

ECO 103, Winter 2015, Required Homework Assignment #6
Due at the start of class on Wednesday, April 8

Read the following material:

Krugman, Paul. March 31, 2015. "Missing Deflation and the Argument for Inflation." *The Conscience of a Liberal, New York Times Blog*

Bernanke, Ben. March 30, 2015. "Why are interest rates so low?" *BenBernanke's Blog, Brookings Institute*

Heath, Michael and Jeff Kearns. March 23, 2015. "Williams Says Fed Rate-Rise Discussion Should Begin Mid-Year." *Bloomberg Business*

1. Do these articles offer any support for the assumption in the AS/AD model that wages are sticky in the short run?
2. Why does Krugman think that the Fed's 2% inflation target may be too low?
3. What do you think is the Fed's motivation for possibly raising interest rates as early as June?
4. Suppose that the Fed does raise interest rates in June. Show the likely effects in the AS/AD model.
5. What do you think is the core disagreement that causes some people to think that the Fed should raise rates while others think that it should not?
6. In the AS/AD model, how can a severe recession lead to deflation?
7. Why does Krugman think that the Great Recession exhibited only minor deflation?
8. According to Bernanke, how do large budget deficits affect monetary policy?