

Write your name on the cover of the test booklet and nowhere else. Enclose this sheet with the booklet. Failure to follow these directions will cost you 1 point. The test has 150 points (to be scaled up to 210 points) and is scheduled to take 74 minutes. Therefore, expect to spend 1 minute for every 2 points. For example, a 12-point question should take 6 minutes. I can give some extra time but not much.

1) (12 points) Answer EITHER Part A OR Part B.

A) When we went through examples of people changing their employment status, the labor force participation rate almost never changed. Why? What did change it? Why did that affect it?

B) Why isn't full employment 0%? Explain your logic mentioning appropriate categories of unemployment.

2) (12 points) Answer EITHER Part A OR Part B.

A) Why might durable goods cause problems for Friedman's Permanent Income Model? Explain your logic.

B) The current unemployment rate is 4.9%. The current labor force participation rate is about 3 percentage points less than it was a decade ago. Given those two facts, is our unemployment rate too low, about correct, or too high? Explain your logic. Make sure you state what you think is the main cause of the labor force participation rate going down.

3) (16 points) Explain EITHER $S_{PVT} = (Y + NFP + TR + INT - T) - C$ OR $c_1 = (y + a_0 - c_0)(1+r) + y_1$.

4) (18 points) Answer EITHER Part A OR Part B.

A) State the two effects that result in the slope of the labor supply curve. Explain how they combine to give us our labor supply curve. Which effect is bigger? Explain your logic.

B) Give an example of a pure income effect for the labor supply/demand diagram. Illustrate the effects on the graph and explain why it moved as drawn.

5) (18 points) Answer EITHER Part A OR Part B.

A) Draw the inter-temporal budget constraint. Illustrate the effects of a decrease in the interest rate. Explain why the curve moves as drawn.

B) Draw the inter-temporal budget constraint. Choose a point where you are saving some now. Explain how you know you are saving some. Illustrate the effects of a stock market crash. Explain why the curve moved as drawn. Given your diagram, would you expect saving to increase or decrease? Explain your logic.

6) (18 points) Answer EITHER Part A OR Part B.

A) Draw Modigliani's Life-Cycle Model diagram. Explain how you found the level of consumption. Why did you find it that way?

B) In December of 2011, Congress and the Obama Administration combined extended the payroll tax cut for two months. Illustrate this on Modigliani's Life-Cycle Model. Explain why the lines moved as drawn. Do you think it stimulated the economy? Why or why not?

7) (22 points) Answer EITHER Part A OR Part B.

A) Use the following data to calculate GDP, GNP, NNP, NI, PI, and DPI. Consumers buy \$1200 worth of goods. Firms buy \$600 worth of machines. The government buys \$700 worth of services. We import \$220 worth of goods and export \$170 worth. We paid foreigners \$10 worth of interest and received \$12. Capital lost \$40 worth of value. Firms received \$18 worth of subsidies, paid \$120 dollars of sales tax, and \$30 worth of business taxes. They retained \$25 of earnings. Consumers paid \$220 worth of income

tax and received \$140 worth of Social Security payments from the government. Show all work. If you need data which is not provided, assume it is zero.

B) For each of the following events, what happens to GDP? Explain your logic including which part of GDP is affected. If GDP is not affected, explain why it is not affected. I sell my car on e-Bay for \$5000. I buy shoes made in Brazil for \$99 which cost Macy's \$59. The government \$1 billion to repair the Pentagon after 9/11. (Assume it was all paid in the same year.)

8) (34 points) Answer EITHER Part A OR Part B.

A) Draw the production function with labor on the axis and draw the labor supply/labor demand diagram. Illustrate the effects of an expected increase in the income tax next year. Explain why the curve(s) moved. Show the starting and ending points and state how you found them.

B) Draw the production function with labor on the axis and draw the labor supply/labor demand diagram. Illustrate the effects of an expected increase in the amount of capital. Explain why the curve(s) moved. Show the starting and ending points and state how you found them.