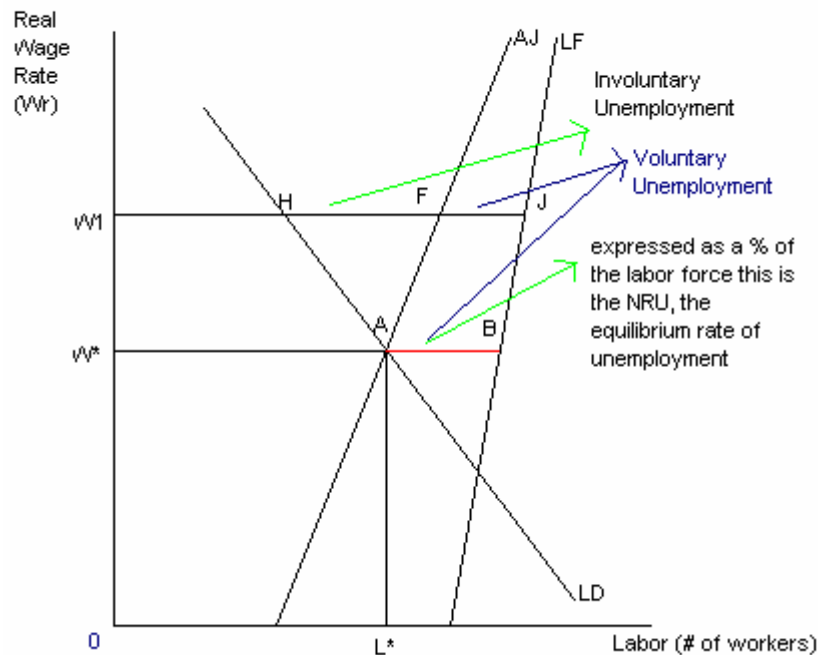


## Natural Rate of Unemployment

The NRU - Equilibrium Unemployment



The LD curve is the labor demand curve; it is negatively sloped as firms will be willing to hire fewer workers at higher wage rates as capital will become relatively cheaper. The LF curve is the labor force curve and shows the number of workers joining the labor force at each wage rate. It is upward sloping because as the real wage rate rises, the opportunity cost of leisure increases. The AJ curve is the 'accept jobs' curve and shows the number of workers who are willing to accept a job offer at each level of the real wage given the level of unemployment benefits. It is upward sloping as the probability of accepting a job offer rises the higher the wage rate given the level of unemployment benefits.

The labor market is in equilibrium at  $W^*$  as there the number of workers firms are willing to hire is equal to the number of workers willing to accept a job offer. Note that there is still unemployment when the labor market is in equilibrium as AB workers are in the labor force but without a job. The unemployment that exists when the labor market is in equilibrium is known as the Natural Rate of Unemployment (NRU) and is of a voluntary nature.

If the wage rate (say, because of labor unions) is at  $W_1$  then HJ are unemployed (disequilibrium unemployment) of which HF are involuntarily unemployed and FJ are voluntarily unemployed (FJ is not the NRU!)

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