

Business in Action, 6e (Bovee/Thill)

Chapter 2 Understanding Basic Economics

1) Economics is the study of how a society uses its scarce resources to produce and distribute goods and services to its citizens.

Answer: TRUE

Explanation: Economics is the study of how a society uses its scarce resources to produce and distribute goods and services to its citizens.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 1

Course LO: Compare and contrast different economic systems

Classification: Concept

2) Macroeconomics studies economic behavior among consumers, businesses, and industries that collectively determine the quantity of goods and services demanded and supplied at different prices.

Answer: FALSE

Explanation: The study of a country's larger economic issues, such as how firms compete, the effect of government policies, and how an economy maintains and allocates its scarce resources, is termed macroeconomics.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 1

Course LO: Compare and contrast different economic systems

Classification: Concept

3) Capital includes land and minerals that a business needs in order to produce goods and services.

Answer: FALSE

Explanation: Capital includes money, computers, machines, tools, and buildings that a business needs in order to produce goods and services.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 1

Course LO: Compare and contrast different economic systems

Classification: Concept

4) Capital is the collective intelligence of an organization.

Answer: FALSE

Explanation: Capital includes money, computers, machines, tools, and buildings that a business needs in order to produce goods and services.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 1

Course LO: Compare and contrast different economic systems

Classification: Concept

5) Scarcity creates competition for resources, and forces trade-offs on the part of every participant in the economy.

Answer: TRUE

Explanation: Scarcity has two powerful effects: It creates competition for resources, and it forces trade-offs on the part of every participant in the economy.

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Difficulty: Moderate

AACSB: Dynamics of the Global Economy

Chapter LO: 1

Course LO: Compare and contrast different economic systems

Classification: Concept

6) Deciding how much money to spend on new manufacturing equipment versus launching a new advertising campaign is described as opportunity cost.

Answer: FALSE

Explanation: Opportunity cost refers to the value of the most appealing alternative from all those that weren't chosen. In other words, opportunity cost is a way to measure the value of what you gave up when you pursued a different opportunity.

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Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 1

Course LO: Compare and contrast different economic systems

Classification: Application

7) Capitalism is a term used to describe the free-market system, one in which private parties own and operate the majority of businesses and where competition, supply, and demand determine which goods and services are produced.

Answer: TRUE

Explanation: Capitalism is a term used to describe the free-market system, one in which private parties own and operate the majority of businesses and where competition, supply, and demand determine which goods and services are produced.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Concept

8) In practice, no economy is truly a free-market economy.

Answer: TRUE

Explanation: Free market economy is a situation in which so many buyers and sellers exist that no single buyer or seller can individually influence market prices. In practice, no economy is truly a free-market economy.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Concept

9) As social equality is a major goal of planned systems, private enterprise and the pursuit of private gain are encouraged.

Answer: FALSE

Explanation: In a planned system, governments largely control the allocation of resources and limit freedom of choice in order to accomplish government goals. Private enterprise and the pursuit of private gain are not encouraged in such a system.

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Difficulty: Moderate

AACSB: Dynamics of the Global Economy

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Concept

10) By taking an ownership of 60% in General Motors in 2009, the U.S. nationalized the automaker.

Answer: TRUE

Explanation: Nationalizing refers to a government's takeover of selected companies or industries. In the given situation, the government has attained a majority stake and the situation is an example of nationalization.

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Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Application

11) Demand refers to the quantities of a good or service that producers will provide on a particular date at various prices.

Answer: FALSE

Explanation: Demand refers to buyers' willingness and ability to purchase products at various price points.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 3

Classification: Concept

12) The demand curve will shift to the left if the price of substitute products increases.

Answer: FALSE

Explanation: The demand curve will shift to the right if the price of substitute products increases.

Page Ref: 31

Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 3

Classification: Application

13) Movement along the supply curve typically slopes upward.

Answer: TRUE

Explanation: Movement along the supply curve typically slopes upward: As prices rise, the quantity that sellers are willing to supply also rises. Similarly, as prices decline, the quantity that sellers are willing to supply declines.

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Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 3

Classification: Concept

14) The supply curve of a firm will shift to the right if technology increases the firm's production costs.

Answer: FALSE

Explanation: The supply curve of a firm will shift to the left if technology increases the firm's production costs.

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Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 3

Classification: Application

15) The point at which quantity of a good or service equals the quantity demanded is known as the equilibrium point.

Answer: TRUE

Explanation: The point at which quantity of a good or service equals the quantity demanded is known as the equilibrium point.

Page Ref: 32

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 3

Classification: Concept

16) The situation in which one supplier thoroughly dominates a market and essentially shuts out other competitors is called monopoly.

Answer: TRUE

Explanation: The situation in which one supplier thoroughly dominates a market and essentially shuts out other competitors is called monopoly.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

17) A deep and prolonged recession can be considered as a depression.

Answer: TRUE

Explanation: A deep and prolonged recession can be considered a depression, which doesn't have an official definition but is generally considered to involve a catastrophic collapse of financial markets.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

18) Frictional unemployment is caused by economic fluctuations.

Answer: FALSE

Explanation: Frictional unemployment refers to the natural flow of workers into and out of jobs, such as when a person leaves one job without first lining up a new job.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

19) Deflation is an economic condition in which prices fall steadily throughout the economy.

Answer: TRUE

Explanation: Deflation is an economic condition in which prices fall steadily throughout the economy.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

20) Cyclical unemployment is caused by a mismatch between workers' skills and current employer needs.

Answer: FALSE

Explanation: Cyclical unemployment refers to seasonal unemployment caused by economic fluctuations. When demand for goods and services drops, businesses reduce production, thereby requiring fewer workers.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

21) Economic development zones, established by governments, offer a variety of financial incentives to businesses that meet specific job creation and local investment criteria.

Answer: TRUE

Explanation: Economic development zones, established by governments, offer a variety of financial incentives to businesses that meet specific job creation and local investment criteria.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 5

Course LO: Explain how economic performance is monitored

Classification: Concept

22) Monetary policy involves changes in the government's revenues and expenditures to stimulate a slow economy or dampen a growing economy that is in danger of overheating and causing inflation.

Answer: FALSE

Explanation: Monetary policy involves adjusting the nation's money supply, the amount of "spendable" money in the economy at any given time, by increasing or decreasing interest rates.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 5

Course LO: Explain how economic performance is monitored

Classification: Concept

23) Sales taxes are the government's largest single source of revenue.

Answer: FALSE

Explanation: Income taxes are the government's largest single source of revenue.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 5

Course LO: Explain how economic performance is monitored

Classification: Concept

24) Leading economic indicators suggest changes that may happen in the economy in the future.

Answer: TRUE

Explanation: Leading economic indicators suggest changes that may happen in the economy in the future.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 6

Course LO: Explain how economic performance is monitored

Classification: Concept

25) GDP considers who is responsible for the production; GNP considers where the production occurs.

Answer: FALSE

Explanation: GNP considers who is responsible for the production; GDP considers where the production occurs.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 6

Course LO: Explain how economic performance is monitored

Classification: Concept

26) _____ is the study of how a society uses its scarce resources to produce and distribute goods and services.

- A) Anthropology
- B) Economics
- C) Proxemics
- D) Entrepreneurship
- E) Sociology

Answer: B

Explanation: B) Economics is the study of how a society uses its scarce resources to produce and distribute goods and services.

Page Ref: 26

Difficulty: Easy

Chapter LO: 1

Course LO: Compare and contrast different economic systems

Classification: Concept

27) Microeconomics is the study of _____.

- A) the costs of production as a means of stimulating the economy and policies that raise capital and labour output by increasing the incentive to produce
- B) economic and financial data of the country by the application of mathematics and statistics
- C) the overall working of an economy in the society including its monetary and fiscal policies
- D) economic behavior among consumers, businesses, and industries that collectively determine the quantity of goods and services demanded and supplied at different prices
- E) a nation's economic issues, such as the effect of government policies and the ownership of factors of production

Answer: D

Explanation: D) The study of economic behavior among consumers, businesses, and industries that collectively determine the quantity of goods and services demanded and supplied at different prices is termed microeconomics.

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Difficulty: Easy

Chapter LO: 1

Course LO: Compare and contrast different economic systems

Classification: Concept

28) The study of a country's larger economic issues, such as how firms compete, the effect of government policies, and how an economy maintains and allocates its scarce resources, is known as _____.

- A) capitalism
- B) entrepreneurship
- C) microeconomics
- D) socialism
- E) macroeconomics

Answer: E

Explanation: E) The study of a country's larger economic issues, such as how firms compete, the effect of government policies, and how an economy maintains and allocates its scarce resources, is termed macroeconomics.

Page Ref: 26

Difficulty: Easy

Chapter LO: 1

Course LO: Compare and contrast different economic systems

Classification: Concept

29) Which of the following refers to people and their individual talents and capacities?

- A) natural resources
- B) knowledge
- C) capital investments
- D) human resources
- E) entrepreneurship

Answer: D

Explanation: D) Human resources are people and their individual talents and capacities.

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Difficulty: Easy

Chapter LO: 1

Course LO: Compare and contrast different economic systems

Classification: Concept

30) The money, computers, machines, tools, and buildings that a business needs in order to produce its good and services are called _____.

- A) natural resources
- B) human resources
- C) capital
- D) knowledge
- E) entrepreneurship

Answer: C

Explanation: C) Capital includes money, computers, machines, tools, and buildings that a business needs in order to produce goods and services.

Page Ref: 26

Difficulty: Easy

Chapter LO: 1

Course LO: Compare and contrast different economic systems

Classification: Concept

31) _____ is the spirit of innovation, the initiative, and the willingness to take the risks involved in creating and operating businesses.

- A) Capitalization
- B) Socialization
- C) Merchandizing
- D) Automation
- E) Entrepreneurship

Answer: E

Explanation: E) Entrepreneurship is the spirit of innovation, the initiative, and the willingness to take the risks involved in creating and operating businesses.

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Difficulty: Easy

Chapter LO: 1

Course LO: Compare and contrast different economic systems

Classification: Concept

32) _____ is a concept that refers to the finite supply of resources.

- A) Redundancy
- B) Scarcity
- C) Deficit
- D) Stringency
- E) Shortage

Answer: B

Explanation: B) Scarcity doesn't mean a shortage of a particular resource; rather, it means that the resource has a finite supply.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 1

Course LO: Compare and contrast different economic systems

Classification: Concept

33) A business owner has to decide whether the company should purchase new manufacturing equipment, open a new retail store in another city, or invest in a major advertising campaign. This decision to give up something to get something else is referred to as _____.

- A) resource development analysis
- B) an arbitrage
- C) demand/supply determination
- D) a trade-off
- E) factor analysis

Answer: D

Explanation: D) Given the universal scarcity of resources, consumers, companies, and governments are constantly forced to make trade-offs, meaning they have to give up something to get something else.

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Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 1

Course LO: Compare and contrast different economic systems

Classification: Application

34) A business owner has to decide whether the company should purchase new manufacturing equipment, open a new retail store in another city, or invest in a major advertising campaign. The value of the most appealing alternative that the business owner did not choose is its _____.

- A) break-even value
- B) decisional value
- C) opportunity cost
- D) factor analysis determination
- E) resource value

Answer: C

Explanation: C) Opportunity cost refers to the value of the most appealing alternative from all those you didn't choose. In other words, opportunity cost is a way to measure the value of what you gave up when you pursued a different opportunity.

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Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 1

Course LO: Compare and contrast different economic systems

Classification: Application

35) A _____ is an economic system in which individuals and companies are largely free to decide what products to produce, how to produce them, whom to sell them to, and at what price to sell them.

- A) planned system
- B) regulated economy
- C) socialist economy
- D) free-market system
- E) communist economy

Answer: D

Explanation: D) In a free-market system, individuals and companies are largely free to decide what products to produce, how to produce them, whom to sell them to, and at what price to sell them. In other words, they have the chance to succeed - or to fail - by their own efforts.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Concept

36) The economic system of the U.S. is such that individuals own and operate the majority of businesses with limited economic intervention by the government. This is characteristic of a _____ economy.

- A) mixed
- B) planned
- C) capitalist
- D) free-market
- E) communist

Answer: A

Explanation: A) The practice of limited intervention is characteristic of a mixed economy or mixed capitalism, which is the economic system of the United States and most other countries. For example, government bodies intervene in the U.S. economy in a variety of ways, such as influencing particular allocations of resources through tax incentives, prohibiting or restricting the sale of certain goods and services, or setting price controls.

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Difficulty: Moderate

AACSB: Dynamics of the Global Economy

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Application

37) Which of the following is characteristic of a country with a planned economic system?

A) The economy relies chiefly on market forces to allocate goods and resources and to determine prices.

B) The economic system combines private and state enterprises with limited intervention from the government.

C) The economy subscribes to capitalistic competition, where private parties own and operate the majority of businesses.

D) The economic system is primarily capitalistic but there is some degree of government ownership of the means of production.

E) The economy is largely controlled by the government and freedom of choice is limited in order to accomplish government goals.

Answer: E

Explanation: E) In a planned system, governments largely control the allocation of resources and limit freedom of choice in order to accomplish government goals. Because social equality is a major goal of planned systems, private enterprise and the pursuit of private gain are generally regarded as wasteful and exploitive.

Page Ref: 29

Difficulty: Moderate

AACSB: Dynamics of the Global Economy

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Concept

38) The economic system that allows individuals the least degree of economic freedom is _____.

A) socialism

B) communism

C) capitalism

D) authoritarianism

E) mixed capitalism

Answer: B

Explanation: B) The planned economic system that allows individuals the least degree of economic freedom is communism, which still exists in a few countries, most notably North Korea and China.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Concept

39) In a country, the state owns all major productive resources from electricity to transportation. The country has very few opportunities for entrepreneurship and the economic classes are absent. The economy of this country is characterized by which of the following economic systems?

- A) anarchism
- B) communism
- C) capitalism
- D) socialism
- E) mixed

Answer: B

Explanation: B) In communism, the state owns of all the major productive resources. Economic classes are absent and there are few opportunities for entrepreneurship.

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Difficulty: Moderate

AACSB: Dynamics of the Global Economy

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Application

40) _____ lies somewhere between capitalism and communism, with a fairly high degree of government planning and some government ownership of capital resources.

- A) Totalitarianism
- B) Liberalism
- C) Authoritarianism
- D) Socialism
- E) Anarchism

Answer: D

Explanation: D) Socialism lies somewhere between capitalism and communism, with a fairly high degree of government planning and some government ownership of capital resources.

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Difficulty: Easy

AACSB: Analytic Skills

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Concept

41) In a country, the government owns many of the key industrial sectors, such as transportation, health care, and communications. Private ownership, however, is allowed in other industries. What type of economic system does this country have?

- A) communism
- B) capitalism
- C) free-market economy
- D) socialism
- E) totalitarianism

Answer: D

Explanation: D) Socialism lies somewhere between capitalism and communism, with a fairly high degree of government planning and some government ownership of capital resources. However, government ownership tends to be focused in industries considered vital to the common welfare, such as transportation, health care, and communications. Private ownership is permitted in other industries.

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Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Application

42) In 2008, the British government became the majority owner of the Royal Bank of Scotland, the second-largest bank in Britain, in an attempt to prevent the bank from collapsing. This is an example of _____.

- A) privatization
- B) anarchism
- C) capitalism
- D) nationalization
- E) socialization

Answer: D

Explanation: D) Governments can change the structure of the economy by nationalizing - assuming ownership of - selected companies or, in extreme cases, even entire industries. Nationalization is less common and more drastic, but it has happened in recent years, most notably during the recent global banking crisis.

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Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Application

43) Which of the following actions of the government indicates the privatization of an industry?

- A) allowing private businesses to operate in an industry that was previously operated by the government
- B) discouraging private business to operate in an industry that is critical for the growth of the economy
- C) acquiring the market leader to gain control of the industry and its resources
- D) imposing taxes on scarce raw materials to discourage unfair pricing by its suppliers
- E) imposing regulations on multinational businesses to protect local businesses

Answer: A

Explanation: A) Governments can change the structure of the economy by nationalizing - assuming ownership of - selected companies or, in extreme cases, even entire industries. They can also move in the opposite direction, privatizing services once performed by the government by allowing private businesses to perform them instead.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Concept

44) The U.S. government's use of Blackwater Security Consulting, a military security company, to guard officials and military installations in Iraq is an example of _____.

- A) privatization
- B) nationalization
- C) capitalization
- D) socialization
- E) communism

Answer: A

Explanation: A) The process of turning over services once performed by the government by allowing private businesses to perform them instead, is known as privatization.

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Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Application

45) _____ refers to the amount of a good or service that customers will buy at a given time.

- A) Demand
- B) Utility
- C) Equilibrium
- D) Necessity
- E) Want

Answer: A

Explanation: A) Demand refers to the amount of a good or service that customers will buy at a given time.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 3

Course LO: Explain how economic performance is monitored

Classification: Concept

46) _____ refers to the quantities of a good or service that producers will provide on a particular date at various prices.

- A) Necessity
- B) Supply
- C) Demand
- D) Utility
- E) Want

Answer: B

Explanation: B) Supply refers to the quantities of a good or service that producers will provide on a particular date at various prices.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 3

Course LO: Explain how economic performance is monitored

Classification: Concept

47) A(n) _____ is a graph showing the relationship between the amount of product that buyers will purchase at various prices, all other factors being equal.

- A) supply curve
- B) inflation rate
- C) demand curve
- D) deflation rate
- E) competitive balance

Answer: C

Explanation: C) A demand curve is a graph showing the relationship between the amount of product that buyers will purchase at various prices, all other factors being equal.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 3

Course LO: Explain how economic performance is monitored

Classification: Concept

48) Demand curves typically slope downward. This implies that a(n) _____.

- A) decrease in price will increase the quantity demanded
- B) decrease in price will decrease the quantity demanded
- C) increase in price will increase the quantity demanded
- D) decrease in price will have no effect on quantity demanded
- E) increase in price will have no effect on quantity demanded

Answer: A

Explanation: A) Demand curves typically slope downward, implying that as price drops, more people are willing to buy.

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Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 3

Course LO: Explain how economic performance is monitored

Classification: Application

49) If consumer demand for a product decreases, the demand curve _____.

- A) moves downward
- B) moves upward
- C) moves to the right
- D) moves to the left
- E) remains stationary

Answer: D

Explanation: D) If overall demand for a product decreases, the entire demand curve moves to the left.

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Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 3

Course LO: Explain how economic performance is monitored

Classification: Concept

50) The _____ depicts the relationship between prices and quantities that sellers will offer for sale, regardless of demand.

- A) demand curve
- B) supply curve
- C) equilibrium point
- D) business cycle
- E) competitive analysis

Answer: B

Explanation: B) The depiction of the relationship between prices and quantities that sellers will offer for sale is called a supply curve.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 3

Course LO: Explain how economic performance is monitored

Classification: Concept

- 51) Movement along the supply curve typically slopes upward because _____.
A) the amount of government regulation in an industry rises with increase in demand
B) the quantity that the sellers are willing to supply rises with decrease in demand
C) the amount of government regulation in an industry rises with increase in price
D) the quantity that the sellers are willing to supply rises with increase in government regulation
E) the quantity that the sellers are willing to supply rises with increase in price

Answer: E

Explanation: E) Movement along the supply curve typically slopes upward: as prices rise, the quantity that sellers are willing to supply also rises. Similarly, as prices decline, the quantity that sellers are willing to supply declines.

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Difficulty: Moderate

AACSB: Dynamics of the Global Economy

Chapter LO: 3

Course LO: Explain how economic performance is monitored

Classification: Concept

- 52) The point at which the demand and supply curves intersect - the point at which the quantity demanded and supplied are equal - is called the _____.

- A) equilibrium point
- B) aggregation point
- C) marginal point
- D) break-even point
- E) distribution point

Answer: A

Explanation: A) The point at which the demand and supply curves intersect - the point at which the quantity demanded and supplied are equal - is the equilibrium point.

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Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 3

Course LO: Explain how economic performance is monitored

Classification: Concept

53) Colonel's Burgers sells 2500 of its flagship burger, Colonel's Treat, each month at a price of \$10 each. The customers are willing to buy 2500 Colonel's Treat burgers each month at the same price. Hence, the price of \$10 per burger is the _____.

- A) sunk cost
- B) break-even price
- C) equilibrium price
- D) opportunity cost
- E) incremental cost

Answer: C

Explanation: C) The point at which demand and supply are equal is known as the equilibrium point. At the equilibrium price point, customers are willing to buy as many burgers as Colonel's Burgers is willing to sell.

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Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 3

Course LO: Explain how economic performance is monitored

Classification: Application

54) _____ is a situation in which no single firm is large enough to influence prices and distort the workings of the free-market system.

- A) Pure monopoly
- B) Pure monopsony
- C) Pure competition
- D) Regulated monopoly
- E) Stabilized monopoly

Answer: C

Explanation: C) Pure competition is a situation in which no single firm is large enough to influence prices and distort the workings of the free-market system.

Page Ref: 34

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

55) Which of the following is a distinct characteristic of a pure monopolistic economy?

- A) many small suppliers, with virtually identical products.
- B) small number of suppliers with products, which can be distinguished in important ways
- C) only one supplier, with monopoly granted by government mandate
- D) only one supplier, with monopoly achieved by innovation and specialization
- E) few suppliers, with products that can be distinguished but are similar enough to be replacements

Answer: D

Explanation: D) In a pure monopoly, only one supplier is in a given market. Monopoly is achieved without government intervention by innovation, specialization, exclusive contracts, or by a simple lack of competitors. Products are unique, with no direct replacements available.

Barriers to entry are extremely high, making the market difficult or impossible to enter.

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Difficulty: Difficult

AACSB: Dynamics of the Global Economy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

56) Due to government mandate, only one company has the exclusive right to provide electricity in all the cities of Borgia. This is an example of a _____.

- A) pure competition
- B) pure monopoly
- C) regulated monopoly
- D) monopolistic competition
- E) regulated monopsony

Answer: C

Explanation: C) Monopolies can happen "naturally," as companies innovate or markets evolve (a pure monopoly) or by government mandate (a regulated monopoly).

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Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Application

57) There are 10 pizza restaurants in a city. Each restaurant claims to have the "best pizza in town" and advertises the ways in which its pizza is different and better than its competitors' pizzas. This is an example of a(n) _____.

- A) regulated monopoly
- B) monopsony
- C) regulated monopsonic competition
- D) monopolistic competition
- E) monopoly

Answer: D

Explanation: D) Most of the competition in advanced free-market economies is monopolistic competition, in which a number of sellers offer products that can be distinguished from competing products in at least some small way.

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Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Application

58) Which of the following is true of the pricing in a market of monopolistic competition?

- A) No single firm can grow large enough to influence prices across the market.
- B) Firms that excel in one or more aspects can gain some control over pricing.
- C) All firms have considerable control over pricing.
- D) Suppliers have total control over the pricing of products.
- E) Prices are set by government mandate.

Answer: B

Explanation: B) In a market characterized by monopolistic competition, firms that excel in one or more aspects can gain some control over pricing.

Page Ref: 35

Difficulty: Moderate

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

59) When the number of competitors in a market is quite small, a situation known as _____ is created.

- A) monopoly
- B) monopsony
- C) oligopoly
- D) monopolistic competition
- E) pure competition

Answer: C

Explanation: C) When the number of competitors in a market is quite small, a situation known as oligopoly is created. Customers have some choice, unlike in a monopoly, but not as many choices as in monopolistic competition.

Page Ref: 35

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

60) Which of the following is a characteristic feature of economic contraction?

- A) decreased unemployment rates
- B) decreased consumer spending
- C) increased income
- D) increased employment
- E) increased demand

Answer: B

Explanation: B) Economic contraction occurs when such spending declines, employment drops, and the economy as a whole slows down.

Page Ref: 36

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

61) _____ is defined as having two consecutive quarters of decline in the country's gross domestic product.

- A) Deflation
- B) Stagnation
- C) Immobilism
- D) Stagflation
- E) Recession

Answer: E

Explanation: E) If the period of downward swing is severe, the nation may enter into a recession, traditionally defined as two consecutive quarters of decline in the gross domestic product.

Page Ref: 36

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

62) A deep and prolonged recession is known as a(n) _____.

- A) contraction
- B) stagnation
- C) deflation
- D) immobilism
- E) depression

Answer: E

Explanation: E) A deep and prolonged recession can be considered a depression, which doesn't have an official definition but is generally considered to involve a catastrophic collapse of financial markets.

Page Ref: 36

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

- 63) When a downward swing or recession is over, the economy enters into a period of _____.
A) recovery
B) depression
C) contraction
D) stagnation
E) immobilism

Answer: A

Explanation: A) When a downward swing or recession is over, the economy enters into a period of recovery.

Page Ref: 36

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

- 64) _____ unemployment is the natural movement of workers into and out of jobs, such as when a person quits one job without first lining up a new job.

- A) Structural
- B) Intrinsic
- C) Frictional
- D) Cyclical
- E) Seasonal

Answer: C

Explanation: C) Frictional unemployment is the natural movement of workers into and out of jobs, such as when a person quits one job without first lining up a new one.

Page Ref: 37

Difficulty: Easy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

65) When demand for goods and services drops, businesses reduce production, thereby requiring fewer workers. The unemployment resulting because of this phenomenon is known as _____ unemployment.

- A) intrinsic
- B) cyclical
- C) structural
- D) seasonal
- E) frictional

Answer: B

Explanation: B) When demand for goods and services drops, businesses reduce production, thereby requiring fewer workers. This leads to cyclical unemployment.

Page Ref: 37

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

66) Workers in a country are unable to find jobs that match their qualifications and the employers are unable to find employees with the skills required to perform the job. This has led to _____ unemployment in this country.

- A) frictional
- B) seasonal
- C) structural
- D) cyclical
- E) intrinsic

Answer: C

Explanation: C) When workers can't find jobs that match their qualifications, and employers can't find employees with the skills their job openings require, it leads to structural unemployment.

Page Ref: 37

Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Application

67) Which of the following types of unemployment is common in industries with predictable increases and decreases in customer demand?

- A) structural
- B) frictional
- C) intrinsic
- D) seasonal
- E) cyclical

Answer: D

Explanation: D) Predictable increases and decreases in the need for workers in industries with seasonal fluctuations in customer demand, lead to seasonal unemployment. It is most common in agriculture, leisure and entertainment, retailing, and accounting services.

Page Ref: 37

Difficulty: Moderate

AACSB: Dynamics of the Global Economy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

68) _____ is a steady rise in the average prices of goods and services throughout the economy.

- A) Recession
- B) Depression
- C) Deflation
- D) Inflation
- E) Arbitration

Answer: D

Explanation: D) Inflation is a steady rise in the average prices of goods and services throughout the economy.

Page Ref: 36

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

69) Inflation is a major concern for consumers, businesses, and government leaders because it _____.

- A) is a precursor to recession
- B) decreases the purchasing power of consumers
- C) decreases the production costs
- D) increases the demand for commodities
- E) decreases the opportunity cost of holding cash balances

Answer: B

Explanation: B) Inflation is a major concern for consumers, businesses, and government leaders because of its effect on purchasing power, or the amount of a good or service you can buy for a given amount of money. When prices go up, purchasing power goes down. If wages keep pace with prices, inflation is less worrisome, but if prices rise faster than wages, consumers definitely feel the pinch.

Page Ref: 37

Difficulty: Moderate

AACSB: Dynamics of the Global Economy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

70) Which of the following is an example of deregulation?

- A) lifting redundant restrictions on airline competition
- B) banning the sale of tobacco to minors under the age of 18
- C) lowering the speed limit on an interstate highway
- D) approving a proposed merger between Google and Microsoft
- E) establishing economic development zones to attract new businesses

Answer: A

Explanation: A) Deregulation is the process of removing regulations to allow the market to prevent excesses and correct itself over time.

Page Ref: 38

Difficulty: Easy

AACSB: Analytic Skills

Chapter LO: 5

Course LO: Explain how economic performance is monitored

Classification: Application

71) The Federal Trade Commission (FTC) is charged with which of the following duties?

- A) overseeing communication by telephone, telegraph, radio, and television
- B) regulating and overseeing carriers engaged in interstate transportation
- C) enforcing laws and regulations to prevent distribution of harmful foods and drugs
- D) protecting the national transportation infrastructure
- E) enforcing laws regarding unfair business practices and deceptive advertising

Answer: E

Explanation: E) The Federal Trade Commission (FTC) enforces laws and guidelines regarding unfair business practices and acts to stop false and deceptive advertising and labeling.

Page Ref: 39

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 5

Course LO: Explain how economic performance is monitored

Classification: Concept

72) _____ laws limit what businesses can and cannot do to ensure that all competitors have an equal chance of succeeding.

- A) Fiscal
- B) Discrimination
- C) Antitrust
- D) Stabilization
- E) Equilibrium

Answer: C

Explanation: C) Antitrust laws limit what businesses can and cannot do to ensure that all competitors have an equal chance of succeeding.

Page Ref: 39

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 5

Course LO: Explain how economic performance is monitored

Classification: Concept

73) _____ policy involves adjusting the nation's money supply by increasing or decreasing interest rates.

- A) Fiscal
- B) Taxation
- C) Cyclical
- D) Antitrust
- E) Monetary

Answer: E

Explanation: E) Monetary policy involves adjusting the nation's money supply, the amount of "spendable" money in the economy at any given time, by increasing or decreasing interest rates.

Page Ref: 40

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 5

Course LO: Explain how economic performance is monitored

Classification: Concept

74) _____ policy involves changes in the government's revenues and expenditures to stimulate a slow economy or dampen a growing economy that is in danger of overheating and causing inflation.

- A) Fiscal
- B) Taxation
- C) Cyclical
- D) Antitrust
- E) Monetary

Answer: A

Explanation: A) Fiscal policy involves changes in the government's revenues and expenditures to stimulate a slow economy or dampen a growing economy that is in danger of overheating and causing inflation.

Page Ref: 40

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 5

Course LO: Explain how economic performance is monitored

Classification: Concept

75) _____ taxes, levied on the earnings of individuals and businesses, are the government's largest single source of revenue.

- A) Income
- B) Property
- C) Sales
- D) Excise
- E) Payroll

Answer: A

Explanation: A) Income taxes are levied on the income earned by individuals and businesses. They are the government's largest single source of revenue.

Page Ref: 40

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 5

Course LO: Explain how economic performance is monitored

Classification: Concept

76) _____ taxes, levied on retail purchases made by customers, are collected by retail businesses at the time of the sale and then forwarded to state governments.

- A) Income
- B) Property
- C) Sales
- D) Excise
- E) Payroll

Answer: C

Explanation: C) Sales taxes are levied on retail purchases made by customers. Sales taxes are collected by retail businesses at the time of the sale and then forwarded to state governments.

Page Ref: 40

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 5

Course LO: Explain how economic performance is monitored

Classification: Concept

77) _____ taxes are implemented, in part, to help control potentially harmful practices, on selected items such as gasoline, tobacco, and liquor.

- A) Income
- B) Property
- C) Sales
- D) Excise
- E) Payroll

Answer: D

Explanation: D) Often referred to as "sin" taxes, excise taxes are implemented, in part, to help control potentially harmful practices, on selected items such as gasoline, tobacco, and liquor.

Page Ref: 40

Difficulty: Moderate

AACSB: Dynamics of the Global Economy

Chapter LO: 5

Course LO: Explain how economic performance is monitored

Classification: Concept

78) _____ taxes are levied on earnings of individuals to help fund Social Security, Medicare, and unemployment compensation.

- A) Excise
- B) Payroll
- C) Sales
- D) Income
- E) Property

Answer: B

Explanation: B) Payroll taxes are levied on earnings of individuals to help fund Social Security, Medicare, and unemployment compensation. Also, corporations must match employee contributions.

Page Ref: 40

Difficulty: Moderate

AACSB: Dynamics of the Global Economy

Chapter LO: 5

Course LO: Explain how economic performance is monitored

Classification: Concept

79) Retail sales, on the day after Thanksgiving, are usually a good indicator of overall retail sales for the Christmas season. This is an example of a _____ indicator.

- A) leading
- B) conversionary
- C) lagging
- D) current
- E) latent

Answer: A

Explanation: A) Leading indicators suggest changes that may happen to the economy in the future and are, therefore, valuable for planning.

Page Ref: 41

Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 6

Course LO: Explain how economic performance is monitored

Classification: Application

80) In early December, it was reported that housing rates in October 2010 were at its 6-month low, which resulted in increased home purchases. This is an example of a _____.

- A) leading indicator
- B) conversionary indicator
- C) lagging indicator
- D) current indicator
- E) latent indicator

Answer: C

Explanation: C) Lagging indicators provide confirmation that something has occurred in the past.

Page Ref: 41

Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 6

Course LO: Explain how economic performance is monitored

Classification: Application

81) The _____ measures the rate of inflation by comparing changes in the prices of a representative basket of goods and services such as clothing, food, housing, and utilities.

- A) gross domestic product (GDP)
- B) producer price index (PPI)
- C) inflationary stability index (ISI)
- D) consumer price index (CPI)
- E) economic stimulus index (ESI)

Answer: D

Explanation: D) The consumer price index (CPI) measures the rate of inflation by comparing the change in prices of a representative "basket" of consumer goods and services, such as clothing, food, housing, and transportation.

Page Ref: 42

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 6

Course LO: Explain how economic performance is monitored

Classification: Concept

82) The _____ measures price at the producer or wholesaler level, reflecting what businesses are paying for the products they need.

- A) gross domestic product (GDP)
- B) producer price index (PPI)
- C) inflationary stability index (ISI)
- D) consumer price index (CPI)
- E) economic stimulus index (ESI)

Answer: B

Explanation: B) The producer price index (PPI) measures price at the producer or wholesaler level, reflecting what businesses are paying for the products they need. Like the CPI, the PPI is often referred to as a single index, but it is actually a family of more than 600 industry-specific indexes.

Page Ref: 42

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 6

Course LO: Explain how economic performance is monitored

Classification: Concept

83) The _____ measures a country's output - its production, distribution, and use of goods and services - by computing the sum of all goods and services produced for final use in a country during a specified period.

- A) gross domestic product (GDP)
- B) producer price index (PPI)
- C) gross national product (GNP)
- D) consumer price index (CPI)
- E) economic stability index (ESI)

Answer: A

Explanation: A) The broadest measure of an economy's health is the gross domestic product (GDP). The GDP measures a country's output - its production, distribution, and use of goods and services - by computing the sum of all goods and services produced for final use in a country during a specified period (usually a year).

Page Ref: 43

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 6

Course LO: Explain how economic performance is monitored

Classification: Concept

84) While gross domestic product (GDP) considers where the production occurs, _____ considers who is responsible for the production.

- A) human development index (HDI)
- B) producer price index (PPI)
- C) gross national product (GNP)
- D) consumer price index (CPI)
- E) economic stability index (ESI)

Answer: C

Explanation: C) GDP has largely replaced an earlier measure called the gross national product (GNP), which excludes the value of production from foreign-owned businesses within a nation's boundaries and includes receipts from the overseas operations of domestic companies. GNP considers who is responsible for the production; GDP considers where the production occurs.

Page Ref: 43

Difficulty: Easy

AACSB: Dynamics of the Global Economy

Chapter LO: 6

Course LO: Explain how economic performance is monitored

Classification: Concept

85) What is economics? Compare and contrast between microeconomics and macroeconomics.
Answer: Economics is the study of how a society uses its scarce resources to produce and distribute goods and services.

Economics is divided into a small-scale perspective and a large-scale perspective. The study of economic behavior among consumers, businesses, and industries that collectively determine the quantity of goods and services demanded and supplied at different prices is termed microeconomics. The study of a country's larger economic issues, such as how firms compete, the effect of government policies, and how an economy maintains and allocates its scarce resources, is termed macroeconomics. While microeconomics looks at the small picture and macroeconomics looks at the big picture, understanding the economy at either scale requires an understanding of how the small and large forces interact. For instance, a number of macro forces and policies determine whether homeowners can afford to install solar energy systems. In turn, the aggregate behavior of all those homeowners at the micro level affects the vitality and direction of the overall economy.

Page Ref: 26

Difficulty: Moderate

AACSB: Reflective Thinking Skills

Chapter LO: 1

Classification: Synthesis

86) Explain the different factors of production.

Answer: Natural resources are things that are useful in their natural state, such as land, forests, minerals, and water.

Human resources are people and their individual talents and capacities.

Capital includes money, computers, machines, tools, and buildings that a business needs in order to produce goods and services.

Entrepreneurship is the spirit of innovation, the initiative, and the willingness to take the risks involved in creating and operating businesses. Knowledge is the collective intelligence of an organization.

Page Ref: 26; 27

Difficulty: Moderate

AACSB: Analytic Skills

Chapter LO: 1

Course LO: Compare and contrast different economic systems

Classification: Concept

87) Compare and contrast between trade-offs and opportunity costs.

Answer: Due to universal scarcity of resources, consumers, companies, and governments are constantly forced to make trade-offs, meaning they have to give up something to get something else. You have to decide how to spend the 24 hours you have every day, and every choice involves a trade-off - the more time you spend on one activity means less time for every other activity you could possibly pursue. Businesses must make similar trade-offs, such as deciding how much money to spend on advertising a new product versus how much to spend on the materials used to make it, or deciding how many employees to have in sales versus customer support.

Opportunity cost refers to the value of the most appealing alternative from all those you didn't choose. In other words, opportunity cost is a way to measure the value of what you gave up when you pursued a different opportunity.

Page Ref: 27; 28

Difficulty: Difficult

AACSB: Reflective Thinking Skills

Chapter LO: 1

Course LO: Compare and contrast different economic systems

Classification: Synthesis

88) Compare and contrast between free-market systems and planned systems.

Answer: In a free-market system, individuals and companies are largely free to decide what products to produce, how to produce them, whom to sell them to, and at what price to sell them. In other words, they have the chance to succeed - or to fail - by their own efforts. Capitalism and private enterprise are the terms most often used to describe the free-market system, one in which private parties (individuals, partnerships, or corporations) own and operate the majority of businesses and where competition, supply, and demand determine which goods and services are produced.

In a planned system, governments largely control the allocation of resources and limit freedom of choice in order to accomplish government goals. Because social equality is a major goal of planned systems, private enterprise and the pursuit of private gain are generally regarded as wasteful and exploitive. The planned system that allows individuals the least degree of economic freedom is communism.

Page Ref: 28; 29

Difficulty: Moderate

AACSB: Reflective Thinking Skills

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Synthesis

89) Is there such a thing as a "free" economy? Elucidate your views.

Answer: In practice, no economy is truly "free."

Local, state, national, and even international governments, such as the European Community, intervene in the economy to accomplish goals that leaders deem socially or economically desirable. This practice of limited intervention is characteristic of a mixed economy or mixed capitalism, which is the economic system of the United States and most other countries. For example, government bodies intervene in the U.S. economy in a variety of ways, such as influencing particular allocations of resources through tax incentives, prohibiting or restricting the sale of certain goods and services, or setting price controls. Price controls can involve maximum allowable prices (such as limiting rent increases) and minimum allowable prices (such as supplementing the prices of agricultural goods to ensure producers a minimum level of income or establishing minimum wage levels).

Page Ref: 29

Difficulty: Difficult

AACSB: Reflective Thinking Skills

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Synthesis

90) What type of economic system lies between capitalism and communism? Explain why it is more effective than other economic systems.

Answer: Socialism is an economic system with a fairly high degree of government planning and some government ownership of capital resources. In a socialist economy, government ownership tends to be focused in industries considered vital to the common welfare, such as transportation, health care, and communications. Private ownership is permitted in other industries. Many European countries, including France and Germany, incorporate varying degrees of socialism. Norway is strongly socialist; while most of the world's economies sank into a deep recession after the collapse of the U.S. housing and credit markets in 2008, Norway's economy remained stable.

Page Ref: 29; 30

Difficulty: Difficult

AACSB: Reflective Thinking Skills

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Synthesis

91) Explain, with the help of an example, why socialism and capitalism are not mutually exclusive.

Answer: While free-market capitalism remains the foundation of the U.S. economy, some important elements of the U.S. economy are socialized and have been for many years. Public schools, the postal service, much of the transportation infrastructure, various local and regional utilities, and several major health care programs all fit the economic definition of socialism. Socialism and capitalism are competing philosophies, but they are not mutually exclusive, and each approach has strengths and weaknesses, which is why most modern economies combine aspects of both.

Page Ref: 30

Difficulty: Difficult

AACSB: Reflective Thinking Skills

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Synthesis

92) In recent years, why have the governments of various countries both nationalized and privatized some of their services?

Answer: In recent years, governments of various countries have done both, for different reasons and in different industries. In the United States, private companies now own or operate a number of highways, bridges, ports, prisons, and other infrastructure elements, providing services once provided by the government. The primary reason for this trend is the belief that private firms motivated by the profit incentive can do a more efficient job of running these facilities.

Nationalization is less common and more drastic, but it has happened in recent years, most notably during the recent global banking crisis. For example, the second-largest bank in Britain, the Royal Bank of Scotland, was effectively nationalized after the British government became the majority owner in an attempt to prevent the bank from collapsing.

Page Ref: 30

Difficulty: Difficult

AACSB: Dynamics of the Global Economy

Chapter LO: 2

Course LO: Compare and contrast different economic systems

Classification: Synthesis

93) List the major factors that affect the overall demand of a product.

Answer: The effects of some of the major factors that can cause overall demand to increase or decrease:

- customer income
- customer preferences toward the product (fears regarding airline safety, for example)
- the price of substitute products (products that can be purchased instead of air travel, including rail tickets, automobile travel, or web conferencing)
- the price of complementary products (such as hotel accommodations or restaurant dining for the airline industry)
- marketing expenditures (for advertising and other promotional efforts)
- customer expectations about future prices and their own financial well-being

Page Ref: 32

Difficulty: Moderate

AACSB: Dynamics of the Global Economy

Chapter LO: 3

Classification: Concept

94) "As the supply and demand curves are dynamic, so is the equilibrium point." Explain this statement with an example.

Answer: As variables affecting supply and demand change, so will the equilibrium price. For example, increased concerns about airline safety could encourage some travelers to choose alternatives such as automobile travel or web conferencing, thus reducing the demand for air travel at every price and moving the equilibrium point as well. Suppliers might respond to such a reduction in demand by either cutting the number of flights offered or lowering ticket prices in order to restore the equilibrium level.

Page Ref: 32; 33

Difficulty: Difficult

AACSB: Reflective Thinking Skills

Chapter LO: 3

Classification: Synthesis

95) How does capitalism promote monopolistic competition in the market?

Answer: Most of the competition in advanced free-market economies is monopolistic competition, in which a number of sellers offer products that can be distinguished from competing products in at least some small way. The risk/reward nature of capitalism promotes constant innovation in pursuit of competitive advantage, rewarding companies that do the best job of satisfying customers.

Page Ref: 35

Difficulty: Difficult

AACSB: Reflective Thinking Skills

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Synthesis

96) Differentiate between structural and cyclical unemployment.

Answer: Structural Unemployment

- It occurs due to a mismatch between workers' skills and current employer needs.
- Workers can't find jobs that match their qualifications, and employers can't find employees with the skills their job openings require.
- A never-ending concern as changes in the external environments of business make some skills obsolete and create demand for new skills.

Cyclical Unemployment

- It is caused by economic fluctuations.
- When demand for goods and services drops, businesses reduce production, thereby requiring fewer workers.
- An increasing number of people who want to work can't find jobs.
- During catastrophic depressions, it can run as high as 20 or 25 percent.

Page Ref: 37

Difficulty: Moderate

AACSB: Dynamics of the Global Economy

Chapter LO: 4

Course LO: Compare and contrast different economic systems

Classification: Concept

97) Compare and contrast between monetary and fiscal policies.

Answer: Monetary policy involves adjusting the nation's money supply, the amount of "spendable" money in the economy at any given time, by increasing or decreasing interest rates. In the United States, monetary policy is controlled primarily by the Federal Reserve Board (often called "the Fed"), a group of government officials who oversee the country's central banking system.

Fiscal policy involves changes in the government's revenues and expenditures to stimulate a slow economy or dampen a growing economy that is in danger of overheating and causing inflation. On the revenue side, governments can adjust the revenue they bring in by changing tax rates and various fees collected from individuals and businesses. When the federal government lowers the income tax rate, for instance, it does so with the hope that consumers and businesses will spend and invest the money they save by paying lower taxes.

Page Ref: 40

Difficulty: Moderate

AACSB: Dynamics of the Global Economy

Chapter LO: 5

Course LO: Explain how economic performance is monitored

Classification: Synthesis

98) Explain the meaning of a leading indicator with the help of an example.

Answer: Leading indicators suggest changes that may happen to the economy in the future and are therefore valuable for planning. Housing starts, for example, are a leading indicator that shows where several industries are headed. When housing starts drop, the construction industry contracts, and the effect soon ripples through other sectors of the economy, from the manufacture of plumbing fixtures, carpet, and appliances to a variety of services, including furniture retailing, real estate sales, and other areas dependent on housing-related transactions. Another key leading indicator is durable-goods orders, or orders for goods that typically last more than three years (which can mean everything from desk chairs to airplanes). A rise in durable-goods orders is a positive indicator that business spending is turning around. In addition to all these indicators, economists closely monitor several price indexes and the nation's economic output to get a sense of how well the economy is working.

Page Ref: 41; 42

Difficulty: Moderate

AACSB: Reflective Thinking Skills

Chapter LO: 6

Course LO: Explain how economic performance is monitored

Classification: Concept

99) Explain three commonly known price indexes.

Answer: Government statisticians compute a huge variety of price indexes, each designed to monitor a particular aspect of economic activity. The best known of these, the consumer price index (CPI), measures the rate of inflation by comparing the change in prices of a representative "basket" of consumer goods and services, such as clothing, food, housing, and transportation. In contrast to the CPI, the producer price index (PPI) measures price at the producer or wholesaler level, reflecting what businesses are paying for the products they need. In addition to monitoring economic activity, PPIs have a number of managerial uses, from helping companies place an accurate value on inventories to protecting buyers and sellers with price-escalation clauses in long-term purchasing contracts. The broadest measure of an economy's health is the gross domestic product (GDP). The GDP measures a country's output - its production, distribution, and use of goods and services - by computing the sum of all goods and services produced for final use in a country during a specified period (usually a year). The products may be produced by either domestic or foreign companies as long as the production takes place within a nation's boundaries.

Page Ref: 42; 43

Difficulty: Moderate

AACSB: Dynamics of the Global Economy

Chapter LO: 6

Course LO: Explain how economic performance is monitored

Classification: Concept