

## ■ PROBLEMS Chapter 16

1. In columns 1 and 2 of the table below is a portion of a short-run aggregate supply schedule. Column 3 shows the number of full-time workers (in millions) that would have to be employed to produce each of the seven real domestic outputs (in billions) in the short-run aggregate supply schedule. The labor force is 80 million workers and the full-employment output of the economy is \$\_\_\_\_\_.

a. If the aggregate demand schedule were that shown in columns 1 and 4,

(1) the price level would be \_\_\_\_\_ and the real output would be \$\_\_\_\_\_.

(2) the number of workers employed would be \_\_\_\_\_, the number of workers unemployed would be \_\_\_\_\_ million, and the unemployment rate would be \_\_\_\_\_%.

b. If aggregate demand were to increase to that shown in columns 1 and 5 and short-run aggregate supply remained constant,

(1) the price level would rise to \_\_\_\_\_ and the real output would rise to \$\_\_\_\_\_.

(2) employment would increase by \_\_\_\_\_ million workers and the unemployment rate would fall to \_\_\_\_\_%.

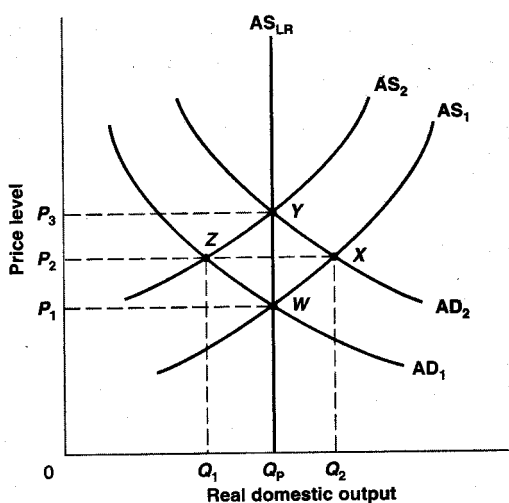
(3) the price level would increase by \_\_\_\_\_ and the rate of inflation would be \_\_\_\_\_%.

c. If aggregate demand were to decrease to that shown in columns 1 and 6 and short-run aggregate supply remained constant,

(1) Price level	(2) Real output supplied	(3) Employment (in millions)	(4) Real output demanded	(5) Real output demanded	(6) Real output demanded
130	\$ 800	69	\$2300	\$2600	\$1900
140	1300	70	2200	2500	1800
150	1700	72	2100	2400	1700
160	2000	75	2000	2300	1600
170	2200	78	1900	2200	1500
180	2300	80	1800	2100	1400
190	2300	80	1700	2000	1300

- (1) the price level would fall to \_\_\_\_\_ and the real output would fall to \$\_\_\_\_\_.  
 (2) employment would decrease by \_\_\_\_\_ compared with situation **a**, and workers and the unemployment rate would rise to \_\_\_\_\_%.  
 (3) the price level would decrease and the rate of inflation would be (positive, negative) \_\_\_\_\_.

2. The following is an aggregate demand and aggregate supply model. Assume that the economy is initially in equilibrium at **AD<sub>1</sub>** and **AS<sub>1</sub>**. The price level will be \_\_\_\_\_ and the real domestic output will be \_\_\_\_\_.



**a.** If there is demand-pull inflation, then

- (1) in the short run, the new equilibrium is at point \_\_\_\_\_, with the price level at \_\_\_\_\_ and real output at \_\_\_\_\_;  
 (2) in the long run, nominal wages will rise so the aggregate supply curve will shift from \_\_\_\_\_ to \_\_\_\_\_. The equilibrium will be at point \_\_\_\_\_ with the price level at \_\_\_\_\_ and real output at \_\_\_\_\_, so the increase in aggregate demand has only moved the economy along its \_\_\_\_\_ curve.

**b.** Now assume that the economy is initially in equilibrium at point **W**, where **AD<sub>1</sub>** and **AS<sub>1</sub>** intersect. If there is cost-push inflation, then

- (1) in the short run, the new equilibrium is at point \_\_\_\_\_, with the price level at \_\_\_\_\_ and real output at \_\_\_\_\_.  
 (2) if the government tries to counter the cost-push inflation with expansionary monetary and fiscal policy, then aggregate demand will shift from \_\_\_\_\_ to \_\_\_\_\_, with the price level becoming \_\_\_\_\_.

\_\_\_\_\_ and real output \_\_\_\_\_, but this policy has a trap because the price level has shifted from \_\_\_\_\_ to \_\_\_\_\_ and the new level of inflation might shift \_\_\_\_\_ leftward. (3) if government does not counter the cost-push inflation, the price level will eventually move to \_\_\_\_\_ and real output to \_\_\_\_\_ as the recession reduces nominal wages and shifts the aggregate supply curve from \_\_\_\_\_ to \_\_\_\_\_.

c. Now assume that the economy is initially in equilibrium at point **Y**, where **AD<sub>2</sub>** and **AS<sub>2</sub>** intersect. If there is a recession that reduces investment spending, then (1) aggregate demand decreases and real output shifts from \_\_\_\_\_ to \_\_\_\_\_, and, assuming that prices and wages are flexible downward, the price level shifts from \_\_\_\_\_ to \_\_\_\_\_.

(2) these events cause real wages to (rise, fall) \_\_\_\_\_, and eventually nominal wages \_\_\_\_\_ to restore the previous real wages.

(3) when this happens, the short-run aggregate supply curve shifts from \_\_\_\_\_ to \_\_\_\_\_ to its new equilibrium at point \_\_\_\_\_. The equilibrium price level is \_\_\_\_\_ and the equilibrium level of output is \_\_\_\_\_ at the long-run aggregate supply curve \_\_\_\_\_.