

Do not write your name on the assignment. Write your name only on the back of this sheet of paper and staple your answers on the front of this sheet of paper. Your assignment will be typed, except graphs can be drawn by hand and mathematical equations can be done by hand. Failure to follow these directions will cost you 1 point on the assignment and failure to type it will cost you 10 points.

1) (15 points) Explain the equation $i = r + \pi + r\pi$. Make sure you explain why all three terms are there and what they represent.

2) (35 points each) Illustrate the following events on BOTH the labor supply/labor demand diagram and on the production function diagram with labor on the x-axis. Explain why the curve(s) moved as drawn and state what happens to the wage, level of employment and GDP.

A) There is an increase in the amount of capital.

B) The wealth of the country increased.

3) (15 points) Why might a decrease in the unemployment rate indicate the economy is doing worse?