W

Stabilize This!

WITSOOTH · CLEVER TRUTH

AP MACROECONOMICS · UNIT 3

Name ______________ Period ______

DRIVING QUESTION

Prices rising AND unemployment rising, at the same time — normal economics says that shouldn't happen easily. When it does, what do you do?

Gut instinct now. Answer it again at the end using the deflator and cyclical unemployment.

BEFORE THE GAME

> *"By 1974, unemployment and inflation were both climbing past 8% at the same time — a combination economists had assumed was nearly impossible." The word they coined for it: stagflation.*
>
> — adapted from Federal Reserve historical data

Your gut answer — if prices are rising fast, should the government raise taxes and cut spending (tighten) to fight it? What's the catch if unemployment is also high?

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Quick prediction — do unemployment insurance payments require a new law to increase during a recession?

☐ Yes ☐ No, automatic

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DURING THE GAME — READ THE DASHBOARD

RD	NOMINAL / REAL GDP	GDP DEFLATOR	ACTUAL / NATURAL U-RATE	CYCLICAL U (W/ SIGN)	UI & TAX DIRECTION
1	______	______	______	______	☐↑ ☐↓
2	______	______	______	______	☐↑ ☐↓
3	______	______	______	______	☐↑ ☐↓
4	______	______	______	______	☐↑ ☐↓
5 ★	______	______	______	______	☐↑ ☐↓

Deflator = (Nominal GDP ÷ Real GDP) × 100 · Cyclical U = Actual U − Natural U (positive = recession, negative = boom). Round 5 ★ is the stagflation trap.

AFTER THE GAME

Round 5 is designed to trick you: high deflator (inflation) AND high unemployment at once. Did your UI/tax-revenue call still follow the labor market, or did the price data pull you off track?

Now use the vocabulary: automatic stabilizers respond to what, specifically — the price level, or the labor market/income? Explain why that distinction matters in a stagflation round.

TRANSFER — NOW APPLY IT

Breaking: "Inflation Hits 8%, Unemployment Climbs to 6%"

Nominal GDP: $22 trillion. Real GDP: $20.5 trillion. Actual unemployment: 6%. Natural rate of unemployment: 4.5%. A news anchor asks: "Should the government cut spending to fight inflation, or increase spending to fight unemployment?"

$22T	$20.5T	6%	4.5%
NOMINAL GDP	REAL GDP	ACTUAL U	NATURAL U

A. Calculate the GDP deflator from the figures above.

B. Calculate cyclical unemployment (with the correct sign).

C. Answer the anchor's question — and explain why "either" tool comes with a real trade-off here.

RETURN TO THE DRIVING QUESTION

Prices rising AND unemployment rising, at the same time — normal economics says that shouldn't happen easily. When it does, what do you do?

Use the deflator, cyclical unemployment, and automatic stabilizers in your final answer.