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recitation_IS19_20160224_Seg01.pdf

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Participants: IS19 (boy, blue and white shirt), S1 (male student, not pictured), S2 (male student, not pictured), S3 (male student, not pictured), S4 (male student, not pictured), S5 (male student, not pictured), S6 (male student, not pictured)

Context: IS19 is teaching a recitation at the whiteboard.

0:00
xxx IS19: so okay now let’s begin our recitation.
xxx but first I want to (. ) tell you my r- my new office hour,
xxx I’ve already posted this on blackboard
xxx under the announcements,
xxx and I want to just remind-
xxx remind you once more just in case.
xxx so now it’s on Monday, from one thirty to two thirty,
xxx yeah and (. ) the other one is on Tuesday,
xxx four to five pm,
xxx they are in the same room
xxx s six twenty
xxx at the sbs building.
xxx so
xxx now let’s begin to talk about this week’s homework.
xxx so.
xxx so the first ((undecipherable)),
xxx so now the question is that one ((undecipherable))
xxx ((undecipherable)) from the present into the future.
xxx so what is this-
xxx what is this (cause) for this function of money.
xxx so as we know uh
xxx money has three functions.
xxx ((undecipherable))
xxx so (. ) the first one is (.2)
xxx uh (. ) store of value
xxx and the second one is the function as (. ) medium of
xxx exchange
xxx (.2) and the third one is as (.)
xxx a unit (. ) of (. ) account.
xxx and from the textbook we can see that,
xxx um. the statement in this question is just um the-
xxx the definition of the function of this store of value.
xxx that it transfers ((undecipherable)) and power
xxx from the present into the future.
xxx that means that if you hold the money,
then you can buy uh any good (.) at-at any time.
or you can buy it (at the moment), or buy it in the future.
and- (.)
so that’s- that’s why it’s called the store of value.
so.
Um.
that means um:
for example if you choose to hold the money,
then-then maybe
uh one month later, you can buy
uh (.) approximately the same amount of good.
but if you choose to hold some uh physical good
for example such as the apple,
then the apple may-may turn bad,
after a month.
so:
it is not a very good way to store the value.
and (.) holding the money is-
relatively an easy way to- to hold the value.
so that’s for the function (as) the
store of value.
and the second one is the medium of exchange
that means that we can use the money to buy goods or
services.
so.
for example if you only hold the apples,
then if you want to buy some pears,
then (.) the-
the individual who owns the pears may not want your apples.
so the transaction may not (.) happen.
but if you take- hold the money,
3:01
then the money can serve as a medium of exchange
and you can buy any good as you want.
so that is its function as a medium of exchange.
and
the third one is the-
uh is the unit of account.
so a-all the prices are
labeled by the-by-uh- by the money
and- or it can be used to record the (data).
so uh for example a car may be uh
twenty thousand dollars
and uh an apple may be one dollars.
so (. ) that’s the third function of money.
so now let’s go through the four questions
the first one is store of value which is the right choice.
and the third and fourth is the other two functions of money.
and for b uh in the index of inflation,
so money is now tied into the index of inflation.
so
so can you name another index (. )
that can serve as an (. ) index of inflation?
from what you have learned?
((pause))
S1: cpi?
IS19: yeah. *mhm
but uh the growth rate of cpi to be precisely.
because the inflation is a kind of growth rate of the price level
so the cpi,
uh can be used to present the- the price level.
or so you can use the growth rate of cpi.
or the gdp deflator.
to represent the-
an index of inflation.
so that’s for question one.
((pause))
so we- we choose a for this question.
and for (. ) question two,
of all (. ) of the following that could be used as money,
which would be most likely to be characterized as fiat money
so.
what is fiat money?
fiat money uh does not have any (. ) intrinsic value.
so there is no in(. )trin(. )sic value
of fiat money.
so when you go ((undecipherable))
among all these four choices
which one does not have a intrinsic value?
so the first one is the-
and-and what is the intrinsic value?
so
uh
if a ((undecipherable)) as a intrinsic value then it may
give you some satisfaction,
or some (.).

It may (.).

You know (.).

So for example (.).

For the first choice the chocolate bars (.).

UH then it has intrinsic value because (.).

You know you can eat it (.).

And it--it can increase your utility or satisfaction (.).

And the second one is silver jewelry (.).

6:00

And so--it also has uh intrinsic value because (.).

It makes you look good and makes you feel happy (.).

So (.).

Silver jewelry (.).

And the third one the gum wrappers (.).

So basically (.).

Uh doesn’t have any intrinsic value. So (.).

It’s useless and it can- can- (.).

It cannot give any utility to you (.).

And the last one is a salt (.).

Again, you know it can add flavor to your food and- (.).

And it can give you some satisfaction (.).

So for this one you choose (.).

Because (.).

It does not have any (.).

Intrinsic value (.).

So you have any questions (.).

Okay (.).

For the- for the third one (.).

So in the long run (.).

If money’s value increases by three percent (.).

Then (.).

There are four statement (.).

And we need to figure out which one is correct (.).

So: in order to (.).

Solve this problem, we need the- uh (.).

Quantitative formula (.).

Which is m times v equals to p times y (.).

And here m is the (.1)

Money supply (.1)

And v is the (.3)

Velocity of money (.3)

And p is the (.3)

Price level (.3)

And y is the (.3)

Real output (.3)

So and from this uh quantitative equation we can get that
uh.
the growth rate of the money,
plus (.2)
the growth rate of the velocity,
equals to the (.3)
growth rate of the price level.
which is the inflation. (.3)
plus (.1)
the growth rate of uh real output.
and in the long run we don’t add this-
this velocity, and
this real output is fixed.
so the growth rate of these two terms is zero. (.2)
and now as the money supply increase by (.3) three percent,
we know that um (.4) the price level or the inflation increases by three percent.
so we choose b
because it says the price level increases by approximately three percent.
and
for a,
it says real income increases by approximately three percent.
it’s not true because in the long run,
all the real terms will-
all the real variables will- uh will stay constant.
so.
a is not true.
it will be constant in the long run.
the real ((undecipherable)) is the y here.
and for c,
the real interest rate increases by three percent.
it’s also wrong because it is a real variable.
and it will not (.) uh change in the long run.
and the last one is the
nominal interest rate is now affected.
so,
from the-
((pause))
from the fisher equation,
which is (.5)
nominal interest rate equals to the
inflation plus the real interest rate.
uh as we know the inflation,
xxx has increased by three percent.
xxx and this real (.)
xxx uh interest rate is constant.
xxx so this nominal interest rate will also increase by (.1)
xxx three percent.
xxx so it is not (. ) affected.
xxx so we do not choose b.
xxx so the answer for (. ) three (. ) b.
xxx ((pause))
xxx so any questions from (. ) °this? ((trails off))
xxx ((pause to erase whiteboard))
xxx a:nd next one
xxx the cost of holding money is equal to what?
xxx so the inflation rate or real interest rate or growth rate
xxx of money or um interest rate.
xxx so now, uh(.)
xxx the cost of holding money is a kind of opportunity cost.
xxx because you choose to hold the money,
xxx then you will lose a opportunity to
xxx buy some for example government bonds
xxx which can give you some interest.
xxx and- so this nominal interest that you- that you lose is-
xxx is the kind of cost of holding money.
xxx so (. ) we choose (. ) d which is the nominal interest rate.
xxx ((pause))
xxx and
xxx ((pause))
xxx before we choose the ((undecipherable)) a inflation rate
xxx so. again from the (. ) fisher (. ) equation,
xxx the nominal (. ) interest rate equals to the inflation (. )
12:02
xxx plus the real interest rate.
xxx so the first two choices only
xxx covers parts of the- parts of the answer.
xxx so both of them consists of the nominal interest rate.
xxx so.
xxx it is not equal to the cost of holding money.
xxx it ((undecipherable)) just part of the cost.
xxx and for c, the growth rate of money supply.
xxx so it will
xxx only influence the inflation and (. ) it is not
xxx relevant to this question.
xxx so it was c for °question four. ((trails off))
xxx okay are we (. ) clear?
xxx ((pause))
so:
now let’s move to question five,
((pause))
so one effect of an unexpected rise in inflation
is that wealth it is redistributed from-
uh from where to where?
so from borrowers to lenders? or
from ((undecipherable)) or-
or from young people to old people or
from ((undecipherable)) to ((undecipherable)).
so.
we also need to refer to this uh
fisher equation.
((undecipherable))
so.
first we need to know that (.) you know
when you (.) uh
settle a-settle a loan agreement between the borrowers and
the lenders,
so here is the borrowers.
((pause))
here’s the lenders.
so they need to set a-a nominal interest rate.
which is i.
and keep it fixed,
and after a (. ) period of-of time, the borrowers will give
the money back to uh the lenders plus the nominal interest.
so.
when they-uh- when they set this-this nominal interest rate,
they actually use this formula.
i equal to
this e pi is the expectation of inflation rate.
and this is the real interest rate.
so for example, the lenders may want uh
real interest rate which equals to r- r now.
and (.) his expectation of the inflation is-
is this-is this e pi.
so they will set
uh the nominal interest rate equals to this i.
but after the-the agreement is settled,
then the inflation (. ) rate will will fluctuate.
so
for example i time t after the agreement is settled,
again from this uh fisher equation,
we can get $i_t$ equals to (.1)

$\pi_t$.

which is the inflation rate at that moment.

at period $t$,

plus (. ) the real (. ) interest rate at that time.

and this $i_t$ is equals to (. ) $i$ because (. ) this is fixed.

so now,

we can do some exam- add and substract uh some items from this equation.

and notice that this (. ) $e\pi$- so a-add and substract that $e\pi$ from this uh inflation rate at this moment and plus the same item.

and then do the same thing for the- for the real interest rate at the beginning so notice that this $e\pi$ plus (. )

$\rho$ now equals to— just equals to $i^*$ right?

and we also have our $i$ (. ) in the other side so these two terms canc-cancel out.

((undecipherable))

((pause to erase board))

so now we got

zero equals to ((pause))

$i_t$ minus $e\pi$

plus $\rho$ minus $\rho$ zero.

and we put these two terms to the other side. °so it’s $\rho$ zero ((trails off))

so why do we need this difference in the real interest rate?

because now we want-

our question is about the redistribution of wealth.

and to decide this redistribution, we need this real- uh- this real (return).

because (when we) um concerns about uh- uh- the wealth, we need to (heed) this real payment.

so.

now there is an unexpected rise.

so this is your expectation,

and uh
unexpected rise in inflation is that this term is positive. so from this equation we know this is also positive. so that implies that the real interest rate um currently at this moment, is less (.) than the interest rate that you want to earn at the beginning. that means that uh the lenders (.) you know this real return is- is paid to the lenders right? so. this means that the wealth of the lenders is (.)

18:01 actually decreased. so their- the wealth is re-redistributed from the lenders, uh to the borrowers. (.1) or put it differently because there is a rise in the inflation, the money is not as valuable as before. so uh as the borrowers only need to pay back the money, so you just pay back something that is less valuable as before. so the wealth just- is redistributed from the lenders to the borrowers. (.1) or you can see more explan- ((undecipherable)) from this- from the- ((trails off while pointing to his writing on the board)) so we choose b for this question. and for c and d, so that’s- that will depends because if the young people are lenders, then their wealth is-is redis- i-is redistributed to the (loan owners). to the old people. and the same thing- the thing is the same for the ((undecipherable)) and ((undecipherable)). it all depends on whether it is a lenders or borrower. ((pause)) so.
does it make sense? °(can help you)? ((IS19 is quiet when asking for questions)) ((pause)) so then- so let’s move to question six.
so question six is about a classical dichotomy.

so: according to the classical dichotomy, variables is affected by monetary policy.

so according to this theory, all variables can be uh (.2) divided into uh two parts real variables,

and the nominal (.2) variables.

so:

for example the:

the real wage

or the real interest-

interest rate

or the real gdp 21:00

they are all real variables.

they are measured in quantity

so in some uh physical limits

and uh for the nominal variables,

they are measured in terms of the money.

so for example the price level.

or the (.2) nominal gdp or

the nominal (wage).

so that-they are defined in terms of the money

so they are nominal variables.

and these classical dichotomy um states that uh.

the-the real variables will only be affected by the-

the other real variables.

and all the nominal variables will only be affected by money

because they are (.2) defined in terms of °money.

so.

this question just asks you

which of these variables is affected by money, (um c).

so: it’s the same to-

that you’ll find which variable is nominal variable.

°for this question.

so the first one the price level
it is the nominal variable. and
the second, the third, and the last one, they are all real variables. so (.) you choose a for this question. ((pause)) questions?
((pause to erase board))

S2: the-the nominal variables only affected by the- uh: money.
IS19: yeah.
((pause)) so you can.
you know o- uh examine the variables separately. so when you examine these real variables, ((undecipherable)) other real variables. and when you (.) consider these nominal variables, you only consider other variables.

S2: yeah.

IS19: you do not need to consider other real variables. (.3) so they can be studied separately based on this (.) theory.
((pause to erase board)) so now for question two, the newspaper article once reported that uh:
the US economy was experienced a low rate of inflation.
it said that low inflation has a downside.
forty five million recipients of social security and other benefits will see their checks go up by just two point eight percent next year.

24:00
so this is um words from an article, a:nd the- (.1) the first one asks you, why does inflation affect uh the increase in social security and other benefits. so.

uh.
first we need to- uh we need to know how these payments from
S3: ((sneezes))=
IS19: =social security are set.
so
as we know the:
legislators always want to ensure that
the real value of the payment
uh (. ) is the same.
so. it will not be affected by the inflation.
so.
uh-uh as this uh nominal,-
uh-uh I mean as this payment from social security is
nominal payment.
so. we also know that nominal payment
over the price, (. ) equals
to the real payment.
so the-the payment from the social security is a type of
nominal payment.
and it is adjusted by the inflation.
so.
both of these terms will (. ) increase in the.-
at the same rate of the inflation.
so.
that implies that this real payment
will not be affected.
so- and the question asks you
why does the inflation affect the increase.
so that’s just because
you know the- the government want to ensure the real value
(. ) of the payment (is not affected).
so.
if there is a-
if there is a change in the price level,
in the- uh in the inflation rate,
then the nominal payment for.-
for this- uh for this payment from social security,
for this particular question,
will also uh growth in the (. ) same rate.
so ((undecipherable))
((long pause to write on board))
((clears throat))

27:00
so because they want to keep the:
real value of benefits (. ) constant.
so (. ) the payment will grow,
at the same speed with this uh inflation.
((pause))
so that’s only a reference for you and ((undecipherable)).
((pause to erase))
then the (. ) second one,
is this effect a cost of inflation as the article suggests?
why or why not?
and (.3)
so first what happens to in-in this-in this question.
uh with the article.
what is the phenomenon?
so the phenomenon is that
(you know) the inflation just increases in a-in a lower rate
and the low (growth) rate.
and that implies that the nominal payment,
or the payment from the social security,
also uh (. ) go ↑ up by-
by a low percent.
so.
this is the effect.
and is this a cost of inflation?
it is not.
so why is that? because.
you know the payment is-
h-have the same rate of the inflation.
and
the real payment will not be affected.
so it will keep constant.
(um) through different years.
so.
as the real payment is constant
so the inflation doesn’t um take-doesn’t make any cost
for this-uh for this society or to the economy.
so.
that’s why (. ) it is not a cost of in- of inflation.
so the cost of inflation is that
so uh.
a higher speed of inflation may cause your real-
may erode your real payment.
may make your real-real value or-or the real output shrink,
so but now,
as the nominal payment is
increase at the same speed as the inflation.
30:00
so the ↑ real payment will not be (. ) affected.
so (. ) there is no cost of (. ) inflation.
and ((undecipherable)) ((mumbling))
((long pause to write))
so.
I just put it simple uh although your nominal,-
xxx your nominal payment is- uh:
xxx does not increase uh ve-very high,
xxx but- uh (. ) but your real payment is the same.
xxx so your purchasing power is the same as before.
xxx so there- that’s why there is a- no cost of inflation.
xxx so when you consider the cost of inflation,
xxx S5: ((coughs))
xxx IS19: we need to concentrate on the- on the real value.
xxx ((pause))
xxx *so are we good with this? ((points to the board))
xxx S6: yeah I'm confused on why the real payment should be fixed
xxx cause the: question didn’t mention about this?
xxx IS19: yes thas is- how this nominal payment-
xxx how this payment from social security is set up.
xxx S6: so they just set up (we need) to the real payment,
xxx to like be equal [every year,
xxx IS19: [uh huh
xxx S6: and if the price- like the money (they can) like increase
xxx we just need to increase the inflation rate?
xxx IS19: ((nods)) yeah.
xxx S6: so (. ) does it work to every problem?
xxx so like-
xxx IS19: no it’s only work for the benefits of the social security.
xxx S6: oh so just for social security the real payment is fixed.
xxx IS19: yeah.
xxx S6: okay thank you.

33:00

xxx ((pause))
xxx IS19: okay so um the last question.
xxx ((pause to erase))
xxx in this question you are given a (. )
xxx money demand function,
xxx and k- the k-
xxx the (parameter) in this function is a con-is constant.
xxx and
xxx you know the money supply grow by twelve percent per year,
xxx and real income grow by four percent per year.
xxx and.
xxx the first part asks you what is the average inflation rate.
xxx so now we
xxx uh there we need to refer to the quantity equation.
xxx which is m v equals p y.
xxx and remember it
xxx implies the growth rate of
xxx money,
plus the,
growth rate of velocity of money,
equals to the
growth rate of price, plus the,
growth rate of y.
real output or real income.
and from the question we know the
uh money supply, (. ) grows by twelve percent,
and this-and this v is ((undecipherable)) and
it is al-always constant.
so the growth-growth rate is zero.
and.
also the growth rate of the real income,
is (. ) four percent,
so based on simple calculation we know that
growth rate of the price level,
which is the inflation,
is eight percent.
so that’s the answer for part one.
((pause to erase))
so: for part two,
it ask you how do you interpret the parameter k.
so now
we write down the real money demand (. ) function first.
so this is the parameter k.
and this is you: r
uh real money demand.
((pause to write))

36:00

and this is your real output.
((pause to write))
so this parameter is just uh
the ratio of the real money demand divided by the (. )
real output.
so
uh it means that for each amount of real output you hold,
how-how much money you-you-
how much money will you hold for each-
uh for each a-amount of the real output.
because this k is the.- (.3)
is the ratio of this two things.
((pause to look at paper))
"so it’s
((long pause to write))
so this is the interpretation for k.
and what is relationship to the velocity of the money? which is the v in that equation.
so.
((pause to erase))
so now we need a (condition) that the money-the real money demand equals to the real money supply.
and then we use these two (.) equations.
we can get uh. (.1)
this k times y equals to (.1)
y over (.)
°g ((pause))
and these two are (. ) cancelled out.
so. (.1)
so we get k equals to one over v or
we can write it as v equals to one over k.
so these two parameters are reciprocal in pattern.
and how to interpret this.
so. remember this k is the-
is the- is the amount of money that one wants to hold, for each amount of uh income.
and this v,
this v is the- the number of (fact) that y unit of-
((undecipherable))
or y unit of the money,
39:00
is used in this economy.
is used for the transactions that happen in this economy.
so.
((pause to write))
((mumbles while writing)) (always change)
((undecipherable))
or enters the °economy.
so that means that
uh if-if the ↑k is more,
which means that for each amount of income you want to hold less money,
then. (.) the number of times a dollar is used, that- that a dollar changes (hand),
it in this economy will increase will be larger.
so.
let me give you an example.
so for example you have uh one hundred apples in this economy.
and (.) the k,

uh equals one uh for each amount of apple you want to hold.

one dollars.

and then,

suppose there are (.) totally one hundred dollars

in this economy.

which is the m here.

and let’s just (normalize) this p equals what.

so (.) this one hundred- this one hundred is the y,

and this is the (.) k,

and this is the (.) money.

so.

uh.

and now this um velocity is uh-

also equals to one.

this is the v.

so now let’s uh assume that

uh the money supply is constant.

it’s still one hundred dollars.

but,

but the-the output may-may increase to two hundred.

and now

and this param-parameter is also one dollars.

and then,

uh: ((pause))

and because uh this-this y increase,

and this-this m is uh-this m is constant,

then you need to use uh

((talking to self)) °uh no. not this is increase.

so for example the k, uh:

the k decrease.

so for each of-uh-each of amount of output,

the amount you hold is is point five dollars.

uh: then this-this v will increase because

uh

because as uh

now you want to hold less money.

then every dollar should be used twice

a-as before.

so it will be used for mo-for more times.

42:00

((pause))

°so.

((pause))

is-is it (.) clear? ((undecipherable))
are you clear with this concept of the velocity of the-
of the money? (.2)
so that means that for y unit of the output, so.
the times of the-
of the- of each amount of money is used in this economy.
((students are packing up))
so now-now let’s fo-focus on this equation.
so.
(nominalize) this one, and this m is-is constant,
so if (. y increases-increases,
then this v also increases.
because uh.
each each dollar should be used more times.
because of the (. increase in this output.
((pause))
so.
that’s all for today and if you have question um
I’ll stay for a while.