Chapter 9 Problems

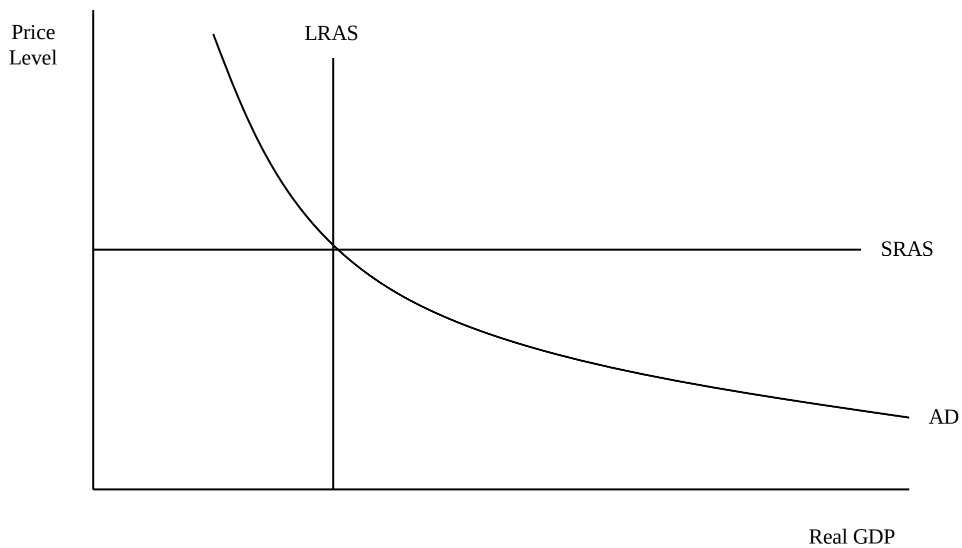
1 Let's employ the SRAS/LRAS/AD curve to analyze the events of September 11th. The terrorist attacks of September 11th caused great pessimism among consumers and, due to their fear of the future, seemed to inhibit consumer spending.

a. How does the decrease in consumer confidence effect the aggregate demand curve? Explain using the Quantity Theory of Money (MV = PY).

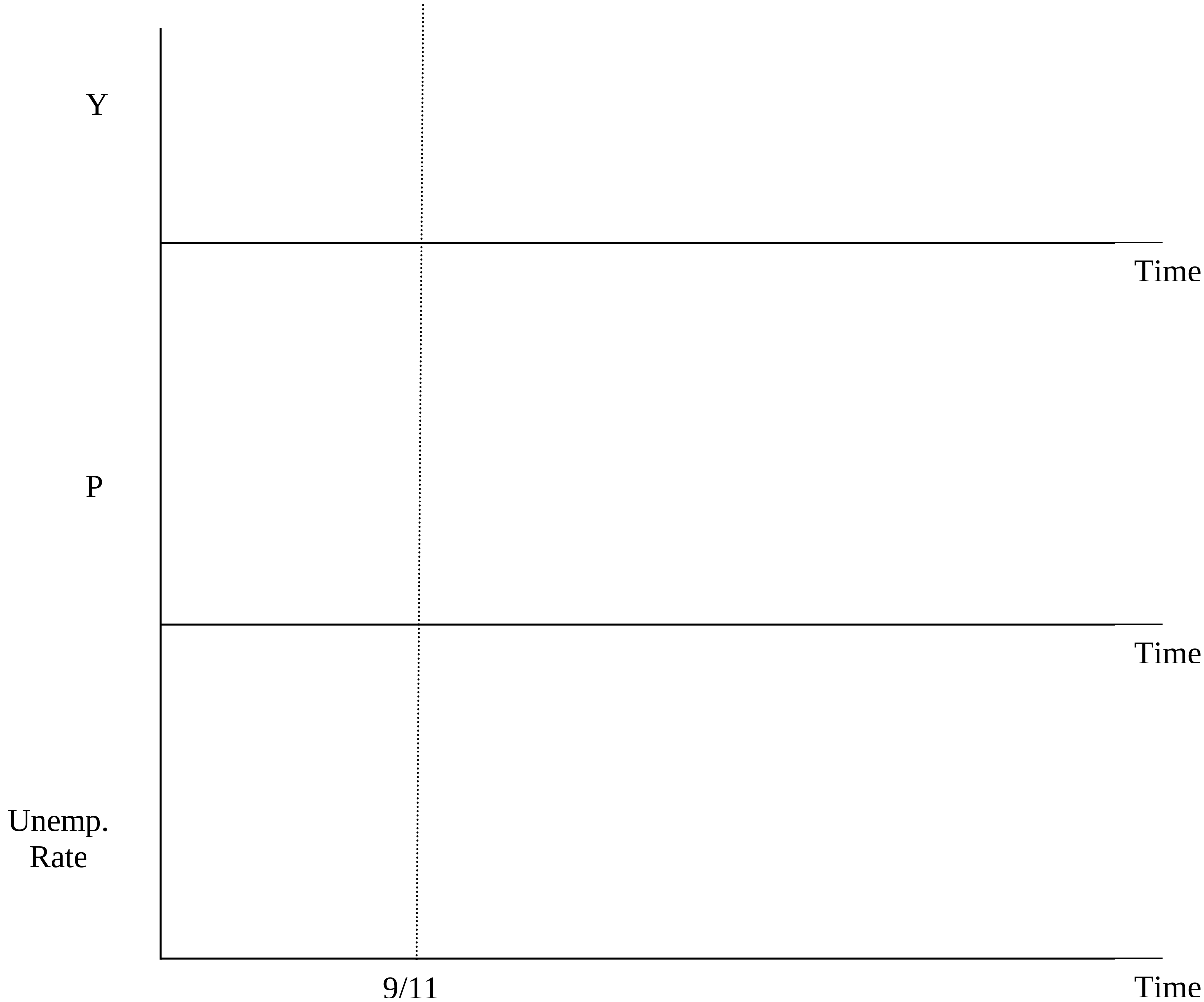
b. How does the decrease in consumer confidence effect the short run aggregate supply curve?

c. How does the decrease in consumer confidence effect the long run aggregate supply curve?

d. Plot the effect of the decline of consumer confidence on the graph below:



e. On the plots below, sketch the effect of the decline in consumer confidence on output, unemployment, prices, real, and nominal interest rates. Be sure to include short, and long run effects.



f. Some monetary authorities have high tolerance for changes in prices and others have low tolerance for changes in prices. Use the table below to contrast two monetary authorities; one of which values price stability and the other that values output stability. How would each monetary authority respond to the events of September 11th.

Monetary Authority (MA)	**How would the MA change the Money Supply?**	**Given the MA's policy, How does the AD change?**	**What is the effect on Output in the SR of the MA policy?**	**What is the effect on Output in the LR of the MA policy?**	**What is the net effect on Output of both the Sept. 11 and MA events?**
Price Stability					
Output Stability					