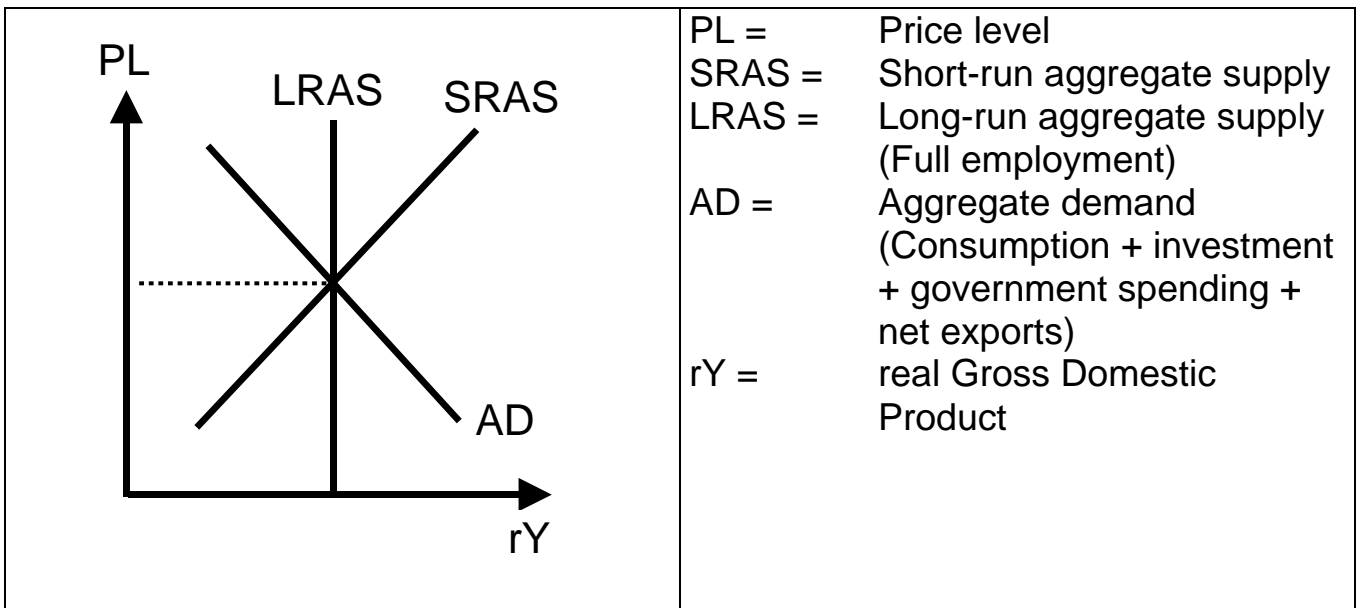
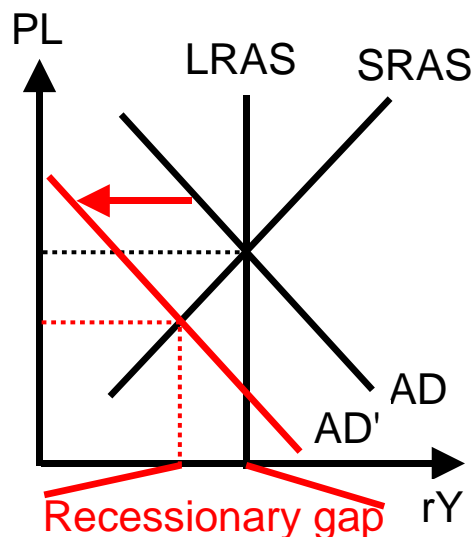


## Classical view versus Keynesian view 2: An example

Initial situation:



Now a recessionary shock occurs (for example by a decrease in AD):

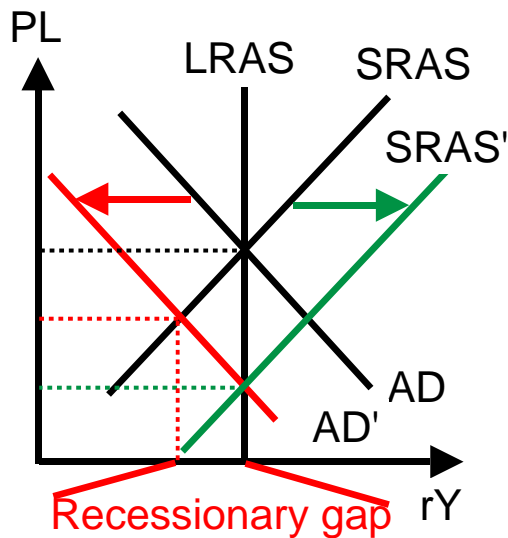


How can one get rid of the recessionary gap in order to achieve LRAS (full employment)? Answer on the next page.

## How to get rid of the recessionary gap?

### Answer by **classical** economists

- In this case, prices and wages fall.
- Therefore, costs for producers are reduced and these hire more workers to supply more goods.
- The SRAS-curve shifts to the right until full employment is achieved.



### Answer by **Keynesian** economists

- Prices and wages are sticky.
- Doing nothing, the recessionary gap could exist for a very long time.
- Therefore, an expansionary fiscal or monetary policy is necessary to get rid of the recessionary gap by increasing AD.

