGDP • lower unemployment
--	--

2 Return to a long-run equilibrium

A return to a long-run equilibrium can be achieved by a shift of the SRAS curve or the AD curve.

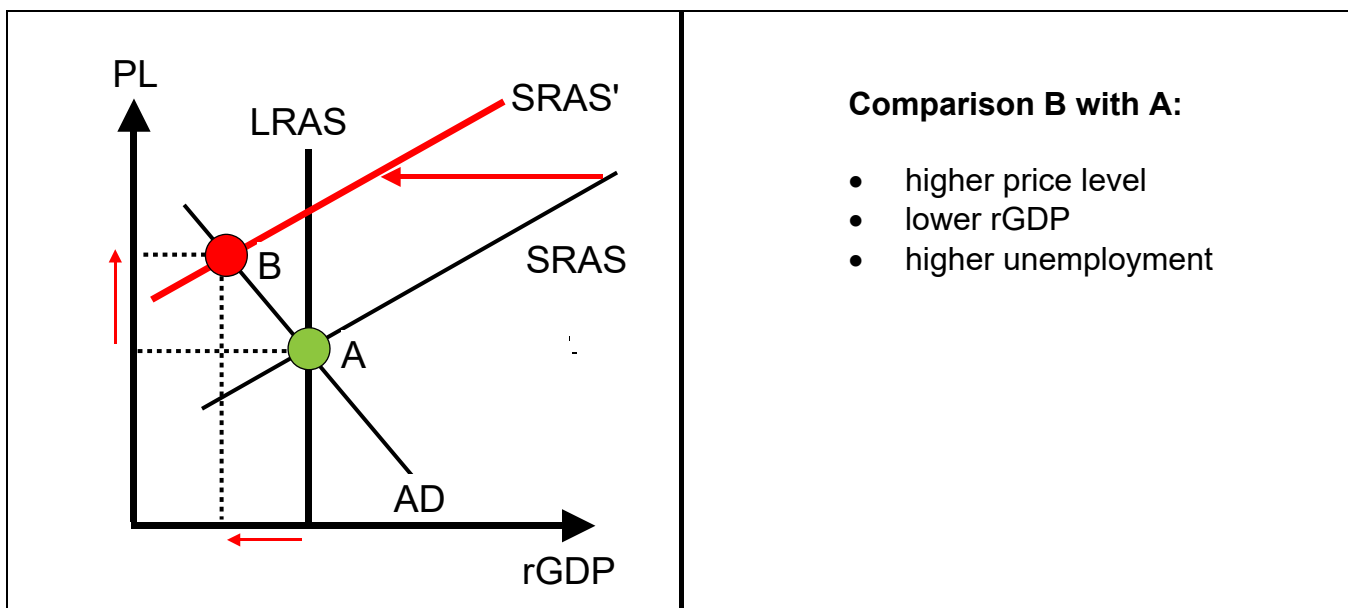
The SRAS curve shifts to the left if the production costs more, e.g. due to higher wages. If this happens with delay, the fiscal policy (government spending, taxes) could ensure that the AD curve shifts to the left until the point A (not shown below).

Now we assume that workers get higher wages, which will bring about a shift of the SRAS curve to the left:



3 Example II: Shift of the SRAS curve to the left (due to higher production costs)

31 Short-run equilibrium



32 Return to a long-run equilibrium

A return to a long-run equilibrium can again be brought about by a shift of the SRAS curve or the AD curve.

A shift of the SRAS curve to the right happens if the production costs less (e.g. due to lower input prices, especially lower wages). In this case, the input prices must be **flexible** (321).

However, if the input prices are **rigid**, the SRAS curve does not shift to the right. In this case, the AD curve is shifted to the right by the fiscal policy (increases in government spending or tax cuts) (322).

321 Input prices are flexible .	322 Input prices are rigid .
<p>Comparison B with A:</p> <ul style="list-style-type: none"> • higher price level • lower rGDP • higher unemployment <p>Comparison A with B:</p> <ul style="list-style-type: none"> • lower price level • higher rGDP • lower unemployment 	<p>Comparison B with A:</p> <ul style="list-style-type: none"> • higher price level • lower rGDP • higher unemployment <p>Comparison C with B:</p> <ul style="list-style-type: none"> • higher price level • higher rGDP • lower unemployment <p>Comparison C with A:</p> <ul style="list-style-type: none"> • higher price level • equal rGDP