

- c) Cyclical unemployment is caused by a mismatch of worker skills and the labor requirements of employers.
- d) Frictional unemployment is unemployment that changes with the seasons.
- e) none of the above.

3. Which statement is true?

- a) Given the consumer basket adjusts regularly, the CPI accounts for changes in product quality.
- b) The substitution bias in the CPI tends to underestimate inflation.
- c) Given frequent updating of the representative consumer basket, the inclusion of new products tends to moderate inflation.
- d) Changes in prices, when they reflect an improvement in product quality, tend to cause an overestimation in changes in the cost of living.
- e) None of the above

Q7: For each of the following scenarios, state whether the unemployment is frictional, structural, or cyclical. Justify your answer.

- a) Nadeem lost his job when the steel mill closed down. He lacks the skills to work in another industry and so has been unemployed over a year.
- b) Aliya was laid off from her job at the auto plant because the recession reduced the demand for cars. She expects to get her job back when the economy picks up.
- c) Waqar is an unskilled worker who works for local moving companies during their busy seasons. The rest of the year he is unemployed.
- d) Tauqeer looked for a job for six weeks after finishing college. He turned down a couple of offers because they didn't let him use the skills he had acquired in university, but now he has a job in the area that he trained for.
- e) Qandeel, a software engineer, lost her job when the start-up company she was working for went bankrupt. She interviewed at five companies before accepting a new job in another firm in the same industry.

Q8: What are the key assumptions of the Keynesian model? Explain why this assumption is needed if one is to accept the view that aggregate spending is a driving force behind short-term fluctuations.

Q9: The government is considering two alternative policies, one involving increased government purchases of 50 units, the other involving tax cuts of 50 units. Which policy will stimulate planned aggregate expenditure more? Why?

*****GOOD LUCK*****