

**Government** – while objectives are largely the same the priorities differ according to the political party

**Firms**

- ⊙ Profits
- ⊙ Market share
- ⊙ Competitors

Different objectives

**Unions / labour**

- ⊙ Higher wages/ benefits e-g. more vacation
- ⊙ Maintain pace with RPI- Retail price index
- ⊙ Wages are ‘sticky’ downwards

**(A)**  
Types of unemployment

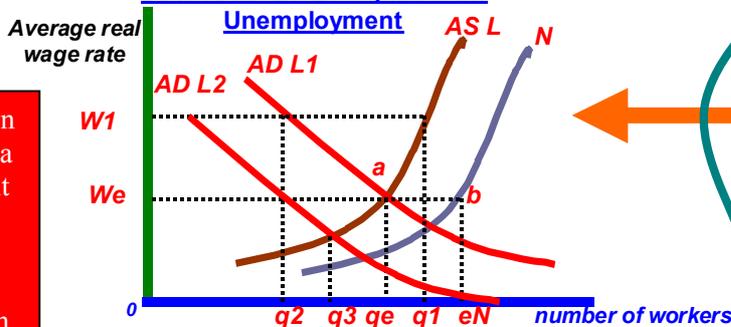
1. Frictional
  2. Seasonal
  3. Structural
  4. Cyclical/ Keynesian or demand deficient (see C)
  5. Hidden
  6. Classical or real wage unemployment (see C)
  7. residual unemployment
- See webnote 309

**(B)**  
Natural Rate of Unemployment  
(monetarist / Friedman school – late 1960’s)  
Is there a natural rate of unemployment or an equilibrium rate of unemployment? Yes!  
**frictional + structural + seasonal unemployment = ‘natural unemployment’.**  
This is clearly indicated in diagram A whereby at the market wage rate of  $W_e$  a natural level on unemployment exists in the economy the quantity of which is represented by  $ab$  or  $q_e$  or  $q_e N$ . See diagram A. Natural rate is that rate established by market forces. At this rate there is no tendency to change wages

**(C)**  
Disequilibrium

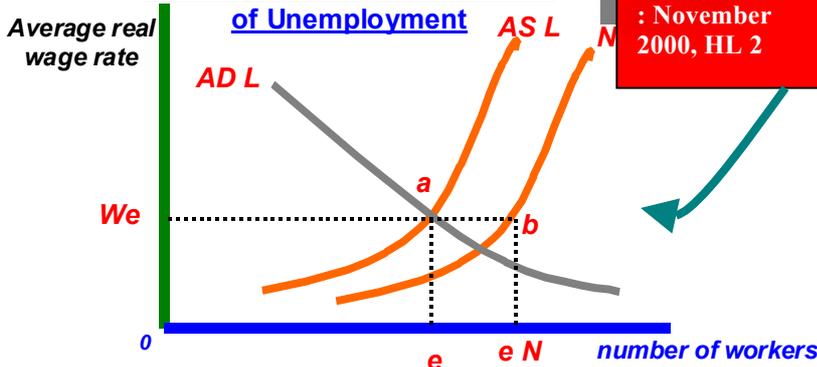
Disequilibrium rate of unemployment i.e. the labour market is not clearing.  
Two possible causes:  
1. Classical or real wage unemployment  
2. demand deficient or cyclical unemployment  
Note: economists disagree as to which of the above causes disequilibrium unemployment

**DIAGRAM B: Disequilibrium Unemployment**



Note: the key issue here is that the labour market is in equilibrium at  $W_e$  a  $q_e$

**DIAGRAM A: The Natural Rate of Unemployment**



Note: the key issue here is that the labour market is in equilibrium at  $W_e$  a  $e$

IB: Explain two ways a government can reduce its natural rate of unemployment.  
2008-Nov h2 q4

IB: What is the natural rate of unemployment : November 2000, HL 2

- (D)**
1. Classical or real wage unemployment
    - ⊙ Trade unions
    - ⊙ Minimum wage legislation
  2. Demand deficient or cyclical (Keynesian) unemployment
    - ⊙ Extends across whole economy
    - ⊙ See inflationary gap/ deflationary webnote 328
    - ⊙ Effectively caused by a fall off in AD for goods and services in the economy (AD L also falls) and whereby the labour markets do not clear
    - ⊙ Labour resists wage cuts and therefore unemployment occurs as labour wage rates do not adjust to the lower demand in the economy. Therefore we have unemployment between  $q_2$  and  $q_e$  in diagram B