Economics of AI: Key

1. The "excited" believe that AI will compliment rather than substitute for human labor. If so, then advances in AI boost the demand for labor (labor demand shifts to the right. The AS curve shifts right increasing the output gap and lowering inflation.

The effect on unemployment is more complicated. By itself, higher labor demand lower unemployment. Because of lower inflation, however, real wages rise. Higher real wages cause firms to move up the new labor demand curve. This raises unemployment. The overall effect on unemployment is ambiguous.

2. The "alarmed" instead believe that AI will substitute for human labor. If so, then the labor demand curve will shift to the left.

When labor demand shifts to the left, so does AS. Here, however, the productivity benefits of AI also cause AS to shift to the right. Based on our model, we cannot say which way it moves. In class, I argued that it will surely shift to the right. If so, the output gap rises and inflation falls.

As inflation falls, real wages rise. Firms move up along the new labor demand curve. Unemployment therefore rises.

3. False. The rise in unemployment would be considered structural unemployment.

4. A bubble refers to cases where a stock price cannot be justified by a firm's current or future profits.

5. Lower aset prices reduce household wealth, causing them to reduce their consumption. This causes the AD curve to shift left, reducing the output gap and inflation.

As inflation falls, real wages rise. Firms move up along the new labor demand curve. Unemployment therefore rises.

6. 'It can't be bargained with. It can't be reasoned with. It doesn't feel pity, or remorse, or fear! And it absolutely will not stop, ever, until you are dead!"