MACROECONOMICS AT WORK EXERCISE

PRODUCTIVITY

REFERENCE: **‘Fed fears slowing work rate’** (by Greg Ip), *Australian Financial Review [from The Wall Street Journal],* 25 January 2005, p.11.

CHAPTERS RELEVANT TO THIS EXERCISE: 9, 16

CONTEXT

The productivity of an economy as a whole refers to ratio of output (total production) that can be produced from a given level of input (the resources that an economy possesses). It is *increases* in productivity that enable *economic growth* to occur, or in other words, for there to be increases in GDP per person over the long term. Macroeconomics is in part about *short-term* fluctuations around the long-term growth path. But it is also concerned with the determinants of that long-term growth path (which set the economy’s *potential* rate of growth in GDP in the long term). In determining appropriate monetary policy in the short term a central bank must also consider long-term factors (for every point in the short term is also a point in the long term!). This article is about productivity trends in the US and their implications for short-term policy.

QUESTIONS

1. Summarise the way in which the concept of ‘productivity’ is explained in the article.

2. Explain the comment in the article that productivity growth determines an economy’s ‘speed limit’.

3. Why might faster productivity growth ease the pressure on inflation?

4. What is the magnitude of the ‘productivity slowdown’ in the US referred to in the article?

5. Explain the suggestion in the article that faster productivity growth allows a ‘looser monetary policy’ to be pursued.

6. What is behind the slowdown in productivity observed in the article?