**Aggregate Demand**

Determine the effect on aggregate demand of each of the following events. Explain whether it represents a change in quantity demanded represented by a movement along the curve (up or down) or a change in demand represented by a shift of the curve (left or right). (Remember, explain means how and why.) Then, in a correctly labeled graph, show how each of the following will affect the AD curve.

1. Business owners are less optimistic about the health of the economy.
2. The government decreases welfare and veteran’s benefits.
3. The Federal Reserve increases interest rates.
4. A rising price level decreases the value of money held for purchases.
5. The government lowers personal income taxes.
6. Consumers expect the job market to be much stronger in the next few months.
7. The stock market has reached new records high levels of value.
8. The stock of physical capital has been falling for nearly a year.

# Aggregate Demand Answer Key

## Determine the effect on aggregate demand of each of the following events. Explain whether it represents a change in quantity demanded represented by a movement along the curve (up or down) or a change in demand represented by a shift of the curve (left or right). (Remember, explain means how and why.) Then, in a correctly labeled graph, show how each of the following will affect the AD curve.

* 1. Business owners are less optimistic about the health of the economy. *AD shifts left; investment spending decreases*



PL



AD

AD2



RGDP

* 1. The government decreases welfare and veteran’s benefits. *AD shifts left; decrease in disposable income and therefore consumer spending*



PL



AD

AD2



RGDP

* 1. The Federal Reserve increases interest rates. *AD shifts left; decrease in investment and interest sensitive consumer spending*



PL



AD

AD2



PL



RGDP

* 1. A rising price level decreases the value of money held for purchases. *There is a movement down the AD curve as consumer purchasing power erodes*



AD



RGDP

* 1. The government lowers personal income taxes. *AD shifts right. Lower taxes implies higher disposable income so consumer spending rises and AD shifts right*



PL



AD2

AD



RGDP

* 1. Consumers expect the job market to be much stronger in the next few months. *AD shifts right; expectations about future employment increase investment and consumer spending*



AD2

AD



PL



RGDP

* 1. The stock market has reached new records high levels of value. *AD shifts right; consumer wealth increases causing more consumer spending*



PL



AD2

AD



RGDP

* 1. The stock of physical capital has been falling for nearly a year. *AD shifts right; investment will increase to replace the failing stock of capital.*



PL



AD

AD2

RGDP