
Business Cycles

- Useful to de-trend output and focus on deviations of output from trend
- We think of trend output as “potential output” or the “natural rate of output”
- We define the **output gap** as percentage deviations of output from potential output

$$\tilde{Y}_t = \frac{Y_t - \bar{Y}_t}{\bar{Y}_t} \approx \log \left(\frac{Y_t}{\bar{Y}_t} \right)$$