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## **Chapter 1: The Challenge of Economics**

### **Multiple Choice Questions**

1. The central problem of economics is the:
  - A. Distribution of goods and services to those in need.
  - B. Scarcity of resources relative to human wants.
  - C. Inefficiency of government operations.
  - D. Unemployment of certain factors of production.
  
2. The primary concern of economics is the study of:
  - A. Why human wants exist and what motivates them.
  - B. How to distribute goods and services according to human needs.
  - C. How best to allocate scarce resources among competing uses.
  - D. Who holds the most political power in a particular country.

3. Which of the following explains why economic choices must be made?
  - A. The factors of production are scarce.
  - B. The factors of production are expensive.
  - C. The factors of production are used inefficiently.
  - D. The factors of production are of inferior quality.
  
4. The study of economics focuses on:
  - A. The behavior of successful businesses.
  - B. The role of money in our economy.
  - C. How best to allocate scarce resources.
  - D. The elimination of opportunity costs.
  
5. Opportunity cost may be defined as the:
  - A. The value of goods or services that are forgone in order to obtain something else.
  - B. Dollar price paid for a final good or service.
  - C. Dollar cost of producing a particular product.
  - D. Dollar cost of the next best alternative resources for producing a good.
  
6. Given that resources are scarce:
  - A. A "free lunch" is possible, but only for a limited number of people.
  - B. Poor countries must make choices, but rich countries do not have to make choices.
  - C. Opportunity costs are experienced whenever choices are made.
  - D. Some choices involve opportunity costs while other choices do not.

7. The opportunity cost of playing tennis with your friend is:
- A. Negative since its good exercise.
  - B. Zero since you already own the tennis racket and play on a public court.
  - C. The next-best alternative use of your time that is forgone.
  - D. The cost of the tennis lessons you took last year.
8. The concept of opportunity cost would become irrelevant if:
- A. The market mechanism functioned to allocate resources.
  - B. The government allocated resources.
  - C. The production possibilities curve bowed outward.
  - D. Resources were no longer scarce.
9. If resources are limited:
- A. People will rush to buy more goods than they would otherwise.
  - B. Businesses will sell more products than they would otherwise.
  - C. Choices that involve tradeoffs must be made.
  - D. All individuals are deprived of basic necessities.
10. Which of the following is true about the factors of production?
- A. The factors of production as well as technology determine the physical limits to production.
  - B. Rich countries have an unlimited quantity of factors.
  - C. The factors include natural resources but not skilled labor.
  - D. Some factors are scarce but other factors are not.

11. If society lacks enough resources to satisfy all the desired uses of the resources, this is known as:

- A. Government failure.
- B. Laissez faire.
- C. Scarcity.
- D. Market failure.

12. Scarcity means:

- A. Retail stores always run out of popular products.
- B. The desire for goods exceeds our capacity to produce them.
- C. Society will run out of the factors of production in the near future.
- D. A surplus of unsold goods in a specific market will not occur.

13. Societies must address the question of WHAT to produce because:

- A. We can't produce all the goods and services we want.
- B. The amount of money in an economy is limited.
- C. We are wasteful and use resources inefficiently.
- D. Our economy experiences market failures.

14. Which of the following is the best example of the "WHAT" economic question?
- A. Is the production process using an efficient amount of labor and capital machinery?
  - B. Who gets the goods once they are produced?
  - C. What is the most efficient method for producing goods?
  - D. What is the optimal mix of output?
15. Which of the following is NOT a factor of production?
- A. A toll-bridge across a lake.
  - B. The money hidden in an old basement.
  - C. A wrecking ball used to tear down old buildings.
  - D. The CEO of a large corporation.
16. In economics, capital refers to:
- A. Money.
  - B. Savings put aside for future investment.
  - C. Goods that can be used to produce other goods.
  - D. The value of a corporation's assets.
17. In economics, which of the following is the best example of capital?
- A. Money held in a checking account.
  - B. A computer used by a lawyer to prepare legal documents.
  - C. Investment in training for employees in an accounting firm.
  - D. The executive producer of a new adventure movie.

18. Which of the following is NOT an example of land, or a natural resource?

- A. Coal.
- B. A river.
- C. Natural gas.
- D. A homebuilder.

19. Which of the following is an example of labor as a factor of production?

- A. People who bring together the skills necessary for creating products and services.
- B. The skills and abilities of workers.
- C. People who are paid an hourly wage but not those paid a salary.
- D. A college or university that educates people.

20. Entrepreneurship refers to:

- A. Natural resources, such as land and water.
- B. Computer technology.
- C. Skilled labor.
- D. Ability to see market opportunities and the will to take risk.

21. In economics, which of the following represents entrepreneurship?

- A. Natural resources.
- B. Skill in creating products and services.
- C. The skills of workers.
- D. Machinery, buildings and networks.

22. Output choices are necessary within a market because of:

- A. Inefficient use of resources.
- B. High prices for goods.
- C. Scarcity of resources.
- D. Limited technology.

23. When economists talk about a trade-off between "guns and butter," they mean:

- A. Society can produce more military goods without giving up any consumer goods.
- B. Military goods are an inefficient use of resources.
- C. The production of more military goods may require fewer consumer goods.
- D. Consumer goods are always more costly than military goods.

**Table 1.1 - Production possibilities and opportunity costs of missiles and houses**

Table 1.1 shows the tradeoff between different combinations of missile production and home construction, *ceteris paribus*. Complete the table by calculating the required opportunity costs for both missiles and houses. Then answer the indicated question(s).

Combination	Number of houses	Opportunity cost of houses in terms of missiles	Number of missiles	Opportunity cost of missiles in terms of houses
J	0		4	
K	10,000		3	
L	17,000		2	
M	21,000		1	
N	23,000		0	

24. In Table 1.1, what is the opportunity cost of increasing the production of missiles from 2 to 3 in terms of houses?
- A. 1,000 houses.
  - B. 3,333 houses.
  - C. 7,000 houses.
  - D. 17,000 houses.
25. In Table 1.1, the opportunity cost of increasing the production of houses from 17,000 to 21,000 in terms of missiles per house is:
- A. 0.00014 of a missile.
  - B. 0.00025 of a missile.
  - C. 2.00 missiles.
  - D. 4.00 missiles.
26. In Table 1.1, the lowest opportunity cost of houses in terms of missiles is:
- A. 0.00010 of a missile per house.
  - B. 0.00050 of a missile per house.
  - C. 7.00 missiles per house.
  - D. 10.00 missiles per house.



27. In Table 1.1, the highest opportunity cost of missiles in terms of houses is:

- A. 500 houses per missile.
- B. 4,000 houses per missile.
- C. 7,000 houses per missile.
- D. 10,000 houses per missile.

28. Which of the following statements about production possibilities is true?

- A. Production possibilities are limited for all countries because resources are scarce.
- B. The production of food does not involve opportunity costs since people must eat.
- C. Production possibilities will expand if the level of inefficiency is reduced.
- D. Production possibilities are only limited for a country if prices are too high.

29. Which of the following is NOT an assumption under which the production possibilities curve is drawn?

- A. The economy's resources are fully employed.
- B. The price level is stable.
- C. Technology is being held constant.
- D. The supplies of factors of production are fixed.
- E. The trade-off of one good for another is always constant.

30. All points on the production possibilities curve:

- A. Represent the use of all available resources.
- B. Are equally desirable.
- C. Represent the same mix of output.
- D. Represent the same opportunity costs.

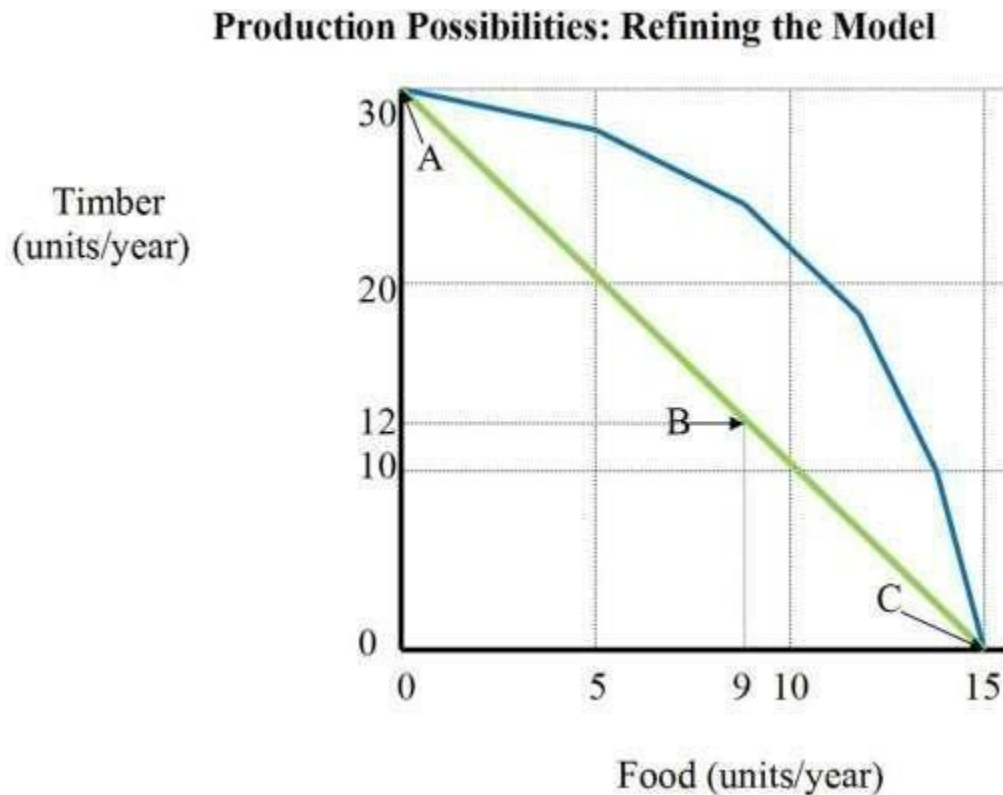
31. Ceteris paribus, if North Korea increases the size of its military, then:

- A. Its production possibilities curve will shift outward.
- B. Its production possibilities curve will shift inward.
- C. Its production of consumer goods will increase.
- D. Its production of consumer goods will decrease.

32. Assuming the level of resources and technology are constant, if France decreases the size of its military, then:

- A. Its' production possibilities curve will shift outward.
- B. Its' production possibilities curve will shift inward.
- C. Its' production of consumer goods can increase.
- D. Its' production of consumer goods must decrease.

**Figure 1.1 - Production Possibilities and Opportunity Costs: Linear Model versus Non-Linear Model**



In the linear production possibilities model, we assume each of five equally-sized parcels of land contributes the same to the production of food and timber: 6 units of timber or 3 units of food.

By contrast, in the non-linear model, we will assume that there are five different types of land in equal-sized plots and that each plot may contribute as follows to the production of

		<u>FOOD</u> or <u>TIMBER</u> :	
A.	Great farmland/Terrible timberland	+5	+2
B.	Good farmland/Poor timberland	+4	+4
C.	Moderate farmland/Moderate timberland	+3	+6
D.	Poor farmland/Good timberland	+2	+8
E.	Terrible farmland/Great timberland	+1	+10





33. Assuming all parcels of land are the same, when all land is in use, one more unit of timber produced will require...
- A. Two more units of food produced
  - B. Five fewer units of food produced
  - C. One-half fewer units of food produced
  - D. Two fewer units of food produced
34. Assuming all parcels of land are the same, there is a constant trade-off in the production of timber and food. When all land is in use, one more unit of food produced will require...
- A. Two more units of timber produced
  - B. Five fewer units of timber produced
  - C. One-half fewer units of timber produced
  - D. Two fewer units of timber produced
35. Assuming all land is equally productive in either use, how much output of each type will be produced with  $\frac{2}{5}$  of the land in timber production and  $\frac{3}{5}$  of the land in food production?
- A. 12 units of timber and 9 units of food
  - B. 9 units of timber and 12 units of food
  - C. 18 units of timber and 9 units of food
  - D. 9 units of timber and 18 units of food

36. Now assume that there are five different types of land in equally-sized parcels:

- A. Great farmland/Terrible timberland
- B. Good farmland/Poor timberland
- C. Moderate farmland/Moderate timberland
- D. Poor farmland/Good timberland
- E. Terrible farmland/Great timberland

Starting from point A on the production possibilities line where 30 units of timber and no food is produced, suppose that we choose to produce more food by moving one parcel of land out of timber production and into food production. In order to minimize the opportunity cost of producing more food, the first plot to be re-purposed should be...

- A.A.
- B.B.
- C. C.
- D.D.
- E. E.

37. In the model where we assume that all parcels of land are the same, the relationship between food and timber produced when all land is in use is:

- A.Linear and inverse.
- B.Direct and linear.
- C. Inverse and nonlinear.
- D. Direct and nonlinear.

38. In the model where we assume that all five parcels of land are NOT the same, the relationship between food and timber produced when all land is in use is:
- A. Linear and inverse.
  - B. Direct and linear.
  - C. Inverse and nonlinear.
  - D. Direct and nonlinear.
39. The most desirable attainable mix of output for society:
- A. Consists of the entire production possibilities curve.
  - B. Consists of a point on the production possibilities curve.
  - C. Consists of a point outside the production possibilities curve.
  - D. Occurs at the origin of the x- and y-axes on which the production possibilities curve is graphed.
40. In attempting to answer the WHAT question, a society seeks to:
- A. Produce the optimal mix of output.
  - B. Exploit its workers in order to produce more output.
  - C. Produce more military goods so that the citizens will be safe.
  - D. Distribute an equal amount of goods to all citizens.



41. Investment refers to all of the following except:

- A. An increase in business inventories.
- B. The purchase of new equipment by a business.
- C. The construction of new factories by a company.
- D. The purchase of stock by an individual.

42. Which of the following is NOT an example of investment?

- A. A hair salon buys additional hair dryers.
- B. The campus bookstore buys new T-shirts with the college logo.
- C. A business owner uses his profits to play the lottery and wins.
- D. Toyota expands the size of its factories located in the United States.

43. Economic growth always takes the form of

- A. An expansion of production possibilities.
- B. A change in how goods are distributed.
- C. A movement along the production possibilities curve.
- D. Higher prices.

44. Economic growth is represented by:

- A. An inward shift of the production possibilities curve.
- B. A point inside the production possibilities curve.
- C. An outward shift of the production possibilities curve.
- D. A movement along the production possibilities curve.

45. The production possibilities curve shifts outward in response to:
- A. A decline in technology or more resources or both.
  - B. A decline in technology or fewer resources or both.
  - C. Improved technology or more resources or both.
  - D. Improved technology or fewer resources or both.
46. Ceteris paribus which of the following is likely to cause an outward shift of the production possibilities curve?
- A. Investment in telecommunications networks.
  - B. The deportation of illegal immigrants.
  - C. An increase in the unemployment rate.
  - D. A tax increase on factors of production.
47. Ceteris paribus when technological change allows a smaller amount of a resource to be used in producing any combination of two goods, there will be:
- A. A movement along the production possibilities curve.
  - B. An outward shift of the production possibilities curve.
  - C. An inward shift of the production possibilities curve.
  - D. No change in the production possibilities curve.

48. Ceteris paribus, which of the following is least likely to contribute to economic growth?

- A. A greater quantity of labor.
- B. A greater quantity of capital.
- C. An increase in prices.
- D. Improved production technology.

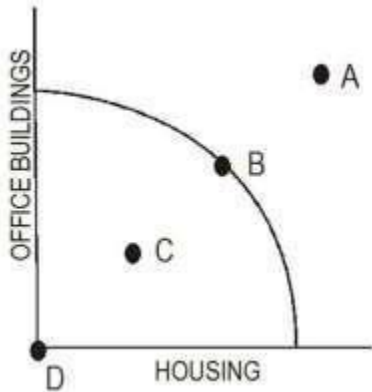
49. Ceteris paribus, which of the following will most likely cause an inward shift of the production possibilities curve?

- A. A decrease in the size of the labor force.
- B. An increase in population.
- C. An increase in knowledge.
- D. An improvement in technology.

50. Ceteris paribus which of the following events would most likely cause the production possibilities curve to shift inward?

- A. The labor supply grows.
- B. New factories are built.
- C. A technological breakthrough occurs that makes production of all goods more efficient.
- D. A major earthquake destroys several industrial centers.

**Figure 1.1 - Production-possibilities curve**



51. Society is employing some of the available technology but not all of it. Select the appropriate point. (See Figure 1.1)

- A.A
- B.B
- C.C
- D.D

52. Society is producing some output, but some of the available resources are unemployed. Select the appropriate point. (See Figure 1.1)

- A.A
- B.B
- C.C
- D.D

53. Society is producing the maximum potential output, given its existing resources and technology. Select the appropriate point. (See Figure 1.1)

A.A

B.B

C. C

D.D

54. Society might be able to produce this combination if new resources were discovered but cannot produce it with current resources. Select the appropriate point. (See Figure 1.1)

A.A

B.B

C. C

D.D

55. It is not possible for society to produce this combination with current resources and technology. Select the appropriate point. (See Figure 1.1)

A.A

B.B

C. C

D.D

56. Society is not producing either good because of extreme inefficiencies. Select the appropriate point. (See Figure 1.1)

A.A

B.B

C.C

D.D

57. When society searches for the optimal method of producing goods and services, it is responding to the:

A. "WHAT" question.

B. "HOW" question.

C. "FOR WHOM" question.

D. "WHY" question.

58. When society struggles with how to divide up the "economic pie," it is responding to the:

A. "FOR WHOM" question.

B. "HOW" question.

C. "WHAT" question.

D. "WHY" question.

59. Welfare programs are designed to address the:

- A. "HOW" question.
- B. "FOR WHOM" question.
- C. Issue of scarce resources.
- D. "WHAT" question.

60. Which of the following best describes the way resources are allocated in the U.S. economy?

- A. By rules.
- B. By markets.
- C. By regulations.
- D. By government.

61. The market mechanism:

- A. Works through central planning by the government.
- B. Eliminates market failures created by the government.
- C. Uses prices as a means of communication between consumers and producers.
- D. Is very inefficient since consumers cannot communicate directly with producers.

62. The market mechanism:

- A. Is an inefficient means of communicating consumer wants to producers.
- B. Relies on government control and planning.
- C. Eliminates the market failures caused by government.
- D. Relies on prices and sales to communicate consumer wants to producers.

63. The essential signal of the market mechanism is:

- A. Income.
- B. Price.
- C. Property.
- D. Government directive.

64. The price of a good or service:

- A. Never has an impact on the market mechanism.
- B. Serves as the essential signal of the market mechanism.
- C. Sometimes plays a role in the market mechanism.
- D. Rarely has an impact on the market mechanism.

65. Which of the following best describes the "invisible hand?"

- A. Price signals drive the market mechanism.
- B. Government regulations influence the allocation of society's scarce resources.
- C. The Internal Revenue Service enforces the nation's tax laws.
- D. Lobbyists influence which laws are passed by Congress.

66. The essential feature of the market mechanism is:

- A. That every consumer is concerned about the welfare of others.
- B. The price signal for both consumers and producers.
- C. Equity in the distribution of income and housing.
- D. Government taxation of profits.



67. Laissez faire refers to:

- A. The belief that government can make better choices than the market about the mix of output.
- B. The economic theory of Karl Marx.
- C. A belief of nonintervention by government in the market mechanism.
- D. A preference for central planning.

68. Which of the following is most consistent with a market economy?

- A. Shortages.
- B. Central planners.
- C. Government directives.
- D. Laissez faire.

69. Which of the following individuals is typically associated with a laissez faire economic policy?

- A. Adam Smith.
- B. Karl Marx.
- C. The Chairman of the Federal Reserve.
- D. John Maynard Keynes.

70. Which of the following statements is consistent with central planning?

- A. The economy relies heavily on the market mechanism to allocate resources.
- B. Government planners play the dominant role in deciding how resources are allocated.
- C. Economic decisions are made by large competitive firms.
- D. Market prices are used to guide production and consumption activities.

71. Karl Marx wrote:

- A. Das Kapital, which was used as the rationale for centrally-planned economies.
- B. Das Kapital, which described the virtues of market-based economies.
- C. The Wealth of Nations, which provided the rationale for centrally-planned economies.
- D. The Wealth of Nations, which described the virtues of market-based economies.

72. Central planning is the principal method for making economic decisions in:

- A. The United States.
- B. Singapore.
- C. New Zealand.
- D. North Korea.

73. The economy of the United States is best characterized as:

- A. Centrally planned.
- B. A laissez faire model.
- C. A mixed economy.
- D. A democratic socialist economy.

74. Which of the following is NOT a reason why the U.S. government intervenes in the economy?

- A. To ensure the safety of products.
- B. To reduce pollution.
- C. To make a profit for the government.
- D. To improve the mix of output.

75. If the market mechanism causes the economy to arrive at the wrong mix of output, there is:

- A. Market failure.
- B. Mixed economy failure.
- C. Government failure.
- D. Laissez faire.

76. Market failure means:

- A. Government solutions fail to improve economic outcomes.
- B. The market mechanism does not produce the best mix of output.
- C. The market allocates goods more efficiently than does the government.
- D. The market is responsive to consumer demand.

77. An externality is:

- A. A cost or benefit of a market activity that impacts a third party.
- B. The private costs that are borne by an individual.
- C. The cost of clean up paid for by the polluter.
- D. A situation in which the government solution makes the outcome worse.

78. Which of the following is an example of a negative externality?

- A. A decrease in available educational options due to government intervention.
- B. An increase in government bureaucracy and red tape.
- C. An increase in the incidence of cancer due to pollution.
- D. An introduction to a pollution decreasing technology.

79. Pollution is an example of:

- A. Inefficiency by the polluting firm.
- B. Market failure.
- C. Government transfers.
- D. Economic instability.

80. If government intervention fails to improve economic outcomes, the result is known as:

- A. Government failure.
- B. Market failure.
- C. Mixed economy failure.
- D. Laissez faire.

81. Government intervention designed to address market failure:

- A. May either improve or worsen the mix of output produced.
- B. Will definitely worsen the mix of output produced.
- C. Will definitely improve the mix of output produced.
- D. Never has an impact on the mix of output produced.

82. Which of the following is an example of government failure?

- A. A negative externality, such as pollution.
- B. An increase in bureaucracy and red tape that fails to improve economic outcomes.
- C. An increase in airline safety.
- D. An increase in the costs of production and an improvement in economic outcomes.

83. Which of the following groups of words best represents macroeconomic goals?

- A. Full employment, price stability, economic growth.
- B. Rate of production, choice of factors of production, and the pricing of specific goods.
- C. Welfare of individual consumers and business firms.
- D. Land, labor, and capital.

84. Macroeconomics focuses on:

- A. Government failure.
- B. The behavior of individuals, firms, and government agencies.
- C. Land, labor, and capital.
- D. The economy as a whole.

85. Microeconomics focuses on:

- A. Full employment, price stability, and economic growth.
- B. The behavior of individuals, firms, and government agencies.
- C. Land, labor, and capital.
- D. Centrally planned economies.

86. Which of the following is associated with microeconomics?

- A. An increase in sales for a chain of pet supply stores.
- B. A decrease in the unemployment rate for the nation.
- C. An increase in the inflation rate for the entire economy.
- D. A decrease in the level of economic growth for the country.

87. Which of the following is associated with microeconomics?

- A. An economy's overall output level.
- B. The country's unemployment rate.
- C. A specific U.S. industry's sales figures.
- D. The economy's rate of growth.

88. Economic theories can be used to do all of the following EXCEPT:

- A. Evaluate economic policy.
- B. Design economic policy.
- C. Explain consumer and market behavior.
- D. Determine exact economic outcomes.

89. Economic models:

- A. Focus on details about the economy.
- B. Focus on basic relationships.
- C. Cannot be constructed because of the complexity of the economy.
- D. Can be used to predict market behavior but not consumer behavior.

90. According to the Latin phrase *ceteris paribus*:

- A. Resources are limited.
- B. Things do not remain equal.
- C. There is no government intervention.
- D. Nothing else changes.

91. Ceteris paribus means:

- A. Leave the market alone.
- B. Noninterference by the government.
- C. Other things remaining equal.
- D. Things are always changing.

92. A HEADLINE article in the text asks parents, "Do you expect your children's generation to enjoy a higher standard of living than your generation?" What is necessary for the standard of living to rise?

- A. Economic growth.
- B. A greater allocation of resources to consumption.
- C. An inward shift in the production possibilities curve.
- D. A less equitable distribution of income.

93. A HEADLINE article in the text indicates that North Korea is running out of food. If North Korea is on its production possibilities curve and reduces its production of food so that it can increase the size of its military, this is most consistent with:

- A. Market failure.
- B. A movement along the production possibilities curve.
- C. An inward shift of the production possibilities curve.
- D. An expansion beyond the production possibilities curve.

94. A HEADLINE article in the text indicates that North Korea is expanding its missile programs, and at the same time it is running out of food. If North Korea is on its production possibilities curve and reduces food production so that it can increase the size of its military, this is an example of:
- A. Opportunity costs.
  - B. Laissez faire.
  - C. Externalities.
  - D. Ceteris paribus.
95. A HEADLINE article in the text indicates that North Korea is expanding its missile programs. Assume North Korea is currently on its production possibilities curve. If the increase in missile production results in a decrease in food production, this is an example of:
- A. Market failure.
  - B. An inward shift of the production possibilities curve.
  - C. Opportunity cost.
  - D. A reduction in available resources.
96. One HEADLINE article in the text suggests that 30 percent of Americans trust the federal government to do the right thing. If government intervention makes the economy worse off, this is referred to as:
- A. Scarce resources.
  - B. Central planning.
  - C. Market failure.
  - D. Government failure.



97. One HEADLINE article in the text suggests that most Americans do not trust the federal government to do the right thing. If they are correct, then government intervention results in:

- A. A decrease in opportunity costs.
- B. A less desirable mix of output.
- C. Market failure.
- D. Less unemployment.

98. In order to understand a particular graph, it is important to know:

- A. The total number of squares in the grid.
- B. Which variable is on the vertical axis and which is on the horizontal axis.
- C. Where a point on the graph is.
- D. Where the maximum quantity is.

99. The slope of a line is:

- A. The vertical distance between the two points, divided by the horizontal distance between the two points.
- B. Always positive.
- C. Sometimes referred to as "run over rise."
- D. The horizontal distance between the two points, divided by the vertical distance between the two points.

100. The slope of a curve is given by the formula:

- A. The percentage change in x coordinates between two points divided by the percentage change in y coordinates.
- B. The percentage change in y coordinates between two points divided by the percentage change in x coordinates.
- C. The change in x coordinates between two points divided by the change in y coordinates.
- D. The change in y coordinates between two points divided by the change in x coordinates.

101. When a curve shifts, this indicates that:

- A. One variable has increased and the other has decreased.
- B. A change has occurred in the underlying relationship between the two variables.
- C. The slope has changed.
- D. The two variables are now unrelated.

102. A linear curve can be distinguished by:

- A. The continuous change in its slope.
- B. The changing relationship between the two variables.
- C. The same slope throughout the curve.
- D. A shift in the curve.

103. If one variable increases when the other variable decreases, then the drawn curve is:

- A. Horizontal.
- B. Downward-sloping.
- C. Upward-sloping.
- D. Vertical.

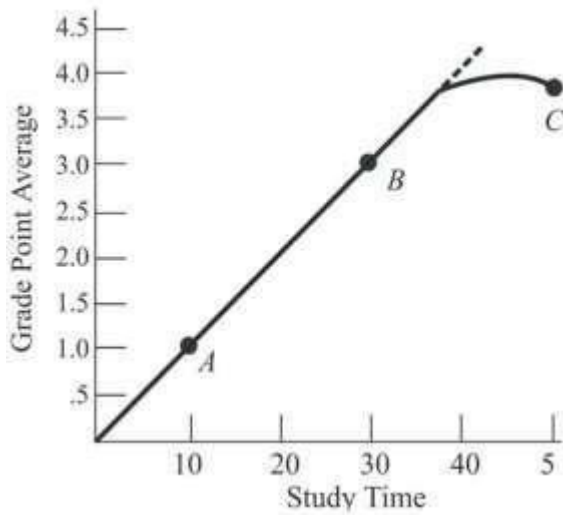
104. If one variable increases when the other variable increases, then the drawn curve is:

- A. Upward-sloping.
- B. Downward-sloping.
- C. Horizontal.
- D. Vertical.

105. A line that slopes upward from left to right has a:

- A. Negative slope.
- B. Positive slope.
- C. Slope that changes as you move along the curve.
- D. Slope of zero.

**Figure 1.2 - Relating grades and hours studied**



106. In Figure 1.2, a grade-point average of 3.0 is associated with how many hours of study time per week?

- A. 10.
- B. 20.
- C. 30.
- D. 40.

107. In Figure 1.2, a grade-point average of 1.0 is associated with how many hours of study time per week?

- A. 10.
- B. 20.
- C. 30.
- D. 40.

108. Figure 1.2 suggests that the relationship between the variables is:

- A. Linear at every point.
- B. Linear at places and nonlinear at places.
- C. Linear at places and nonlinear at places but always negatively sloped.
- D. Negative after 30 hours of study time.

109. Based on Figure 1.2, if a student wants to achieve a grade-point average of 3.0, he or she should study:

- A. An average of 40 hours per week.
- B. An average of 30 hours per week.
- C. An average of 20 hours per week.
- D. An average of 10 hours per week.

110. Based on Figure 1.2, if a student wants to achieve a grade-point average of 2.0, he or she should study:

- A. An average of 40 hours per week.
- B. An average of 30 hours per week.
- C. An average of 20 hours per week.
- D. An average of 10 hours per week.

111. Based on Figure 1.2, if a student studies 40 hours per week, he or she will:

- A. Earn a grade-point average between 3.5 and 4.0.
- B. Earn a grade-point average of exactly 3.0.
- C. Drop out of school because of the stress.
- D. Earn a lower grade-point average than if the study time is reduced to 30 hours per week.

112. Based on Figure 1.2, if a student studies 30 hours per week, he or she will:

- A. Earn a grade-point average of between 3.5 and 4.0.
- B. Earn a grade-point average of 3.0.
- C. Earn a grade-point average 2.0.
- D. Drop out of school because of the stress.

### **True / False Questions**

113. Economics is the study of how to allocate scarce resources among competing uses.

True False

114. When an economic choice is made, it is possible to avoid opportunity costs.

True False

115. The quantity of capital in an economy is unlimited since more can always be produced.

True False

116. Scarcity is not an issue in countries such as the United States since people live in nice homes and have plenty to eat.

True False

117. Every economy faces the situation of scarcity of resources.

True False

118. The United States is a prosperous nation because its resources are sufficient to meet the desires of its citizens.

True False

119. All economies must decide what to produce, how to produce it, and who gets the output.

True False

120. The factors of production include the land, labor, and money used to produce goods and services.

True False

121. Capital includes the machinery and buildings used to produce goods and services.

True False

122. When a society is operating on the production possibilities curve, it is using its available resources efficiently in the production of goods and services.

True False

123. More resources and better technology shift the production possibilities curve inward.

True False

124. To experience future economic growth, an economy must allocate some of its scarce resources to investment.

True False

125. The FOR WHOM to produce question focuses on the distribution of output across the members of society.

True False

126. The invisible hand refers to the price signal in a free market economy.

True False

127. Adam Smith was a proponent of the doctrine of laissez faire.

True False

128. The United States relies primarily on central planning to allocate resources.

True False

129. Karl Marx encouraged a policy of laissez faire because he believed that the market mechanism provided society with the best answers to the WHAT, HOW, and FOR WHOM questions.

True False



130. A "mixed economy" is one that relies solely on market signals to allocate goods and services.

True False

131. Pollution is an example of an externality.

True False

132. Government failure occurs when government intervention fails to improve economic outcomes.

True False

133. Because the economy is so complex, it is impossible to construct a theory about how it works.

True False

### **Essay Questions**

134. Explain opportunity cost. Give one example of an opportunity cost.

135. What are the factors of production? How do these factors play a role in an economy answering the three basic economic questions?

136. Define market mechanism and discuss Adam Smith's explanation of the "invisible hand."

## Chapter 01 The Challenge of Economics **Answer Key**

### Multiple Choice Questions

1. The central problem of economics is the:
  - A. Distribution of goods and services to those in need.
  - B. Scarcity of resources relative to human wants.
  - C. Inefficiency of government operations.
  - D. Unemployment of certain factors of production.

There are only a finite amount of resources.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 1 Easy*

*Learning Objective: 01-01 Explain the meaning of scarcity.*

*Topic: The Central Problem of Scarcity*

2. The primary concern of economics is the study of:
- A. Why human wants exist and what motivates them.
  - B. How to distribute goods and services according to human needs.
  - C. How best to allocate scarce resources among competing uses.
  - D. Who holds the most political power in a particular country.

There are not enough resources for everyone to have all that they desire.

*AACSB: Analytic*

*Blooms: Remember*

*Difficulty: 1 Easy*

*Learning Objective: 01-01 Explain the meaning of scarcity.*

*Topic: The Central Problem of Scarcity*

3. Which of the following explains why economic choices must be made?
- A. The factors of production are scarce.
  - B. The factors of production are expensive.
  - C. The factors of production are used inefficiently.
  - D. The factors of production are of inferior quality.

There is not an infinite amount of the factors of production.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-01 Explain the meaning of scarcity.*

*Topic: The Central Problem of Scarcity*

4. The study of economics focuses on:
- A. The behavior of successful businesses.
  - B. The role of money in our economy.
  - C. How best to allocate scarce resources.
  - D. The elimination of opportunity costs.

The goal of economic theory is to figure out how to use scarce resources in the best possible way.

*AACSB: Analytic  
Blooms: Remember  
Difficulty: 1 Easy*

*Learning Objective: 01-01 Explain the meaning of scarcity.  
Topic: The Central Problem of Scarcity*

5. Opportunity cost may be defined as the:
- A. The value of goods or services that are forgone in order to obtain something else.
  - B. Dollar price paid for a final good or service.
  - C. Dollar cost of producing a particular product.
  - D. Dollar cost of the next best alternative resources for producing a good.

The opportunity cost is the value of the next best alternative that is forgone.

*AACSB: Analytic  
Blooms: Remember  
Difficulty: 2 Medium*

*Learning Objective: 01-02 Define opportunity cost.  
Topic: The Central Problem of Scarcity*

6. Given that resources are scarce:

- A. A "free lunch" is possible, but only for a limited number of people.
- B. Poor countries must make choices, but rich countries do not have to make choices.
- C. Opportunity costs are experienced whenever choices are made.
- D. Some choices involve opportunity costs while other choices do not.

Resources required in the production of desired goods and services are limited so there is an opportunity cost for each production decision.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 2 Medium*

*Learning Objective: 01-02 Define opportunity cost.*

*Topic: The Central Problem of Scarcity*

7. The opportunity cost of playing tennis with your friend is:

- A. Negative since its good exercise.
- B. Zero since you already own the tennis racket and play on a public court.
- C. The next-best alternative use of your time that is forgone.
- D. The cost of the tennis lessons you took last year.

An opportunity cost is an opportunity lost.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 2 Medium*

*Learning Objective: 01-02 Define opportunity cost.*

*Topic: The Central Problem of Scarcity*

8. The concept of opportunity cost would become irrelevant if:

- A. The market mechanism functioned to allocate resources.
- B. The government allocated resources.
- C. The production possibilities curve bowed outward.
- D. Resources were no longer scarce.

If no resources were scarce, consumers would not have to make choices.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 2 Medium*

*Learning Objective: 01-02 Define opportunity cost.*

*Topic: The Central Problem of Scarcity*

9. If resources are limited:

- A. People will rush to buy more goods than they would otherwise.
- B. Businesses will sell more products than they would otherwise.
- C. Choices that involve tradeoffs must be made.
- D. All individuals are deprived of basic necessities.

Available resources always fall short of our desires.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 2 Medium*

*Learning Objective: 01-02 Define opportunity cost.*

*Topic: The Central Problem of Scarcity*

10. Which of the following is true about the factors of production?

- A. The factors of production as well as technology determine the physical limits to production.
- B. Rich countries have an unlimited quantity of factors.
- C. The factors include natural resources but not skilled labor.
- D. Some factors are scarce but other factors are not.

The more advanced our technological and managerial abilities, the more output we will be able to produce with available factors of production.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 1 Easy*

*Learning Objective: 01-01 Explain the meaning of scarcity.*

*Topic: The Central Problem of Scarcity*

11. If society lacks enough resources to satisfy all the desired uses of the resources, this is known as:

- A. Government failure.
- B. Laissez faire.
- C. Scarcity.
- D. Market failure.

All factors of production are finite.

*AACSB: Analytic*

*Blooms: Remember*

*Difficulty: 1 Easy*

*Learning Objective: 01-01 Explain the meaning of scarcity.*

*Topic: The Central Problem of Scarcity*



12. Scarcity means:

- A. Retail stores always run out of popular products.
- B. The desire for goods exceeds our capacity to produce them.
- C. Society will run out of the factors of production in the near future.
- D. A surplus of unsold goods in a specific market will not occur.

Given that resources are finite, consumers will not be able to have everything they desire.

*AACSB: Analytic  
Blooms: Remember  
Difficulty: 1 Easy*

*Learning Objective: 01-01 Explain the meaning of scarcity.  
Topic: The Central Problem of Scarcity*

13. Societies must address the question of WHAT to produce because:

- A. We can't produce all the goods and services we want.
- B. The amount of money in an economy is limited.
- C. We are wasteful and use resources inefficiently.
- D. Our economy experiences market failures.

With finite factors of production, society must decide what is best to produce for the majority of the population.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 1 Easy*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: Three Basic Economic Questions*

14. Which of the following is the best example of the "WHAT" economic question?
- A. Is the production process using an efficient amount of labor and capital machinery?
  - B. Who gets the goods once they are produced?
  - C. What is the most efficient method for producing goods?
  - D. What is the optimal mix of output?

Societies must decide how to use a combination of factors of production in order attempt to satisfy wants and needs. Society must decide WHAT to produce to satisfy those wants and needs.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 2 Medium*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

15. Which of the following is NOT a factor of production?
- A. A toll-bridge across a lake.
  - B. The money hidden in an old basement.
  - C. A wrecking ball used to tear down old buildings.
  - D. The CEO of a large corporation.

In economics, capital is referred to as the goods that are used to make goods. Money is not a factor of production.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 2 Medium*

*Learning Objective: 01-03 Recite society's three core economic questions.*

16. In economics, capital refers to:

- A. Money.
- B. Savings put aside for future investment.
- C. Goods that can be used to produce other goods.
- D. The value of a corporation's assets.

Capital would include items such as machinery, buildings, and networks.

Money is not economic capital.

*AACSB: Analytic*

*Blooms: Remember*

*Difficulty: 2 Medium*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

17. In economics, which of the following is the best example of capital?

- A. Money held in a checking account.
- B. A computer used by a lawyer to prepare legal documents.
- C. Investment in training for employees in an accounting firm.
- D. The executive producer of a new adventure movie.

Capital refers to goods that are used to produce other goods. In this example, the computer is the good used to produce the document which is the other good.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 2 Medium*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

18. Which of the following is NOT an example of land, or a natural resource?

- A. Coal.
- B. A river.
- C. Natural gas.
- D. A homebuilder.

A homebuilder would be an example of a labor resource.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 2 Medium*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

19. Which of the following is an example of labor as a factor of production?

- A. People who bring together the skills necessary for creating products and services.
- B. The skills and abilities of workers.
- C. People who are paid an hourly wage but not those paid a salary.
- D. A college or university that educates people.

Labor is the number and skills of workers.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 2 Medium*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

20. Entrepreneurship refers to:

- A. Natural resources, such as land and water.
- B. Computer technology.
- C. Skilled labor.
- D. Ability to see market opportunities and the will to take risk.

Entrepreneurship is skill in creating products, services, and processes.

*AACSB: Analytic  
Blooms: Remember  
Difficulty: 1 Easy*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: Three Basic Economic Questions*

21. In economics, which of the following represents entrepreneurship?

- A. Natural resources.
- B. Skill in creating products and services.
- C. The skills of workers.
- D. Machinery, buildings and networks.

Entrepreneurship is defined as the skill in creating products, services, and processes.

*AACSB: Reflective Thinking  
Blooms: Analyze  
Difficulty: 2 Medium*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: Three Basic Economic Questions*

22. Output choices are necessary within a market because of:

- A. Inefficient use of resources.
- B. High prices for goods.
- C. Scarcity of resources.
- D. Limited technology.

With limited factors of production and technology output would have a finite limit.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 2 Medium  
Learning Objective: 01-01 Explain the meaning of scarcity.  
Topic: Three Basic Economic Questions*

23. When economists talk about a trade-off between "guns and butter," they mean:

- A. Society can produce more military goods without giving up any consumer goods.
- B. Military goods are an inefficient use of resources.
- C. The production of more military goods may require fewer consumer goods.
- D. Consumer goods are always more costly than military goods.

In this case guns represent military spending while butter represents consumer goods.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 2 Medium  
Learning Objective: 01-02 Define opportunity cost.  
Topic: Three Basic Economic Questions*

**Table 1.1 - Production possibilities and opportunity costs of missiles and houses**

Table 1.1 shows the tradeoff between different combinations of missile production and home construction, *ceteris paribus*. Complete the table by calculating the required opportunity costs for both missiles and houses. Then answer the indicated question(s).

Combination	Number of houses	Opportunity cost of houses in terms of missiles	Number of missiles	Opportunity cost of missiles in terms of houses
J	0		4	
K	10,000		3	
L	17,000		2	
M	21,000		1	
N	23,000		0	

24. In Table 1.1, what is the opportunity cost of increasing the production of missiles from 2 to 3 in terms of houses?
- A. 1,000 houses.
  - B. 3,333 houses.
  - C. 7,000 houses.
  - D. 17,000 houses.

Seventeen thousand houses are built when two missiles are built. Ten thousand houses are built when three missiles are built. Over this range of production seven thousand houses are sacrificed to that an additional missile can be produced.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 2 Medium*

*Learning Objective: 01-02 Define opportunity cost.*

*Topic: Three Basic Economic Questions*

25. In Table 1.1, the opportunity cost of increasing the production of houses from 17,000 to 21,000 in terms of missiles per house is:
- A. 0.00014 of a missile.
  - B. 0.00025 of a missile.
  - C. 2.00 missiles.
  - D. 4.00 missiles.

The difference in the production of 17,000 houses to 21,000 houses is 4,000. The difference between the number of missiles produced is one. Therefore the opportunity cost of increasing the production of houses from 17,000 to 21,000 in terms of missiles per house is .00025.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 2 Medium*

*Learning Objective: 01-02 Define opportunity cost.*

*Topic: Three Basic Economic Questions*

26. In Table 1.1, the lowest opportunity cost of houses in terms of missiles is:
- A. 0.00010 of a missile per house.
  - B. 0.00050 of a missile per house.
  - C. 7.00 missiles per house.
  - D. 10.00 missiles per house.

When 10,000 houses are built the cost is 1 missile. Therefore, the house share is .00010 of the cost of 1 missile.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*



*Learning Objective: 01-02 Define opportunity cost.  
Topic: Three Basic Economic Questions*

27. In Table 1.1, the highest opportunity cost of missiles in terms of houses is:
- A. 500 houses per missile.
  - B. 4,000 houses per missile.
  - C. 7,000 houses per missile.
  - D. 10,000 houses per missile.

The creation of 1 missile creates the highest cost at 10,000 houses. This is the opportunity cost of producing the fourth missile given an economy is already producing three.

*AACSB: Reflective Thinking  
Blooms: Analyze  
Difficulty: 3 Hard*

*Learning Objective: 01-02 Define opportunity cost.  
Topic: Three Basic Economic Questions*

28. Which of the following statements about production possibilities is true?
- A. Production possibilities are limited for all countries because resources are scarce.
  - B. The production of food does not involve opportunity costs since people must eat.
  - C. Production possibilities will expand if the level of inefficiency is reduced.
  - D. Production possibilities are only limited for a country if prices are too high.

No country has an infinite amount of resources.

*AACSB: Reflective Thinking  
Blooms: Analyze  
Difficulty: 2 Medium*

*Learning Objective: 01-01 Explain the meaning of scarcity.*

29. Which of the following is NOT an assumption under which the production possibilities curve is drawn?
- A. The economy's resources are fully employed.
  - B. The price level is stable.
  - C. Technology is being held constant.
  - D. The supplies of factors of production are fixed.
  - E. The trade-off of one good for another is always constant.

The production possibilities curve represents the alternative combinations of goods and services that could be produced in a given time period with all available resources and technology. Price is not a factor.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 2 Medium  
Learning Objective: 01-02 Define opportunity cost.  
Topic: Three Basic Economic Questions*

30. All points on the production possibilities curve:

- A. Represent the use of all available resources.
- B. Are equally desirable.
- C. Represent the same mix of output.
- D. Represent the same opportunity costs.

A production possibilities curve describes the various combination of final goods or services that could be produced in a given time period with available resources and technology.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-01 Explain the meaning of scarcity.*

*Topic: Three Basic Economic Questions*

31. Ceteris paribus, if North Korea increases the size of its military, then:

- A. Its production possibilities curve will shift outward.
- B. Its production possibilities curve will shift inward.
- C. Its production of consumer goods will increase.
- D. Its production of consumer goods will decrease.

Because of limited resources the increase in military production will decrease the production of consumer goods.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 2 Medium*

*Learning Objective: 01-02 Define opportunity cost.*

*Topic: Three Basic Economic Questions*

32. Assuming the level of resources and technology are constant, if France decreases the size of its military, then:
- A. Its' production possibilities curve will shift outward.
  - B. Its' production possibilities curve will shift inward.
  - C. Its' production of consumer goods can increase.
  - D. Its' production of consumer goods must decrease.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

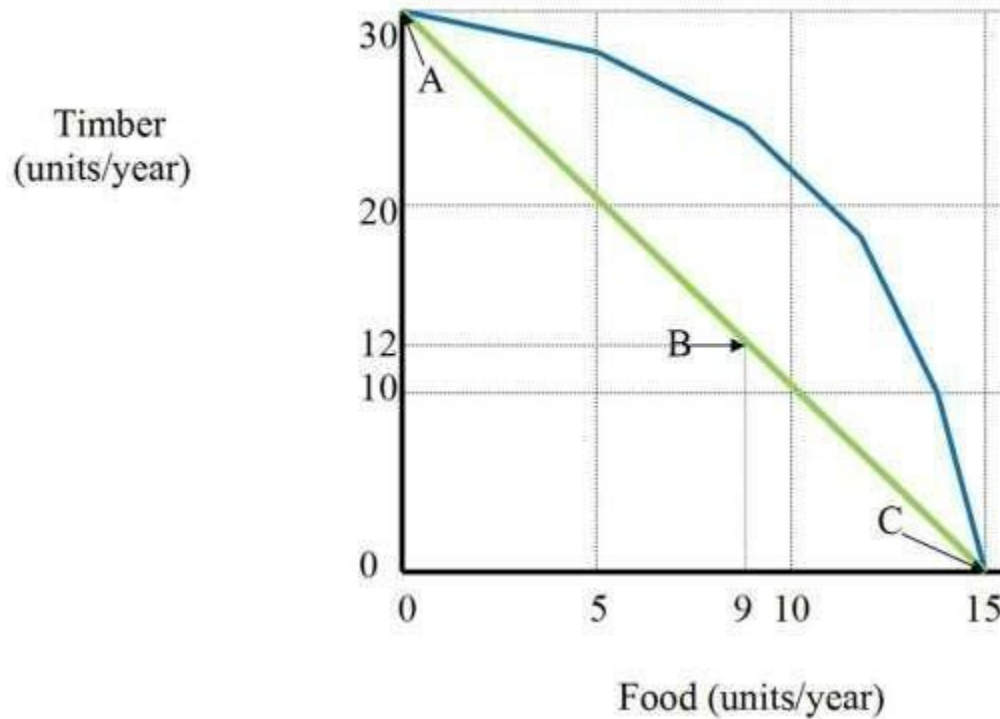
*Difficulty: 2 Medium*

*Learning Objective: 01-02 Define opportunity cost.*

*Topic: Three Basic Economic Questions*

**Figure 1.1 - Production Possibilities and Opportunity Costs: Linear Model versus Non-Linear Model**

**Production Possibilities: Refining the Model**



In the linear production possibilities model, we assume each of five equally-sized parcels of land contributes the same to the production of food and timber: 6 units of timber or 3 units of food.

By contrast, in the non-linear model, we will assume that there are five different types of land in equal-sized plots and that each plot may contribute as follows to the production of

		<u>FOOD</u> or <u>TIMBER</u> :	
A.	Great farmland/Terrible timberland	+5	+2
B.	Good farmland/Poor timberland	+4	+4
C.	Moderate farmland/Moderate timberland	+3	+6
D.	Poor farmland/Good timberland	+2	+8
E.	Terrible farmland/Great timberland	+1	+10

33. Assuming all parcels of land are the same, when all land is in use, one more unit of timber produced will require...
- A. Two more units of food produced
  - B. Five fewer units of food produced
  - C. One-half fewer units of food produced
  - D. Two fewer units of food produced

*AACSB: Analytic*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-02 Define opportunity cost.*

*Topic: The Central Problem of Scarcity and Appendix: Using Graphs*

34. Assuming all parcels of land are the same, there is a constant trade-off in the production of timber and food. When all land is in use, one more unit of food produced will require...
- A. Two more units of timber produced
  - B. Five fewer units of timber produced
  - C. One-half fewer units of timber produced
  - D. Two fewer units of timber produced

*AACSB: Analytic*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-02 Define opportunity cost.*

*Topic: The Central Problem of Scarcity and Appendix: Using Graphs*

35. Assuming all land is equally productive in either use, how much output of each type will be produced with  $\frac{2}{5}$  of the land in timber production and  $\frac{3}{5}$  of the land in food production?
- A. 12 units of timber and 9 units of food
  - B. 9 units of timber and 12 units of food
  - C. 18 units of timber and 9 units of food
  - D. 9 units of timber and 18 units of food

*AACSB: Analytic*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-02 Define opportunity cost.*

*Topic: The Central Problem of Scarcity and Appendix: Using Graphs*

36. Now assume that there are five different types of land in equally-sized parcels:

- A. Great farmland/Terrible timberland
- B. Good farmland/Poor timberland
- C. Moderate farmland/Moderate timberland
- D. Poor farmland/Good timberland
- E. Terrible farmland/Great timberland

Starting from point A on the production possibilities line where 30 units of timber and no food is produced, suppose that we choose to produce more food by moving one parcel of land out of timber production and into food production. In order to minimize the opportunity cost of producing more food, the first plot to be re-purposed should be...

- A. A.
- B. B.
- C. C.
- D. D.
- E. E.

*AACSB: Analytic*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-02 Define opportunity cost.*

*Topic: The Central Problem of Scarcity and Appendix: Using Graphs*



37. In the model where we assume that all parcels of land are the same, the relationship between food and timber produced when all land is in use is:

- A. Linear and inverse.
- B. Direct and linear.
- C. Inverse and nonlinear.
- D. Direct and nonlinear.

*AACSB: Analytic*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-02 Define opportunity cost.*

*Topic: The Central Problem of Scarcity and Appendix: Using Graphs*

38. In the model where we assume that all five parcels of land are NOT the same, the relationship between food and timber produced when all land is in use is:

- A. Linear and inverse.
- B. Direct and linear.
- C. Inverse and nonlinear.
- D. Direct and nonlinear.

*AACSB: Analytic*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-02 Define opportunity cost.*

*Topic: The Central Problem of Scarcity and Appendix: Using Graphs*

39. The most desirable attainable mix of output for society:
- A. Consists of the entire production possibilities curve.
  - B. Consists of a point on the production possibilities curve.
  - C. Consists of a point outside the production possibilities curve.
  - D. Occurs at the origin of the x- and y-axes on which the production possibilities curve is graphed.

There is no single point on the production possibilities curve that is right for all nations at all times.

*AACSB: Analytic  
Blooms: Remember  
Difficulty: 1 Easy*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: Three Basic Economic Questions*

40. In attempting to answer the WHAT question, a society seeks to:
- A. Produce the optimal mix of output.
  - B. Exploit its workers in order to produce more output.
  - C. Produce more military goods so that the citizens will be safe.
  - D. Distribute an equal amount of goods to all citizens.

Locating and producing the optimal mix of output is the essence of the WHAT challenge.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 2 Medium*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: Three Basic Economic Questions*

41. Investment refers to all of the following except:

- A. An increase in business inventories.
- B. The purchase of new equipment by a business.
- C. The construction of new factories by a company.
- D. The purchase of stock by an individual.

Economic investments enhance the ability to produce.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

42. Which of the following is NOT an example of investment?

- A. A hair salon buys additional hair dryers.
- B. The campus bookstore buys new T-shirts with the college logo.
- C. A business owner uses his profits to play the lottery and wins.
- D. Toyota expands the size of its factories located in the United States.

Lottery is a game of chance is not an investment.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

43. Economic growth always takes the form of
- A. An expansion of production possibilities.
  - B. A change in how goods are distributed.
  - C. A movement along the production possibilities curve.
  - D. Higher prices.

Economic growth expands the possibilities to produce more.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 2 Medium*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

44. Economic growth is represented by:
- A. An inward shift of the production possibilities curve.
  - B. A point inside the production possibilities curve.
  - C. An outward shift of the production possibilities curve.
  - D. A movement along the production possibilities curve.

Production possibilities increase and shift outward with growth in resources and technology.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

45. The production possibilities curve shifts outward in response to:
- A. A decline in technology or more resources or both.
  - B. A decline in technology or fewer resources or both.
  - C. Improved technology or more resources or both.
  - D. Improved technology or fewer resources or both.

Outward shifts occur with growth. Growth is due to improved technologies which use fewer resources and/or an increase in resources.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 2 Medium*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: Three Basic Economic Questions*

46. Ceteris paribus which of the following is likely to cause an outward shift of the production possibilities curve?
- A. Investment in telecommunications networks.
  - B. The deportation of illegal immigrants.
  - C. An increase in the unemployment rate.
  - D. A tax increase on factors of production.

Investment in new technologies is necessary to economic growth.

*AACSB: Reflective Thinking  
Blooms: Analyze  
Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: Three Basic Economic Questions*

47. Ceteris paribus when technological change allows a smaller amount of a resource to be used in producing any combination of two goods, there will be:

- A. A movement along the production possibilities curve.
- B. An outward shift of the production possibilities curve.
- C. An inward shift of the production possibilities curve.
- D. No change in the production possibilities curve.

Change in technology allows for resources to be used more efficiently.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

48. Ceteris paribus, which of the following is least likely to contribute to economic growth?

- A. A greater quantity of labor.
- B. A greater quantity of capital.
- C. An increase in prices.
- D. Improved production technology.

Price is not a factor in growth.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

49. Ceteris paribus, which of the following will most likely cause an inward shift of the production possibilities curve?

- A. A decrease in the size of the labor force.
- B. An increase in population.
- C. An increase in knowledge.
- D. An improvement in technology.

Labor is a factor of production. If there is a reduction of labor production possibilities decrease.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

50. Ceteris paribus which of the following events would most likely cause the production possibilities curve to shift inward?

- A. The labor supply grows.
- B. New factories are built.
- C. A technological breakthrough occurs that makes production of all goods more efficient.
- D. A major earthquake destroys several industrial centers.

In this scenario, loss of industrial centers creates a reduction in capital which would cause production to decrease.

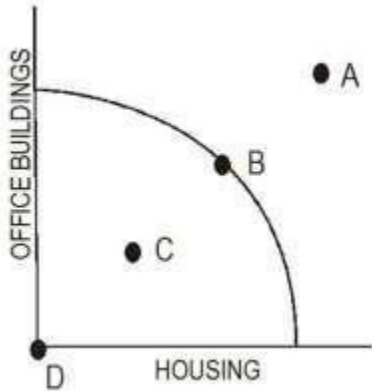
*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.*

**Figure 1.1 - Production-possibilities curve**



51. Society is employing some of the available technology but not all of it. Select the appropriate point. (See Figure 1.1)

- A. A
- B. B
- C. C
- D. D

When all resources are not used to their fullest capacity, production falls below the curve.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*



52. Society is producing some output, but some of the available resources are unemployed. Select the appropriate point. (See Figure 1.1)

- A. A
- B. B
- C. C
- D. D

Point C falls below the production possibilities curve, which indicates some resources are not being used to the fullest potential.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

53. Society is producing the maximum potential output, given its existing resources and technology. Select the appropriate point. (See Figure 1.1)

- A. A
- B. B
- C. C
- D. D

Point B represents the point on the possibilities curve that best represents the optimal use of resources.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: Three Basic Economic Questions*

54. Society might be able to produce this combination if new resources were discovered but cannot produce it with current resources. Select the appropriate point. (See Figure 1.1)

- A. A
- B. B
- C. C
- D. D

If new resources are discovered the production possibilities curve shifts to the right.

*AACSB: Reflective Thinking  
Blooms: Analyze  
Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: Three Basic Economic Questions*

55. It is not possible for society to produce this combination with current resources and technology. Select the appropriate point. (See Figure 1.1)

- A. A
- B. B
- C. C
- D. D

There are not sufficient resources to produce at this level.

*AACSB: Reflective Thinking  
Blooms: Analyze  
Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: Three Basic Economic Questions*

56. Society is not producing either good because of extreme inefficiencies. Select the appropriate point. (See Figure 1.1)
- A. A
  - B. B
  - C. C
  - D. D

At point D there is no production of either houses or office buildings.

*AACSB: Reflective Thinking  
Blooms: Analyze  
Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: Three Basic Economic Questions*

57. When society searches for the optimal method of producing goods and services, it is responding to the:
- A. "WHAT" question.
  - B. "HOW" question.
  - C. "FOR WHOM" question.
  - D. "WHY" question.

The best possible answer to the HOW question will entail both efficiency in the use of factors of production and adequate safeguards for the environment and other social concerns.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

58. When society struggles with how to divide up the "economic pie," it is responding to the:

- A. "FOR WHOM" question.
- B. "HOW" question.
- C. "WHAT" question.
- D. "WHY" question.

Everyone wants a slice of the "economic pie" that would best fit their needs.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

59. Welfare programs are designed to address the:

- A. "HOW" question.
- B. "FOR WHOM" question.
- C. Issue of scarce resources.
- D. "WHAT" question.

The optimal distribution of income must satisfy our sense of fairness and as well as our desire for more output.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

60. Which of the following best describes the way resources are allocated in the U.S. economy?
- A. By rules.
  - B. By markets.
  - C. By regulations.
  - D. By government.

The use of market prices and sales to signal desired outputs.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-04 Discuss how market and command economies differ.*

*Topic: The Mechanisms of Choice*

61. The market mechanism:
- A. Works through central planning by the government.
  - B. Eliminates market failures created by the government.
  - C. Uses prices as a means of communication between consumers and producers.
  - D. Is very inefficient since consumers cannot communicate directly with producers.

The market mechanism signals producers what products are demanded.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-04 Discuss how market and command economies differ.*

62. The market mechanism:

- A. Is an inefficient means of communicating consumer wants to producers.
- B. Relies on government control and planning.
- C. Eliminates the market failures caused by government.
- D. Relies on prices and sales to communicate consumer wants to producers.

Prices and sales indicate to producers what they should continue to produce.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-04 Discuss how market and command economies differ.*

*Topic: The Mechanisms of Choice*

63. The essential signal of the market mechanism is:

- A. Income.
- B. Price.
- C. Property.
- D. Government directive.

Price and sales send signals to producers about what mix of output consumers want.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-04 Discuss how market and command economies differ.*

*Topic: The Mechanisms of Choice*

64. The price of a good or service:

- A. Never has an impact on the market mechanism.
- B. Serves as the essential signal of the market mechanism.
- C. Sometimes plays a role in the market mechanism.
- D. Rarely has an impact on the market mechanism.

Price and sales send signals to producers about what mix of output consumers want.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 2 Medium*

*Learning Objective: 01-04 Discuss how market and command economies differ.*

*Topic: The Mechanisms of Choice*

65. Which of the following best describes the "invisible hand?"

- A. Price signals drive the market mechanism.
- B. Government regulations influence the allocation of society's scarce resources.
- C. The Internal Revenue Service enforces the nation's tax laws.
- D. Lobbyists influence which laws are passed by Congress.

No direct communication between consumer and producer is required to signal what the market desires.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-04 Discuss how market and command economies differ.*

*Topic: The Mechanisms of Choice*

66. The essential feature of the market mechanism is:

- A. That every consumer is concerned about the welfare of others.
- B. The price signal for both consumers and producers.
- C. Equity in the distribution of income and housing.
- D. Government taxation of profits.

Price is a determining factor for consumers to buy and producers to sell.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 2 Medium*

*Learning Objective: 01-04 Discuss how market and command economies differ.  
Topic: The Mechanisms of Choice*

67. Laissez faire refers to:

- A. The belief that government can make better choices than the market about the mix of output.
- B. The economic theory of Karl Marx.
- C. A belief of nonintervention by government in the market mechanism.
- D. A preference for central planning.

Laissez faire means hands off which invites the government to stay out of the market decisions.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 2 Medium*

*Learning Objective: 01-04 Discuss how market and command economies differ.  
Topic: The Mechanisms of Choice*



68. Which of the following is most consistent with a market economy?

- A. Shortages.
- B. Central planners.
- C. Government directives.
- D. Laissez faire.

Laissez faire means hands off which invites the government to stay out of the market decisions.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 1 Easy*

*Learning Objective: 01-04 Discuss how market and command economies differ.  
Topic: The Mechanisms of Choice*

69. Which of the following individuals is typically associated with a laissez faire economic policy?

- A. Adam Smith.
- B. Karl Marx.
- C. The Chairman of the Federal Reserve.
- D. John Maynard Keynes.

Adam Smith argued that nations would prosper with less government interference.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 1 Easy*

*Learning Objective: 01-04 Discuss how market and command economies differ.  
Topic: The Mechanisms of Choice*

70. Which of the following statements is consistent with central planning?

- A. The economy relies heavily on the market mechanism to allocate resources.
- B. Government planners play the dominant role in deciding how resources are allocated.
- C. Economic decisions are made by large competitive firms.
- D. Market prices are used to guide production and consumption activities.

The government, not the market, assumes responsibility for deciding what goods are to be produced.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-04 Discuss how market and command economies differ.*

*Topic: The Mechanisms of Choice*

71. Karl Marx wrote:

- A. Das Kapital, which was used as the rationale for centrally-planned economies.
- B. Das Kapital, which described the virtues of market-based economies.
- C. The Wealth of Nations, which provided the rationale for centrally-planned economies.
- D. The Wealth of Nations, which described the virtues of market-based economies.

Karl Marx proposed central planning.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-04 Discuss how market and command economies differ.*

*Topic: The Mechanisms of Choice*

72. Central planning is the principal method for making economic decisions in:

- A. The United States.
- B. Singapore.
- C. New Zealand.
- D. North Korea.

Central planning is still the principal mechanism of choice in some countries that still tend to be communist.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 3 Hard*

*Learning Objective: 01-04 Discuss how market and command economies differ.  
Topic: The Mechanisms of Choice*

73. The economy of the United States is best characterized as:

- A. Centrally planned.
- B. A laissez faire model.
- C. A mixed economy.
- D. A democratic socialist economy.

The U.S. uses a mix of market mechanism and government directives to make economic choices.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 2 Medium*

*Learning Objective: 01-04 Discuss how market and command economies differ.  
Topic: The Mechanisms of Choice*

74. Which of the following is NOT a reason why the U.S. government intervenes in the economy?

- A. To ensure the safety of products.
- B. To reduce pollution.
- C. To make a profit for the government.
- D. To improve the mix of output.

The government is not a business and does not seek profits.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 2 Medium*

*Learning Objective: 01-05 Describe the nature of market and government failure.*

*Topic: Undesirable Choices*

75. If the market mechanism causes the economy to arrive at the wrong mix of output, there is:

- A. Market failure.
- B. Mixed economy failure.
- C. Government failure.
- D. Laissez faire.

The market may not always pick the best possible mix of output.

*AACSB: Analytic  
Blooms: Remember  
Difficulty: 1 Easy*

*Learning Objective: 01-05 Describe the nature of market and government failure.*

*Topic: Undesirable Choices*

76. Market failure means:

- A. Government solutions fail to improve economic outcomes.
- B. The market mechanism does not produce the best mix of output.
- C. The market allocates goods more efficiently than does the government.
- D. The market is responsive to consumer demand.

The market did not produce the best possible mix of outputs.

*AACSB: Analytic  
Blooms: Remember  
Difficulty: 1 Easy*

*Learning Objective: 01-05 Describe the nature of market and government failure.  
Topic: Undesirable Choices*

77. An externality is:

- A. A cost or benefit of a market activity that impacts a third party.
- B. The private costs that are borne by an individual.
- C. The cost of clean up paid for by the polluter.
- D. A situation in which the government solution makes the outcome worse.

An externality is a cost imposed on innocent third parties.

*AACSB: Analytic  
Blooms: Remember  
Difficulty: 1 Easy*

*Learning Objective: 01-05 Describe the nature of market and government failure.  
Topic: Undesirable Choices*

78. Which of the following is an example of a negative externality?

- A. A decrease in available educational options due to government intervention.
- B. An increase in government bureaucracy and red tape.
- C. An increase in the incidence of cancer due to pollution.
- D. An introduction to a pollution decreasing technology.

The cancer was a result of pollution and borne by a third party.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 2 Medium*

*Learning Objective: 01-05 Describe the nature of market and government failure.  
Topic: Undesirable Choices*

79. Pollution is an example of:

- A. Inefficiency by the polluting firm.
- B. Market failure.
- C. Government transfers.
- D. Economic instability.

When the market mechanism selects the wrong choice of HOW to produce, this will cause a market failure.

*AACSB: Reflective Thinking  
Blooms: Analyze  
Difficulty: 3 Hard*

*Learning Objective: 01-05 Describe the nature of market and government failure.  
Topic: Undesirable Choices*

80. If government intervention fails to improve economic outcomes, the result is known as:

- A. Government failure.
- B. Market failure.
- C. Mixed economy failure.
- D. Laissez faire.

The government may not necessarily offer better answers to the three basic questions.

*AACSB: Analytic  
Blooms: Remember  
Difficulty: 1 Easy*

*Learning Objective: 01-05 Describe the nature of market and government failure.  
Topic: Undesirable Choices*

81. Government intervention designed to address market failure:

- A. May either improve or worsen the mix of output produced.
- B. Will definitely worsen the mix of output produced.
- C. Will definitely improve the mix of output produced.
- D. Never has an impact on the mix of output produced.

Government intervention might not just worsen the mix of output but even reduce the total amount of output.

*AACSB: Reflective Thinking  
Blooms: Analyze  
Difficulty: 3 Hard*

*Learning Objective: 01-05 Describe the nature of market and government failure.  
Topic: Undesirable Choices*

82. Which of the following is an example of government failure?

- A. A negative externality, such as pollution.
- B. An increase in bureaucracy and red tape that fails to improve economic outcomes.
- C. An increase in airline safety.
- D. An increase in the costs of production and an improvement in economic outcomes.

An increase in bureaucratic red tape may burden private industry and reduce the total amount of output.

*AACSB: Analytic*

*Blooms: Remember*

*Difficulty: 2 Medium*

*Learning Objective: 01-05 Describe the nature of market and government failure.*

*Topic: Undesirable Choices*

83. Which of the following groups of words best represents macroeconomic goals?

- A. Full employment, price stability, economic growth.
- B. Rate of production, choice of factors of production, and the pricing of specific goods.
- C. Welfare of individual consumers and business firms.
- D. Land, labor, and capital.

Macroeconomics focuses on the behavior of an entire economy—the big picture.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: What Economics is All About*



84. Macroeconomics focuses on:

- A. Government failure.
- B. The behavior of individuals, firms, and government agencies.
- C. Land, labor, and capital.
- D. The economy as a whole.

The essential concern of macroeconomics is to understand and improve the performance of the economy as a whole.

*AACSB: Analytic  
Blooms: Remember  
Difficulty: 1 Easy*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: What Economics is All About*

85. Microeconomics focuses on:

- A. Full employment, price stability, and economic growth.
- B. The behavior of individuals, firms, and government agencies.
- C. Land, labor, and capital.
- D. Centrally planned economies.

Microeconomics focuses on individuals, firms, and government agencies.

*AACSB: Analytic  
Blooms: Remember  
Difficulty: 1 Easy*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: What Economics is All About*

86. Which of the following is associated with microeconomics?

- A. An increase in sales for a chain of pet supply stores.
- B. A decrease in the unemployment rate for the nation.
- C. An increase in the inflation rate for the entire economy.
- D. A decrease in the level of economic growth for the country.

One focus of microeconomics is on individual firms.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: What Economics is All About*

87. Which of the following is associated with microeconomics?

- A. An economy's overall output level.
- B. The country's unemployment rate.
- C. A specific U.S. industry's sales figures.
- D. The economy's rate of growth.

One focus of microeconomics is on individual firms.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: What Economics is All About*

88. Economic theories can be used to do all of the following EXCEPT:

- A. Evaluate economic policy.
- B. Design economic policy.
- C. Explain consumer and market behavior.
- D. Determine exact economic outcomes.

There are too many factors that contribute to economic theory; exact economic outcomes cannot be determined.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: What Economics is All About*

89. Economic models:

- A. Focus on details about the economy.
- B. Focus on basic relationships.
- C. Cannot be constructed because of the complexity of the economy.
- D. Can be used to predict market behavior but not consumer behavior.

Models are used like maps to show basic relationships.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 2 Medium*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: What Economics is All About*

90. According to the Latin phrase *ceteris paribus*:

- A. Resources are limited.
- B. Things do not remain equal.
- C. There is no government intervention.
- D. Nothing else changes.

The assertion is that all things remain equal except for one.

*AACSB: Analytic  
Blooms: Remember  
Difficulty: 1 Easy*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: What Economics is All About*

91. *Ceteris paribus* means:

- A. Leave the market alone.
- B. Noninterference by the government.
- C. Other things remaining equal.
- D. Things are always changing.

Only one circumstance will change in a model, all other circumstances' will remain constant.

*AACSB: Analytic  
Blooms: Remember  
Difficulty: 1 Easy*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: What Economics is All About*

92. A HEADLINE article in the text asks parents, "Do you expect your children's generation to enjoy a higher standard of living than your generation?" What is necessary for the standard of living to rise?

- A. Economic growth.
- B. A greater allocation of resources to consumption.
- C. An inward shift in the production possibilities curve.
- D. A less equitable distribution of income.

Economic growth is essential for future generations to continue to enjoy a higher standard of living than the past generation.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: What Economics is All About*

93. A HEADLINE article in the text indicates that North Korea is running out of food. If North Korea is on its production possibilities curve and reduces its production of food so that it can increase the size of its military, this is most consistent with:

- A. Market failure.
- B. A movement along the production possibilities curve.
- C. An inward shift of the production possibilities curve.
- D. An expansion beyond the production possibilities curve.

With a reduction in food production there are more resources to produce military goods. This leads to a movement along the production possibilities curve.

*AACSB: Reflective Thinking*

*Blooms: Analyze*  
*Difficulty: 3 Hard*  
*Learning Objective: 01-02 Define opportunity cost.*  
*Topic: What Economics is All About*

94. A HEADLINE article in the text indicates that North Korea is expanding its missile programs, and at the same time it is running out of food. If North Korea is on its production possibilities curve and reduces food production so that it can increase the size of its military, this is an example of:
- A. Opportunity costs.
  - B. Laissez faire.
  - C. Externalities.
  - D. Ceteris paribus.

Resources used for the military aren't available for producing food. This is an opportunity cost to the production of missiles.

*AACSB: Reflective Thinking*  
*Blooms: Analyze*  
*Difficulty: 3 Hard*  
*Learning Objective: 01-02 Define opportunity cost.*  
*Topic: What Economics is All About*

95. A HEADLINE article in the text indicates that North Korea is expanding its missile programs. Assume North Korea is currently on its production possibilities curve. If the increase in missile production results in a decrease in food production, this is an example of:

- A. Market failure.
- B. An inward shift of the production possibilities curve.
- C. Opportunity cost.
- D. A reduction in available resources.

Resources used for the military aren't available for producing food. This is an opportunity cost to the production of missiles in terms of food.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-02 Define opportunity cost.*

*Topic: What Economics is All About*

96. One HEADLINE article in the text suggests that 30 percent of Americans trust the federal government to do the right thing. If government intervention makes the economy worse off, this is referred to as:

- A. Scarce resources.
- B. Central planning.
- C. Market failure.
- D. Government failure.

Government intervention may fail to improve market outcomes.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-05 Describe the nature of market and government failure.*

*Topic: What Economics is All About*

97. One HEADLINE article in the text suggests that most Americans do not trust the federal government to do the right thing. If they are correct, then government intervention results in:

- A. A decrease in opportunity costs.
- B. A less desirable mix of output.
- C. Market failure.
- D. Less unemployment.

A government failure may result in a less desirable mix of output.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-05 Describe the nature of market and government failure.*

*Topic: What Economics is All About*

98. In order to understand a particular graph, it is important to know:

- A. The total number of squares in the grid.
- B. Which variable is on the vertical axis and which is on the horizontal axis.
- C. Where a point on the graph is.
- D. Where the maximum quantity is.

The horizontal and vertical axis identifies the variables.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*



99. The slope of a line is:
- A. The vertical distance between the two points, divided by the horizontal distance between the two points.
  - B. Always positive.
  - C. Sometimes referred to as "run over rise."
  - D. The horizontal distance between the two points, divided by the vertical distance between the two points.

Divide the vertical distance between the two points, by the horizontal distance between the two points.

*AACSB: Reflective Thinking  
Blooms: Analyze  
Difficulty: 3 Hard  
Topic: Appendix: Using Graphs*

100. The slope of a curve is given by the formula:
- A. The percentage change in x coordinates between two points divided by the percentage change in y coordinates.
  - B. The percentage change in y coordinates between two points divided by the percentage change in x coordinates.
  - C. The change in x coordinates between two points divided by the change in y coordinates.
  - D. The change in y coordinates between two points divided by the change in x coordinates.

Slope equals the rise divided by the run.



*Blooms: Understand*  
*Difficulty: 3 Hard*  
*Topic: Appendix: Using Graphs*

101. When a curve shifts, this indicates that:

- A. One variable has increased and the other has decreased.
- B. A change has occurred in the underlying relationship between the two variables.
- C. The slope has changed.
- D. The two variables are now unrelated.

Shifts are reflective of changes in the underlying relationships between the two variables.

*AACSB: Reflective Thinking*  
*Blooms: Analyze*  
*Difficulty: 3 Hard*  
*Topic: Appendix: Using Graphs*

102. A linear curve can be distinguished by:

- A. The continuous change in its slope.
- B. The changing relationship between the two variables.
- C. The same slope throughout the curve.
- D. A shift in the curve.

A distinguishing feature of linear curves is that they have the same slope throughout.

*AACSB: Analytic*  
*Blooms: Understand*  
*Difficulty: 3 Hard*  
*Topic: Appendix: Using Graphs*



103. If one variable increases when the other variable decreases, then the drawn curve is:

- A. Horizontal.
- B. Downward-sloping.
- C. Upward-sloping.
- D. Vertical.

The A negative relationship among the variables produces a negatively sloped curve.

*AACSB: Reflective Thinking*  
*Blooms: Analyze*  
*Difficulty: 3 Hard*  
*Topic: Appendix: Using Graphs*

104. If one variable increases when the other variable increases, then the drawn curve is:

- A. Upward-sloping.
- B. Downward-sloping.
- C. Horizontal.
- D. Vertical.

Variables of both axes are moving upward to the right.

*AACSB: Reflective Thinking*  
*Blooms: Analyze*  
*Difficulty: 3 Hard*  
*Topic: Appendix: Using Graphs*

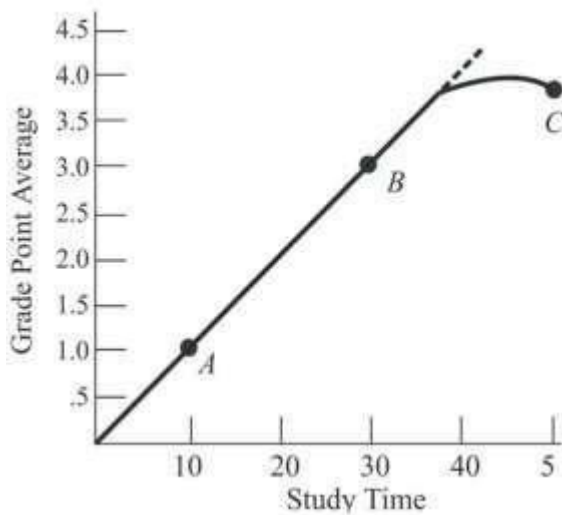
105. A line that slopes upward from left to right has a:

- A. Negative slope.
- B. Positive slope.
- C. Slope that changes as you move along the curve.
- D. Slope of zero.

All variables are increasing in this case.

*AACSB: Reflective Thinking*  
*Blooms: Analyze*  
*Difficulty: 3 Hard*  
*Topic: Appendix: Using Graphs*

**Figure 1.2 - Relating grades and hours studied**



106. In Figure 1.2, a grade-point average of 3.0 is associated with how many hours of study time per week?

- A. 10.
- B. 20.
- C. 30.**
- D. 40.

A grade of 3.0 intersects with 30 hours of study time.

*AACSB: Reflective Thinking*  
*Blooms: Apply*  
*Difficulty: 2 Medium*  
*Topic: Appendix: Using Graphs*

107. In Figure 1.2, a grade-point average of 1.0 is associated with how many hours of study time per week?

- A. 10.**
- B. 20.
- C. 30.
- D. 40.

A grade of 1.0 intersects with 10 hours of study time.

*AACSB: Reflective Thinking*  
*Blooms: Apply*  
*Difficulty: 2 Medium*  
*Topic: Appendix: Using Graphs*

108. Figure 1.2 suggests that the relationship between the variables is:

- A. Linear at every point.
- B. Linear at places and nonlinear at places.
- C. Linear at places and nonlinear at places but always negatively sloped.
- D. Negative after 30 hours of study time.

The line is straight until approximately 4.0 then moves downward.

*AACSB: Reflective Thinking*  
*Blooms: Apply*  
*Difficulty: 3 Hard*  
*Topic: Appendix: Using Graphs*

109. Based on Figure 1.2, if a student wants to achieve a grade-point average of 3.0, he or she should study:

- A. An average of 40 hours per week.
- B. An average of 30 hours per week.
- C. An average of 20 hours per week.
- D. An average of 10 hours per week.

A grade of 3.0 intersects with 30 hours.

*AACSB: Reflective Thinking*  
*Blooms: Apply*  
*Difficulty: 2 Medium*  
*Topic: Appendix: Using Graphs*



110. Based on Figure 1.2, if a student wants to achieve a grade-point average of 2.0, he or she should study:

- A. An average of 40 hours per week.
- B. An average of 30 hours per week.
- C. An average of 20 hours per week.
- D. An average of 10 hours per week.

A grade of 2.0 intersects with 20 hours.

*AACSB: Reflective Thinking*  
*Blooms: Apply*  
*Difficulty: 2 Medium*  
*Topic: Appendix: Using Graphs*

111. Based on Figure 1.2, if a student studies 40 hours per week, he or she will:

- A. Earn a grade-point average between 3.5 and 4.0.
- B. Earn a grade-point average of exactly 3.0.
- C. Drop out of school because of the stress.
- D. Earn a lower grade-point average than if the study time is reduced to 30 hours per week.

A point between 3.5 and 4.0 intersects with 40 hours.

*AACSB: Reflective Thinking*  
*Blooms: Apply*  
*Difficulty: 2 Medium*  
*Topic: Appendix: Using Graphs*

112. Based on Figure 1.2, if a student studies 30 hours per week, he or she will:

- A. Earn a grade-point average of between 3.5 and 4.0.
- B. Earn a grade-point average of 3.0.
- C. Earn a grade-point average 2.0.
- D. Drop out of school because of the stress.

The intersection of 3.0 and 30 hours earns a grade of 3.0.

*AACSB: Reflective Thinking*  
*Blooms: Apply*  
*Difficulty: 2 Medium*  
*Topic: Appendix: Using Graphs*

### **True / False Questions**

113. Economics is the study of how to allocate scarce resources among competing uses.

**TRUE**

Economics is the study of how to allocate scarce resources among various uses.

*AACSB: Analytic*  
*Blooms: Remember*  
*Difficulty: 1 Easy*  
*Learning Objective: 01-01 Explain the meaning of scarcity.*  
*Topic: The Central Problem of Scarcity*

114. When an economic choice is made, it is possible to avoid opportunity costs.

**FALSE**

The opportunity cost of a good is the sacrifice of the next-best alternative goods that are forgone.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 1 Easy*

*Learning Objective: 01-02 Define opportunity cost.*

*Topic: The Central Problem of Scarcity*

115. The quantity of capital in an economy is unlimited since more can always be produced.

**FALSE**

All factors of production are finite.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-01 Explain the meaning of scarcity.*

*Topic: The Central Problem of Scarcity*

116. Scarcity is not an issue in countries such as the United States since people live in nice homes and have plenty to eat.

**FALSE**

The resources of the U.S. are not sufficient to meet the desires of all its citizens.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-01 Explain the meaning of scarcity.*

*Topic: The Central Problem of Scarcity*

117. Every economy faces the situation of scarcity of resources.

**TRUE**

No economy can escape scarcity.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-01 Explain the meaning of scarcity.*

*Topic: The Central Problem of Scarcity*

118. The United States is a prosperous nation because its resources are sufficient to meet the desires of its citizens.

**FALSE**

Not all desires of every citizen are met.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-01 Explain the meaning of scarcity.*

*Topic: The Central Problem of Scarcity*

119. All economies must decide what to produce, how to produce it, and who gets the output.

**TRUE**

The three basic economic questions are WHAT, FOR WHOM, and HOW.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

120. The factors of production include the land, labor, and money used to produce goods and services.

**FALSE**

The factors of production include land, labor and capital.

*AACSB: Analytic*

*Blooms: Remember*

*Difficulty: 1 Easy*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

121. Capital includes the machinery and buildings used to produce goods and services.

**TRUE**

Capital is the good used to produce other goods.

*AACSB: Analytic*

*Blooms: Remember*

*Difficulty: 1 Easy*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: Three Basic Economic Questions*

122. When a society is operating on the production possibilities curve, it is using its available resources efficiently in the production of goods and services.

**TRUE**

All resources are being used efficiently.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 1 Easy*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: Three Basic Economic Questions*

123. More resources and better technology shift the production possibilities curve inward.

**FALSE**

Economic growth will expand the production possibilities outward, allowing more production thus shifting the production possibilities curve to the right.

*AACSB: Analytic  
Blooms: Understand  
Difficulty: 2 Medium*

*Learning Objective: 01-03 Recite society's three core economic questions.  
Topic: Three Basic Economic Questions*

124. To experience future economic growth, an economy must allocate some of its scarce resources to investment.

**TRUE**

Investment is necessary for growth.

*AACSB: Reflective Thinking*

*Blooms: Analyze*

*Difficulty: 2 Medium*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

125. The FOR WHOM to produce question focuses on the distribution of output across the members of society.

**TRUE**

FOR WHOM question address issues of distribution and who will get what share of goods and services.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

126. The invisible hand refers to the price signal in a free market economy.

**TRUE**

No direct communication is needed between the producer and the consumer.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-04 Discuss how market and command economies differ.*

*Topic: The Mechanisms of Choice*

127. Adam Smith was a proponent of the doctrine of laissez faire.

**TRUE**

Adam Smith preferred little or no government intervention.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-04 Discuss how market and command economies differ.*

*Topic: The Mechanisms of Choice*

128. The United States relies primarily on central planning to allocate resources.

**FALSE**

Because the U.S. uses a combination of government directives and market mechanisms to determine economic outcomes, the United States is a mixed economy.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-04 Discuss how market and command economies differ.*

*Topic: The Mechanisms of Choice*



129. Karl Marx encouraged a policy of laissez faire because he believed that the market mechanism provided society with the best answers to the WHAT, HOW, and FOR WHOM questions.

**FALSE**

Karl Marx believed central planning was necessary to keep workers from being exploited.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-04 Discuss how market and command economies differ.*

*Topic: The Mechanisms of Choice*

130. A "mixed economy" is one that relies solely on market signals to allocate goods and services.

**FALSE**

A mixed economy relies on both market signals and government directives to allocate goods and services.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 2 Medium*

*Learning Objective: 01-04 Discuss how market and command economies differ.*

*Topic: The Mechanisms of Choice*

131. Pollution is an example of an externality.

**TRUE**

An externality places the burden on an innocent third party.

*Blooms: Remember*

*Difficulty: 1 Easy*

*Learning Objective: 01-05 Describe the nature of market and government failure.*

*Topic: Undesirable Choices*

132. Government failure occurs when government intervention fails to improve economic outcomes.

**TRUE**

Government intervention does not always result in a positive outcome.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 1 Easy*

*Learning Objective: 01-05 Describe the nature of market and government failure.*

*Topic: Undesirable Choices*

133. Because the economy is so complex, it is impossible to construct a theory about how it works.

**FALSE**

The focus of economics is on basic relationships, ignoring unnecessary details. Therefore, theories, or models of economic behavior are possible to formulate.

*AACSB: Analytic*

*Blooms: Understand*

*Difficulty: 1 Easy*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: What Economics is All About*

## **Essay Questions**

134. Explain opportunity cost. Give one example of an opportunity cost.

An opportunity cost is the value of the second best choice. Example: A student stays home to study for an exam instead of going to a movie with friends. (Answers may vary)

*AACSB: Analytic*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-02 Define opportunity cost.*

*Topic: The Central Problem of Scarcity*

135. What are the factors of production? How do these factors play a role in an economy answering the three basic economic questions?

The factors of production are Land, Labor, Capital, and Entrepreneurship. Each factor of production plays a role in answering the WHAT, HOW, and FOR WHOM questions by distributing scarce resources in the best possible way. (Answers may vary)

*AACSB: Analytic*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-03 Recite society's three core economic questions.*

*Topic: Three Basic Economic Questions*

136. Define market mechanism and discuss Adam Smith's explanation of the "invisible hand."

The market mechanism is central in reshuffling resources and outputs. Market sales and prices send a signal to producers about what mix of output consumers want. Without direct communication between consumers and producers the "invisible hand" communicates sales and prices.

*AACSB: Analytic*

*Blooms: Analyze*

*Difficulty: 3 Hard*

*Learning Objective: 01-04 Discuss how market and command economies differ.*

*Topic: The Mechanisms of Choice*