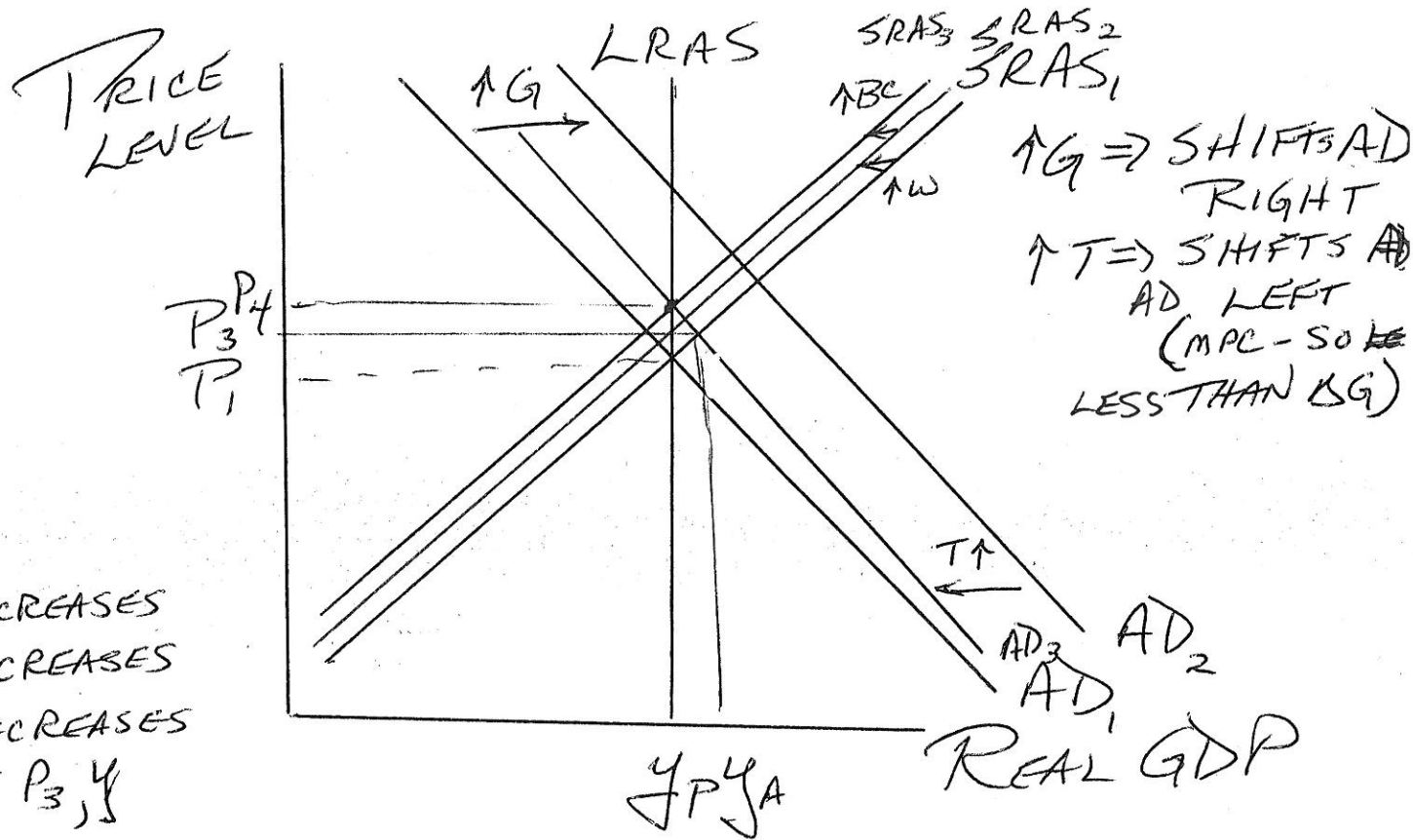


SCENARIOS

#2. Suppose we have a balanced budget increase ($\Delta G = \Delta T$), so that we start at long-run equilibrium. Explain what happens in the short-run first, then explain the long-run final position.



LR. AS $y_A > y_p \Rightarrow$ WAGES RISE, PRICE EXPECTATIONS RISE,
BUSINESS COSTS INCREASE SO SRAS SHIFTS LEFT TO SRAS₃

FINAL POSITION: $U = U_N$; $y = y_p$; P INCREASES TO P_4