

Problem Set Chapters 3 and 4 – Selected Assigned Problems Answers
GOUCHER COLLEGE
EC 217 - Intermediate Macro Theory
Spring 2015

Problem Set 3

Review Questions – Questions 12 and 13.

Analytical Problems – Questions 2 and 6.

Additional Problem: If you were appointed economic king, what policies would you implement to increase total factor productivity? Explain.

Answers to Problem Set 3

Review Questions

12. Frictional unemployment arises as workers and firms search to find matches. A certain amount of frictional unemployment is necessary, because it is not always possible to find the right match right away. For example, an unemployed banker may not want to take a job flipping hamburgers if he or she cannot find another banking job right away, because the match would be very poor. By remaining unemployed and continuing to search for a more suitable job, the banker is likely to make a better match. That will be better both for the banker (since the salary is likely to be higher) and for society as a whole (since the better match means greater productivity in the economy).
13. Structural unemployment occurs when people suffer long spells of unemployment or are chronically unemployed (with many spells of unemployment). Structural unemployment arises when the number of potential workers with low skill levels exceeds the number of jobs requiring low skill levels, or when the economy undergoes structural change, when workers who lose their jobs in shrinking industries may have difficulty finding new jobs.

Analytical Problems

2. (a) An increase in the number of immigrants increases the labor force, increasing employment and increasing full-employment output.
- (b) If energy supplies become depleted, this is likely to reduce productivity, because energy is a factor of production. So the reduction in energy supplies reduces full-employment output.
- (c) Better education raises future productivity and output, but has no effect on current full-employment output.
- (d) This reduction in the capital stock reduces full-employment output .

6. Yes, it is possible for the unemployment rate and the employment ratio to rise during the same month. For example, suppose the population falls, the labor force is constant, the number of unemployed rises, and the number of employed falls (but by less than the decline in population). Then the unemployment rate rises, since there are more unemployed but the same labor force, but the employment ratio rises, since population declines more than employment does.

Yes, it is possible for the participation rate to fall at the same time that the employment ratio is rising. For example, suppose that population is constant, the labor force declines, employment rises, and unemployment falls. The participation rate falls, since there are fewer people in the labor force from the same population. The employment ratio is rising, since employment rises while population is constant.

Problem Set 4

Review Questions – Question 10.

Additional Problems:

1. Should the Government Reduce Taxes on Capital?
2. Is Saving Too Low in the United States?
3. Should Social Security Funds Be Invested in the Stock Market?

Answers to Problem Set 4

Review Questions

10. The saving curve slopes upward because saving is assumed to increase with an increase in the expected real interest rate. The investment curve slopes downward because investment is lower the higher is the expected real interest rate. The saving curve would be shifted to the right by an increase in current output, a decrease in expected future output, a decrease in wealth, a decrease in government purchases, and possibly by a rise in taxes. The investment curve would shift to the right by a decline in the effective tax rate or a rise in expected future marginal product of capital