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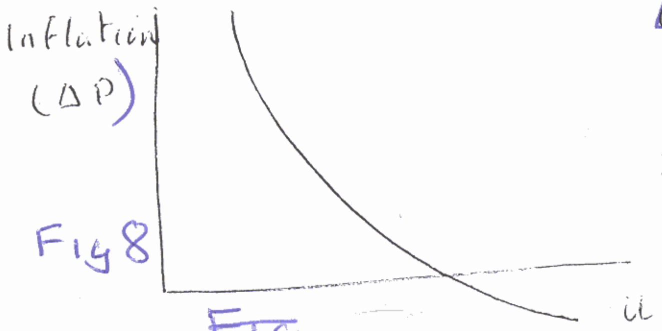
which gets passed on to higher prices. Hence:

$\Delta P_t = f(U_t)$ (6)

That is it is shaped like:



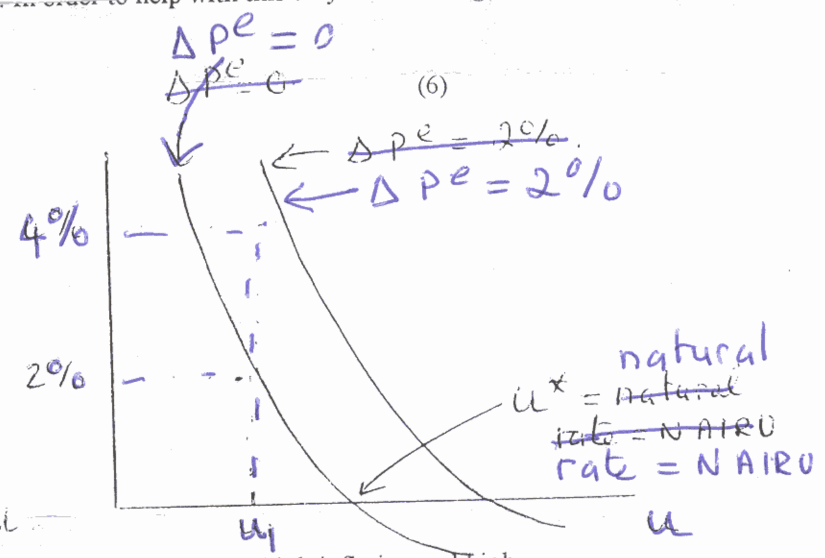


Fig 8

Problems emerged with the Philips curve in the 1970s when we observed high inflation and high unemployment - something which was not supposed to happen. Ed Phelps had put forward a theory in

equilibrium wage rate.

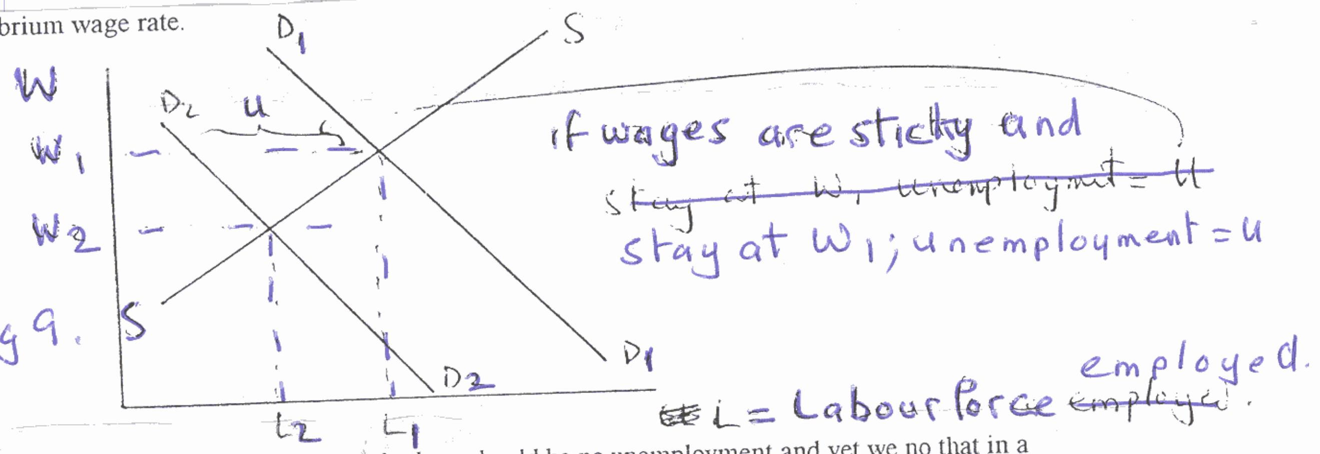


Fig 9.

OK, but if demand equals supply surely there should be no unemployment and yet we no that in a modern economy there is never any unemployment so how do the new classical school explain that