

DUE DATE: \_\_\_\_\_

NAME: \_\_\_\_\_

**UNIT 11: ECONOMIC HEALTH INDICATORS: INFLATION & UNEMPLOYMENT WORKSHEET**

*USE THE LECTURE NOTES TO ANSWER THE FOLLOWING QUESTIONS (10 pts each)*

1. What does the word “**Aggregate**” mean?

2. What is stagflation?

3. If aggregate supply exceeds aggregate demand what will happen to the CPI (average price level of products)? *(circle one)*

**INCREASE**

**DECREASE**

4. What kind of inflation would it be if producers begin to experience an increase in the cost to manufacture their products?

5. John Keynes believed in what kind of economics: Demand or Supply-side? *(circle one)*

**DEMAND-SIDE**

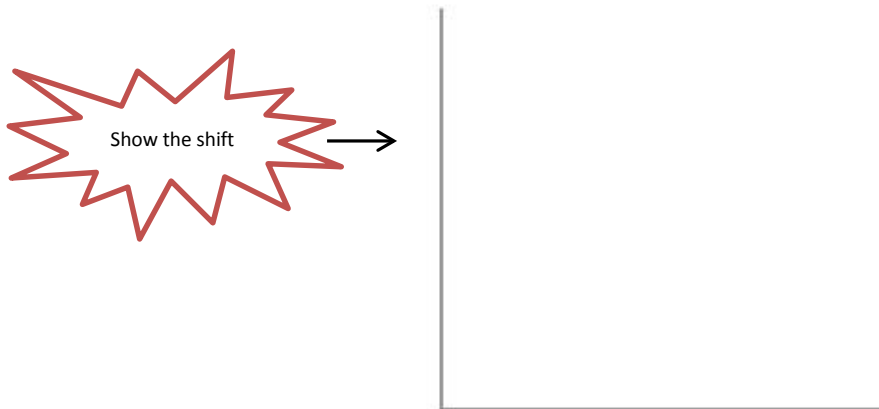
**SUPPLY-SIDE**

6. What would happen to GDP if aggregate demand were to decrease or if aggregate supply were to decrease? *(circle one)*

**INCREASE**

**DECREASE**

7. Using the following chart, construct an **aggregate demand** and **aggregate supply** curve and **illustrate** what happens to the **CPI** and **GDP** if **aggregate demand increases**. *Label both axis and show the shift in aggregate demand.*



8. What government agency is responsible for calculating the employment rate?

9. List **THREE** people who are **NOT** counted in the unemployment rate?

1.

2.

3.

10. What is the problem with measuring unemployment?

11. What type of unemployment would indicate that an economy is in the growth or peak of its business cycle? (*circle one*)

**FRICTIONAL      STRUCTURAL      SEASONAL      CYCLICAL**

12. What type of unemployment would you be experiencing if you are removed from your job because your skills do not match what the employer needs? (*circle one*)

**FRICTIONAL      STRUCTURAL      SEASONAL      CYCLICAL**

13. The following news headlines read “GDP Falls to New Low, Businesses Begin to Shut-Down”. What type of unemployment would you be most likely to experience? (*circle one*)

**FRICTIONAL      STRUCTURAL      SEASONAL      CYCLICAL**

## UNIT 11: ECONOMIC HEALTH INDICATORS: INFLATION AND UNEMPLOYMENT NOTES

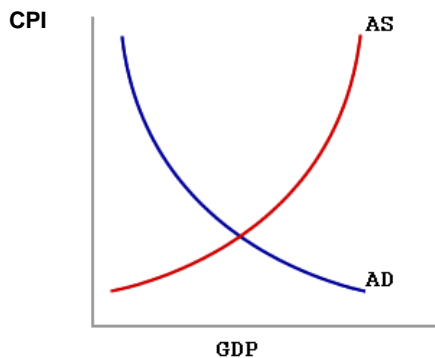
### 1.) Basic Terms to Know

- **Aggregate** means TOTAL. So when you see "aggregate demand (or aggregate supply), just substitute the word aggregate for the word TOTAL.
- **Aggregate** output is the same as GDP (Total output IS what GDP measures! GDP is TOTAL output!)
- **Deflation:** A general decline in prices of goods and services, usually caused by a reduction in the supply of money or credit.
- **Inflation:** A rate of increase in the general price level of all goods and services.
- **Hyperinflation:** a rapid increase in general price level
- **Stagflation:** Is a recession COMBINED with inflation (increased prices). *THIS IS THE WORST ECONOMIC EVENT THAT CAN OCCUR, EXCEPT FOR A DEPRESSION.*

### 2.) The business cycle and how it relates to the demand and supply curves

The business cycle affects aggregate demand and aggregate supply in any economy. The two curves are shown below.

Notice that QUANTITY has been substituted with GDP. In MACROECONOMICS we are measuring national trends, so we measure not the single quantity of ONE good, but the aggregate quantity of all goods produced.



### 3.) Causes of Inflation

There are 2 ways that inflation can occur, either through **demand-pull inflation** or **cost-push inflation**.

- **Demand-pull inflation:** inflation caused by an increase in demand or in the supply of money.

EXAMPLE: If the government does anything to put more money in our pockets and demand increases (which, if you look at the graph, would cause an increase in the price level), then this is called demand-pull inflation.

EXAMPLE: If the economy is in a period of huge growth and the unemployment rate is falling, then consumers are going to have more money. Aggregate demand will increase, causing an increase in prices.

- **Cost-push inflation:** inflation caused by a rise in prices due to an increase in the cost of production. Increases in the cost of labor, raw materials, equipment, and borrowing money push up the cost of production.

EXAMPLE: If the hurricane destroys reserves of oil, then supply decreases. The supply curve will shift to the left, which would increase the price level. Looking at the graph, this would decrease GDP and increase the price level.

### 4.) US Government Policies on How to Increase GDP in the Economy

#### Supply-side Economics or Demand-side Economics

- **Demand-side Economics:** policy that focuses on shifting the aggregate demand curve as a way of promoting full employment and price stability (*this was the policy between 1930 & 1970*).
  - \* **Keynesian Economics:** the economy can be regulated by focusing on the demand-side economics (*based on theory developed by John Keynes*).
  - \* **FDR's New Deal policy:** government would "pump" money into the economy by way of social programs and more government purchases.
- **Supply-side Economics:** policy that focuses on a rightward shift of the aggregate supply curve through tax cuts or other changes that increase production incentives (*this has been the policy since the 1980s*).
  - \* **President Reagan's policy:** cut the business taxes. This will reduce the costs of production and will cause supply to increase, thus increasing GDP AND it will reduce the price level (deflation) if demand stays constant.

### 5.) Relationship between GDP and the Unemployment Rate

- As **GDP increases = the unemployment rate decreases**. When we increase output of a nation, then more people are needed to produce this output (more workers are needed).
- What would happen if (1) the aggregate supply or (2) the aggregate demand decreased (shifted left)? GDP would **fall** in both situations, which could indicate a **recession** causing high **cyclical unemployment** (*look below for definition of cyclical unemployment*).

#### 6.) How to measure employment

- When counting employment, the Bureau of Labor Statistics **ONLY** counts those that are currently working **OR** are seeking employment.
- The following people are **NOT** counted in the Labor Force (currently working):
  1. People under 16 years old
  2. Retire individuals
  3. Students enrolled fulltime (more than 9 credit hours)
  4. People working part-time (under 30 hours a week)
  5. People in the military or institutionalized (prison or mental hospital)

#### 7.) 4 Types of Unemployment

1. **Frictional:** unemployment associated with people moving from one job to another or moving into the labor force.
2. **Structural:** unemployment that arises when changes in technology or international competition change the skills needed to perform jobs or change the location of jobs. Basically people **DO NOT** have the skills necessary for a job.
3. **Seasonal:** unemployment due to the climate
4. **Cyclical:** unemployment caused by the **recession** period of the business cycle.

#### 8.) Problems with measuring unemployment

- Economists **DO NOT** take into account the effects of **UNDEREMPLOYMENT** (*the workers are overqualified for their jobs or work fewer hours than they prefer*)
- **Full Employment:** There is no **cyclical** unemployment present in the economy.\* *Economists consider a unemployment rate of 4% - 5% to be full employment*