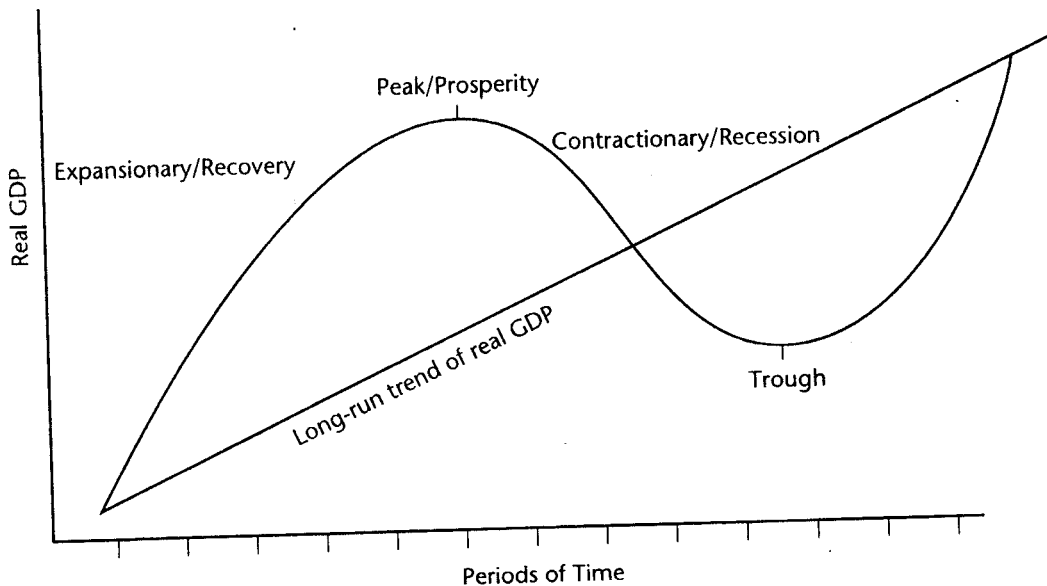


## ACTIVITY 14

## The Business Cycle

The Business Cycle



The curved line on the graph *The Business Cycle* shows a sample business cycle for an economy. The straight line represents the long-run trend of real GDP. The business cycle can conveniently be divided into four phases:

**1. Expansionary or recovery phase.**

Real output in the economy is increasing and the unemployment rate is declining. As the economic expansion continues, inflation may continue to accelerate.

**2. Peak or prosperity phase.** Real output in the economy is at a high level, unemployment is relatively low, and inflation may be high.

**3. Contractionary or recession phase.**

Real output in the economy is decreasing and the unemployment rate is rising. As the con-

traction continues, inflationary pressures subside. If the recession continues long enough, prices may actually start to fall, a situation known as *deflation*.

**4. Trough.** The lowest point of real GDP reached during a business cycle is known as the trough. If the trough is particularly deep, it may be called a depression. A *depression* is an economic situation where the level of output falls to especially low levels and unemployment climbs to very high levels relative to the historical average. There is no precise decline in output at which a serious recession becomes a depression. However, most business cycles do not end in a depression. The most recent depression experienced in the United States was during the 1930s.

**ACTIVITY 14 continued**

1. The table *The U.S. Economy, from 1970* contains information for the U.S. economy from 1970 through 1991. For each year, first identify whether the economy was in an expansionary (E) or a contractionary (C) phase. Then, go back and pick out the years that correspond to a business-cycle peak and mark them with a (P) and the years that correspond to a trough and mark them with a (T).

**The U.S. Economy, from 1970**

Year	Real GDP in 1987 dollars (billions)	% change from previous year	Civilian unemployment rate	Inflation rate CPI Dec. to Dec.	Phase of the business cycle
1970	2,873.9	0.0	4.9	5.6	_____
1971	2,955.9	2.9	5.9	3.3	_____
1972	3,107.1	5.1	5.6	3.4	_____
1973	3,268.6	5.2	4.9	8.7	_____
1974	3,248.1	-0.6	5.6	12.3	_____
1975	3,221.7	-0.8	8.5	6.9	_____
1976	3,380.8	4.9	7.7	4.9	_____
1977	3,533.3	4.5	7.1	6.7	_____
1978	3,703.5	4.8	6.1	9.0	_____
1979	3,796.8	2.5	5.8	13.3	_____
1980	3,776.3	-0.5	7.1	12.5	_____
1981	3,843.1	1.8	7.6	8.9	_____
1982	3,760.3	-2.2	9.7	3.8	_____
1983	3,906.6	3.9	9.6	3.8	_____
1984	4,148.5	6.2	7.5	3.9	_____
1985	4,279.8	3.2	7.2	3.8	_____
1986	4,404.5	2.9	7.0	1.1	_____
1987	4,539.9	3.1	6.2	4.4	_____
1988	4,718.6	3.9	5.5	4.4	_____
1989	4,838.0	2.5	5.3	4.6	_____
1990	4,877.5	0.8	5.5	6.1	_____
1991	4,821.0	-1.2	6.7	3.1	_____
1992			7.4		_____
1993					_____
1994					_____
1995					_____
1996					_____
1997					_____
1998					_____
1999					_____

SOURCE: 1993 *Economic Report of the President*, U.S. Government Printing Office, Washington, DC.

### ACTIVITY 14 continued

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2. How many business cycles did the U.S. economy have between 1970 and 1991?  
\_\_\_\_\_
3. In how many years was output expanding? \_\_\_\_\_
4. In how many years was output contracting? \_\_\_\_\_
5. What economic expansionary period looks best to you? Why?
  
6. What economic contraction/recession looks worst to you? Why?
  
7. During years in which real GDP fell, what happened to the unemployment rate compared with the previous year? Why?
  
8. Look at the unemployment rate in years corresponding to a business-cycle peak. Why do you think there was still some unemployment in those years?
  
9. Based on the years 1970-1991, how does the rate of inflation correspond with the business cycle?