

This review sheet is intended to cover everything that could be on the exam; however, it is possible that I will have accidentally left something off. You are still responsible for everything in the chapters covered except anything that I explicitly say you are not responsible for. Therefore, if I left something off of this sheet, it can still be on the exam. There will be no multiple-choice questions. Most of the questions will be like the ones in the homework assignments, and possibly a few definition questions, but I am more likely to ask questions that make you use the definitions rather than recite them. I will probably ask one of the questions from the book at the end of the chapters.

The review session will be at a time to be determined in class.

Chapter 5: What are **negative externalities** and **positive externalities**? How are they seen on the graph? What is the best way to offset them? Show that on the supply and demand diagram. Know the economic reasons for **providing a legal system, promoting competition, providing public goods, and income redistribution**. Know what **government sponsored** and **government deterred goods** are. What is the difference between **voting** and **spending**?

Chapter 6: How do we calculate **marginal tax rate, average tax rate, and total taxes paid**? What is meant by **proportional, progressive, and regressive taxes**? What is the **tax base**? How can increasing a tax result in less revenue? What are **sales, excise, ad valorem, and specific (unit) taxes**? What is the **Laffer Curve**? The book actually draws it in Chapter 13. What are **Medicare** and **Social Security**? What are their effects on the economy? What is the problem with Social Security? What are some of the proposals for solving the problem? What are the pluses and minus of using each “solution”? I am most likely to give you a proposal for a solution and ask you how it would work, and whether or not you would implement my proposal.

Chapter 7: What are, and how do we calculate, the **unemployment rate, labor force participation rate, and inflation rate**? What are **stocks** and **flows**? How do they relate to unemployment rates? Know how to classify people by the reason they are unemployed, i.e., laid off, job leaver, etc. Know how to tell who is in which category of unemployment, i.e., **frictional, structural, seasonal, and cyclical**. What is the **natural rate of unemployment, a.k.a., full employment unemployment rate**? How do **discouraged workers** and **underemployment** complicate the unemployment picture? What are the other costs of unemployment besides lowered production? How do we calculate **CPI, PPI, PCE Index** and **GDP deflator**. I won't ask you to do the calculation, but you may have to describe how it is done. Know how to calculate inflation from those numbers. Why does it matter if inflation is anticipated or unanticipated? What are the **costs of unanticipated and anticipated inflation**? (I added **shoe leather costs**.) Note that if inflation is expected to be 10% and it ends up being 7%, we had unexpected **deflation** of 3% and that hurts borrowers. Know what an **expansion (a.k.a. boom), contraction, recession, depression, trough, and peak** are. What is a **leading indicator**?

Chapter 8: What is the simple **circular flow**? What do we mean by product markets and factor markets? Know what is calculated in **GDP** and what is not. That method is the **expenditure method (C+I+G+X)**. Remember that “X” can be negative and that *you are likely to get the definition of “I” wrong. Stocks and bonds are not investments.* Ignore inventory investment. It is very small and confusing. Why should GDP calculated this way equal the **sum of the incomes and the sum of the value added**? What are some problems with trying to calculate GDP? What are some of the limitations in our understanding the meaning of different levels? Ignore GDI because they state it is the same as GDP, just calculated differently. Know how to get from **GDP to NDP, NI, PI, and DPI**. Note that if you know what those terms are trying to measure, you ought to be able to figure out what is added and what is subtracted. Capital consumption allowance is another way to calculate depreciation. What is the difference between **real and nominal GDP**? Ignore the chain-weighted measure for real GDP. How do we compare GDP across countries?

Non-graded Homework Assignment #4A to be reviewed with Assignment #4.

- 1) (5 points) Suppose the nominal interest rate you are earning at your bank is 15% and the inflation rate is 10%, calculate the real interest rate. Show all work.
- 2) (20 points) Suppose the price level at the beginning of the year was 200 and at the end of the year it was 210. What was the inflation rate? Show all calculations. If people had expect an inflation rate of 10%, who would gain and who would lose from this? Explain your logic.
- 3) (10 points each) For each event, tell me how much GDP changes and which part of GDP is changing. Explain your logic.
 - A) I pay you \$50 to shovel my driveway.
 - B) You buy \$500 worth of Google stock paying \$9 in commissions.
 - C) Bethany College renovated Cochran Hall. Pretend it cost \$200,000.
 - D) The government pays your grandmother \$500 in Social Security.
 - E) The government pays President Obama's salary of \$30,000 this month.
 - F) You buy a used car for \$3000 which cost the dealer \$1800.
- 4) (15 points) Explain three reasons why real GDP per capita is not a good measure of how much we produce per person.