GROUP 11 :-)

Use the *IS-LM* model to analyze the effects of

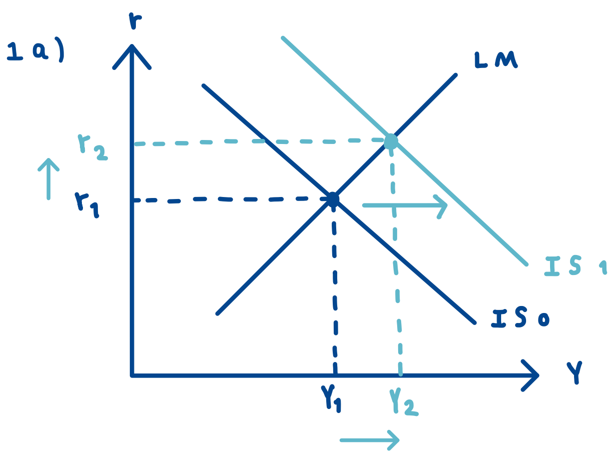
1. a boom in the stock market that makes consumers wealthier. (odd-numbered group)

For each shock,

a. use the *IS-LM* diagram to show the effects of the shock on ***Y*** and ***r***. Explain the mechanism.

b. determine what happens to ***C***, ***I***, and the unemployment rate.

1 a)



When the stock market boom, its makes consumer become wealthier and drives the increase of thier income. Consumers feel they can afford to spend more which it means that the AD will increase and national income (Y) will eventually increase So, the IS curve shift to the right and then interest rate (r) will increase to take money out of the economy for reduce inflation.

1b) With this situation, consumption (C) will increase because the stock market boom and the increase in their income Investment (I) will decrease because interest rate (r) is higher. As national income (Y) increase then unemployment rate will decrease because firms will hire more workers to produce the addition output that is demanded.

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