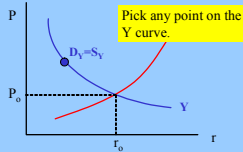
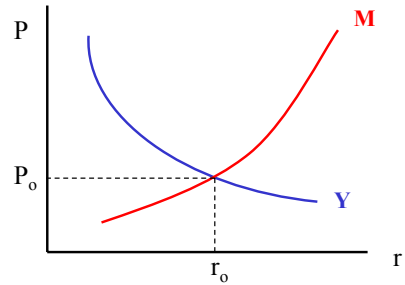


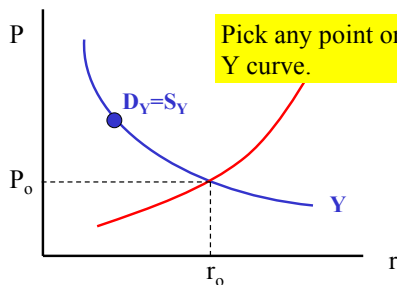
## A Tax Cut



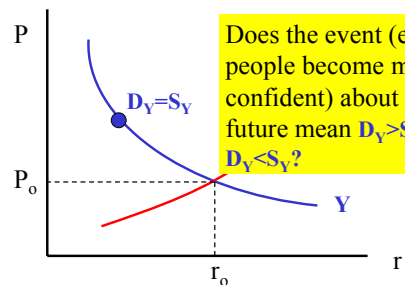
## The Y and M Curves



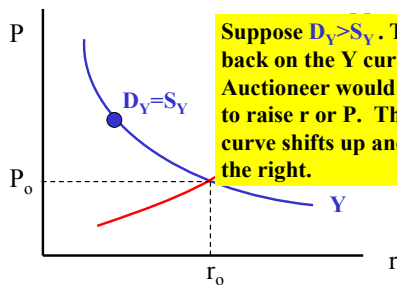
## The Y Curve



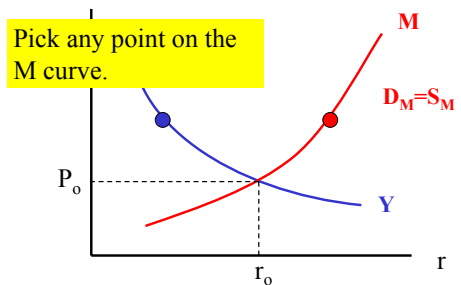
## The Y Curve



## The Y Curve

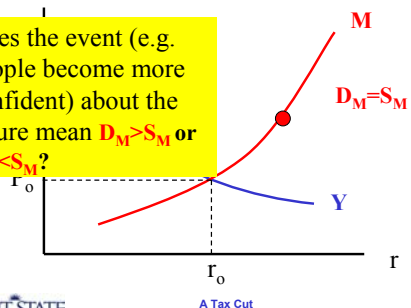


## The M Curve



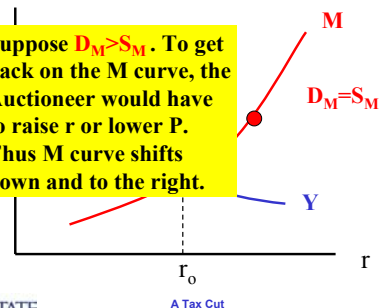
## The M Curve

Does the event (e.g. people become more confident) about the future mean  $D_M > S_M$  or  $D_M < S_M$ ?



## The M Curve

Suppose  $D_M > S_M$ . To get back on the M curve, the Auctioneer would have to raise  $r$  or lower  $P$ . Thus M curve shifts down and to the right.

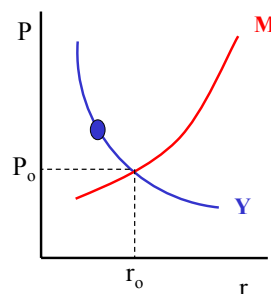


## Some Problems

- The government gives everyone a \$300 tax rebate this year, adding to the national debt.

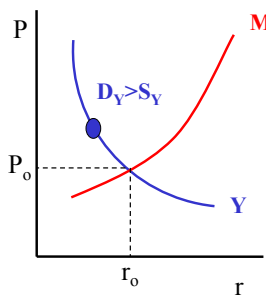
## The Tax Cut

- Pick a point on the Y curve.



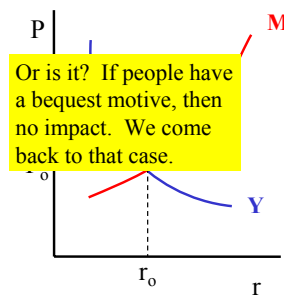
## The Tax Cut

- Pick a point on the Y curve.
- $D_Y > S_Y$ 
  - Wealth up by a fraction of the tax cut; consumption up as well



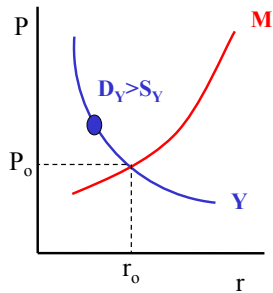
## The Tax Cut

- Pick a point on the Y curve.
- $D_Y > S_Y$ 
  - Wealth up by a fraction of the tax cut; consumption up as well



## The Tax Cut

- Pick a point on the Y curve.
- $D_Y > S_Y$
- The Auctioneer must lower  $D_Y$

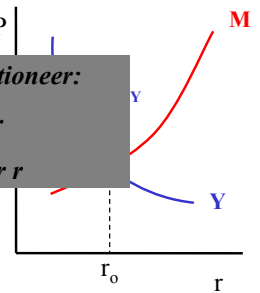


A Tax Cut

## The Tax Cut

- Pick a point on the Y curve.
- $D_Y > S_Y$
- The Auctioneer must lower  $D_Y$

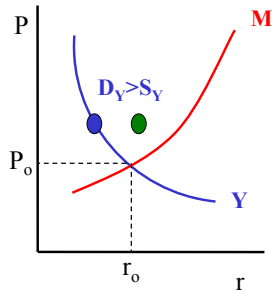
*Memo to the auctioneer:*  
**To cut  $D_Y$ , raise  $r$**   
**To raise  $D_Y$ , lower  $r$**



A Tax Cut

## The Tax Cut

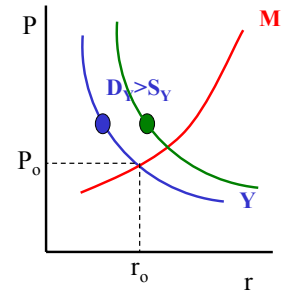
- Pick a point on the Y curve.
- $D_Y > S_Y$
- The Auctioneer must lower  $D_Y$



A Tax Cut

## The Tax Cut

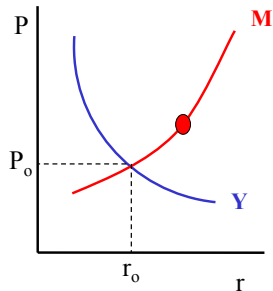
- Pick a point on the Y curve.
- $D_Y > S_Y$
- The Auctioneer must lower  $D_Y$
- The Y curve shifts up and to the right



A Tax Cut

## The Tax Cut

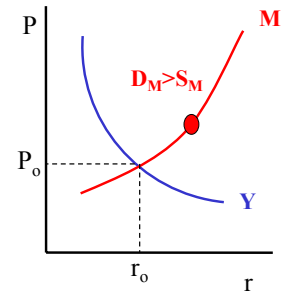
- Pick a point on the M curve.



A Tax Cut

## The Tax Cut

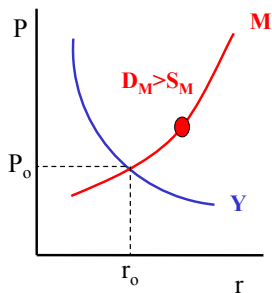
- Pick a point on the M curve.
- $D_M > S_M$



A Tax Cut

## The Tax Cut

- Pick a point on the M curve.
- $D_M > S_M$ 
  - Wealth Up
  - Consumption Up
  - Money Demand Up

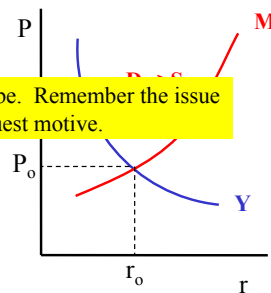


A Tax Cut

## The Tax Cut

- Pick a point on the M curve.
- $D_M > S_M$ 
  - Wealth Up
  - Consumption Up
  - Money Demand Up

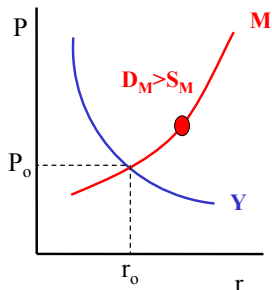
Well, maybe. Remember the issue of the bequest motive.



A Tax Cut

## The Tax Cut

- Pick a point on the M curve.
- $D_M > S_M$
- The Auctioneer must lower  $D_M$

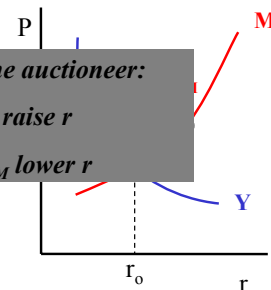


A Tax Cut

## The Tax Cut

- Pick a point on the M curve.
- $D_M > S_M$
- The Auctioneer must lower  $D_M$

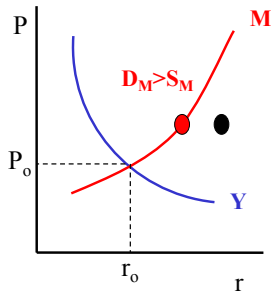
**Memo to the auctioneer:**  
 To cut  $D_M$ , raise  $r$   
 To raise  $D_M$ , lower  $r$



A Tax Cut

## The Tax Cut

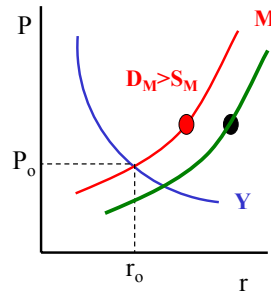
- Pick a point on the M curve.
- $D_M > S_M$
- The Auctioneer must lower  $D_M$



A Tax Cut

## The Tax Cut

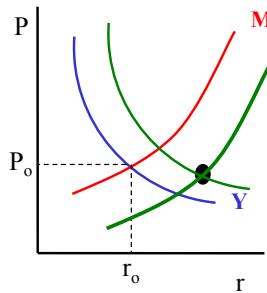
- Pick a point on the M curve.
- $D_M > S_M$
- The Auctioneer must lower  $D_M$
- The M curve shifts down and to the right.



A Tax Cut

## The Tax Cut

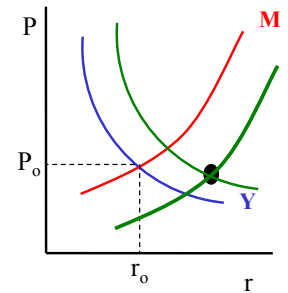
- The Y curve shifts up and to the right.
- The M curve shifts down and to the right.



A Tax Cut

## The Tax Cut

- The Y curve shifts up and to the right.
- The M curve shifts down and to the right.
- Price level uncertain
- Interest rate up.

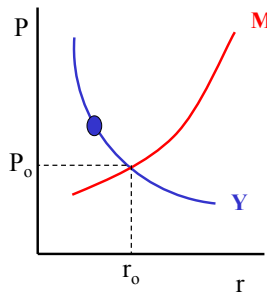


A Tax Cut

## The Tax Cut II

- Pick a point on the Y curve.

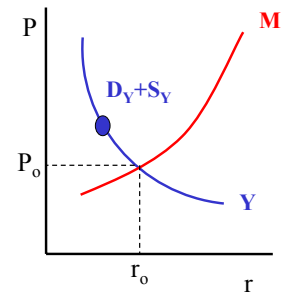
**Tax Cut II**  
assumes a  
bequest motive



A Tax Cut

## The Tax Cut II

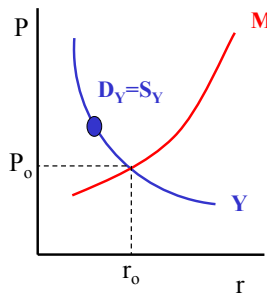
- Pick a point on the Y curve.
- $D_Y = S_Y$   
– No change in Z



A Tax Cut

## The Tax Cut II

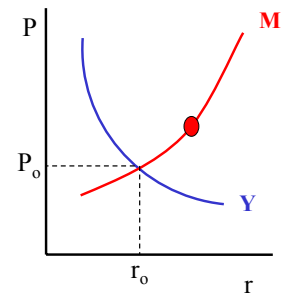
- Pick a point on the Y curve.
- $D_Y = S_Y$
- The Y curve is unchanged!



A Tax Cut

## The Tax Cut II

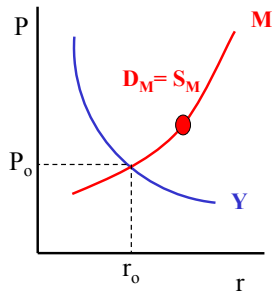
- Pick a point on the M curve.



A Tax Cut

## The Tax Cut II

- Pick a point on the M curve.
- $D_M = S_M$ 
  - No change in Z

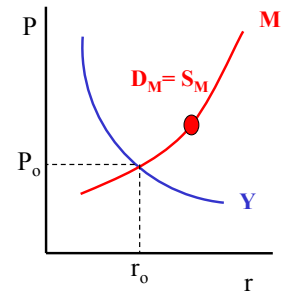


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## The Tax Cut II

- Pick a point on the M curve.
- $D_M = S_M$
- The M curve is unaffected!

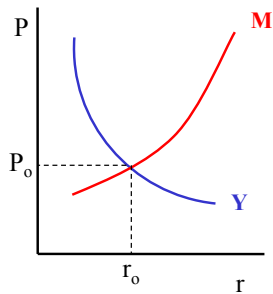


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## The Tax Cut II

- The Y curve doesn't change.
- The M curve doesn't change

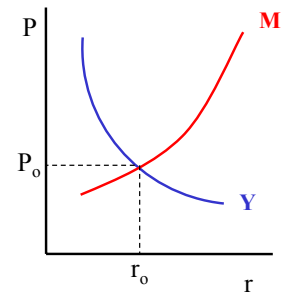


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## The Tax Cut II

- The Y curve doesn't change.
- The M curve doesn't change
- P and r are unaffected.
- The tax cut is a non-event.



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End

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