

CH.24 EXTRA QUESTIONS

1. Classicals saw the Depression as a political problem, not an economic problem. Why?
2. Did Keynesian or Classical economics support laissez-faire policy?
3. Would Keynesian or Classical economists be more likely to emphasize the fallacy of composition?
4. As the problem of inflation grew in the 1970s, did Keynesian or Classical economics grow in importance?
5. Is structural stagnation a Keynesian or a Classical theory?
6. In what way is potential output not purely a physical measure based on the number of workers and existing factories?
7. What are two ways in which long-term economic growth is measured?
8. What has happened to growth rates in Western Europe and the United States in recent years?
9. How does the U.S. per capita growth rate since 1940 compare to growth rates in other areas around the world?
10. Draw a representative business cycle, and label each of the four phases.
11. How does a structural stagnation differ from a recession?
12. Which has the more pessimistic view of the problems facing the U.S. economy: structural stagnation theory or conventional business-cycle theory?
13. Distinguish between structural unemployment and cyclical unemployment.
14. What type of unemployment is best studied within the long-run framework?
15. What type of unemployment is best studied under the short-run framework?
16. Suppose the total labor force is 189 million of a possible 244 million working-age adults. The total number of unemployed is 15 million. What is the standard unemployment rate?
17. Does the standard unemployment rate underestimate or overestimate the unemployment problem? Explain.

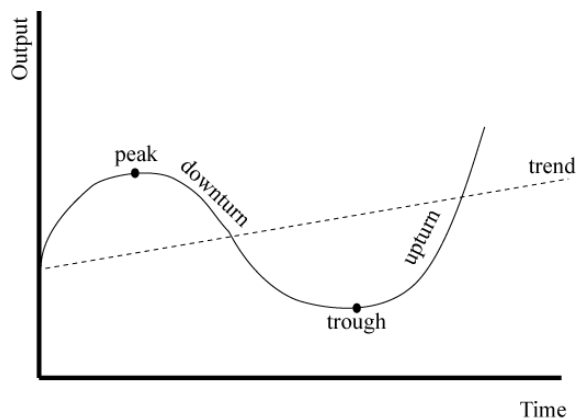
18. Using only a pencil and paper, who is most likely to calculate the square root of 4,959 to three decimal places more quickly—you or your grandparents? What does that tell you about jobs in the future?

19. How will concerns in the future about employment likely change with the information revolution?

Answers

1. Classical economists felt that if the wage level fell, the Depression would end. They saw labor unions as preventing the fall in wages, and they believed that the government lacked the political will to break up unions.
2. Classical economics supported laissez-faire policies because they believed business cycles were temporary glitches which the market would correct.
3. Keynesian economists are more likely to emphasize the fallacy of composition. The fallacy of composition is the false assumption that what is true for a part will also be true for the whole. Keynes carefully distinguished the adjustment process for a single market from the adjustment process for the aggregate economy, arguing that the effects differ significantly between the two.
4. Classical economics grew in importance in the 1970s because Keynesians didn't have a model for inflation, whereas Classical did.
5. Structural stagnation is neither a Keynesian nor a Classical theory. It includes elements of both. Structural stagnation occurs in the time period between the long run Classical analysis and the short run Keynesian analysis, so both analyses are needed to model it.
6. Potential output is the highest amount of output an economy can sustainably produce and sell using existing production processes and resources. Potential output is not purely a physical measure because unemployed workers do not contribute to potential output, factories may be technologically obsolete, and production must be sustainable to be equal to potential.
7. Economic growth is measured by changes in total output and changes in output per person.

8. Growth has slowed in recent years in both Western Europe and the United States.
9. From 1940 to 1970 the U.S. economy grew at a rate of about 2.5 percent per year, which was lower than Western Europe and Japan but higher than many other countries. In the following decades, U.S. growth was higher than most except for India and China, which have experienced considerable growth. Since 2000 the U.S. economy has been slower than many countries, averaging about 2 percent per year in the first decades of the 2000s.
10. A representative business cycle is shown in the accompanying graph. Each of the four phases—peak, downturn, trough, and upturn—is clearly labeled.



11. Structural stagnation is a period of protracted slow growth and high unemployment. Because the expansion of the economy is slow with structural stagnation, the economy does not return to its long-term trend. In contrast, a recession is a short period of declining output followed by an expansionary period that returns the economy to its long-term trend.
12. The structural stagnation theory is more pessimistic because it argues that the economy must undergo structural changes before it will return to its long-term growth trend. An example is that with structural stagnation, workers will have to accept lower wages or learn new skills before the economy returns to its potential. In the conventional business cycle view, the economic recession is short-lived as those who become unemployed will be rehired without having to accept lower wages or learn new skills.

13. Structural unemployment is unemployment caused by the institutional structure of an economy or by economic restructuring making some skills obsolete, whereas cyclical unemployment is unemployment resulting from fluctuations in economic activity. A fall in structural unemployment requires structural changes; a fall in cyclical unemployment does not.
14. Structural unemployment, which results from changes in the structure of the economy, is best studied in the long-run framework. Cyclical unemployment goes up and down with the business cycle.
15. Cyclical unemployment, which results from fluctuations in economic activity, is best studied in the short-run framework. Cyclical unemployment goes up and down with the business cycle. Structural unemployment is caused by the institutional structure of an economy and economic restructuring, and therefore is best studied in the long-run framework.
16. The unemployment rate is the total number of unemployed as a fraction of the labor force.

Unemployment rate = (Number of unemployed/Labor Force) $\times$ 100.

Unemployment rate = (15/189) $\times$ 100 = 7.9%

17. Some economists argue that the standard unemployment rate underestimates unemployment because people who have gotten frustrated and stopped trying to find jobs are not counted as unemployed. Also, the standard unemployment rate doesn't include people who are underemployed such as people who are working part-time but would like to work full-time. Others point out that, because of unemployment insurance, people often say they are looking for work when they really aren't, and therefore unemployment is overstated. Furthermore, these economists believe that people could find a job if they really wanted to and instead turn down jobs they find unappealing. So, there are tendencies both to overestimate and underestimate the problem.

The official measure of unemployment is based on judgments about who should be counted as unemployed. Keynesians argue that discouraged workers who would like jobs but have left the labor force should be included in the measure of unemployment because there is a lack of decent jobs and affordable transportation. Classicals believe that some of those counted as unemployed are choosing to be unemployed and should not be counted.

18. You are much more likely to be able to calculate this problem quickly with the use of a calculator, but your grandparents didn't have calculators at their disposal, so they learned to do such calculations by hand. While your grandparents may have been employed in “calculator” jobs, working to solve equations and functions by hand, any teenager today can quickly compute the answer on the calculator programmed into almost all of today’s phones. The jobs your grandparents once held are now obsolete, performed more efficiently and productively by algorithms.

This example is indicative of a coming change that will likely impact a vast array of job sectors. Positions that once required human know-how will soon be replaced by algorithms and intelligent software. In the future, as the skills required to perform many mid-level professional jobs are instead done by computers and algorithms, more humans will be most needed to act as technicians, completing any work that may have been missed by the computer and monitoring the software. As learning-based software continues to improve, even the programmers that are needed to code algorithms may be replaced by automated systems that perform the job more efficiently. New jobs will be forthcoming, but they will likely be quite different jobs than we currently have.

19. As the information revolution outpaces human intelligence and replaces most mid-level mental strength jobs with computer algorithms, the nature of the jobs will change. In the future, low- and mid-level, mundane technician jobs will likely be replaced with algorithms. High-level jobs for the super intelligent will exist—designing algorithms that design algorithms, and supplemental jobs cleaning up the issues that are not efficiently done by algorithms will also be available as well many service jobs that are not doable by robots. There will likely be jobs for all, but these jobs will likely require a different education than students currently have.