FIGURE 7.1 The Aggregate Demand (AD) Curve
FIGURE 7.2 Output Declines When AD Shifts Inward
Figure 7.3 A Price Shock

After the price shock, output is lower.

The initial point.
FIGURE 7.4 The Consumption Function

Consumption function

\[ C = a + bY_d \]

Slope = \( b = \frac{\Delta C}{\Delta Y_d} \)
The 45-degree line shows where spending and income are equal.

Spending line = \( a + b(1 - t)Y + I + G + X \)

At this level of income, spending would fall short of the amount of income.

At this level of income, spending would exceed the amount of income.

**FIGURE 7.5 Spending Balance**
### Table 7.1 Example of the Multiplier Process (Billions of Dollars)

<table>
<thead>
<tr>
<th>Round</th>
<th>Reduction This Round</th>
<th>Sum to Date</th>
<th>Calculation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>10.000</td>
<td>10.000</td>
<td>Exogenous drop in investment</td>
</tr>
<tr>
<td>2</td>
<td>6.300</td>
<td>16.300</td>
<td>$b(1 - t)(10) = (0.6300)(10)$</td>
</tr>
<tr>
<td>3</td>
<td>3.969</td>
<td>20.269</td>
<td>$[b(1 - t)]^2(10) = (0.3969)(10)$</td>
</tr>
<tr>
<td>4</td>
<td>2.500</td>
<td>22.769</td>
<td>$[b(1 - t)]^3(10) = (0.2500)(10)$</td>
</tr>
<tr>
<td>5</td>
<td>1.575</td>
<td>24.344</td>
<td>$[b(1 - t)]^4(10) = (0.1575)(10)$</td>
</tr>
<tr>
<td>6</td>
<td>0.992</td>
<td>25.336</td>
<td>$[b(1 - t)]^5(10) = (0.0992)(10)$</td>
</tr>
</tbody>
</table>
FIGURE 7.6 The Multiplier

1. Spending line shifts down by $\Delta I$

2. Income is reduced by
   \[
   \frac{1}{1 - b(1 - t)} \Delta I
   \]
FIGURE 7.7 The Government Spending Multiplier

1. Spending line shifts up by $\Delta G$

2. Income is increased by $\frac{1}{1 - b (1 - t)} \Delta G$

Old level of income  New level of income

INCOME ($Y$) OR GDP