

**Chapter 2—Thinking Like an Economist**

---

**MULTIPLE CHOICE**

1. Which statement best describes the way economists study the economy?
- Economists study the past, but do not try to predict the future.
  - Economists use a probabilistic approach based on correlations between economic events.
  - Economists devise theories, collect data, and then analyze the data to test the theories.
  - Economists use controlled experiments much the same way a biologist or physicist does.

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 21-22  
BLM: Remember                      NOT: Macro TB\_2-1

2. Which are terms used by an economist?
- vector spaces and axioms
  - torts and venues
  - ego and cognitive dissonance
  - comparative advantage and elasticity

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 22-24  
BLM: Remember                      NOT: Macro TB\_2-2

3. What is meant by scientific method?
- the use of modern electronic testing equipment to understand the world
  - the dispassionate development and testing of theories about how the world works
  - the use of controlled experiments in understanding the way the world works
  - finding evidence to support preconceived theories about how the world works

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 22-24  
BLM: Remember                      NOT: Macro TB\_2-3

4. Who said, “The whole of science is nothing more than a refinement of everyday thinking”?
- Isaac Newton
  - Albert Einstein
  - Sigmund Freud
  - Stephen Hawking

ANS: B                      PTS: 1                      DIF: Easy                      REF: p. 22-24  
BLM: Remember                      NOT: Macro TB\_2-4

5. What observation did Albert Einstein once make about science?
- “The whole of science is nothing more than a refinement of everyday thinking.”
  - “The whole of science is nothing more than an interesting intellectual exercise.”
  - “In order to understand science, one must rely solely on abstraction.”
  - “In order to understand science, one must transcend everyday thinking.”

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 22-24  
BLM: Remember                      NOT: Macro TB\_2-5

6. Sir Isaac Newton developed the theory of gravity after observing an apple fall from a tree. What is this an example of?
- a controlled experiment used to develop scientific theory
  - being in the right place at the right time
  - an idea whose time had come

d. the interplay between observation and theory in science

ANS: D PTS: 1 DIF: Average REF: p. 22-24  
BLM: Remember NOT: Macro TB\_2-6

7. What is a common thread between economics and other sciences, such as physics?

- a. Experiments are most often conducted in a lab.
- b. Real-world observations often lead to theories.
- c. They deal with similar phenomena.
- d. They deal primarily with abstract concepts.

ANS: B PTS: 1 DIF: Average REF: p. 22-23  
BLM: Remember NOT: Macro TB\_2-7

8. Why is the use of theory and observation more difficult in economics than in sciences, such as physics?

- a. It is difficult to evaluate an economic experiment.
- b. It is difficult to devise an economic experiment.
- c. It is difficult to actually perform an experiment in an economic system.
- d. It is difficult to collect sufficient data.

ANS: C PTS: 1 DIF: Average REF: p. 22-24  
BLM: Remember NOT: Macro TB\_2-8

9. Because it is difficult for economists to use experiments to generate data, what must they generally do?

- a. do without data
- b. use whatever data the world gives them
- c. select a committee of economists to make up data for all economists to use
- d. use hypothetical, computer-generated data

ANS: B PTS: 1 DIF: Average REF: p. 22-24  
BLM: Remember NOT: Macro TB\_2-9

10. What happens when economists test theories?

- a. They must make do with whatever data the world gives them.
- b. They can manipulate conditions easier than other scientific fields.
- c. They can enlist the government's help to manipulate economic conditions.
- d. They can achieve statistically valid results with much smaller sample sizes.

ANS: A PTS: 1 DIF: Average REF: p. 22-24  
BLM: Remember NOT: Macro TB\_2-10

11. Which of the following is one difficulty economists face that some other scientists do not?

- a. Unlike other sciences, economic studies must include the largest economic player, the government.
- b. Economists unfortunately receive less government funding than other scientists.
- c. Corporations are reluctant to disclose necessary information for economic research.
- d. Experiments are often difficult to conduct in economics.

ANS: D PTS: 1 DIF: Average REF: p. 22-24  
BLM: Remember NOT: Macro TB\_2-11

12. Where do the most common data for testing economic theories come from?

- a. carefully controlled and conducted laboratory experiments
- b. traditional economies
- c. historical episodes of economic change

d. centrally planned economies

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 22-24  
BLM: Remember                      NOT: Macro TB\_2-12

13. For economists, what are often used as substitutes for laboratory experiments?
- a. natural experiments offered by history
  - b. computer-generated experiments
  - c. studies conducted by other disciplines, such as sociologists
  - d. well-constructed simulations

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 22-24  
BLM: Remember                      NOT: Macro TB\_2-13

14. Why do economists make assumptions?
- a. to diminish the chance of wrong answers
  - b. to make the world easier to understand
  - c. because all scientists make assumptions
  - d. to make certain that all necessary variables are included

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 22-24  
BLM: Remember                      NOT: Macro TB\_2-14

15. Which of the following does the art of scientific thinking include?
- a. knowledge of human behaviour
  - b. understanding every scientific field, including physics, biology, and economics
  - c. deciding which assumptions to make
  - d. being able to mathematically express natural forces

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 23  
BLM: Remember                      NOT: Macro TB\_2-15

16. If an economist develops a theory about international trade based on the assumption that there are only two countries and two goods, what is most likely?
- a. The theory can be useful only in situations involving two countries and two goods.
  - b. It is a total waste of time, since the actual world has many countries trading many goods.
  - c. The theory can be useful in helping economists understand the complex world of international trade involving many countries and many goods.
  - d. The theory can be useful in the classroom, but has no use in the real world.

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 23  
BLM: Higher Order                      NOT: Macro TB\_2-16

17. Why are historical episodes valuable to economists?
- a. They allow economists to see how far the discipline has evolved.
  - b. Hindsight is always 20/20.
  - c. It is easier to evaluate a past situation than to predict a future situation.
  - d. They allow economists to evaluate economic theories of the present.

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 23  
BLM: Remember                      NOT: Macro TB\_2-17

18. What is a good theory?
- a. a widely accepted theory
  - b. a theory that starts from realistic assumptions
  - c. a theory that helps us understand how the world works

d. a theory where no logical mistakes were made in developing it

ANS: C                      PTS: 1                      DIF: Challenging    REF: p. 22-24  
BLM: Higher Order                      NOT: Macro TB\_2-18

19. What is the goal of theories?

- a. to provide an interesting, but not useful, framework of analysis
- b. to provoke stimulating debates in scientific journals
- c. to demonstrate that the developer of the theory is capable of logical thinking
- d. to help scientists understand how the world works

ANS: D                      PTS: 1                      DIF: Easy                      REF: p. 23  
BLM: Remember                      NOT: Macro TB\_2-19

20. When economists attempt to simplify the real world and make it easier to understand, what do they do?

- a. They make assumptions.
- b. They make mistakes in judgment.
- c. They make predictions.
- d. They make evaluations.

ANS: A                      PTS: 1                      DIF: Easy                      REF: p. 23  
BLM: Remember                      NOT: Macro TB\_2-20

21. What can good assumptions do?

- a. cause economists to leave out important variables that make their theories worthless
- b. simplify the complex world and make it easier to understand
- c. further complicate an already difficult topic
- d. allow economists to see the “big picture” instead of only small segments

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 23  
BLM: Remember                      NOT: Macro TB\_2-21

22. How does a scientist make assumptions?

- a. A scientist chooses the assumptions that best prove a desired result.
- b. A scientist chooses the assumptions that best describe reality.
- c. A scientist chooses the assumptions that would be most widely accepted.
- d. A scientist chooses the assumptions that best capture the essential features of the problem.

ANS: D                      PTS: 1                      DIF: Easy                      REF: p. 22-24  
BLM: Remember                      NOT: Macro TB\_2-22

23. What makes a model compelling?

- a. its mathematical structure
- b. its simplicity
- c. its predictions
- d. its assumptions

ANS: C                      PTS: 1                      DIF: Easy                      REF: p. 22-24  
BLM: Remember                      NOT: Macro TB\_2-23

24. What happens when scientists make good assumptions?

- a. They greatly simplify the problem without substantially affecting the answer.
- b. They further complicate an already complicated subject.
- c. They can leave out necessary variables that may result in incorrect answers.
- d. They may not be able to reach an appropriate conclusion.

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 22-24  
BLM: Remember                      NOT: Macro TB\_2-24

25. Which of the following is an example of a product that experiences infrequent price changes?
- a. stocks on the Toronto Stock Exchange
  - b. gasoline
  - c. the newsstand price of magazines
  - d. gold in international markets

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 22-24  
BLM: Remember                      NOT: Macro TB\_2-25

26. When studying the effects of public policy changes, what have economists often observed?
- a. There is a difference between the long run and the short run.
  - b. Unemployment and inflation are directly related in the short run.
  - c. With stock prices, what goes up must come down.
  - d. If the policy is well designed, it will always be effective.

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 23-24  
BLM: Remember                      NOT: Macro TB\_2-26

27. When studying the effects of public policy changes, what do economists do?
- a. They often falsify results if the desired effect is not reached.
  - b. They may make different assumptions for the long run and the short run.
  - c. They attempt to consider only the direct effects and not the indirect effects.
  - d. They can immediately change policies if they are ineffective.

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 23-24  
BLM: Remember                      NOT: Macro TB\_2-27

28. What do good economic models do?
- a. They often leave out important variables, causing serious errors.
  - b. They omit many details to allow us to see what is truly important.
  - c. They are designed to give a complete picture of a given relationship.
  - d. They leave economics to be interpreted in many ways by governments.

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 24  
BLM: Remember                      NOT: Macro TB\_2-28

29. Why do economists use models?
- a. to learn how the economy works
  - b. to make their profession appear more precise
  - c. to make economics accessible to the public
  - d. to make sure that all of the details of the economy are included in their analysis

ANS: A                      PTS: 1                      DIF: Easy                      REF: p. 24  
BLM: Remember                      NOT: Macro TB\_2-29

30. Which of the following best describes economic models?
- a. They are based on unrealistic assumptions.
  - b. They accurately describe the reality.
  - c. They allow economists to learn how the economy works.
  - d. They include as many variables as possible.

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 24

BLM: Remember NOT: Macro TB\_2-30

31. How do economists begin building an economic model?
- by writing grants for government funding
  - by conducting controlled experiments in a lab
  - by making assumptions
  - by reviewing statistical forecasts

ANS: C PTS: 1 DIF: Average REF: p. 24

BLM: Remember NOT: Macro TB\_2-31

32. What is a model?
- a theoretical abstraction with very little value
  - a useful tool to only the ones who constructed it
  - a realistic and carefully constructed theory
  - a simplification of real life

ANS: D PTS: 1 DIF: Easy REF: p. 24

BLM: Remember NOT: Macro TB\_2-32

33. Which of the following is NOT a characteristic of economic models?
- Models simplify reality.
  - Models can explain how the economy is organized.
  - Models assume away irrelevant details.
  - Models cannot be used to make predictions.

ANS: D PTS: 1 DIF: Average REF: p. 24

BLM: Higher Order NOT: Macro TB\_2-33

34. Which of the following is NOT a common characteristic of economic models?
- They are often built using the tools of mathematics.
  - They are useful to economists, but not to policymakers.
  - They include only the important features of an economy.
  - They are built using assumptions.

ANS: B PTS: 1 DIF: Average REF: p. 24

BLM: Higher Order NOT: Macro TB\_2-34

35. Which of the following best describes economic models?
- Economic models attempt to mirror reality exactly.
  - Economic models are useful, but should not be used for policymaking.
  - Economic models omit many details to allow us to see what is truly important.
  - Economic models cannot be used in the real world because they omit details.

ANS: C PTS: 1 DIF: Average REF: p. 24

BLM: Higher Order NOT: Macro TB\_2-35

36. What are the foundation stones from which economic models are built?
- economic policies
  - legal systems
  - assumptions
  - statistical forecasts

ANS: C PTS: 1 DIF: Easy REF: p. 24

BLM: Remember NOT: Macro TB\_2-36

37. What is a circular-flow diagram?
- a. a visual model of how the economy is organized
  - b. a mathematical model of how the economy works
  - c. a model that shows the effects of government on the economy
  - d. a visual model of the relationship between money, prices, and businesses

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 24  
BLM: Remember                      NOT: Macro TB\_2-37

38. What does a circular-flow diagram do?
- a. It illustrates cost-benefit analysis.
  - b. It explains how the economy is organized.
  - c. It shows the flow of traffic in an economic region.
  - d. It explains how banks circulate money in the economy.

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 25  
BLM: Remember                      NOT: Macro TB\_2-38

39. What are factors of production?
- a. the mathematical calculations firms make to determine production
  - b. weather and social and political conditions that affect production
  - c. the physical relationships between economic inputs and outputs
  - d. inputs into the production process

ANS: D                      PTS: 1                      DIF: Easy                      REF: p. 25  
BLM: Remember                      NOT: Macro TB\_2-39

40. In the simple circular-flow diagram, who are the decision makers?
- a. firms and government
  - b. households and firms
  - c. households and government
  - d. households, firms, and government

ANS: B                      PTS: 1                      DIF: Easy                      REF: p. 25  
BLM: Remember                      NOT: Macro TB\_2-40

41. What do the two loops in the circular-flow diagram represent?
- a. the flow of goods and the flow of services
  - b. the flow of dollars and the flow of financial assets
  - c. the flow of inputs and outputs and the flow of dollars
  - d. the flow of capital goods and the flow of consumer goods

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 25  
BLM: Remember                      NOT: Macro TB\_2-41

42. In a circular-flow diagram, which flows are involved?
- a. Taxes flow from households to firms, and transfer payments flow from firms to households.
  - b. Income payments flow from firms to households, and sales revenue flows from households to firms.
  - c. Resources flow from firms to households, and goods and services flow from households to firms.
  - d. Inputs and outputs flow in the same direction as the flow of dollars, from firms to households.

ANS: B                      PTS: 1                      DIF: Challenging                      REF: p. 25

BLM: Remember NOT: Macro TB\_2-42

43. Which of the following is a characteristic of the circular-flow model?
- a. Firms are sellers in the resource market and the product market.
  - b. Firms are buyers in the product market.
  - c. Households are sellers in the resource market.
  - d. Households are buyers in the resource market.

ANS: C PTS: 1 DIF: Challenging REF: p. 25

BLM: Remember NOT: Macro TB\_2-43

44. In the circular-flow diagram, which flows are involved?
- a. Income from factors of production flows from firms to households.
  - b. Goods and services flow from households to firms.
  - c. Factors of production flow from firms to households.
  - d. Spending on goods and services flow from firms to households.

ANS: A PTS: 1 DIF: Challenging REF: p. 25

BLM: Remember NOT: Macro TB\_2-44

45. Which of the following would NOT be considered a factor of production?
- a. labour
  - b. land
  - c. capital
  - d. money

ANS: D PTS: 1 DIF: Easy REF: p. 25

BLM: Remember NOT: Macro TB\_2-45

46. What is another name for goods and services produced by firms?
- a. factors of production
  - b. outputs
  - c. inputs
  - d. resources

ANS: B PTS: 1 DIF: Easy REF: p. 25

BLM: Remember NOT: Macro TB\_2-46

47. Which of the following is a characteristic of factors of production?
- a. They are used to produce goods and services.
  - b. They are owned by firms.
  - c. They are abundant in most economies.
  - d. They are used by both firms and households.

ANS: A PTS: 1 DIF: Easy REF: p. 25

BLM: Remember NOT: Macro TB\_2-47

48. What is another term for factors of production?
- a. inputs
  - b. outputs
  - c. goods
  - d. services

ANS: A PTS: 1 DIF: Easy REF: p. 25

BLM: Remember NOT: Macro TB\_2-48



49. According to a simple circular-flow diagram, how many markets do households and firms interact in?
- one type of market
  - two types of markets
  - three types of markets
  - four types of markets

ANS: B                      PTS: 1                      DIF: Easy                      REF: p. 25  
BLM: Remember                      NOT: Macro TB\_2-49

50. In the simple circular-flow diagram, what do markets consist of?
- the market for goods and services, the financial market, and the market for the factors of production
  - the market for the factors of production and the financial market
  - the market for goods and services and the financial market
  - the market for goods and services and the market for factors of production

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 25  
BLM: Remember                      NOT: Macro TB\_2-50

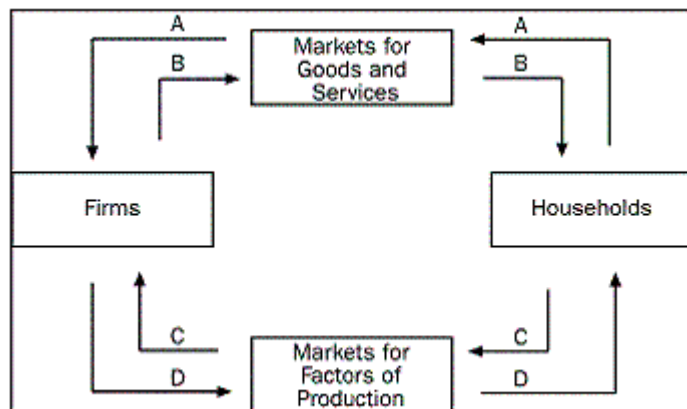
51. In the goods and services market, how do households and firms interact?
- Households and firms are both buyers.
  - Households are sellers and firms are buyers.
  - Households are buyers and firms are sellers.
  - Households and firms are both sellers.

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 25  
BLM: Remember                      NOT: Macro TB\_2-51

52. In the factors of production market, how do households and firms interact?
- Households are sellers and firms are buyers.
  - Households are buyers and firms are sellers.
  - Households and firms are both buyers.
  - Households and firms are both sellers.

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 25  
BLM: Remember                      NOT: Macro TB\_2-52

**Figure 2-1**



53. Refer to Figure 2-1. Which arrow shows the flow of goods and services?
- arrow A

- b. arrow B
- c. arrow C
- d. arrow D

ANS: B  
BLM: Higher Order

PTS: 1

DIF: Average REF: p. 25  
NOT: Macro TB\_2-53

54. Refer to Figure 2-1. Which arrow shows the flow of spending by households?
- a. arrow A
  - b. arrow B
  - c. arrow C
  - d. arrow D

ANS: A  
BLM: Higher Order

PTS: 1

DIF: Average REF: p. 25  
NOT: Macro TB\_2-54

55. Refer to Figure 2-1. Which arrow shows the flow of the factors of production?
- a. arrow A
  - b. arrow B
  - c. arrow C
  - d. arrow D

ANS: C  
BLM: Higher Order

PTS: 1

DIF: Average REF: p. 25  
NOT: Macro TB\_2-55

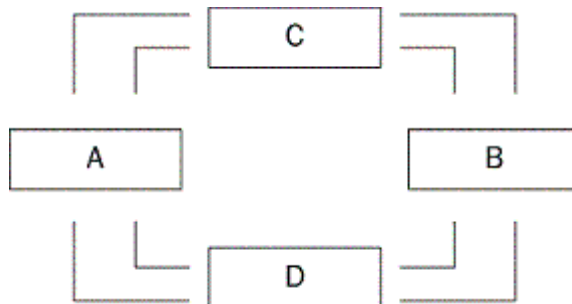
56. Refer to Figure 2-1. Which arrow shows the flow of income payments?
- a. arrow A
  - b. arrow B
  - c. arrow C
  - d. arrow D

ANS: D  
BLM: Higher Order

PTS: 1

DIF: Average REF: p. 25  
NOT: Macro TB\_2-56

**Figure 2-2**



57. Refer to Figure 2-2. What do boxes A and B represent?
- a. firms and households
  - b. government and the foreign sector
  - c. the goods and services market and the factors of production market
  - d. households and government

ANS: A  
BLM: Higher Order

PTS: 1

DIF: Challenging REF: p. 25  
NOT: Macro TB\_2-57

58. Refer to Figure 2-2. What do boxes C and D represent?

- a. households and firms
- b. the goods and services market and the factors of production market
- c. the goods and services market and the financial market
- d. households and government

ANS: B                      PTS: 1                      DIF: Challenging    REF: p. 25  
BLM: Higher Order                      NOT: Macro TB\_2-58

59. Refer to Figure 2-2. In which market are households sellers?

- a. the factors of production market
- b. the goods and services market
- c. both the factors of production market and the goods and services market
- d. neither the factors of production market nor the goods and services market

ANS: A                      PTS: 1                      DIF: Easy                      REF: p. 25  
BLM: Remember                      NOT: Macro TB\_2-59

60. Refer to Figure 2-2. In which market are firms sellers?

- a. the goods and services market
- b. the factors of production market
- c. both the factors of production market and the goods and services market
- d. neither the factors of production market nor the goods and services market

ANS: A                      PTS: 1                      DIF: Easy                      REF: p. 25  
BLM: Remember                      NOT: Macro TB\_2-60

61. Refer to Figure 2-2. Who owns the factors of production?

- a. the government
- b. firms
- c. households
- d. corporations

ANS: C                      PTS: 1                      DIF: Easy                      REF: p. 25  
BLM: Remember                      NOT: Macro TB\_2-61

62. Refer to Figure 2-2. What does the inner loop represent?

- a. the flow of inputs to firms and output to households
- b. the flow of output to firms and inputs to households
- c. the flow of spending to firms and factor payments to households
- d. the flow of spending to households and factor payments to firms

ANS: A                      PTS: 1                      DIF: Challenging    REF: p. 25  
BLM: Remember                      NOT: Macro TB\_2-62

63. Refer to Figure 2-2. What does the outer loop represent?

- a. the flow of goods
- b. the flow of spending
- c. the flow of factors of production
- d. the flow of services

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 25  
BLM: Remember                      NOT: Macro TB\_2-63

64. Refer to Figure 2-2. Which of the following best characterizes the money held by households in the circular-flow diagram?

- a. It is earned from the sale of factors of production.
- b. It becomes profit to firms.
- c. It cannot be tracked in the circular-flow diagram.
- d. It is used to purchase factors of production.

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 25  
BLM: Remember                      NOT: Macro TB\_2-64

65. What happens in the markets for factors of production?
- a. Households provide firms with labour, land, and capital.
  - b. Households provide firms with savings for investment.
  - c. Firms provide households with goods and services.
  - d. The government provides firms with inputs for the production process.

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 25  
BLM: Remember                      NOT: Macro TB\_2-65

66. What happens in the markets for goods and services?
- a. Households provide firms with savings for investment.
  - b. Households provide firms with labour, land, and capital.
  - c. Firms provide households with the output they produced.
  - d. The government provides firms with inputs for the production process.

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 25  
BLM: Remember                      NOT: Macro TB\_2-66

67. What are the four sectors in a more complex circular-flow diagram?
- a. households, government, financial markets, and international trade
  - b. households, firms, government, and financial markets
  - c. households, firms, financial markets, and international trade
  - d. households, firms, government, and international trade

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 26  
BLM: Remember                      NOT: Macro TB\_2-67

68. In economics, what does capital refer to?
- a. the finances necessary for firms to produce their products
  - b. buildings and machines used in the production process
  - c. the money households use to purchase firms' output
  - d. the value of stock market shares to investors

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 24-26  
BLM: Remember                      NOT: Macro TB\_2-68

69. What revenue is received by firms from sales that is NOT used to pay for factors of production?
- a. rent
  - b. wages
  - c. profit
  - d. interest

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 24-25  
BLM: Remember                      NOT: Macro TB\_2-69

70. What does a point on a country's production possibilities frontier represent?
- a. a combination of two goods that an economy will never be able to produce
  - b. a combination of two goods that an economy can produce using all available resources and

technology

- c. a combination of two goods that an economy can produce using some of its resources and technology
- d. a combination of two goods that an economy may be able to produce sometime in the future with additional resources and technology

ANS: B                      PTS: 1                      DIF: Challenging      REF: p. 26  
BLM: Remember      NOT: Macro TB\_2-70

71. Why are production possibilities frontiers usually bowed outward?
- a. The more resources a society uses to produce one good, the fewer resources it has available to produce another good.
  - b. It reflects the fact that the opportunity cost of producing a good falls as one produces more and more of it.
  - c. It is because of the effects of technological change.
  - d. Resources are specialized; that is, some are better at producing particular goods rather than other goods.

ANS: D                      PTS: 1                      DIF: Average              REF: p. 26-28  
BLM: Remember      NOT: Macro TB\_2-71

72. Why are production possibilities frontiers usually bowed outward?
- a. constant opportunity cost
  - b. increasing opportunity cost
  - c. decreasing opportunity cost
  - d. increasing productivity

ANS: B                      PTS: 1                      DIF: Average              REF: p. 26-28  
BLM: Remember      NOT: Macro TB\_2-72

73. Suppose an economy produces two goods: food and machines. This economy always operates on its production possibilities frontier. Last year, it produced 50 units of food and 30 machines. This year, it is producing 55 units of food and 33 machines. Which of the following would NOT explain the increase in output?
- a. a reduction in unemployment
  - b. an increase in the labour force
  - c. an improvement in technology
  - d. an increase in worker productivity

ANS: A                      PTS: 1                      DIF: Average              REF: p. 26-28  
BLM: Higher Order                      NOT: Macro TB\_2-73

74. Suppose an economy produces two goods: food and machines. This economy always operates on its production possibilities frontier. Last year, it produced 72 units of food and 28 machines. This year, it is producing 75 units of food and 30 machines. Which of the following would NOT explain the increase in output?
- a. a reduction in unemployment
  - b. an increase in the labour force
  - c. an improvement in technology
  - d. an increase in worker productivity

ANS: A                      PTS: 1                      DIF: Average              REF: p. 26-28  
BLM: Higher Order                      NOT: Macro TB\_2-74

75. Suppose an economy produces two goods: food and machines. This economy always operates on its production possibilities frontier. Last year, it produced 91 units of food and 48 machines. This year, it is producing 92 units of food and 53 machines. Which of the following would NOT explain the increase in output?
- a. a reduction in unemployment
  - b. an increase in the labour force
  - c. an improvement in technology
  - d. an increase in worker productivity

ANS: A

PTS: 1

DIF: Average

REF: p. 26-28

BLM: Higher Order

NOT: Macro TB\_2-75

76. The country of Econoland produces two goods: textbooks and widgets. Last year, it produced 200 textbooks and 500 widgets. This year, it produced 250 textbooks and 600 widgets. Given no other information, which of the following could NOT explain the change?
- a. Econoland experienced a reduction in unemployment.
  - b. Econoland experienced an improvement in widget-making technology.
  - c. Econoland acquired more resources.
  - d. Econoland experienced a high level of emigration out of the country.

ANS: D

PTS: 1

DIF: Average

REF: p. 26-28

BLM: Higher Order

NOT: Macro TB\_2-76

77. The country of Econoland produces two goods: textbooks and widgets. Last year, it produced 300 textbooks and 600 widgets. This year, it produced 350 textbooks and 700 widgets. Given no other information, which of the following could NOT explain the change?
- a. Econoland experienced a reduction in unemployment.
  - b. Econoland experienced an improvement in widget-making technology.
  - c. Econoland acquired more resources.
  - d. Econoland experienced a high level of emigration out of the country.

ANS: D

PTS: 1

DIF: Average

REF: p. 26-28

BLM: Higher Order

NOT: Macro TB\_2-77

78. Suppose there are two countries, Freedonia and Sylvania, which have identical amounts of resources, identical technologies, and identical populations. Both produce two types of goods, consumer goods and capital goods, and they both always operate on their production possibilities frontiers. The only difference is that this year Freedonia chooses to produce relatively more consumer goods than Sylvania. What will happen as a result?
- a. Freedonia will have a higher living standard this year but will grow slower than Sylvania.
  - b. Freedonia will have a higher living standard this year and will grow faster than Sylvania.
  - c. Sylvania will have a higher living standard this year but will grow slower than Freedonia.
  - d. Sylvania will have a higher living standard this year and will grow faster than Freedonia.

ANS: A

PTS: 1

DIF: Challenging

REF: p. 26-28

BLM: Higher Order

NOT: Macro TB\_2-78

79. Suppose there are two countries, Freedonia and Sylvania, which have identical amounts of resources, identical technologies, and identical populations. Both produce two types of goods, consumer goods and capital goods, and they both always operate on their production possibilities frontiers. The only difference is that this year Sylvania chooses to produce relatively more consumer goods than Freedonia. What will happen as a result?
- a. Freedonia will have a higher living standard this year but will grow slower than Sylvania.
  - b. Freedonia will have a higher living standard this year and will grow faster than Sylvania.
  - c. Sylvania will have a higher living standard this year but will grow slower than Freedonia.

d. Sylvania will have a higher living standard this year and will grow faster than Freedonia.

ANS: C                      PTS: 1                      DIF: Challenging    REF: p. 26-28  
BLM: Higher Order                      NOT: Macro TB\_2-79

80. What is the production possibilities frontier?
- a. a map that shows the frontier beyond which agriculture is unprofitable
  - b. a map that shows areas of the world in which capitalist production is now possible
  - c. a graph that shows the various combinations of resources that can be used to produce a given level of output
  - d. a graph that shows the various combinations of output the economy can possibly produce given the available resources and technology

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 26-28  
BLM: Remember                      NOT: Macro TB\_2-80

81. In what region of the production possibilities frontier can an economy produce?
- a. An economy can produce only on the production possibilities frontier.
  - b. An economy can produce at any point inside or outside the production possibilities frontier.
  - c. An economy can produce at any point on or inside the production possibilities frontier, but not outside the frontier.
  - d. An economy can produce at any point inside the production possibilities frontier, but not on or outside the frontier.

ANS: C                      PTS: 1                      DIF: Challenging    REF: p. 26-28  
BLM: Remember                      NOT: Macro TB\_2-81

82. When is an economic outcome said to be efficient?
- a. if the economy is using all of the resources it has available
  - b. if the economy is conserving on resources and not using all it has
  - c. if the economy is getting all it can from the scarce resources it has available
  - d. if the economy is able to produce more than its current production without additional resources

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 26-28  
BLM: Remember                      NOT: Macro TB\_2-82

83. When constructing a production possibilities frontier, which of the following is NOT an assumption?
- a. The economy produces only two goods.
  - b. All the economy's factors of production are being used.
  - c. The economy has a fixed level of technology.
  - d. The economy may increase its available factors of production.

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 26-28  
BLM: Remember                      NOT: Macro TB\_2-83

84. On a production possibilities frontier, when is production efficient?
- a. if the production point is on the frontier
  - b. if the production point is outside the frontier
  - c. if the production point is on or inside the frontier
  - d. if the production point is inside the frontier

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 26-28  
BLM: Remember                      NOT: Macro TB\_2-84

85. What does it mean if an economy is producing efficiently?
- a. There is no way to produce more of one good without producing less of the other.
  - b. It is possible to produce more of both goods.
  - c. It is possible to produce more of one good without producing less of the other.
  - d. It is not possible to produce more of one good at any cost.

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 26-28  
BLM: Remember                      NOT: Macro TB\_2-85

86. Which of the following concepts is NOT illustrated by the production possibilities frontier?
- a. efficiency
  - b. opportunity cost
  - c. equity
  - d. tradeoffs

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 27  
BLM: Higher Order                      NOT: Macro TB\_2-86

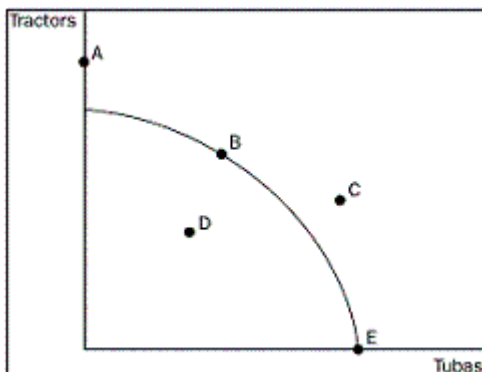
87. When a production possibilities frontier is linear, what does it show?
- a. a truer picture of real life than a bowed-out production possibilities frontier
  - b. that resources are perfectly shiftable from the production of one good to another
  - c. an example of increasing opportunity cost
  - d. an example of decreasing opportunity cost

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 27  
BLM: Remember                      NOT: Macro TB\_2-87

88. Suppose a nation is currently producing at a point inside its production possibilities frontier. What do we know?
- a. The nation is producing beyond its capacity, and inflation will occur.
  - b. The nation is not using all available resources and is inefficient.
  - c. The nation is producing an efficient combination of goods.
  - d. There will be a large opportunity cost if the nation tries to increase production.

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 27  
BLM: Remember                      NOT: Macro TB\_2-88

**Figure 2-3**



89. Refer to Figure 2-3. At which point or points can the economy produce?
- a. points B, D, and E
  - b. points A, B, D, and E
  - c. points D and C



d. point D

ANS: A                      PTS: 1  
BLM: Higher Order

DIF: Average              REF: p. 27  
NOT: Macro TB\_2-89

90. Refer to Figure 2-3. Which point represents the maximum possible production of tubas?

- a. point A
- b. point B
- c. point C
- d. point E

ANS: D                      PTS: 1  
BLM: Higher Order

DIF: Average              REF: p. 27  
NOT: Macro TB\_2-90

91. Refer to Figure 2-3. At which point or points can the economy NOT produce?

- a. point A
- b. point C
- c. points A and C
- d. points A, C, and D

ANS: C                      PTS: 1  
BLM: Higher Order

DIF: Challenging          REF: p. 27  
NOT: Macro TB\_2-91

92. Refer to Figure 2-3. Which point or points are efficient?

- a. points B and E
- b. points A, B, and E
- c. point D
- d. point C

ANS: A                      PTS: 1  
BLM: Higher Order

DIF: Challenging          REF: p. 27  
NOT: Macro TB\_2-92

93. Refer to Figure 2-3. Which point or points are inefficient?

- a. points A and C
- b. points D and C
- c. point C
- d. point D

ANS: D                      PTS: 1  
BLM: Higher Order

DIF: Average              REF: p. 27  
NOT: Macro TB\_2-93

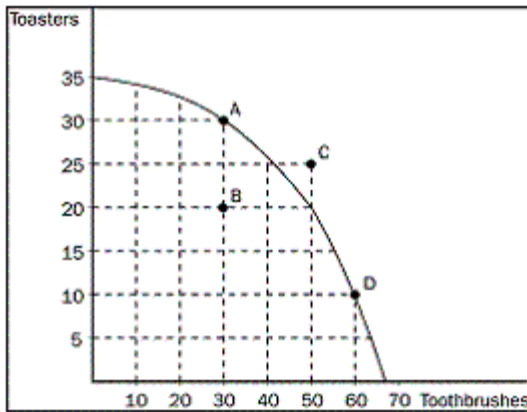
94. What is the opportunity cost of obtaining more of one good, as shown on the production possibilities frontier?

- a. the amount of the other good that must be given up
- b. the market price of the additional amount produced
- c. the amount of resources that must be devoted to its production
- d. the number of dollars that must be spent to produce it

ANS: A                      PTS: 1  
BLM: Higher Order

DIF: Average              REF: p. 27  
NOT: Macro TB\_2-94

#### **Figure 2-4**



95. Refer to Figure 2-4. What is the opportunity cost to the economy of getting 30 additional toothbrushes by moving from point A to point D?
- 10 toasters
  - 15 toasters
  - 20 toasters
  - 25 toasters

ANS: C PTS: 1

DIF: Average REF: p. 27

BLM: Higher Order

NOT: Macro TB\_2-95

96. Refer to Figure 2-4. Suppose the economy is at point A. What is the opportunity cost of increasing the production of toothbrushes by 20 units?
- 10 toasters
  - 20 toasters
  - 30 toasters
  - 40 toasters

ANS: A PTS: 1

DIF: Challenging REF: p. 27

BLM: Higher Order

NOT: Macro TB\_2-96

97. Refer to Figure 2-4. What is the opportunity cost in terms of toothbrushes of getting 10 additional toasters by moving from point B to point A?
- 20 toothbrushes
  - 10 toothbrushes
  - 5 toothbrushes
  - 0 toothbrushes

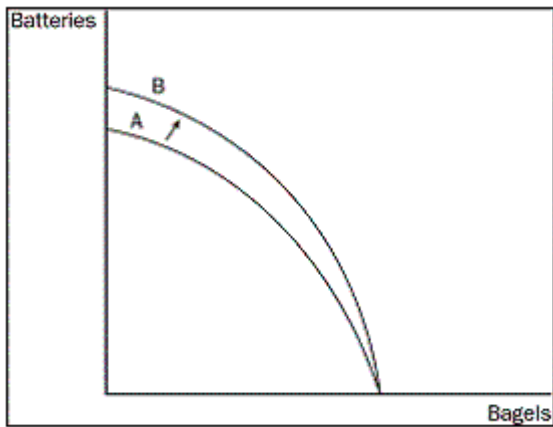
ANS: D PTS: 1

DIF: Challenging REF: p. 27

BLM: Higher Order

NOT: Macro TB\_2-97

**Figure 2-5**



98. Refer to Figure 2-5. Which of the following most likely caused the shift of the production possibilities frontier from A to B?
- technological improvement in the production of batteries
  - more labour available in the economy
  - a general technological breakthrough
  - more capital available in the economy

ANS: A

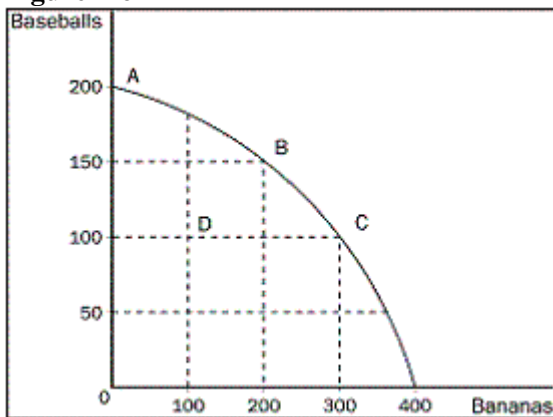
PTS: 1

DIF: Average REF: p. 27

BLM: Higher Order

NOT: Macro TB\_2-98

**Figure 2-6**



99. Refer to Figure 2-6. What is the opportunity cost to society of the movement from point A to point C?
- 50 baseballs
  - 100 baseballs
  - 100 bananas
  - 300 bananas

ANS: B

PTS: 1

DIF: Average REF: p. 27

BLM: Higher Order

NOT: Macro TB\_2-99

100. Refer to Figure 2-6. What is the opportunity cost to society of moving from point B to point D?
- 100 bananas and 100 baseballs
  - 50 bananas and 50 baseballs
  - 100 bananas and 50 baseballs
  - 50 bananas and 100 baseballs

ANS: C

PTS: 1

DIF: Average REF: p. 27

101. Refer to Figure 2-6. What was the most likely cause of the movement from point C to point D?
- unemployment
  - a decrease in society's preference for bananas
  - a decrease in society's preference for playing baseball
  - a shift to a longer working day

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 27

BLM: Higher Order                      NOT: Macro TB\_2-101

102. Refer to Figure 2-6. If this economy put all available resources into the production of bananas, how many could it produce?
- 200
  - 300
  - 400
  - 600

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 27

BLM: Higher Order                      NOT: Macro TB\_2-102

103. How can the production possibilities frontiers shift outward?
- if government increases the amount of money in the economy
  - if there is an increase in technology
  - if resources can be moved from the production of one good to another
  - if opportunity costs are reduced

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 28-29

BLM: Remember                      NOT: Macro TB\_2-103

104. When is the production possibilities frontier bowed outward?
- if resources are not perfectly shiftable
  - if the amount of resources increases
  - if the level of technology increases
  - if opportunity costs are constant

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 28-29

BLM: Remember                      NOT: Macro TB\_2-104

105. When a production possibilities frontier shifts outward, what concept is being demonstrated?
- tradeoffs
  - efficiency
  - economic growth
  - opportunity cost

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 28-29

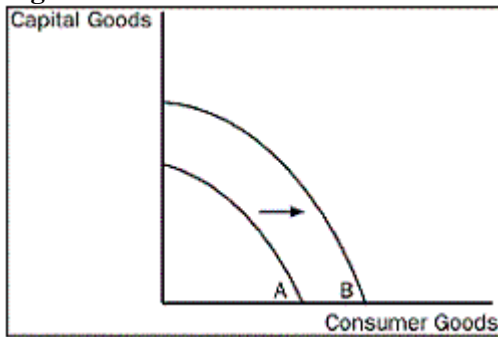
BLM: Remember                      NOT: Macro TB\_2-105

106. When an economy is operating inside its production possibilities frontier, what do we know?
- There are unused resources or inefficiencies in the economy.
  - The economy is operating with efficiency.
  - Moving to a point on its production possibilities frontier would be economic growth.
  - To produce more of one good, the economy would have to give up some of the other good.

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 27

BLM: Remember                      NOT: Macro TB\_2-106

**Figure 2-7**



107. Refer to Figure 2-7. Which of the following would most likely have caused the production possibilities frontier to shift outward from A to B?
- a. an increase in resources necessary to produce capital goods
  - b. an improvement in the technology of producing consumer goods
  - c. an increase in the overall level of technology in the economy
  - d. an increase in unemployment

ANS: C

PTS: 1

DIF: Average

REF: p. 28-29

BLM: Higher Order

NOT: Macro TB\_2-107

108. Refer to Figure 2-7. What would best describe the movement from frontier A to B?
- a. a downturn in the economy
  - b. economic growth
  - c. a more equitable distribution of income
  - d. an improvement in the allocation of resources

ANS: B

PTS: 1

DIF: Average

REF: p. 28-29

BLM: Higher Order

NOT: Macro TB\_2-108

109. What would unemployment cause an economy to do?
- a. produce inside its production possibilities frontier
  - b. produce on its production possibilities frontier
  - c. produce outside its production possibilities frontier
  - d. cause many different scenarios on its production possibilities frontier depending on its severity

ANS: A

PTS: 1

DIF: Average

REF: p. 27

BLM: Higher Order

NOT: Macro TB\_2-109

**Table 2-1**

Production Possibilities for Toyland

Dolls	Fire Trucks
400	0
300	200
200	350
100	450
0	500

110. Refer to Table 2-1. What is the opportunity cost to Toyland of increasing the production of dolls from 200 to 300?

- a. 200 fire trucks
- b. 150 fire trucks
- c. 100 fire trucks
- d. 50 fire trucks

ANS: B                      PTS: 1  
BLM: Higher Order

DIF: Average              REF: p. 27  
NOT: Macro TB\_2-110

111. Refer to Table 2-1. What is the opportunity cost to Toyland of increasing the production of dolls from 300 to 400?
- a. 200 fire trucks
  - b. 150 fire trucks
  - c. 100 fire trucks
  - d. 50 fire trucks

ANS: A                      PTS: 1  
BLM: Higher Order

DIF: Average              REF: p. 27  
NOT: Macro TB\_2-111

112. Refer to Table 2-1. What is the opportunity cost to Toyland of increasing the production of dolls from 100 to 200?
- a. 200 fire trucks
  - b. 150 fire trucks
  - c. 100 fire trucks
  - d. 50 fire trucks

ANS: C                      PTS: 1  
BLM: Higher Order

DIF: Average              REF: p. 27  
NOT: Macro TB\_2-112

113. Refer to Table 2-1. What is the opportunity cost to Toyland of increasing the production of dolls from 0 to 100?
- a. 200 fire trucks
  - b. 150 fire trucks
  - c. 100 fire trucks
  - d. 50 fire trucks

ANS: D                      PTS: 1  
BLM: Higher Order

DIF: Average              REF: p. 27  
NOT: Macro TB\_2-113

114. Refer to Table 2-1. What is the opportunity cost to Toyland of increasing the production of fire trucks from 0 to 200?
- a. 200 dolls
  - b. 150 dolls
  - c. 100 dolls
  - d. 50 dolls

ANS: C                      PTS: 1  
BLM: Higher Order

DIF: Average              REF: p. 27  
NOT: Macro TB\_2-114

115. Refer to Table 2-1. What is the opportunity cost to Toyland of increasing the production of fire trucks from 450 to 500?
- a. 200 dolls
  - b. 150 dolls
  - c. 100 dolls
  - d. 50 dolls

ANS: C                      PTS: 1

DIF: Average              REF: p. 27

116. Refer to Table 2-1. How does the opportunity cost of producing an additional 100 dolls change as more dolls are produced?
- It is constant and equal to 50 fire trucks.
  - It is constant and equal to 100 fire trucks.
  - It decreases as more dolls are produced.
  - It increases as more dolls are produced.

ANS: D

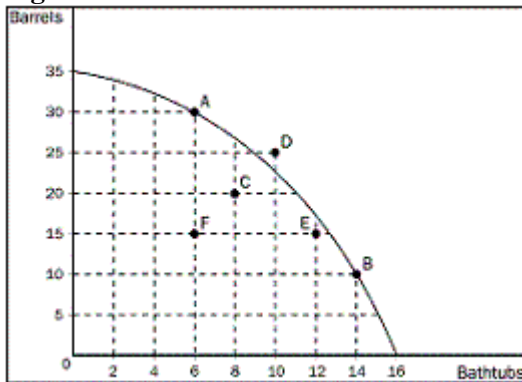
PTS: 1

DIF: Average

REF: p. 27

BLM: Higher Order

NOT: Macro TB\_2-116

**Figure 2-8**

117. Refer to Figure 2-8. What would be an efficient combination of bathtubs and barrels?
- 30 barrels and 6 bathtubs
  - 20 barrels and 8 bathtubs
  - 25 barrels and 10 bathtubs
  - 15 barrels and 12 bathtubs

ANS: A

PTS: 1

DIF: Challenging

REF: p. 27

BLM: Higher Order

NOT: Macro TB\_2-117

118. Refer to Figure 2-8. What is the opportunity cost of moving from point A to point B?
- 8 bathtubs
  - 20 barrels
  - the difference between the 8 bathtubs you get and the 20 barrels you give up
  - the difference between the 20 barrels you get and the 8 bathtubs you give up

ANS: B

PTS: 1

DIF: Challenging

REF: p. 27

BLM: Higher Order

NOT: Macro TB\_2-118

119. Refer to Figure 2-8. If this economy puts all of its resources into the production of bathtubs, how many could it produce?
- 35 barrels and 0 bathtubs
  - 20 barrels and 12 bathtubs
  - 12 barrels and 35 bathtubs
  - 0 barrels and 16 bathtubs

ANS: D

PTS: 1

DIF: Average

REF: p. 27

BLM: Higher Order

NOT: Macro TB\_2-119

120. Refer to Figure 2-8. Which of the following combinations is impossible for this economy to produce?

- a. 30 barrels and 6 bathtubs
- b. 25 barrels and 10 bathtubs
- c. 20 barrels and 8 bathtubs
- d. 10 barrels and 14 bathtubs

ANS: B                      PTS: 1                      DIF: Challenging    REF: p. 27  
 BLM: Higher Order                      NOT: Macro TB\_2-120

121. Refer to Figure 2-8. What would happen if this economy moved from point C to point E?
- a. It still would not be producing efficiently.
  - b. There would be no gain in either bathtubs or barrels.
  - c. It would be producing more barrels and more bathtubs than at point C.
  - d. It is not possible for this economy to move from point C to point E without additional resources.

ANS: A                      PTS: 1                      DIF: Challenging    REF: p. 27  
 BLM: Higher Order                      NOT: Macro TB\_2-121

122. What two broad subfields is the field of economics traditionally divided into?
- a. national economics and international economics
  - b. consumer economics and producer economics
  - c. private sector economics and public sector economics
  - d. microeconomics and macroeconomics

ANS: D                      PTS: 1                      DIF: Easy                      REF: p. 29  
 BLM: Remember                      NOT: Macro TB\_2-122

123. What does microeconomics study?
- a. the behaviour of consumers
  - b. how individual households and firms make decisions
  - c. how government affects the economy
  - d. how the economy as a whole works

ANS: B                      PTS: 1                      DIF: Easy                      REF: p. 29  
 BLM: Remember                      NOT: Macro TB\_2-123

124. What does macroeconomics study?
- a. individual decision makers
  - b. economic history
  - c. economy-wide phenomena
  - d. how firms maximize profit

ANS: C                      PTS: 1                      DIF: Easy                      REF: p. 29  
 BLM: Remember                      NOT: Macro TB\_2-124

125. Which of the following would be considered a topic of study in macroeconomics?
- a. the impact of agricultural price support programs in the cotton industry
  - b. the effect on Canadian steel producers due to an import quota imposed on foreign steel
  - c. the effect of an increase in the price of imported oil on the Canadian inflation rate
  - d. the effect of an increase in the price of imported coffee beans on the Canadian coffee industry

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 29  
 BLM: Remember                      NOT: Macro TB\_2-125

126. Which of the following might a microeconomist NOT study?



- a. the effects of rent control on housing in Toronto
- b. how a college student makes financial decisions
- c. how tariffs on shoes affects the shoe industry
- d. the effect on the economy when unemployment rates change

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 29  
 BLM: Higher Order                      NOT: Macro TB\_2-126

127. Which of the following would a macroeconomist NOT study?
- a. the impact of minimum-wage laws on employment in the fast food industry
  - b. the effect of changes in saving rates on GDP
  - c. the impact of monetary policy on the rate of inflation
  - d. the effect of tax policy on the rate of economic growth

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 29  
 BLM: Higher Order                      NOT: Macro TB\_2-127

128. What are economists who try to explain economic phenomena considered?
- a. scientists
  - b. policy advisors
  - c. mathematicians
  - d. teachers

ANS: A                      PTS: 1                      DIF: Easy                      REF: p. 30  
 BLM: Remember                      NOT: Macro TB\_2-128

129. What are economists who try to improve the world considered?
- a. mathematicians
  - b. policy advisors
  - c. scientists
  - d. politicians

ANS: B                      PTS: 1                      DIF: Easy                      REF: p. 30  
 BLM: Remember                      NOT: Macro TB\_2-129

130. What are the roles of economists when trying to explain or to improve the world?
- a. In trying to explain the world, economists are policy advisers; in trying to improve the world, they are scientists.
  - b. In trying to explain the world, economists are mathematicians; in trying to improve the world, they are policymakers.
  - c. In trying to explain the world, economists are mathematicians; in trying to improve the world, they are scientists.
  - d. In trying to explain the world, economists are scientists; in trying to improve the world, they are policy advisers.

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 30  
 BLM: Remember                      NOT: Macro TB\_2-130

131. For economists, what are the two types of statements about the world?
- a. assumptions and theories
  - b. true statements and false statements
  - c. specific statements and general statements
  - d. positive statements and normative statements

ANS: D                      PTS: 1                      DIF: Easy                      REF: p. 30  
 BLM: Remember                      NOT: Macro TB\_2-131

132. How do economists view positive statements?
- a. affirmative, justifying existing economic policy
  - b. optimistic, putting the best possible interpretation on things
  - c. descriptive, making a claim about how the world is
  - d. prescriptive, making a claim about how the world ought to be

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 30  
BLM: Remember                      NOT: Macro TB\_2-132

133. How do economists view normative statements?
- a. descriptive, making a claim about how the world is
  - b. as statements about the normal condition of the world
  - c. prescriptive, making a claim about how the world ought to be
  - d. as statements that establish production goals for the economy

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 30  
BLM: Remember                      NOT: Macro TB\_2-133

134. Which of the following is an example of a positive statement?
- a. Prices rise when the government prints too much money.
  - b. If welfare payments increase, the world will be a better place.
  - c. Inflation is more harmful to the economy than unemployment.
  - d. The benefits to the economy of improved equity are greater than the costs of reduced efficiency.

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 30  
BLM: Higher Order                      NOT: Macro TB\_2-134

135. What does a normative statement describe?
- a. how the world was in the past
  - b. how the world is
  - c. how the world will be in the future
  - d. how the world ought to be

ANS: D                      PTS: 1                      DIF: Easy                      REF: p. 30  
BLM: Remember                      NOT: Macro TB\_2-135

136. Which of the following is an example of a normative statement?
- a. If the price of a product decreases, quantity demanded increases.
  - b. Reducing tax rates on the wealthy would be good for the country.
  - c. If the national saving rate was to increase, so would the rate of economic growth.
  - d. An increase in minimum wages will increase unemployment.

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 30  
BLM: Higher Order                      NOT: Macro TB\_2-136

137. What type of statement is “Prices rise when the government prints too much money”?
- a. a positive economic statement
  - b. a statement made by the Harper administration
  - c. a normative economic statement
  - d. a welfare statement

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 30  
BLM: Higher Order                      NOT: Macro TB\_2-137

138. What do economists from the Department of Finance provide?

- a. the annual Economic Report of the Prime Minister
- b. the Senate with the annual budget
- c. enforcement of the competition laws
- d. advice on tax policy to the Prime Minister

ANS: D                      PTS: 1                      DIF: Easy                      REF: p. 31  
BLM: Remember        NOT: Macro TB\_2-138

139. When economists are speaking as policy advisors, which statements are they more likely to use?

- a. normative statements
- b. positive statements
- c. objective statements
- d. descriptive statements

ANS: A                      PTS: 1                      DIF: Easy                      REF: p. 30-31  
BLM: Higher Order        NOT: Macro TB\_2-139

140. What does evaluating a positive statement involve?

- a. evaluating values as well as facts
- b. examining evidence
- c. views on ethics and religion
- d. consideration of the government's policy goals

ANS: B                      PTS: 1                      DIF: Easy                      REF: p. 30  
BLM: Remember        NOT: Macro TB\_2-140

141. Which of the following is NOT a positive statement?

- a. Higher gasoline prices will reduce gasoline consumption.
- b. Equity is more important than efficiency.
- c. Trade restrictions lower our standard of living.
- d. If a nation wants to avoid inflation, it should not print too much money.

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 30  
BLM: Higher Order        NOT: Macro TB\_2-141

142. Two economists, Adam and Joan, are discussing the possibility of substantially reforming the current federal tax system. Adam thinks the current system is fine, but Joan is in favour of reform. Which of the following is the LEAST likely explanation for the disagreement?

- a. Adam is a positive economist, and Joan is a normative economist.
- b. Adam and Joan have different positive views about the effect of changing the tax system.
- c. Adam and Joan have different values, and so they have different normative views about policy.
- d. Adam is better off under the current system, and Joan would be better off if the reforms were implemented.

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 30  
BLM: Higher Order        NOT: Macro TB\_2-142

143. When do you know an economist has crossed the line from scientist to policy adviser?

- a. when he explains just the facts
- b. when he makes positive statements
- c. when he makes normative statements
- d. when he cannot reach a conclusion

ANS: C                      PTS: 1                      DIF: Easy                      REF: p. 31

144. What do economists at Industry Canada do?
- a. conduct monetary policy
  - b. give advice to overseas development projects
  - c. help design and enforce Canada's competition laws
  - d. decide which industries should be protected

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 31

BLM: Remember                      NOT: Macro TB\_2-144

145. What do economists at the Canadian International Development Agency do?
- a. give advice on overseas development projects
  - b. collect data to help other economists
  - c. help formulate labour market policies
  - d. set monetary policy

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 31

BLM: Remember                      NOT: Macro TB\_2-145

146. What do economists at the Bank of Canada do?
- a. analyze data on labour markets
  - b. help negotiate trade agreements
  - c. analyze macroeconomic developments
  - d. enforce competition laws

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 31

BLM: Remember                      NOT: Macro TB\_2-146

147. In which department do economists help enforce competition laws?
- a. Environment Canada
  - b. Industry Canada
  - c. Ministry of Finance
  - d. Canadian International Development Agency

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 31

BLM: Remember                      NOT: Macro TB\_2-147

148. Economists outside the government also offer policy advice. Which of the following institutions does NOT publish reports by economists?
- a. C.D. Howe Institute
  - b. Fraser Institute
  - c. Institute for Research on Public Policy
  - d. H.M. Holmes Institute

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 31

BLM: Remember                      NOT: Macro TB\_2-148

149. What do economists at Foreign Affairs Canada and International Trade Canada do?
- a. help negotiate trade agreements with other countries
  - b. offer advice on overseas economic development projects
  - c. publish economic research
  - d. compile databases on the economy

ANS: A                      PTS: 1                      DIF: Easy                      REF: p. 31

BLM: Remember                      NOT: Macro TB\_2-149

150. What do the duties of the economists employed by Human Resources and Skill Development Canada include?
- a. advising Parliament
  - b. designing tax policy
  - c. writing the annual Economic Report
  - d. studying the relationship between average wages and gender

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 31

BLM: Remember                      NOT: Macro TB\_2-150

151. Who designs tax policy?
- a. Ministry of Finance
  - b. Bank of Canada
  - c. Human Resources
  - d. Department of Justice

ANS: A                      PTS: 1                      DIF: Easy                      REF: p. 31

BLM: Remember                      NOT: Macro TB\_2-151

152. What is a duty of Human Resources Canada?
- a. to analyze data on workers
  - b. to design tax policy
  - c. to enforce the country's antitrust laws
  - d. to advise the Prime Minister

ANS: A                      PTS: 1                      DIF: Easy                      REF: p. 31

BLM: Remember                      NOT: Macro TB\_2-152

153. What does The Bank of Canada do?
- a. designs tax policy
  - b. enforces the country's antitrust laws
  - c. sets the country's monetary policy
  - d. analyzes the data on workers

ANS: C                      PTS: 1                      DIF: Easy                      REF: p. 31

BLM: Remember                      NOT: Macro TB\_2-153

154. What does Human Resources Canada do?
- a. enforces the country's antitrust laws
  - b. analyzes economic developments in Canada
  - c. sets the country's monetary policy
  - d. helps formulate labour market policies

ANS: D                      PTS: 1                      DIF: Easy                      REF: p. 31

BLM: Remember                      NOT: Macro TB\_2-154

155. What famous economist said, "The ideas of economists and political philosophers ... are more powerful than is commonly understood"?
- a. Gregory Mankiw
  - b. John Maynard Keynes
  - c. Paul Krugman
  - d. David Ricardo

ANS: B                      PTS: 1                      DIF: Easy                      REF: p. 32

BLM: Remember                      NOT: Macro TB\_2-155

156. What are the two basic reasons why economists often appear to give conflicting advice to policymakers?
- a. differences in opinions and education
  - b. differences in scientific judgments and values
  - c. differences in scientific judgments and education
  - d. differences in opinions and values

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 33

BLM: Remember                      NOT: Macro TB\_2-156

157. Why did George Bernard Shaw, among others, criticize economists?
- a. because they have too much influence over government decisions
  - b. because many ideas are too theoretical and therefore do not work in “real life”
  - c. because they tend to speak a different language, causing most people to not understand them
  - d. because they seem to give conflicting advice to policymakers

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 35

BLM: Remember                      NOT: Macro TB\_2-157

158. What are tariffs and quotas?
- a. policies that restrict trade among nations
  - b. instruments implemented to increase trade efficiency
  - c. measures endorsed by almost all economists
  - d. policies meant to improve the well-being of consumers

ANS: A                      PTS: 1                      DIF: Challenging                      REF: p. 36

BLM: Remember                      NOT: Macro TB\_2-158

159. What did a survey that asked the opinion of academic, business, and government economists on ten propositions about economic policy find?
- a. The respondents were almost equally divided on the propositions.
  - b. The respondents favoured the propositions by a slight margin.
  - c. The respondents disagreed with the propositions by a slight margin.
  - d. There was overwhelming endorsement of the propositions among the respondents.

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 36

BLM: Remember                      NOT: Macro TB\_2-159

160. What do almost all economists agree on about rent control?
- a. It improves the availability and quality of housing.
  - b. It allows the market for housing to work more efficiently.
  - c. It adversely affects the availability and quality of housing.
  - d. It is a very inexpensive way to help the most needy members of society.

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 36

BLM: Remember                      NOT: Macro TB\_2-160

161. Which of the following is the best explanation for why policies such as rent control and import quotas persist in spite of the fact that experts are united in their opposition to such policies?
- a. Economists have not yet convinced the general public that the policies are undesirable.
  - b. Economists are simply wrong about the economic impact of these policies.
  - c. Economists have different values than do most people.
  - d. Economists are usually of a different political party than are lawmakers.

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 36  
BLM: Remember                      NOT: Macro TB\_2-161

162. What are the three propositions about which most economists agree most often (in order from first to third)?
- rent control, tariffs and quotas, and floating exchange rates
  - tariffs and quotas, floating exchange rates, and fiscal policy
  - rent control, fiscal policy, and tariffs and quotas
  - fiscal policy, rent control, and floating exchange rates

ANS: A                      PTS: 1                      DIF: Challenging                      REF: p. 36  
BLM: Remember                      NOT: Macro TB\_2-162

163. What is the single most important purpose of your textbook?
- to teach you about the effects of the government's economic policies
  - to teach you the language of economics
  - to teach you the economist's way of thinking
  - to teach you how to make money

ANS: C                      PTS: 1                      DIF: Easy                      REF: p. 37-38  
BLM: Remember                      NOT: Macro TB\_2-163

164. How would any economist who says all policy decisions are easy be best described?
- They must understand the relationship between a market economy and the government.
  - They must be running for office.
  - They have a Ph.D. in economics.
  - They cannot be trusted.

ANS: D                      PTS: 1                      DIF: Easy                      REF: p. 37  
BLM: Remember                      NOT: Macro TB\_2-164

165. What did John Maynard Keynes believe the ideas of economists to be?
- generally incorrect
  - powerful
  - pie-in-the-sky ideals
  - not taken seriously

ANS: B                      PTS: 1                      DIF: Easy                      REF: p. 38  
BLM: Remember                      NOT: Macro TB\_2-165

166. How did John Maynard Keynes refer to economics?
- as an easy subject at which very few excel
  - as an easy subject, but not as easy as philosophy or the pure sciences
  - as an easy subject, which very few can enjoy
  - as an easy subject, which deals primarily with common sense

ANS: A                      PTS: 1                      DIF: Easy                      REF: p. 38  
BLM: Remember                      NOT: Macro TB\_2-166

167. How did the great economist John Maynard Keynes explain his comment that although economics is an easy subject compared with the higher branches of philosophy or pure science, it is a subject at which few excel?
- Most people who study economics are not very bright.
  - Good economists must possess a rare combination of gifts.
  - Economics is actually quite boring; hence, people tend to lose interest in it.

d. Good thinkers become frustrated with economics because it is not logical or relevant.

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 38  
BLM: Remember                      NOT: Macro TB\_2-167

168. Which of the following is a one-variable graph?

- a. a demand curve
- b. a production possibilities curve
- c. a circular-flow diagram
- d. a pie chart

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 42  
BLM: Remember                      NOT: Macro TB\_2-168

169. In a pie chart, what does each “slice” of the pie represent?

- a. a specific percentage of the total pie
- b. an equal share of the total pie
- c. the amount of the pie each of the two variables represents
- d. one-half of the total pie

ANS: A                      PTS: 1                      DIF: Easy                      REF: p. 41  
BLM: Remember                      NOT: Macro TB\_2-169

170. Why are graphs such as bar graphs limited?

- a. They can only show variables that are positively related.
- b. They are extremely difficult to understand.
- c. They provide information for only a single variable.
- d. They provide information on no more than two variables.

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 41  
BLM: Remember                      NOT: Macro TB\_2-170

171. In order to provide information on two variables, what must an economist use?

- a. a bar graph
- b. a pie chart
- c. the coordinate system
- d. a time-series graph

ANS: C                      PTS: 1                      DIF: Easy                      REF: p. 44  
BLM: Remember                      NOT: Macro TB\_2-171

172. What is a type of graph that can be used to display the relationship between two variables?

- a. a pie chart
- b. a bar graph
- c. a time-series graph
- d. the coordinate system

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 42  
BLM: Remember                      NOT: Macro TB\_2-172

173. What is a coordinate system used for?

- a. to show the flow of income and products in an economic system
- b. to organize labour and other resources in the production process
- c. to allow economists to show two variables on a single graph
- d. to teach economists how to draw graphs consistently



ANS: C                      PTS: 1                      DIF: Average                      REF: p. 42  
BLM: Remember                      NOT: Macro TB\_2-173

174. What is an ordered pair?
- a. the process of checking calculations twice before placing them on a graph
  - b. two numbers that can be represented by a single point on a graph
  - c. two numbers that are represented by side-by-side points on a graph
  - d. two points on a graph that are equal distances from the origin

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 42  
BLM: Remember                      NOT: Macro TB\_2-174

175. What is the first number in an ordered pair?
- a. the y-coordinate
  - b. the x-coordinate
  - c. either x or y, depending on the quadrant
  - d. not useful to know, since most graphs in economics use p and q, not x and y

ANS: B                      PTS: 1                      DIF: Easy                      REF: p. 42  
BLM: Remember                      NOT: Macro TB\_2-175

176. What is the ordered pair that represents the origin on a graph?
- a. (1, 1)
  - b. (0, 0)
  - c. (0, 1)
  - d. (1, 0)

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 42  
BLM: Remember                      NOT: Macro TB\_2-176

177. What is the x-coordinate?
- a. the first number of an ordered pair, which represents the point's horizontal location
  - b. the second number of an ordered pair, which represents the point's horizontal location
  - c. the first number of an ordered pair, which represents the point's vertical location
  - d. the second number of an ordered pair, which represents the point's vertical location

ANS: A                      PTS: 1                      DIF: Challenging                      REF: p. 43  
BLM: Remember                      NOT: Macro TB\_2-177

178. What is the y-coordinate?
- a. the first number of an ordered pair, which represents the point's horizontal location
  - b. the second number of an ordered pair, which represents the point's horizontal location
  - c. the first number of an ordered pair, which represents the point's vertical location
  - d. the second number of an ordered pair, which represents the point's vertical location

ANS: D                      PTS: 1                      DIF: Challenging                      REF: p. 43  
BLM: Remember                      NOT: Macro TB\_2-178

179. What does the x-coordinate give?
- a. the diagonal location of the point
  - b. the vertical location of the point
  - c. the horizontal location of the point
  - d. the quadrant location of the point

ANS: C                      PTS: 1                      DIF: Easy                      REF: p. 43  
BLM: Remember                      NOT: Macro TB\_2-179

180. What is the point where both x and y are zero called?

- a. the origin
- b. the null
- c. the zero coordinate
- d. the centre

ANS: A

PTS: 1

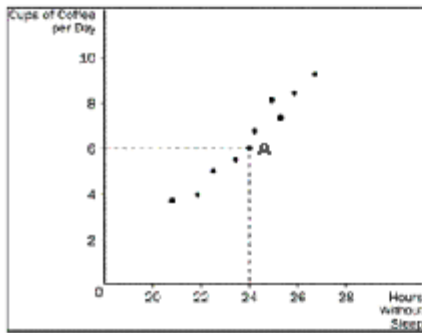
DIF: Easy

REF: p. 43

BLM: Remember

NOT: Macro TB\_2-180

**Figure 2-9**



181. Refer to Figure 2-9. What is this type of graph known as?

- a. a time-series graph
- b. a bar graph
- c. a scatterplot graph
- d. a pie chart

ANS: C

PTS: 1

DIF: Average

REF: p. 44

BLM: Higher Order

NOT: Macro TB\_2-181

182. Refer to Figure 2-9. What is the correct designation of point A?

- a. (6, 0)
- b. (0, 24)
- c. (6, 24)
- d. (24, 6)

ANS: D

PTS: 1

DIF: Average

REF: p. 44

BLM: Higher Order

NOT: Macro TB\_2-182

183. Refer to Figure 2-9. What do cups of coffee per day and the hours that someone can go without sleep have?

- a. a positive correlation
- b. a negative correlation
- c. a random correlation
- d. no correlation

ANS: A

PTS: 1

DIF: Average

REF: p. 44

BLM: Higher Order

NOT: Macro TB\_2-183

184. Refer to Figure 2-9. What would you say about the relationship between coffee and hours without sleep?

- a. The less coffee a person drinks per day, the more time he can go without sleep.

- b. There is no relationship between how much coffee per day a person drinks and how long they can go without sleep.
- c. The more coffee a person drinks per day, the longer he can go without sleep.
- d. The relationship between cups of coffee per day and time without sleep is too unpredictable to consider.

ANS: C                      PTS: 1                      DIF: Challenging    REF: p. 44  
 BLM: Higher Order                      NOT: Macro TB\_2-184

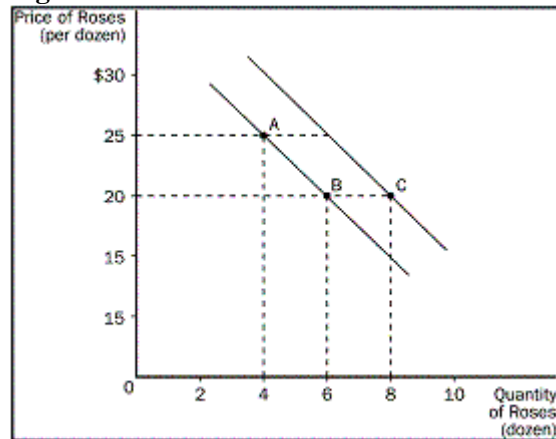
185. Refer to Figure 2-9. What are the curves shown?
- a. supply curves
  - b. demand curves
  - c. preference curves
  - d. income-consumption curves

ANS: B                      PTS: 1                      DIF: Easy                      REF: p. 45  
 BLM: Higher Order                      NOT: Macro TB\_2-185

186. What happens when two variables have a negative correlation?
- a. They tend to move in opposite directions.
  - b. They tend to move in the same direction.
  - c. One variable will move while the other remains constant.
  - d. The movement of the two variables is unpredictable.

ANS: A                      PTS: 1                      DIF: Easy                      REF: p. 45  
 BLM: Higher Order                      NOT: Macro TB\_2-186

**Figure 2-10**



187. Refer to Figure 2-10. What is the movement from point A to point B?
- a. a shift of the curve
  - b. a change in preferences
  - c. a movement along the curve
  - d. a change in consumer income

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 46  
 BLM: Higher Order                      NOT: Macro TB\_2-187

188. Refer to Figure 2-10. What is the movement from point B to point C?
- a. a shift of the curve
  - b. a change in price

- c. a movement along the curve
- d. a change in costs to the firm

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 46  
BLM: Higher Order                      NOT: Macro TB\_2-188

189. Refer to Figure 2-10. What is the slope of the curve between point A and point B?
- a.  $5/2$
  - b.  $2/5$
  - c.  $-2/5$
  - d.  $-5/2$

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 47  
BLM: Higher Order                      NOT: Macro TB\_2-189

190. Refer to Figure 2-10. What could have caused the movement from point B to point C?
- a. inflation
  - b. a change in income
  - c. a change in the price of roses
  - d. a change in the cost of producing roses

ANS: B                      PTS: 1                      DIF: Challenging                      REF: p. 46-47  
BLM: Higher Order                      NOT: Macro TB\_2-190

191. Refer to Figure 2-10. How are the price of roses and the quantity of roses related?
- a. directly related, and therefore moving in the same direction
  - b. directly related, and therefore moving in opposite directions
  - c. inversely related, and therefore moving in opposite directions
  - d. independent of each other

ANS: C                      PTS: 1                      DIF: Challenging                      REF: p. 47  
BLM: Higher Order                      NOT: Macro TB\_2-191

192. What does a demand curve show?
- a. the relationship between income and quantity demanded
  - b. the relationship between price and income
  - c. the relationship between price and quantity demanded
  - d. the relationship among income, price, and quantity demanded

ANS: C                      PTS: 1                      DIF: Average                      REF: p. 45  
BLM: Remember                      NOT: Macro TB\_2-192

193. What does a relatively steep demand curve mean?
- a. quantity demand will adjust slightly to a price change
  - b. quantity demand will adjust greatly to a price change
  - c. quantity demand will not adjust to a price change
  - d. the change in quantity demand will exactly equal a change in price

ANS: A                      PTS: 1                      DIF: Challenging                      REF: p. 45-47  
BLM: Remember                      NOT: Macro TB\_2-193

194. If Steven chooses to buy more bagels per month at each price, what will happen to his demand curve?
- a. It will shift inward.
  - b. It will shift outward.
  - c. It will not shift, but he will move along his demand curve from left to right.
  - d. It will not shift, but he will move along his demand curve from right to left.

ANS: B                      PTS: 1                      DIF: Challenging    REF: p. 46  
BLM: Higher Order                      NOT: Macro TB\_2-194

195. What happens when a relevant variable that is not named on either axis changes?
- a. There will be a movement along the curve.
  - b. The curve may or may not change depending on how the variables are related.
  - c. The curve will be unaffected since only the variables on the axis affect the curve.
  - d. The curve will shift.

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 46  
BLM: Remember                      NOT: Macro TB\_2-195

196. What happens when a variable on an axis of a graph changes?
- a. The curve will not shift.
  - b. The curve will shift.
  - c. The curve may or may not change depending on how the variables are related.
  - d. The curve will shift if the variable is on the vertical axis, but not on the horizontal axis.

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 46  
BLM: Remember                      NOT: Macro TB\_2-196

197. How is the slope of a straight line calculated?
- a. rise divided by run
  - b. run divided by rise
  - c. the average of rise and run
  - d. rise plus run

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 47  
BLM: Remember                      NOT: Macro TB\_2-197

198. How is the slope of a line calculated?
- a. change in x/change in y
  - b. change in y/change in x
  - c.  $x/y$
  - d.  $x + y$

ANS: B                      PTS: 1                      DIF: Average                      REF: p. 47  
BLM: Remember                      NOT: Macro TB\_2-198

199. What will the slope of a fairly flat upward-sloping line be?
- a. a small positive number
  - b. a large positive number
  - c. a small negative number
  - d. a large negative number

ANS: A                      PTS: 1                      DIF: Challenging    REF: p. 47  
BLM: Remember                      NOT: Macro TB\_2-199

200. Which of the following statements about slope is NOT correct?
- a. Slope explains how much one variable responds to changes in another variable.
  - b. Slope can be computed by  $\Delta x$  divided by  $\Delta y$ .
  - c. Slope is positive if the two variables are moving in the same direction.
  - d. Slope does not change if the line is linear.

ANS: B                      PTS: 1                      DIF: Challenging    REF: p. 47

201. Which of the following is NOT a problem associated with graphing in economics?
- omitted variables
  - holding everything else constant
  - reverse causality
  - the ability to show a relationship between two variables

ANS: D                      PTS: 1                      DIF: Average                      REF: p. 48-50

BLM: Remember                      NOT: Macro TB\_2-201

202. Bill has noticed that increases in unemployment insurance claims are associated with recessions, and therefore advocates limits on unemployment insurance so as to prevent recessions. Martha has noticed that most drug addicts once attended schools, and therefore advocates getting rid of schools so as to prevent drug addiction. What do we know about the reasoning of Bill and Martha?
- The reasoning of both Bill and Martha suffers from the omitted variable problem.
  - The reasoning of both Bill and Martha suffers from the reverse causality problem.
  - Bill's reasoning suffers from the reverse causality problem, and Martha's reasoning suffers from the omitted variable problem.
  - Martha's reasoning suffers from the reverse causality problem, and Bill's reasoning suffers from the omitted variable problem.

ANS: A                      PTS: 1                      DIF: Average                      REF: p. 48-50

BLM: Higher Order                      NOT: Macro TB\_2-202

### TRUE/FALSE

1. While the scientific method is applicable to studying natural sciences, it is not useful in studying an economic system.

ANS: F                      PTS: 1                      DIF: Average                      REF: p. 22

BLM: Remember                      NOT: Macro TB\_2-203

2. Since natural experiments offered by history cannot be used in economics, carefully constructed laboratory experiments must be used.

ANS: F                      PTS: 1                      DIF: Average                      REF: p. 22

BLM: Remember                      NOT: Macro TB\_2-204

3. An economic model can accurately explain how the economy is organized because it is designed to include every feature of the real world.

ANS: F                      PTS: 1                      DIF: Average                      REF: p. 24

BLM: Remember                      NOT: Macro TB\_2-205

4. All scientific models, including economic models, simplify reality in order to improve our understanding of it.

ANS: T                      PTS: 1                      DIF: Average                      REF: p. 24

BLM: Remember                      NOT: Macro TB\_2-206

5. A circular-flow diagram is a visual model of how an economy is organized.

ANS: T                      PTS: 1                      DIF: Average                      REF: p. 24-25

BLM: Remember NOT: Macro TB\_2-207

6. In a simple circular-flow diagram, firms own the factors of production and use them to produce goods and services.

ANS: F PTS: 1 DIF: Average REF: p. 24-25  
BLM: Remember NOT: Macro TB\_2-208

7. In a simple circular-flow diagram, the two types of markets in which households and firms interact are the markets for goods and services and the markets for factors of production.

ANS: T PTS: 1 DIF: Average REF: p. 24-25  
BLM: Remember NOT: Macro TB\_2-209

8. In the markets for goods and services, as in the markets for the factors of production, households are buyers and firms are sellers.

ANS: F PTS: 1 DIF: Average REF: p. 24-25  
BLM: Remember NOT: Macro TB\_2-210

9. In a circular-flow diagram, one loop shows the flow of real goods, services, and factors of production, and the other loop shows the corresponding flow of dollars.

ANS: T PTS: 1 DIF: Average REF: p. 24-25  
BLM: Remember NOT: Macro TB\_2-211

10. A production possibilities frontier is a graph that shows the various combinations of outputs the economy can possibly produce given its factors of production and technology.

ANS: T PTS: 1 DIF: Average REF: p. 26-28  
BLM: Remember NOT: Macro TB\_2-212

11. An economy can produce at any point on or outside the production possibilities frontier, but it cannot produce at points inside the frontier.

ANS: F PTS: 1 DIF: Easy REF: p. 26-28  
BLM: Remember NOT: Macro TB\_2-213

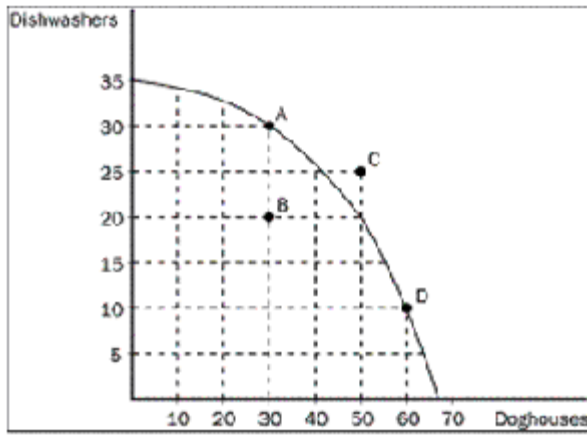
12. An efficient outcome in economics is one in which the economy is conserving the largest possible amount of resources, while still meeting the needs of society.

ANS: F PTS: 1 DIF: Average REF: p. 26-28  
BLM: Remember NOT: Macro TB\_2-214

13. An economy is being efficient if it is impossible to produce more of one good without producing less of another.

ANS: T PTS: 1 DIF: Average REF: p. 26-28  
BLM: Remember NOT: Macro TB\_2-215

**Figure 2-11**



14. Refer to Figure 2-11. Points A, B, and D represent feasible or attainable outcomes for society.

ANS: T                      PTS: 1                      DIF: Average                      REF: p. 27  
 BLM: Higher Order                      NOT: Macro TB\_2-216

15. Refer to Figure 2-11. The opportunity cost to the economy of moving from point A to point B is 10 dishwashers.

ANS: T                      PTS: 1                      DIF: Average                      REF: p. 27  
 BLM: Higher Order                      NOT: Macro TB\_2-217

16. Refer to Figure 2-11. The opportunity cost of more doghouses increases as more doghouses are produced.

ANS: T                      PTS: 1                      DIF: Average                      REF: p. 27  
 BLM: Higher Order                      NOT: Macro TB\_2-218

17. The tradeoff between the production of different goods can change because of technological improvement over time.

ANS: T                      PTS: 1                      DIF: Challenging                      REF: p. 28-29  
 BLM: Remember                      NOT: Macro TB\_2-219

18. Economic growth causes a production possibilities frontier to shift outward.

ANS: T                      PTS: 1                      DIF: Average                      REF: p. 28-29  
 BLM: Remember                      NOT: Macro TB\_2-220

19. The field of economics is divided into two subfields: microeconomics and macroeconomics.

ANS: T                      PTS: 1                      DIF: Average                      REF: p. 29  
 BLM: Remember                      NOT: Macro TB\_2-221

20. Normative statements describe how the world is, while positive statements prescribe how the world should be.

ANS: F                      PTS: 1                      DIF: Average                      REF: p. 30  
 BLM: Remember                      NOT: Macro TB\_2-222



21. “Society would be better if the welfare system were abolished” is a normative statement, not a positive statement.

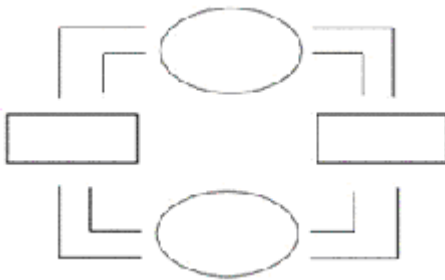
ANS: T                      PTS: 1                      DIF: Easy                      REF: p. 30  
BLM: Remember        NOT: Macro TB\_2-223

22. When economists are trying to explain the world they are acting as scientists, and when they are trying to improve it, they are policymakers.

ANS: T                      PTS: 1                      DIF: Average                      REF: p. 31  
BLM: Remember        NOT: Macro TB\_2-224

### SHORT ANSWER

1. Using this outline, draw a circular-flow diagram representing the interactions between households and firms in a simple economy. Explain briefly the various parts of the diagram.



ANS:

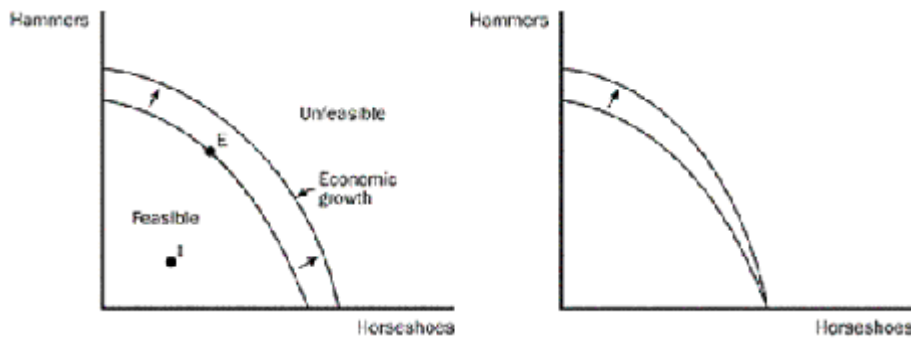
This diagram should duplicate the essential characteristics of the diagram in the text, with an explanation of the meaning of each flow and each market. It is important that the student understands that the inner loop represents the flow of real goods and services and that the outer loop represents the corresponding flow of payments.

PTS: 1                      DIF: Average                      REF: p. 25                      BLM: Higher Order  
NOT: Macro TB\_2-225

2. Draw a production possibilities frontier showing increasing opportunity cost for hammers and horseshoes.
- On the graph, identify the area of feasible outcomes and the area of unfeasible outcomes.
  - On the graph, label a point that is efficient as point E and a point that is inefficient as point I.
  - On the graph, illustrate the effect of the discovery of a new vein of iron ore, a resource needed to make both horseshoes and hammers, on this economy.
  - On a separate graph for hammers and horseshoes, illustrate the effect a new computerized assembly line in the production of hammers would have.

ANS:

The graph on the left answers a, b and c. The graph on the right answers d.



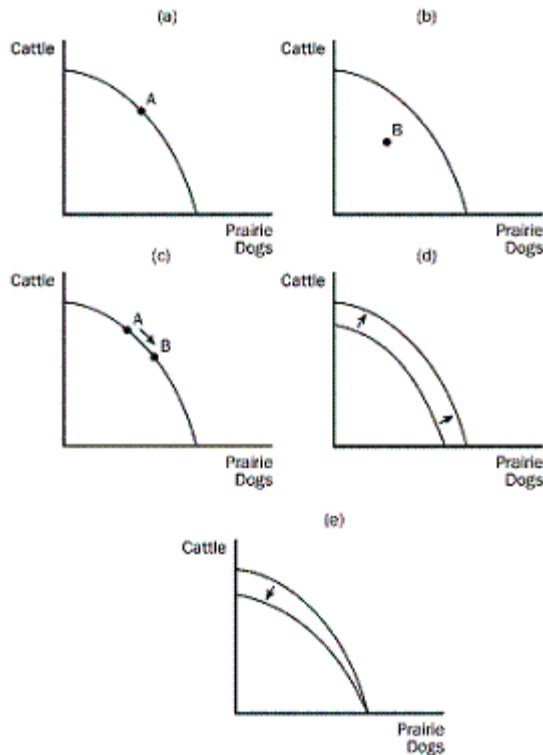
PTS: 1 DIF: Average REF: p. 27-29 BLM: Higher Order  
 NOT: Macro TB\_2-226

3. The prairie dog has always been considered a problem for Canadian cattle ranchers. They dig holes that cattle and horses can step in, and they eat grass necessary for cattle. Recently, ranchers have discovered that there is a demand for prairie dogs as pets. In some areas, prairie dogs can sell for as high as \$150. Cattlemen are now fencing off prairie dog towns on their land so these towns will not be disturbed by their cattle.

Draw a production possibilities frontier demonstrating a rancher's production option between cattle production and prairie dog production, showing increasing opportunity cost and what would happen in each of the following situations (using a separate graph for each situation):

- a. The outcome is efficient, with ranchers choosing to produce equal numbers of cattle and prairie dogs.
- b. As a protest against the government introducing the grey wolf back into the wild in their province, ranchers decide not to use 25% of the available grassland for grazing.
- c. The price of prairie dogs increases to \$200 each, so ranchers decide to allot additional land for prairie dogs.
- d. The government grants new leases to ranchers, giving them 10 000 new hectares of grassland each for grazing.
- e. A drought destroys most of the available grass for grazing of cattle, but not prairie dogs since they also eat plant roots.

ANS:



PTS: 1      DIF: Average      REF: p. 27-29      BLM: Higher Order  
 NOT: Macro TB\_2-227

4. Identify each of the following topics as being part of microeconomics or macroeconomics:
- the impact of a change in consumer income on the purchase of luxury automobiles
  - the effect of a change in the price of Coke on the purchase of Pepsi
  - the impact of a war in the Middle East on the rate of inflation in Canada
  - factors influencing the rate of economic growth
  - factors influencing the demand for tractors
  - the impact of tax policy on national saving
  - the effect of pollution taxes on the Canadian copper industry
  - the degree of competition in the cable television industry
  - the effect of a balanced-budget policy on economic stability
  - the impact of deregulation on the financial industry

ANS:

a, b, e, g, h, and j are microeconomic topics. c, d, f, and i are macroeconomic topics.

PTS: 1      DIF: Average      REF: p. 29-30      BLM: Higher Order  
 NOT: Macro TB\_2-228

5. Which of the following statements are positive and which are normative?
- The minimum wage creates unemployment among young and unskilled workers.
  - The minimum wage ought to be abolished.
  - If the price of a product in a market decreases, other things equal, quantity demanded will increase.
  - A little bit of inflation is worse for society than a little bit of unemployment.
  - There is a tradeoff between inflation and unemployment in the short run.

- f. If consumer income increases, other things equal, the demand for automobiles will increase.
- g. The Canadian income distribution is not equitable.
- h. Canadian workers deserve more liberal unemployment benefits.
- i. If interest rates increase, investment will decrease.
- j. If welfare benefits were reduced, the country would be better off.

ANS:

a, c, e, f, and i are positive statements. b, d, g, h, and j are normative statements.

PTS: 1

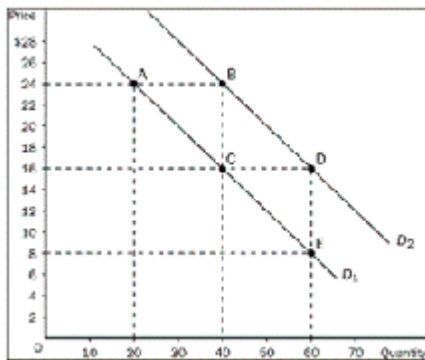
DIF: Average

REF: p. 30-31

BLM: Higher Order

NOT: Macro TB\_2-229

6. Use the following demand curve to answer the following questions:
  - a. How would point A be represented as an ordered pair?
  - b. What type of curve is this?
  - c. Does this curve show a positive or negative correlation between price and quantity?
  - d. Compute the slope of D1 between points A and C.
  - e. What is the slope of D1 between points C and E? Why would you NOT have to calculate this answer?
  - f. What is it called if we move from D1 to D2?
  - g. How do you know that the slope of D2 is the same as the slope of D1?



ANS:

- a. (20, 24)
- b. a demand curve
- c. a negative correlation between price and quantity
- d.  $-8/20$  or  $-2/5$
- e.  $-2/5$ ; because the slope of a straight line is constant
- f. an increase in demand
- g. because the two lines are parallel

PTS: 1

DIF: Average

REF: p. 45-47

BLM: Higher Order

NOT: Macro TB\_2-230

## PROBLEM

1. All people use models in their everyday lives, and I am no exception in this regard. While meteorologists use extremely complex weather forecasting models, my model is much simpler. My model predicts that if it is cold in the morning, it will be cold in the afternoon.
  - a. Why do I need such a silly model, instead of using more reliable forecasts that are easily and

- freely available?
- What is the main assumption of my model?
  - How did I choose the assumption underlying my model?
  - Is my assumption (and, therefore, my model) realistic?
  - Is my model useful?
  - How can I improve the predictions of my model?
  - What is your model of weather forecasting when deciding what to wear for the day?
  - What other simple models of weather forecasting can you imagine?

ANS:

- People think in models. Even when I know the “official” weather forecast of the day, I use some kind of a rudimentary model to decide whether to trust the forecast. Another reason for which I need my model is that I may not have access to more informed forecasts. And yet another reason is that I need very short-term forecasts, such as is it going to rain over the next half an hour? Can I go out to run in the park?
- The main assumption of my model is that the weather is stable over the day.
- The assumption underlying my model is based on past experience concerning how fast the weather changes in the area.
- My model is not very realistic, because the weather sometimes changes quickly.
- Absolutely. If I had no model, I wouldn’t be able to make up my mind as to how to dress. Every decision people make is based on some model, even when people are not fully aware of that.
- One way is to gather more information about the current outside temperature and atmospheric pressure. Another way would be to look out the window to see how other people are dressed. This last method is indeed very valuable, since it uses the power of collective wisdom.
- Different people have different models. For instance, some people carry an umbrella all the time, implicitly assuming that rain is always possible.
- Other model could assume that the weather is going to be this afternoon the same as yesterday afternoon; yet somebody else may assume that the weather is the same all month: hot and dry in July and August, warm and rainy in September, etc.

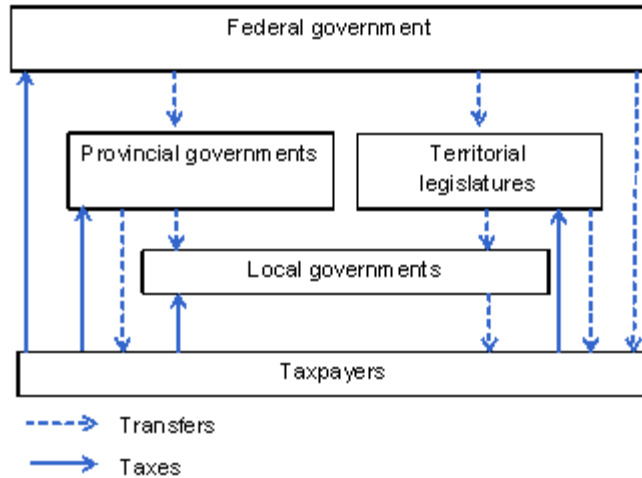
PTS: 1

NOT: Macro TB\_2-231

- This is an exercise in model building, based on the idea that one better understands the concept of models when faced with the task of making them.
  - Construct a block diagram showing how different levels of governments interact with taxpayers and with each other in a federal state like Canada. Indicate with arrows what they exchange with each other. Identify the main elements of your model.
  - Describe your model in a few sentences.
  - What makes your description to be a model, instead of an accurate picture of the Canadian economy?
  - What purpose can your model serve, or is there anything that this model helped you understand?

ANS:

a.



- b. A federal state has mainly three levels of government: federal, provincial, and local. Taxpayers, according to the model illustrated at point a, pay taxes directly to each level of government and receive transfers from each level of government. (This structure may be different for other federal structures.)
- c. This is a very simplified model. It does not say, for instance, how much taxes people pay to various levels of government or how much of the tax revenue is paid back to taxpayers. The model also omits to show what governments provide other than transfers.
- d. The model can be useful in describing the structure of a federal state, in particular showing how taxes and transfers move between taxpayers and various levels of government. The model needs to be more complex for other purposes, such as analysis.

PTS: 1

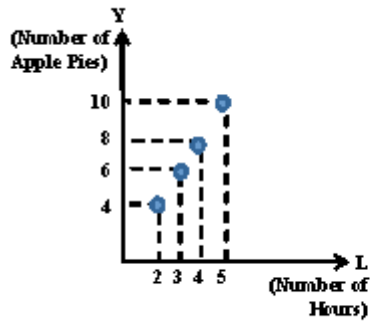
NOT: Macro TB\_2-232

3. The purpose of this exercise is to acquaint you with some simple mathematical relationships and how they translate into graphs. Economic models can come under the form of equations such as  $Y=F(L)$ , where  $Y$  is sometimes called the “dependent variable” and  $L$  is the “independent variable.”  $F$ , called “function,” tells us what the precise relationship between  $Y$  and  $L$  is. Theoretical relationships (models) are those that can be described by an equation like this. When equations are sufficiently simple, they can be put under the form of a curve in a graph. Consider the equation  $Y=2 \times L$ , where  $Y$  is the number of apple pies that Jonathan can cook in  $L$  hours. This equation describes the process of producing apple pies.
  - a. How many pies does Jonathan cook in 2, 3, 4, and 5 hours?
  - b. Draw a vertical axis and label it  $Y$ ; draw a horizontal axis and label it  $L$ . Show on this graph the four pairs  $(L, Y)$  you determined in part a.
  - c. Draw a line connecting your four points and extend it to the left until it reaches the vertical axis.
  - d. Identify a few assumptions that underlie your apple pie production model.
  - e. Are your assumptions realistic?
  - f. Can you identify a few limitations of your model?
  - g. What could you use this model for?

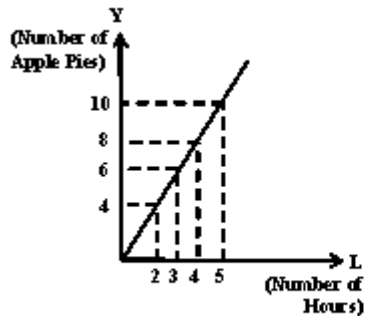
ANS:

- a. We use the equation to calculate the number of pies corresponding to various numbers of hours of work:  $Y=2 \times 2 = 4$ , when  $L=2$ . Similarly, we can find  $Y=6$  for 3 hours,  $Y=8$  for 4 hours, and  $Y=10$  when Jonathan works 5 hours.

b.



c.



- d. An important assumption of this model is that Jonathan never gets tired, even after a few hours of work: he is able to produce the same number of apple pies in the 5th hour as in the first. Another assumption is that Jonathan needs no preparation time: At the end of the first ten minutes, he must have produced already  $2/6=1/3$  of a finished pie.
- e. The assumptions are realistic as long as we do not ask Jonathan how many pies he has produced after ten minutes or if we do not make Jonathan work many extra hours.
- f. The conditions mentioned in the answer to point e are also the limitations of the model. In general, we should not try to use the model to predict the number of apple pies in unusual circumstances.
- g. The model can be used to predict, under normal circumstances, how many apple pies can be produced in a certain number of hours, and what the cost of that production would be.

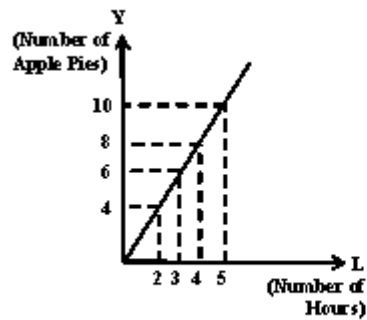
PTS: 1

NOT: Macro TB\_2-233

4. The purpose of this exercise is to show you how a mathematical (economic) model can be adjusted to better represent an economic phenomenon. Consider the equation  $Y=2 \times L$ , where Y is the number of apple pies that Jonathan can cook in L hours. This equation describes the process of producing apple pies.
  - a. In a Y?2-L graph, draw the line described by the equation  $Y=2 \times L$ . What is the slope of this line? What does the slope represent? Note that the slope is the same for the first, second, and all subsequent hours. In other words, the slope is constant. Why is the constant slope of the line a limitation of your model?
  - b. How should the slope change for higher values of L, the number of hours worked, to account for the fact that the worker might get tired?
  - c. How could you modify the model to capture the change in slope you identified in part b?

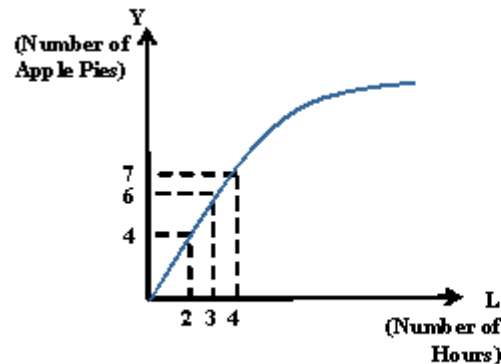
ANS:

a.



The slope of the curve can be calculated by the ratio  $\Delta Y / \Delta L$ , where the symbol  $\Delta$  represents a small change. For instance, if  $L$  changes from 4 to 5,  $\Delta L = 5 - 4 = 1$ ; the corresponding change in  $Y$  is an increase from 8 to 10. Thus, the slope =  $\Delta Y / \Delta L = (10 - 8) / (5 - 4) = 2$ . The slope shows by how much  $Y$  changes when  $L$  increases by one unit. In our example, the slope shows how many pies Jonathan produces in an extra hour. Constant slope suggests that Jonathan doesn't ever get tired: he produces in the late hours of the workday as much as in the first hours. This may be a limitation of the model.

- b. A more realistic model should imply that Jonathan produces fewer pies per hour after a few hours of work than at the beginning of the workday. Since the number of apple pies per hour is the slope, we want the slope to become smaller at larger values of  $L$ . In other words, we want the curve to go up at larger  $L$ s, but at a lower and lower rate.
- c. The following graph represents such a modified curve that better represents our situation. The curve becomes flatter at larger values of  $L$ .



ouslope you identified at point b?apture the change he number of hours worked?s. In other words, the slope is constant. hours,

PTS: 1

NOT: Macro TB\_2-234

5. This exercise will show you how different theories (models) can lead to very different courses of action. Suppose we ask the following question: Does income inequality promote economic growth and society's overall prosperity? Suppose two economists come up with the following theories (models): Economist A believes that wealth accumulation in just a few hands increases savings because consumption is necessarily limited. Higher savings, in turn, allow investing in new production facilities that increase the country's overall income and everybody is better off. So, Economist A advocates a non-equalitarian society.



Economist B thinks that a very unequal distribution of wealth will increase capacities of production beyond the purchasing power of an essentially poor mass of consumers. For a while, consumers will increase their consumption, and prosperity, by borrowing from the rich, but eventually they will not be able to repay their debts and the economy will collapse for lack of demand. At that point, investing in new production facilities becomes unnecessary. In conclusion, Economist B thinks that extreme income inequality is counterproductive.

- a. What are the policy implications of the two theories? (In other words, does it matter which theory is correct?)
- b. How would a scientist determine which theory is correct?
- c. Under what conditions would each of the two models be correct? Could one use both models under different circumstances?

ANS:

- a. The two theories have very different implications for policymaking. If policymakers believe the first theory, they advocate low corporate taxes, large corporations, little employment protection measures, and unregulated economies. If theory B is believed to be true, policymakers advocate a very progressive income tax system, so that an important part of large incomes is redistributed to the poor.
- b. The scientific method would try to compare economies that are similar in all respects except for income inequality, and see which of them fares better in terms of social prosperity, however one would like to measure it.
- c. The first model might be correct at relatively low levels of inequality, and the second would be correct when inequality reaches extreme levels. The question is: How low is “low” inequality, and what level could be dubbed “extreme”? It is hard to tell, unfortunately.

PTS: 1

NOT: Macro TB\_2-235