

Review Sheet for Exam #2

Exercise #1: Consider the following labor market data.

Table 1: Change in U.S. Employment March 2020- April 2020

	March 2020	April 2020
Population	259,758	259,896
Employed	155,772	133,403
Unemployed (ASW)	7,140	23,078
Part Time for Econ. Reasons	5,765	10,887
Discouraged Workers	514	574

i. Calculate the labor force participation rate in both months.

ii. Calculate the U-3 unemployment rate in both months.

iii. Calculate the U-6 unemployment rate in both months.

iv. How many unemployed workers would have to find jobs (compared to April 2020) to lower the unemployment rate to 5%?

v. How many unemployed workers would have to drop out of the labor force (compared to April 2020) to lower the unemployment rate to 5%?

vi. How would you tell if the increase in unemployment from March to April was due to worse macroeconomic conditions?

Exercise #2: Suppose that the economy starts at full employment where inflation equals its 2% target. Now suppose that the government lowers taxes.

i. Using the AS/AD model, show the short term impact on output and inflation.

ii. In the AS/AD model, when will changes in tax rates have the smallest effect on output.

iii. Using a model of the labor market, show the impact of lower taxes on unemployment.

iv. Using the AS/AD model, show how the economy eventually returns to the point where output equals potential output.

Exercise #3: Conceptual Questions on Money and Monetary Policy:

1. Why is the definition of money not limited to just currency (notes and coins)?
2. Why do we describe money as a social convention?
3. Can M2 ever be smaller than M1?
4. Why do many countries have independent Central banks conduct monetary policy?
5. What are the goals of Central Banks in conducting monetary policy.
6. Expansionary monetary policy increases aggregate demand. Given this, why don't Central Banks just conduct monetary policy aggressively enough to quickly and easily eliminate recessions?

Other Questions to help you prepare for the exam:

1. Why does the U-3 unemployment rate receive more attention than the u-6 rate? How do they differ?
2. Why are decreases in the unemployment rate sometimes seen as bad news?
3. Why did U.S. labor force participation increase in the 60s and 70s? Why has it declined over the past decade?
4. What might we learn by comparing average income to median income?
5. What are some events that increase aggregate supply?
6. What are some events that increase aggregate demand?
7. Why do most macroeconomists believe that aggregate labor markets are not well modeled by basic supply and demand?
8. The aggregate supply curve gets steeper as output increases. What does this tell us about the economy?
9. Why do most modern economies use fiat money?
10. What is commodity backed money?
11. What is the Fed's "dual mandate?"
12. Why is the Chairperson of the Fed selected by locking ten economists in a room with a pride of lions, and then choosing the last one left?
13. How has the way that the Fed sets interest rates changed since 2008?
14. Why do U.S. financial institutions hold reserves at the Fed?
15. True or False? Most households borrow at the Federal Funds rate in order to finance a home.
16. Why do so many Central Banks target 2% inflation?