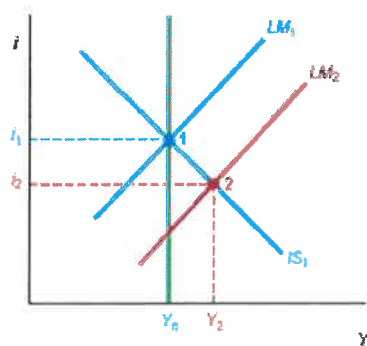


IS-LM Model in the Long Run

- To see what happens in the *ISLM* model in the long run, we make use of the concept of the **natural rate level of output** (denoted by Y_n), which is the rate of output at which the price level has no tendency to rise or fall.
- When output is above the natural rate level, the booming economy will cause prices to rise; when output is below the natural rate level, the slack in the economy will cause prices to fall.



- $M^s \uparrow$, LM shifts right
- in the long run the price level does change
 $P \uparrow$, $M^s/P \downarrow$, LM curve shifts left
- equilibrium is in the Point 1

- $G \uparrow$, IS shifts right
- in the long run the price level does change
 $P \uparrow$, $M^s/P \downarrow$, LM curve shifts left
- equilibrium is in the Point 2'

