

Chapter 28

1. Use the following information about Employment Country to answer question 1. Numbers are in millions.

	2004	2005
Population	223.6	226.5
Adult population	168.2	169.5
Number of unemployed	7.4	8.1
Number of employed	105.2	104.2

- a. What is the labour force in 2004 and 2005?
- b. What is the labour force participation rate in 2004 and 2005?
- c. What is the unemployment rate in 2004 and 2005?
- d. From 2004 to 2005, the adult population went up while the labour force went down. Provide a number of explanations why this might have occurred.
- e. If the natural rate of unemployment in Employment Country is 6.6 per cent, how much is cyclical unemployment in 2004 and 2005? Is Employment Country likely to be experiencing a recession in either of these years?
2. Suppose the labour market is segmented into two distinct markets: the market for low-skill workers and the market for high-skill workers. Further, suppose the competitive equilibrium wage in the low-skill market is €3.00/hour while the competitive equilibrium wage in the high-skill market is €15.00/hour.
- a. If the minimum wage is set at €5.00/hour, which market will exhibit the greatest amount of unemployment? Demonstrate it graphically in Exhibit 1.

Exhibit 1



- b. Does the minimum wage have any impact on the high skill market? Why?
 - c. Do your results seem consistent with labour market statistics? Explain.
 - d. Suppose the high-skill market becomes unionised and the new negotiated wage is €18.00/hour. Will this have any affect on the low skill market? Explain.
3. Answer the following questions about the composition of unemployment.
- a. What are some of the sources of unemployment?
 - b. Which type of unemployment is initiated by the firm?
 - c. Why might a firm pay wages in excess of the competitive equilibrium?
 - d. Which type of efficiency wage is unlikely to be relevant in the west European economies? Why?
 - e. How does frictional unemployment differ from the other sources of unemployment?