

Chapter 1—The Role and Method of Economics

TRUE/FALSE

1. Since resources are abundant, we do not have to make choices about their use.

ANS: F PTS: 1

2. It is possible to completely eliminate scarcity.

ANS: F PTS: 1

3. Scarcity applies to decision makers in macroeconomics but not in microeconomics.

ANS: F PTS: 1

4. One topic that microeconomics explores is how prices are determined in individual markets, while macroeconomics is concerned with issues such as the economy's overall rate of inflation, economic growth and unemployment.

ANS: T PTS: 1

5. Microeconomics is the branch of economics in which you study inflation and unemployment in the economy.

ANS: F PTS: 1

6. Microeconomics explores the allocation of scarce resources from the perspective of small economic units such as consumers and firms.

ANS: T PTS: 1

7. To an economist, individuals are acting "rationally" if they are striving to do their best to achieve their goals.

ANS: T PTS: 1

8. Economists presume that when making a decision, individuals consider both the current action and the future consequences of that action.

ANS: T PTS: 1

9. Economic models are of limited use since they cannot be tested empirically.

ANS: F PTS: 1

10. A hypothesis is a normative statement.

ANS: F PTS: 1

11. A testable proposition that predicts how people will react to changed circumstances is called a hypothesis.

ANS: T PTS: 1

12. A good economic theory should capture as many details about real-world behavior as possible.

ANS: F PTS: 1

13. The main concern of economics is to study how well the stock markets are performing.

ANS: F PTS: 1

14. "*Ceteris paribus*" is a Latin expression that means "holding everything else constant."

ANS: T PTS: 1

15. The fallacy of composition states that even if something is true for an individual, it is not necessarily true for many individuals as a group.

ANS: T PTS: 1

16. When two variables repeatedly change at the same time, there must be a causal relationship between them.

ANS: F PTS: 1

17. Normative analysis focuses on statements that can be tested against real-world data.

ANS: F PTS: 1

18. "A tax cut will lead to higher inflation" is an example of a positive economic statement.

ANS: T PTS: 1

19. To be a positive economic statement, an assertion must be factual.

ANS: F PTS: 1

20. Most disagreements among economists stem from normative issues.

ANS: T PTS: 1

MULTIPLE CHOICE

1. Economics is most importantly concerned with:
- how to profit from trading in the stock market.
 - government taxation and spending.
 - studying how we allocate scarce resources to satisfy unlimited wants.
 - how to reduce inflation.
 - how to successfully launch a business.

ANS: C PTS: 1

2. The central question in economics is how to:

- a. regulate the supply of money.
- b. make the best use of scarce resources to satisfy our unlimited wants.
- c. reduce the wants of individuals, businesses and government.
- d. find more resources to satisfy everyone's wants.

ANS: B PTS: 1

3. Scarcity exists for those with
- a. lower incomes.
 - b. average incomes.
 - c. higher incomes.
 - d. all of the above.
 - e. a. and b. above only

ANS: D PTS: 1

4. The problem of scarcity:
- a. exists because resources are limited relative to wants.
 - b. exists because resources are unlimited relative to wants.
 - c. is solved by economists using abstract models.
 - d. can be eliminated through appropriate government intervention into markets.
 - e. does not exist in communist societies.

ANS: A PTS: 1

5. Which of the following forces us to choose among alternatives?
- a. Value
 - b. Scarcity
 - c. Rarity
 - d. Market mechanism

ANS: B PTS: 1

6. Scarcity is the result of:
- a. government decision making.
 - b. inappropriate normative judgments.
 - c. positive economics.
 - d. wants that exceed the resources necessary to provide them.

ANS: D PTS: 1

7. Scarcity exists because of:
- a. the allocation of goods by prices.
 - b. specialization and division of labor.
 - c. the market mechanism.
 - d. unlimited wants and limited resources.

ANS: D PTS: 1

8. Economics is a social science that primarily explores how:
- a. businesses market products under competitive conditions.
 - b. stock and bond prices fluctuate when there are changes in demand or supply.
 - c. the government allocates its budget among competing political interests.
 - d. goods and services are produced and distributed in a world with limited resources.
 - e. high employment and low inflation levels can be maintained.

ANS: D PTS: 1

9. Economics is primarily the study of:
- a. human greed.
 - b. how firms compete for profits in the marketplace.
 - c. how limited resources are allocated to satisfy unlimited wants.
 - d. unemployed resources.
 - e. how successful investors make money in the stock market.

ANS: C PTS: 1

10. Which of the following goods would be considered scarce?
- a. iPods
 - b. crude oil
 - c. tax preparation services
 - d. all of the above

ANS: D PTS: 1

11. Scarcity:
- a. exists because basic human survival needs cannot be satisfied with available resources.
 - b. occurs only in centrally planned economies.
 - c. will likely be eliminated by technological progress.
 - d. exists only in poor nations.
 - e. occurs if there are insufficient resources to provide for human wants.

ANS: E PTS: 1

12. The fundamental economic problem is:
- a. poverty.
 - b. unemployment.
 - c. scarcity.
 - d. government intervention into markets.
 - e. inflation.

ANS: C PTS: 1

13. Which of the following is an example of an individual motivated by self-interest?
- a. a student volunteering at a soup kitchen
 - b. an attorney providing free legal service to low income families
 - c. a young person volunteering for the Peace Corps
 - d. a man buying a new Camaro
 - e. all of the above

ANS: E PTS: 1

14. Scarcity, as defined by an economist, means:
- a. demand exceeds supply at the current market price.
 - b. consumers are too poor to purchase the available goods and services.
 - c. supply exceeds demand at the current market price.
 - d. the desire for goods exceeds our ability to produce them with limited available resources.

ANS: D PTS: 1

15. Which of the following statements are true?
- a. Scarcity refers to shortages at existing market prices.

- b. As a result of scarcity, individuals must make choices and face trade-offs.
- c. It is impossible to satisfy unlimited human wants with limited resources.
- d. All of the above are true statements.
- e. Only b. and c. are true statements.

ANS: E PTS: 1

16. In order to determine if a hypothesis is valid we must utilize
- a. qualitative analysis.
 - b. empirical analysis.
 - c. marginal analysis.
 - d. average analysis.
 - e. production analysis.

ANS: B PTS: 1

17. Economics is primarily the study of:
- a. how choices are made because of scarcity.
 - b. corporate balance sheets and income statements.
 - c. how to operate a business.
 - d. how to make money in the stock market.
 - e. how to allocate scarce resources to satisfy unlimited needs.

ANS: A PTS: 1

18. When economists say goods are scarce, they mean that:
- a. consumers do not have enough money to purchase the goods.
 - b. the desire for goods and services exceeds our ability to produce them with limited resources.
 - c. at the current price, consumers are willing to buy more of a good than suppliers are willing to produce.
 - d. government programs are needed to lift families out of poverty.

ANS: B PTS: 1

19. Economics is concerned with:
- a. the choices people must make because resources are scarce.
 - b. human decision makers and the factors that influence their choices.
 - c. the allocation of limited resources to satisfy virtually unlimited desires.
 - d. all of the above.

ANS: D PTS: 1

20. Scarcity is:
- a. only a problem in modern industrialized economies.
 - b. only a problem in impoverished economies.
 - c. only a problem in centrally planned economies.
 - d. a word meaning that there is a shortage of goods at the current market price.
 - e. a problem that necessitates making choices and tradeoffs.

ANS: E PTS: 1

21. Scarcity means that:
- a. there will always be families living below the poverty line.
 - b. resources are unlimited.
 - c. human wants are limited.

- d. limited resources cannot satisfy all of our unlimited human wants.
- e. choices are unnecessary.

ANS: D PTS: 1

22. Economics is the study of how people cope with:

- a. fluctuations in stock prices.
- b. greed.
- c. limited human wants.
- d. limited resources.

ANS: D PTS: 1

23. A "scarce" good is a good:

- a. for which it is impossible to increase production any further given the available resources and technology.
- b. for which there is a shortage at the current market price.
- c. that is always in demand at any price.
- d. for which available resources are insufficient to satisfy unlimited human desires for it.
- e. that cannot be produced using mass production techniques.

ANS: D PTS: 1

24. Fundamentally, economics is concerned with:

- a. how scarce resources are allocated to satisfy limited wants.
- b. how limited resources are allocated to satisfy scarce wants.
- c. how limited resources are allocated to satisfy unlimited wants.
- d. how limited wants can be used to satisfy limited resources.
- e. how unlimited wants can be used to satisfy unlimited resources.

ANS: C PTS: 1

25. By the study of "scarcity," an economist means how we best utilize our:

- a. limited resources in order to promote full employment and price stability.
- b. unlimited desires in order to best use our unlimited resources.
- c. unlimited resources to best satisfy our unlimited desires.
- d. limited resources in order to best satisfy our unlimited desires.
- e. unlimited resources in order to best satisfy our limited desires.

ANS: D PTS: 1

26. Scarcity would cease to exist as an economic problem if:

- a. we learned to cooperate and not compete with each other.
- b. there were new discoveries of an abundance of natural resources.
- c. output per worker increased.
- d. none of the above.

ANS: D PTS: 1

27. In economic terms, religious and spiritual services are treated as:

- a. goods that people desire.
- b. resources or inputs.
- c. marginal benefits.
- d. *priceless* commodities.

ANS: A PTS: 1

28. Economics is primarily concerned with the study of:
- a. problems such as poverty and unemployment.
 - b. limited desires pursuing unlimited resources.
 - c. production and distribution of goods in a world of unlimited resources.
 - d. production and distribution of goods in a world of limited resources.
 - e. the evolution of firms from small startups to successful corporations.

ANS: D PTS: 1

29. Economics is a science that:
- a. typically uses controlled experiments to learn about consumer and firm behavior.
 - b. uses models that cannot be tested empirically due to the complex nature of the economy.
 - c. explores how choices are made between conflicting wants and desires in a world of scarcity.
 - d. relies entirely upon normative analysis.
 - e. primarily focuses on budgetary decisions made by political leaders.

ANS: C PTS: 1

30. Economics:
- a. is a natural science like biology and chemistry.
 - b. is composed of two main branches known as positive and normative economics.
 - c. is a science concerned with reaching generalizations about human behavior, not unlike sociology or psychology.
 - d. is concerned with predicting business conditions in the future, not with the current state of the stock market.
 - e. is concerned with firm behavior, not human behavior.

ANS: C PTS: 1

31. The real core of the economic problem is to:
- a. increase the amount of leisure time available to people.
 - b. guarantee everyone on the planet a minimum level of food, shelter and clean water.
 - c. allocate limited resources among competing uses.
 - d. eliminate scarcity.

ANS: C PTS: 1

32. Understanding economics would be helpful to which of the following individuals?
- a. a college student planning her next semester courses
 - b. an engineer building a superhighway
 - c. a fashion designer selecting fabric for a new spring collection
 - d. a restaurant owner deciding whether to expand his establishment's hours of operation
 - e. All of the above.

ANS: E PTS: 1

33. *Ceteris paribus* if the price of cell phones increases we would expect that consumers would want to buy
- a. fewer cell phones because of the higher price.
 - b. more cell phones because of the higher price.
 - c. fewer cell phones because of improved technology of other goods.
 - d. more cell phones because of improved wireless coverage areas and speed

ANS: A PTS: 1

34. Economics:
- a. is a narrowly focused discipline.
 - b. is a broad-ranging, problem-solving discipline.
 - c. concerns itself only with monetary decisions.
 - d. says very little about "everyday life."
 - e. deals strictly with business management decisions.

ANS: B PTS: 1

35. Which of the following are likely to be studied in a microeconomics course?
- a. choices made by individual consumers
 - b. the production decisions made by individual firms
 - c. how the economy's total output is measured
 - d. how an increase in government spending affects the level of unemployment
 - e. Both a. and b. are likely to be studied in a microeconomics course.

ANS: E PTS: 1

36. Economic decisions are made:
- a. only at the management level of corporations.
 - b. only by government leaders.
 - c. only where monetary exchanges take place.
 - d. in both the private and public sectors.

ANS: D PTS: 1

37. The basic difference between macroeconomics and microeconomics is:
- a. microeconomics concentrates on individual markets while macroeconomics focuses primarily on international trade.
 - b. microeconomics concentrates on the behavior of individual consumers while macroeconomics focuses on the behavior of firms.
 - c. microeconomics concentrates on the behavior of individual consumers and firms while macroeconomics focuses on the performance of the entire economy.
 - d. microeconomics explores the causes of inflation while macroeconomics focuses on the causes of unemployment.

ANS: C PTS: 1

38. Economics can be divided into two main branches of study:
- a. capitalism and communism.
 - b. capitalism and socialism.
 - c. demand and supply.
 - d. microeconomics and macroeconomics.
 - e. fiscal policy and monetary policy.

ANS: D PTS: 1

39. Which of the following is most likely a topic of discussion in macroeconomics?
- a. an increase in the price of a pizza
 - b. a decrease in the production of VCRs by a consumer electronics company
 - c. an increase in the wage rate paid to automobile workers
 - d. a decrease in the unemployment rate
 - e. the entry of new firms into the software industry

ANS: D PTS: 1

40. Which of the following is an example of microeconomic analysis?
- a. impact of taxation on national income
 - b. impact of national income on tax revenues
 - c. rate of increase in the national debt
 - d. relationship between inflation and interest rates set by the Federal Reserve
 - e. none of the above

ANS: E PTS: 1

41. The branch of economics that studies the aggregate decisions of all households and all firms is called:
- a. positive economics.
 - b. normative economics.
 - c. microeconomics.
 - d. macroeconomics.
 - e. environmental economics.

ANS: D PTS: 1

42. Which of the following statements most likely lies within the realm of microeconomics?
- a. Unemployment rises during a recession and falls during an expansion.
 - b. A rapid acceleration of the supply of money may create inflation.
 - c. An increase in government spending will increase the aggregate demand for goods and services in the economy.
 - d. An increase in labor costs will increase the additional cost of producing another airplane.
 - e. A decrease in federal income tax rates will stimulate increased consumer spending.

ANS: D PTS: 1

43. Which of the following statements most likely lies within the realm of macroeconomics?
- a. An increase in the price of automobiles will lead to a decrease in the quantity of automobiles demanded.
 - b. Due to process innovations in computer chip manufacturing, the market supply of computers increased.
 - c. Due to an economic recession, manufacturing firms began implementing layoffs of their workforces.
 - d. Anticipating that the benefits would outweigh costs involved, an undergraduate student purchases the course textbook.
 - e. A consumer electronics firm found that it could minimize its losses by shutting down its operations altogether.

ANS: C PTS: 1

44. Most people consider economics a(n):
- a. social science.
 - b. physical science.
 - c. accounting science.
 - d. earth science.
 - e. anthropological science.

ANS: A PTS: 1

45. Macroeconomic topics do not usually include:
- a. the rate of inflation.
 - b. the rate of unemployment.

- c. economic growth.
- d. the profit maximizing decisions of an individual manufacturer.
- e. the control of the money supply by the central bank.

ANS: D PTS: 1

46. Which of the following lies primarily within the realm of microeconomics?
- a. an empirical analysis of the relationship between the growth of the money supply and the rate of inflation
 - b. an economic model forecasting the impact of a tax increase on consumer spending and national output
 - c. a study of supply and demand conditions in the market for orange juice
 - d. a model forecasting the impact of a change in interest rates on the level of investment in the economy

ANS: C PTS: 1

47. Which of the following lies primarily within the realm of macroeconomics?
- a. a study of the elasticity of demand for gasoline
 - b. a study of how tax cuts stimulate aggregate production
 - c. an analysis of supply and demand conditions in the electricity market
 - d. a study of the impact of "mad cow" disease on the price of beef worldwide

ANS: B PTS: 1

48. Which of the following is most likely a topic of discussion in a microeconomics course?
- a. a decrease in the share of national income paid to the government in taxes
 - b. an increase in the price of lumber used to construct houses
 - c. an increase in the rate of inflation
 - d. an increase in the number of jobless individuals filing unemployment claims
 - e. the size of the national debt

ANS: B PTS: 1

49. The basic difference between macroeconomics and microeconomics is that:
- a. microeconomics looks at the forest (aggregate markets) while macroeconomics is concerned with the trees (individual markets).
 - b. macroeconomics is concerned with policy decisions while microeconomics applies only to theory.
 - c. microeconomics is concerned with the trees (individual markets) while macroeconomics is concerned with the forest (aggregate markets).
 - d. macroeconomics is concerned with positive economics while microeconomics is concerned with normative economics.

ANS: C PTS: 1

50. The branch of economics that focuses on outcomes in highly aggregated markets, such as the markets for labor or consumer products, is called:
- a. macroeconomics.
 - b. Marxian economics.
 - c. positive economics.
 - d. normative economics.
 - e. microeconomics.

ANS: A PTS: 1

51. The branch of economics that focuses on the conduct of affairs within narrowly defined units, such as households or business firms, is called:
- a. macroeconomics.
 - b. microeconomics.
 - c. socioeconomics.
 - d. applied economics.
 - e. market economics.

ANS: B PTS: 1

52. Microeconomic topics do not usually include:
- a. how wages are determined in the labor market.
 - b. the magnitude of national income.
 - c. how firms choose output to maximize profits.
 - d. how consumers maximize utility subject to a budget constraint.
 - e. the monopolization of an industry by a single firm.

ANS: B PTS: 1

53. The branch of economics that studies the economy as a whole is:
- a. normative economics.
 - b. positive economics.
 - c. microeconomics.
 - d. macroeconomics.
 - e. global economics.

ANS: D PTS: 1

54. Macroeconomics:
- a. is narrower in scope than microeconomics.
 - b. analyzes mergers and acquisitions between firms.
 - c. is concerned with the expansion and contraction of the overall economy.
 - d. is concerned with the expansion of a small sole proprietorship into a large corporation.
 - e. is primarily concerned with the decisions of individual households.

ANS: C PTS: 1

55. Microeconomic topics do not usually include:
- a. the regulation of monopoly firms.
 - b. the impact of large government budget deficits on private investment spending.
 - c. the determinants of the supply of wheat by farmers.
 - d. the determinants of the demand for DVD players by consumers.
 - e. the impact of a change in the price of leather used to manufacture shoes.

ANS: B PTS: 1

56. Macroeconomic topics do not generally include:
- a. inflation.
 - b. aggregate demand.
 - c. government spending and taxation.
 - d. the production decisions of individual firms.
 - e. the measurement of total economic output.

ANS: D PTS: 1

57. Measuring the rate of inflation is primarily a concern of:

- a. positive economics.
- b. normative economics.
- c. microeconomics.
- d. macroeconomics.
- e. accounting.

ANS: D PTS: 1

58. The determination of prices in the market for automobiles is primarily a concern of:

- a. positive economics.
- b. normative economics.
- c. microeconomics.
- d. macroeconomics.
- e. accounting.

ANS: C PTS: 1

59. Microeconomics:

- a. provides an overall view of the economy and how it functions.
- b. explores the behavior of individual consumers and firms when confronted with scarcity.
- c. examines the aggregate behavior of consumers and firms when confronted with scarcity.
- d. is a "positive" science, whereas macroeconomics is a "normative" science.
- e. is concerned with full employment, price stability and economic growth.

ANS: B PTS: 1

60. Microeconomics primarily models:

- a. the overall economy.
- b. the behavior of firms but not households.
- c. the behavior of households but not firms.
- d. the behavior of both firms and households and how they interact in the marketplace.
- e. how the government balances the federal budget.

ANS: D PTS: 1

61. Macroeconomics primarily examines:

- a. the behavior of individual households and firms.
- b. how prices are determined within individual markets.
- c. the output levels that maximize the profits of business firms.
- d. broad issues such as national output, employment and inflation.
- e. the consumption decisions of individual households.

ANS: D PTS: 1

62. Microeconomics differs from macroeconomics in that:

- a. microeconomics studies individual decision making while macroeconomics examines aggregate decision making.
- b. microeconomics studies aggregate decision making while macroeconomics examines individual decision making.
- c. microeconomics utilizes positive economic analysis while macroeconomics utilizes normative economic analysis.
- d. microeconomics is concerned with consumer behavior while macroeconomics is concerned with firm behavior.
- e. There is no difference between microeconomics and macroeconomics.

ANS: A PTS: 1

63. When economists assume that people act rationally, it means they:
- a. make decisions based on complete and accurate information.
 - b. make decisions that will not be regretted later on.
 - c. make decisions based on what they believe is best for themselves using available information.
 - d. make decisions based solely on what is best for society.
 - e. commit no errors in judgment.

ANS: C PTS: 1

64. Most of economic analysis assumes that people's actions are:
- a. motivated by submerged emotional needs.
 - b. driven by magnetic forces generated by planetary movements.
 - c. motivated primarily by concern for the well-being of others.
 - d. motivated by self-interest.
 - e. motivated purely by money.

ANS: D PTS: 1

65. Which of the following is not an example of the use of the problem solving perspective provided by economics?
- a. An investor considers the tax consequences of selling stocks in order to buy bonds (which she believes offer a better return).
 - b. A rancher recognizes that raising more cattle this year will damage his pasture and limit next year's herd size.
 - c. The Fogelberg family takes its vacation at Lake Arrowhead this year simply because they have done so for as long as anyone can remember.
 - d. An economics student contemplates the other subjects that she should be studying before deciding to study economics this evening.

ANS: C PTS: 1

66. Economists believe that individuals act as if they are motivated by self-interest and:
- a. respond selfishly.
 - b. respond in predictable ways to changing circumstances.
 - c. it leads to inconsistent and unpredictable behavior.
 - d. all of the above.

ANS: B PTS: 1

67. From an economists' perspective, which of the following observations is not true?
- a. Self-interest is purely monetary in nature.
 - b. Self-interest can include benevolence.
 - c. Self-interest is a good predictor of human behavior in most situations.
 - d. Self-interest is not the same as selfishness.

ANS: A PTS: 1

68. When economists refer to economic behavior, they mean that:
- a. from time to time, everyone behaves irrationally.
 - b. changes in incentives influence behavior in unpredictable ways.
 - c. the pursuit of money is the most significant factor influencing decision making.
 - d. rational people try to anticipate the likely consequences of their actions.

ANS: D PTS: 1

69. When making decisions, economists believe that individuals act rationally if they:
- a. seek to improve their own situations and not try to anticipate future consequences of their actions.
 - b. only pursue the goals of the community.
 - c. try to anticipate future consequences and seek to improve their own situations.
 - d. always choose alternatives that offer the greatest financial reward.
 - e. do either c. or d.

ANS: C PTS: 1

70. Economists believe that individuals act as if they are motivated:
- a. primarily by the opinions of their peers.
 - b. primarily by human feelings.
 - c. primarily by self-interest.
 - d. only by concern for the larger community.
 - e. by none of the above.

ANS: C PTS: 1

71. What according to an economist, forms the basis of rational human behavior under current and anticipated future circumstances?
- a. Scarcity and rarity
 - b. Opportunities and pay-offs
 - c. Values and information
 - d. Legal consequences

ANS: C PTS: 1

72. A person behaving rationally will attempt to:
- a. always avoid illegal actions.
 - b. explain or rationalize a decision.
 - c. refrain from normative analysis.
 - d. consider the future consequences of her/his behavior.
 - e. refrain from positive economic analysis.

ANS: D PTS: 1

73. "As a rational person, you would expect individuals to always avoid actions that are illegal."
- a. This is a true statement because most people don't want to suffer the penalties associated with criminal behavior.
 - b. This is a true statement because most individuals are good citizens and prefer not to commit crimes.
 - c. This is a false statement because it is expected that individuals will consider the consequences of their actions and that some will choose to commit illegal acts anyway.
 - d. This is a false statement because only people with certain genetic predispositions are likely to commit crimes.

ANS: C PTS: 1

74. An economic hypothesis is tested:
- a. by assessing the realism of its assumptions.
 - b. by comparing the hypothesis's predictions to real-world data.
 - c. most frequently by using a controlled experiment.
 - d. by assessing the level of descriptive detail.

e. by none of the above. Economic hypotheses are theoretical and therefore cannot be tested.

ANS: B PTS: 1

75. Difficulty in prediction social sciences is the result of analyzing ____ but can be overcome by focusing on ____ groups.

- a. experiments; small groups
- b. experiments; large groups
- c. human behavior; small groups
- d. human behavior; large groups

ANS: D PTS: 1

76. An economic theory:

- a. should be as detailed as possible in order to model the complexity of an economy.
- b. is an abstraction from reality.
- c. is only useful if it rests on realistic assumptions.
- d. is unrealistic and therefore of dubious usefulness in explaining what occurs in a complex economy.

ANS: B PTS: 1

77. A good economic theory:

- a. rests on realistic assumptions.
- b. explains economic behavior and predicts well.
- c. can best be expressed mathematically.
- d. always provides a highly detailed analysis of an economic sector.

ANS: B PTS: 1

78. A good economic theory:

- a. includes every detail that affects the economic behavior of interest.
- b. relies on simplifying assumptions in order to explain economic behavior.
- c. does not rely on simplifying assumptions.
- d. is impossible to achieve because of the difficulty of conducting controlled experiments.
- e. is normative and therefore not testable.

ANS: B PTS: 1

79. Economics is different from a "hard" science like physics because:

- a. economists abstract from reality in creating their theories.
- b. economics is easier to study than physics.
- c. economists must explain their theories to policy makers who lack formal mathematical training.
- d. economists cannot easily control all the variables that might influence human behavior.
- e. research in economics is primarily conducted in a very "social" way via interviews of consumers and corporate leaders.

ANS: D PTS: 1

80. An economic hypothesis:

- a. can be tested using empirical analysis.
- b. can be tested using normative analysis.
- c. cannot be tested since it is normative in nature.
- d. cannot be tested since it is a positive economic statement.

ANS: A PTS: 1

81. A hypothesis is:
- a normative economic statement.
 - a testable proposition.
 - a statement that cannot be evaluated using real-world data.
 - a model with no connection to the real world.

ANS: B PTS: 1

82. A theory can best be defined as:
- an untestable assertion or statement of untestable fact.
 - a testable statement that can be definitively proven to be true or false using empirical analysis.
 - a normative statement that can be tested empirically through analysis of real-world data.
 - a deliberate simplification of factual relationships that attempts to explain and predict how those relationships work.

ANS: D PTS: 1

83. Which of the following statements is most accurate?
- The terms scarcity and shortage refer to the same concept.
 - Scarcity can and will be eliminated in the short run.
 - Scarcity can and will be eliminated in the long run.
 - Scarcity cannot be eliminated in any time frame.

ANS: C PTS: 1

84. Which of the following is correct?
- "Theory" and "hypothesis" are interchangeable terms meaning the same thing.
 - A hypothesis may result from a tested and confirmed theory.
 - A theory may result from a tested and confirmed hypothesis.
 - A hypothesis is a theory whose formulation relies on mathematics.

ANS: C PTS: 1

85. Economists use theories to:
- abstract from the complexities of the world.
 - understand economic behavior.
 - explain and help predict human behavior.
 - do all of the above.

ANS: D PTS: 1

86. An economic theory is tested by:
- assessing the realism of its assumptions.
 - polling economists to see if there is consensus as to the validity of the hypothesis.
 - comparing and contrasting its simplicity with related theories.
 - comparing its predictions with real-world data.

ANS: D PTS: 1

87. The best test of an economic theory is:
- the rigor of its mathematical formulation.
 - its ability to explain and predict.
 - the accuracy of its assumptions.

d. the level of real-world detail it captures.

ANS: B PTS: 1

88. Economists need to develop abstractions in order to:
- avoid analyzing real-world economic interactions, which are too complicated to understand.
 - distinguish normative economic behavior from positive economic behavior.
 - avoid committing the fallacy of composition.
 - understand and explain economic behavior.
 - justify their salaries, much in the way lawyers speak and write in "legalese."

ANS: D PTS: 1

89. What is the difference between a theory and a hypothesis?
- A hypothesis abstracts from reality while a theory describes reality.
 - A theory abstracts from reality while a hypothesis describes reality.
 - A theory is an established explanation.
 - A hypothesis is not an established explanation.
 - both c. and d. above

ANS: E PTS: 1

90. Identify the chain of events in creating a theory:
- gather data, evaluate results, tentatively accept the theory, support or refute the hypothesis.
 - predict behavior, evaluate the results, formulate a hypothesis.
 - select a theory, create a hypothesis, evaluate the evidence.
 - formulate a hypothesis, gather data, evaluate the results, support or refute the hypothesis, tentatively accept theory.

ANS: D PTS: 1

91. An economist at the University of Alaska at Anchorage has been asked to explain why the price of Alaskan crude oil has fallen recently. In order to assemble a scholarly answer, the professor should take which steps?
- Develop a hypothesis, test the proposition by engaging in empirical analysis, and examine the data to see if it fits with the facts.
 - Gather data on crude oil prices and seemingly unrelated variables in order to look for associations, then formulate a hypothesis based on those unexpected associations.
 - Ask people in Alaska why they are not purchasing oil.
 - None of the above. The oil industry is controlled by a cartel; therefore price changes in the industry cannot be explained using economic theories.

ANS: A PTS: 1

92. An economist might hypothesize that people will buy less gasoline at a price of \$3.00 per gallon than at \$2.50 per gallon. In order for the hypothesis to become a theory, it would have to be tested. Which of the following observations would seem to support this hypothesis?
- People in each region buy the same amount of gasoline regardless of the price.
 - Gasoline consumption varies with the quantity of cars purchased in each region.
 - Individuals line up to purchase more gasoline at higher prices with the expectation that the fuel will be of higher quality.
 - Individuals in each region respond to an increase in price by purchasing less gasoline.

ANS: D PTS: 1

93. When economists use the term "*ceteris paribus*," they mean that:
- a. the causal relationship between two economic variables cannot be determined.
 - b. the analysis is true for the individual but not for the economy as a whole.
 - c. all other variables except the ones specified are assumed to be constant.
 - d. their conclusions are based on normative rather than positive economic analysis.

ANS: C PTS: 1

94. The term "*ceteris paribus*" means that:
- a. everything is variable.
 - b. all variables except those specified are constant.
 - c. no one knows which variables will change and which will remain constant.
 - d. what is true for the individual is not necessarily true for the whole.
 - e. all variables are held constant.

ANS: B PTS: 1

95. Economists use the term "*ceteris paribus*" to indicate that:
- a. the analysis is true for the individual but not for the economy as a whole.
 - b. supply and demand are in balance.
 - c. their conclusions are based on normative rather than positive economic analysis.
 - d. other things are assumed to remain constant.

ANS: D PTS: 1

96. "*Ceteris paribus*" means:
- a. if events A and B occur together, one must cause the other.
 - b. all relevant details are included.
 - c. what is true for the individual must be true for the whole.
 - d. holding other things constant.
 - e. association does not imply causation.

ANS: D PTS: 1

97. The importance of the *ceteris paribus* assumption is that it:
- a. allows one to separate normative economic issues from positive economic ones.
 - b. allows one to generalize from the whole to the individual.
 - c. allows one to analyze the relationship between two variables apart from the influence of other variables.
 - d. allows one to hold all variables constant so the economy can be carefully observed in a suspended state.

ANS: C PTS: 1

98. A theory asserts that manufacturers are less willing to sell units of output as the price of a good decreases. However, as the price of computers fell throughout the 1990s, more computers were sold. Which of the following best explains the apparent conflict between theory and data?
- a. The theory must be invalid.
 - b. The theory rests on assumptions that are too simplistic.
 - c. It is likely that variables other than the price and quantity of computers sold were changing.
 - d. All variables other than the price and quantity of computers sold were unchanged.

ANS: C PTS: 1

99. A theory asserts that consumers will purchase less of a good at higher prices than they will at lower prices. However, when the average price of cars increased throughout the 1990s, more cars were purchased. Which of the following best explains the apparent conflict between theory and data?
- The *ceteris paribus* assumption is valid.
 - It is likely that variables other than the price and quantity of cars demanded were changing.
 - The theory is valid. However, the price and quantity data gathered by researchers was clearly measured incorrectly.
 - The theory must be invalid.

ANS: B PTS: 1

100. Which factor best explains the increased level of difficulty in observation and prediction in the social sciences than in physical sciences?
- Abstraction
 - Fallacy of composition
 - Scarcity
 - Self-interest
 - Human behavior

ANS: E PTS: 1

101. A leading game-console manufacturer slashes the price of its flagship product by ten percent. Holding other things such as income and preferences constant, which of the following is the most likely group behavior prediction?
- Price reduction will have no impact on purchase patterns.
 - Price reduction will be associated with a reduction in quality; thereby reducing sales.
 - More game consoles will be sold at lower prices.
 - Group behavior cannot be predicted.

ANS: C PTS: 1

102. A scientist trying to test a theory about the relationship between people's consumption of alcohol and their longevity would want to hold all of the following variables constant except ____:
- the amount of alcohol that people in the experimental group consumed.
 - the amount of cigarettes that people in the experimental group smoked.
 - the amount of dietary fat that people in the experimental group consumed.
 - past histories of heart and lung disease.

ANS: A PTS: 1

103. Which of the following statements can explain why an association between Event A and Event B may not imply causality from A to B?
- The observed association may be coincidental.
 - There may be a third variable that is responsible for causing both events.
 - Causality may run from Event B to Event A instead of in the opposite direction.
 - All of the above can explain why an association between Event A and Event B may not imply causality from A to B.

ANS: D PTS: 1

104. In the discussion of correlation and causation, correlation means:
- two sets of phenomena may be related, but one does not necessarily cause the other.
 - two sets of phenomena are not related and one may in fact cause the other.
 - that when two phenomena are repeatedly observed together, one must cause the other.

- d. that if a groundhog sees his shadow in February, this phenomena causes there to be six more weeks of bad weather.

ANS: A PTS: 1

105. If individuals who sit in the back of the classroom receive lower grades on average than the rest of the class, does that mean that sitting in the back of a classroom causes one to perform poorly on exams?
- a. Not necessarily. The reoccurrence of a certain relationship between two variables does not necessarily imply causation.
 - b. It is not possible for an economist to determine causation between variables.
 - c. The reoccurrence of such a relationship is sufficient evidence that sitting in the back of a classroom will lead to lower grades.
 - d. The reoccurrence of such a relationship is sufficient evidence that students who receive low grades prefer to keep a low profile and always sit in the back of the classroom.

ANS: A PTS: 1

106. If two variables appear to be causally related, it is possible that:
- a. they are indeed related.
 - b. the two variables appear related by sheer coincidence.
 - c. causation may run in the opposite direction.
 - d. an additional correlated factor may be the source of the causality.
 - e. all of the above are possible answers.

ANS: E PTS: 1

107. Ten-year-old Josh observes that people who play football are larger than normal and tells his mom that he's going to play football because it will make him big and strong. Josh is:
- a. committing the fallacy of composition.
 - b. violating the *ceteris paribus* assumption.
 - c. mistaking correlation for causation.
 - d. committing the fallacy of decomposition.

ANS: C PTS: 1

108. Many people have heard that the stock market rises when a team from the National Football Conference (NFC) wins the Super Bowl, and falls when a team from the American Football Conference (AFC) is victorious. If you conclude that there is a causal relationship between the outcome of the Super Bowl and stock prices, you probably are:
- a. confusing correlation with causation.
 - b. violating the *ceteris paribus* assumption.
 - c. committing the fallacy of composition.
 - d. confusing the direction of causality, since everyone knows that stock prices determine which team wins the Super Bowl.

ANS: A PTS: 1

109. A student football team manager examined variables influencing the team's record and concluded that the best scores resulted when the "third-string" team played the most minutes. Therefore he recommended that the third-string team become the first team. This conclusion was probably erroneous because the manager has:
- a. confused positive and normative analysis.
 - b. committed the fallacy of composition.
 - c. failed to recognize that correlation is not causation.
 - d. incorrectly analyzed the direction of causation.

ANS: D PTS: 1

110. If rain dancing is associated with rain, does that necessarily mean rain dancing causes rain?
- a. No. This is an example of a failure to properly employ the *ceteris paribus* assumption.
 - b. If it rains after individuals have engaged in rain dancing then there is certainly causation at work.
 - c. No. This is an example of the fallacy of composition.
 - d. No. Two variables may be correlated without one necessarily causing the other.
 - e. No. This is an example of a failure to understand the difference between positive and normative economic analysis.

ANS: D PTS: 1

111. "When one basketball team spends a large sum of money acquiring better players, it is better off. If all teams do the same thing, all of them are better off." These statements demonstrate:
- a. the fallacy of composition.
 - b. confusing association with causation.
 - c. a misunderstanding of the direction of causality.
 - d. the *ceteris paribus* condition.

ANS: A PTS: 1

112. Which of the following best illustrates the fallacy of composition?
- a. If Mr. Smith had more money, he could buy more scarce goods; if the Adams family had more money, it could buy additional goods.
 - b. If Ms. Spann had more money, she could buy more scarce goods; if the nation had more money, everyone could buy more scarce goods.
 - c. If other variables are not held constant, economists may not observe the relationship between price and quantity demanded that is expected.
 - d. Aggregate consumption may not behave in the same manner as the consumption of a particular individual.

ANS: B PTS: 1

113. The fallacy of composition is:
- a. the erroneous view that an economic activity can sometimes exceed the sum of its components.
 - b. the erroneous view that what is true for the individual will also be true for the group.
 - c. the view that the aggregation of economic activity will necessarily lead to an outcome that is different than the outcome generated by each individual in the group.
 - d. the idea that association need not imply causation.
 - e. the failure to hold other variables constant when analyzing the relationship between two particular variables.

ANS: B PTS: 1

114. Which of the following best illustrates the fallacy of composition?
- a. If I stand up at a baseball game I will be able to see the game better; if all fans stood up at a baseball game they would all be able to see the game better.
 - b. If I wore a jacket to a baseball game in October, I would be warmer; if all fans wore jackets they would all be warmer.
 - c. If I purchase fewer concessions at a baseball game, I will save money; if all fans purchase fewer concessions then all can save money.
 - d. If I yell more during a baseball game it will be louder if all fans yell more during the game it will be much louder.

ANS: A PTS: 1

115. The fallacy of composition is the erroneous view that:
- a. an increase in the supply of money will cause a general increase in the level of prices.
 - b. a small change in an economic variable will have an unrecognizable but significant effect on the economy.
 - c. when two events are associated, the one observed first must have caused the second.
 - d. if something is true for an individual, then it must also be true for a group.

ANS: D PTS: 1

116. Which of the following best illustrates the fallacy of composition?
- a. If the price of a product rises, the quantity supplied will decline.
 - b. The average wage rate tends to increase at approximately the same rate as inflation; hence, wage increases must cause inflation.
 - c. Resources are scarce; therefore, there is no such thing as a free lunch.
 - d. If I talk loudly at a party, I have a better chance of being heard by my listeners. If everyone at the party talks loudly, everyone can be heard more clearly.

ANS: D PTS: 1

117. Which of the following best illustrates the fallacy of composition?
- a. I hate driving to work when the traffic is so heavy, so I decide to leave 30 minutes earlier than in the past. If everyone were to leave 30 minutes earlier for work, we'd all get to work faster.
 - b. A great many people have been immunized against polio because it can be such a devastating disease. As a result, I probably do not personally need to be immunized against polio.
 - c. Whenever I attend a baseball game at the local stadium, the home team wins. Therefore, if I attend all of the team's local games, they will achieve a perfect winning record at home.
 - d. The parking at Ohio State University is in short supply on the main campus. It would be better for more people to ride the bus to school.

ANS: A PTS: 1

118. If U.S. consumers bought more gasoline in 2008 (when prices averaged \$3.22 per gallon) than they did in 1970 (when prices averaged \$0.30 per gallon), does that mean that people buy more gasoline at higher prices?
- a. No, because 1970 prices are ancient history compared to 2001 prices.
 - b. No, because there is too little information provided about inflation, consumer income and other variables to make an appropriate comparison.
 - c. Yes, because gas is a necessity that is in short supply. Consumers are always willing to buy more gasoline-even at higher prices.
 - d. Yes, because gasoline is a luxury good that consumers willingly purchase - even at higher prices.

ANS: B PTS: 1

119. The fallacy of composition is essentially the error of:
- a. confusing association with causation.
 - b. confusing normative economics with positive economics.
 - c. generalizing from the individual to the whole.
 - d. omitting relevant variables from an economic model.
 - e. generalizing from the whole to the individual.

ANS: C PTS: 1

120. "I woke up earlier today to beat other fishermen to the fish and yet I caught the same number of fish at 5 a.m. as I did at noon." Which of the following best explains this occurrence?
- a. Many other fishermen also believe that they can catch a greater quantity of fish if they arrive earlier at the fishing area. So the area is crowded early in the day.
 - b. The fish do not care when they eat, so they are likely to bite on the bait at any time during the day.
 - c. The catching of fish is mostly luck, so timing is not important.
 - d. The early bird catches the worm.

ANS: A PTS: 1

121. In a congressional debate about agricultural price supports, senators, members of congress, and other experts made the following four statements. Which of these is a normative statement?
- a. "Price supports are important because America should preserve the small family farm."
 - b. "Without price supports, the price of wheat and corn will fall by over twenty percent."
 - c. "The decline in commodity prices caused by the removal of price supports will result in fewer, larger farms."
 - d. "The decline in commodity prices caused by the removal of price supports will reduce the number of tractors sold in the United States."

ANS: A PTS: 1

122. Your mother tells you, "Watching ten hours of TV per day will make you stupid." This is a positive statement because:
- a. your mother says it with a positive tone in her voice.
 - b. it is your mother's opinion.
 - c. it is a proposition that can be tested.
 - d. your mother is only thinking of your best interest.

ANS: C PTS: 1

123. Suppose there are two members of the U.S. Congress who were once economics professors. Why is it important to be able to distinguish their positive from their normative statements about economic policy?
- a. Their positive statements help us understand the economy's response to a particular policy, while their normative statements reflect their value judgments.
 - b. Their positive statements help us understand the good results of a policy change, and their normative statements help us understand the negative results.
 - c. We really do not have to worry about them since trained economists never make normative statements.
 - d. Economists are always making assumptions, and policy should not be based on assumptions.
 - e. Economists are "tricky" by nature, so we need to be able to distinguish truth from political rhetoric.

ANS: A PTS: 1

124. Positive statements are:
- a. prescriptive, making claims about how the world ought to be.
 - b. descriptive, making claims about how the world is.
 - c. optimistic, putting the best possible interpretation on things.
 - d. affirmative, justifying existing economic policy.

ANS: B PTS: 1

125. Normative statements are:
- prescriptive, making claims about how the world ought to be.
 - descriptive, making claims about how the world is.
 - optimistic, putting the best possible interpretation on things.
 - statements that establish production goals for the economy.

ANS: A PTS: 1

126. Which of the following is a positive statement?
- The average high temperature in Miami, Florida in February is lower than the average high temperature in Chicago, Illinois.
 - An increase in cigarette smoking will lead to a decrease in the likelihood of getting lung cancer.
 - 30 minutes of exercise three or more times per week will decrease the occurrence of heart disease.
 - all of the above

ANS: D PTS: 1

127. Which of the following represents a normative statement?
- A decrease in price leads to an increase in quantity demanded.
 - The temperature outside is 90 degrees.
 - The study of economics is more important than the study of history.
 - People will buy less butter at \$1.50 per pound than they will at \$1.00 per pound.
 - As an economy develops, the nation's birth rate tends to fall.

ANS: C PTS: 1

128. Which of the following is a statement of positive economics?
- New tax laws are needed to help the poor.
 - Teenage unemployment should be reduced.
 - We should increase Social Security payments to the elderly.
 - An increase in tax rates will reduce unemployment.
 - It is only fair that firms that are protected from competition by government-granted monopolies pay higher corporate taxes.

ANS: D PTS: 1

129. "The government should levy higher taxes on the rich and use the additional revenues to provide better housing for the poor." This statement illustrates:
- the fallacy of composition.
 - the basic principle of economics.
 - a normative economic statement.
 - a positive economic statement.
 - ceteris paribus*.

ANS: C PTS: 1

130. "The minimum wage should be increased so that low-income workers can afford to feed their families." This is an example of:
- a positive economic statement.
 - a negative economic statement.
 - the fallacy of composition.

- d. a normative economic statement.
- e. confusing correlation with causation.

ANS: D PTS: 1

131. "A reduction in the rate at which stock dividends are taxed will lead to greater investment in the stock market." This is an example of:
- a. a positive economic statement.
 - b. a negative economic statement.
 - c. the fallacy of composition.
 - d. a normative economic statement.
 - e. confusing correlation with causation.

ANS: A PTS: 1

132. Which of the following is an example of a normative statement?
- a. Higher unemployment rates are common among young people.
 - b. Young people should learn how to prepare their own taxes.
 - c. Auto insurance rates are generally lower for younger drivers.
 - d. Persons under the age of 30 watch more movies than those over the age of 30.
 - e. An individual under the age of 30 will generally have a longer life expectancy than someone over the age of 50.

ANS: B PTS: 1

133. An economic study concludes that an investment tax credit would increase business investment next year. This is an example of:
- a. normative analysis.
 - b. positive analysis.
 - c. negative economic analysis.
 - d. the fallacy of composition.
 - e. generalizing from the whole to the individual.

ANS: B PTS: 1

134. Which of the following is a normative statement?
- a. An increase in taxes will cause higher unemployment.
 - b. An increase in tariffs will increase the domestic prices paid by consumers.
 - c. Income should be redistributed from the top 2% of wage earners to the lower income brackets.
 - d. Running government budget deficits leads to higher market interest rates.
 - e. Increasing the money supply will lead to inflation.

ANS: C PTS: 1

135. When President Harry Truman said that he wanted to find a one-armed economist because his economic advisors always said, "On the one hand . . . and on the other hand . . ." he recognized that the advice of economists is often equivocal. Why is their advice often equivocal?
- a. Economists cannot make up their minds on policy matters.
 - b. Economists always disagree with each other on policy issues.
 - c. Economists are aware that tradeoffs are involved in most policy questions.
 - d. Economists are often unable to identify the critical questions involved in policy issues.

ANS: C PTS: 1

136. Graphs are useful because of the way they:

- a. facilitate interpretation and analysis of data.
- b. clarify interpretation and analysis of ideas.
- c. permit a person to more easily see relationships.
- d. convey an idea that might otherwise take many words.
- e. do all of the above.

ANS: E PTS: 1

137. The beginning point of a graph (the 0,0 point) is known as:

- a. ground zero.
- b. the quadrant.
- c. the origin.
- d. variable one.
- e. the beginning.

ANS: C PTS: 1

138. Which of the following graphs or charts must add up to one hundred percent?

- a. a labor graph
- b. a pie chart
- c. a time-series graph
- d. a scatter diagram

ANS: B PTS: 1

139. "The hotter it gets, the more water people drink." This statement implies that the relationship between temperature and water consumption must have:

- a. no relationship.
- b. a negative slope.
- c. a positive slope.
- d. either positive or negative slope.

ANS: C PTS: 1

140. Which of the following is an example of a relationship with a negative slope?

- a. spending increases as incomes rise
- b. more items purchased when prices drop
- c. more items sold when quality improves
- d. less items purchased when quality decreases

ANS: B PTS: 1

141. Considering a linear curve, which of the following is not a correct observation?

- a. Its slope can be measured as a ratio of the change in the Y value to the change in the X value.
- b. It is also called a straight-line curve.
- c. Its slope can be measured as a ratio of the rise over the run.
- d. It should have a positive slope.

ANS: D PTS: 1

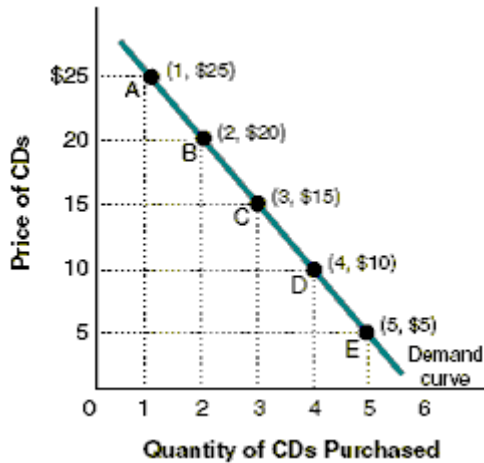
142. Most students expect that if they spend more time studying, the outcome will be improved grades in the course. This supposes that:

- a. a positive relationship exists between studying and grades.
- b. a negative relationship exists between studying and grades.
- c. grades are independent variables.

d. grades are not dependent variables.

ANS: A PTS: 1

Exhibit 1-1



143. Referring to **Exhibit 1-1**, which point on the demand curve represents the maximum number of CDs purchased?
- A
 - B
 - C
 - D
 - E

ANS: E PTS: 1

144. **Exhibit 1-1** demonstrates that:
- price and quantity purchased are positively related.
 - there is an inverse relationship between price and quantity purchased.
 - as the price increases, the quantity purchased increases.
 - price and quantity purchased share a direct relationship.

ANS: B PTS: 1

Table 1-1

Combination	Price of Apples per Bushel in Dollars	Quantity of Apples Purchased in Bushels
A	9	3
B	7	4
C	5	6
D	4	8
E	2	10

145. **Table 1-1** demonstrates that price and quantity at each combination:
- are inversely related.
 - are negatively related.
 - are positively related.
 - have no affect on each other.
 - can be expressed as either inversely or negatively related.

ANS: E PTS: 1

146. **Table 1-1** demonstrates that:

- a. more apples are purchased at each and every price.
- b. more apples are purchased as the price declines.
- c. fewer apples are purchased as the price declines.
- d. fewer apples are purchased at each and every price.

ANS: B PTS: 1

147. Which of the following topics would be covered in microeconomics?

- a. The effects of an increase in the supply of lumber on the homebuilding industry.
- b. The unemployment rate.
- c. The effects of interest rates on the overall economy.
- d. The inflation rate.

ANS: A PTS: 1

148. Which of the following questions is addressed primarily by macroeconomics?

- a. The allocation of scarce satellite orbit slots.
- b. Decisions made by a manufacturer of a particular good.
- c. Policies to control the inflation rate.
- d. A consumer's decision to buy more clothing and less food.

ANS: C PTS: 1

149. A microeconomist would most likely study the effect of a reduction in income tax rates on:

- a. total output in the economy.
- b. the output of the steel industry.
- c. inflation.
- d. unemployment

ANS: B PTS: 1

150. A macroeconomist would most likely study the effect of a reduction in income tax rates on:

- a. inflation.
- b. the output of the steel industry.
- c. total output in the economy.
- d. unemployment
- e. all of the above except b.

ANS: E PTS: 1

151. Which of the following is true?

- a. Virtually all theories in economics are expressed using a *ceteris paribus* ("let everything else be equal" or "holding everything else constant") assumption.
- b. The fallacy of composition is that, even if something is true for an individual, it is not necessarily true for many individuals as a group.
- c. One must always be careful not to confuse correlation with causation.
- d. Positive analysis involves statements about what is or what is likely to happen.
- e. All of the above are true.

ANS: E PTS: 1

152. What would not be held constant in testing a theory that if a student studies harder, he will get a better grade?

- a. The course being taken.
- b. The ability and effort of the other students in the class.
- c. The grading scale in the course.
- d. The number of hours the student spends studying.
- e. All of the above would be held constant in testing such a theory.

ANS: D PTS: 1

153. Which of the following is most likely an example of correlation but not an example of causation?
- a. In the U.S., more pizza is consumed on Super Bowl Sunday than any other day of the year. consumed
 - b. The cost of advertising during the first half of the Super Bowl is greater than the cost of advertising in the second half.
 - c. Each time I eat a chili dog and drink a beer before a game, my teams wins.
 - d. Generally speaking winning football team tend to average more rushing yards than losing football teams.

ANS: C PTS: 1

154. Which of the following involves the fallacy of composition?
- a. Because sitting in the back of classrooms is correlated with getting lower grades in the class, students should always sit closer to the front of the classroom.
 - b. Historically, the stock market rises in years the NFC team wins the Super Bowl and falls when the AFC wins the Super Bowl, I am rooting for the NFC team to win for the sake of my investment portfolio.
 - c. When a basketball team spends more to get better players, it is more successful, which proves that all the teams should spend more to get better players.
 - d. An increase in the amount of money I have will make me better off, so an increase in the supply of money in the economy will make Americans as a group better off.
 - e. Both c. and d. involve the fallacy of composition.

ANS: E PTS: 1

155. The *ceteris paribus* assumption is used in economic analyses in order to:
- a. cover special cases.
 - b. include all relevant factors.
 - c. add realism.
 - d. simplify the analysis of a complex world.

ANS: D PTS: 1

156. Which of the following best illustrates the fallacy of composition?
- a. If I have more money, I will be better off; therefore if we all had more money, we all would be better off.
 - b. If I buy more gas each week, my gas consumption increases; therefore, if all gas consumers buy more gas each week, total gas consumption will increase.
 - c. If I spend more time studying, I will learn more; therefore, if all students spend more time studying, they will learn more.
 - d. If women's hemlines are higher this year, the Dow Jones Industrials average will fall.

ANS: A PTS: 1

157. Which of the following is true?
- a. Positive analysis involves what is or what is likely to happen.
 - b. Normative analysis involves judgments about what should or ought to be the case.

- c. Both a. and b. are true.
- d. Neither a. or b. are true.

ANS: C PTS: 1

158. Which of the following is false?
- a. A positive statement must be testable but need not be true.
 - b. A hypothesis is a normative statement.
 - c. Normative analysis involves subjective, non-testable statements.
 - d. The majority of disagreements in economics stem from normative issues.

ANS: B PTS: 1

159. Which of the following is a positive statement?
- a. Increased money supply growth will lead to a higher rate of inflation.
 - b. The average distance between the earth and the moon is 100,000 miles.
 - c. There are more millionaires in Uganda than in the United States.
 - d. People watch more TV during finals week than during the rest of the term.
 - e. All of the above are positive statements.

ANS: E PTS: 1

160. "Mandating longer sentences for any criminal's third arrest will lead to a reduction in crime. Less crime will reduce the number of police officers cities will hire." This quotation:
- a. contains positive statements only.
 - b. contains normative statements only.
 - c. contains both normative and positive statements.
 - d. contains neither normative nor positive statements.

ANS: A PTS: 1

161. Which of the following contains only normative statements?
- a. A higher income tax rate would increase tax revenues, which should be used to give more aid to the poor.
 - b. The birth rate is reduced as economies urbanize, but that also leads to a decreased average age of developing countries' populations.
 - c. An increase in the price of corn will decrease the amount of corn purchased. However, it will increase the amount of wheat purchased.
 - d. A decrease in the price of butter will increase the amount of butter purchased, but that would be bad because it would increase Americans' cholesterol levels.
 - e. none of the above contain only normative statements.

ANS: E PTS: 1

162. Which of the following is a statement of positive economics?
- a. The income tax reduces after-tax incomes of the rich.
 - b. A reduction in tax rates makes the after-tax distribution of income fairer.
 - c. Tax rates ought to be reduced so that people will work more.
 - d. All of the above are statements of positive economics.
 - e. None of the above is statements of positive economics.

ANS: A PTS: 1

163. Which of the following is a statement of positive economics?
- a. Unemployment is a more severe problem in societies than inflation.
 - b. Our current unemployment rate is a serious problem.

- c. If the overall unemployment rate is 6 percent, black unemployment rates will exceed 12 percent.
- d. An unemployment rate of 4 percent would be too low.

ANS: C PTS: 1

164. Bill says: "The imposition of a tax on tequila will increase its price." Bob says: "Taxes should be imposed on tequila because college students drink too much."
- a. Both statements are normative.
 - b. Both statements are positive.
 - c. Bill's statement is normative, and Bob's statement is positive.
 - d. Bill's statement is positive, and Bob's statement is normative.

ANS: D PTS: 1

165. "Employment fell last month to its lowest level in the last six years" is an example of:
- a. the fallacy of composition.
 - b. positive economics.
 - c. normative economics.
 - d. a refutable statement.
 - e. both b. and d.

ANS: E PTS: 1

166. Which of the following statements is true?
- a. All economists are concerned with freedom and fairness and support government intervention in the economy.
 - b. Those economists primarily concerned with freedom do not support government intervention in the economy.
 - c. Those economists primarily concerned with fairness do not support government intervention in the economy.
 - d. All economists are opposed to government intervention in the economy.

ANS: B PTS: 1

SHORT ANSWER

1. Identify whether each of the following topics would be primarily a concern of microeconomics or macroeconomics:
- a. The decision by a household to eat in rather than go out for dinner this evening.
 - b. The unemployment rate increased from 4.5% to 4.8%.
 - c. A decision by the Federal Reserve Bank to decrease the supply of money in the economy.
 - d. The general level of prices increased by 5% last year.
 - e. The price of bicycles increased by \$30 last year.
 - f. The family restaurant chain closed down after losing much of its customer base to fast-food competitors over the last few years.

ANS:

Microeconomic topics: a, e, and f

Macroeconomic topics: b, c, and d

PTS: 1

2. Can activities like driving faster than the speed limit or driving without wearing a seat belt be considered rational behavior? Why or why not?

ANS:

These activities would be considered rational if the perceived benefits are greater than the perceived costs. The decision to act in a certain way can be rational even if the actions turns out to be something that the individual later regrets.

PTS: 1

3. Explain why economists believe that an individual who commits a crime does so acting in his/her own self-interest.

ANS:

It is expected that the individual committing a crime is trying to make her/himself better off, and has considered the potential consequences of her/his actions (perhaps getting caught and punished).

PTS: 1

4. What is the difference between a hypothesis and a theory?

ANS:

A hypothesis about behavior is the first step in developing and constructing a theory. A hypothesis is testable and makes a prediction about behavior in response to changed circumstances. If a hypothesis is shown to be consistent with real-world data, it can be tentatively accepted as an economic theory.

PTS: 1

5. Why is abstraction important in developing economic theories?

ANS:

Economic theories cannot realistically include every event that has ever occurred. A theory weeds out the irrelevant facts from the relevant ones. An economic theory provides a broad view, not a detailed examination, of human economic behavior.

PTS: 1

6. The Environmental Protection Agency asks you to help them understand the causes of urban pollution. You develop the following two hypotheses. Test each hypothesis against the given facts, identify which fits the facts better, and offer a theory based on your observation.

- I. Air pollution will be a greater problem the higher the average temperature in an urban area.
- II. Air pollution will be a greater problem the greater the population located in an urban area.

Urban Area	Days with Polluted Air	Average Max Temperature	Population (in thousands)
Los Angeles, CA	104.3	70.4	15,302
Portland, ME	11.8	54.9	445
Cincinnati, OH	1.3	63.2	1,894
Milwaukee, WI	3.9	54.3	1,637
San Diego, CA	11.8	70.8	2,632

El Paso, TX	3.7	77.5	665
Atlanta, GA	4.2	71.2	3,331
Philadelphia, PA	10.3	63.4	5,957

ANS:

This data supports hypothesis II better than hypothesis I. Four of the five cities that experienced the most days of polluted air are large population centers. Only three of the five hottest cities ranked among the lowest in air quality, by contrast. The other two, El Paso and Atlanta, experienced a comparatively low number of days of polluted air. Therefore we can make a theoretical statement that, in general, air pollution will increase as population increases. Surprisingly, Portland, Maine, has the coldest climate and also a small population base and it experienced a low quality of air more often than most cities.

PTS: 1

7. Darla is surprised to find that the quality of in-flight service remains much the same despite a steep hike in air-fares recently. What could be wrong in her assumption that a higher price naturally translates into better quality?

ANS:

The fact that two variables might be related does not necessarily mean that one causes the other to occur. Darla could be ignoring other variables involved in this scenario. Increase in fares might have been necessitated by factors such as increase in aviation fuel prices, margin pressures etc.

PTS: 1

8. Identify the error in judgment in each of the following statements:
- "If you leave a concert during the encore, you will avoid traffic and get home more rapidly; therefore everyone should leave during the encore."
 - "Whenever I wear my lucky baseball cap to an exam, I receive an 'A.' My baseball cap must induce the teacher to give me good grades."

ANS:

Statement I is an example of the fallacy of composition.

Statement II is an example of confusing association with causation.

PTS: 1

9. "Government should do all it can to slow the process of global warming." Is this a positive or normative statement? Explain your answer.

ANS:

This is a normative statement. The key is the inclusion of the word "should" in the statement. It is a value judgment, although one that is shared by many people.

PTS: 1

10. "The president of the world's biggest polluter (the United States) needs to do more than propose well-intentioned but insufficient measures that amount to using a squirt gun to quell a raging fire." Is this a positive or a normative economic statement? Explain your answer.

ANS:

This statement is normative. The key is the phrase "the president . . . needs to do more." This is a value judgment on the speaker's part.

PTS: 1

11. "If the price of wine increases, the quantity purchased will increase." Is this a positive or a normative economic statement? Explain your answer.

ANS:

Since it is a testable proposition, it is a positive economic statement. The statement need not be true, only testable.

PTS: 1

12. Indicate whether each of the following is a positive or normative economic statement:
- I. The imposition of a price ceiling below equilibrium price will lead to a shortage of housing.
 - II. The local government should control the rate of increase in rents so that low-income residents are not forced to move from the area.

ANS:

Statement I is a positive economic statement because it is testable.

Statement II is a normative economic statement because it reflects a value judgment.

PTS: 1

13. When economists disagree, it is often over what type of issues?

ANS:

Economists generally disagree on policy issues that require utilizing normative economic analysis. Differences in beliefs or values lead to conflicts as to the best resolution of an economic problem.

PTS: 1

14. Why would economists disagree over positive analysis?

ANS:

Economists might disagree over positive analysis for at least two reasons. One, a particular model may yield mixed results. Two, the information available may be insufficient to make a compelling theory.

PTS: 1

15. What is the difference between dependent and independent variables?

ANS:

A variable is a quantity that can take on different numeric values. A dependent variable is one that depends on the independent variables. That is, the dependent variable value changes according to the values of independent variables, while an independent variable is truly independent.

PTS: 1

16. Why are graphs such an important tool in economics?

ANS:

Graphs allow us to express a substantial amount of information in a limited space and represent relationships between different variables.

PTS: 1

17. How do we measure the slope of a linear curve?

ANS:

A straight-line curve is called a linear curve. The slope of a linear curve between two points measures the relative rates of change of two variables. Specifically, the slope of a linear curve can be defined as the ratio of the change in the Y value to the change in the X value. The slope can also be expressed as the ratio of the rise to the run, where the rise is the change in the Y variable (along the vertical axis) and the run is the change in the X variable (along the horizontal axis).

PTS: 1

18. How do we find the slope of a nonlinear curve?

ANS:

We can find the slope at a given point by drawing a straight-line tangent to that point on the curve (when a straight line just touches the curve without actually crossing it) and calculating the slope of the tangent line.

PTS: 1

19. Why is prediction in social sciences like economics more difficult than in physical sciences?

ANS:

The major reason for the difference is that the social scientists are concerned with human behavior. Human behavior is more variable and often less readily predictable than the behavior of experiments observed in a laboratory.

PTS: 1