Test Bank for Modern Principles of Economics 5th Cowen

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Name:_____ Class:_____ Date:_____

Chapter 1

1. Recall Chapter 1's opening story about the British sea captains and the convicted felons. In what way were incentives used to solve the problem of the high mortality rate on board the ships?

a. Payment (to ship captains) was to be offered for each prisoner that was taken aboard the ships.
b. Payment (to ship captains) was made independent of the regulations passed for prisoner welfare.
c. Regulations were passed so that prisoners could get better food, water, and medical care.
d. Payment (to ship captains) was made dependent on the survival rate of prisoners.

ANSWER: d

2. Recall Chapter 1's opening story about the British sea captains and the convicted felons. Instead of paying the sea captains for each prisoner placed on board the ships in Great Britain, an economist suggested:

a. paying for each prisoner who walked off the ship in Australia.
b. paying for food and water to reduce the costs of caring for prisoners during the transit.
c. doing nothing, since the suggested change would not matter.
d. that new regulations be passed to require prisoner safety and health.

ANSWER: a

3. In his book *The Wealth of Nations*, Adam Smith claimed that individuals:

a. always act in an altruistic way.
b. always consider the effect of their actions on others.
c. are motivated by self-interest.
d. are not concerned with resources.

ANSWER: c

4. In the opening story, the payment to captains of prisoner transport ships for each convict who arrived in Australia instead of for each convict who boarded the ship:

a. made no difference.
b. saved the lives of hundreds of convicts.
c. increased the volume of slave trafficking.
d. shows that people care more about morality than about their self-interest.

ANSWER: b

5. Several states offer rebates on the purchase of electric vehicles. This practice highlights the idea of:

a. self-interest.
b. trade-offs.
c. incentives.
d. thinking on the margin.

ANSWER: c

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6. Every day, people work at serving people meals at restaurants all around the world. These people work for our benefit because:
   a. people think on the margin.
   b. trade-offs are everywhere.
   c. they benefit by doing so.
   d. institutions require them to do so.

ANSWER: c

7. Economists think that people are self-interested:
   a. only when monetary incentives are present.
   b. because they respond to incentives in predictable ways.
   c. only rarely in response to incentives.
   d. unless they are being altruistic.

ANSWER: b

8. The basic postulate of economics indicates that changes in incentives influence the:
   a. actions of producers but not consumers.
   b. actions of consumers but not producers.
   c. choices of individuals only when they buy and sell goods in the marketplace.
   d. choices of individuals with regard to a wide range of activities, including those generally perceived as social or political.

ANSWER: d

9. According to economists, people respond to:
   a. other people.
   b. social interest.
   c. money.
   d. incentives.

ANSWER: d

10. Adam Smith wrote, “It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own interest.” He meant that:
   a. most of us no longer get our dinner directly from the butcher, the brewer, and the baker.
   b. butchers, brewers, and bakers are not productive members of society.
   c. high-interest payments mean that no one has to work anymore.
   d. people work for the benefit of others because it benefits them to do so.

ANSWER: d

11. Which financing method for transporting prisoners from point A to B will result in the greatest number of

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prisoners surviving the trip? Assume there are 50 prisoners being transported.

a. The ship's captain is paid $100 by the government for every live prisoner that is loaded on board at point A.
b. The ship's captain is paid $100 by the government for every live prisoner that is unloaded at point B.
c. The ship's captain is paid $400 by the government for every live prisoner that is loaded on board at point A.
d. The ship's captain is paid a flat rate of $3,000 for the trip, rather than being paid per prisoner.

ANSWER: b

12. The main incentive for business activity is:

a. government subsidies.
b. technological advancement.
c. profit.
d. employment.

ANSWER: c

13. Suppose a certain business wants to encourage its employees to live healthier lives. The easiest way for the business to realize this goal is to:

a. give each employee $100 a month for a gym membership.
b. install a gym in the office building.
c. reduce health insurance benefits.
d. pay a monthly bonus to employees who log an hour of exercise a week on a fitness tracker.

ANSWER: d

14. Many companies pay their factory employees based on piece rates—the more they produce, the more they get paid. This practice highlights the role of:

a. marginal thinking.
b. incentives.
c. trade-offs.
d. sunk costs.

ANSWER: b

15. If there were no _____, the "invisible hand" would not function as Adam Smith describes.

a. money
b. self-interest
c. trade
d. inflation

ANSWER: b

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16. Based on the ideas of Adam Smith, it is _____ barbers wash, cut, and style hair, but _____.
    a. not out of benevolence that; from their regard for their own self-interest
    b. out of benevolence that; sometimes from their regard for their own self-interest
    c. not out of self-interest that; out of their benevolence
    d. from charity and good will that; only if they can charge high prices

ANSWER: a

17. In the 1800s, the federal government paid railroad companies for each mile of track built. This payment scheme created incentives for railroad companies to lay track:
    a. between points A and B using the most direct route.
    b. between points A and B using the most indirect route.
    c. as slowly as possible.
    d. using the best materials possible.

ANSWER: b

18. Adam Smith's “invisible hand” refers to:
    a. people's pursuit of their own self-interest.
    b. people's pursuit of the social interest.
    c. social justice.
    d. government control.

ANSWER: a

19. Adam Smith coined the term “invisible hand” to mean:
    a. a physical hand that leads individuals to promote social interest by pursuing self-interest.
    b. a metaphorical hand that leads individuals to promote social interest by pursuing self-interest.
    c. a physical hand that leads individuals to promote self-interest by pursuing social interest.
    d. a metaphorical hand that leads individuals to promote self-interest by pursuing social interest.

ANSWER: b

20. What is the “invisible hand”?
    a. the idea that government economic planning tends to benefit not only the individual but also all of society
    b. the principle that most people avoid economic transactions with so-called “outsiders”
    c. the idea that people pursuing their own self-interest actually benefit the public at large
    d. the notion that the pursuit of profit leads to the exploitation of consumers

ANSWER: c

21. Adam Smith sought to explain the concept of aligning self-interest with the promotion of society's overall interest by:

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a. using an analysis of wealth as productivity.
b. suggesting that markets are led by an invisible hand.
c. arguing that markets are ineffective institutions.
d. suggesting that government increase regulations.

ANSWER: b

22. The idea that markets work efficiently:
a. refers to the fact that self-interest can be aligned with social interest.
b. means that trade-offs can be reduced by channeling greed toward good ends.
c. suggests that there is never any need for government regulation, taxes, or subsidies.
d. has been known for many centuries.

ANSWER: a

23. Which of the following statements reflects Adam Smith's important insight into marketplace behavior?
a. Society benefits when people and firms pursue their own self-interest.
b. Markets are usually an inefficient way of organizing economic activity.
c. Greedy, self-interested behavior needs to be constrained to ensure strong economic growth.
d. Trade restrictions on imported goods increase domestic employment.

ANSWER: a

24. Adam Smith's metaphor of the “invisible hand” refers to the notion that:
a. greed is always good when externally motivated.
b. behavior based on self-interest can lead to an overall benefit to society.
c. market incentive can lead to negative side effects.
d. markets always align self-interest with social interest.

ANSWER: b

25. When markets don't align self-interest with social interest:
a. markets will still manage to reach an efficient outcome.
b. governments may improve the situation by changing incentives.
c. societal costs will always exceed individual benefits.
d. individual benefits will exceed societal benefits.

ANSWER: b

26. If market incentives to produce are too strong, the market will end up producing:
a. too much of the good.
b. too little of the good.
c. a quantity equal to the efficient outcome, as market incentives can never be considered too strong.

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d. zero output.

ANSWER: a

27. If market incentives to produce are too weak, the market will end up producing:
    a. too much of the good.
    b. too little of the good.
    c. a quantity equal to the efficient outcome, as any incentive will result in economic efficiency.
    d. zero output.

ANSWER: b

28. According to economists, socially good outcomes arise whenever people pursue:
    a. self-interest.
    b. either self-interest or the social interest.
    c. self-interest, and it aligns with the social interest.
    d. self-interest, and it does not align with the social interest.

ANSWER: c

29. The "invisible hand" concept is:
    a. always present as a force in market outcomes.
    b. never present as a force in market outcomes.
    c. frequently present as a force in market outcomes.
    d. not well understood as it relates to market outcomes.

ANSWER: c

30. When the social interest is aligned with self-interest:
    a. the free market functions in the best interest of society.
    b. regulatory action may improve upon the free market outcome.
    c. the relevant market should be banned.
    d. the relevant production process should be outsourced.

ANSWER: a

31. When it comes to getting a college education, most people consider _____, not _____.
    a. the social interest; their self-interest
    b. their public interest; their social interest
    c. their costs; their benefits
    d. their self-interest; the social interest

ANSWER: d

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32. Government can help to align self-interest with the social interest by:
    a. enacting policies that increase incentives to work and trade.
    b. decreasing international trade.
    c. promoting charity work.
    d. banning free markets.

ANSWER: a

33. Suppose that you do not study for your economics course but still earn a good grade. This is an example of a bad institution because:
    a. your school is not very selective; anyone can get in.
    b. your self-interest in not studying conflicts with the social interest of having people who understand economics.
    c. your school has a reputation of training excellent economists.
    d. sometimes the "invisible hand" is absent, not just invisible.

ANSWER: b

34. During the COVID-19 pandemic, many state governors instituted stay-at-home orders to prevent the spread of the illness. This example highlights the idea that:
    a. greed is bad.
    b. markets align self-interest with the social interest.
    c. government can sometimes improve market outcomes.
    d. incentives are not always important.

ANSWER: c

35. Which of the following choices best illustrates the concept of Adam Smith's "invisible hand"?
    a. Etsy creates a Web site for an artist who sells his artwork to a collector in another country.
    b. A fishery is depleted due to overfishing.
    c. Government requires owners to have their vehicles' emissions tested each year.
    d. A factory that provides much-needed employment is built on the site of the only playground for the children in town.

ANSWER: a

36. Which of the following is an example of self-interest that attempts to promote public interest?
    a. A factory spills chemicals into a nearby river.
    b. The prime minister of Canada restricts the trade of lumber with the United States.
    c. The Cincinnati Reds beat the Atlanta Braves.
    d. An entrepreneur creates a crowd-funding Web site to provide funding for a public school's fine arts program.

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ANSWER: d

37. It takes approximately _____ years and _____ to bring a new drug to the market.
    a. 12; $1 billion
    b. 2; $100,000
    c. 4; $5 million
    d. 6; $20 billion

ANSWER: a

38. When the unemployment rate falls, college enrollment tends to:
    a. rise.
    b. remain the same.
    c. fall.
    d. defy prediction.

ANSWER: c

39. The great economic problem is how to arrange our scarce resources:
    a. to provide the most profit possible.
    b. to meet the basic needs of all people.
    c. to satisfy as many of our wants as possible.
    d. to prevent them from being completely depleted.

ANSWER: c

40. Scarcity:
    a. is when a resource is completely used up.
    b. is when there isn't enough to satisfy all our wants.
    c. happens only in a few economies around the world.
    d. can be fixed with good economic policy.

ANSWER: b

41. The opportunity cost of a choice is:
    a. the value of the opportunities lost.
    b. the net value of the opportunities gained.
    c. the difference between the benefits and costs of the choice.
    d. sometimes positive or negative.

ANSWER: a

42. In the market for pharmaceuticals, the issue of “drug lag” illustrates which of the following ideas?

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a. The longer a drug is tested for safety, the lower the opportunity cost in terms of lives lost.
b. If a drug is not tested for safety, it might kill more people.
c. Because of the higher cost of testing a drug, it takes longer to make it, and more lives are lost.
d. Lives are being lost because safe drugs that are still in the testing stage have not yet been approved.

ANSWER: d

43. In the market for pharmaceuticals, the issue of "drug loss" illustrates which of the following ideas?
a. The longer a drug is tested for safety, the lower is the opportunity cost in terms of lives lost.
b. If a drug is not tested for safety, it might kill more people.
c. Because of the higher cost of testing a drug, fewer drugs are made, and more lives are lost.
d. Lives are being lost because safe drugs that are still in the testing stage have not been approved.

ANSWER: c

44. What you give up to obtain an item is called your:
a. opportunity cost.
b. explicit cost.
c. true cost.
d. direct cost.

ANSWER: a

45. Opportunity costs are important because:
a. monetary costs are higher than opportunity costs.
b. only monetary costs should be considered when making choices.
c. they determine how to make the world more productive.
d. people change their behavior when opportunity costs change.

ANSWER: d

46. The opportunity cost of a choice is:
a. the opportunity of using the money to buy something else cheaper.
b. the money cost that a person does not have to pay when doing something.
c. the money that a buyer has to pay for an item.
d. the value of the next best opportunity foregone.

ANSWER: d

47. Estimates suggest that tens of thousands of people have died because the FDA withheld beta-blockers from the market while testing to determine whether the drugs were safe and effective. This is an example of:
a. drug lag.
b. drug loss.

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c. bureaucratic incompetence.
d. market failure.

ANSWER: a

48. According to economists, when the FDA raises the approval requirements for new drugs:
a. everyone will benefit and be better off.
b. society will potentially lose a new drug approval.
c. everyone but the drug makers will lose.
d. people will only demand more drug testing.

ANSWER: b

49. If the FDA enacts more stringent pharmaceutical drug tests, two costs of this policy would be:
a. drug lag and drug lapse.
b. drug lapse and drug misallocation.
c. drug loss and drug lag.
d. drug misallocation and drug loss.

ANSWER: c

50. Mark Zuckerberg dropped out of college and founded Facebook. His opportunity cost of attending college was:
a. tuition, the cost of books, and room and board.
b. tuition, the cost of books, and a low-paying job.
c. tuition, the cost of books, and the income from his Facebook pursuits.
d. only the income from his Facebook pursuits.

ANSWER: c

51. When the opportunity cost of a choice decreases:
a. individuals are more likely to choose that same option.
b. individuals are less likely to choose that same option.
c. the marginal benefits of that choice increase as well.
d. the marginal benefits of that choice decrease.

ANSWER: a

52. During a recession, we expect that the opportunity cost of attending college:
a. rises.
b. falls.
c. remains the same.
d. cannot be determined from the information given.

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ANSWER: b

53. Quitting your current job to work full-time at your profitable new business is most likely a direct application of the principle of:

a. gains from trade.
b. specialization.
c. thinking on the margin.
d. opportunity cost.

ANSWER: d

54. In an effort to prevent the spread of COVID-19, many state governors requested that businesses shut down to assist in the effectiveness of stay-at-home orders. This policy caused many businesses to lay off their employees. What concept does this example represent?

a. trade-offs
b. marginal pollution
c. sunk costs
d. public provision

ANSWER: a

55. The opportunity cost of winning a free ticket to the World Series worth $885 and choosing to attend the game is:

a. zero, since the ticket was free.
b. priceless, if the person really loves baseball.
c. at least $885, the lost market value of selling the ticket, and the time to go.
d. zero, if the person would rather go to the game than do anything else.

ANSWER: c

56. You must decide whether to work this afternoon or study for your biology test. Your decision highlights the following "Big Idea" in economics.

a. Institutions Matter
b. Incentives Matter
c. Economics Is Fun
d. Trade-offs Are Everywhere

ANSWER: d

57. Why do you think researchers sometimes find a positive relationship between the unemployment rate and college enrollment rates?

a. The opportunity cost of attending college rises during economic booms, leading to higher college enrollment rates.
b. The opportunity cost of attending college rises during recessions, leading to higher college

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enrollment rates.

c. The opportunity cost of attending college falls during recessions, leading to higher college enrollment rates.

d. The opportunity cost of attending college falls during economic booms, leading to higher college enrollment rates.

ANSWER: c

58. The opportunity cost of attending college is:

a. tuition and books.

b. travel expenses, tuition, and books.

c. the psychic costs of missing your family and friends while in school.

d. lost wages from not working full-time.

ANSWER: d

59. Each of the following ideas is central to economics EXCEPT:

a. "good institutions can eliminate economic trade-offs."

b. "people react to incentives."

c. "specialization and trade benefit everyone."

d. "prices rise when the government prints too much money."

ANSWER: a

60. As the FDA uses _____ time and resources to ensure the safety of new drugs, _____.

a. more; more people will die from taking unsafe drugs

b. less; fewer people will die waiting for access to life-saving medicine

c. more; fewer people will die waiting for access to life-saving medicine

d. less; fewer people will die from taking unsafe drugs

ANSWER: b

61. During the Middle Ages, expensive castle-based warfare was the dominant method of conflict. Warfare was also the main function of government. Which reason best explains why few universities were built during this time?

a. The lack of professors meant there was no incentive to create universities.

b. The opportunity cost of building universities was fewer castles.

c. There were no benefits to attending college at the time.

d. Local rulers did not care about long-term growth.

ANSWER: b

62. Most people do not buy the safest car they can find. Why not?

a. Other factors matter besides safety, such as comfort, cost, and fuel economy.

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b. People do not take the time to understand the safety features of cars.
c. Consumers are unaware of the risks of different cars.
d. The statement is false. People do buy the safest car they can find.

ANSWER: a

63. Some people take jobs that are dangerous, but such jobs pay well. For example, oil rig workers make $78,000 per year on average. Why?
a. Oil rig workers are accepting of the danger in trade for higher salaries.
b. Oil rig workers do not understand the danger involved in the job.
c. Oil rig workers are assessing the opportunity cost of the danger in the job.
d. Oil rig workers only care about the positive characteristics of the job.

ANSWER: a

64. Fluctuations in graduate school enrollment correlate positively with fluctuations in unemployment. What is the most likely reason why?
a. The opportunity cost of going to graduate school is high when jobs are difficult to find.
b. When jobs are easy to find, there are strong incentives to go to grad school.
c. The opportunity cost of going to graduate school is low when jobs are hard to find.
d. Even if you have a job, the salary will be so low that going to graduate school is worth the effort.

ANSWER: c

65. Manuel insists that he places an infinite value on his life. Stefan is suspicious of this claim and points out to Manuel that he sometimes eats ice cream when broccoli would be much better for him. What Big Idea is Stefan using?
a. Trade Makes People Better Off: Manuel could not make his own ice cream, though he could grow his own broccoli; Manuel must be trading for ice cream.
b. Incentives Matter: No one is paying Manuel to be healthy.
c. Think on the Margin: "Infinite value" is too much to be on the margin.
d. Trade-offs Are Everywhere: Gaining some enjoyment is worth giving up some safety.

ANSWER: d

66. Why is it less costly to attend college during a recession?
a. Tuition is much lower during a recession.
b. The opportunity cost is higher during a recession because there are more labor market opportunities.
c. The opportunity cost is lower during a recession because there are fewer labor market opportunities.
d. Colleges give out better grades during recessions, so the opportunity cost is lower.

ANSWER: c

67. Why might the FDA err on the side of "overtesting" pharmaceutical drugs rather than use a level of testing

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that is economically efficient?

a. Dangerous side effects are more important than drug loss and drug lag.
b. Dangerous side effects are less important than drug loss and drug lag.
c. Drug lag and drug loss are not significant concerns in the case of most pharmaceutical drugs.
d. Dangerous side effects are not relevant in most pharmaceutical drug cases.

ANSWER: a

68. What should happen to crime rates when the unemployment rate rises?

a. Crime rates should fall because the economic gains to property crime will be lower when incomes are lower.
b. Crime rates should rise because the opportunity cost of crime (i.e., getting a legitimate job) has fallen.
c. Crime rates should fall because the opportunity cost of crime (i.e., getting a legitimate job) has risen.
d. Crime rates should rise because the trade-offs have been eliminated.

ANSWER: b

69. In the 2 hours between classes a student can do one of three things, ranking them from most to least desirable as: (1) chat with friends, (2) study economics, or (3) eat lunch. This student's opportunity cost of chatting with friends is:

a. the total value of studying economics and eating lunch.
b. the value of studying economics.
c. the value of chatting with friends.
d. nothing because students do not pay their friends to chat with them.

ANSWER: b

70. Over the weekend, Bella can do one of three things, ranked as most to least desirable: (1) go to the beach, (2) study economics, or (3) work. Bella’s opportunity cost of going to the beach is:

a. the value of studying economics and working.
b. the value of studying economics.
c. the value of going to the beach.
d. the value of working.

ANSWER: b

71. How is the unemployment rate related to the opportunity cost of college?

a. As the unemployment rate increases, the opportunity cost of attending college falls because fewer opportunities for employment exist.
b. As the unemployment rate decreases, the opportunity cost of attending college falls, since it becomes easier to pay for tuition when employed.
c. As the unemployment rate increases, the opportunity cost of attending college increases because fewer people are giving up the opportunity of working to attend college.

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d. As the unemployment rate increases, the opportunity cost of attending college increases because more people are giving up the opportunity of working to attend college.

ANSWER: a

72. The opportunity cost of committing a crime and spending 5 years in jail:
a. is the same for everyone.
b. is higher for people who are employed than for the unemployed.
c. is zero because the costs of jail are paid for by the government.
d. equals the fines and legal fees.

ANSWER: b

73. Dinah quits her administrative job, which pays $50,000 a year, to finish her 4-year college degree. Her annual college expenses are $11,000 for tuition; $1,900 for books; and $2,500 for food. The opportunity cost of attending college for the year is:
a. $15,400.
b. $12,900.
c. $65,400.
d. $62,900.

ANSWER: d

74. Air travel from Chicago to Los Angeles costs $800 and takes 4 hours. A bus ticket between the cities costs $100 and takes 104 hours. Other things being constant, the minimum value of one's time that would induce a rational individual to fly rather than drive would be:
a. $1 per hour.
b. $7 per hour.
c. $12 per hour.
d. $120 per hour.

ANSWER: b

75. You are given a ticket to a Garth Brooks concert worth $150. You value the ticket at only $100, sell it to a friend for $100, and attend a Chris Stapleton concert for $175. The opportunity cost of attending the Chris Stapleton concert is:
a. $25 worth of alternative goods and services.
b. $75 worth of alternative goods and services.
c. $175 worth of alternative goods and services.
d. $275 worth of alternative goods and services.

ANSWER: c

76. On June 13, 2011, writer Sebastian Anthony at Extreme Tech wrote, “During the two days that the Les Paul

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[Google] doodle was online, those 740 million visitors spent 26 seconds more on the Google home page than normal. That's a total of almost 10.7 million work hours spent playing with the Les Paul Google Doodle. Assuming the average Google user earns $25/hour, the doodle cost companies around the world $268 million in lost productivity." Mr. Anthony's mistake is overestimating opportunity costs. He is doing this by assuming that:

a. labor has no incentive to work.
b. all those work hours would have been spent working if not for the doodle.
c. none of the Google visitors sleep.
d. labor is not making a marginal decision.

ANSWER: b

77. Economists Jevons, Menger, and Walras are credited with:
a. explaining the limitations of monetary policy.
b. formulating the theory of comparative advantage.
c. developing the concept of opportunity cost.
d. starting the "marginal revolution."

ANSWER: d

78. What is meant by the term "marginal revolution"?
a. the public disdain toward the institution of marginal tax rates
b. the transformation in economic thought that occurred with the discovery of marginal thinking
c. the institution of the death penalty for drug dealers
d. the effect of policies on crime

ANSWER: b

79. What is thinking on the margin?
a. making decisions that are of noneconomic importance
b. making choices that are based on historical precedents
c. making choices that ignore the marginal benefits, but not the marginal costs, of some activity
d. making choices by comparing the additional benefits and additional costs from doing a little bit more of some activity

ANSWER: d

80. Deciding whether to study an additional hour for an exam by comparing the additional benefits to the additional costs of an extra hour of study is an example of:
a. the social interest.
b. the invisible hand.
c. marginal thinking.
d. the power of trade.

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ANSWER: c

81. When deciding whether or not to undertake an activity, economists compare:
    a. the total cost of the activity against the total benefit received.
    b. the total benefit of the activity against the total cost of production.
    c. the additional cost of the activity against the additional benefits received.
    d. the average cost of the activity versus the total benefits received.

ANSWER: c

82. A student at a party deciding whether to stay a few more minutes is:
    a. thinking on the margin.
    b. increasing the rate of unemployment.
    c. aligning her self-interest with the social interest.
    d. paying high interest rates.

ANSWER: a

83. Economists believe people make decisions by:
    a. comparing marginal costs with marginal benefits.
    b. thinking about costs but not benefits.
    c. thinking about benefits but not costs.
    d. comparing total costs with total benefits.

ANSWER: a

84. An example of a marginal decision is deciding whether to:
    a. invest half your savings in Google or Microsoft.
    b. buy one more apple or one more banana.
    c. commit your life to economics or biology.
    d. study for 5 hours or for 10 hours.

ANSWER: b

85. All of the following are decisions made on the margin EXCEPT:
    a. eating dessert at a restaurant.
    b. budgeting $10,000 to buy a new car.
    c. buying new shoes to go with your new clothes.
    d. reading for one more hour before going to sleep.

ANSWER: b

86. Decreasing one's driving speed when one sees a police cruiser is an application of the principle of:

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a. gains from trade.
b. returns from specialization.
c. marginal thinking.
d. opportunity cost.

ANSWER: c

87. Imposing the death penalty on rapists may increase the number of murders because:
a. the death penalty is not a deterrent to the behavior of a rapist.
b. once a victim is raped, there is no additional penalty imposed for also killing the victim.
c. rapists are irrational and place no value on the life of their victims.
d. rapists do not think about the consequences of their actions.

ANSWER: b

88. A grocery store is running a "buy-one-get-another-at-one-half-off" promotion on a dozen doughnuts. So the first dozen is $6, and the second would be $3. A person would buy the second dozen if their marginal benefit from the second dozen doughnuts is:
a. greater than $3.
b. greater than $6.
c. greater than $9.
d. less than $3.

ANSWER: a

89. What is a plausible economic explanation for why Braille "dots" are commonly found on drive-up automatic teller machines even though blind customers likely will not use a drive-up automatic teller machine?
a. Blind people must be able to use such machines because the Americans with Disabilities Act requires such dots on the keys.
b. The marginal cost of making two different types of keypads is substantial, and the benefit of providing keypads without the Braille dots is less than that marginal cost.
c. The marginal cost of making the keys with the Braille dots is less than making the keys without the Braille dots.
d. There is no economic concept that explains why the keypads have Braille dots.

ANSWER: b

90. Suppose your teacher finishes class 30 minutes early on the day before an exam. She indicates that you may leave, or you may stay on for an optional study period that will last for the remaining 30 minutes of the scheduled class time. You should:
a. always choose to stay for the study period, since you have already paid for the class time.
b. choose to stay only if you like the instructor, since the value obtained is higher than if you disliked the instructor.
c. choose to stay only if the benefits gained from the extra study session exceed the cost of another 30

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minutes in class.

d. choose to stay for the study session only if you do not plan to study on your own for the exam.

ANSWER: c

91. Suppose you have ordered a value meal at a local fast-food restaurant. The cashier asks if you would like to "supersize" your meal. In order to make an efficient decision, you should compare:

a. the total cost of the larger, "supersized" meal versus the total benefits received.

b. the additional cost of the larger meal versus the additional benefits received.

c. the total cost of the larger meal versus the additional cost to the restaurant.

d. the benefits of the smaller meal versus the additional benefits obtained from consuming the "supersized" meal.

ANSWER: b

92. If the costs of staying at a party a few more minutes are higher than the benefits, you should:

a. stay longer.

b. leave the party.

c. never have attended the party in the first place.

d. have thrown your own party.

ANSWER: b

93. If the costs of studying for your economics test for 30 more minutes are higher than the benefits, you should:

a. continue to study.

b. quit studying.

c. not study in the first place.

d. study for another hour.

ANSWER: b

94. When deciding how much to study for an economics class, students should study until:

a. the total benefits exceed the total costs.

b. the total costs equal the total benefits.

c. the marginal benefits exceed the marginal costs.

d. the marginal costs exceed the marginal benefits.

ANSWER: d

95. When deciding whether to eat more food at a buffet, diners should eat until:

a. total benefit exceeds total cost.

b. total cost equals total benefit.

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c. marginal benefit exceeds marginal cost.
d. marginal cost exceeds marginal benefit.

ANSWER: d

96. A high-school graduate deciding to go to college makes that decision by:
a. comparing the total income earned per year after graduating from college with the total cost of going to college.
b. comparing the additional income earned per year after graduating from college with the additional cost of going to college.
c. thinking about the benefit to society if she goes to college.
d. following what her friends do.

ANSWER: b

97. Suppose a customer at a restaurant is deciding whether or not to order dessert. Marginal thinking means that the customer should compare:
a. the total benefit from the entire meal and dessert with the additional cost of the dessert.
b. the total benefit from the entire meal and dessert with the total cost of the meal and dessert.
c. the additional benefit from the dessert with the additional cost of the dessert.
d. the marginal benefit from the meal with the marginal cost of the dessert.

ANSWER: c

98. A customer at a fast-food restaurant may choose to order a burger for $4.00 and fries for $1.50 or order a value meal (that includes the burger, fries, and a drink) for $6.00. What is the marginal cost of the drink if the customer orders the value meal?
a. $6.00
b. $1.50
c. $0.00
d. $0.50

ANSWER: d

99. At Cordless Cellular Phone Services, an unlimited cell phone plan costs $50 per month and has unlimited minutes, texts, and data. What is the marginal fee for the 1,000th minute used?
a. $0.50
b. $0
c. $0.05
d. $0.10

ANSWER: b

100. An automobile gets 40 miles per gallon, and a gallon of fuel costs $4.00. What is the marginal fuel cost for

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a typical mile of driving with this vehicle?

a. $0.05
b. $0.10
c. $0.15
d. $0.20

ANSWER: b

101. The average tax on a professor's income of $100,000 is 18%, and the marginal tax rate above $100,000 is 45%. If the professor teaches during the summer and earns an additional $10,000 (bringing her total earnings for the year to $110,000), how much of the summer income does she keep after paying taxes?

a. $4,500
b. $1,800
c. $6,300
d. $5,500

ANSWER: d

102. Joe runs a landscape business. He knows that providing landscaping services costs him $100 per hour on average, while the cost of providing such services is $150 per hour after 5 PM (due to overtime pay, reduced productivity, and the added wear and tear on his equipment). A potential client offers Joe $130 per hour to provide services but needs him to provide the services after 5 PM due to circumstances at the property.

a. Joe should take the job, since $130 exceeds his average cost of production.
b. Joe should take the job, since he is making a $30 profit per hour.
c. Joe should decline the job, since he would lose $150 per hour worked on the job.
d. Joe should decline the job, since he would lose $20 per hour worked.

ANSWER: d

103. A person has a comparative advantage in activity X when that person's:

a. opportunity cost of performing that activity is very high.
b. ability to perform that activity exceeds that of all other people.
c. government negotiates a favorable trade agreement.
d. opportunity cost is lower for him than for other trading partners.

ANSWER: d

104. The real power of trade lies in people's ability to:

a. get things they can't produce.
b. get the lowest price possible.
c. increase their consumption.
d. specialize and increase production.

ANSWER: d

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105. One benefit of trade is that it:
   a. increases the division of knowledge because trade makes people more self-sufficient, producing more of what they consume.
   b. allows for increased specialization and mass-production techniques that lower per unit costs of production.
   c. lowers productivity, leading to greater domestic employment.
   d. decreases economies of scale, making production more efficient.

ANSWER: b

106. When two people voluntarily trade with each other:
   a. one person will be better off, and the other person will be worse off.
   b. both of them will be better off.
   c. both of them will be worse off.
   d. whether they will be better off or worse off depends on how they negotiate with each other.

ANSWER: b

107. Patterns of specialization and trade are explained by:
   a. the principle of comparative advantage.
   b. the principle of absolute advantage.
   c. people's productivity.
   d. government control and regulation.

ANSWER: a

108. When Angel has a comparative advantage over Blake in cooking, it means that:
   a. the opportunity cost of cooking is higher for Angel than for Blake.
   b. the opportunity cost of cooking is lower for Angel than for Blake.
   c. Angel can cook faster than Blake can.
   d. Blake can cook faster than Angel can.

ANSWER: b

109. When Asha has a comparative advantage over Jabari in welding, it means that:
   a. the opportunity cost of welding is higher for Asha than for Jabari.
   b. the opportunity cost of welding is lower for Asha than for Jabari.
   c. Asha can weld faster than Jabari can.
   d. Jabari can weld faster than Asha can.

ANSWER: b

110. It makes sense that Martha Stewart hires another person to do her ironing because:

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a. she never learned how to iron.
b. her opportunity cost of ironing is the same as the opportunity cost for the person she hires.
c. her opportunity cost of ironing is lower than the opportunity cost for the person she hires.
d. her opportunity cost of ironing is higher than the opportunity cost for the person she hires.

ANSWER: d

111. Trade increases production partly by taking advantage of:
a. economies of scale.
b. economies of scope.
c. realism.
d. pluralism.

ANSWER: a

112. Trade increases production partly by taking advantage of:
a. specialization.
b. mercantilism.
c. idealism.
d. internalization.

ANSWER: a

113. Self-sufficiency:
a. is the key to prosperity.
b. is not a popular idea.
c. results in poverty and death.
d. means being able and willing to trade.

ANSWER: c

114. Which of the following statements is TRUE about trade?
a. Everyone can benefit from trade, even people who trade with someone from a foreign country.
b. Comparative advantage is based on specializing in products that have a high opportunity cost of production.
c. If a person can do everything better than anyone else, there is no reason for that person to trade with others.
d. Trade makes one party better off but the other party worse off, so there is no net gain to society.

ANSWER: a

115. Without trade, we would all be able to produce:
a. products we enjoy with trade.

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b. somewhat less than we do now.
c. very little.
d. more than we do now.

ANSWER: c

116. As the United States becomes more productive at manufacturing chemicals and pharmaceutical drugs, the opportunity cost of producing other items such as textiles _____, leading to _____ demand for foreign textiles.
a. increases; increased
b. decreases; increased
c. increases; decreased
d. decreases; decreased

ANSWER: a

117. The better Martha Stewart is at running her business:
a. the higher her opportunity cost of ironing her own shirts.
b. the lower her opportunity cost of ironing her own shirts.
c. the more it makes sense for her to iron her own shirts because she will have more time.
d. the more it makes sense for her to spend her time away from her business.

ANSWER: a

118. What factor is responsible for ending malaria in the United States?
a. inflation
b. wealth
c. the gold standard
d. yardstick competition

ANSWER: b

119. Which of the following helped the most to bring an end to malaria in the United States?
a. government aid to the poor
b. climate change
c. economic growth
d. spending on health care

ANSWER: c

120. Which of the following best explains why economists want to understand the determinants of economic wealth?
a. Economists, like everyone else, are self-interested.
b. As overall wealth increases, distribution of wealth tends to equalize as well.

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c. Higher levels of wealth tend to generate better health and human rights outcomes across countries.
d. The determinants of economic wealth are easier to study than the determinants of economic growth.

ANSWER: c

121. One of the effects of economic growth is:
a. a higher rate of infant mortality.
b. less leisure time.
c. a lower level of reported happiness.
d. better sanitation and health outcomes.

ANSWER: d

122. How are wealth and economic growth related?
a. Increases in wealth help facilitate economic growth.
b. Economic growth causes increases in wealth.
c. Wealth and economic growth are negatively related.
d. Economic growth causes resource depletion and reduces society's wealth.

ANSWER: b

123. The historical rise in living standards of American workers is primarily a result of:
a. the influence of labor unions in America.
b. tariff protection imposed by the American government.
c. the enactment of minimum wage laws in America.
d. the rise in American productivity.

ANSWER: d

124. Countries with _____ have _____ infant survival.
a. higher wealth; higher
b. higher wealth; lower
c. higher productivity; lower
d. higher productivity; higher

ANSWER: a

125. Wealthy countries tend to have _____ physical capital per worker and _____ human capital per worker.
a. little; a lot of
b. a lot of; little
c. a lot of; a lot of
d. no; a lot of

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ANSWER: c

126. Today GDP per capita in South Korea is _____ than in North Korea.
a. 10 times less
b. two times less
c. two times greater
d. 10 times greater

ANSWER: d

127. In 1950, GDP per capita in South Korea was _____ GDP per capita in North Korea.
a. 10 times less than
b. two times less than
c. roughly equal to
d. two times greater than

ANSWER: c

128. South Korea became much richer than North Korea as a result of:
a. foreign aid from the United States.
b. a different cultural background.
c. a different language.
d. its economic systems and incentives.

ANSWER: d

129. North Korea and South Korea were equally poor in 1950, but today South Korea is _____ than North Korea.
a. 10 times richer
b. two times richer
c. two times poorer
d. 10 times poorer

ANSWER: a

130. Which of the following best characterizes rich countries?
a. a very large number of workers
b. significant levels of human and physical capital per worker
c. strong government restrictions on private property rights
d. closed markets and the use of the latest technological knowledge

ANSWER: b

131. What are the institutions that help foster the appropriate incentives for economic growth?

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a. regulated labor and credit markets; and unions
b. communal property rights and absence of a profit–loss system
c. a dependable legal system, property rights, and competitive and open markets
d. production and export quotas; and supply and demand

ANSWER: c

132. An economy in which entrepreneurs are free to experiment with new ideas and bring innovative products to the market will:
a. help economic growth but not affect living standards.
b. lead to improved living standards and increased economic growth.
c. lead to increased living standards but stagnate economic growth.
d. help stagnate living standards but increase economic growth.

ANSWER: b

133. Among the most powerful institutions for supporting good incentives are:
a. government price controls.
b. monopolies.
c. legal limits on excessive profits.
d. property rights.

ANSWER: d

134. Each of the following will act as good incentives to innovate and induce economic growth EXCEPT:
a. government regulations.
b. a dependable legal system.
c. political stability.
d. property rights.

ANSWER: a

135. A dependable legal system and competitive, open markets help to:
a. shape incentives that induce economic growth.
b. reduce liberty and varied freedoms.
c. bring about honest government and political stability.
d. increase inefficiencies.

ANSWER: a

136. Entrepreneurial activity is encouraged by:
a. good institutions.
b. opportunity costs.

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c. economic growth.
d. trade-offs.

ANSWER: a

137. Institutions that promote economic growth include:
a. policies that provide incentives for people to produce and trade.
b. government control in markets.
c. income redistribution from the rich to the poor.
d. the amount of goods and services that are provided citizens by their government.

ANSWER: a

138. Ideas:
a. will run out some day.
b. are not depleted when they are used.
c. are not an important factor in economic growth.
d. occur at the same rate no matter what.

ANSWER: b

139. Institutions that support economic growth are the ones that:
a. encourage consumption and discourage savings.
b. give the government more control over what is produced and how it is produced.
c. require companies to act in the social interest.
d. provide incentives for entrepreneurs to take risks and innovate.

ANSWER: d

140. Which option best explains why firms develop new ideas for production techniques and product features?
a. because they are interested in sharing their new ideas with the world
b. because they are interested in making a profit
c. because it will be in the social interest
d. because doing so will make their customers happy

ANSWER: b

141. If North Korea and South Korea were both equally poor in 1950, why has South Korea developed so much faster since then?
a. The two countries have different linguistic, cultural, and historical backgrounds.
b. North Korea has an economic system that develops incentives.
c. South Korea has maintained a more market-based economic system.
d. South Korea began with a higher per capita GDP.

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ANSWER: c

142. A National Geographic Channel special, *Inside North Korea*, reported on Dr. Sanduk Ruit's humanitarian mission to North Korea, one of the poorest countries in the world. Over a 10-day period, he performed 1,000 relatively straightforward eye surgeries to remove blindness due to cataracts. Why is it not surprising that North Korea doesn't have doctors to perform this surgery?

a. North Korea specializes in other things and trades for medical services.
b. North Korea is too poor to afford qualified eye doctors.
c. The “invisible hand” allocates resources to other areas.
d. North Korea suffers from too many economic booms and busts to afford such surgeries.

ANSWER: b

143. Research spearheaded by Dr. Norman Borlaug in the 1950s and 1960s helped develop high-yield wheat that is now in use all over the world. It was so successful that some credit Borlaug with saving more than 1 billion people from dying of starvation. What quality do ideas have that makes this claim so credible?

a. They don't require many resources to develop, just careful thought.
b. They create incentives, transform human behavior, and allow people to pursue their own self-interest.
c. They are intangible, allowing them to easily be improved upon.
d. They aren't depleted when they are used, allowing them to spread quickly and without limit.

ANSWER: d

144. The Great Depression was:

a. a natural manifestation of competitive markets.
b. cut short because of well-thought-out monetary policy.
c. to date, the worst economic period in U.S. economic history.
d. about as severe as the 2008–2009 recession.

ANSWER: c

145. In a recession, generally:

a. unemployment increases.
b. employment increases.
c. wages decrease and unemployment increases.
d. wages increase and unemployment increases.

ANSWER: c

146. During the Great Depression, the U.S. unemployment rate exceeded

a. 35%.
b. 30%.
c. 25%.

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d. 20%.

ANSWER: d

147. During the Great Depression, U.S. national output fell by:
a. 35%.
b. 30%.
c. 25%.
d. 20%.

ANSWER: b

148. The Great Depression:
a. was the normal response of an economy to changing economic conditions.
b. could not have been lessened with appropriate monetary policy.
c. generated unemployment rates of more than 20%.
d. was not an important economic event.

ANSWER: c

149. Which of the following statements is TRUE?
a. The Great Depression, despite its name, was really a small economic downturn with very little unemployment.
b. The Great Depression refers to the severe economic downturn that occurred during the nineteenth century.
c. The Great Depression would have been less severe if the Federal Reserve had acted appropriately.
d. Well-functioning economies grow at a constant rate and do not experience booms and busts.

ANSWER: c

150. Booms and busts refer to the:
a. fluctuations in economic activity over time.
b. theory of the second best.
c. decreases in a nation's output growth over time.
d. monetary inflation and deflation caused by the central bank.

ANSWER: a

151. Two major policies used by the government to affect economic conditions are:
a. acceleration and recalibration policy.
b. recalculation and normalization policy.
c. fiscal and monetary policy.
d. passive and active policy.

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ANSWER: c

152. Monetary and fiscal policies:
a. can reduce the severity of economic busts.
b. have been proven to be ineffective and are no longer used during recessions.
c. work only during times of rapid inflation.
d. are tools used during economic booms but not economic busts.

ANSWER: a

153. Economists have discovered that economic booms and busts:
a. are needless and can be eliminated.
b. should be encouraged because they help make people better off.
c. can be moderated but not eliminated.
d. cause people to specialize so that they become more productive.

ANSWER: c

154. Most developed countries:
a. have stopped growing.
b. grow at an unsteady rate.
c. grow at a steady rate.
d. grow at an increasing rate.

ANSWER: b

155. Economic booms and busts:
a. can be moderated but cannot be avoided.
b. can be avoided by employing growth-encouraging institutions.
c. do not occur, since the economy always grows at a constant pace.
d. occur only when countries have bad institutions.

ANSWER: a

156. All booms and busts:
a. are part of an economy's normal response to changing economic conditions.
b. are avoidable.
c. are caused by the weather.
d. affect the rate of economic growth.

ANSWER: d

157. Monetary and fiscal policy:

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a. can make matters worse if poorly used.
b. are useless.
c. can prevent all recessions.
d. are all-powerful.

ANSWER: a

158. Which of the following explains why economic booms and busts cannot be avoided?
a. The effects of fiscal and monetary policies will never be completely understood.
b. The time lags of both fiscal and monetary policies make eliminating boom–bust cycles impossible.
c. Economic booms–busts could be avoided if politicians would put good economics ahead of good politics.
d. The economy is always being struck by unavoidable shocks.

ANSWER: d

159. In Zimbabwe, the government _____ the _____ money, which caused the country's severe inflation.
a. decreased; demand for
b. decreased; supply of
c. increased; supply of
d. increased; demand for

ANSWER: c

160. Inflation is:
a. a decrease in the general level of prices.
b. an increase in a price of a good.
c. an increase in the general level of prices.
d. an increase in the prices of goods in a particular classification, like food or energy.

ANSWER: c

161. According to Milton Friedman, “Inflation is always and everywhere a:
a. capitalist problem.”
b. communist problem.”
c. monetary phenomenon.”
d. situation caused by haphazard technological growth.”

ANSWER: c

162. The _____ has the power to regulate the money supply in the United States.
a. Federal Reserve
b. president

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c. Senate
d. House of Representatives

ANSWER: a

163. From 2007 to 2009, the inflation rate in Zimbabwe could be characterized as:
a. negative.
b. zero.
c. positive but low.
d. positive and high.

ANSWER: d

164. The Zimbabwean government printed money as fast as it could for years. As a result:
a. prices fell rapidly in Zimbabwe.
b. the Zimbabwean economy grew rapidly.
c. Zimbabwe experienced mild inflation.
d. Zimbabwe experienced inflation at a rate of billions of percent per month.

ANSWER: d

165. Milton Friedman argued that:
a. prices need to be regulated and set by the government to prevent inflation.
b. general price level increases result from the government printing too much money.
c. inflation is a phenomenon of capitalist economies.
d. appropriate antitrust policy can prevent businesses from causing inflation.

ANSWER: b

166. The central bank of the United States is known as the:
a. Federal Reserve.
b. Central Bank of the United States.
c. Central Reserve Union.
d. Federal Central Bank.

ANSWER: a

167. The central bank of the United States is:
a. the Senate.
b. the Department of Treasury.
c. the Federal Reserve.
d. Wall Street.

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ANSWER: c

168. Inflation can be defined as:
a. the general rise in the level of output in an economy.
b. the boom–bust cycles of an economy.
c. the rise and fall of the general level of prices in an economy.
d. the increase in the general level of prices in an economy.

ANSWER: d

169. An increase in the general price level is:
a. depreciation.
b. appreciation.
c. deflation.
d. inflation.

ANSWER: d

170. Inflation:
a. is a decrease in the general level of prices.
b. is an increase in the general level of prices.
c. makes it easier to figure out real values for goods, services, and investments.
d. is a rare problem in macroeconomics.

ANSWER: b

171. Central banking in the United States refers to:
a. the operation of the Federal Reserve in its attempts to affect the economy.
b. how commercial banks interact with one another to earn more profits.
c. the federal government's control of the U.S. banking system.
d. how banking decisions are centralized in New York City.

ANSWER: a

172. Inflation is primarily caused by:
a. businesses raising their prices in response to increasing energy prices.
b. the government printing too much money.
c. misguided fiscal policy.
d. economic downturns in GDP.

ANSWER: b

173. Most economists believe that an increase in the supply of money results in:

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a. an increase in the demand for goods and services.
b. higher unemployment in the short run.
c. higher inflation in the long run.
d. no change for the economy.

ANSWER: c

174. Inflation is bad for an economy because:
a. there is an increase in demand for goods.
b. it leads to higher employment and wages.
c. people have a hard time figuring out the real values of goods, services, and investments.
d. people feel richer.

ANSWER: c

175. Inflation occurs largely as a result of:
a. the government having a large debt.
b. a shortage in the supply of goods or services.
c. the government printing too much money.
d. a recession.

ANSWER: c

176. Which of the following would be the most likely to cause inflation?
a. massive increases in government spending
b. sustained increases in the money supply
c. increases in interest rates
d. a decline in the purchasing power of the dollar

ANSWER: b

177. When people spend more money without an increase in the supply of goods, prices:
a. must rise.
b. must fall.
c. may rise or fall.
d. must stay the same.

ANSWER: a

178. In Zimbabwe, price increases of 150,000% per year were caused by:
a. the country's unsustainable trade deficit.
b. marginal tax rates as high as 90%.
c. large increases in the money supply.

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d. deregulated prices.

ANSWER: c

179. Inflation typically arises from:
a. a sufficiently rapid contraction of the money supply.
b. a constant money supply.
c. a sufficiently rapid increase in the money supply.
d. an increase in the price level.

ANSWER: c

180. What is one cause of inflation?
a. the persistent rise in prices in the economy
b. the inability of production to keep up with spending in the economy
c. increased spending by people and the government
d. economic growth without money growth

ANSWER: b

181. A policymaker wants to reduce inflation. In order to make an intelligent decision about how to do so, the policymaker:
a. should use a simple rule: once inflation is gone, it will always be gone.
b. needs to know the causes of inflation, for example, the government printing too much money.
c. should find out if people are really better off as a result of the inflation.
d. should realize that inflation can be reduced without any costs.

ANSWER: b

182. In an episode of *DuckTales* (a Disney cartoon starring Scrooge McDuck) entitled "Dough Ray Me," one of the characters invented a duplicating machine. Other characters used the machine to start duplicating money at a phenomenal rate. What would you expect to happen? (And indeed, the episode does show this happening.)
a. More people would save money.
b. The government would print more money.
c. It would create massive inflation.
d. Wages would fall.

ANSWER: c

183. Which statement is correct regarding the Federal Reserve?
a. Most economists believe that the Federal Reserve does more good than harm.
b. The Federal Reserve has developed the ability to manage the economy with great precision.
c. Its control of the money supply is not connected to the performance of the economy.

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d. The Federal Reserve's decisions usually have an immediate effect on the economy's unemployment rate.

ANSWER: a

184. The Fed's decisions:
a. are always right.
b. affect the economy with no lag at all.
c. often take months for their effects to be felt in the economy.
d. never help avoid recessions.

ANSWER: c

185. Which statement explains why the Federal Reserve has a tough job?
a. There are lags in the effects of monetary policy, and economic conditions continuously change.
b. Legally it is not allowed to change the supply of money; it can only make recommendations to the president.
c. It takes a long time for Congress to agree on a policy.
d. It can change the supply of money, but that doesn't affect spending or the rate of unemployment.

ANSWER: a

186. The decisions made by the Federal Reserve Bank sometimes result in negative effects on the economy because:
a. the economy is weakened when the Fed uses monetary policy.
b. the government uses money inefficiently when it comes to fiscal policy.
c. the Fed finds that forecasting economic conditions is easy but controlling the money supply is difficult.
d. too much money or too little money might induce inflation or unemployment due to bad timing of decisions.

ANSWER: d

187. The main objective of a central bank is to:
a. supply the right amount of money to keep the economy stable.
b. supply as much money as it can to help the economy grow.
c. supply the government with the money it needs to operate.
d. make sure every citizen has the amount of money he or she wants to have.

ANSWER: a

188. If the central bank creates too much money, _____ is the result. If the central bank doesn't create enough money, an economic _____ is the result.
a. deflation; boom

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b. inflation; boom
c. deflation; slowdown
d. inflation; slowdown

ANSWER: d

189. Which of these quotes from the text captures what makes central banking difficult?
a. "No one can foresee the future."
b. "We cannot avoid all recessions."
c. "Markets, however, do not always align self-interest with social interest."
d. "In some situations the Fed must accept a certain amount of either inflation or unemployment."

ANSWER: a

190. The average starting salary of economics majors is just behind that of:
a. political science majors.
b. marketing majors.
c. chemical and nuclear engineering majors.
d. education majors.

ANSWER: c

191. Economists believe that people are self-interested all the time.
a. True
b. False

ANSWER: b

192. People are rational and sometimes respond in unpredictable ways to incentives.
a. True
b. False

ANSWER: b

193. People are often irrational and respond in unpredictable ways to incentives.
a. True
b. False

ANSWER: b

194. Economists think that no one is ever self-interested.
a. True
b. False

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ANSWER: b

195. Economists think that people behaving in their self-interest is bad for society.
a. True
b. False

ANSWER: b

196. Economists believe that people will not respond to nonmonetary incentives, like love or status.
a. True
b. False

ANSWER: b

197. In addition to monetary incentives, economists also believe people respond to incentives like fame, power, reputation, and love.
a. True
b. False

ANSWER: a

198. Economists argue that self-interested people respond only to monetary incentives.
a. True
b. False

ANSWER: b

199. Because people instinctively act in their self-interest, markets will often produce outcomes in line with the social interest.
a. True
b. False

ANSWER: a

200. Because people instinctively act in the social interest, markets will produce outcomes in line with the social interest.
a. True
b. False

ANSWER: b

201. Markets align self-interest with the social interest as long as the government doesn't interfere.
a. True
b. False

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ANSWER: b

202. Under the right conditions, markets align self-interest with the social interest, but sometimes government intervention is necessary.

a. True
b. False

ANSWER: a

203. An example of a case in which free markets do not align self-interest with social interest is pollution-emitting production.

a. True
b. False

ANSWER: a

204. An example of Adam Smith's “invisible hand” is self-interested businesspeople developing a better keyboard for the blind in hopes of making large profits.

a. True
b. False

ANSWER: a

205. The opportunity cost of attending college includes tuition, room and board, cost of meals, and the lost opportunity to make money at a job.

a. True
b. False

ANSWER: b

206. The opportunity cost of playing 2 hours of Fortnite is the value of the opportunity lost from the 2 hours of play.

a. True
b. False

ANSWER: a

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

a. True
b. False

ANSWER: b

208. In a large class, each student's opportunity cost of taking an exam is likely to be the same.

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a. True
b. False

ANSWER: b

209. One student's opportunity cost of studying for an exam may be lost work time, while another's may be lost time for playing video games.
a. True
b. False

ANSWER: a

210. The FDA faces societal trade-offs when it decides how safe drugs need to be before allowing patients to use them. For example, if the FDA raises the cost of testing for drug safety, some safe drugs will never be developed, and people will unnecessarily die.
a. True
b. False

ANSWER: a

211. A student spends 4 years in college. College tuition, fees, and room and board cost $10,000 per year. This student's opportunity cost of attending college is $10,000.
a. True
b. False

ANSWER: b

212. Marginal thinking was simultaneously described by three economists—Stanley Jevons, Carl Menger, and Adam Smith.
a. True
b. False

ANSWER: b

213. A marginal change is a small incremental adjustment to an existing plan of action.
a. True
b. False

ANSWER: a

214. The term "marginal" in economics means "additional."
a. True
b. False

ANSWER: a

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215. When deciding whether to eat a second piece of pizza, you should compare the total benefit of the two pieces of pizza with the total cost.

a. True
b. False

ANSWER: b

216. One of the Big Ideas in economic thinking is that there is an incentive to do something if the total benefit is bigger than the total cost.

a. True
b. False

ANSWER: b

217. One of the Big Ideas in economic thinking is that there is an incentive to do something if the marginal benefit is bigger than the marginal cost.

a. True
b. False

ANSWER: a

218. The general manager of a Major League Baseball team reasons that hiring an all-star-caliber third baseman would allow the team to win 13 more games per season, generating more fan interest and higher ticket sales. The estimated increase in ticket and merchandise sales is $10.5 million per year, but it would cost the team $12 million a year to hire an all-star-caliber third baseman. Using marginal cost–benefit thinking, the general manager will not hire the all-star-caliber third baseman.

a. True
b. False

ANSWER: a

219. The economics of trade depends on whether the trading partners live in the same country and share the same language and religion.

a. True
b. False

ANSWER: b

220. Everyone can benefit from trade through increased specialization, division of knowledge, and productivity.

a. True
b. False

ANSWER: a

221. While trade has many benefits, the division of knowledge is a negative outcome of trade.

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a. True
b. False

ANSWER: b

222. Two people can benefit from trade if they both live in the same country but not if they live in different countries.
a. True
b. False

ANSWER: b

223. The theory of comparative advantage concludes that people can produce more by specializing than by doing everything themselves.
a. True
b. False

ANSWER: a

224. Greater emphasis on self-sufficiency and trading less with foreign countries would increase incomes and living standards in the United States.
a. True
b. False

ANSWER: b

225. Less emphasis on self-sufficiency and trading more with other nations will increase incomes and living standards in the United States.
a. True
b. False

ANSWER: a

226. In the process of trading in free markets, firms and consumers benefit, but workers do not.
a. True
b. False

ANSWER: b

227. Economic wealth is uncorrelated with the level of women's rights and political liberty in a country.
a. True
b. False

ANSWER: b

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228. America was so poor in past centuries that even George Washington caught malaria.
a. True
b. False

ANSWER: a

229. Because of their low incomes, about a million people in the United States die from malaria each year.
a. True
b. False

ANSWER: b

230. While economic growth does increase the quality of life, the trade-off is that life expectancy is now shorter than in the past.
a. True
b. False

ANSWER: b

231. People in developing countries are more vulnerable to illness and disease than people in developed countries mainly because they lack the ability to pay for preventative interventions.
a. True
b. False

ANSWER: a

232. People in wealthier economies tend to lead richer and more fulfilled lives.
a. True
b. False

ANSWER: a

233. Understanding economic growth is one of the most important tasks of economics.
a. True
b. False

ANSWER: a

234. Understanding economic growth is not important in economics, but understanding wealth is.
a. True
b. False

ANSWER: b

235. South Korea is an example of a country that has adopted good institutions for promoting economic growth.

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a. True
b. False

ANSWER: a

236. For countries to be wealthy, they need lots of physical and human capital per worker, which, in turn, depends on a system of private property rights, political stability, a just legal system, honest government, and competitive and open markets.
a. True
b. False

ANSWER: a

237. If two countries are initially at the same level of development, the institution of well-functioning markets can allow one country to develop faster than the other.
a. True
b. False

ANSWER: a

238. The environment best suited for economic growth is one with well-functioning competitive markets, property rights, and creativity in firms.
a. True
b. False

ANSWER: a

239. Monetary and fiscal policies are among a government's tools for mitigating economic fluctuations.
a. True
b. False

ANSWER: a

240. The Federal Reserve acted quickly and appropriately to diffuse the Great Depression.
a. True
b. False

ANSWER: b

241. During the Great Depression, the unemployment rate rose above 20%.
a. True
b. False

ANSWER: a

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242. During the Great Depression, the unemployment rate rose above 35%.
a. True
b. False

ANSWER: b

243. A period marked by falling wages, falling national output, and rising unemployment is called a recession.
a. True
b. False

ANSWER: a

244. Economies MUST experience both booms and busts. All economists can do is work to limit the extent of the economic fluctuations.
a. True
b. False

ANSWER: a

245. Monetary and fiscal policies have the potential to make a recession worse.
a. True
b. False

ANSWER: a

246. Monetary and fiscal policies have the potential to improve unemployment and GDP during a recession.
a. True
b. False

ANSWER: a

247. Modern economic understanding allows us to avoid economic booms and busts, although political constraints prevent the needed policies from being implemented.
a. True
b. False

ANSWER: b

248. High inflation in Zimbabwe in 2009 was a result of the Zimbabwean government's printing too much money.
a. True
b. False

ANSWER: a

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249. When the government decreases the supply of money, there is an increase in the general level of prices.
a. True
b. False

ANSWER: b

250. Central banks can cause inflation.
a. True
b. False

ANSWER: a

251. In the long run, excess money printing by the government causes inflation and economic busts.
a. True
b. False

ANSWER: a

252. One of the drawbacks of inflation is that it creates a lot of uncertainty about prices.
a. True
b. False

ANSWER: a

253. Inflation makes it more difficult to figure out the real value of goods.
a. True
b. False

ANSWER: a

254. During the period of dramatic inflation in Zimbabwe, if you had 1 trillion Zimbabwean dollars, you still were not very rich.
a. True
b. False

ANSWER: a

255. Inflation increases the value of money by increasing the purchasing power of money.
a. True
b. False

ANSWER: b

256. If there is high inflation, individual households will be hurt, but economic disruptions on the national level will not result.

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a. True
b. False

ANSWER: b

257. Most economists believe the Federal Reserve does more good than harm to the U.S. economy.
a. True
b. False

ANSWER: a

258. The Federal Reserve's attempts to combat a recession and high unemployment could result in higher inflation.
a. True
b. False

ANSWER: a

259. The Federal Reserve has a dual mandate to promote maximum employment and stable prices. This can be hard because attempts to reduce unemployment can cause more inflation.
a. True
b. False

ANSWER: a

260. The study of economics increases your understanding of the distant past, present events, and future possibilities.
a. True
b. False

ANSWER: a

261. Among other things, an understanding of economics can help you better manage your finances.
a. True
b. False

ANSWER: a

262. One of the limitations of economics is that the principles apply only to the American economic system and not to foreign economies.
a. True
b. False

ANSWER: b

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Chapter 1

263. There are 10 Big Ideas in Chapter 1. List four of them.

ANSWER: A student could list any four of the following Big Ideas:

Incentives Matter
Good Institutions Align Self-Interest with the Social Interest
Trade-offs Are Everywhere
Think at the Margin
Trade Makes People Better Off
Wealth and Economic Growth Are Important
Institutions Matter
Economic Booms and Busts Cannot Be Avoided but Can Be Moderated
Inflation Is Caused by Increases in the Supply of Money
Central Banking Is a Hard Job

264. In his book *The Wealth of Nations*, Adam Smith explained, "It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own interest." Explain what Adam Smith meant by this. Be sure to tie your explanation to one or more of the Big Ideas in economics discussed in the text.

ANSWER: He meant that economists believe that people respond in predictable ways to incentives (Incentives Matter). Every day, we rely on the work of millions of other people to provide us with food, clothing, and shelter. These people work for our benefit because doing so benefits them in the form of profits/income. When these people act in their own self-interest, they also end up promoting the social interest (Good Institutions Align Self-Interest with the Social Interest).

265. How do self-interested businesses benefit society?

ANSWER: The goal of business is to maximize profits, a self-interested pursuit. Maximizing profits, however, requires that businesses cater to their customers' tastes and preferences. Cowen/Tabarrok discuss how supermarkets keep their shelves stocked with products from all over the world and how millions of other people provide the public with food, clothing, and shelter. Paraphrasing Adam Smith: People do these things out of their own self-interest to earn money, not from their own innate kindness. Thus behavior done out of self-interest helps bring a variety of products to the market in sufficient quantity.

266. Let's assume that your favorite musician (who sells platinum records and has sold-out concerts) is a great cook. He also makes splendid cakes and pies. He could sell the pies and cakes for $30 each. Why doesn't he spend his whole day baking and cooking?

ANSWER: He does not spend the whole day baking and cooking because he can make a lot more money singing and signing record deals. The opportunity cost of baking pies and cakes would be too high.

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

ANSWER: Opportunity cost is that which you must give up to obtain some item. The opportunity cost of a person attending college is the value of the best alternative use of that person's time and other resources used in the process. For most students this would be the income the student gives up by not working. A student's opportunity cost of coming to class is the value of the best opportunity the student gave up, such as sleep, a Frisbee game, or being with a girlfriend/boyfriend.

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268. Why do airlines sometimes advertise last-minute airline ticket sales at low prices? What economic principle are they applying?

ANSWER: The airlines are engaging in marginal thinking. They weigh the costs versus benefits of selling a ticket at a sale price. The marginal cost of a last-minute passenger will be a little extra paperwork, some extra jet fuel, and some refreshments on the aircraft. The marginal benefit (the incentive for the airline to offer the sale) of having the last-minute passenger is the extra revenue from serving that customer. If the marginal revenue is greater than the marginal cost, the airline will benefit from selling the airline ticket on sale.

269. Using the marginal thinking concept, explain a student's decision to wake up and attend an 8 AM class in the winter (the student is already registered for the class).

ANSWER: On the one hand, the student will stand to gain extra knowledge from the single session of the class. If the subject is interesting and the teacher is good, this is equivalent to an hour of enjoyment and learning. On the other hand, the student is sleepy, and it is cold and uncomfortable outside. If the class has no attendance policy and there is no exam scheduled and no assignment due, the student may feel that she has nothing to lose by missing one class. Weighing the marginal costs versus the marginal benefits, the student may thus opt to sleep in! A penalty associated with nonattendance when there is an exam scheduled or an assignment due raises the marginal cost of nonattendance.

270. Why do you think economists generally support increased trade?

ANSWER: People will be better off if they can exchange things they value less for things they value more. Doing so will make everyone involved in such trading activity better off.

271. Wherein lies the power of trade?

ANSWER: The power of trade comes from people specializing in the activity of their comparative advantage and trading for more things than they could produce on their own.

272. Using the concepts of incentives and good institutions, explain how a country might achieve economic growth.

ANSWER: Economic growth stems from having well-functioning markets, consumers who are wealthy enough to purchase the goods and services produced, development of physical and human capital per worker, good institutions, and technological advancement.

If consumers can afford goods and services, and wealth is increasing, firms will have markets. Wealthy consumers also save more, which allows firms to invest more. Firms' primary incentive is profit. If firms see the possibility of sales and profit, they will innovate and use and create new technologies in production and product attributes. They will increase efficiency and reduce waste. As firms and consumers become wealthier, more incentives arise for investment and the development of physical and human capital.

However, investment will not occur adequately or efficiently if good institutions do not exist. Good institutions include well-established property rights, an honest government, a dependable legal system, and well-functioning markets.

273. Many industrialized nations have been pumping trillions of dollars into their economies in the form of stimulus packages, tax rebates, and bailouts in order to stimulate additional consumer spending and business

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investment and to ward off global recession. If a large portion of these funds are obtained through the printing of new money, explain whether or not this will help or hurt these economies in the long run.

ANSWER: If the stimulus packages and bailouts are able to increase both consumer spending and business investment, then it is more likely that these initiatives will be successful in warding off recession. However, if these stimulus packages are financed by the printing of new money, then this will most likely lead to increased inflation in the long run, hence dampening the expansionary effects of the stimulus.

274. Explain why central banking is a hard job.

ANSWER: Too much money in the economy means that inflation will result. Not enough money in the economy is bad as well and can lead to a recession or a slowing of economic growth. The Fed is always trying to get it "just right," but some of the time it fails. Sometimes the failure is a mistake because forecasting where the economy is headed is very difficult. Central banking relies on economic tools, but in the final analysis, it is as much an art as a science.

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