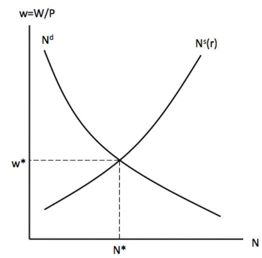
EE312 Macroeconomics, 1/2014 (Sec. 046402)
Chapter 9. Business Cycle Models with Flexible Prices and Wages: A Short Note

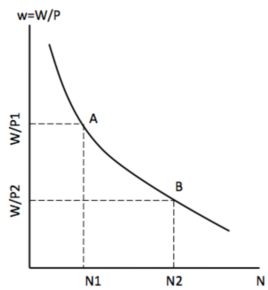
1 Sticky Wage Model

1.1 Output Supply Curve

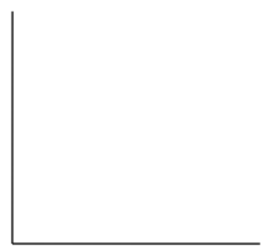


- $w* = \dfrac{W^*}{P^*}$
- If W is fixed at W_1 ($W_1 > W^*$) $\Rightarrow w_1 = \dfrac{W_1}{P^*} .... \dfrac{W^*}{P^*}$, $N_1 .... N^*$
- If W is fixed at W_2 ($W_2 > W^*$) $\Rightarrow w_2 = \dfrac{W_2}{P^*} .... \dfrac{W^*}{P^*}$, $N_2 .... N^*$

Labour Market



Production Function



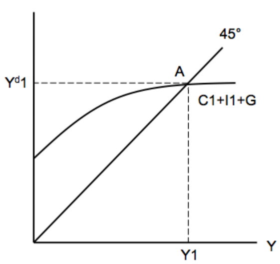
Output Supply Curve

- Output is not related to the real interest rate. / Higher $W \Rightarrow AS$ shift to the ..../ Lower $z \Rightarrow AS$ shift to the ....

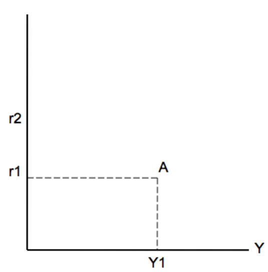
1.2 Output Demand Curve

1.2.1 IS curve

Income-Expenditure Identity



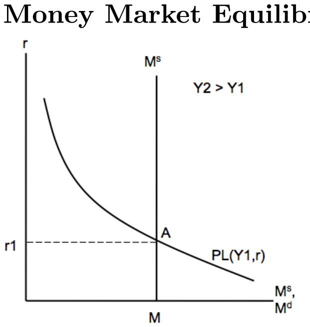
IS Curve



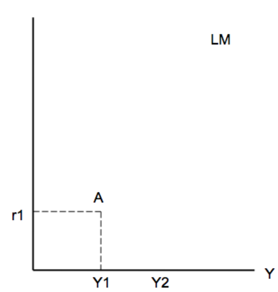
- IS curve shifts to the **right**
  G....... PV of taxes (T) ......
  an anticipated ...... in future income.
  current and future C ....
  current capital stock K ......
  future TFP (z') ......
  (MP'_K .... I^d ....)

1.2.2 LM curve

Money Market Equilibrium



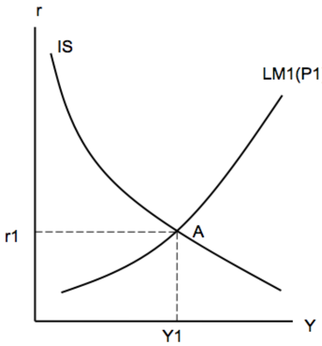
LM Curve



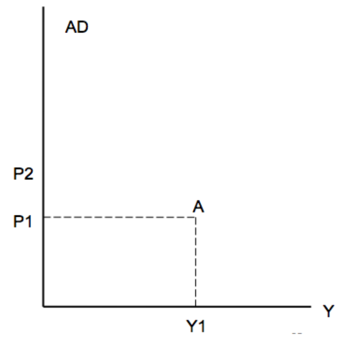
- LM curve shifts to the **right**
  M^s....
  P....
  M^d....

1.2.3 AD curve

Simultaneous Equilibrium



AD Curve

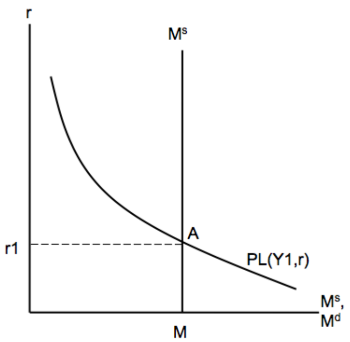


- If the IS curve shifts right, the AD shifts right.
  G.... , PV of taxes (T) ....
  current capital stock K ....
  future TFP (z') ....
- If the LM curve shifts right, the AD shifts right.
  M^s.... , P.... , M^d....

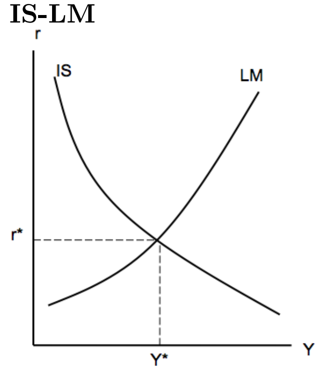
1.3 IS-LM, AD-AS, Labour Market

2 Non-Neutrality of Money

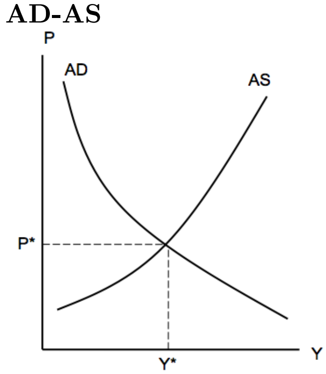
Money Market

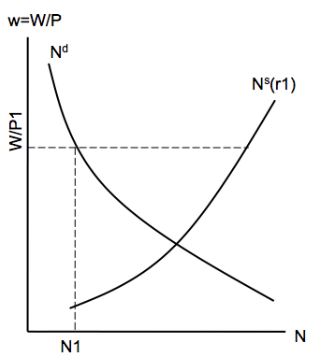


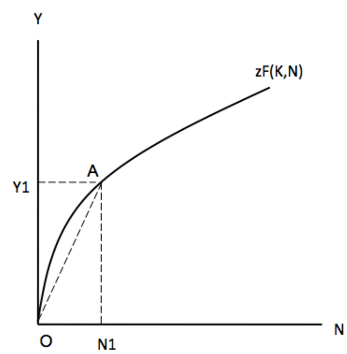
IS-LM



AD-AS

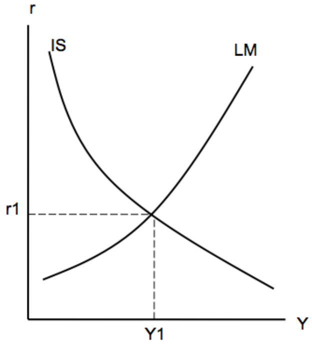




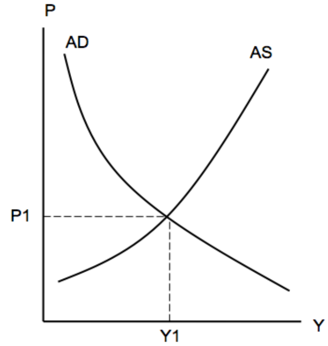


3 AD shocks as a cause of cycle

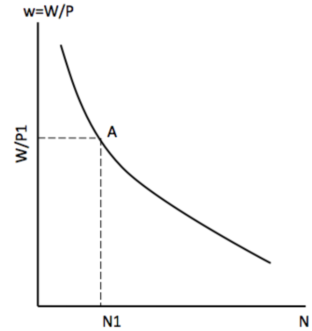
IS-LM : $I\uparrow$



AD-AS



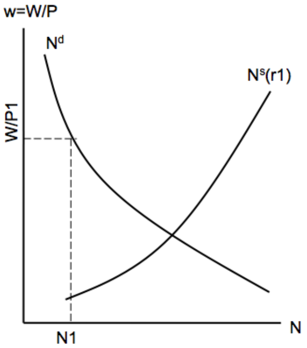
Labour Market



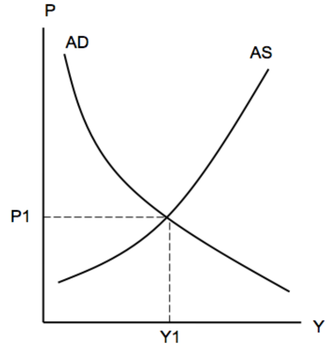
4 Keynesian short run and long run

4.1 Long-run market adjustment

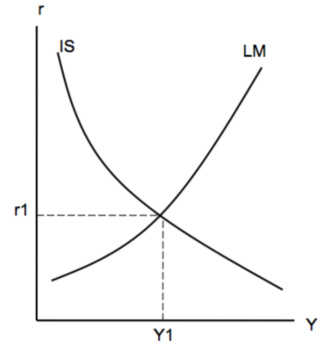
Labour Market



AD-AS: good market adjustment



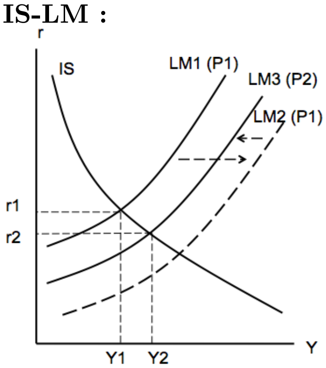
IS-LM



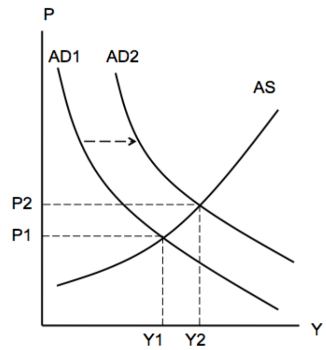
4.2 Keynesian Stabilization Policy : counter cyclical policy

4.2.1 Easy-money policy

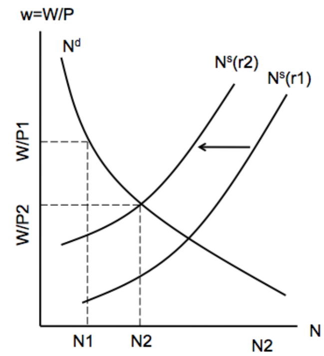
IS-LM :



AD-AS

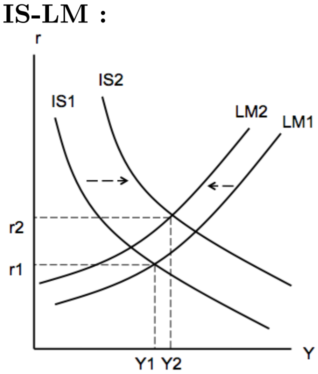


Labour Market

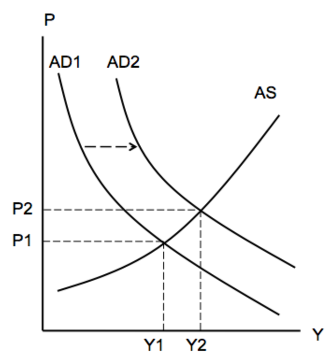


4.2.2 Expansionary fiscal policy

IS-LM :



AD-AS



Labour Market