

Giuliano Manzi

*1. What kind of economic recession might respond best to a Keynesian perspective?*

Keynesian economics is a macroeconomic economic theory of total spending in the economy and its effects on output, employment, and inflation. Keynesian economics was developed by the British economist John Maynard Keynes during the 1930s to understand the Great Depression. Keynesian economics is considered a "demand-side" theory that focuses on changes in the economy over the short run. Keynes theory was the first to sharply separate the study of economic behavior and markets based on individual incentives from the study of broad national economic aggregate variables and constructs.

Based on his theory, Keynes advocated for increased government expenditures and lower taxes to stimulate demand and pull the global economy out of the depression. Subsequently, Keynesian economics was used to refer to the concept that optimal economic performance could be achieved—and economic slumps prevented by influencing aggregate demand through activist stabilization and economic intervention policies by the government.

Keynesians believe that the solution to a recession is expansionary fiscal policy, such as tax cuts to stimulate consumption and investment, or direct increases in government spending, either of which would shift the aggregate demand curve to the right.

*2. Keynesian policy is about shifting the AD curve, not the AS curve. What are some ways to shift AD?*

Changes in foreign income, changes in expectations, changes in exchange rates, changes in the distribution of income, and changes in fiscal and monetary policies.

It might be that consumer time preferences change, and future consumption is valued more highly than present consumption. Contractionary fiscal policy can also shift aggregate demand to the left. The government might decide to raise taxes or decrease spending to fix a budget deficit.

The aggregate demand curve, or AD curve, shifts to the right as the components of aggregate demand—consumption spending, investment spending, government spending, and spending on exports minus imports—rise. The AD curve will shift back to the left as these components fall.

*3. What kind of economic recession might respond best to Neo-classical perspective?*

Neoclassical economics is a broad theory that focuses on supply and demand as the driving forces behind the production, pricing, and consumption of goods and services. It emerged in around 1900 to compete with the earlier theories of classical economics.

Neoclassical economics theories underlie modern-day economics, along with the tenets of Keynesian economics. Although the neoclassical approach is the most widely taught theory of economics, it has its detractors.

Neoclassical economists believe that the economy will rebound out of a recession or eventually contract during an expansion because prices and wage rates are flexible and will adjust either upward or downward to restore the economy to its potential GDP.

#### **4. Neo-classical policy is about shifting the AS curve. What are some ways to shift AS?**

The aggregate supply curve shifts to the right as productivity increases or the price of key inputs falls, making a combination of lower inflation, higher output, and lower unemployment possible.

Along with energy prices, two other key inputs that may shift the SRAS curve are the cost of labor, or wages, and the cost of imported goods that are used as inputs for other products. Any event that results in a change of production costs shifts the short-run supply curve outwards or inwards if the production costs are decreased or increased. Factors that impact and shift the short-run curve are taxes and subsidies, wages, and the price of raw materials.