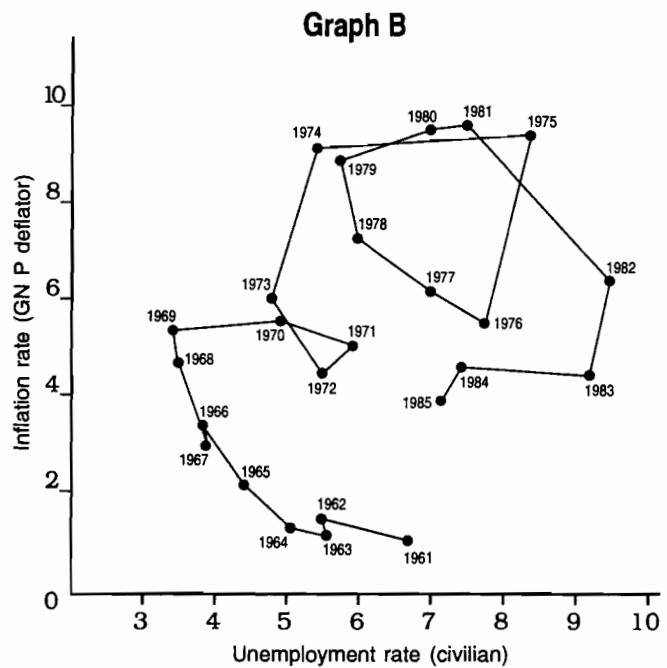
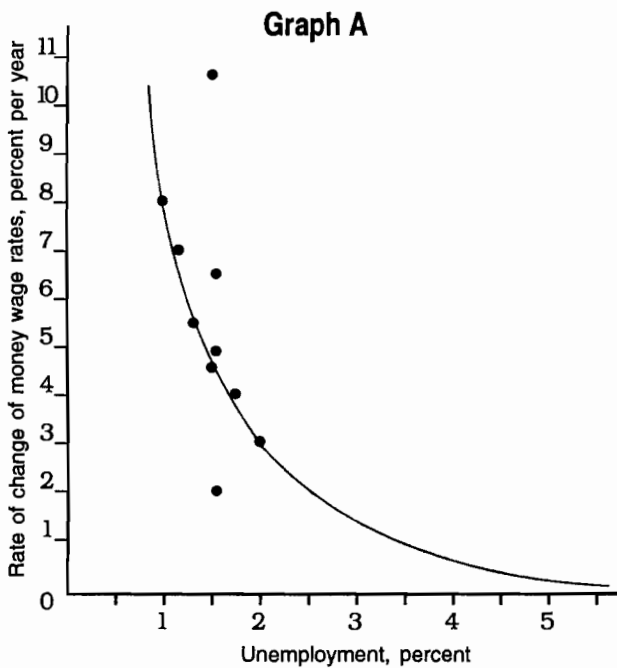


## The Phillips Curve— The Trade-Off Between Unemployment and Inflation

The first major economist to describe the trade-off between inflation and unemployment was A.W. Phillips of the London School of Economics in 1958. This trade-off came to be known as the Phillips Curve. He based his curve on a study of wages and unemployment in Great Britain between 1861 and 1913. He found that the lower the rate of inflation, the higher the unemployment, and vice-versa. Graph A depicts the normal Phillips Curve as a trade-off between inflation and unemployment. Graph B shows the actual relationship between unemployment and inflation in the United States between 1961 and 1987. Analyze the graphs by answering the questions that follow.



1. Why is the study of inflation and unemployment important?
2. Are any portions of the actual data in graph B consistent with the Phillips Curve (graph A)?
3. What was the inflation rate for 1979? What was the unemployment rate for the same year? Compare these figures with those of 1980. Is this trend consistent with the Phillips theory?
4. Check the inflation and unemployment rates for 1981 and 1982. Is this trend consistent with the Phillips theory?
5. What might account for the differences in the trends in these two examples? Speculate.
6. Given the differences between the relationships illustrated by the Phillips Curve and the real world, why do we study such theories?