

February 25, 2007

## Study Questions For Introduction to Economics

### Questions for Chapter 1

1. Define the following terms (each is a separate question): economics, the market economy, negative externality, common law, damage complaint, damage payment, equality under the law, contract law, right of first possession, indirect exchange, barter society, money economy, medium of exchange, capital accounting, free enterprise, pure market economy, public good.
2. Tell the three conditions of the market economy under which economists assume people act.
3. Tell the two characteristics of the private property system.
4. Give two examples of a non-ownable good or resource.
5. Give an example of a non-appropriable good or resource.
6. Tell the meaning of the statement “Susan owns and controls the trees on a small island that is inside of Mountain Lake.” Answer by referring to her legal rights and the legal rights of others. (Hint: there is no definitive answer to the question. You must use your imagination)
7. Describe the causal relationship between (1) a private property system and (2) specialization. (Which causes which and how? You should mention exchange in your answer.)
8. Give an example of an action that causes a harmful effect that is different from the text.
9. Give an example of an action that causes the harmful externality. Then tell two different individuals who could own the legal right to control the performance of the action.
10. Give an example in which individuals exchange the legal right to control an action that causes a harmful externality.
11. Give a brief description of how the common law evolved.
12. Give an example of a judgment made by a common law judge in a dispute resolution case that is different from the text. Show how the judgment takes account of future generations.
13. Define equality under the law and tell its opposite.

14. Put yourself in the shoes of a common law judge. Suppose that A claims that B has injured him by taking gold that was on land that he discovered. B responds that the land on which the gold was located is unowned and that he is entitled to it. And investigation reveals A had indeed been the first discoverer of the gold and also that the land is unowned. Would you allow B to keep the gold? Explain.
15. Consider the legal right of first possession. Suppose that you are in a position to decide who has this legal right. Tell two criteria you could use to decide this. In answering this question, you should begin with an example if a particular good or resource. In other words. Choose a good or resource and tell two ways that someone could determine who should have the legal right of first possession.
16. Who possesses the legal right to a good or resource that is produced through teamwork? Explain.
17. Consider a bicycle that you now own. Under common law, who has the *right of first possession*? In your answer be sure to tell what the right of first possession is.
18. What can a government do to promote free enterprise?
19. Does free enterprise imply that two people can make any kind of contract they want? Explain.
20. Tell the reasoning behind the statement that free enterprise implies competition.
21. Does free enterprise means that everyone can earn money? Explain.
22. It is evident that free enterprise is good from the standpoint of consumers of goods. Why then do people often oppose it?
23. Tell the difference between a barter society and a money economy from the standpoint of someone who wants a good that is produced by someone else.
24. What are the three functions of money?
25. What is the opposite of indirect exchange?
26. Is money wanted for its value in use? Explain.
27. Explain how money helps in capital accounting. You can use the example of a resource owner, a consumer, worker, or saver. Your example must show that you understand the meaning of capital accounting.
28. Identify and describe the four fundamental roles in a market economy.
29. Tell the types of income in a market economy and who earns the different types.

30. Give four reasons why private property rights can never be complete in real market economies.
31. Define a common property resource and give an example.
32. Give an example of a public good and show that it has the two characteristics that a public good must have.
33. Distinguish between government intervention and cultural intervention in a market economy.
34. According to the text, why should one study economics?

## Study Questions for Chapter 2

1. Define the following terms (each is a separate question): (a) want, (b) time preference, (c) good, (d) "free good," (e) marginal unit, (f) inframarginal unit, (g) marginal characteristic, (h) durable good, (i) perishable good, (j) deterioration, (k) obsolescence, (l) depreciation, (m) appreciation, (n) complementary goods, (o) substitute goods, (p) joint want, and (q) cost. (Examples are ordinarily not sufficient, although they may be used to clarify a definition.)
2. Tell the difference between a *want* and a *need*.
3. Does a person have a choice of whether to satisfy a need? Explain.
4. Tell the two requirements for a thing to be a good.
5. By using an example that is different from the one in the text, identify a generalized want that can be satisfied by different specific goods.
6. Give an example of a person's wants that change over time.
7. Give an example of a person with high time preference and one with low time preference. Explain why your examples are appropriate.
8. "Wants are always relative." Explain what an economist means by this statement.
9. Think of something (besides the example in the text) that you believe you would never sell or that you would not want to sell. By using this thing as an example, show that you understand the argument that your want for it is relative. You may either agree or disagree with the argument but you must show that you understand it.
10. Describe a preference structure.
11. Consider a shopper who makes only one shopping trip for food per month. At present, all of his cupboards are bare. He has no food. Nor does he plan to buy any more food later in the month, after he makes his one trip to the supermarket. Finally, assume that he buys only for himself and only to satisfy his own wants. While he is shopping he buys ten pounds of lamb chops at \$2.00 per pound and five pounds of cheese at \$1.50 per pound. Does his choice express that he wants lamb more than he wants cheese? Explain in some detail.
12. Redo problem #7 but make the price of cheese (a) \$2.00 per pound, (b) \$3.00 per pound, (c) \$4.00 per pound, and (d) \$5.00 per pound.
13. Why do diamonds have a higher price than water, even though water as a whole gives greater satisfaction than diamonds?
14. When a person chooses to buy a good, he compares its price with the money value of his

satisfaction. In some cases he pays attention to the marginal unit. In other cases, he pays attention to the marginal characteristic. In what circumstance does he pay attention to the marginal characteristic instead of the marginal unit?

15. Give an example of a good, other than a house, which you may choose on the basis of marginal characteristics of a good instead of marginal units. Explain why your example is a good one.
16. Is tobacco a durable good?
17. Give an example of a durable good that is re-usable. Also give an example of one that is not re-usable.
18. Tell the difference between the deterioration of a good and the obsolescence of a good.
19. Give an example of a good that has depreciated due to its obsolescence.
20. Give an example of a good that satisfies joint wants. Be sure to give one that is different from those in the text. Explain why your example is a good one.
21. When an economist gives an example of a good, her example is hypothetical. Explain why.
22. What is the purpose of using the word "opportunity" to refer to cost in economics?
23. Briefly tell the cost, in economic terms, of playing a video game at a local arcade.  
(Alternative question: tell the cost, in economic terms, of attending a performance of traditional dances for which you must buy a ticket.)

### Study Questions for Chapter 3

1. Define the following terms (each is a separate question): (a) labor, (b) land, (c) capital goods, (d) human capital, (e) specialized resource, (f) non-specific resource, (g) complementary character of a human capital, (h) transformation character of a human capital, (h) structure of technical knowledge, (i) producing entrepreneur (j) profit, (k) revenue to a producing entrepreneur, (l) costs to a producing entrepreneur. Examples are ordinarily not sufficient, although they may be used to clarify a definition.
2. Classify the following resources into one of four broad types. Explain if necessary. (a) a hammer, (b) knowledge of welding, (c) a recently-seeded front lawn, (d) an oasis in a secluded desert, (e) the energy used in digging a ditch, (f) a wild rabbit, (g) an apple tree growing in an orchard. If you are in doubt about which category to use, explain your choice.
3. How are human capital and capital goods similar? How are they different?
4. Tell the difference between a specialized resource and a non-specific resource. Give examples of each.
5. Tell the two necessary conditions for a thing or action to be classified as a resource.
6. Give seven examples of types of human capital in a market interaction.
7. Describe and give examples of four classes of human capital to the solitary actor.
8. Give an example of the complementary character of human capital that differs from that given in the text.
9. Human capital has a transformation character. It can transform... Fill in the blank with two different types of transformation human capital and give an example of each.
10. Using an example other than that in the text, describe at least three orders of technical knowledge, explaining which is first-order, which is second-order, and which is third-order knowledge.
11. Explain why the term "structure" of knowledge of different resources is preferred to the term "orders."
12. What is the difference between the structure of technical knowledge to the solitary actor and the structure of production?
13. Give an example of two-person barter. Show that the satisfaction of one person's wants depends on both his own human capital and the human capital of his trading partner. Make sure that you identify several types of human capital. Do not use the same example that was used in the textbook.

14. Give an example of two-person barter. Show that trading and specializing economize on the acquisition and use of human capital. Make sure that you identify more than one type of human capital. Do not use the same example that was used in the textbook.
15. Give an example of two-person barter. Show that trading and specializing enable each person to benefit from human capital even if they do not know that the human capital exists. Make sure that you identify more than one type of human capital. Do not use the same example that was used in the textbook.
16. The text states the principle that in market interaction no one's plan to gain from specializing could be realized unless numerous others possessed and used their own specialized human capital. Give an example that shows (a) the realization of A's plan to gain from specializing and (b) the specialized human capital possessed by others that enables A's plan to be realized.
17. The text states the principle that trading and specializing in market interaction expand the opportunities to benefit from production by giving people incentives to produce new human capital that would otherwise not exist. (a) Give a specific example of a person who possesses such an incentive. (b) Explain how opportunities expand as a result.
18. Distinguish risk bearing from uncertainty bearing.
19. Using examples, tell the difference between the penniless entrepreneur and the capitalist entrepreneur.
20. Tell the difference between the producing entrepreneur and the non-entrepreneur.

## Questions for Chapter 4

1. Define the following terms (each is a separate question): (a) specialization (b) marginal cost, (c) absolute advantage, (d) comparative advantage, (e) terms of trade in exchange, (f) terms of trade in international trade theory, (g) intellectual property rights, (h) patent system, (i) copyright system.
2. According to what Smith taught, what causes a nation to have large “amounts” of human capital.
3. Smith wrote that under the conditions of a market economy, individuals have incentives to cause a “division of labor. Tell the difference between a division of labor by an employer and a division of labor in small business and the trades.
4. A commentator once said that Adam Smith believed that the division of labor in market interaction is the result of *natural differences* among people. According to the text, was the commentator correct? Explain.
5. Tell Adam Smith's explanation of the “wealth of nations.” In other words, what causes a nation to become wealthy, according to Smith.
6. Specialization, according to the principle of lowest opportunity cost, ordinarily requires an exchange of legal rights. By using an example that is different from the text, tell the kind of legal rights that must be exchanged for such specialization to occur.
7. Tell the principle of lowest opportunity cost.
8. What does it mean to say that an item is *scarce*?
9. In a two-person situation, suppose that A can produce a particular good in less time than B. Does this necessarily mean that A can produce the good at a lower cost? Explain.
10. If there is no initial right to a resource that is regarded as valuable to more than one person, individuals have an incentive to create the right. Describe the incentive. In other words tell how people can gain by creating the right. Illustrate by an example.
11. Explain why begrudging and other discrimination based on reasons other than productivity is costly to the person who begrudges or discriminates.
12. Give an example that is different from the one in the text in which the exchange of rights would lead to shared specialization. Be sure that your example includes all of the necessary conditions.
13. Be able to do a problem similar to that in table 4-3. (This is the table that shows two stage

production.)

14. In a two-person, two-good model, assume that A can produce 1 kilo of rice in 2 hours and 1 kilo of fish in 3 hours. B can produce a kilo of rice in 8 hours and a kilo of fish in 10 hours.
  - a. Which has an absolute advantage in producing rice?
  - b. Which has an absolute advantage in producing fish?
  - c. Which has a comparative advantage in producing rice?
  - d. Which has a comparative advantage in producing fish?
  - e. What is the opportunity cost of producing rice to A?
  - f. What is the opportunity cost of producing rice to B?
15. In the last problem, show that there are potential gains from trade.
16. Be able to do other problems that are similar to these last four.
17. In a two-person, two-good model, assume that A can produce 1 kilo of rice in 4 hours and 1 kilo of fish in 5 hours. B can produce a kilo of rice in 3 hours and a kilo of fish in 2 hours.
  - a. Which has an absolute advantage in producing rice?
  - b. Which has an absolute advantage in producing fish?
  - c. Which has a comparative advantage in producing rice?
  - d. Which has a comparative advantage in producing fish?
  - e. What is the opportunity cost of producing rice to A?
  - f. What is the opportunity cost of producing rice to B?
18. In the last problem, show that there are potential gains from trade.
19. Describe David Ricardo's theory of international trade, according to the text.
20. In a two-person trade, can a person lose from trade? Explain.
21. Tell how Smith's idea that specialization *is produced* helps to expand David Ricardo's theory of international trade, as described in the text.
22. Assume a two-person, two-good world in which there is, at first, no comparative advantage and, therefore, no incentive to exchange. Each person has the same skills and wants. Starting with this situation, give an example that is different from text in which one of the people improves his ability to produce one of the goods. Can this lead to a future exchange between the two? Explain.
23. If a person in market interaction specializes, does everyone gain? Explain.
24. Tell the reasoning behind Adam Smith's observation that the diversity of human capital is limited by the extent of the market.
25. Describe the benefits of a patent system.

26. Give an example of harm caused by specialization.

27. Give an example of harm caused by invention.

## Study Questions for Chapter 5

1. Define economic growth, gross domestic product, real GDP, real GDP per capita, Smith's invisible hand theorem, natural resource curse, law of diminishing returns, Malthus's principle of population, subsistence theory of wages, over-production crises, Marx's alienation thesis, innovation, copying.
2. "Capitalism promotes selfishness instead of altruism. Therefore private property rights should be restricted and business should be regulated in the public interest." How would Adam Smith have reacted to this statement?
3. Explain how selfish behavior in the economy can promote the general interest.
4. Give an example of the invisible hand theorem that is different from the text.
5. What policies should the government follow to promote free enterprise?
6. Tell Smith's theory of economic growth.
7. In his theory of international trade, did Smith believe that a country should try to restrict imports? Explain.
8. Tell three ways that the poor gain from interaction under the conditions of free enterprise.
9. "In a market economy, poverty is typically only a temporary state..." Explain, according to the textbook, the reasoning behind this statement.
10. Adam Smith argued that people who get rich in market interaction must, in the process, provide benefits for others. Does this mean that he also believed that the distribution of wealth which existed during his time was fair? Explain.
11. Are the citizens of a nation that is large with abundant resources assured of being wealthier than smaller nations with non-abundant resources. Explain by referring to Adam Smith's view.
12. According to Adam Smith, why did port cities develop faster and grow bigger than the hinterland.
13. Is there a causal relationship between low transportation costs and the diversity of human capital?
14. Thomas Malthus believed that the wages of the working classes were destined to remain at bare subsistence, no matter how much an economy grew. What reason (s) did Malthus give for this belief.

15. Tell the checks on population growth that Thomas Malthus mentioned in his principle of population. Include both negative and positive checks.
16. According to the critics of Thomas Malthus, what was the main shortcoming of his subsistence theory of working class wages?
17. Malthus's principle of population applies to some societies in today's world. Explain.
18. Tell the events that would lead to a revolution by the working class, according to Karl Marx.
19. Explain why workers might become alienated from their jobs in a capitalist society, according to Marx.
20. How did later socialist writers mentioned in the text differ from Karl Marx on the issue of what would cause a revolution.
21. Why would workers *not* revolt, according to Karl Marx's critics.
22. According to Karl Marx's critics, why is alienation not a serious problem in market interaction?
23. According to Carl Menger, what causes progress (i.e., economic growth)?
24. Can a country *without* abundant natural resources (land) experience a high rate of economic growth? Explain.
25. How have people overcome the limitation on economic growth due to the absence of natural waterways?
26. Briefly state Frank Knight's theory of economic growth. (In your answer, you should mention the private property system and the actions that the private property system give people incentives to perform.)
27. Both a lender to a business and a financial investor in a business contribute to economic growth. Tell how these roles are the same and how they are different. In your answer, say something about the nature of the judgments they make.
28. Tell the difference between a *financial* investment and a *real* investment.
29. Real investments can yield new human capital in two ways, according to Knight. Identify these.
30. Using the textbook as your guide, describe the modern view of economic growth based on

the assumptions (1) that people try to avoid decreases in their standards of living and (2) that people compete in their roles as entrepreneurs. In your answer be sure that you explain how each assumption is important. A simple list is insufficient.

31. How does competition in market interaction cause a fall in someone's standard living? In your answer, distinguish between a fall in the standards of living in the economy as a whole and a fall in the standard of living of one person who lives in an economy.

## Questions for Chapter Six

1. Define communication by means of markets and prices, firm, industry, coordination along a supply chain, demand, demand curve, marginal consumer, dis-coordination in distribution, monopoly, monopolist, collusive monopoly, price taker, price maker, marginal revenue, price elasticity of demand, price elastic, price inelastic, monopoly price.
2. Tell the difference between hierarchical coordination and market coordination.
3. Why does coordination imply a judgment about the net benefits of specialization and exchange?
4. What is the meaning of the assumption of diminishing marginal utility?
5. Why does a demand curve have a negative slope? (It is not sufficient to tell the meaning of a negative slope.)
6. Why does the marginal cost of producing a good increase as more is produced?
7. Draw a demand line and compare quantity that would be demanded at a relatively high price with one that would be demanded at a relatively low price.
8. Give an example, and show on a graph, a market that is dis-coordinated because too many resources are being used to produce a good. Show the amount of the good that is being produced and the marginal cost and marginal utility that are associated with that quantity. Is marginal cost greater than, less than, or equal to marginal utility?
9. Give an example and show on a graph a market that is dis-coordinated because too few resources are being used to produce a good. Show the amount of the good that is being produced and the marginal cost and marginal utility that are associated with that quantity. Is marginal cost greater than, less than, or equal to marginal utility?
10. How much of a good is produced in a completely coordinated market? Illustrate your answer with a graph.
11. Suppose that you are an entrepreneur in a market that is dis-coordinated because too few resources are being used. What should you do?
12. Suppose that you are an entrepreneur in a market that is dis-coordinated because too many resources are being used. What should you do?
13. Economists sometimes say that too many resources are used to produce some good. Tell what they mean by this.
14. Identify the three types of technological advance.

15. Use the concept of a completely coordinated economy as a basis for telling who gains and who loses from a technological advance.
16. It is obvious that entrepreneurs make errors. Why, then, do economists build models in which entrepreneurs do not make errors?
17. Identify three ways that a person can achieve a monopoly position in a pure market economy?
18. Be able to do a problem like the following: Assume that a monopolist is charging a price of \$100 and that he raises price to \$120. Quantity demanded falls from 1000 units to 500 units. By reducing price, was he able to increase his revenue? Calculate approximately the price elasticity of demand in this case. Is demand price elastic or price inelastic? (You should use the formula on page 13 to calculate price elasticity of demand.)
19. If you are presented on the examination with a graph like figure 6-10, you should be able to calculate the price elasticity of demand, to tell whether an increase or decrease in price would increase or decrease revenue, and to tell whether demand is price elastic or price inelastic. (You should use the formula on page 13 to calculate price elasticity of demand.)
20. Explain the dis-coordination caused by a monopolist who charges a monopoly price.
21. Charging a monopoly price for a good is sometimes called *wasteful*. Explain the wastefulness of monopoly pricing. First do this for a monopolist who is *not* a producer. Then do it for a monopolist who is a producer.
22. To be a monopoly producer in a pure market economy, a person must own a monopoly over a resource. Explain why a person who does not have a monopoly over a resource could not be a monopoly producer.
23. Draw a graph showing the price that a monopolist who has no costs of production would charge and the quantity he would sell if he wanted to maximize profit. Show on the graph the marginal revenue at the quantity that maximizes his profit.
24. Assume that the monopolist faces increasing marginal cost. Draw a graph showing the price that a producing monopolist would charge and the quantity he would sell if he wanted to maximize profit. Show on the graph the quantity produced, the size of his marginal cost, the size of his marginal revenue and the price that he charges if he maximizes profit.

## Questions for Chapter Seven

1. Define market conditions, shortage, price controls, price ceiling, price floor,.
2. Draw a graph that shows an increase in demand for peanuts. Be sure to label the graph correctly.
3. Demonstrate on a graph that an increase in demand represents an increase in the quantity demanded at each price. (It is sufficient to use two prices). Be sure to label the graph correctly.
4. Demonstrate on a graph that an increase in demand represents an increase in price that the marginal consumer is willing to pay for each quantity. (It is sufficient to use two quantities). Be sure to label the graph correctly.
5. Draw a graph of a decrease in demand for peanuts. Be sure to label the graph correctly.
6. Show the effects on a graph of an increase in the demand for peanuts on the completely coordinated market price and quantity. Be sure to label the graph correctly.
7. If the price of peanuts rise because of an increase in demand, who is responsible for the higher prices. Explain by referring to a graph. Be sure to label the graph correctly.
8. Show the effects on a graph of a decrease in the demand for peanuts. Be sure to label the graph correctly.
9. Draw a graph that shows an increase in the marginal cost of producing peanuts. Be sure to label the graph correctly.
10. Draw a graph that shows how an increase in the marginal cost of supplying peanuts effects the completely coordinated market price and quantity.
11. Suppose that there is a price ceiling on oranges that equals the current price. Explain by referring to a graph the effects of an increase in demand for oranges under these conditions.
12. Suppose that there is a price floor on rice that equals the current price. Explain by referring to a graph the effects of an decrease in demand for rice under these conditions.
13. Give an example of dis-coordination caused by a price control.

## Questions for Chapter Eight

1. Define supply chain for a resource, downstream industry, upstream industry, appraisal, futures contract, commodities exchange, futures market, commodities broker, to hedge.
2. Chocolate is made from cocoa. Assume that Chokoluck is a U.S. chocolate manufacturing company. It imports cocoa from an exporter in Brazil, who buys it from a Brazilian cocoa plantation. Chokoluck uses the cocoa to make chocolate bars. The chocolate bars are sold to a candy distributor who, in turn, sells them in convenience stores. Identify a business that is *upstream* from Chokoluck. Identify a business that is *downstream* from Chokoluck.
3. Using the example in question 2, tell how an unexpectedly good growing season for cocoa would be communicated along the supply chain.
4. Using the example in question 2, tell how an unexpected fall in the consumer demand for chocolate bars would be communicated along the supply chain for cocoa.
5. Suppose that there is a particularly bad growing season for grapes in California. Consumers of grape juice would be harmed by this. Tell how the entrepreneurial communication leads to adjustments that lessen the impact on consumers of grape juice. Hint: use the example of the wheat farmer as a guide.
6. Referring to question 4, assume that apple juice is a substitute for grape juice. Tell how adjustments in the apple industry could lessen the impact on consumers from a particularly bad growing season for grapes.
7. How does a person in market interaction decide which kind of human capital to produce?
8. Tell how the service of inventory maintenance aids coordination.
9. Using the example of chocolate bars, tell how inventory maintenance by convenience stores would benefit consumers of those bars if there was a sudden, unexpected increase in demand.
10. Using the example of chocolate bars, tell how inventory maintenance by companies that distribute chocolate bars to convenience stores would benefit consumers of those bars if there was a sudden, unexpected increase in demand.
11. Choose any industry and tell how inventory maintenance benefits consumers in the event of a disaster, such as a massive hurricane.
12. “Decisions of each person in market interaction help others to coordinate. Explain why this is true by referring to (1) consumers and (2) employees.
13. “Practically all exchanges are speculative.” Explain.

14. "Inventory maintenance is inherently speculative." Explain.
15. Pure speculation in land should be deterred. Present an argument to support this conclusion. In building your example, be sure to define *pure speculation*.
16. How can pure speculation in land benefit consumers? Do not use the same example as used in the text.
17. Is the sale of information a substitute for pure speculation? Use an example to illustrate.
18. Tell the two coordination services provided by pure speculators who make superior appraisals.
19. The text claims that pure speculation can cause resources to be allocated more efficiently. By giving an example, explain how.
20. Explain how speculation in non-renewable resources benefits individuals in the role of consumers. You may wish to use an example.
21. Explain how speculation in commodities markets benefits individuals in the role of consumers. You may wish to use an example. If you do, use one that is different from the text.
22. Explain how speculation in foreign exchange markets benefits individuals in the role of consumers. You may wish to use an example. If you do, use one that is different from the text.
23. Suppose that pure speculators correctly believe that the demand for oranges at the end of this growing season will be higher than producers and other participants in the supply chain believe it would be. Tell how their speculation can benefit consumers.
24. Suppose that pure speculators correctly believe that the demand for oranges at the end of this growing season will be lower than producers and other participants in the supply chain believe it would be. Tell how their speculation can benefit consumers.
25. Pure speculation may benefit consumers by encouraging producers to adjust their supplies in order to account for the superior knowledge of the speculators.

## Study Questions for Chapter 9

1. Using the textbook definitions, define cyclical unemployment, work, work force, unemployment rate, determinant of demand, offsetting change in demand, wage rate, marginal revenue product, marginal revenue product curve, unemployable, supply conditions, determinant of supply, work-saving technological advance, price elasticity of supply, technological unemployment, natural rate of unemployment.
2. Define unemployment by referring to the three parts of the definition.
3. How is work produced and who produces it?
4. When thinking about work, we can classify a person as employed or as unemployed. Name two other categories of people in relation to work.
5. Suppose that a person is laid off by an employer and remains unemployed for a long time. How long must he remain unemployed before he should be classified as not in the work force? Explain.
6. Can a person be classified as unemployed even if he can find another job? Explain.
7. Consider two people: a worker who has just been laid off and a housewife. Both are equally skilled at working and both are offered the same rate of pay by a prospective employer. They both turn down the offer. Both report that they would accept the offer if it was twice as high. According to the text, are both of these classified as unemployed? Explain.
8. Tell the two immediate causes of unemployment.
9. Leaders of labor unions sometimes claim that unemployment is caused by employers only. Tell why this viewpoint is unbalanced.
10. Tell five reasons why the demand for a consumer good is continually changing. In other words identify five determinants of demand.
11. Starting with a point at which producers have fully adjusted to all previous changes (a completely coordinated economy), assume that there is an increase in demand for chicken that is completely offset by a decrease in demand for beef (refer to Chapter 6). Tell how producers in the chicken industry would adjust to the change. In your story, tell what would happen to the prices and quantities of chicken and the prices and quantities of the resources needed to produce chicken. Also, be sure to tell the effects on unemployment, if any.
12. Starting with a point at which producers have fully adjusted to all previous changes (a completely coordinated economy), assume that there is an increase in demand for chicken that is completely offset by a decrease in demand for beef. Show graphically the effects of the increase in demand for chicken. Also show graphically the effects on the market for a

particular kind of work that is employed to produce chickens. Be sure to label your two graphs properly and to explain your graph in words.

13. Starting with a point at which producers have fully adjusted to all previous changes (a completely coordinated economy), assume that there is an increase in demand for chicken that is completely offset by a decrease in demand for beef. Tell how producers in the beef industry would adjust to the change. In your story, tell what would happen to the prices and quantities of beef and the prices and quantities of the resources needed to produce beef. Be sure to tell the effects on unemployment, if any.
14. Starting with a point at which producers have fully adjusted to all previous changes (a completely coordinated economy), assume that there is an increase in demand for chicken that is completely offset by a decrease in demand for beef. Show graphically the effects of the decrease in demand for beef. Also show graphically the effects on the market for a particular kind of work that is employed to produce beef. Be sure to label your two graphs properly and to explain your graph in words.
15. Why is the supply curve for a particular kind of work upsloping?
16. Starting with a point at which producers have fully adjusted to all previous changes (a completely coordinated economy), show graphically the effects of an increase in the supply of nurses on the market for nurses. Be sure to label your graphs properly and to explain your graph in words.
17. Starting with a point at which producers have fully adjusted to all previous changes (a completely coordinated economy), show graphically the effects of a decrease in the supply of electrical engineers on the market for electrical engineers. Be sure to label your graphs properly and to explain your graph in words.
18. Starting with a point at which hair styling shops have fully adjusted to all previous changes (a completely coordinated economy), show graphically the effects on the price and quantity of hairdos. Be sure to label your graphs properly and to explain your graph in words.
19. Starting with a point at which pharmacy shops have fully adjusted to all previous changes (a completely coordinated economy), show graphically the effects on the price and quantity of medicines from pharmacy shops. Be sure to label your graphs properly and to explain your graph in words.
20. If the wage rate for convenience store clerks is \$8 per hour, the number of hours supplied is 10,000 per week. If the wage rate falls to \$6 per hour, the number of hours supplied is 5,000. Calculate approximately the price elasticity of the supply of convenience store clerk work. Is supply elastic or inelastic? (Be able to other problems like this.)
21. If the salary of beginning computer engineers is \$50,000 per year, the number of hours supplied is 20,000 per week. If the salary is raised to \$70,000, the number of hours supplied

rises to 25,000. Calculate approximately the price elasticity of the supply of computer engineer work. Is supply elastic or inelastic? (Be able to other problems like this.)

22. Suppose that there is an increase (decrease) in demand for nuclear physicists. The supply is price inelastic. Would you expect the salary to rise (fall) by a greater or lesser percent than the number of hours of this work supplied?
23. Suppose that there is an increase (decrease) in demand for restaurant delivery drivers. The supply is price elastic. Would you expect the salary to rise (fall) by a greater or lesser percent than the number of hours of this work supplied?
24. Tell the determinants of supply.
25. Give an example of unemployment that is caused by a work-saving technological advance. Use an example that is different from the text. Be sure to explain how the change leads to the unemployment.
26. Suppose that there is a specific work-saving technological advance at one of the links on the supply chain in the structure of production. Will there be an increase or decrease in employment at that link? Explain.
27. Suppose that there is a specific work-saving technological advance at one of the links on the supply chain in the structure of production. Will there be an increase or decrease in employment at the next link downstream from the advance? Explain.
28. Suppose that there is a specific work-saving technological advance at one of the links on the supply chain in the structure of production. Will there be an increase or decrease in employment at the next link upstream from the advance? Explain.
29. Suppose that a technological advance occurs that reduces the costs per unit of producing mountain bikes. Assume that all mountain bikes are alike. The technological advance enables entrepreneurs to produce the same bike at a lower cost per unit. Show on a graph the gains to consumers of mountain bikes. In your answer distinguish between consumers who would have bought bikes before the increase in demand and consumers who buy bikes *only* after the increase in demand.
30. What kind of event could cause a decrease in resources?
31. According to the text, why is there no natural rate of unemployment in the market economy?

## Study Questions for Chapter 10

1. Define money, barter, token coin, commodity money warehouse, bank, debaser, counterfeiter, hyperinflation, financial institution, central bank, central bank note, check clearing system, transferable bank deposit, debit card, credit card, scrip.
2. Give an example of a good that functions as a medium of exchange in a barter society. Be sure to explain why it is a medium of exchange.
3. Define commodity money and give an example of it.
4. Tell the difference between media of exchange in a barter society and the medium of exchange in a money economy.
5. Why have silver coins been more valuable in exchange than the equivalent weight of silver.
6. Tell the characteristics of gold that have made it a good medium of exchange.
7. Define representative money and give an example of it.
8. Tell the action that a commodity money warehouse manager must take to *redeem* representative money.
9. Suppose that you are a warehouse manager in a commodity money economy. You store gold coins and issue warehouse receipts. What actions could you agree to take if you wanted to expand your business and to encourage people to use representative money in exchange rather than commodity money?
10. Tell the four characteristics of representative money.
11. Identify the two types of credit money.
12. Define paper credit money and give an example of it.
13. Suppose that there is only a single issuer of paper money and that every piece of paper money looks like every other piece. Is it possible that some of the money will be representative money and some will be credit money? If not, tell why not. If so, explain how two things that are identical in appearance and in use can be classified differently.
14. Tell how paper credit money could emerge in a system in which all money is, at first, representative money.
15. Define government money and give an example of it.

16. Suppose that you live in a society that contains both commodity money and government credit money. If you plan to hold money, are you likely to have greater security by holding commodity money or by holding government money? Explain.

17. Identify the three duties of a modern central bank.

18. Tell the difference between a debit card and a credit card.

19. A gold warehouse that issues representative money is obligated by law to redeem its money in commodities if someone demands it. Similarly, a modern bank is obligated by law to pay currency to people who possess checking account or debit card balances. However, if a modern bank has difficulty meeting its deposits, it possesses a means of meeting the demands that the commodity money warehouse does not have. What is this means?

20. Name and describe three ways to use transferable deposits.

21. Why is the U.S. dollar the mostly widely used money in international trade today?

22. How could a government introduce money into a barter society without monetizing commodities or debt?

## Study Questions for Chapter 11

1. Define quantity theory of money, business cycle, monetary theory of the business cycle, hoarding, discount rate, reserves, fractional reserve banking system, reserve requirement (required reserve ratio), fully loaned up bank, central bank deposit insurance, bank run, excess reserves, short of reserves, deposit multiplier, open market operations, trade surplus, trade deficit, inflation, deflation, total cash holding, velocity of circulation of money, aggregate real output, price level, money output, expansion phase of the business cycle, contraction phase of the business cycle, peak of the business cycle, trough of the business cycle, amplitude of the business cycle, periodicity of the business cycle, money income, real income, money illusion, recession, depression, recovery, stagflation, absolute prices, relative prices.
2. Give an example of currency that is out of circulation. Then tell how it can get into circulation.
3. In a modern banking system, how does an ordinary banker create money?
4. Ordinary banks typically issue more transferable deposits than they can back with their customer deposits of government currency (central bank notes and coins). Why do they do this? In your answer, tell who receives the additional transferable deposits.
5. Can a modern bank invest new money in the stock market? Explain.
6. In a modern banking system, a bank lends out a share of its deposits. What would happen if many loans were not repaid and, as a result, a banker had insufficient currency to meet depositors demands to withdraw them or transfer them to others? Answer in some detail.
7. Why is a central bank some times called a “lender of last resort?”
8. Are bank runs likely today? Explain.
9. In a modern banking system, how is the central bank likely to respond if a private bank fails to meet the required reserve ratio set by the central bank?
10. Tell what happens in the federal funds market.
11. Assume that all banks in a modern national banking system are fully loaned up. The central bank wants to increase the quantity of money. What is it likely to do?
12. Assume that all banks in a modern national banking system are fully loaned up. The central bank prints \$500 in currency and uses it to buy government bonds equal to \$500. The reserve requirement is 25%. Tell the maximum amount of new money that will result from the central bank’s decision.
13. Assume that all banks in a modern national banking system are fully loaned up. The central bank prints \$200 in currency and uses it to buy government bonds equal to \$200. The reserve

requirement is 10%. Tell the maximum amount of new money that will result from the central bank's decision.

14. Assume that all banks in a modern national banking system are fully loaned up. The reserve requirement is 20%. The central bank wants to increase the quantity of money by \$40,000. Tell how it could achieve this goal.

15. Assume that all banks in a modern national banking system are fully loaned up. The reserve requirement is 25%. The central bank wants to increase the quantity of money by \$20,000. Tell how it could achieve this goal.

16. Tell three ways that the central bank may control the quantity of money and identify the one that is most often used.

17. Describe the international gold standard.

18. Imagine that you are living in the nineteenth century and that your nation is on the gold standard. Economists predict that next year, gold will flow into the country from some of the newly discovered colonies in South America. Also, they predict that your country will import a greater money value of goods from other countries than it exports. Do you believe that there will be inflation or deflation? Explain your answer.

19. Tell the difference between absolute prices and relative prices. In your answer, be sure to define each term.

20. What is meant by the quantity independence characteristic of money's services?

21. Write the quantity theory of money equation in expanded form – i.e., including all of the different types of specific goods. Tell what each variable in the equation refers to.

22. Write the abbreviated form of the quantity theory of money equation and tell what each variable in the equation refers to.

23. Draw a picture of a business cycle including the expansion phase, the contraction phase, the peak and the trough. Be sure to identify the phases, the peak, and trough in your picture.

24. For the simple monetary theory of the business cycle, describe in words the expansion phase. Pay special attention to the factors that cause the expansion.

25. For the simple monetary theory of the business cycle, use the quantity theory of money equation, with arrows, to show what happens to the four variables during the expansion phase of the cycle.

26. For the simple monetary theory of the business cycle, describe in words the transition from the expansion phase to the contraction phase. Pay special attention to the causes of the transition

and their effects.

27. Tell the difference between money income and real income.

28. For the simple monetary theory of the business cycle, describe in words the contraction phase. Pay special attention to the factors that cause the contraction.

29. For the simple monetary theory of the business cycle, use the quantity theory of money equation, with arrows, to show what happens to the four variables during the contraction phase of the business cycle.

30. Why does the business cycle come to an end?

31. The quantity independence characteristic of money suggests that it does not matter how much money there is. If this is so, what is wrong with allowing the central bank to increase the quantity of money?

## Study Questions for Chapter 12

1. Using textbook definitions, define near-future goods demand, rate of interest, supply of loanable funds, supply of loanable funds curve, demand for loanable funds, demand for loanable funds curve.
2. Why does the supply of loanable funds curve for a given length of time and beginning at a particular time have a positive slope?
3. Why does the demand for loanable funds curve for a given length of time and beginning at a particular time have a negative slope?
4. Coordination in a single loan market could not exist unless there is also coordination between consumers and producing entrepreneurs. Explain. Once coordination is achieved, these people do not wish to change. Describe the actions that they do not want to change.
5. Draw a graph that shows a completely coordinated loan market. Be sure to label your graph.
6. In words, tell the effects of a decrease in near-future demand on market interest rates and amounts of funds lent in loanable funds markets.
7. Draw a graph to represent the effects of a decrease in near-future goods demand on a market for loanable funds. Label your graph and explain the curves and points on your graph.
8. In words, tell the effects of an increase in near-future demand on market interest rates and amounts of funds lent in loanable funds markets.
9. Draw a graph to represent the effects of an increase in near-future goods demand on a market for loanable funds. Label your graph and explain the curves and points on your graph.
10. In words, tell the effects of an entrepreneur's discovery of a new long-term profit opportunity on market interest rates and the amounts of funds lent in loanable funds markets of the same length and beginning time.
11. Draw a graph to represent the effects of an entrepreneur's discovery of a new long run profit opportunity on the market interest rate and amount of funds lent in loanable funds markets in which the length of loan and beginning time are the same as the loan most desired by the entrepreneur-discover. Label your graph and explain the curves and points on your graph.
12. Identify the main difference between the more complex theory of the business cycle in this chapter and the simple theory in chapter 11. Pay special attention to "unfinished and abandoned projects."
13. Does anyone lose when individuals earn speculative gains by betting on their knowledge

about future monetary policy? Explain.

14. Central bank actions to increase or decrease the quantity of money may lead to a “central bank prediction contest.” Explain what this is and how it can be caused by central bank actions.

## Questions for Chapter 13

1. Define: real output gap, risk averse, liquidity, liquidity trap, macroeconomic equilibrium, demand shock, supply shock, fiscal policy, expansionary fiscal policy, contractionary fiscal policy, full employment macroeconomic equilibrium, unemployment economy, inflation economy, expansionary monetary policy, contractionary monetary policy.
2. When economists speak of “macroeconomic problems,” what do they have in mind?
3. Tell the stated purpose of the U.S. Employment Act of 1946.
4. J. M. Keynes wrote that, under ordinary conditions (i.e., whether there is a business cycle or not) real output was not likely to reach its potential without government help. What reason did he give for this?
5. How can it be determined whether someone is risk averse?
6. J. M. Keynes argued that business cycles are likely to be more severe than expected. What reasons did he give for this?
7. According to Keynes, how could entrepreneurial investments increase the amplitude of business cycles?
8. Why was there downward inflexibility of wages in England during the time when Keynes wrote?
9. Tell how downward inflexibility of wages can cause unemployment to be greater than otherwise during a business activity contraction.
10. J.M. Keynes believed that the interest rate might be incapable of being used to coordinate a market for loanable funds during a contraction. What reason did he give?
11. By referring to a graph, explain how a liquidity trap might prevent entrepreneurs from using the interest rate to coordinate a market for loanable funds, as Keynes believed it might.
12. Tell the relatively simple remedy recommended by Keynes to the deficiencies of a market economy that he had identified.
13. List the three types of spending in Keynesian economics. In your answer disregard imports and exports.
14. List and tell the composition of each of the three types of spending in Keynesian economics. In your answer disregard imports and exports.
15. Draw a diagram showing macroeconomic equilibrium. Be sure to label your axes correctly.

16. Describe a condition in which the price level is too high to achieve macroeconomic equilibrium. In other words, describe the real output that is produced and the spending on it. You may use a graph but, if you do, be sure to label it correctly.

17. Describe a condition in which the price level is too low to achieve macroeconomic equilibrium. In other words, describe the real output that is produced and the spending on it. You may use a graph but, if you do, be sure to label it correctly.

18. What could cause a supply shock in Keynesian economics?

19. What could cause a demand shock in Keynesian economics?

20. Using a graph, show the effect of a positive (negative) demand shock on the equilibrium *price level* and *real output* in Keynesian economics. In other words, show whether these variables rise or fall according to Keynesian economics? Be sure to label your axes correctly and to tell what your graph means.

21. Using a graph, show the effect of a positive (negative) supply shock on the equilibrium *price level* and *real output* in Keynesian economics. In other words, do they rise or fall according to Keynesian economics? Be sure to label your axes correctly and to tell what your graph means.

22. According to Keynesian economics, which component (s) of total spending is fiscal policy intended to change?

23. According to Keynesian economics, which component (s) of total spending is monetary policy intended to change?

24. According to Keynesian economics, tell how expansionary (contractionary) fiscal policy would affect an unemployment (inflation) economy. You may wish to use a graph. Be sure to label your axes and curves properly and to explain the graph in words.

25. According to Keynesian economics, tell how expansionary (contractionary) monetary policy would affect an unemployment (inflation) economy. You may wish to use a graph. Be sure to label your axes and curves properly and to explain the graph in words.

26. According to Keynesian economics, how can fiscal policy be used to mediate a negative demand shock. In your answer be sure to tell what a negative demand shock is.

27. According to Keynesian economics, how can fiscal policy be used to mediate a negative supply shock. In your answer be sure to tell what a negative supply shock is.

28. According to Keynesian economics, tell how monetary policy can be used to reduce the unemployment that exists in an unemployment economy to its target level. You may wish to use a graph. Be sure to label your axes and curves properly and to explain the graph in words.

29. According to Keynesian economics, tell how monetary policy can be used to eliminate the inflation in an inflation economy. You may wish to use a graph. Be sure to label your axes and curves properly and to explain the graph in words.

## Questions for Chapter 14

1. Define: government balanced budget, government budget deficit, government budget surplus, crowding out effect of government borrowing, monetizing the deficit, monetarism, tax rate, tax wedge, progressive income tax.
2. Describe the reasoning behind the idea that Keynesian fiscal policy is only likely to have significant effects if there is a change in the quantity of money.
3. Tell the reasoning behind the monetarist proposal that the growth in the quantity of money should equal the projected growth of real output.
4. Some monetarists have criticized the proposal that the growth in the quantity of money should equal the projected growth of real output. What is the basis for their criticism.
5. Some monetarists believe that the quantity of money should not be changed. How do these monetarists answer the following challenge. "If there is economic growth, prices will fall and disrupt entrepreneurial calculation?"
6. Briefly, tell the main difference between demand management macroeconomic policies and supply-side policies.
7. Explain the difference in the U.S. between the *average* income tax rate and the *marginal* income tax rate? Tell why they may be different for a person who earns income.
8. According to supply-siders, a decrease in high marginal rates of tax would give people two kinds of incentives that might result in a reduction in waste. What are they?
9. Describe two methods of illegal tax avoidance that might be caused by a high income tax rate.
10. How would a reduction (increase) in the tax rate effect the crime rate, according to supply-side economists?
11. Can a reduction in tax rates cause tax revenues to rise? Explain.
12. Draw a Laffer curve and explain it's significance. Make sure to label your grjh properly.

## Questions for Chapter Fifteen

1. Define: tariff, quota, price convergence, rules of origin, flexible exchange rate system.
2. Name three factors that gave the entrepreneurs of different nations an incentive to greatly increase international trade after 1850.
3. Identify the major independent actions by sovereign nations that helped to increase world trade after 1945.
4. Describe the Bretton Woods international monetary system. In your description, tell the actions that the U.S. and other countries were required to take in order to be part of the system.
5. Identify the major international agreements that helped to increase world trade after 1945.

## Questions for Chapter Sixteen

1. Define: trade in services, capital inflow, capital outflow, capital control, protectionist, “picking winners” policy in international trade, unfair competition in international trade, dumping, and “race to the bottom.”
2. Under a flexible exchange rate system, tell the main effects of an outflow of currency.
3. Under a flexible exchange rate system, tell the main effects of an inflow of currency.
4. In a flexible exchange rate system, does an inflow of currency refer to foreign currency entering the economy? Explain.
5. Tell why a government might want to keep the value of its currency low in relation to other currencies.
6. Suppose that a nation unexpectedly allows imports of a good that was previously prohibited. According to the text, the losses to some producers and resource suppliers are offset by gains to other producers and resource suppliers. To discover these gains, it is necessary to trace the money that is exchanged for the foreign currency that is needed to buy the imports. Describe two possible uses of the money and then describe the offsetting gains.
7. State the infant industry argument for protecting a domestic firm from foreign competition. Also tell what is wrong with the argument, according to the text.
8. The text presents two reasons why firms and industries should not be singled out for help in international competition. Identify these and explain these if you need to do so in order to demonstrate that you understand them.
9. State the unfair competition argument for protection against foreign competition. Then tell the counter-argument.
10. Give at least two examples of detestable methods of production in the detestable methods argument for protection against foreign competition. Also state the counter-argument presented by the text.
11. State the external effects argument for protection against foreign competition. Give an example.
12. It is sometimes argued that a domestic firm that is not permitted to pollute the environment should be protected from competition by a foreign firm that is allowed to pollute. What is the counter-argument to this?