

Economics 314
Daily Question #20

Spring 2013
April 8

In a price-setting model with real and nominal rigidities, explain why it is possible for the following situation to exist:

- For changes in aggregate demand that are very small ($|\Delta m| < A_1$), a firm would not adjust prices regardless of whether other firms do or do not.
- For changes in aggregate demand that are moderate in size ($A_1 < |\Delta m| < A_2$), a firm would adjust prices if and only if other firms do.
- For changes in aggregate demand that are large ($|\Delta m| > A_2$), a firm would adjust prices regardless of what other firms do.