

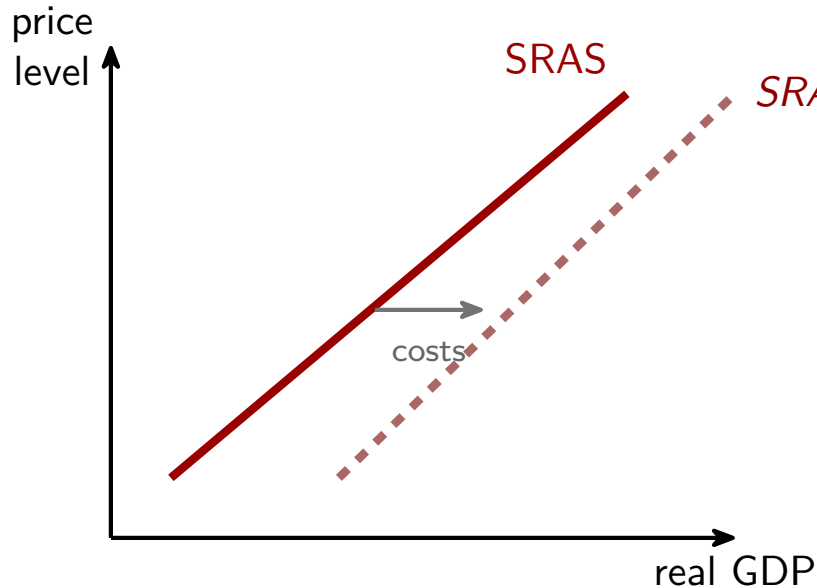
Exercise walk-through

3.4

Long-Run Aggregate Supply (LRAS)

AP Macroeconomics

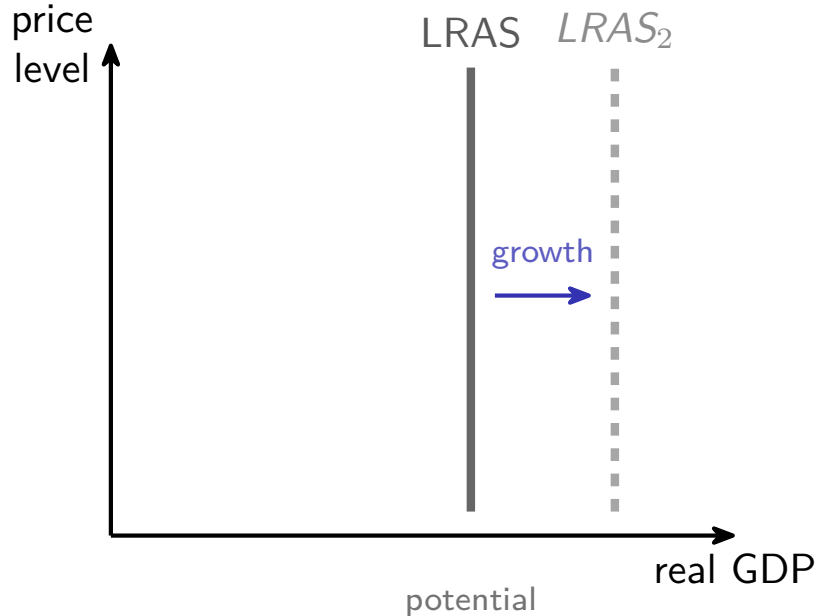
Short-run aggregate supply



In the short run some costs are **sticky** above all **nominal wages**. A higher price level with fixed wages $\Rightarrow$ more profit per unit $\Rightarrow$ more output. So SRAS slopes **up**. Shifters: input prices, **productivity**, **supply shocks**.

- higher costs $\Rightarrow$ shift **left**
- better productivity $\Rightarrow$ shift **right**

Long-run aggregate supply



In the long run wages and prices are **fully flexible**, so output settles at **potential GDP** – the **full-employment output**. LRAS is **vertical**: the same real output at any price level.

More resources, capital, or better technology shift LRAS **right** – that is **economic growth**.

Potential output, and the curve that shows it

Full-employment output

Full-employment (potential) output is what the economy produces when unemployment sits at its natural rate.

LRAS

Vertical at that output: in the long run the price level does not change what the economy can produce.

The PPC

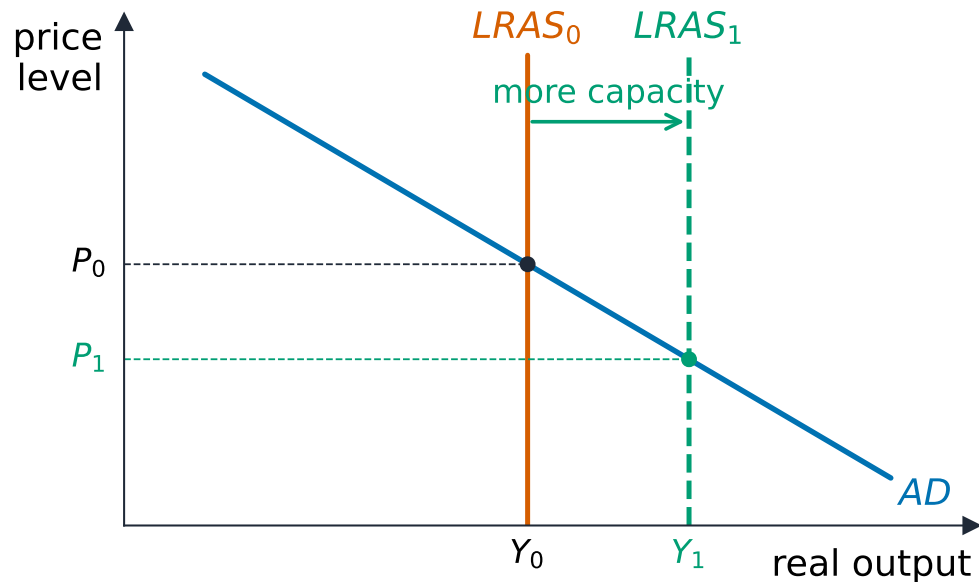
The **production possibilities curve (PPC)** shows the same limit in goods-against-goods form – and both shift out for the same reasons.

What shifts it

More or better resources, more capital, better technology, higher productivity.

An AD shift moves output only until wages adjust. Only an LRAS shift raises output permanently.

Supply-side policy shifts long-run aggregate supply



Supply-side policy shifts long-run aggregate supply right: more output, lower prices

Exercises 2.1-2.3

2.1 State the shape of the LRAS curve.

[1]

2.2 State what determines the position of the LRAS curve.

[1]

2.3 State the effect of economic growth on LRAS.

[1]

Exercises 2.1-2.3

2.1 State the shape of the LRAS curve.

[1]

2.1

- vertical (at potential output)

2.2 State what determines the position of the LRAS curve.

[1]

2.2

- the quantity and quality of resources, the capital stock, and technology

2.3 State the effect of economic growth on LRAS.

[1]

2.3

- it shifts LRAS to the right

Exercises 3.1-3.2

3.1 The LRAS curve is

[1]

☐

A upward-sloping

B downward-sloping

C vertical

D horizontal

3.2 LRAS is vertical because, in the long run, wages and prices are

[1]

☐

A sticky

B fully flexible

C fixed by law

D zero

Exercises 3.1-3.2

3.1 The LRAS curve is

[1]

☐

- A upward-sloping
- B downward-sloping
- C vertical
- D horizontal

3.1 C

- vertical.

3.2 LRAS is vertical because, in the long run, wages and prices are

[1]

☐

- A sticky
- B fully flexible
- C fixed by law
- D zero

3.2 B

- fully flexible.

Exercise 3.3 (a)

3.3 A country's capital stock and technology both improve.

(a) State the effect on LRAS.

[1]

Exercise 3.3 (a)

3.3 A country's capital stock and technology both improve.

(a) State the effect on LRAS.

[1]

(a)

- LRAS increases

Exercise 3.3 (b)

3.3 A country's capital stock and technology both improve.

(b) State the direction LRAS shifts.

[1]

Exercise 3.3 (b)

3.3 A country's capital stock and technology both improve.

(b) State the direction LRAS shifts.

[1]

(b)

- to the right

Exercise 3.3 (c)

3.3 A country's capital stock and technology both improve.

(c) Name this process.

[1]

Exercise 3.3 (c)

3.3 A country's capital stock and technology both improve.

(c) Name this process.

[1]

(c)

- (long-run) economic growth