

Name: _____ Class: _____ Date: _____

Chapter 1 - Ten Principles of Economics

1. Which word comes from the Greek word for “one who manages a household”?

- a. market
- b. consumer
- c. producer
- d. economy

ANSWER: d

2. From which of the following is the word “economy” derived?

- a. environment
- b. one who manages a household
- c. one who participates in a market
- d. allocation

ANSWER: b

3. What do households and economies have in common?

- a. They both must allocate scarce resources.
- b. They both face difficulties saving money.
- c. They both must sell the goods and services they produce.
- d. They both must have a central decision maker.

ANSWER: a

4. What concept does economics primarily deal with?

- a. scarcity
- b. poverty
- c. change
- d. power

ANSWER: a

5. What is NOT included in the decisions that every society must make?

- a. what goods will be produced
- b. who will produce the goods
- c. what determines consumer preferences
- d. who will consume the goods

ANSWER: c

6. Why do both households and societies face many decisions?

- a. Resources are scarce.
- b. Populations may fluctuate over time.
- c. Wages for households and therefore society fluctuate with business cycles.
- d. People, by nature, tend to disagree.

ANSWER: a

7. When is a good considered scarce in a society?

- a. when more output of the good is possible

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- b. when everyone in that society cannot have all they want of the good
- c. when the government restricts production of the good
- d. when only the richest people in the economy can buy all they want of the good

ANSWER: b

8. When does scarcity exist?

- a. when there is less than an infinite amount of a resource or good
- b. when society can meet the wants of every individual
- c. when there is less of a good or resource available than people wish to have
- d. when the government fails to produce goods

ANSWER: c

9. How are goods and services allocated in a market economy?

- a. by government decisions
- b. by giving each individual just enough for a decent standard of living
- c. by the actions of all firms and consumers
- d. by inherited rights and properties

ANSWER: c

10. Approximately what percentage of the world's economies experience scarcity?

- a. 25
- b. 50
- c. 75
- d. 100

ANSWER: d

11. What is an economy experiencing when a society cannot produce all the goods and services people wish to have?

- a. scarcity
- b. misallocation
- c. externalities
- d. market failure

ANSWER: a

12. For society, when is a good NOT scarce?

- a. if at least one individual in society can obtain all he or she wants of the good
- b. if firms are producing at full capacity
- c. if all members of society can have all they want of the good
- d. if those who have enough income can buy all they want of the good

ANSWER: c

13. Which good best meets the definition of scarcity?

- a. air
- b. water in the ocean
- c. electricity in a city

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- d. wood in a forest

ANSWER: c

14. What does economics study?

- a. finance
- b. how society manages its scarce resources
- c. central planning
- d. government regulation

ANSWER: b

15. What does economics study?

- a. how society manages its scarce resources
- b. the government's role in society
- c. how to increase production
- d. how firms make profits

ANSWER: a

16. In most societies, who allocates resources?

- a. a single central planner
- b. those who own the resources
- c. those firms that use resources to provide goods and services
- d. the combined actions of millions of households and firms

ANSWER: d

17. What do economists study?

- a. how people make decisions
- b. how governments interact with one another
- c. the forces and trends that affect only the economy as a whole
- d. how societies change over time

ANSWER: a

18. Which of the following is NOT a major area of study for economists?

- a. how people make decisions
- b. how countries choose national leaders
- c. how people interact with each other
- d. how forces and trends affect the overall economy

ANSWER: b

19. What concept is illustrated by the adage, "There is no such thing as a free lunch"?

- a. tradeoffs
- b. scarcity
- c. productivity
- d. efficiency

ANSWER: a

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20. What does the saying “There is no such thing as a free lunch” mean?
- a. Even people on welfare have to pay for food.
 - b. The cost of living is always increasing.
 - c. To get something we like, we usually have to give up another thing we like.
 - d. All costs are included in the price of a product.

ANSWER: c

21. What are economists illustrating when they use the phrase “There is no such thing as a free lunch”?
- a. how inflation increases prices
 - b. that to get one thing, we must give up something else
 - c. that nothing is free in a market economy
 - d. that if something looks too good to be true, it probably is

ANSWER: b

22. Which statement best describes the concept represented by the adage “There is no such thing as a free lunch”?
- a. Melissa can only attend the concert if she takes her sister with her.
 - b. Greg is hungry and homeless.
 - c. Brian must repair the tire on his bike before he can ride it to class.
 - d. Olivia must decide between skiing at Whistler or Lake Louise for spring break.

ANSWER: d

23. Guns and butter represent the classic societal tradeoff between spending on which two items?
- a. durable and nondurable goods
 - b. imports and exports
 - c. national defence and consumer goods
 - d. law enforcement and agriculture

ANSWER: c

24. Henry decides to spend two hours playing golf rather than working at his job, which pays \$8 per hour. What is Henry’s tradeoff?
- a. the \$16 he could have earned working for two hours
 - b. nothing, because he enjoys playing golf more than working
 - c. the increase in skill he obtains from playing golf for those two hours
 - d. nothing, because he spent \$16 for green fees to play golf

ANSWER: a

25. What happens when society requires that firms reduce pollution?
- a. There is a tradeoff because of reduced incomes to the firms' owners, workers, and customers.
 - b. There is no tradeoff, since everyone benefits from reduced pollution.
 - c. There is no tradeoff for society as a whole because the cost of reducing pollution falls only on the firms affected by the requirements.
 - d. There is a tradeoff only if some firms are forced to close.

ANSWER: a

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26. Daniel decides to spend the last two hours of the night before his economics exam studying instead of sleeping. For Daniel, what would his tradeoff be?

- a. nothing, because no dollar value can be put on sleep
- b. nothing, because studying would be more beneficial than sleep
- c. the six hours of sleep he could have had if he had gone to bed before midnight
- d. the two hours of rest he would have gotten

ANSWER: d

27. How does a tradeoff exist between a clean environment and a higher level of income?

- a. Studies show that individuals with higher levels of income purchase more environmentally friendly products than low-income individuals.
- b. To pay for pollution cleanup, the government must increase taxes, which lowers income.
- c. Laws that reduce pollution raise costs of production and reduce incomes.
- d. By employing individuals to clean up pollution, employment and income both rise.

ANSWER: c

28. Which of the following would NOT be a result of laws that require firms to reduce pollution?

- a. lower spending by government
- b. higher prices to consumers
- c. lower wages to workers
- d. smaller profit to firms

ANSWER: a

29. What will pollution regulations do?

- a. increase profit to firms
- b. impose a tradeoff on society
- c. allow firms to raise workers' wages
- d. lower prices for consumers

ANSWER: b

30. Which concept best defines efficiency?

- a. absolute fairness
- b. equal distribution
- c. minimum waste
- d. consumer satisfaction

ANSWER: c

31. What does efficiency mean?

- a. Society is conserving resources in order to save them for the future.
- b. Society's goods and services are distributed fairly among society's members.
- c. Society has lessened its dependence on non-renewable energy sources.
- d. Society is getting the most it can from its scarce resources.

ANSWER: d

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32. In which situation would economists use the word equity?

- a. Each member of society has the same income.
- b. Society is getting the most it can from its scarce resources.
- c. Those in society who have the least will receive the most.
- d. The benefits of society's resources are distributed fairly among society's members.

ANSWER: d

33. What is one definition of equity?

- a. equality
- b. efficiency
- c. fairness
- d. similarity

ANSWER: c

34. What happens when government policies are being designed?

- a. There is usually a tradeoff between equity and efficiency.
- b. Equity and efficiency goals are usually independent of each other.
- c. Equity can usually be achieved without an efficiency loss.
- d. Increasing efficiency usually results in more equity.

ANSWER: a

35. What happens when government policies such as the welfare system try to help the neediest members of society?

- a. It increases equity and reduces efficiency.
- b. It reduces charitable contributions in an economy.
- c. It increases the productivity of the needy in society.
- d. It causes market failure to occur.

ANSWER: a

36. What is likely to occur when the government implements programs such as progressive income tax rates?

- a. Equity and efficiency is increased.
- b. Equity is increased and efficiency is decreased.
- c. Equity is decreased, and efficiency is increased.
- d. Equity is decreased, and efficiency is decreased.

ANSWER: b

37. What happens when the government attempts to cut the economic pie into more equal slices?

- a. It is easier to cut the pie, and therefore the economy can produce a larger pie.
- b. The government can more easily allocate the pie to those most in need.
- c. The pie gets smaller, and there will be less pie for everyone.
- d. The economy will spend too much time cutting the pie and lose the ability to produce enough pie for everyone.

ANSWER: c

38. When the government attempts to improve equity in an economy, what is often the result?

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- a. an increase in overall output in the economy
- b. additional government revenue since overall income will increase
- c. an actual reduction in equity
- d. reduced efficiency in the economy

ANSWER: d

39. When the government redistributes income from the rich to the poor, what is the result?
- a. Efficiency is improved, but equity is not.
 - b. Both rich people and poor people benefit directly.
 - c. People work less and produce fewer goods and services.
 - d. Rich people consume fewer goods, but poor people consume more goods, resulting in no real change.

ANSWER: c

40. In economics, what is the cost of something?
- a. the dollar amount of obtaining it
 - b. the value of the resources needed to produce it
 - c. what you give up to obtain it
 - d. the amount of labour to produce it

ANSWER: c

41. What is the term for what you give up to obtain an item?
- a. opportunity cost
 - b. explicit cost
 - c. true cost
 - d. direct cost

ANSWER: a

42. David receives \$200 as a birthday gift. In deciding how to spend the money, he narrows his options down to four: A, B, C, and D. The price of each option is \$100, but David prefers B to C, C to A, and A to D. What is the opportunity cost of option B?

- a. It is David's valuation of C.
- b. It is David's valuation of A, C, and D together.
- c. It is \$200.
- d. It is \$100.

ANSWER: a

43. What is the opportunity cost of going to university?
- a. the total spent on food, clothing, books, transportation, tuition, lodging, and other expenses
 - b. the value of the best opportunity a student gives up to attend university
 - c. zero, for students who are fortunate enough to attend on a scholarship
 - d. zero, because a college education will allow a student to earn a larger income after graduation

ANSWER: b

44. For most students, what is the largest single cost of a university education?

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- a. the wages given up to attend school
- b. tuition, fees, and books
- c. room and board
- d. transportation, parking, and entertainment

ANSWER: a

45. What is the largest single cost of going to university?

- a. books
- b. room and board
- c. tuition
- d. lost wages

ANSWER: d

46. What is the opportunity cost of an item?

- a. the number of hours needed to earn money to buy it
- b. what you give up to get that item
- c. usually more than the dollar value of the item
- d. the value of the resources needed to produce the item

ANSWER: b

47. Murray receives \$100 as a birthday gift. In deciding how to spend the money, he narrows his options down to four choices: A, B, C, and D. Each option costs \$100, but Murray values each option differently. Finally, he decides on C. What is the opportunity cost of C?

- a. the value to him of the option he would have chosen if C was not available
- b. the value to him of options A, B, and D combined
- c. \$300
- d. \$100

ANSWER: a

48. Mallory decides to spend three hours working overtime rather than watching Netflix with her friends. She earns \$9 an hour. What is her opportunity cost of working?

- a. the \$27 she earns working
- b. the \$27 minus the enjoyment she would have received from watching Netflix
- c. the enjoyment she would have received had she watched Netflix
- d. nothing, because she would have received less than \$27 of enjoyment from Netflix

ANSWER: c

49. Robert spends an hour studying instead of going hiking. What is the opportunity cost to him of studying?

- a. the improvement in his grades from studying for the hour
- b. the difference between the improvement in his grades from studying minus the enjoyment of hiking
- c. the enjoyment and exercise he would have received had he gone hiking
- d. nothing, because Russell chose to study rather than to go hiking the value of studying must have been greater than the value of hiking

ANSWER: c

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50. What do we know about college-age athletes who drop out of college to play professional sports?

- a. They are not rational decision makers.
- b. They are well aware that their opportunity cost of attending college is very high.
- c. They are concerned more about present circumstances than their future.
- d. They underestimate the value of a college education.

ANSWER: b

51. How do people make decisions at the margin?

- a. by following the business cycle
- b. by experience
- c. by calculating dollar costs
- d. by comparing costs and benefits

ANSWER: d

52. What does the word “margin” mean?

- a. edge
- b. distance
- c. inside
- d. measure

ANSWER: a

53. What does making decisions “at the margin” mean?

- a. that people make those decisions that do not impose a marginal cost
- b. that people evaluate how easily a decision can be reversed if problems arise
- c. that people compare the marginal costs and marginal benefits of each decision
- d. that people always calculate the marginal dollar costs for each decision

ANSWER: c

54. What is a marginal change?

- a. a long-term trend
- b. a large, significant adjustment
- c. a change for the worse, and so is usually short term
- d. a small incremental adjustment

ANSWER: d

55. What is the best example of a marginal change?

- a. After graduating from university, Audrey’s income increases from \$500 per month to \$3000 per month.
- b. In 2015 minimum wage in Saskatchewan increased from \$10 per hour to \$10.20.
- c. Housing prices in an area increase by 40% when a new highway is built in a small town.
- d. A hard freeze wipes out half of the tobacco crop in Ontario and the price of cigarettes doubles.

ANSWER: b

56. What is the best example of a marginal change?

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- a. After graduating from university, Neville's income increases from \$1000 per month to \$1,100 per month.
- b. Jadelyn completes the six-month probationary period at her job and is now paid \$11.25 per hour instead of \$11.00.
- c. Housing prices in an area increase by 50% when a new freeway is built in a small town.
- d. A hard freeze wipes out half of the potato crop in Prince Edward Island and the price of potatoes doubles.

ANSWER: b

57. What is the best example of a marginal change?

- a. College tuition rose by 1% last year.
- b. Kim gets a big promotion at work. She also gets a raise from \$25,000 per year to \$40,000 per year.
- c. Mark graduates from university and takes a job. His income increases from \$10,000 per year to \$50,000 per year.
- d. A drought hits Saskatchewan and the price of wheat increases from \$4.00 per bushel to \$8.00 per bushel.

ANSWER: a

58. Which situation best illustrates a marginal change?

- a. Nancy retires and takes a part-time job. She was working 40 hours per week, but now works 10 hours per week.
- b. Provincial University has announced that due to provincial budget deficits, tuition must rise by 25% next year.
- c. Adam moved from Edmonton to Toronto and now pays 40% more for rent than before.
- d. Banff, which usually receives 600 cm of snow per year, received 620cm last year.

ANSWER: d

59. After much consideration, you have chosen Cancun over Fort Lauderdale for your spring break trip this year. For this decision to change, what must occur?

- a. The marginal benefit of Cancun must increase.
- b. The marginal cost of Cancun must decrease.
- c. The marginal benefit of Fort Lauderdale must increase.
- d. The marginal cost of Fort Lauderdale must increase.

ANSWER: c

60. The average cost per seat on a train trip from Edmonton to Jasper is \$140. Suppose no refreshments are served and three seats are empty. How could the train company increase its profit?

- a. if it charged no less than \$140 for the three remaining seats
- b. if it charged more than \$140 for the three remaining seats
- c. if it charged any ticket price above \$0 for the remaining seats
- d. if it left the seats empty

ANSWER: c

61. The average cost per seat on an airplane trip from Calgary to Kelowna is \$250. Suppose no refreshments are served and seven seats are empty. How could the airline company increase its profit?

- a. if it charged no less than \$250 for the seven remaining seats
- b. if it charged more than \$250 for the seven remaining seats
- c. if it charged any ticket price above \$0 for the remaining seats

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d. if it left the seats empty

ANSWER: c

62. When does a rational decision maker take an action?

- a. only if the marginal benefit is less than the marginal cost
- b. only if the marginal benefit is greater than the marginal cost
- c. only if the average benefit is greater than the average cost
- d. only if the marginal benefit is greater than both the average cost and the marginal cost

ANSWER: b

63. Mike has spent \$500 purchasing and repairing an old fishing boat, which he expects to sell for \$800. He discovers that he needs an additional repair, which will cost \$400. He can sell the boat as it is now for \$300. What should he do?

- a. He should take the \$300.
- b. He should never sell something for less than its cost.
- c. He should complete the repairs and sell the boat.
- d. It doesn't matter which action he takes; the outcome is the same either way.

ANSWER: c

64. Mike has spent \$800 purchasing and repairing an old motorcycle, which he expects to sell for \$1,200. He discovers that he needs an additional repair, which will cost \$200. He can sell the motorcycle as it is now for \$400. What should he do?

- a. He should take the \$400.
- b. He should never sell something for less than it cost.
- c. He should complete the repairs and sell the motorcycle.
- d. It doesn't matter which action he takes; the outcome is the same either way.

ANSWER: c

65. Carol has spent \$2000 purchasing and repairing an old car, which she expects to sell for \$2400. She discovers that she needs an additional repair, which will cost \$400. She can sell the car as it is now for \$2000. What should she do?

- a. She should sell the car now for \$2000.
- b. She should never sell something for less than it cost.
- c. She should complete the repairs and sell the car.
- d. It doesn't matter which action she takes; the outcome is the same either way.

ANSWER: d

66. Tim has spent \$2500 purchasing and repairing a Hummer, which he expects to sell for \$3500. He discovers that he needs an additional repair, which will cost \$1100. He can sell the Hummer as it is now for \$900. What should he do?

- a. He should take the \$900.
- b. He should never sell something for less than it cost.
- c. He should complete the repairs and sell the Hummer.
- d. It doesn't matter which action he takes; the outcome is the same either way.

ANSWER: c

67. Monica has spent \$120,000 purchasing and repairing an old cabin, which she expects to sell for \$130,000. She discovers that she needs an additional repair, which will cost \$20,000. She can sell the cabin as it is now for \$115,000.

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What should she do?

- a. She should take the \$115,000.
- b. She should never sell something for less than its cost.
- c. She should complete the repairs and sell the cabin.
- d. It doesn't matter which action she takes; the outcome is the same either way.

ANSWER: a

68. Stan buys a 1966 Mustang, which he plans to restore and sell. He anticipates that the cost of the car and the repairs will be \$15,000 and that he can sell it for \$19,000. When he has spent \$15,000, he discovers he needs to replace the engine, which will cost \$4000. He can sell the car without the new engine for \$9000. What should Stan do?

- a. He should complete the repairs and sell the car for \$13,000.
- b. He should sell the car now for \$9000.
- c. He should never try such an expensive project again.
- d. He should be totally indifferent between finishing the project and selling the car now.

ANSWER: d

69. Stan buys a 1966 Mustang, which he plans to restore and sell. He anticipates that the cost of the car and the repairs will be \$15,000 and that he can sell it for \$19,000. When he has spent \$14,000, he discovers he needs to replace the engine, which will cost \$5000. He can sell the car without the new engine for \$16,000. What should Stan do?

- a. He should complete the repairs and sell the car for \$19,000.
- b. He should sell the car now for \$16,000.
- c. He should keep the car for his own use because selling it would be a loss.
- d. He should be totally indifferent between finishing the project and selling the car now.

ANSWER: b

70. Lisa buys a 1982 BMW, which she plans to restore and sell. She anticipates that the cost of the car and the repairs will be \$11,000 and that she can sell it for \$20,000. After she has spent \$11,000, she discovers she needs to replace the engine, which will cost \$5000. She can sell the car without the new engine for \$14,000. What should Lisa do?

- a. She should complete the repairs for \$5000 and sell the car for \$20,000.
- b. She should sell the car now for \$14,000.
- c. She should keep the car for her own use because selling it would be a loss.
- d. She should be totally indifferent between finishing the project and selling the car now.

ANSWER: a

71. Lisa buys a 1982 BMW, which she plans to restore and sell. She anticipates that the cost of the car and the repairs will be \$10,000 and that she can sell it for \$15,000. After she has spent \$10,000, she discovers she needs to replace the engine, which will cost \$4000. She can sell the car without the new engine for \$11,000. What should Lisa do?

- a. She should complete the repairs for \$4000 and sell the car for \$15,000.
- b. She should sell the car now for \$11,000.
- c. She should keep the car because selling it would be a loss.
- d. She should be totally indifferent between finishing the project and selling the car now.

ANSWER: d

72. A donut shop sells fresh baked donuts from 5 a.m. until 3 p.m. every day but Sunday. The cost of making and selling a dozen glazed donuts is \$1.00. Because this shop does not sell day-old donuts the next day, what should the manager do if

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he still has 10 dozen left at 2:30 p.m.?

- a. lower the price of the remaining donuts even if the price falls below \$1.00
- b. lower the price of the remaining donuts as long as it's more than \$1.00
- c. lower the price on all donuts so they will all be sold earlier in the day
- d. donate them to the local Food Bank and produce ten fewer dozen tomorrow

ANSWER: a

73. A donut shop sells fresh baked donuts from 5 a.m. until 3 p.m. every day but Sunday. The cost of making and selling a dozen glazed donuts is \$2.00. Because this shop does not sell day-old donuts the next day, what should the manager do if she still has ten dozen left at 2:30 p.m.?

- a. lower the price of the remaining donuts even if the price falls below \$2.00
- b. lower the price of the remaining donuts as long as it's more than \$2.00
- c. lower the price on all donuts so they will all be sold earlier in the day
- d. donate them to the local Food Bank and produce ten fewer dozen tomorrow

ANSWER: a

74. A furniture maker currently produces 100 tables per week and sells them for a profit. She is considering expanding her operation in order to make more tables. Should she expand?

- a. Yes, because making tables is profitable.
- b. No, because she may not be able to sell the additional tables.
- c. It depends on the marginal cost of producing more tables and the marginal revenue she will earn from selling more tables.
- d. It depends on the average cost of producing more tables and the average revenue she will earn from selling more tables.

ANSWER: c

75. In the nation of Dictatorland, farmers traditionally feed grain to their livestock. Central planners, however, decided to increase the price of grain to make grain farmers happy and to reduce the price of bread made from that grain to make city dwellers happy. Now the price of bread is lower than the price of grain. What might we now expect?

- a. farmers to continue to feed grain to their livestock
- b. farmers to start feeding bread to their livestock
- c. city dwellers to start buying grain to make bread to eat
- d. city dwellers to start buying grain to make bread to sell

ANSWER: b

76. Your professor loves her work teaching economics. She has been offered other positions in the corporate world making 25 percent more, but has decided to stay in teaching. What might change her decision?

- a. if the marginal cost of teaching increased
- b. if the marginal benefit of teaching increased
- c. if the marginal cost of teaching decreased
- d. if the marginal cost of a corporate job increased

ANSWER: a

77. Suppose your management professor has been offered a corporate job with a 30 percent pay increase. Why has he decided to take the job?

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- a. The marginal cost of leaving was greater than the marginal benefit.
- b. The marginal benefit of leaving was greater than the marginal cost.
- c. The marginal benefit of teaching was greater than the marginal cost.
- d. The marginal cost of teaching was greater than the marginal benefit.

ANSWER: b

78. Suppose your management professor has been offered a corporate job with a 30 percent pay increase. Why has he decided NOT to take the job?

- a. The marginal cost of leaving was greater than the marginal benefit.
- b. The marginal benefit of leaving was greater than the marginal cost.
- c. The marginal benefit of leaving was less than the marginal cost.
- d. The marginal benefit of teaching was greater than the marginal cost.

ANSWER: c

79. When policymakers make policies that change the costs and benefits that people face, what is the result for society?

- a. people's behaviours are altered
- b. people ignore incentives
- c. inflation occurs
- d. government revenue is reduced

ANSWER: a

80. According to economists, what do people respond to?

- a. laws
- b. incentives
- c. threats more than rewards
- d. positives, but not negatives

ANSWER: b

81. What did Ralph Nader's book *Unsafe at Any Speed* cause the U.S. government to require?

- a. child booster seats in all new cars
- b. seat belts in all new cars
- c. air bags in all new cars
- d. stricter drunk driving laws

ANSWER: b

82. What has been the result of laws requiring that drivers wear seat belts?

- a. a reduction in both driver deaths and pedestrian deaths
- b. fewer accidents and fewer deaths per accident
- c. fewer driver deaths, fewer accidents, and fewer pedestrian deaths
- d. little change in the number of driver deaths, but more accidents and more pedestrian deaths

ANSWER: d

83. What has been one effect of a government-imposed seat belt law?

- a. fewer pedestrian deaths

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- b. safer driving
- c. an increase in the number of accidents
- d. everyone now wears seat belts

ANSWER: c

84. What does NOT result when seat belt laws alter a driver's cost-benefit calculation?

- a. Fewer drivers are killed.
- b. More pedestrians are killed.
- c. Drivers drive faster.
- d. More accidents occur.

ANSWER: a

85. In the former Soviet Union, producers were paid for meeting output targets, not for selling products. Under those circumstances, what were the economic incentives for producers?

- a. to produce good quality products which last longer so output targets can be reduced
- b. to conserve on costs, so as to maintain efficiency in the economy
- c. to produce enough to meet the output target, without regard for quality or cost
- d. to produce those products that society desires most

ANSWER: c

86. How can trade benefit a family?

- a. by allowing the family to buy a greater variety of goods and services at a lower cost
- b. by allowing each person to buy only the goods and services they want most
- c. only if the family is not in economic competition with other families
- d. trade can only benefit entire nations, not individuals

ANSWER: a

87. How does trade affect the well-being of the nations involved?

- a. Trade makes every nation better off.
- b. Trade makes exporting nations better off and importing nations worse off.
- c. Trade makes a nation better off only if the nation cannot produce that good itself.
- d. Trade makes rich nations better off and poor nations worse off.

ANSWER: a

88. What does trade NOT achieve?

- a. increased competition
- b. equal gains for both countries involved
- c. some gains for both countries involved
- d. greater production efficiency

ANSWER: b

89. What is NOT a benefit from trade?

- a. the ability to specialize
- b. a greater variety of goods and services becoming available

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- c. less competition
- d. lower prices

ANSWER: c

90. What is the effect of a trade between Canada and India?

- a. benefits for both Canada and India
- b. a losing proposition for Canada because India has cheaper labour
- c. trade between the two countries would be inefficient due to the high cost of transporting the goods
- d. a losing proposition for India because Canadian workers are more productive

ANSWER: a

91. With which nations does Canada benefit from trade?

- a. only nations that can produce goods Canada cannot produce
- b. with any nation
- c. with any nation not in economic competition with Canada
- d. only with less developed nations

ANSWER: b

92. What will be the probable outcome if Japan chooses to engage in trade?

- a. It will only benefit if it trades with countries that produce goods it cannot produce.
- b. It cannot benefit if it trades with less developed countries.
- c. It will only benefit if it trades with countries that are geographically close Japan.
- d. It can benefit by trading with any other country.

ANSWER: d

93. If Canada decides to trade with Mexico, what do we know about the probable outcome?

- a. Mexico will be better off, but trade with a less developed country will not help Canada.
- b. It will not benefit Mexico because workers in Canada are more productive.
- c. It will benefit Mexico because workers in Canada are more productive.
- d. Mexico and Canada can both be better off.

ANSWER: d

94. If France is better than Latvia at producing wine, but Latvia is better than France at producing lumber, what should happen?

- a. Latvia should sell lumber to France, and should buy French wine.
- b. Latvia should impose a tariff on French wine in order to protect jobs in the Latvian lumber industry.
- c. Latvia should subsidize its wine industry so that it can compete with French wine.
- d. Latvia should put a quota on the amount of French wine imported.

ANSWER: a

95. How good are markets at organizing economic activity?

- a. Markets are usually a good way to organize economic activity.
- b. Markets are usually inferior to central planning as a way to organize economic activity.
- c. Markets fail and are therefore not a good way to organize economic activity.

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d. Markets are a good way to organize economic activity in developed nations, but not in less developed nations.

ANSWER: a

96. What is NOT a characteristic of markets?

- a. Firms decide whom to hire and what to produce.
- b. Government policies do not affect the decisions of firms and households.
- c. Households decide which firms to work for and what to buy with their incomes.
- d. Firms and households guide the decisions based on profit and self-interest.

ANSWER: b

97. In what economy are the decisions of firms and households guided by profit and self-interest?

- a. a command economy
- b. a traditional economy
- c. a market economy
- d. in every economy

ANSWER: c

98. A friend of yours asks you why market prices are better than government-determined prices. What do you say?

- a. Because they generally reflect the value of a good to society, but not the cost of making it.
- b. Because they generally reflect the cost to society of making a good, but not its value.
- c. Because they generally reflect both the value of a good to society and the cost of making it.
- d. Because they generally reflect neither the value of a good to society nor the cost of making it.

ANSWER: c

99. In a market economy, what guides economic activity?

- a. the government
- b. businesses
- c. central planners
- d. prices

ANSWER: d

100. In a market economy, decisions are guided by individual self-interest. What impact does this have?

- a. There is still the ability to achieve desirable economic well-being for society as a whole.
- b. There is a strong need for government intervention in the market.
- c. There is less efficiency in market economies than in command economies.
- d. There is more need for a strong legal system to control individual greed.

ANSWER: a

101. How do prices direct economic activity in a market economy?

- a. by influencing the actions of buyers and sellers
- b. by reducing scarcity of the goods and services produced
- c. by eliminating the need for government intervention
- d. by allocating goods and services produced in the most equitable way

ANSWER: a

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102. In a market economy, what do prices reflect?

- a. the popularity of a good in society
- b. the cost to society of making the good
- c. the quantity society will ultimately choose to produce
- d. the level of wealth in society

ANSWER: b

103. What is one advantage that market economies have over central planning?

- a. They provide an equal distribution of goods and services to consumers.
- b. They establish government economic control.
- c. They solve the problem of scarcity.
- d. They are more efficient.

ANSWER: d

104. To what extent does the invisible hand model of a market ensure equity and efficiency?

- a. The invisible hand always ensures both equity and efficiency.
- b. The invisible hand cannot ensure either equity or efficiency.
- c. The invisible hand is more effective at ensuring efficiency than it is at ensuring equity.
- d. The invisible hand is more effective at ensuring equity than it is at ensuring efficiency.

ANSWER: c

105. According to Adam Smith, what is the success of decentralized market economies primarily due to?

- a. the basic benevolence of society
- b. society's justice (legal) system
- c. individuals' self-interest
- d. basic human survival instincts

ANSWER: c

106. How is the self-interest of the participants in an economy guided into promoting general economic self-interest?

- a. by the invisible hand
- b. by market power
- c. by government intervention
- d. by property rights

ANSWER: a

107. Which observation was made famous by Adam Smith in his book *The Wealth of Nations*?

- a. There is no such thing as a free lunch.
- b. People buy more when prices are low than when prices are high.
- c. People tend to spend more than they earn.
- d. Markets are guided by an invisible hand that leads to desirable outcomes.

ANSWER: d

108. Who coined the term "invisible hand"?

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- a. Adam Smith
- b. David Ricardo
- c. John Maynard Keynes
- d. Milton Friedman

ANSWER: a

109. How does the invisible hand direct economic activity?

- a. through advertising
- b. through prices
- c. through central planning
- d. through government regulations

ANSWER: b

110. How does a market economy reward people?

- a. according to their need for goods and services
- b. according to their willingness to work
- c. according to their ability to produce things that other people are willing to pay for
- d. according to their ability to produce things of cultural importance

ANSWER: c

111. What can hinder the invisible hand's ability to coordinate the decisions of the firms and households in the economy?

- a. government actions that distort prices
- b. increased competition in the market
- c. extended periods of unemployment
- d. a dramatic reduction in consumer spending

ANSWER: a

112. When was Adam Smith's book *The Wealth of Nations* published?

- a. 1692
- b. 1776
- c. 1816
- d. 1936

ANSWER: b

113. When people act in their self-interest, what typically happens in a market system, according to Adam Smith?

- a. They help only themselves.
- b. They harm others.
- c. They help others, but not as much as they would have if they were not self-interested.
- d. They help others even more than when they seek to help others.

ANSWER: d

114. How does the invisible hand primarily work to promote general well-being in the economy?

- a. through government intervention
- b. through the political process

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- c. through self-interest
- d. through altruism

ANSWER: c

115. Why do taxes adversely affect the allocation of resources in society?

- a. because they do not always fall more heavily on the rich
- b. because the taxes collected are not enough to finance government spending
- c. because not everyone pays taxes
- d. because they distort prices and thus the decisions of households and firms

ANSWER: d

116. What is a primary function of prices in a market economy?

- a. to provide participants with economic information
- b. to provide participants with spending limits
- c. to provide participants with accounting capabilities
- d. to provide participants with an equitable distribution of goods

ANSWER: a

117. What happens when the government prevents prices from adjusting naturally to supply and demand?

- a. It stabilizes the economy by reducing market uncertainties.
- b. It adversely affects the allocation of resources.
- c. There is an improvement in equity that justifies the reduction in efficiency.
- d. There is an improvement in efficiency that justifies the reduction in equity.

ANSWER: b

118. What is one component necessary for markets to work?

- a. government intervention
- b. a non-profit sector of society
- c. property rights
- d. abundant resources

ANSWER: c

119. What is one necessary role of government in a market economy?

- a. to tax goods and services that are most desired by consumers
- b. to maintain subsidized housing for low-income households
- c. to provide services such as pensions
- d. to enforce property rights

ANSWER: d

120. How does the government enforce property rights?

- a. by requiring property owners to pay property taxes
- b. by providing police and courts
- c. by allowing people to decide whether or not they wish to own property
- d. by providing a system of recording property deeds

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ANSWER: b

121. What would happen without the government's protection of property rights?

- a. Businesses would have less incentive to provide goods and services.
- b. There would be less government regulation of businesses and prices would be lower for consumers.
- c. Taxes would be lower, causing less market inefficiencies.
- d. Businesses would have more freedom with production processes.

ANSWER: a

122. What does the term "market failure" refer to?

- a. a situation in which the market on its own fails to allocate resources efficiently
- b. an unsuccessful advertising campaign that reduces consumer demand
- c. a situation in which competition among firms leads to bankruptcies
- d. a firm that is forced out of business because of new by-laws

ANSWER: a

123. Which of the following is NOT a reason for the government to intervene in the market?

- a. to promote efficiency
- b. to enforce property rights
- c. to promote equity
- d. to protect an industry

ANSWER: d

124. What are two very likely reasons for a government to intervene in a market?

- a. to promote stability and to raise revenues
- b. to promote equity and to promote efficiency
- c. to promote equity and to promote stability
- d. to promote efficiency and to raise revenues

ANSWER: b

125. What are two causes of market failure?

- a. externalities and market power
- b. market power and incorrect forecasts of consumer demand
- c. externalities and foreign competition
- d. government intervention and foreign competition

ANSWER: a

126. What term refers to a situation in which markets fail to allocate resources efficiently?

- a. economic depression
- b. market failure
- c. corporate bankruptcy
- d. disequilibrium

ANSWER: b

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127. Which of the following is an example of market power?

- a. a fast food restaurant in a university town
- b. a wheat farmer in Saskatchewan
- c. the only motel is in a remote Yukon town
- d. a shoe store in Ontario

ANSWER: c

128. Which of the following is an example of a firm with market power?

- a. a deli in Winnipeg
- b. a bike rental company in Victoria
- c. the Science Centre in Vancouver
- d. a farmer in Quebec

ANSWER: c

129. What can cause market failure?

- a. low consumer demand
- b. government intervention and price controls
- c. externalities and market power
- d. high prices and foreign competition

ANSWER: c

130. What is an externality?

- a. the impact of one person's actions on the well-being of a bystander
- b. the impact of a person's actions on that person's well-being
- c. the impact of society's decisions on the well-being of another society
- d. the impact of society's decisions on the well-being of one person in the society

ANSWER: a

131. What is an example of an externality?

- a. the impact of bad weather on the income of farmers
- b. the impact of the personal income tax on a person's ability to purchase goods and services
- c. the impact of pollution from a factory on the health of people in the vicinity of the factory
- d. the impact of increases in health care costs on the health of individuals in society

ANSWER: c

132. Which of the following is most likely to generate an externality?

- a. Teachers at a local high school purchase a coffee maker for the staffroom.
- b. A couple with young children moves next door to the children's grandparents.
- c. A newlywed couple buys furniture for their condo.
- d. John buys a tractor to mow his newly purchased five-hectare lot.

ANSWER: b

133. If an externality is present in a market, what may enhance economic efficiency?

- a. government intervention

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- b. increased competition
- c. better informed market participants
- d. more defined property rights

ANSWER: a

134. What will happen if a copper refinery does NOT bear the entire cost of the smoke it emits?

- a. It will not emit any smoke so as to avoid the entire cost of the smoke.
- b. It will emit lower levels of smoke.
- c. It will emit an acceptable level of smoke.
- d. It will emit too much smoke.

ANSWER: d

135. Which of these consumption activities will most likely impose an external cost?

- a. an executive plays a vigorous game of golf
- b. a student in a dorm plays a YouTube video at 120 decibels late at night
- c. a young mother exercises to a yoga video
- d. a construction worker eats a sandwich during his lunch break

ANSWER: b

136. Which activity will most likely result in an external benefit?

- a. a student buys a deck of cards to play solitaire in her dorm room
- b. a group of children plant a vegetable garden on a vacant lot in their neighbourhood
- c. an executive purchases a book to read on a business trip
- d. a 10-year-old buys new Nikes with his allowance money he has saved

ANSWER: b

137. If education produces external benefits for society, what might NOT be an appropriate policy for society to establish regarding education?

- a. tax incentives for schooling
- b. mandatory minimum levels of education
- c. programs that promote the hiring of high school dropouts
- d. free bussing to local high schools

ANSWER: c

138. According to an economic principle, what is the effect of government intervention in the presence of a market failure?

- a. Government action does not improve on the market outcome because sometimes public policies simply reward the politically powerful.
- b. Government action does not improve on the market outcome because some leaders are not fully informed.
- c. Government action can sometimes improve on the market outcome.
- d. Government action will always improve on the market outcome.

ANSWER: c

139. What happens if a sawmill creates too much air pollution?

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- a. Interference by the government will surely make the matter worse.
- b. A sense of social responsibility will cause the owners of the mill to reduce pollution.
- c. The government can raise economic well-being by providing health care to those affected by the pollution.
- d. The government can raise economic well-being through environmental regulation.

ANSWER: d

140. Which term refers to a single entity that has the ability to influence market prices?

- a. competition
- b. market power
- c. efficiency
- d. productivity

ANSWER: b

141. What is market power?

- a. the power of a single person or group to influence market prices
- b. the ability of a person or group of people to successfully market new products
- c. the power of the government to regulate a market
- d. the relative importance of a market to the overall economy

ANSWER: a

142. What is an example of a monopoly?

- a. a jewellery store in Burnaby, British Columbia
- b. a souvenir shop in Cancun, Mexico
- c. an electric company in Outlook, Saskatchewan
- d. a doctor in St. John's, New Brunswick

ANSWER: c

143. Which business most likely has market power?

- a. a furniture store in Kingston
- b. a vineyard in the Okanagan Valley
- c. a maple sugar candy store in Sherbrooke, Quebec
- d. a hockey arena in the small town of Invermere, British Columbia

ANSWER: d

144. How could you justify higher income tax rates on rich people in Canada?

- a. on the basis of market efficiency
- b. on the basis of the lack of other sources of government revenue
- c. on the basis of equity for society
- d. on the basis of government bias against the wealthy

ANSWER: c

145. What is the primary determinant of a country's standard of living?

- a. the ability to reduce foreign competition
- b. the ability to produce goods and services

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- c. the total supply of money in the economy
- d. the average age of the country's labour force

ANSWER: b

146. In 2014, what was the average Canadian income?

- a. \$25,368
- b. \$29,000
- c. \$36,800
- d. \$49,000

ANSWER: d

147. In Canada, incomes have historically grown about 2% per year. At this rate, how long will it take for incomes to double?

- a. 10 years
- b. 25 years
- c. 35 years
- d. 50 years

ANSWER: c

148. What is the income of a typical worker in a country most closely linked to?

- a. population
- b. productivity
- c. the number of labour unions
- d. government policies

ANSWER: b

149. If the average income of an Australian is higher than the average income of a Russian, what is the most likely reason?

- a. Productivity is higher in Australia than in Russia.
- b. Australia has a more industrial economy than Russia.
- c. There is more competition in Australia than in Russia.
- d. Labour unions are more aggressive in Australia than in Russia.

ANSWER: a

150. Suppose that the average income of a Kenyan is higher than the average income of a South African. What might you conclude?

- a. South African firms are faced with stricter government regulations than Kenyan firms.
- b. Total income is divided among fewer workers in Kenya since it has a smaller labour force than South Africa.
- c. Kenya's climate allows for longer growing seasons and therefore Kenya can produce large quantities of grain.
- d. Productivity in Kenya is higher than in South Africa.

ANSWER: d

151. A typical worker in Italy can produce 24 units of product in an eight-hour day, where a typical worker in Poland produces 25 units of product in a 10-hour day. What can we conclude?

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- a. Worker productivity in Poland is higher than in Italy.
- b. The standard of living will be higher in Italy than in Poland.
- c. Productivity for the Polish worker is three units per hour and 2.5 units per hour for the Italian worker.
- d. There will be no difference between the standard of living in Italy and Poland.

ANSWER: b

152. A worker in Bangladesh can earn \$1 per day making cotton cloth on a handloom. A worker in Canada can earn \$100 per day making cotton cloth with a mechanical loom. What accounts for the difference in wages?

- a. Canadian textile workers belong to a union.
- b. There is little demand for cotton cloth in Bangladesh and great demand in Canada.
- c. Labour is more productive making cotton cloth with a mechanical loom than with a hand loom.
- d. Bangladesh has a low-wage policy to make its textile industry more competitive in world markets.

ANSWER: c

153. Over the past century, how much has the average income in Canada risen by?

- a. twofold
- b. fivefold
- c. eightfold
- d. tenfold

ANSWER: c

154. What causes almost all variation in living standards in different countries?

- a. population growth rates
- b. endowments of natural resources
- c. proximity to foreign markets
- d. productivity

ANSWER: d

155. What is the definition of productivity?

- a. the amount of goods and services produced from each hour of a worker's time
- b. the amount of labour that can be saved by replacing workers with machines
- c. the actual amount of effort workers put into an hour of working time
- d. the estimated amount of effort workers put into an hour of working time

ANSWER: a

156. What term refers to the amount of goods and services produced from each hour of a worker's time?

- a. total output
- b. productivity
- c. marginal product
- d. quantity

ANSWER: b

157. Which of the following displays a direct, or positive, relationship?

- a. a country's productivity and its standard of living

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- b. a country's government spending and its tax rates
- c. a country's total population and its per-capita income
- d. a country's prices for its goods and services and its exports

ANSWER: a

158. What might a government do to enact a policy to increase living standards?

- a. allow corporate tax write-offs for money spent on worker safety
- b. make it more difficult to receive unemployment benefits
- c. increase educational opportunities for workers
- d. prohibit unions from organizing

ANSWER: c

159. To improve living standards, what should policymakers do?

- a. impose restriction on foreign competition
- b. formulate policies designed to increase productivity
- c. impose tougher immigration policies
- d. provide subsidized childcare to low-income families

ANSWER: b

160. To increase living standards, what should public policy do?

- a. ensure that workers are well educated and have the necessary tools and technology
- b. make unemployment benefits easier to obtain
- c. move workers into jobs directly from high school
- d. ensure that workers have access to union membership and benefits

ANSWER: a

161. What could policymakers do to raise productivity?

- a. increase spending on education
- b. lower tax credits to firms for capital improvements
- c. reduce the number of imports allowed into the economy
- d. eliminate minimum wage laws

ANSWER: a

162. What is an increase in the overall level of prices in an economy called?

- a. economic growth
- b. inflation
- c. monetary policy
- d. rate of return

ANSWER: b

163. What is the definition of inflation?

- a. a period of rising productivity in the economy
- b. a period of rising income in the economy
- c. an increase in the overall level of output in the economy

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- d. an increase in the overall level of prices in the economy

ANSWER: d

164. What happened when the German government increased the quantity of money in the German economy in the 1920s?

- a. Germany experienced hyperinflation.
- b. More people in Germany could afford luxury goods.
- c. Unemployment increased.
- d. Germany was able to repay all its foreign debts.

ANSWER: a

165. What happened to prices in Germany during the early 1920s?

- a. They doubled annually.
- b. They doubled monthly.
- c. They tripled monthly.
- d. They tripled annually.

ANSWER: c

166. When and where did one of the worst episodes of inflation occur?

- a. in Canada in the 1990s
- b. in Argentina in the 1950s
- c. in Russia in the 1930s
- d. in Germany in the 1920s

ANSWER: d

167. What is almost always the cause of large or persistent inflation?

- a. an increase in demand for domestic production
- b. growth in the quantity of money
- c. foreign competition
- d. higher worker productivity

ANSWER: b

168. What was inflation in Canada in the 1990s?

- a. It was almost zero.
- b. It was about 2 percent per year.
- c. It was approaching double digits.
- d. It was about 10 percent per year.

ANSWER: b

169. During the 1990s, the United Kingdom experienced low levels of inflation while Turkey experienced high levels of inflation. What best explains the difference?

- a. The United Kingdom was more industrialized than Turkey.
- b. The United Kingdom printed money at a slower rate than Turkey.
- c. Workers in the United Kingdom were more productive than workers in Turkey.

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d. There were more cases of market failure in Turkey than in the United Kingdom.

ANSWER: b

170. What does inflation cause?

- a. incomes to fall
- b. productivity to increase
- c. the government to lower taxes
- d. the value of money to fall

ANSWER: d

171. Which statement best describes the relationship between inflation and unemployment?

- a. In the short run, reducing inflation is associated with falling unemployment.
- b. In the short run, reducing inflation is associated with rising unemployment.
- c. In the long run, reducing inflation is associated with falling unemployment.
- d. In the long run, reducing inflation is associated with rising unemployment.

ANSWER: b

172. What is the effect of an increase in the money supply in the economy?

- a. It increases unemployment in the short run.
- b. It increases inflation in the long run.
- c. It increases inflation in the short run.
- d. It increases unemployment in the long run.

ANSWER: b

173. In the short run, what does the tenth principle of economics illustrate?

- a. the tradeoff between inflation and unemployment
- b. the tradeoff between equity and efficiency
- c. labour productivity in an economy
- d. the level of government intervention in a market economy

ANSWER: a

174. Although the tenth principle of economics is controversial, what do most economists believe?

- a. Society faces a tradeoff between unemployment and inflation in the short run only.
- b. Society faces a tradeoff between unemployment and inflation in the long run only.
- c. No tradeoff exists between unemployment and inflation.
- d. Society faces a continuous tradeoff between unemployment and inflation.

ANSWER: a

175. Which policy target will NOT affect the combination of inflation and unemployment the economy experiences?

- a. taxes
- b. government spending
- c. the money supply
- d. market prices

ANSWER: d

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176. What does the tenth principle of economics help explain?

- a. the business cycle
- b. supply and demand
- c. trade balance
- d. money supply changes

ANSWER: a

177. What is the business cycle?

- a. the relationship between unemployment and inflation
- b. the irregular fluctuations in economic activity
- c. the positive relationship between the quantity of money in an economy and inflation
- d. the negative relationship between imports and net exports

ANSWER: b

178. Which statement is consistent with the tenth principle of economics?

- a. If we increase the rate of inflation from 3 percent to 6 percent, then the rate of unemployment will temporarily fall.
- b. If we increase the rate of inflation from 3 percent to 6 percent, then the rate of unemployment will temporarily rise.
- c. If we increase the rate of inflation from 3 percent to 6 percent, then the rate of unemployment will permanently fall.
- d. If we increase the rate of inflation from 3 percent to 6 percent, then the rate of unemployment will permanently rise.

ANSWER: a

179. What would happen if the world's resources were to suddenly double?

- a. The scarcity principle would still apply.
- b. The scarcity principle would not be relevant.
- c. Everyone's wants would be met.
- d. No tradeoffs would be needed.

ANSWER: a

180. The Students' Union on campus provides free popcorn to all students who attend their annual meeting. In this instance, how will the principle of scarcity apply?

- a. It will only apply to students who miss class to attend.
- b. It will apply in terms of the time given up to attend.
- c. It will not apply because the popcorn is free.
- d. It will not apply because no tradeoffs are involved.

ANSWER: b

181. Why are gasoline prices in Canada higher than in the United States?

- a. higher taxes in Canada
- b. larger oil reserves in the United States
- c. higher cost of transporting oil in Canada

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- d. higher cost of refining oil in Canada

ANSWER: a

182. Why is the opportunity cost of gasoline in Canada higher than in the United States when measured by “Minutes Worked per Kilometre Driven”?

- a. The fuel economy in the two countries is different.
- b. Gas prices are lower and average wages are higher in the United States.
- c. Both gas prices and average wages are higher in the United States.
- d. Both gas prices and average wages are lower in the United States.

ANSWER: b

183. What is the best way to measure the opportunity cost of gasoline?

- a. by the average price of a litre of gasoline
- b. by the fuel efficiency of the average North American car
- c. by the pollution emitted per 1 km of driving
- d. by the number of minutes of work needed to pay for 1 km of driving

ANSWER: d

184. What happened to the opportunity cost of gasoline from 1997 to 2014?

- a. increased significantly
- b. decreased significantly
- c. remained relatively constant
- d. decreased slightly

ANSWER: c

185. Monica has spent \$30,000 purchasing and repairing an old cabin, which she expects to sell for \$40,000. She discovers that she needs an additional repair, which will cost \$15,000. She can sell the cabin as it is now for \$25,000. What should she do?

- a. She should take the \$25,000.
- b. She should never sell something for less than its cost.
- c. She should complete the repairs and sell the cabin.
- d. It doesn't matter which action she takes; the outcome is the same either way.

ANSWER: d

186. Mike has spent \$500 purchasing and repairing an old fishing boat, which he expects to sell for \$800. He discovers that he needs an additional repair, which will cost \$600. He can sell the boat as it is now for \$300. What should he do?

- a. He should take the \$300.
- b. He should never sell something for less than its cost.
- c. He should complete the repairs and sell the boat.
- d. It doesn't matter which action he takes; the outcome is the same either way.

ANSWER: d

187. Scarcity means that there is less of a good or resource available than people wish to have.

- a. True

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b. False

ANSWER: True

188. Economics is the study of how fairly goods and services are distributed within society.

a. True

b. False

ANSWER: False

189. With careful planning, we can usually get something that we like without having to give up something else that we like.

a. True

b. False

ANSWER: False

190. Equity means everyone in the economy should receive an equal share of the goods and services produced.

a. True

b. False

ANSWER: False

191. Equity refers to how the pie is divided, and efficiency refers to the size of the economic pie.

a. True

b. False

ANSWER: True

192. Tuition is the single-largest cost of attending college for most students.

a. True

b. False

ANSWER: False

193. The cost of an action is measured in terms of foregone opportunities.

a. True

b. False

ANSWER: True

194. A marginal change is a small incremental adjustment to an existing plan of action.

a. True

b. False

ANSWER: True

195. If the average cost of transporting a passenger on the train from Brockville to Toronto is \$75, it would be irrational for the railroad to allow any passenger to ride for less than \$75.

a. True

b. False

ANSWER: False

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196. A rational decision maker takes an action if and only if the marginal cost exceeds the marginal benefit.

- a. True
- b. False

ANSWER: False

197. Trade allows each person to specialize in the activities he or she does best, thus increasing each individual's productivity.

- a. True
- b. False

ANSWER: True

198. Trade with any nation can be mutually beneficial.

- a. True
- b. False

ANSWER: True

199. A market economy cannot produce a socially desirable outcome because individuals are motivated by their own selfish interests.

- a. True
- b. False

ANSWER: False

200. Since taxes affect only the price paid by the buyer, they cannot have an adverse impact on the allocation of society's resources.

- a. True
- b. False

ANSWER: False

201. The government can potentially improve market outcomes if market inequalities or market failure exist.

- a. True
- b. False

ANSWER: True

202. Market failure refers to a situation in which the market does not allocate resources efficiently.

- a. True
- b. False

ANSWER: True

203. Productivity is defined as the quantity of goods and services produced from each hour of a worker's time.

- a. True
- b. False

ANSWER: True

204. Productivity is the primary determinant of a country's living standards.

- a. True

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b. False

ANSWER: True

205. Inflation increases the value of money.

a. True

b. False

ANSWER: False

206. Government spending is the primary source of inflation.

a. True

b. False

ANSWER: False

207. The tenth principle of economics shows the short-run tradeoff between inflation and economic growth.

a. True

b. False

ANSWER: False

208. What would happen to the study of economics if scarcity disappeared?

ANSWER: Since economics is the study of how society allocates its scarce resources, if there were no scarcity, there would be no need for economics. Everyone could have all the goods and services they wanted. No one would have to make decisions based on tradeoffs, because there would be no opportunity cost associated with the decision. (It is difficult to conceive of a situation where time is not scarce, however.)

209. One tradeoff society faces is between efficiency and equity. Define each term. If the Canadian government redistributes income from the rich to the poor, explain how this action affects equity as well as efficiency in the economy.

ANSWER: Efficiency is the property of society getting the most it can from its scarce resources. Equity is defined as the property of distributing economic prosperity fairly among the members of society. Often, these two goals conflict. When the government redistributes income from the rich to the poor, it reduces the reward for working hard. Fewer goods and services are produced and the economic pie gets smaller. When the government tries to cut the economic pie into more equal slices, the pie gets smaller. Policies aimed at achieving a more equal distribution of economic well-being, such as the welfare system, try to help those members of society who are most in need. The individual income tax asks the financially successful to contribute more than others to support the government.

210. Define opportunity cost. What is the opportunity cost to you of attending university? What was your opportunity cost of coming to class today?

ANSWER: Whatever must be given up to obtain some item is its opportunity cost. Basically, this would be a person's second choice. The opportunity cost of a person attending college is the value of the best alternative use of that person's time. For most students this would be the income the student gives up by not working. A student's opportunity cost of coming to class was the value of the best opportunity the student gave up.

211. With the understanding that people respond to incentives, outline the possible outcome for teachers if the K–12 school year is extended to 11 months per year instead of the existing 10 months per year.

ANSWER: The concept of working longer per year would be perceived by many teachers as a definite increase in the cost of teaching. Even with additional compensation, many teachers look at summers off as a major benefit of the education profession. If this benefit were eliminated or even diminished, some teachers may perceive that the marginal cost of teaching would now be greater than the marginal benefit and would choose to leave teaching.

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212. Under what conditions might government intervention in an economy improve the market outcome?

ANSWER: If there is a market failure, such as an externality or monopoly, government regulation might improve the well-being of society by promoting efficiency. If the distribution of income or wealth is considered to be unfair by society, government intervention might achieve a more equitable distribution of economic well-being.

213. Explain how an attempt by the government to lower inflation could cause unemployment to increase in the short run.

ANSWER: To lower inflation, the government may choose to reduce the money supply in the economy. When the money supply is reduced, prices do not adjust immediately. Lower spending, combined with prices that are too high, reduces sales and causes workers to be laid off. Hence, the lower price level is associated with higher unemployment.

214. In each of the following decision situations, show what tradeoffs are involved.

- a) You are driving and need to decide how fast to drive.
- b) You meet a young lady at a party and you are considering whether to ask her out.
- c) You like a co-worker whom you have known for a couple of years, and you need to decide whether to go on a date with him.
- d) You ponder moving back with your parents.
- e) You need to decide whether to buy a used or a new car.
- f) You are thinking about opening a computer services business in your basement.
- g) You are a consultant for the City of Toronto. The city council asks you to analyze the implications of a new high-rise office building in downtown.

ANSWER:

- a) Driving faster gets you earlier to your destination. However, driving faster is less safe, takes more gas, and may get you a ticket.
- b) If you ask her out you might enjoy her company and form a long-term relationship. However, you may not enjoy her company, wasting some time and money. Moreover, if you ask her and she refuses, you will feel humiliated, wishing you had not done so.
- c) If you ask him and he accepts, you will enjoy his company and you may have a long-term relationship. However, you may get to know a side of his personality that you may not like, or he may not like you, and you will both be embarrassed and try to avoid each other at work.
- d) If you move back with your parents, you will have to comply with the rules of the house. You will enjoy less freedom, but more money and, perhaps, a more comfortable life.
- e) A used car may be substantially cheaper, it requires lower insurance costs, and you do not need to pay interest on the loan that you might need for the new car. However, it may break down more often and it may be less fun to own and drive.
- f) There are many positive sides of having your own business, starting from learning how to run it to the profits you might make. The costs of running it are, however, substantial: you could rent your basement for a monthly rental fee, you could use your time in a more lucrative employment, or you could use more of your time for travelling.
- g) A new office building will contribute to the economic and social development of the city. There are, however, costs such as an increase in traffic congestion or higher prices because of the increased demand for adjacent services and utilities.

215. An economic principle is that people respond to incentives. Identify the incentives and discuss the possible outcomes in each of the following situations.

- a) A Liberal government decides to increase the level of required health benefits that firms pay on behalf of their employees.
- b) The City of Winnipeg decides to set a rather high regulated parking fee in downtown in order to reduce traffic congestion.
- c) A very popular hip-hop singer asks his managers to set concert prices very low such that everybody can afford them.

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- d) The government of Canada subsidizes the purchases of new electric cars.
- e) A provincial government subsidizes tuition fees for all students who get admitted to college for the whole period of studies.
- f) A father gives his daughter \$50 when she gets a grade of D at school, \$100 for a C, \$500 for a B, and \$1000 for an A.

ANSWER:

- a) People will increase their demand for health services beyond the system's capacity when health care becomes more affordable. Firms, on the other hand, will hire fewer workers as the cost of labour increases due to the new health benefits provisions.
- b) When parking fees are high, traffic congestion may not decrease as desired. Why? Because high parking fees makes building more parking lots by private entrepreneurs more profitable. With more parking lots available, people who were previously deterred by the difficulty of finding a parking spot will prefer now to drive to work.
- c) If tickets to a concert are cheap, some entrepreneurs will buy a large number of them to re-sell them for profit. Thus, those who were supposed to benefit from the lower prices will actually have to pay even more. The benefit from low prices goes to the entrepreneurs.
- d) Subsidizing a certain industry always diverts resources from other production sectors. Besides, the subsidized sector does not face the true market costs of their activity, and are not well prepared to survive when the subsidies are terminated.
- e) When tuition is fully subsidized, more students will want to go to college, but many have little incentive to devote great effort to their studies.
- f) After a few good grades and a sufficient amount of money, the daughter might find working hard for an A not worth the effort.

216. Suppose you have your own pizza delivery business and receive a call to deliver to a remote client. You need to decide whether to take the call. If you don't, there are no consequences, since someone else will. Based on the distance to the client, you calculate that it would cost you \$5 to deliver, and expect to receive \$6 for the service. You also pay monthly rent for the car, which on average, based on past experience, comes down to about \$2 per trip. Your time doesn't matter, as you have nothing more enjoyable or useful to do for the time being. How do you make this decision? What economic principle is at work in your decision process?

ANSWER: The benefit from the trip is \$6 and the overall cost is $\$5 + \$2 = \$7$. Apparently, the cost exceeds the benefit, so you should not take the job. However, this conclusion is wrong, because you pay the rent no matter how many calls you take. Therefore, the \$2 rent is irrelevant in deciding whether to take a new call. The correct way of thinking is to compare the additional benefit of \$6 to the additional cost of \$5 and take the call. The main principle involved in this problem is that people think at the margin: an action should be undertaken only if the additional costs are less than the additional benefits. Costs that are not directly related to the action and have to be paid anyway are irrelevant.

217. In each of the following situations, identify the relevant economic principle and explain how it applies.

- a) Peter has lived in his own apartment for many years. However, rents have recently increased so much that Peter considers moving into a smaller apartment and renting out his own.
- b) Alfonso is a talented singer and he strongly wants to pursue an artist's career. However, he is two years short of graduating from law school. He is certain he will never be a lawyer because he does not like it and has no gift to be a lawyer. However, his family insists he finish his studies, since he has already spent so much time and money on law studies. What should he do?
- c) There are a few industrial sites in town, producing essential goods and services for the residents and providing the citizens with vital jobs. However, the businesses, including an airport in the very downtown, also produce pollution, congestion, and noise. People understand the blessings of economic and civil freedoms and are pleased and proud to have productive activities in their town. They started, though, to crave for a more pleasant place to live in. What economic principle can give these people some guidance about what to do?

ANSWER:

- a) Though Peter does not pay rent for living in his apartment, he misses the opportunity of making a good profit. This missed opportunity is, in fact, Peter's cost of living in his home. The economic principle guiding Peter's decision is Principle #2, which defines opportunity cost.

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- b) Since Alfonso is certain he will never be a lawyer, there is no point in continuing his studies. (The only reason for doing so would be if there was a reasonable chance that he would be forced in the future to make a living using his law studies.) The economic principle at work here is that sunk (past) costs are irrelevant when making decisions.
- c) Under some conditions such as pollution, the existence of a government can improve the outcome of a free market economy. Thus, the people in the small town should get together and draft regulations that limit companies' appetite for pollution.

218. For your birthday, your friends have joined forces and offer you a choice among the following options (they will pay all expenses of your choice): A) A two-week trip to an exotic destination; B) A new, high-tech mountain bike, C) An annual pass to your preferred sports team games, and D) A dinner with your preferred celebrity. Suppose your subjective valuations of these options are as follows: A)\$800, B)\$700, C)\$1500, and D)\$1000. If you are a rational individual, you will obviously choose C, the annual pass, because it is the option of your highest valuation.

- a) What is your opportunity cost of choosing option C? Explain.
- b) Now, suppose your friends announce at the last minute a fifth option, E, a cheque of \$1100. What is now your opportunity cost of choosing option C?
- c) As you can see, the theory of opportunity cost implies that the cost of an action depends on other, seemingly unrelated facts. Why does this make sense?

ANSWER: a) The opportunity cost of an action is your valuation of the next desired alternative. In this case, the next-desired alternative is the dinner, which you value at \$1000. In other words, you "pay" (i.e., give up) \$1000 for your annual pass.

b) When the new alternative becomes available, your (opportunity) cost of choosing the pass raises to \$1100.

c) Although you do not actually pay anything for any of these choices, there is a cost for choosing one over another. To see why this makes sense, think of the following scenario: Suppose that after making and announcing your choice you found out that there was yet another choice available, of which you were not aware. That sixth alternative would have been a flight to the International Space Station, which would have given you an immense pleasure. Would you regret just a little bit that you chose the annual pass instead of the outer space trip that was simply lost in your inbox? Do you feel you have just lost something? If yes, it proves that the opportunity cost theory does make some sense.