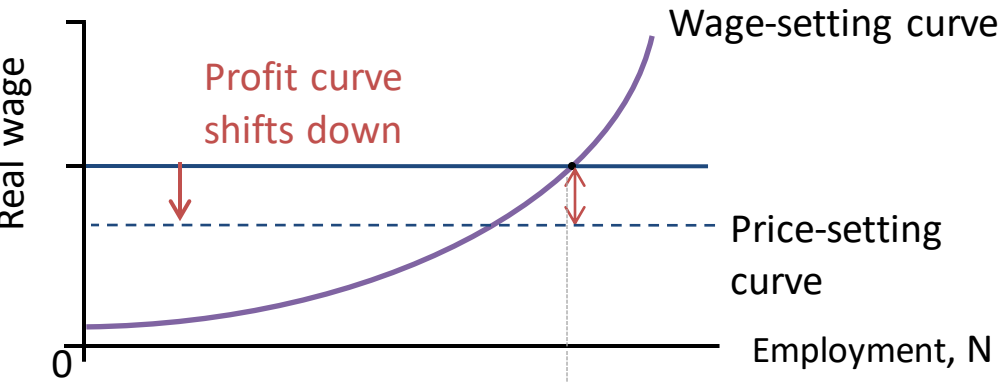


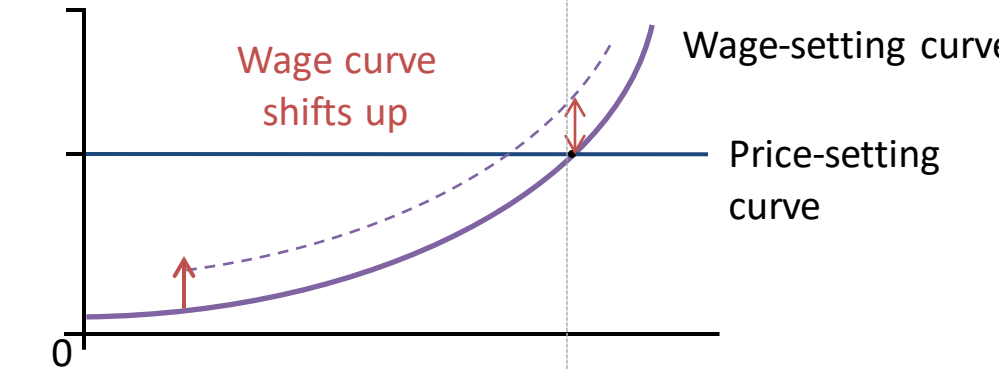
Unit 15

INFLATION, UNEMPLOYMENT, AND MONETARY
POLICY

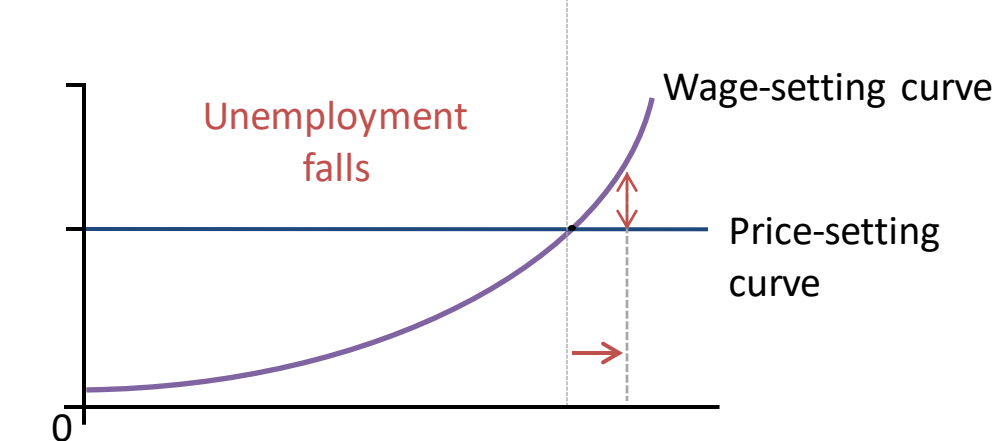
Figure 15.2. Three causes of inflation.



1. Owners' power rises relative to consumers (e.g. lower competition) – medium to long run



2. Employees' power rises relative to owners (e.g. stronger unions) – medium to long run



3. Employees' power rises relative to owners in a business cycle upswing – short to medium run

Figure MCQ3 Equilibrium in the labour market.

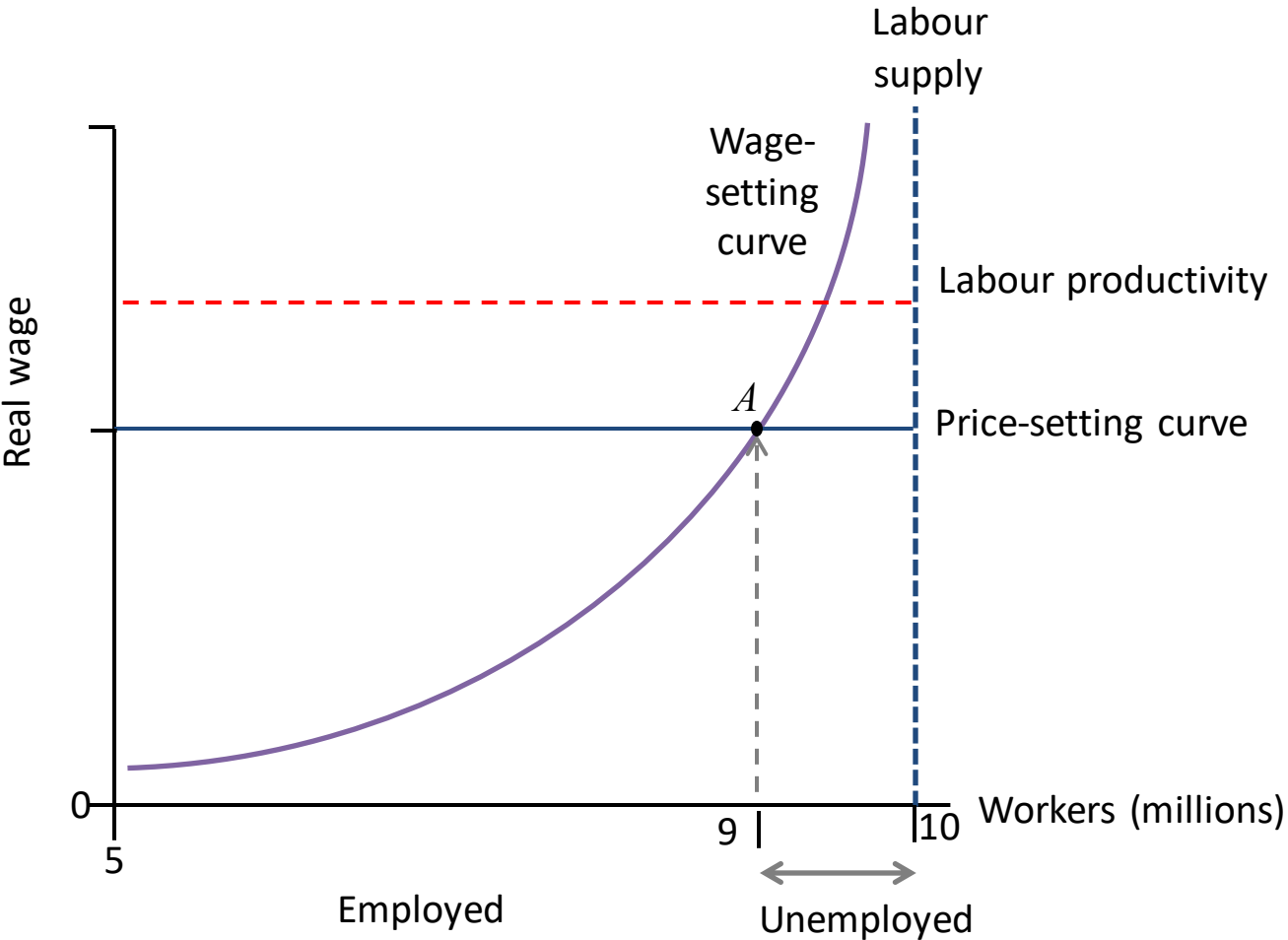


Figure 15.4a. Inflation and conflict over the pie: Stable price level at labour market equilibrium.

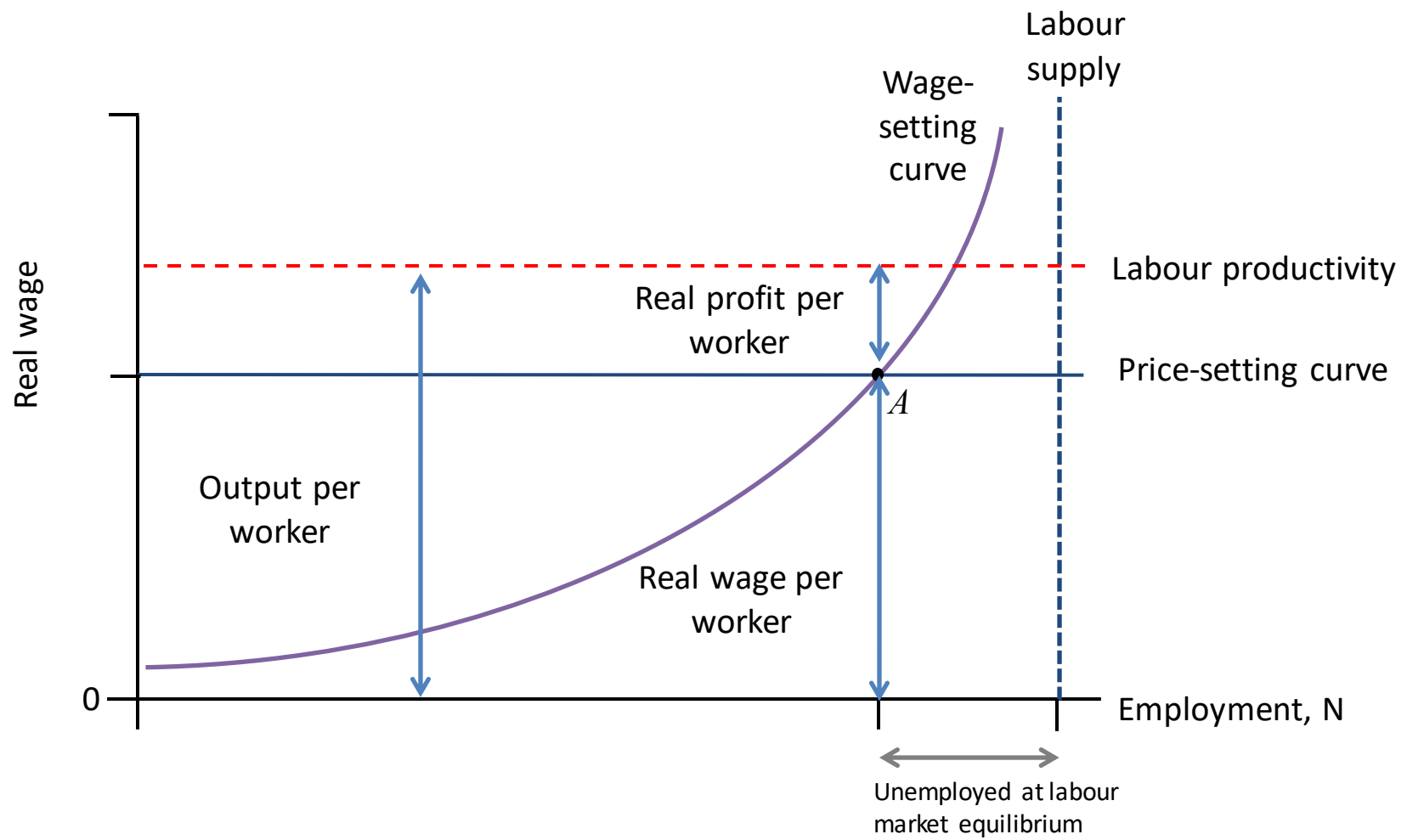


Figure 15.4b. Inflation and conflict over the pie at low and high unemployment.

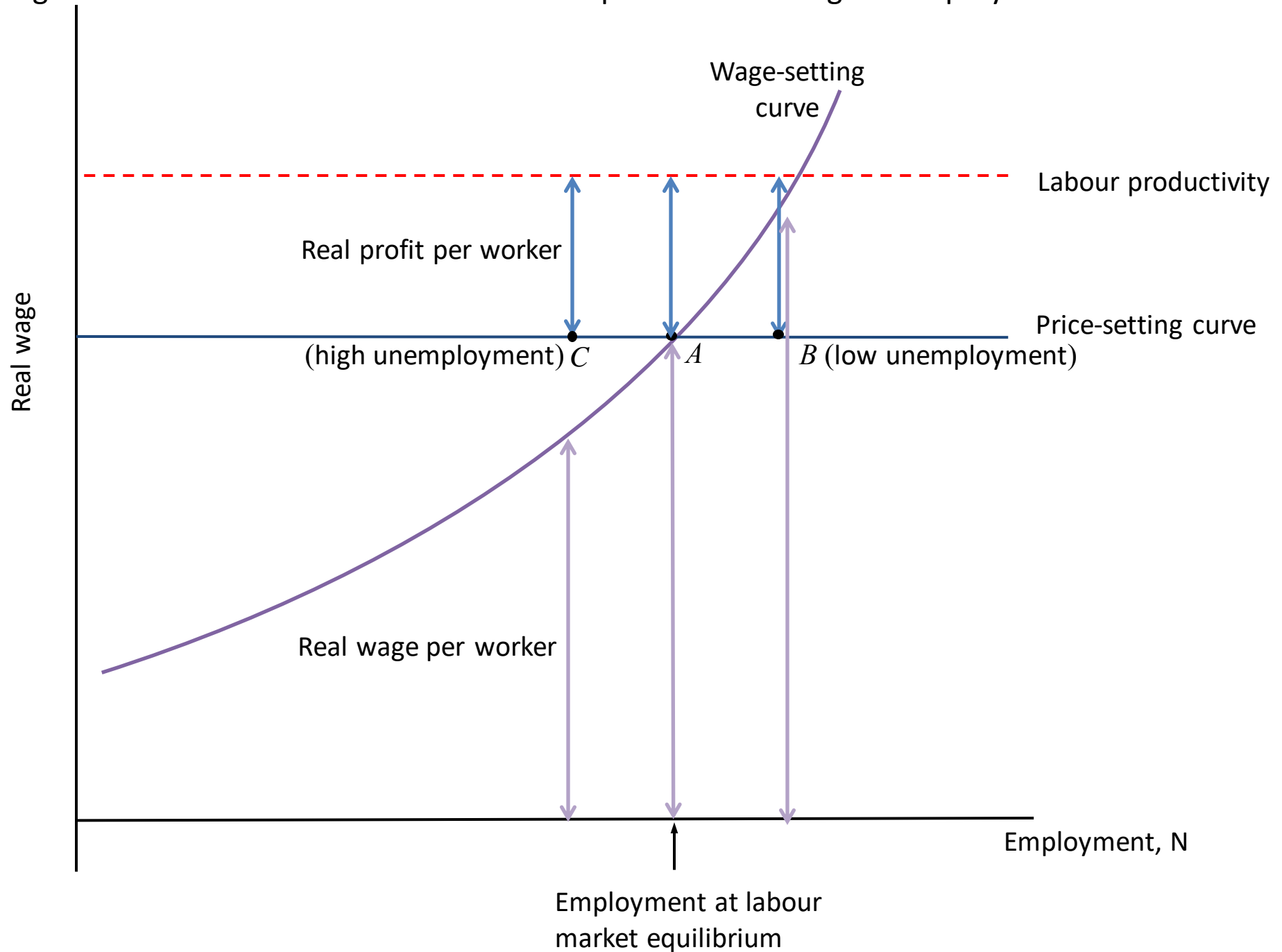


Figure 15.4c. Bargaining gaps, inflation, and the Phillips curve.

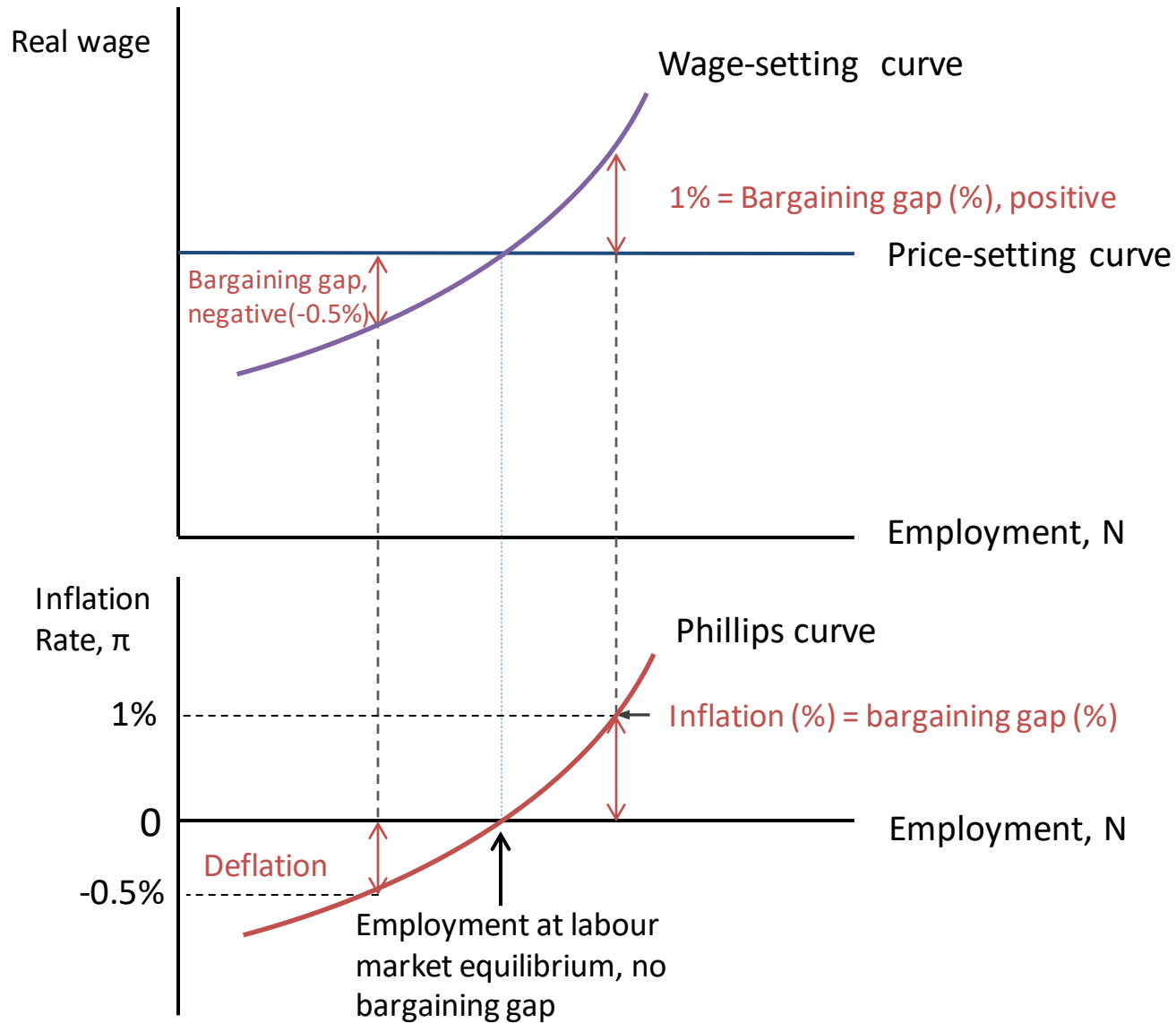
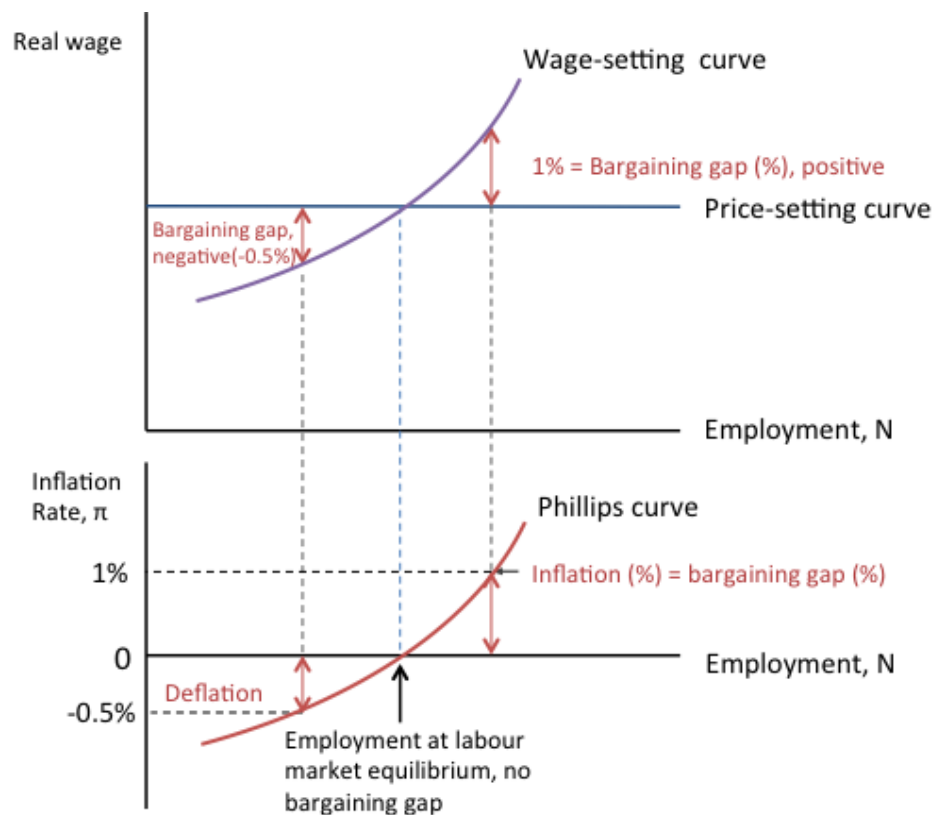


Figure 15.4d. The short-and medium-run models: Aggregate demand, employment, and inflation

Supply side
(medium run)



Demand side
(short run)

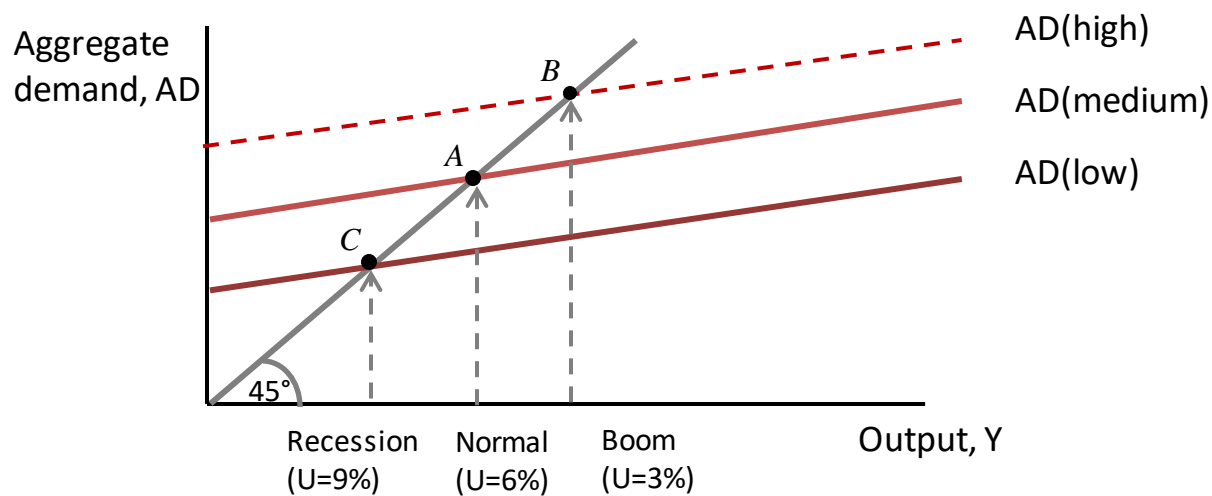
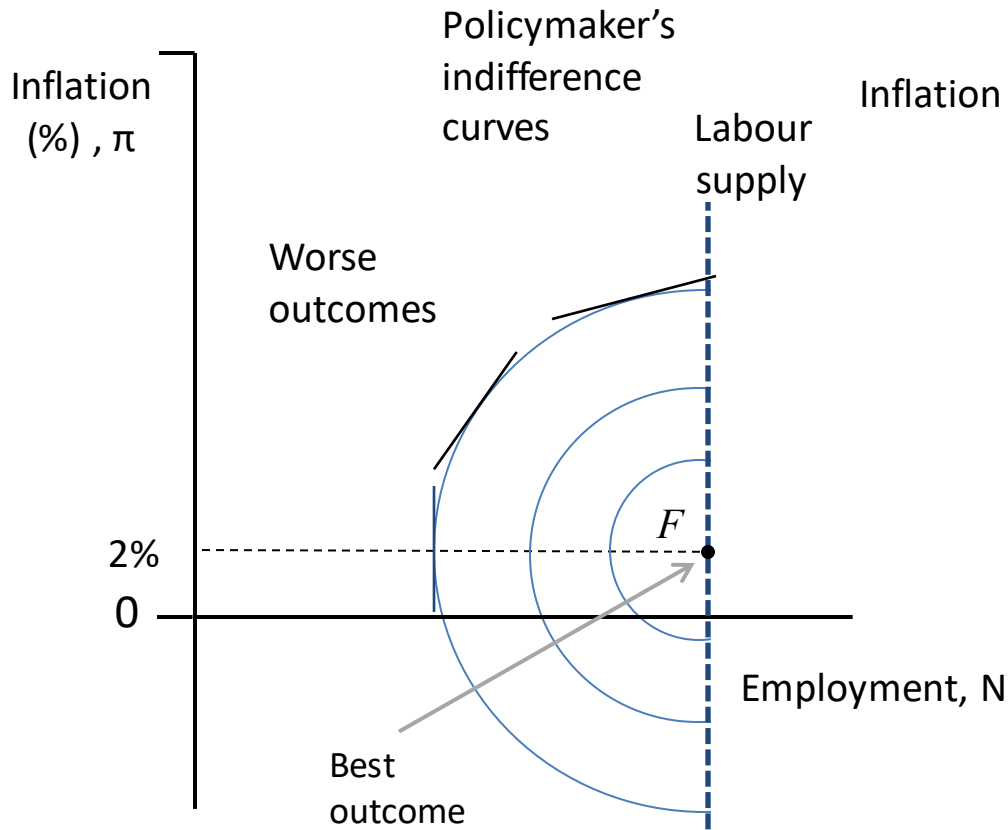
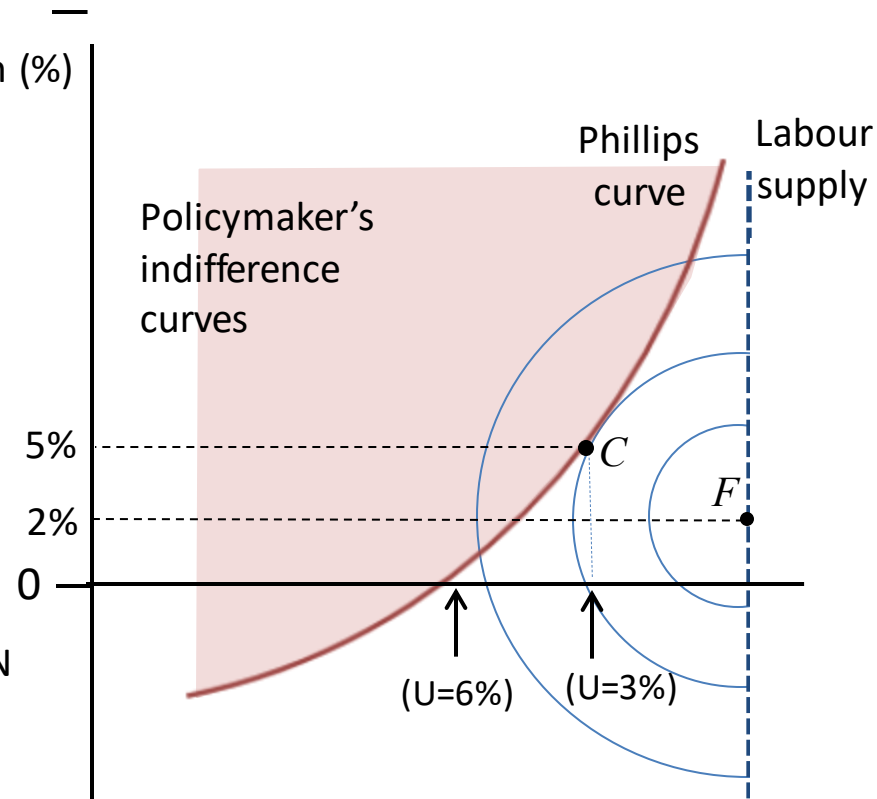


Figure 15.5. The Phillips curve and the policymaker's preferences.



a. The policymakers' preferences



b. The policymakers' preferences and the Phillips curve tradeoff

Figure 15.6. Phillips curves in the United States (1960-2014).

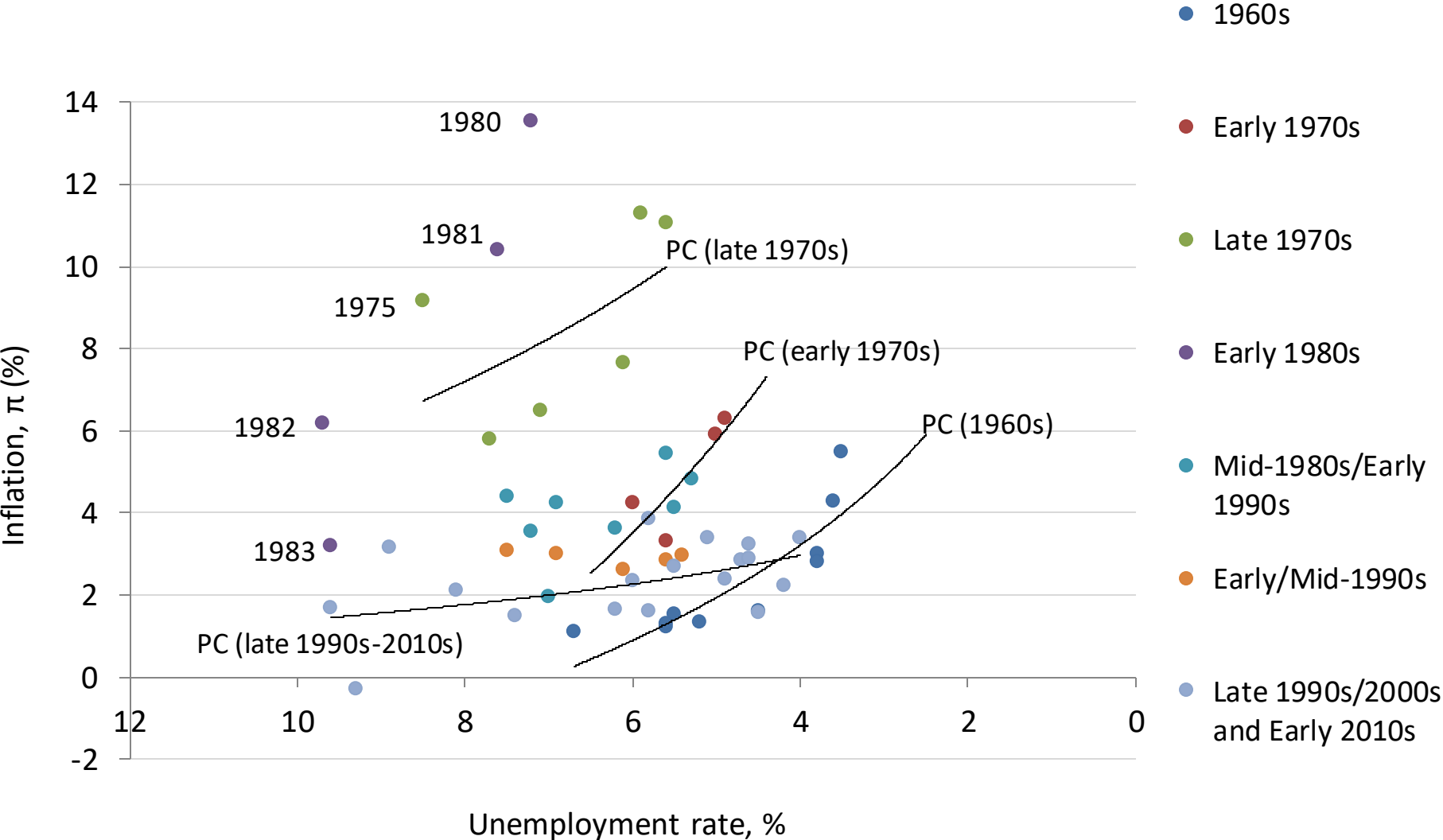


Figure 15.7. Bargaining gaps, expected inflation, and the Phillips curve.

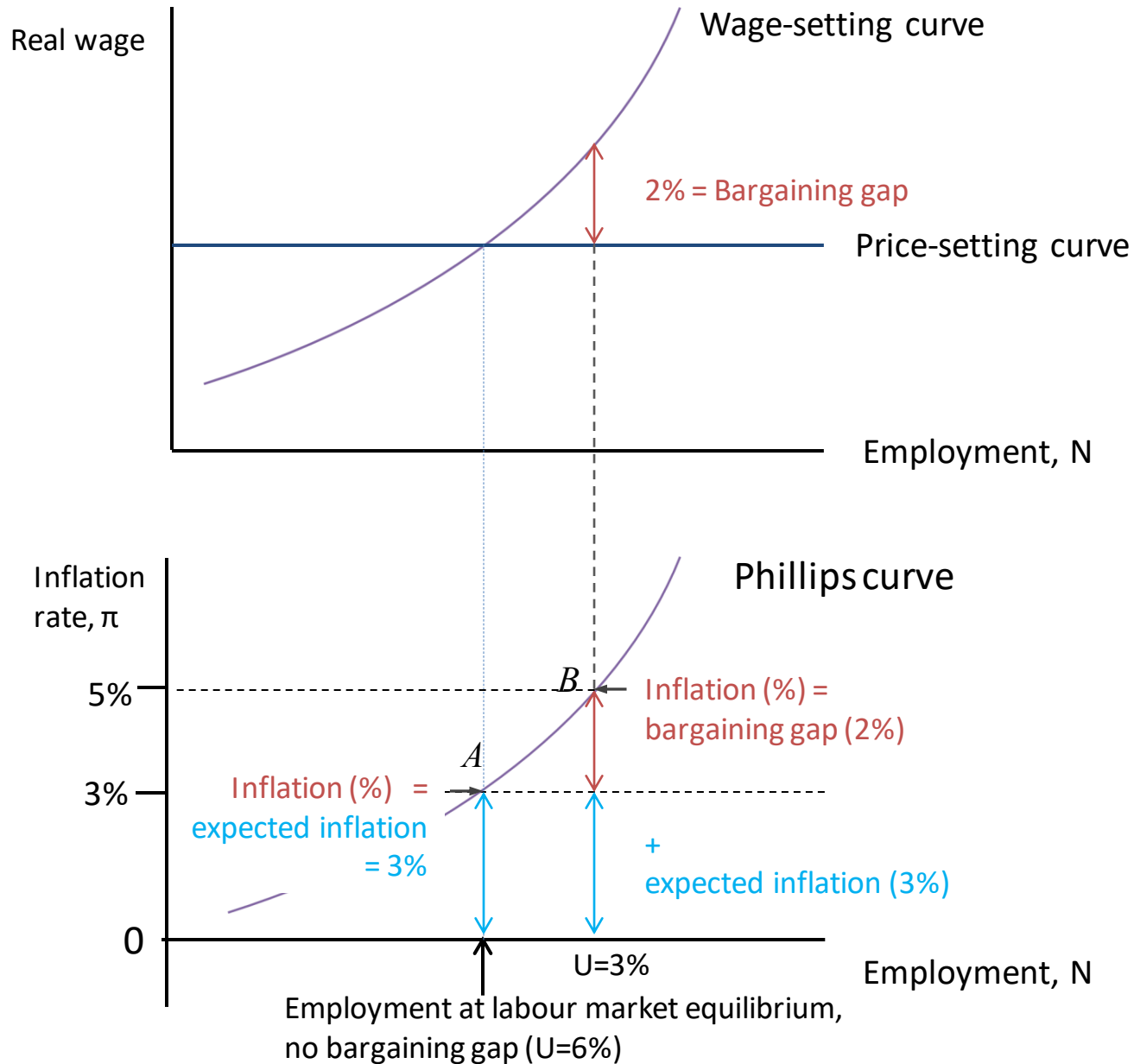


Figure 15.8. Unstable Phillips curves: Expected inflation and the bargaining gap.

	Year	What inflation rate is expected? The inflation rate in the previous year (1)	Unemployment	Bargaining gap (3)	Inflation outcome: expectations plus bargaining gap (1)+(3)	Are wage setters and price setters disappointed (are their claims inconsistent)?
Stable inflation	1	3%	6%	0	3%	No
	2	3%	6%	0	3%	No
	3	3%	6%	0	3%	No
Rising inflation	1	3%	3%	2%	5%	Yes
	2	5%	3%	2%	7%	Yes
	3	7%	3%	2%	9%	Yes

Figure 15.9. Inflation expectations and Phillips curves.

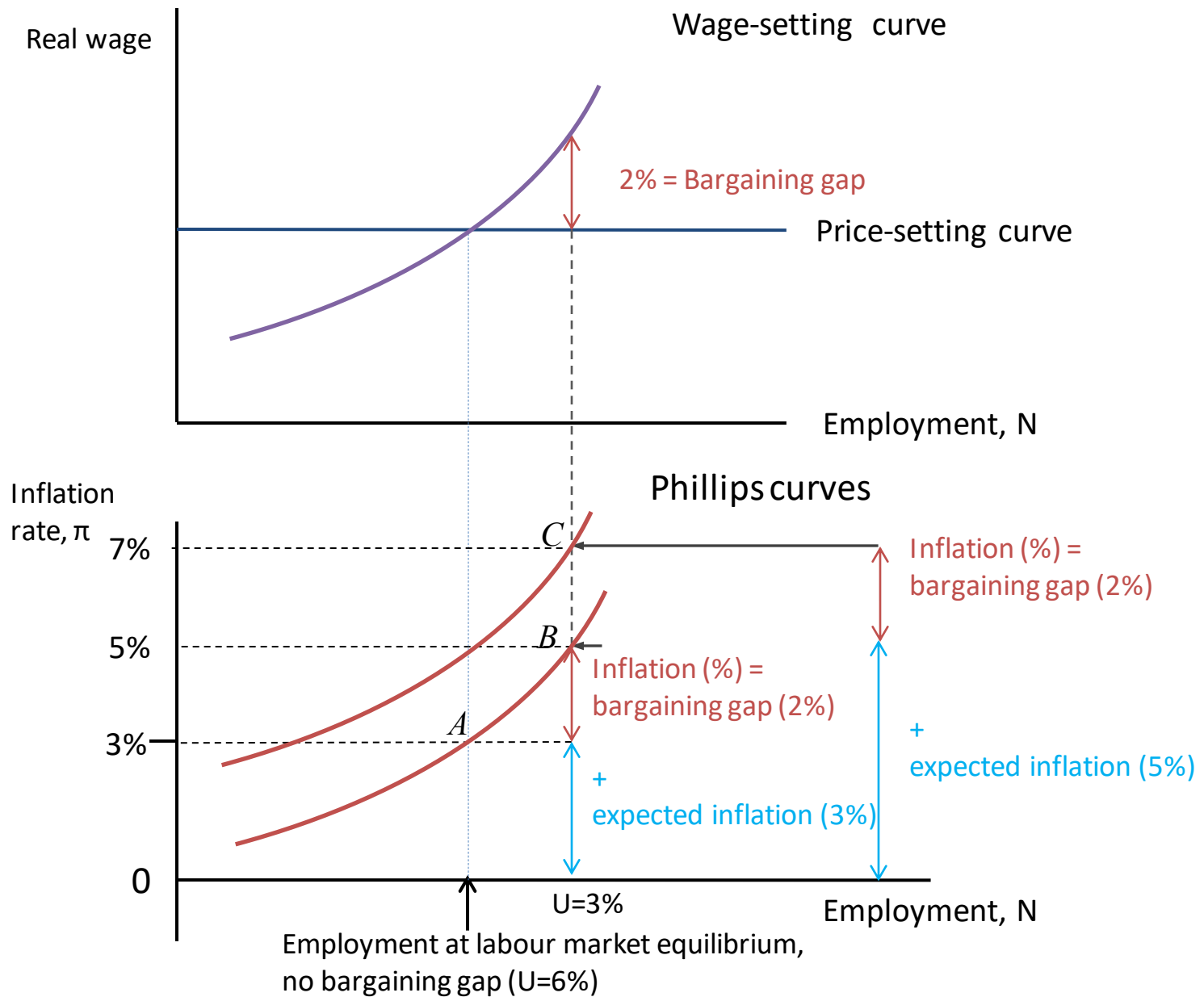


Figure 15.10. Inflation, expected inflation, and the bargaining gap.

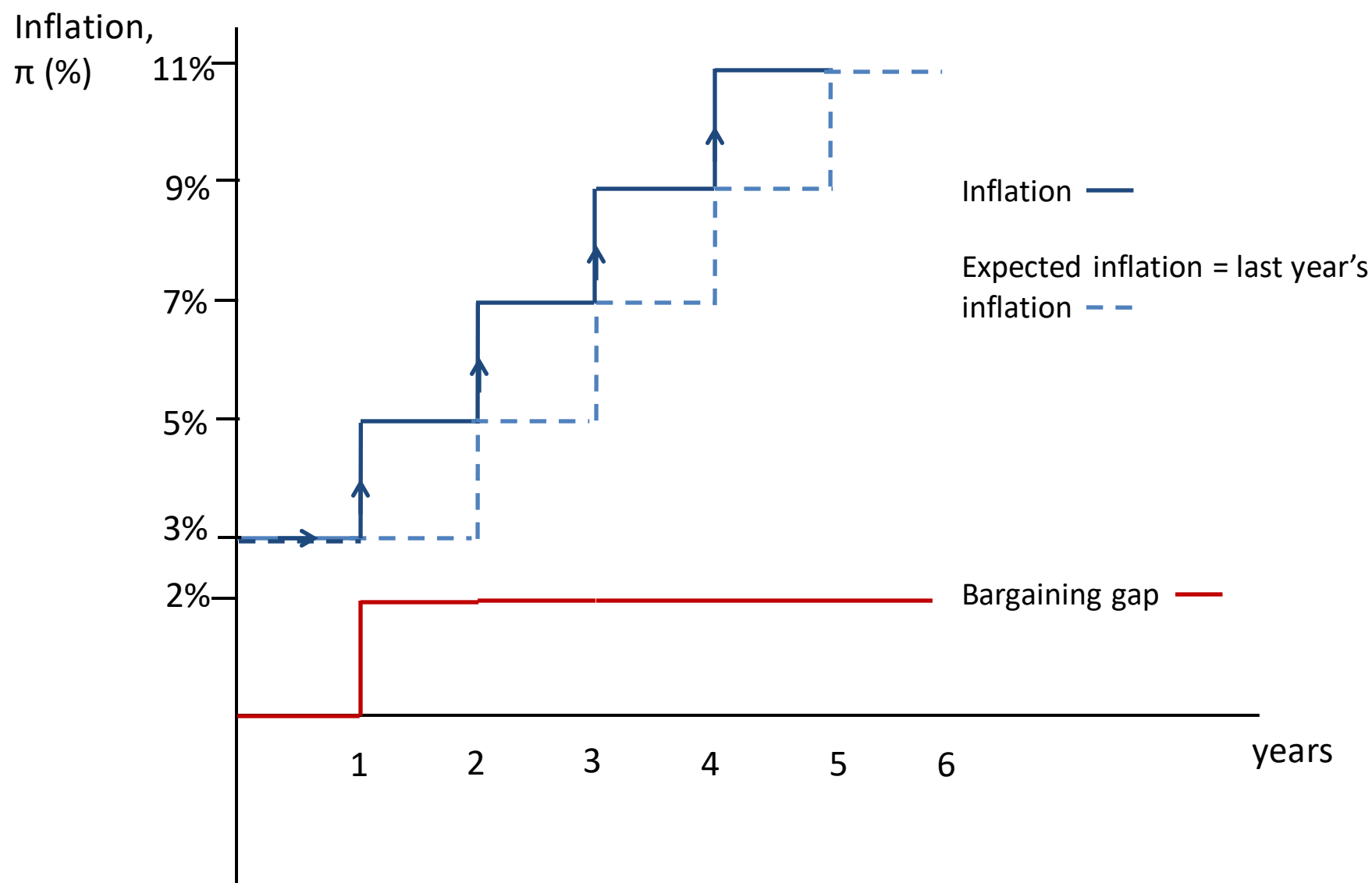


Figure 15.11. An oil shock and the price-setting curve.

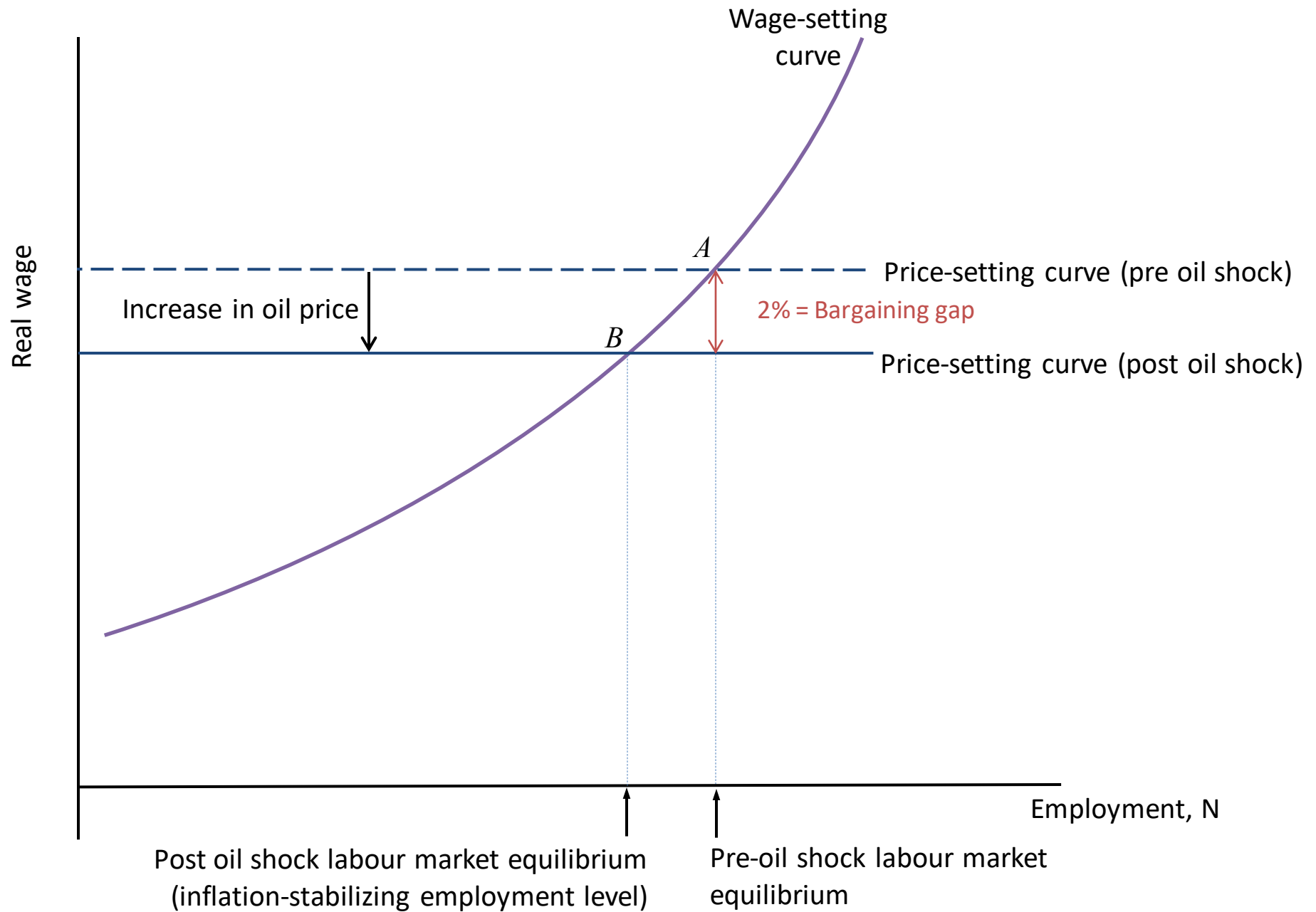


Figure 15.12. UK GDP growth and real oil prices (1950-2015).

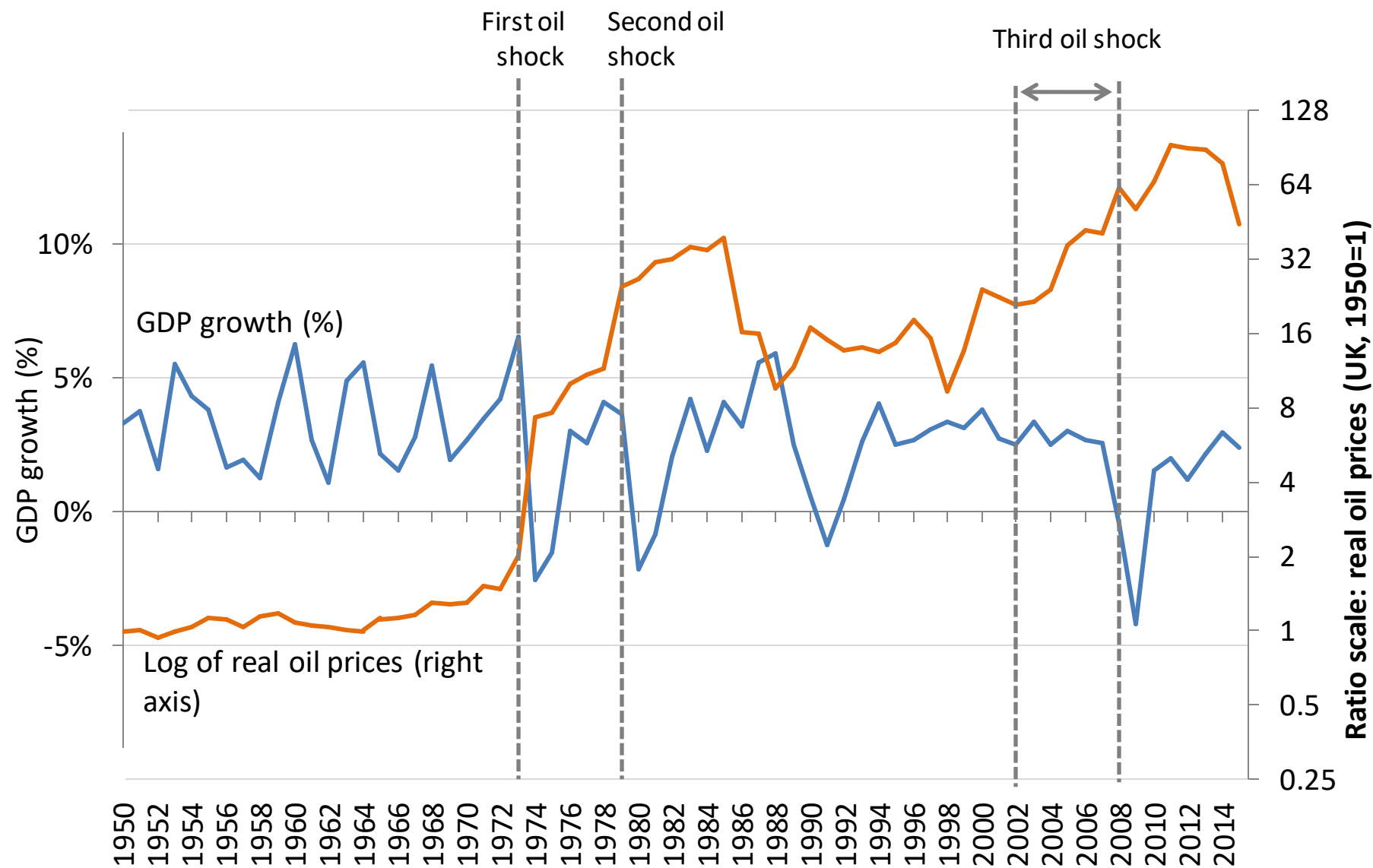


Figure 15.13. UK Inflation and unemployment rate (1950-2015).

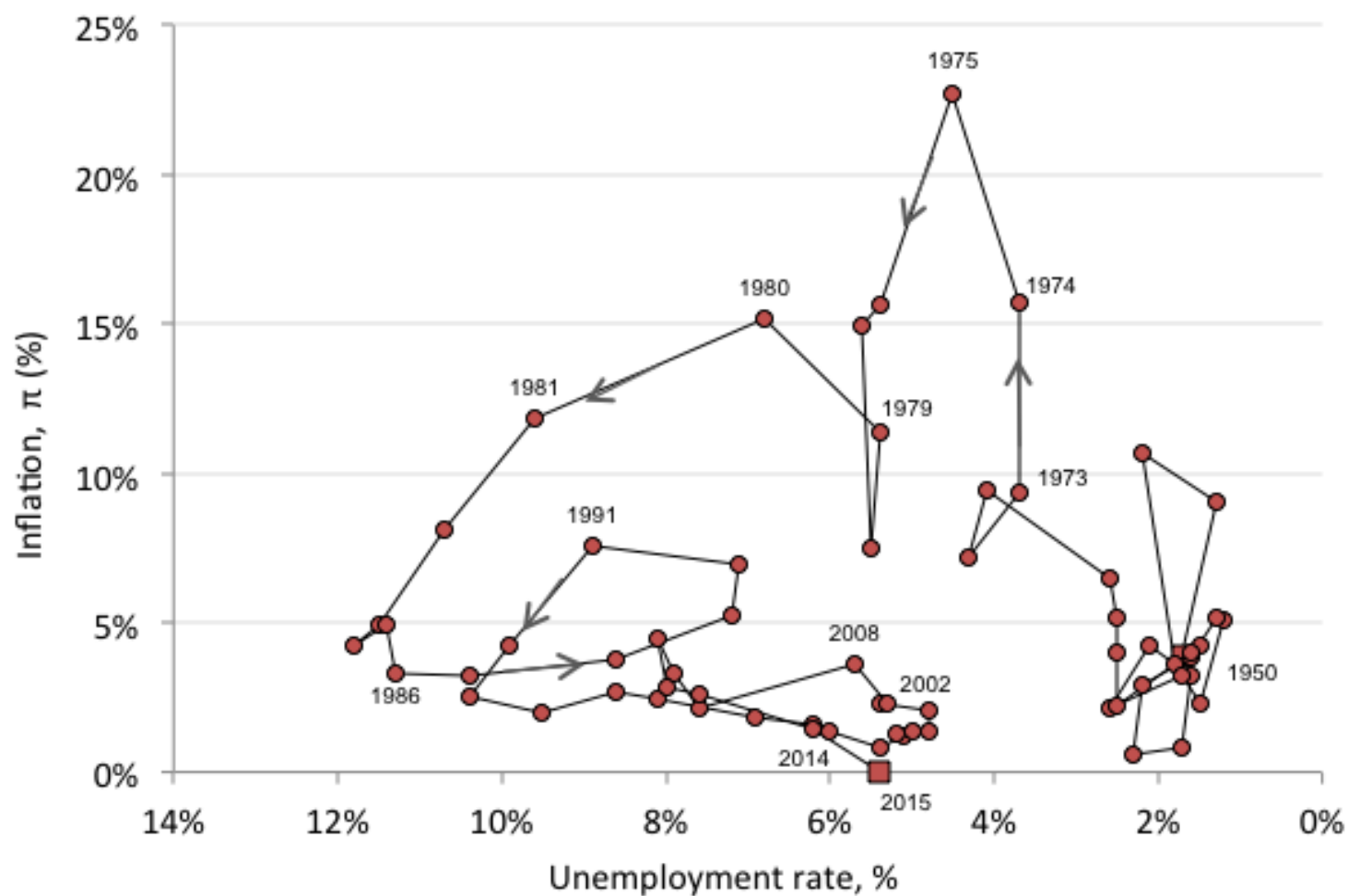


Figure 15.14. Monetary policy transmission mechanisms.

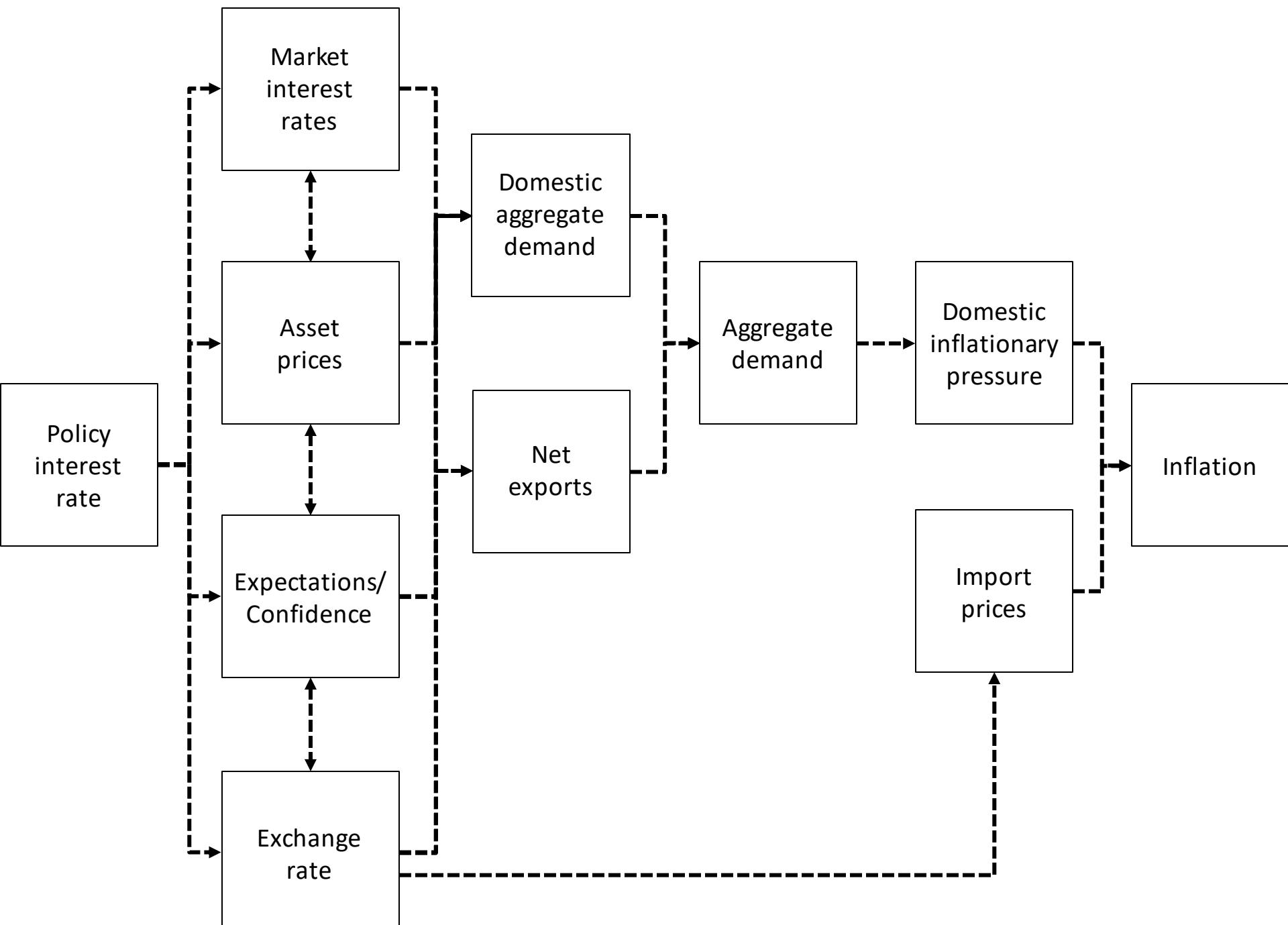
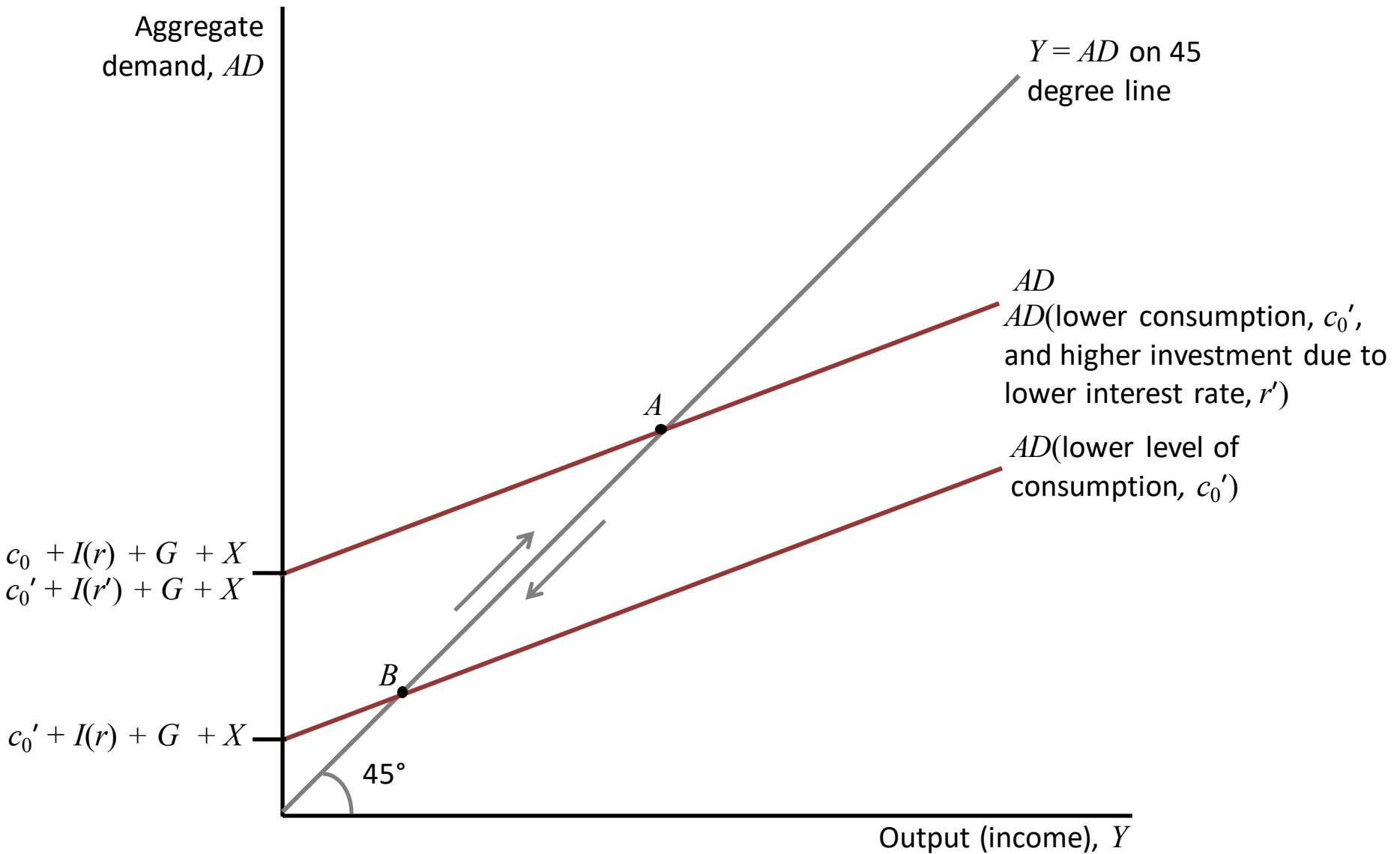


Figure 15.15. The use of monetary policy to stabilise the economy in a recession.



Note: $AD = c_0 + c_1(1 - t)Y + I(r) + G + X - mY$

Figure 15.16. The policy mix: Fiscal and monetary policy in the US following the collapse of the tech bubble.

		2000	2001	2002	2003
Real Gross Domestic Product (annual%change)		4.1	0.9	1.8	2.8
Contribution to % change in GDP	Change in nonresidential investment	1.15	-1.2	-0.66	0.69
	Change in residential investment	-0.07	0.09	0.39	0.66
	Change in government expenditure	0.10	0.88	0.74	0.36
	Change in other contributions	2.92	1.13	1.33	1.09
Federal Reserve nominal interest rate (annual average, %)		6.24	3.89	1.67	1.13
Unemployment rate (%)		4	4.7	5.8	6
Inflation rate (%)		3.4	2.8	1.6	2.3

Figure 15.17. A policy intervention to restore employment and output after a fall in investment.

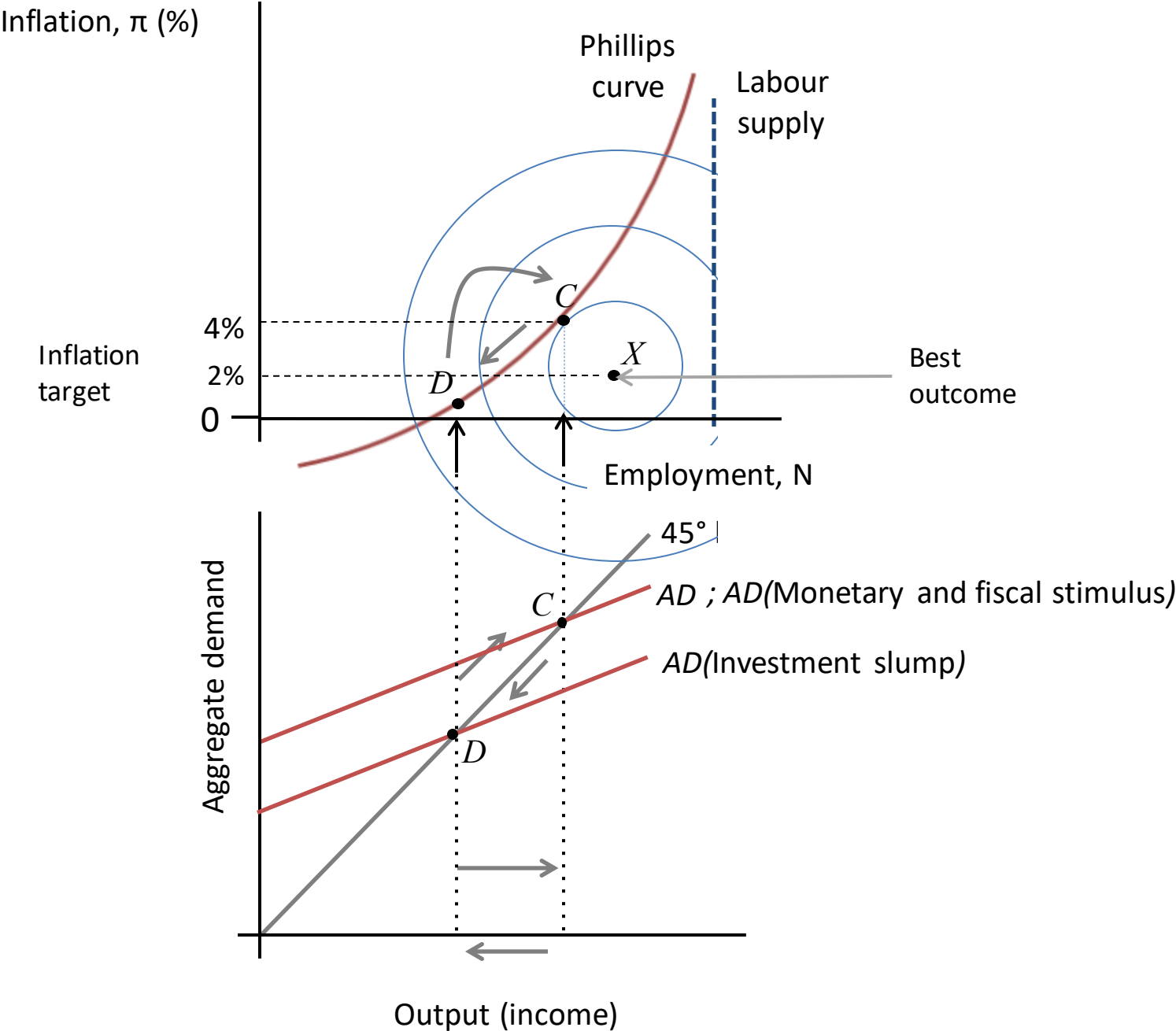


Figure 15.18. Countries who had inflation-targeting central banks by 2012.

Country	Inflation targeting adoption date	Inflation rate at adoption date (%)	2010 end-of-year inflation (%)	Target inflation rate (%)
New Zealand	1990	3.30	4.03	1 - 3
Canada	1991	6.90	2.23	2 +/- 1
United Kingdom	1992	4.00	3.39	2
Australia	1993	2.00	2.65	2 - 3
Sweden	1993	1.80	2.10	2
Czech Republic	1997	6.80	2.00	3 +/- 1
Israel	1997	8.10	2.62	2 +/- 1
Poland	1998	10.60	3.10	2.5 +/- 1
Brazil	1999	3.30	5.91	4.5 +/- 1
Chile	1999	3.20	2.97	3 +/- 1
Colombia	1999	9.30	3.17	2 - 4
South Africa	2000	2.60	3.50	3 - 6
Thailand	2000	0.80	3.05	0.5 - 3
Hungary	2001	10.80	4.20	3 +/- 1
Mexico	2001	9.00	4.40	3 +/- 1
Iceland	2001	4.10	2.37	2.5 +/- 1.5
Korea, Republic of	2001	2.90	3.51	3 +/- 1
Norway	2001	3.60	2.76	2.5 +/- 1
Peru	2002	-0.10	2.08	2 +/- 1
Philippines	2002	4.50	3.00	4 +/- 1
Guatemala	2005	9.20	5.39	5 +/- 1
Indonesia	2005	7.40	6.96	5 +/- 1
Romania	2005	9.30	8.00	3 +/- 1
Serbia	2006	10.80	10.29	4 - 8
Turkey	2006	7.70	6.40	5.5 +/- 2
Armenia	2006	5.20	9.35	4.5 +/- 1.5
Ghana	2007	10.50	8.58	8.5 +/- 2
Albania	2009	3.70	2.40	2 +/- 1

Figure 15.20. The economy's inflation-stabilizing unemployment rate.

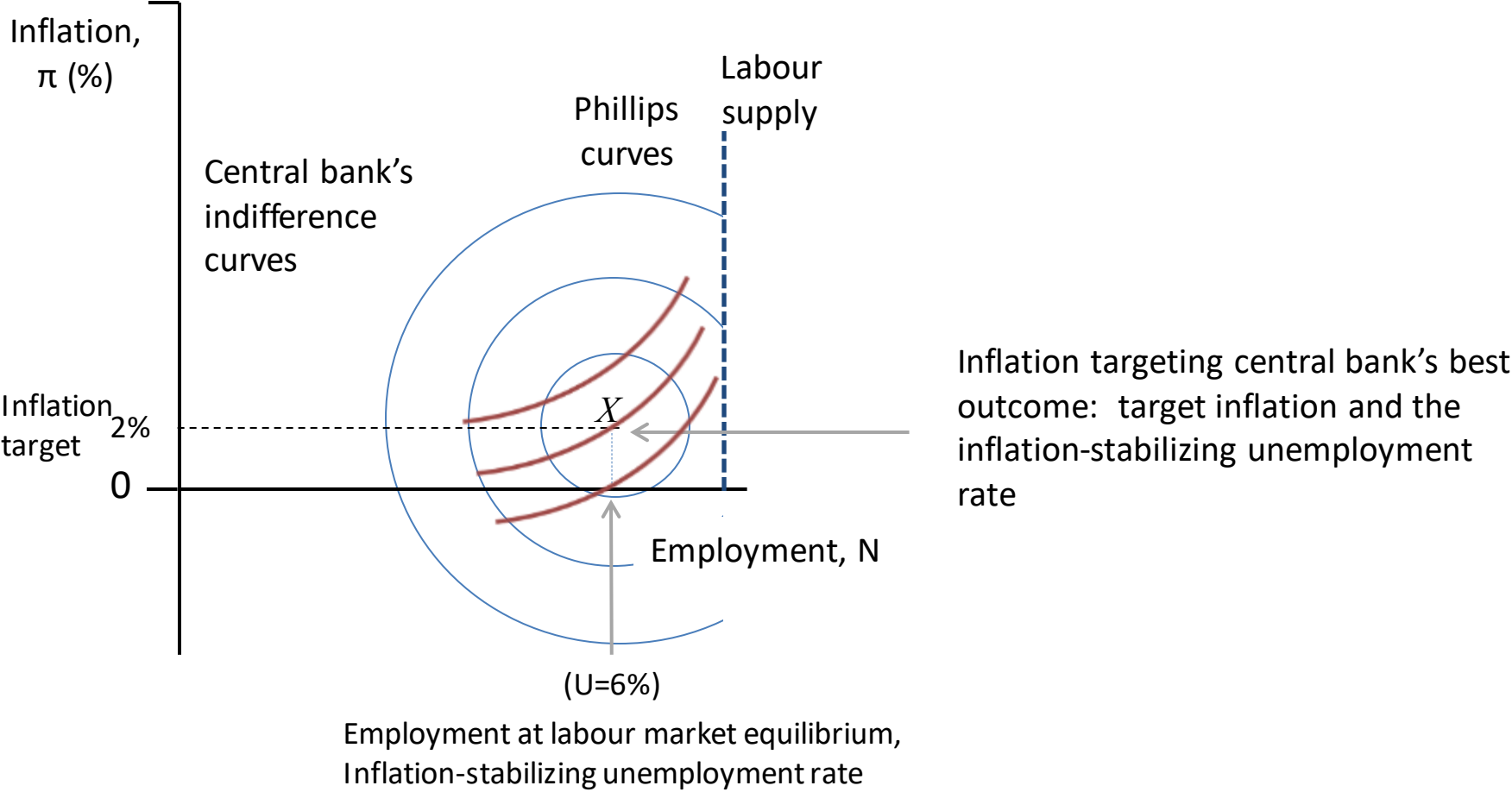


Figure 15.21. Price responses to rising employment and capacity utilisation.

