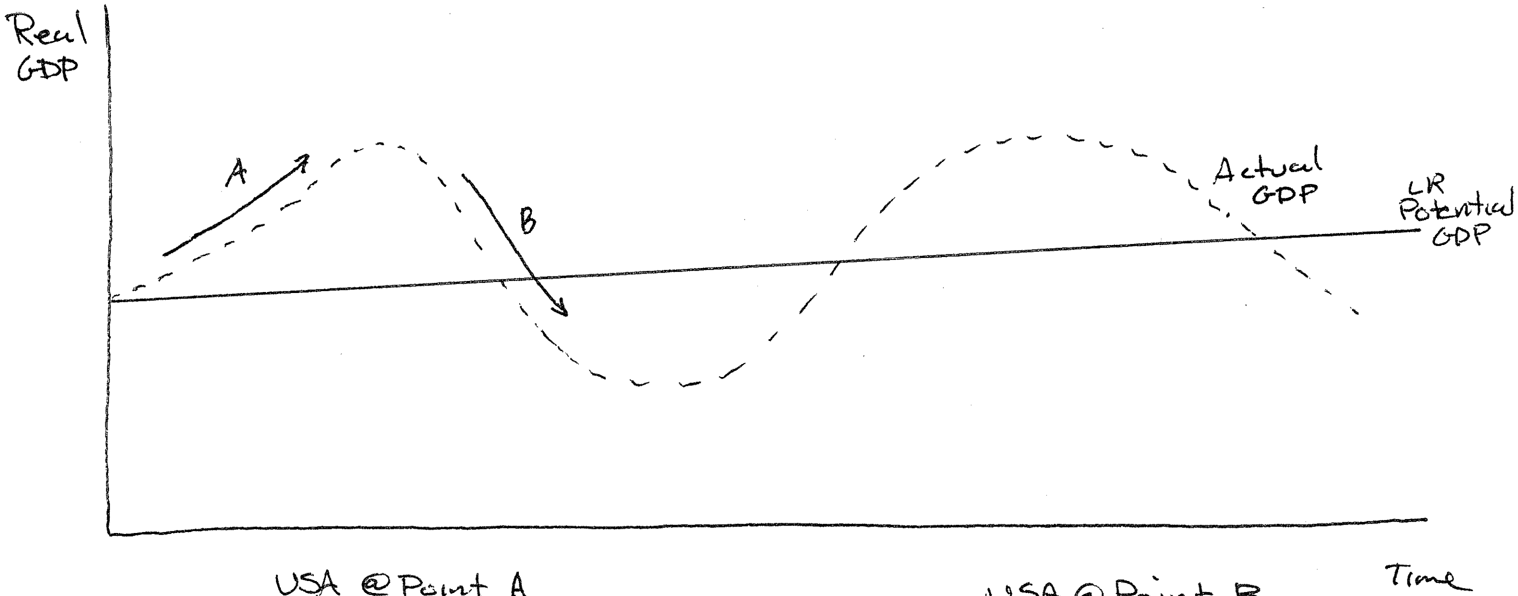
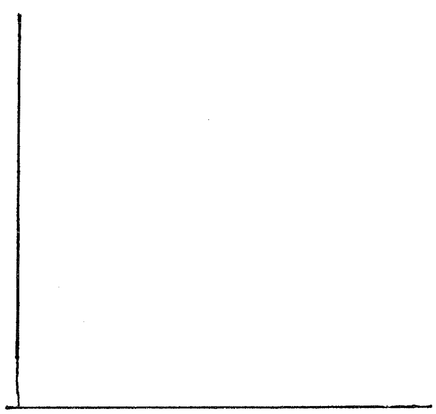
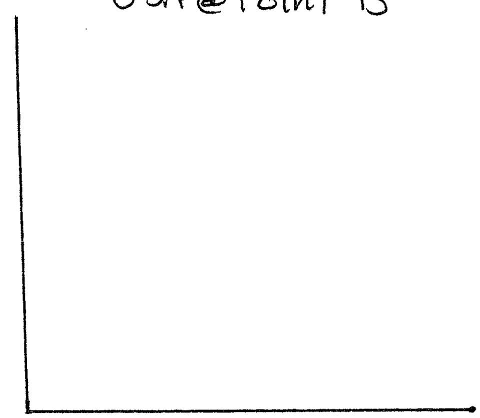
# BUSINESS CYCLE & STABILIZATION THEORY




USA @ Point A



USA @ Point B



Appropriate Gov't Policy @ A

Appropriate Gov't policy @ B

Automatic Stabilizers

Automatic stabilizers

Impact on tax revenue & Gov't budget

Impact on revenue & budget

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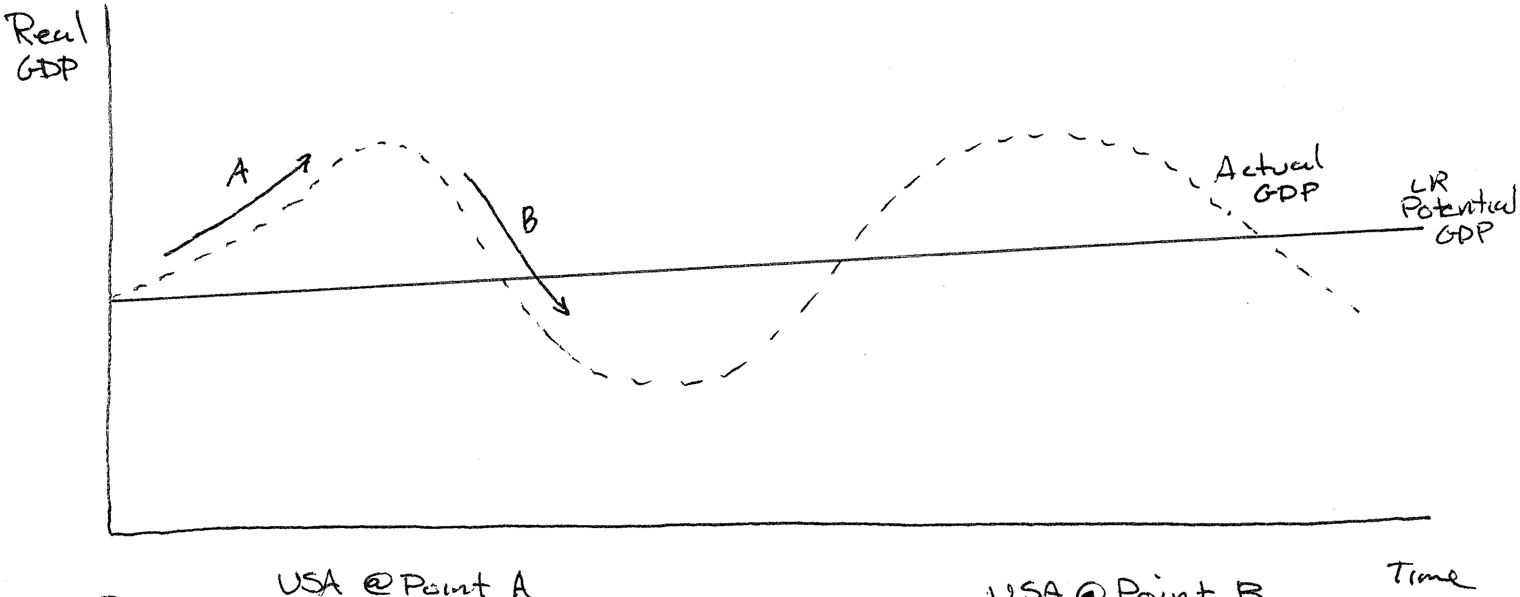
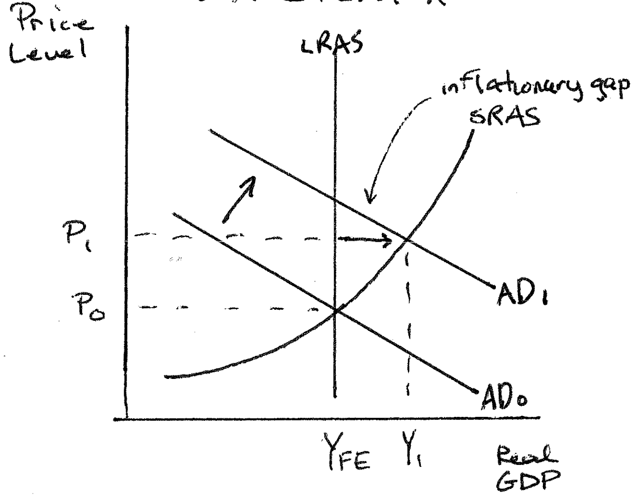
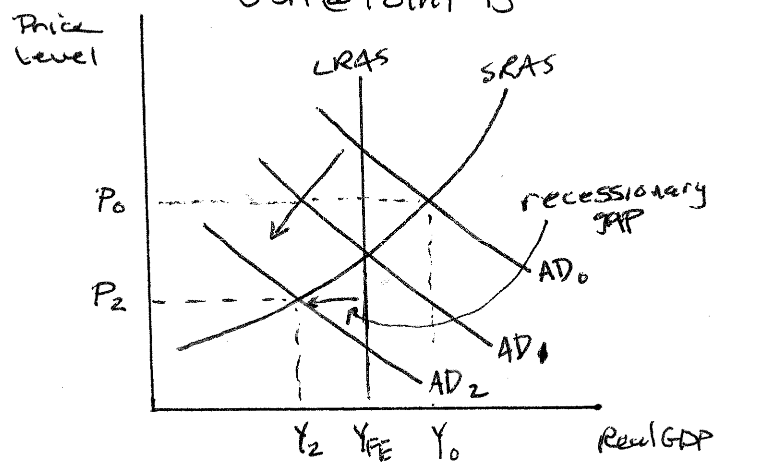



USA @ Point A




USA @ Point B




## Appropriate Gov't Policy @ A

- Raise r
- increase taxes
- reduce G spending

* negative multiplier

## Appropriate Gov't policy @ B

- lower r → ↑I & ↑C → ↑AD
- lower taxes → ↑yd → ↑C → ↑AD
- increase G spending → G↑ → ↑yd → ↑C → ↑AD

* multiplier effect

## Automatic Stabilizers

transfer pymts ↓

taxes ↑ business profits increase,
more wages = wage taxes

## Impact on tax revenue & Gov't budget

revenues ↑ as spending ↓ reducing deficit or creating budget surplus

## Automatic stabilizers

transfer pymts ↑ medicaid
Food & housing assistance
unempl. insurance

taxes ↓ due to fewer hours worked,
layoffs, firings, profits ↓

## Impact on revenue & budget

Revenue drops as spending increases.
If budget was in balance before,
recession causes deficit