- In the short run, equilibrium levels of GDP can occur at less than, greater than, or equal to the full-employment level of GDP. The long-run equilibrium can occur only at full employment.
- Fiscal policy consists of government actions to increase or decrease aggregate demand. These actions involve changes in government expenditures and taxation.
- Macroeconomic policy includes both fiscal and monetary policy. Both monetary and fiscal policies are primarily aggregate demand policies. Other economic policies are used to affect aggregate supply.
- The government uses a contractionary fiscal policy to decrease aggregate demand when there are inflationary pressures in the economy. The government may increase taxes, decrease spending, or do a combination of the two.
- The government uses an expansionary fiscal policy to increase aggregate demand during a recession. The government may decrease taxes, increase spending, or do a combination of the two.
- Discretionary fiscal policy means the federal government must take deliberate action or pass a new law changing taxes or spending. The automatic or built-in stabilizers change government spending or taxes without new laws being passed or deliberate action being taken.
- Fiscal policy that changes taxes or government spending will affect the government's budget. When the government spends more than it taxes in a year, it creates a budget deficit. When the government taxes more than it spends in a year, it creates a budget surplus. The summation of the budget deficits and surpluses over time is the national debt. Deficits and debt have an effect on the macroeconomy.
- Crowding out is the effect on investment and consumption spending of an increase in interest rates caused by increased borrowing by the federal government. The higher interest rates crowd out business and consumer borrowing.
- A Phillips curve illustrates the trade-off between inflation and unemployment. The trade-off differs in the short and long run, varies at different times, and is often different for increases and decreases in output.
- The short-run Phillips curve shows a trade-off between the inflation rate and the unemployment rate. There is no trade-off between inflation and unemployment in the long run. The long-run Phillips curve is vertical.