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| **AP Macroeconomics**  Mrs. Shackett  Phillips Curve | Name |

1. Draw AS/AD with long-run equilibrium. Label the price level PL1 and rGDP as Y1. Graph the effect on the equilibrium price level and rGDP if there is a decrease in AD. Label the equilibrium price level and rGDP after the decrease in AD as PL2 and Y2.
2. What happens to each of the following in the short run?

Real GDP \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

The unemployment rate \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

The price level \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

Real wages \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

1. Draw a graph of a short-run Phillips curve. Make sure you label your axes correctly! You will plot PL1 and PL2 along with their corresponding unemployment rates. There are no numbers for PL1 and PL2; just plot PL1 at some level and then plot PL2 either above or below it. Then select some unemployment rate (U1) to go with PL1 and then plot U2 either above or below U1 as shown in the graph above.
2. Draw AS/AD with long-run equilibrium. Label the price level PL1 and rGDP as Y1. Graph the effect on the equilibrium price level and rGDP if there is an increase in oil prices. Label the equilibrium price level and rGDP after the decrease in AD as PL3 and Y3.
3. What happens to each of the following in the short run?

Real GDP \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

The unemployment rate \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

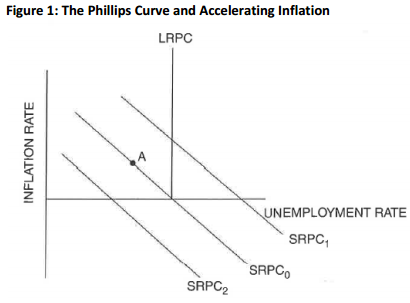
The price level \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

Real wages \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

1. On the short-run Phillips curve you drew before, plot the information and unemployment rates that result when the price of oil increases.
2. Suppose the economy is experiencing 2% inflation. News of rising energy costs increase people’s expectations of inflation. Demonstrate the change on a new correctly labeled SRPC graph.
3. If the government increases spending, how does it affect inflationary expectations? Explain.
4. If people are confident that a new Federal Reserve policy will achieve and maintain price stability, how does it affect inflationary expectations? Explain.
5. What will happen to the actual rate of inflation if people expect a higher inflation rate in the future? What will happen to the actual rate of inflation if people expect a lower inflation rate in the future? Explain.

THE LONG-RUN PHILLIPS CURVE

1. Draw a graph of the LRPC. Be sure to correctly label the axes and label the point at which the LRPC intersects the horizontal axis. What does the slope of the LRPC indicate about the trade‐off between the inflation rate and the unemployment rate? Explain.
2. Use the graph in problem 11 to show the effect on the LRPC if the natural rate of unemployment decrease. What happens to the LRAS when the natural rate of unemployment decreases?



1. What change in inflationary expectations is shown by the shift in the short-run Phillips curve from SRPC0 to SRPC1 in Figure 1?
2. At point A on the graph, the actual inflation is (*greater than/less than*) the expected rate of inflation, which will cause the SRPC to shift to the (*left/right*).
3. Label point B on the graph where the economy will be in long-run equilibrium after the change in inflationary expectations.
4. Label point C on the graph where the economy will be if policy makers attempt to keep the unemployment rate where it was at point A after the change in inflationary expectations. If the government continues to drive down the unemployment rate below the natural rate, what trend will continue to occur? Explain.