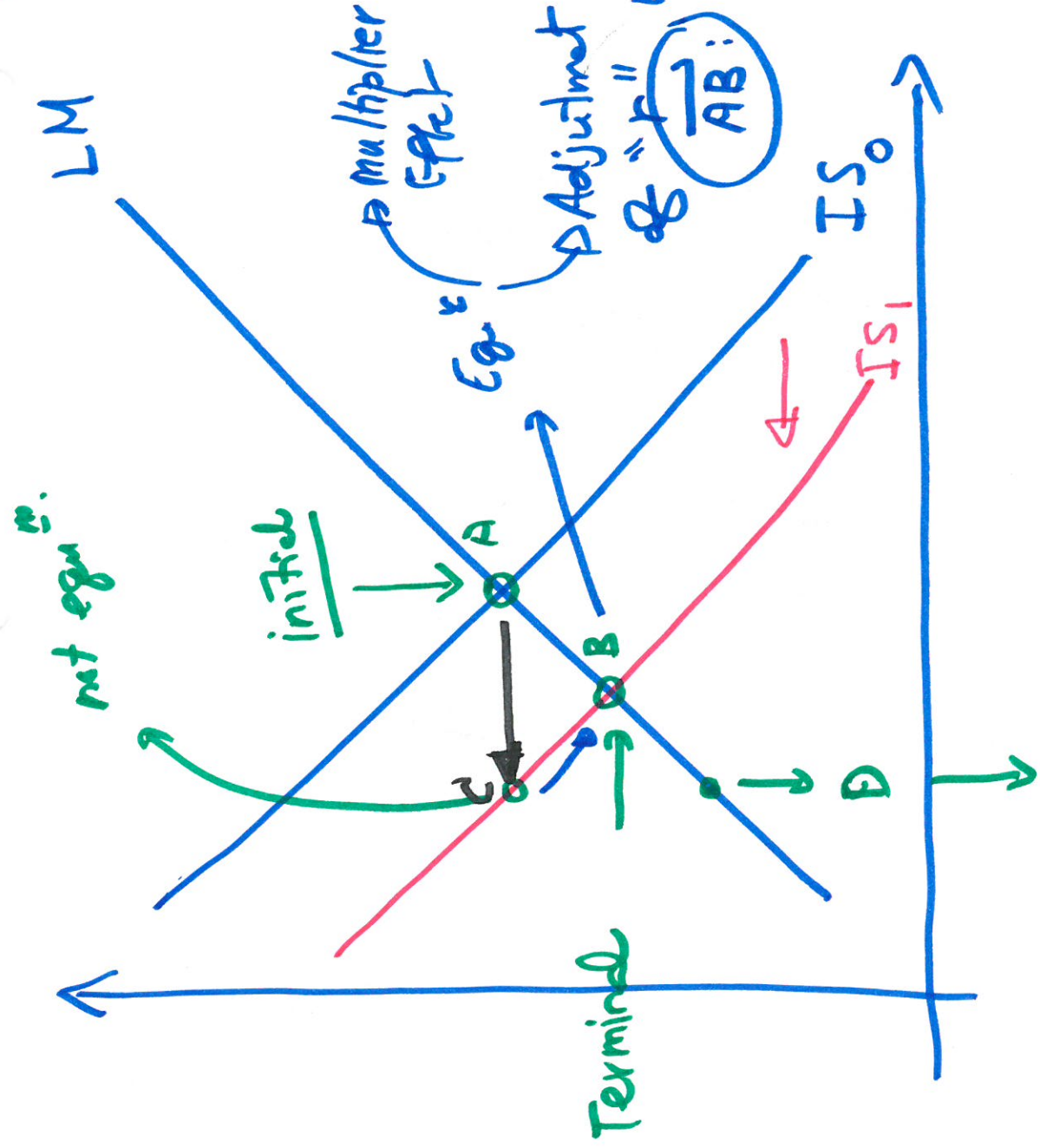


① Drop in Investment
(due to negative
shocks)

→ firms to reconsider
output.

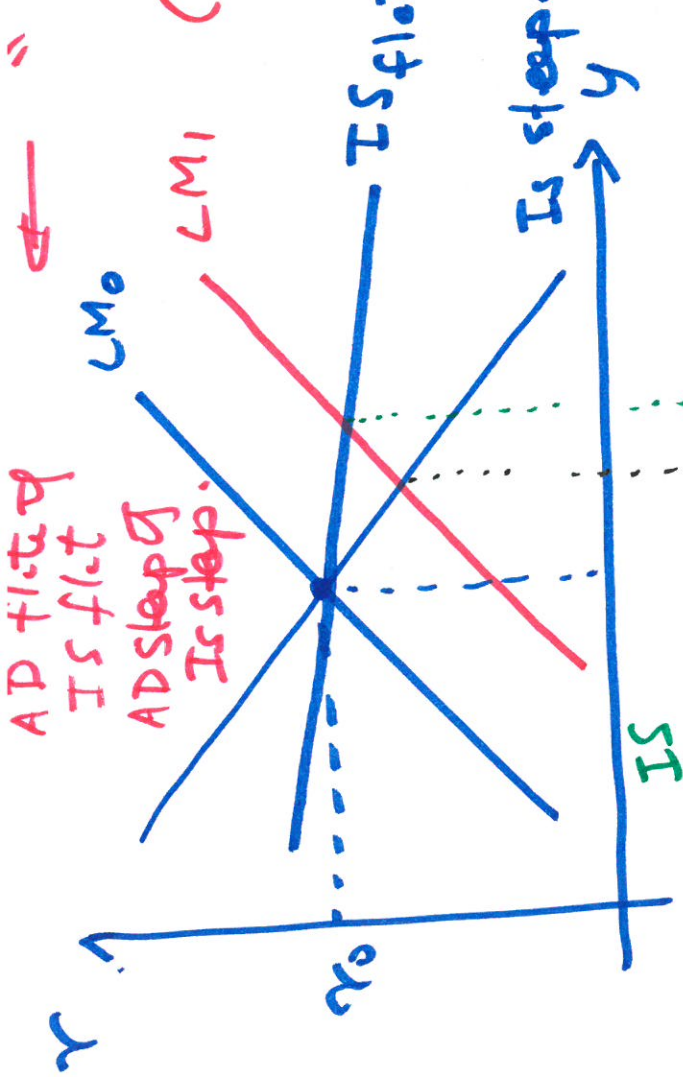
$IS_0 \rightarrow IS_1$
AC: multiplier effect.
Investment drops /
fixed interest rate.
"A → C": Keynesian
Cross diagram.



interest rate will be
falling. counteract
Partially offset
by a lower "r"

Level required to clear
Financial market.

What determine the slope of AD



IS curve flat

→ MP is very effective

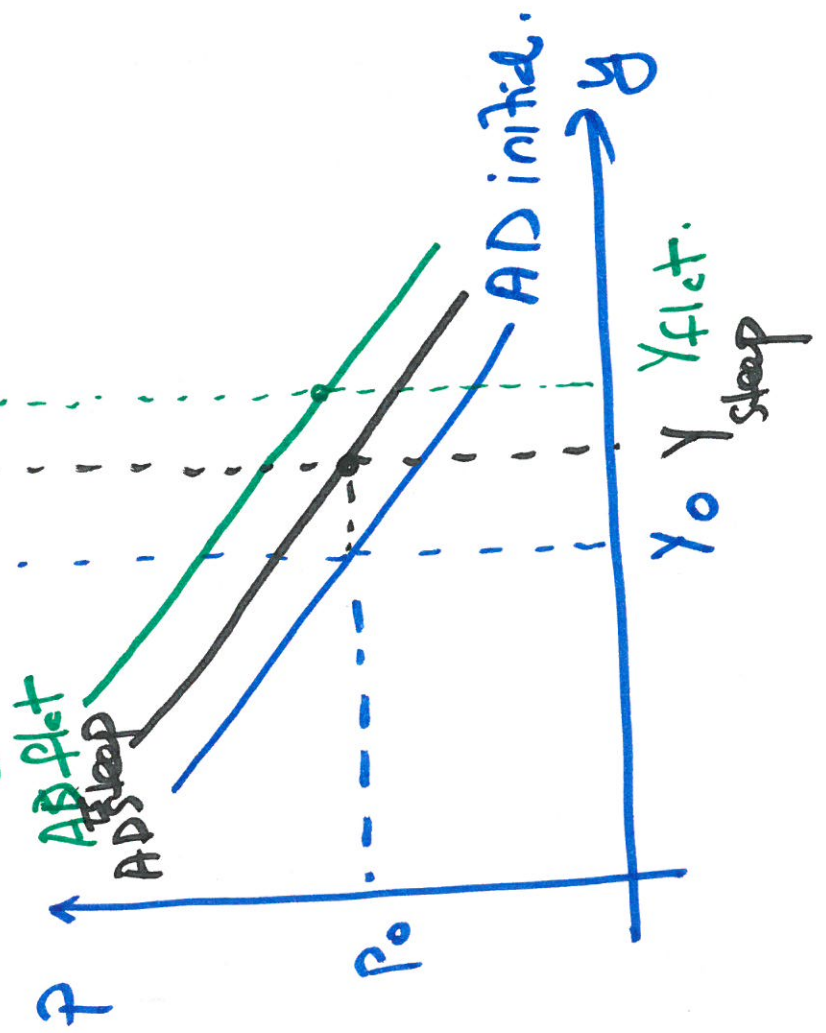
→ AD → shift more

→ size of horizontal

shift refers to

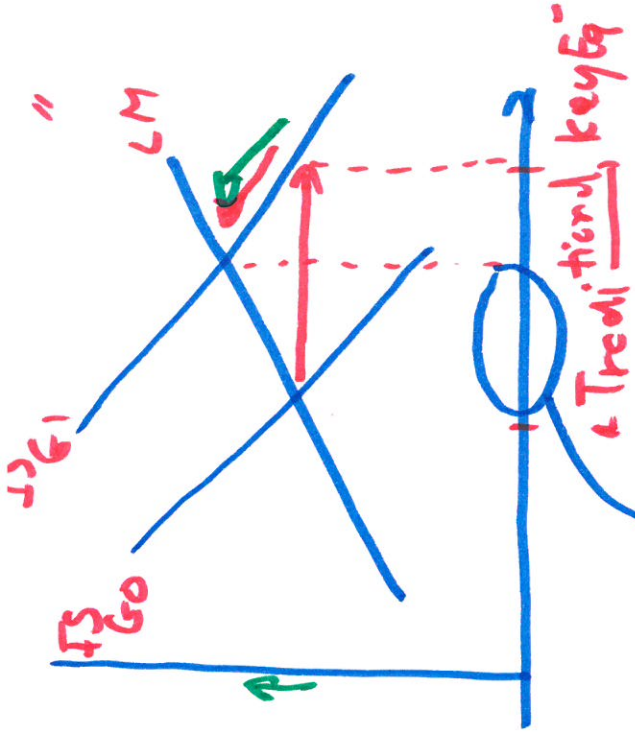
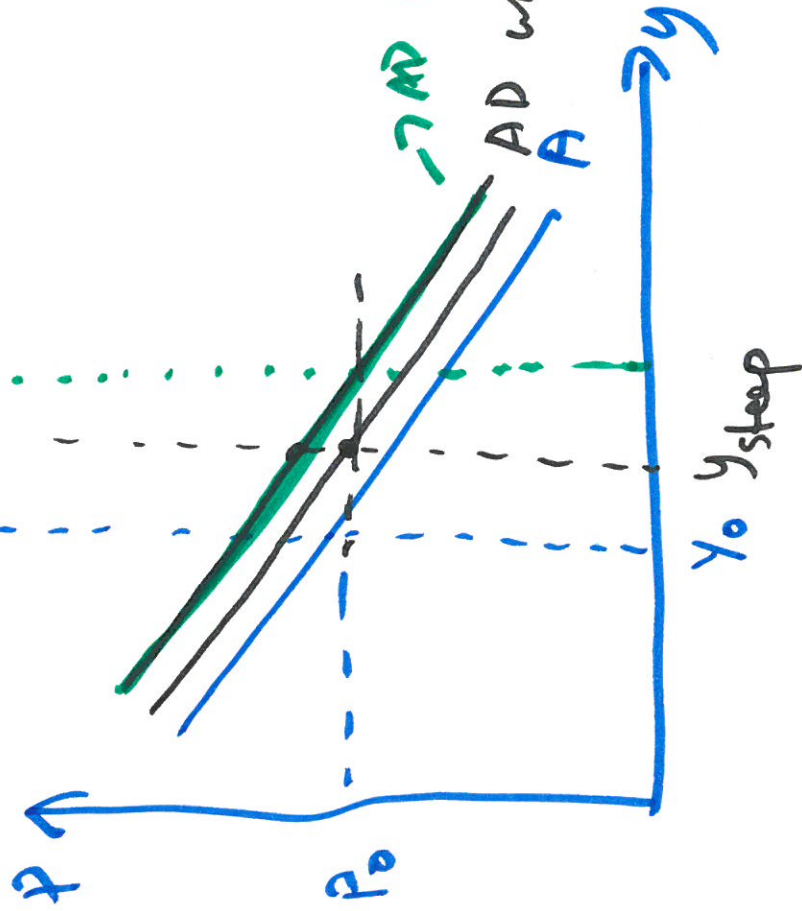
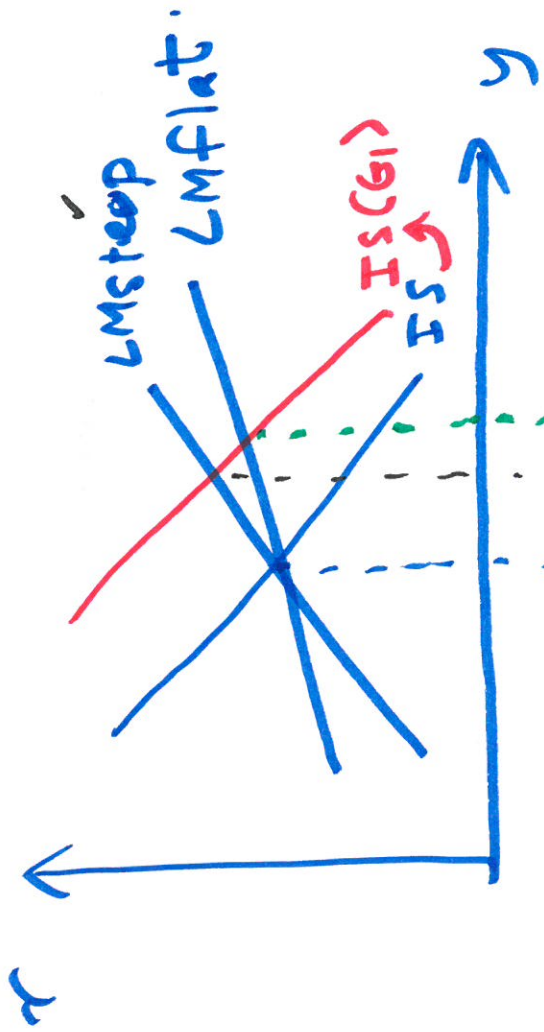
the effectiveness of

monetary policy



AD flat if IS flat
AD steep if IS steep

y_0 y_{flat}
 y_{steep}



Total net
Effect of
G↑

"Crowding
out effect"

↓ Private
iP → AE↓

"Traditional key"

Crowding out steep LM
is more than Crowding out
flat LM.