

Edexcel (A) Economics A-level

Theme 2: The UK Economy, Performance and Policies

2.3 Aggregate Supply

2.3.1 The characteristics of Aggregate Supply (AS)

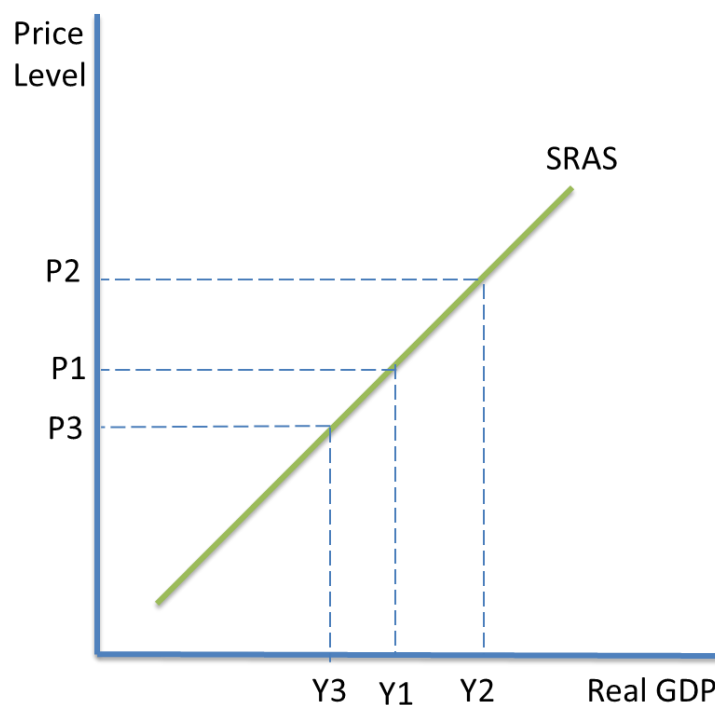
Notes



The AS curve:

- Aggregate supply shows the quantity of real GDP which is supplied at different price levels in the economy.
- The AS curve is upward sloping because at a higher price level, producers are willing to supply more because they can earn more profits.

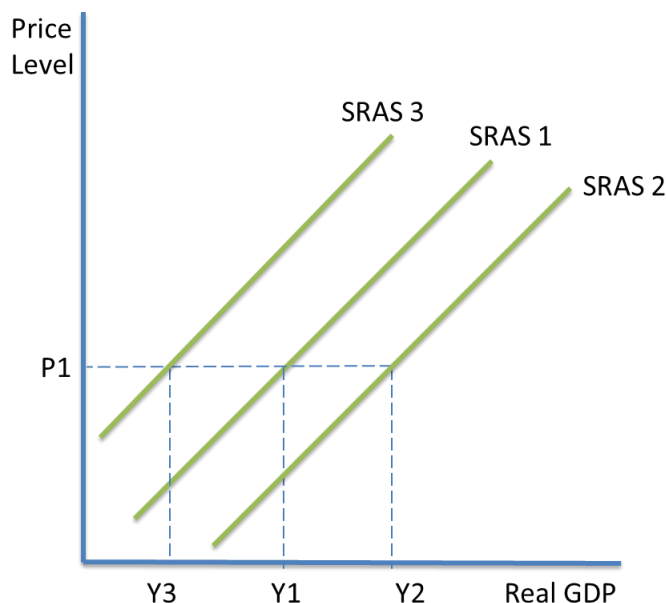
Moving along the AS curve:



- Only changes in the price level, which occur due to changes in AD, lead to movements along the AS curve.
- If AD increases, there is an **expansion** in the SRAS, from Y1 to Y2. If AD falls, there is a **contraction** in SRAS, from Y1 to Y3.



Shifting the AS curve:

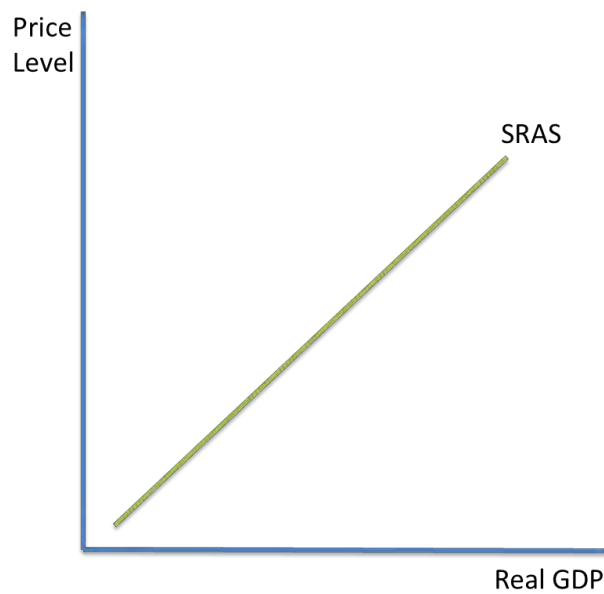


- The SRAS curve shifts when there are changes in the conditions of supply.
 - The cost of employment might change, e.g. wages, taxes, labour productivity
 - The cost of other inputs e.g. raw materials, commodity prices, the exchange rate if products are imported
 - Government regulation or intervention, such as environmental laws and taxes, and business regulation. Business regulation is sometimes called 'red tape'.

The relationship between short run AS and long run AS:

- The short run aggregate supply curve (SRAS) only covers the period immediately after a change in the price level. It shows the planned output of an economy when prices change, whilst the cost of production and productivity of the factor inputs are kept constant. These could be wage rates or how technologically advanced capital is, for example.
- The curve is upward sloping because supply is assumed to be responsive to a change in AD, which is reflected in the price level.





- The long run aggregate supply curve (LRAS) shows the potential supply of an economy in the long run. This is when prices, and the costs and productivity of factor inputs, can change. Similarly to the PPF, it can show the economy's productive potential.
- The curve is vertical, because supply is assumed not to change as the price level changes.

