

1. Economic activity moves from a period of expansion to a \_\_\_\_\_ and then moves into a period of \_\_\_\_\_ until it reaches a \_\_\_\_\_.
- A. peak; expansion; trough
  - B. peak, recession; trough
  - C. trough; expansion; peak
  - D. trough; recession; peak
2. Industrial production, total sales, nonfarm employment, and after-tax household income are examples of \_\_\_\_\_ indicators of economic activity.
- A. coincident
  - B. preceding
  - C. lagged
  - D. real
3. When recessions are the result of slowing growth in potential output, the government's best response is a policy to:
- A. increase aggregate demand.
  - B. decrease aggregate demand.
  - C. promote saving and investment.
  - D. reduce government spending.
4. Changes in the growth rate of potential output and deviations of actual output from potential output are two logical explanations for:
- A. the decline in the natural rate of unemployment.
  - B. short-term economic fluctuations.
  - C. increasing wage inequality.
  - D. skill-biased technological change.
5. If the output gap equals -\$200 million, then
- A. cyclical unemployment equals the sum of structural and frictional unemployment.
  - B. there is a recessionary gap.
  - C. there is no cyclical unemployment.
  - D. potential GDP is less than actual GDP.

6. If the cyclical rate of employment equals 1% and the actual rate of unemployment equals 8%, then the natural rate of unemployment must equal:

- A. -10%.
- B. 9%.
- C. 1%.
- D. 7%.

$$v - v^* = \text{Cyclical}$$
$$8 - v^* = 1$$

7. Compared to older workers, younger workers change jobs more frequently, so they are more prone to \_\_\_\_\_ unemployment and have fewer skills, so they are more prone to \_\_\_\_\_ unemployment.

- A. cyclical; frictional
- B. frictional; structural
- C. structural; frictional
- D. frictional; cyclical

8. According to Okun's Law, each extra percentage point of \_\_\_\_\_ unemployment is associated with a \_\_\_\_\_ percentage point increase in the output gap, measured in relation to potential output.

- A. frictional; 2
- B. frictional; 4
- C. cyclical; 2
- D. cyclical; 4

9. According to Okun's Law, when cyclical unemployment increases from 1 to 2 percent, the output gap increases from \_\_\_\_\_ percent.

- A. -2 to -4
- B. -1 to -2
- C. 3 to 4
- D. 1 to 2

$$\frac{Y - Y^*}{Y^*} \times 100 = -2(v - v^*)$$

10. If the natural rate of unemployment is 4 percent, what is the actual rate of unemployment if output is 2 percent below potential?

- A. 2%
- B. 4%
- C. 5%
- D. 6%

$$-2 = -2(v - 4)$$
$$v = 5$$

11. In Macroland, a country that operates according to Okun's law, potential GDP equals \$10 trillion, the actual rate of unemployment is 8 percent, and the natural unemployment rate is 6 percent. What is real GDP in Macroland?

- A. \$9.6 trillion
- B. \$9.8 trillion
- C. \$10 trillion
- D. \$10.2 trillion

$$\frac{Y - 10}{10} \times 100 = -2(2)$$

$$Y = -0.4 + 10$$

12. If the actual rate of unemployment equals the natural rate of unemployment, then:

- A. potential output is greater than real GDP.
- B. potential output equals real GDP.
- C. potential output is less than real GDP.
- D. there is a recessionary gap.

13. In the long run, output gaps are eliminated by:

- A. reducing potential output.
- B. increasing potential output.
- C. price changes.
- D. increased efficiency in labor markets.

14. If firms maintain preset prices in the short run, then the primary cause of outputs gaps is changes in:

- A. potential output.
- B. prices.
- C. capital and technology.
- D. ~~economywide~~ spending.

15. Two possible explanations for the decline in the natural rate of unemployment in the United States over the past twenty years are:

- A. the changing age structure of the population and more efficient labor markets.
- B. advances in computer technology and globalization.
- C. increasing wage inequality and skill-biased technological change.
- D. greater quantities of human capital and increased average labor productivity.