

# TEST ITEM FILE

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## **Economics: Canada in the Global Environment**

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## **Chapter 1 What Is Economics?**

### 1.1 Definition of Economics

1) In a world characterized by scarcity

- A) all goods are free.
- B) opportunity cost is zero.
- C) we are not limited by time.
- D) individuals need not work to obtain goods.
- E) people must make choices among alternatives.

Answer: E

Diff: 1 Type: MC

Topic: Definition of Economics

2) Which of the following is the best definition of economics?

- A) the study of how a provincial government allocates tax dollars
- B) the study of how consumers spend their income
- C) the study of how producers decide what inputs to hire and what outputs to produce
- D) the study of how individuals, businesses, governments, and entire societies make choices as they cope with scarcity and the incentives that influence and reconcile those choices
- E) the study of how consumers and producers meet each other at the market

Answer: D

Diff: 1 Type: MC

Topic: Definition of Economics

3) Which of the following is a microeconomic topic?

- A) the reasons why a consumer buys less honey
- B) the reasons why the average price level in a country falls
- C) the cause of increasing unemployment
- D) the effect of the government budget deficit on inflation
- E) the reasons why the labour force in a country decreases

Answer: A

Diff: 1 Type: MC

Topic: Definition of Economics

4) The study of how wages are set for New Brunswick teachers is classified as

- A) a macroeconomic topic.
- B) a microeconomic topic.
- C) economics of social interest.
- D) economics of private interest.
- E) normative economics.

Answer: B

Diff: 1 Type: MC

Topic: Definition of Economics

- 5) Which of the following newspaper headlines concerns a macroeconomic issue?
- A) Why are people buying more SUVs and fewer minivans?
  - B) How would a tax on e-commerce affect chapters.indigo.ca?
  - C) How would an unexpected freeze in Oxford, Nova Scotia change the price of blueberries in the Maritimes?
  - D) Why is Japan's economy stagnant?
  - E) Why do grain producers purchase less pesticides?

Answer: D

Diff: 1 Type: MC

Topic: Definition of Economics

- 6) The branch of economics that studies the choices of individuals and businesses is
- A) macroeconomics.
  - B) microeconomics.
  - C) positive economics.
  - D) normative economics.
  - E) social economics.

Answer: B

Diff: 1 Type: MC

Topic: Definition of Economics

Source: Study Guide

- 7) Each of the following would be considered a macroeconomic topic *except*
- A) the reasons for a decrease in the unemployment rate.
  - B) the cause of recessions.
  - C) the effect of the government budget deficit on inflation.
  - D) the determination of aggregate income.
  - E) the selection of production techniques.

Answer: E

Diff: 2 Type: MC

Topic: Definition of Economics

- 8) Complete the following sentence. Macroeconomics
- A) is primarily concerned with the operation of individual markets in the economy.
  - B) deals mainly with the economic behaviour of households.
  - C) is the only part of economics to deal with government decisions.
  - D) is primarily concerned with the behaviour of the stock market.
  - E) is the study of the national economy and the global economy.

Answer: E

Diff: 2 Type: MC

Topic: Definition of Economics

9) The determination of prices in individual markets is primarily a concern of

- A) positive economics.
- B) negative economics.
- C) macroeconomics.
- D) microeconomics.
- E) descriptive economics.

Answer: D

Diff: 2 Type: MC

Topic: Definition of Economics

10) Which one of the following topics does macroeconomics study?

- A) decisions of individual firms
- B) effects of government safety regulations on the price of cars
- C) the performance of the global economy
- D) prices of individual goods and services
- E) effects of taxes on the price of gasoline

Answer: C

Diff: 2 Type: MC

Topic: Definition of Economics

11) Which one of the following topics does microeconomics study?

- A) reasons for a fall in the price of orange juice
- B) the effect of a rise in the Canadian dollar on Canada's exports
- C) effect of interest rates on national economic growth
- D) effect of the government budget deficit on employment
- E) determination of total production in a country

Answer: A

Diff: 2 Type: MC

Topic: Definition of Economics

12) Complete the following sentence. Microeconomics is

- A) not concerned with factors of production.
- B) concerned with normative issues only.
- C) concerned with the size of the total amount of income earned by all households in an economy.
- D) the branch of economics that studies the choices of individuals and businesses.
- E) concerned exclusively with the role of the government in the economy.

Answer: D

Diff: 2 Type: MC

Topic: Definition of Economics

13) Which of the following would be considered a microeconomic topic?

- A) the severity of a recession
- B) the cause of unemployment in the economy
- C) the effect of the government budget deficit on inflation
- D) the determination of aggregate income
- E) the study of how wages are set for mine workers

Answer: E

Diff: 2 Type: MC

Topic: Definition of Economics

14) The branch of economics that studies the national economy and the global economy is

- A) macroeconomics.
- B) microeconomics.
- C) Keynesian economics.
- D) positive economics.
- E) normative economics.

Answer: A

Diff: 1 Type: MC

Topic: Definition of Economics

15) The fact that human wants cannot be fully satisfied with available resources is called the problem of

- A) opportunity cost.
- B) scarcity.
- C) normative economics.
- D) marginal cost.
- E) the big tradeoff.

Answer: B

Diff: 1 Type: MC

Topic: Definition of Economics

16) The problem of scarcity exists

- A) only in economies that lack incentives.
- B) only in economies that have incentives.
- C) in all economies.
- D) only when people are unemployed.
- E) now but will be eliminated with economic growth.

Answer: C

Diff: 2 Type: MC

Topic: Definition of Economics

17) The inescapable economic fact is that

- A) there are unlimited wants and limited resources.
- B) there are unlimited resources, and we just have to figure out how to allocate them.
- C) capitalists are always exploiting the workers.
- D) unions are always exploiting firms.
- E) capitalists and unions cannot work together.

Answer: A

Diff: 2 Type: MC

Topic: Definition of Economics

18) An incentive \_\_\_\_\_.

- A) could be a reward but could not be a penalty
- B) could be a penalty but could not be a reward
- C) could be either a reward or a penalty
- D) is the opposite of a tradeoff
- E) occurs in the macroeconomy but not in the microeconomy

Answer: C

Type: MC

19) Scarcity confronts \_\_\_\_\_.

- A) neither the poor nor the rich
- B) the rich but not the poor
- C) the poor but not the rich
- D) the rich and the poor
- E) families with incomes less than \$25,000 a year

Answer: D

Type: MC

## 1.2 Two Big Economic Questions

1) The two big economic questions

- A) involve self-interest only.
- B) involve only social interest.
- C) involve neither self-interest nor social interest.
- D) do not arise from scarcity.
- E) involve both self-interest and social interest.

Answer: E

Diff: 1 Type: MC

Topic: Two Big Economic Questions

2) The two big economic questions

- A) summarize the scope of economics.
- B) are "what goods and services are produced?" and "how are goods and services produced?"
- C) have nothing to do with goods and services.
- D) do not consider for whom goods and services are produced.
- E) have nothing to do with the way goods and services are produced.

Answer: A

Diff: 1 Type: MC

Topic: Two Big Economic Questions

3) The two big economic questions include all of the following *except*

- A) *what* to produce.
- B) *why* to produce.
- C) *how* to produce.
- D) *for whom* to produce.
- E) can choices made in the pursuit of self-interest also promote the social interest.

Answer: B

Diff: 2 Type: MC

Topic: Two Big Economic Questions

4) When a firm decides to produce more hybrid cars and fewer gas guzzlers, it is answering the \_\_\_\_\_ question.

- A) "how"
- B) "what"
- C) "who"
- D) "where"
- E) "when"

Answer: B

Diff: 2 Type: MC

Topic: Two Big Economic Questions

5) When a textile firm decides to produce more silk fabric and less cotton fabric, it is answering the \_\_\_\_\_ question.

- A) "who"
- B) "how"
- C) "what"
- D) "where"
- E) "when"

Answer: C

Diff: 2 Type: MC

Topic: Two Big Economic Questions

6) When a farmer decides to harvest tomatoes using machines instead of migrant workers, the farmer is answering the \_\_\_\_\_ question.

- A) "what"
- B) "how"
- C) "who"
- D) "where"
- E) "when"

Answer: B

Diff: 2 Type: MC

Topic: Two Big Economic Questions

7) Complete the following sentence. Capital is

- A) money in the bank.
- B) "gifts of nature."
- C) tools, instruments, machines, buildings, and other constructions that businesses use to produce goods and services.
- D) land.
- E) stocks and bonds.

Answer: C

Diff: 1 Type: MC

Topic: Two Big Economic Questions

8) When a firm decides to produce computers using robots instead of people, it is answering the \_\_\_\_\_ question.

- A) "what"
- B) "where"
- C) "how"
- D) "who"
- E) "when"

Answer: C

Diff: 2 Type: MC

Topic: Two Big Economic Questions

9) To meet increased demand for its good, a firm decides to hire a few high-skilled workers, rather than hire many low-skilled workers. The firm is answering the \_\_\_\_\_ question.

- A) "when"
- B) "what"
- C) "who"
- D) "where"
- E) "how"

Answer: E

Diff: 2 Type: MC

Topic: Two Big Economic Questions

10) An art museum decides to offer tours by having visitors listen to CDs rather than have tour guides. The museum is answering the \_\_\_\_\_ question.

- A) "what"
- B) "who"
- C) "how"
- D) "where"
- E) "when"

Answer: C

Diff: 2 Type: MC

Topic: Two Big Economic Questions

11) To earn income, people sell the services of the factors of production they own. Land earns \_\_\_\_\_; labour earns \_\_\_\_\_; capital earns \_\_\_\_\_ and entrepreneurship earns \_\_\_\_\_.

- A) profit; wages; rent; interest
- B) wages; interest; profit; rent
- C) rent; wages; interest; profit
- D) profit; interest; wages; rent
- E) interest; profit; rent; wages

Answer: C

Diff: 2 Type: MC

Topic: Two Big Economic Questions

12) The fact that some people can afford to live in beautiful homes while others are homeless is an example of an economy facing the \_\_\_\_\_ question.

- A) "what"
- B) "how"
- C) "for whom"
- D) "where"
- E) "when"

Answer: C

Diff: 2 Type: MC

Topic: Two Big Economic Questions

13) The fact that a hockey star earns \$3 million a year while a teacher earns \$50,000 annually is an example of an economy facing the \_\_\_\_\_ question.

- A) "what"
- B) "how"
- C) "where"
- D) "for whom"
- E) "when"

Answer: D

Diff: 2 Type: MC

Topic: Two Big Economic Questions

14) Complete the following sentence. Entrepreneurship is

- A) defined as money.
- B) traded on the stock market.
- C) categorized as capital.
- D) the human resource that organizes labour, land and capital.
- E) categorized as the factor of production labour.

Answer: D

Diff: 2 Type: MC

Topic: Two Big Economic Questions

15) Sue, who has a law degree, earns \$200,000 a year, while Chris, a high-school dropout, earns \$5.00 an hour. This is an example of an economy facing the \_\_\_\_\_ question.

- A) "what"
- B) "how"
- C) "for whom"
- D) "where"
- E) "when"

Answer: C

Diff: 2 Type: MC

Topic: Two Big Economic Questions

16) A star athlete can afford a garage full of exotic cars while other people can only afford to take a city bus for transportation. This is an example of an economy facing the \_\_\_\_\_ question.

- A) "what"
- B) "how"
- C) "for whom"
- D) "where"
- E) "when"

Answer: C

Diff: 2 Type: MC

Topic: Two Big Economic Questions

- 17) Complete the following sentence. Financial capital is
- A) one of the "gifts of nature."
  - B) the tools and machines that are used to produce goods and services.
  - C) money, stocks, and bonds.
  - D) used in the production of goods and services.
  - E) land.

Answer: C

Diff: 1 Type: MC

Topic: Two Big Economic Questions

- 18) Which factor of production earns the most income?
- A) capital
  - B) land
  - C) labour
  - D) entrepreneurship
  - E) the stock market

Answer: C

Diff: 2 Type: MC

Topic: Two Big Economic Questions

- 19) What choices are best for the entire society?
- A) self-interest choices
  - B) minority group choices
  - C) social interest choices
  - D) ethnic group choices
  - E) regional interest choices

Answer: C

Diff: 1 Type: MC

Topic: Two Big Economic Questions

- 20) Self-interest choices are
- A) those choices which are best for the person making them.
  - B) never in the social interest.
  - C) always in the social interest.
  - D) those choices that are best for all residents of a region.
  - E) choices that are agreed to by majority vote.

Answer: A

Diff: 3 Type: MC

Topic: Two Big Economic Questions

21) The expansion of international trade, borrowing and lending, and investment is

- A) the big tradeoff.
- B) industrial revolution.
- C) corporate revolution.
- D) globalization.
- E) antiglobalization.

Answer: D

Diff: 3 Type: MC

Topic: Two Big Economic Questions

22) Which of the following relates factors of production to the sources of income correctly?

- A) Land earns interest.
- B) Land earns rent.
- C) Labour earns rent.
- D) Capital earns profit.
- E) Entrepreneurship earns rent.

Answer: B

Diff: 1 Type: MC

Topic: Two Big Economic Questions

23) Which statement about incomes earned by factors of production is *false*?

- A) Land earns rent.
- B) Natural resources earn rent.
- C) Labour earns wages.
- D) Capital earns profit.
- E) Entrepreneurship earns profit.

Answer: D

Diff: 1 Type: MC

Topic: Two Big Economic Questions

24) A tractor is an example of which of the following factors of production?

- A) capital
- B) labour
- C) land
- D) entrepreneurship
- E) energy

Answer: A

Diff: 1 Type: MC

Topic: Two Big Economic Questions

25) Which one of the following is an example of capital as a factor of production?

- A) money held by Tim Hortons
- B) a Bell Canada bond
- C) an automobile factory owned by Ford
- D) a high school teacher
- E) natural gas

Answer: C

Diff: 1 Type: MC

Topic: Two Big Economic Questions

26) Which of the following would an economist classify as capital?

- A) natural resources
- B) a deposit of silver
- C) entrepreneurship
- D) a computer
- E) land

Answer: D

Diff: 1 Type: MC

Topic: Two Big Economic Questions

27) Which one of the following is labour?

- A) money
- B) a carpenter's hammer
- C) a shoe factory
- D) a bread-slicing machine
- E) a singer's voice

Answer: E

Diff: 1 Type: MC

Topic: Two Big Economic Questions

28) Which one of the following would economists classify as land?

- A) an automotive plant in British Columbia
- B) rich agricultural soil in Saskatchewan
- C) an oil rig in the Atlantic Ocean
- D) an elementary school in Nova Scotia
- E) automobiles parked in a parking lot in Manitoba

Answer: B

Diff: 2 Type: MC

Topic: Two Big Economic Questions

29) Which one of the following is an example of land?

- A) Bono's singing voice
- B) a computer program
- C) Lake Erie
- D) a road
- E) a dam

Answer: C

Diff: 1 Type: MC

Topic: Two Big Economic Questions

30) Which one of the following is an example of a factor of production?

- A) an insurance policy
- B) a donut
- C) the skills of a welder
- D) an IBM stock certificate
- E) a computer game

Answer: C

Diff: 1 Type: MC

Topic: Two Big Economic Questions

31) Which one of the following is an example of capital?

- A) money
- B) a carpenter
- C) pasture
- D) a bread-slicing machine
- E) a university professor

Answer: D

Diff: 1 Type: MC

Topic: Two Big Economic Questions

32) The creation of a successful movie illustrates choices made in self-interest that also achieve the social interest if \_\_\_\_\_.

- A) the movie has a higher attendance than any other movie produced that year
- B) the movie is produced at the lowest possible cost, and the movie gives the greatest possible benefit
- C) the movie addresses a social issue
- D) the movie is an Academy award winner because an Academy award winning movie is most popular with the movie-going public
- E) the movie is produced in a country where workers typically earn less than workers in North America

Answer: B

Diff: 1 Type: MC

Topic: Two Big Economic Questions

Source: MyEconLab

33) The creation of a successful movie can influence the main questions that economics seeks to answer. Choose the statement that is *false*.

- A) The movie influences the *how* question because the movie can create new production techniques, which can be used in subsequent films.
- B) The movie influences the *for whom* question because the people who earn higher incomes through the movie production buy more goods and services.
- C) The movie influences the *when* question because movie crews work on many different films and must be available for the entire production.
- D) The movie influences the *what* question because it can lead to spinoff goods or a new movie genre, which can result in the production of similar films.
- E) The movie influences the *how* question because it can use unknown actors or Academy Award winners.

Answer: C

Diff: 1 Type: MC

Topic: Two Big Economic Questions

Source: MyEconLab

34) Choose the correct statement.

- A) Canada produces more services than goods.
- B) Canada produces more goods than services.
- C) Canada produces an equal quantity of goods and services.
- D) China's production of services is a greater percentage of its total production than Canada's.
- E) Canada's production of manufacturing is a greater percentage of its total production than China's.

Answer: A

Type: MC

35) In Canada \_\_\_\_\_ percent of the adult population have completed high school and \_\_\_\_\_ percent have a university degree.

- A) 23; 93
- B) 93; 53
- C) 93; 23
- D) 100; 53
- E) 53; 23

Answer: C

Type: MC

36) Which of the following is *not* a factor of production?

- A) the water used to cool a nuclear power plant
- B) the effort of farmers raising cattle
- C) the wages paid to workers
- D) the management skill of a small business owner
- E) the land used by a farmer to grow wheat

Answer: C

Type: MC

### 1.3 The Economic Way of Thinking

1) Opportunity cost is

- A) the value of your favourite activity.
- B) your value of leisure.
- C) the money you spend on food, shelter, and clothing.
- D) the marginal benefit from an activity.
- E) the highest-valued alternative that we give up to get something.

Answer: E

Diff: 2 Type: MC

Topic: The Economic Way of Thinking

2) During the next hour John can choose one of the following three activities: playing basketball, watching television, or reading a book. The opportunity cost of reading a book

- A) depends on how much the book cost when it was purchased.
- B) is the value of playing basketball if John prefers that to watching television.
- C) is the value of playing basketball *and* the value of watching television.
- D) depends on how much John enjoys the book.
- E) is the value of watching television if John prefers playing basketball to watching television.

Answer: B

Diff: 3 Type: MC

Topic: The Economic Way of Thinking

3) Sally has to decide whether to study for her economics test or her accounting test. If she chooses to study for accounting, her opportunity cost of studying accounting is

- A) studying economics.
- B) less than the value of studying economics.
- C) not comparable to the value of studying economics.
- D) equal to the value of studying economics.
- E) the future lost wages that will occur if she fails her accounting exam.

Answer: A

Diff: 2 Type: MC

Topic: The Economic Way of Thinking

4) When the government of Alberta chooses to build more roads, the required resources are no longer available to provide better health care facilities. This situation illustrates the concept of

- A) marginal benefit.
- B) monetary cost.
- C) opportunity cost.
- D) human capital.
- E) entrepreneurship.

Answer: C

Type: MC

Topic: The Economic Way of Thinking

- 5) The concept of opportunity cost
- A) is relevant only for European countries.
  - B) suggests that individuals can achieve all they want.
  - C) suggests a major increase in public education spending means a reduced expansion in the public healthcare system.
  - D) is relevant only for developed countries.
  - E) is relevant only for developing countries.

Answer: C

Diff: 2 Type: MC

Topic: The Economic Way of Thinking

- 6) Which one of the following is a necessary consequence of scarcity?

- A) no choices required
- B) high profits
- C) the requirement of making choices
- D) all wants are satisfied
- E) low profits

Answer: C

Diff: 1 Type: MC

Topic: The Economic Way of Thinking

- 7) To make choices, people must

- A) be able to carry out complex mathematical calculations.
- B) have unlimited resources.
- C) be free from government constraint.
- D) have unlimited access to information at no cost.
- E) evaluate the values of alternative actions.

Answer: E

Diff: 2 Type: MC

Topic: The Economic Way of Thinking

- 8) When the government chooses to use resources to build a dam, those resources are no longer available to build a highway. This illustrates the concept of

- A) a market.
- B) macroeconomics.
- C) opportunity cost.
- D) a "how" tradeoff.
- E) the big tradeoff.

Answer: C

Diff: 2 Type: MC

Topic: The Economic Way of Thinking

Source: Study Guide

9) What is the definition of marginal benefit?

- A) the cost of an increase in an activity
- B) the sum of benefit and cost that arises from an increase in an activity
- C) the cost of a decrease in an activity
- D) the benefit that arises from an increase in an activity
- E) the benefit that arises from a decrease in an activity

Answer: D

Diff: 2 Type: MC

Topic: The Economic Way of Thinking

10) When asked in an interview what she missed the most because of the time she spent training for the Olympics, a rower, who lived on her own, answered "a normal social life." She also revealed that she had given up a job that paid \$30,000 per year to train fulltime. She received a grant of \$8,000 per year from Sport Canada, but this failed to cover all her training expenses. Her food and rent were \$5,000 per year and training expenses were \$12,000 per year. Aside from the value of a normal social life, what is the annual opportunity cost, expressed in dollars, to this rower of "Going for Gold"?

- A) \$25,000
- B) \$4,000
- C) \$30,000
- D) \$39,000
- E) \$34,000

Answer: E

Diff: 3 Type: MC

Topic: The Economic Way of Thinking

11) Saskatchewan had more hospitals than Ontario, despite having one-tenth the population. The Saskatchewan government closed many of these hospitals in spite of widespread local protests. Which one of the following arguments is true?

- A) Since hospitals have positive benefits, they should never be closed.
- B) If Saskatchewan had more hospitals than Ontario, it must have had too many hospitals.
- C) The Saskatchewan government must have thought the marginal benefit from one of these hospitals exceeded its marginal cost.
- D) The Saskatchewan government must have thought the marginal benefit from one of these hospitals was less than its marginal cost.
- E) The communities where these hospitals existed bore no costs from these decisions, because they did not pay for any of the hospital operating costs.

Answer: D

Diff: 3 Type: MC

Topic: The Economic Way of Thinking

- 12) "There can be too much of a good thing." This statement suggests that
- A) choices made in self-interest cannot be applied to many economic decisions.
  - B) a good may be produced to the point where its marginal cost exceeds its marginal benefit.
  - C) certain goods and services such as education and health care are inherently desirable and should be produced regardless of costs and benefits.
  - D) a good may be produced to the point where its marginal benefit exceeds its marginal cost.
  - E) a good may be produced to the point where its marginal benefit is equal to its marginal cost.

Answer: B

Diff: 2 Type: MC

Topic: The Economic Way of Thinking

- 13) Which of the following sayings best describes opportunity cost?

- A) "Make hay while the sun shines."
- B) "Love of money is the root of all evil."
- C) "Boldly go where no one has gone before."
- D) "There's no such thing as a free lunch."
- E) "Baseball has been very good to me."

Answer: D

Diff: 2 Type: MC

Topic: The Economic Way of Thinking

Source: Study Guide

- 14) If you take an additional class this term, you can graduate earlier. This is an example of

- A) opportunity cost.
- B) total cost.
- C) the pursuit social interest.
- D) marginal benefit.
- E) social cost.

Answer: D

Diff: 2 Type: MC

Topic: The Economic Way of Thinking

- 15) Marginal benefit is the

- A) total benefit from an activity.
- B) additional benefit from a decrease in an activity.
- C) additional benefit from an increase in an activity.
- D) opportunity cost of a decrease in an activity.
- E) opportunity cost of an increase in an activity.

Answer: C

Diff: 1 Type: MC

Topic: The Economic Way of Thinking

Source: Study Guide

16) Complete the following sentence. Marginal cost is

- A) the total cost of an activity.
- B) the cost of a decrease in an activity.
- C) the cost of an increase in an activity.
- D) the opportunity cost of a decrease in an activity.
- E) equal to marginal benefit.

Answer: C

Diff: 1 Type: MC

Topic: The Economic Way of Thinking

17) The big tradeoff is the tradeoff between

- A) taxes and transfers.
- B) equality and efficiency.
- C) current consumption and a higher future standard of living.
- D) guns and butter.
- E) personal security and private property.

Answer: B

Diff: 1 Type: MC

Topic: The Economic Way of Thinking

Source: Study Guide

18) Monika will choose to eat a seventh pizza slice if

- A) the marginal benefit from the seventh slice is greater than its marginal cost.
- B) the marginal benefit from the seventh slice is less than its marginal cost.
- C) the total benefit from all seven slices is greater than their total cost.
- D) the total benefit from all seven slices is less than their total cost.
- E) she has enough money to pay for it.

Answer: A

Diff: 2 Type: MC

Topic: The Economic Way of Thinking

Source: Study Guide

19) Before starring as Tony Stark in *Iron Man*, Robert Downey Jr. had played in 45 movies that had average first-weekend box office revenues of a bit less than \$5 million. *Iron Man* grossed \$102 million in its first weekend. The success of *Iron Man* \_\_\_\_\_ the opportunity cost of hiring Robert Downey Jr.

Movie producers now have \_\_\_\_\_ incentive to hire Robert Downey Jr.

- A) increases; less
- B) decreases; less
- C) decreases; more
- D) increases; more
- E) decreases; zero

Answer: D

Diff: 1 Type: MC

Topic: The Economic Way of Thinking

Source: MyEconLab

20) The night before a history test, you decide to go to the movies instead of reviewing your notes. You get 60 percent on your test compared with the 75 percent that you normally score. You \_\_\_\_\_ a tradeoff \_\_\_\_\_, and the opportunity cost of your evening at the movies was \_\_\_\_\_.

- A) faced; between a higher test score and an evening at the movies; the 15 percent fall in your grade
- B) did not face; because your roommates agreed you should go to the movies and not study; zero
- C) did not face; because you made the best choice; zero
- D) faced; between a higher test score and an evening at the movies; the mark of 60 percent on your test
- E) did not face; most students get 60 percent on history tests; the mark of 60 percent on your test

Answer: A

Diff: 1 Type: MC

Topic: The Economic Way of Thinking

Source: MyEconLab

21) A university decides to change its late night bus service between the campus and student housing from a fare-based service to a free service. This statement means that the incentive to ride the bus \_\_\_\_\_ and the opportunity cost of a bus ride \_\_\_\_\_. The university's decision is a \_\_\_\_\_ decision.

- A) changes; decreases; microeconomic
- B) changes; decreases; macroeconomic
- C) remains the same; remains the same; macroeconomic
- D) remains the same; remains the same; microeconomic
- E) changes; increases; microeconomic

Answer: A

Diff: 1 Type: MC

Topic: The Economic Way of Thinking

Source: MyEconLab

Use the information below to answer the following question.

### Fact 1.1.1 Costs Soar for London Olympics

The regeneration of East London, the site of the 2012 Olympic Games, is set to add extra £1.5 billion to taxpayers' bill.

*The Times*, London, July 6, 2006

22) Refer to Fact 1.1.1. The cost of regenerating East London \_\_\_\_\_ an opportunity cost of hosting the 2012 Olympic Games \_\_\_\_\_.

A) is not; because few people attending the 2012 Olympics will spend much time outside Olympic venues

B) is; if the costs of the East London regeneration is equal to a significant percentage of the total amount spent by London taxpayers to host the 2012 Olympics

C) is; if the regeneration of East London would not occur unless London hosted the 2012 Olympics

D) is not; because regenerating East London is an unnecessary expense

E) is; if the property taxes of people living in East London increase

Answer: C

Diff: 1 Type: MC

Topic: The Economic Way of Thinking

Source: MyEconLab

23) You have the choice of going on vacation to Florida for one week, staying at work for the week, or spending the week doing fix-up projects around your house. If you decide to go to Florida, the opportunity cost of the trip is \_\_\_\_\_.

A) working *and* doing fix-up projects

B) working *or* doing fix-up projects, depending on which you would have done otherwise

C) working, because you would be giving up dollars

D) nothing because you will enjoy the trip to Florida

E) variable depending on the weather you leave behind in Canada

Answer: B

Type: MC

24) Laura is a manager for HP. When Laura must decide whether to produce a few additional printers, she is choosing at the margin when she compares \_\_\_\_\_.

A) the total revenue from sales of printers to the total cost of producing all the printers

B) the extra revenue from selling a few additional printers to the extra costs of producing the printers

C) the extra revenue from selling a few additional printers to the average cost of producing the additional printers

D) the revenue from selling HP's printers as compared to printers from competing companies, such as Lexmark

E) the cost of producing HP's printers as compared to printers from competing companies, such as Lexmark

Answer: B

Type: MC

25) Which of the following creates an incentive to increase the amount of an activity?

- A) an increase in the marginal cost of the activity and a decrease in the marginal benefit from the activity
- B) a decrease in the marginal cost of the activity and an increase in the marginal benefit from the activity
- C) constant marginal cost and constant marginal benefit from the activity
- D) an increase in the marginal cost of the activity and an equal increase in the marginal benefit from the activity
- E) a decrease in the marginal cost of the activity and an equal decrease in the marginal benefit from the activity

Answer: B

Type: MC

## 1.4 Economics as Social Science and Policy Tool

1) Statements about "what ought to be" are called

- A) positive statements.
- B) normative statements.
- C) economic statements.
- D) scientific statements.
- E) hypotheses.

Answer: B

Diff: 1 Type: MC

Topic: Economics as Social Science and Policy Tool

2) Statements about "what is" are called

- A) positive statements.
- B) normative statements.
- C) economic statements.
- D) scientific statements.
- E) hypotheses.

Answer: A

Diff: 1 Type: MC

Topic: Economics as Social Science and Policy Tool

3) Which of the following statements is normative?

- A) Scientists should not make normative statements.
- B) Warts are caused by handling toads.
- C) As e-book prices fall, people buy more of them.
- D) If income increases, sales of luxury goods fall.
- E) There is more caffeine in a cup of tea than in a cup of coffee.

Answer: A

Diff: 2 Type: MC

Topic: Economics as Social Science and Policy Tool

Source: Study Guide

4) A positive statement is

- A) about what ought to be.
- B) about what is.
- C) always true.
- D) capable of evaluation as true or false by observation and measurement.
- E) B and D.

Answer: E

Diff: 1 Type: MC

Topic: Economics as Social Science and Policy Tool

Source: Study Guide

- 5) A positive statement is
- A) always true.
  - B) always false.
  - C) about what ought to be.
  - D) what is currently believed about the way the world operates.
  - E) an opinion that cannot be verified.

Answer: D

Diff: 1 Type: MC

Topic: Economics as Social Science and Policy Tool

- 6) A normative statement is
- A) about what should be.
  - B) about what is.
  - C) always true.
  - D) always false.
  - E) capable of evaluation, as true or false, by observation and measurement.

Answer: A

Diff: 1 Type: MC

Topic: Economics as Social Science and Policy Tool

- 7) "The rich should face higher income tax rates than the poor." This is an example of
- A) a normative statement.
  - B) a positive statement.
  - C) a negative statement.
  - D) economic reasoning.
  - E) neither a normative nor a positive statement.

Answer: A

Diff: 2 Type: MC

Topic: Economics as Social Science and Policy Tool

- 8) Which of the following is an example of a positive statement?
- A) Canada should cut back on its use of carbon-based fuels such as coal and oil.
  - B) Increasing the minimum wage results in more unemployment.
  - C) Every Canadian should have equal access to health care.
  - D) The Bank of Canada ought to cut the interest rate.
  - E) Canada should have lower tax rates for wealthier Canadians.

Answer: B

Diff: 2 Type: MC

Topic: Economics as Social Science and Policy Tool

9) Complete the following sentence. Economic *models*

- A) do not answer questions about the economic world.
- B) include most of the details of the economic world.
- C) describe some aspect of the economic world, but include only those features needed for the purpose at hand.
- D) answer questions that arise from normative statements.
- E) were first developed in the 1970s.

Answer: C

Diff: 2 Type: MC

Topic: Economics as Social Science and Policy Tool

10) The scientific purpose of simplifying assumptions in an economic model is to

- A) avoid confronting difficult issues.
- B) eliminate the need for further testing of the implications of the model.
- C) abstract from the complexities of the real world those issues that are not important for the issues under examination.
- D) eliminate the possibility of personal bias in the model.
- E) add necessary hypotheses to the problem.

Answer: C

Diff: 2 Type: MC

Topic: Economics as Social Science and Policy Tool

11) Model *A* is superior to model *B* if

- A) it contains more real world detail than model *B*.
- B) it contains fewer unrealistic assumptions than model *B*.
- C) its predictions correspond more closely to the facts than the predictions of model *B*.
- D) it is preferred by a majority of researchers in a public opinion poll.
- E) it is scientifically "elegant."

Answer: C

Diff: 2 Type: MC

Topic: Economics as Social Science and Policy Tool

12) In choosing among alternative models, economists generally have the strongest preference for models that

- A) have assumptions that are close to exact replicas of reality.
- B) are detailed and complex, with every available fact and figure included.
- C) have few assumptions and are as simple as possible, even if they cannot predict very well.
- D) predict better than any other that is available.
- E) have assumptions that are complicated.

Answer: D

Type: MC

Topic: Economics as Social Science and Policy Tool

13) A normative statement is a statement regarding

- A) what is usually the case.
- B) the assumptions of an economic model.
- C) what ought to be.
- D) the predictions of an economic model.
- E) what is.

Answer: C

Diff: 1 Type: MC

Topic: Economics as Social Science and Policy Tool

Source: Study Guide

14) "The rich face higher income tax rates than the poor" is an example of a

- A) a normative statement.
- B) a positive statement.
- C) a predictive statement.
- D) a theoretical statement.
- E) an analytical statement.

Answer: B

Diff: 1 Type: MC

Topic: Economics as Social Science and Policy Tool

15) An economic model is tested by

- A) examining the realism of its assumptions.
- B) comparing its predictions with the facts.
- C) comparing its complexity to other models that deal with similar issues.
- D) the Testing Committee of the Canadian Economic Association.
- E) comparing its descriptions and examining the realism of its assumptions.

Answer: B

Diff: 2 Type: MC

Topic: Economics as Social Science and Policy Tool

16) Which of the following is a positive statement?

- A) Low rents restrict the supply of housing.
- B) Low rents are better for a city than high rents.
- C) Housing costs too much.
- D) Owners of apartment buildings ought to be free to charge whatever rent they want.
- E) Government should control the rents that apartment owners charge.

Answer: A

Diff: 2 Type: MC

Topic: Economics as Social Science and Policy Tool

Source: Study Guide

17) "The rich face higher income tax rates than the poor, which is not good since it is the rich who provide jobs for the poor." This is an example of

- A) a normative statement.
- B) a positive statement.
- C) a negative statement.
- D) a theoretical statement.
- E) a descriptive statement.

Answer: A

Diff: 2 Type: MC

Topic: Economics as Social Science and Policy Tool

18) An economic model is

- A) tested by examining the realism of its assumptions.
- B) useful if it predicts well, even if its assumptions are not realistic.
- C) tested by the Testing Committee of the Canadian Economic Association.
- D) not useful unless it predicts with 100 percent accuracy.
- E) not useful because it simplifies real problems.

Answer: B

Diff: 1 Type: MC

Topic: Economics as Social Science and Policy Tool

19) Select the best statement about economic models.

- A) An economic model must always be correct in its predictions or it must be discarded.
- B) An economic model is evaluated based on the realism of its assumptions.
- C) An economic model should not generate predictions about actual events in the real world, since it discusses only abstract events.
- D) An economic model will be discarded if its predictions are often in conflict with the facts.
- E) Economic models are all false.

Answer: D

Diff: 2 Type: MC

Topic: Economics as Social Science and Policy Tool

20) To disentangle cause and effect, economists use economic models and use \_\_\_\_\_ to test the predictions of those models.

- A) the *what*, *how*, and *for whom* questions
- B) positive statements and normative statements
- C) personal economic policy, business economic policy, and government economic policy
- D) natural experiments, statistical investigations, and economic experiments
- E) marginal benefit and marginal cost

Answer: D

Diff: 2 Type: MC

Topic: Economics as Social Science and Policy Tool

Source: MyEconLab

21) Which of the following statements are positive?

1. The federal government should increase production of biofuels.
2. Air travel has increased since September 11.
3. The greatest number of accidents are caused by drunk drivers.
4. We ought to have a cure for cancer.

- A) statements 1 and 4 are positive
- B) statements 2 and 3 are positive
- C) statements 1 and 2 are positive
- D) statements 3 and 4 are positive
- E) statements 2 and 4 are positive

Answer: B

Diff: 2 Type: MC

Topic: Economics as Social Science and Policy Tool

Source: MyEconLab

22) Which of the following statements are true regarding "positive" statements?

- I. They describe what "ought to be."
- II. They describe what is believed about how the world appears.
- III. They can be tested as to their truthfulness.

- A) I and II
- B) II and III
- C) I and III
- D) I, II and III
- E) None of the statements are true.

Answer: B

Type: MC

23) Which of the following is a normative statement?

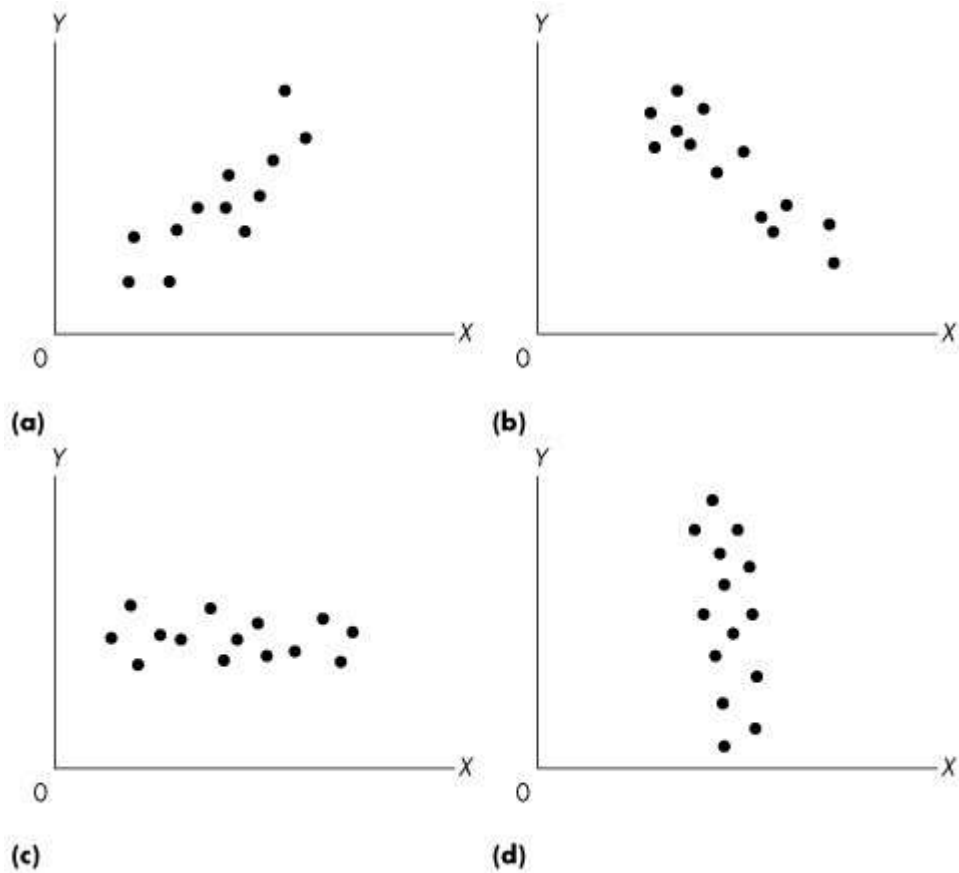
- A) Next year's inflation rate will be under 4 percent.
- B) Consumers will buy more gasoline over the December holiday period than they bought during the summer holiday period even if the price of gas is 10 cents a litre higher than it was during the summer.
- C) Government cuts in welfare spending impose an unfair hardship on the poor.
- D) A wheat shortage or surplus is always the result of federal government policies.
- E) Hurricane Irene caused more damage in the United States than Hurricane Katrina.

Answer: C

Type: MC

## 1.5 Appendix: Graphing Data

Use the figure below to answer the following questions.



**Figure 1A.1.5**

- 1) The graphs in Figure 1A.1.5 are examples of
- A) dot graphs.
  - B) graphs that show no relationship between  $x$  and  $y$ .
  - C) dot diagrams.
  - D) scatter diagrams.
  - E) none of the above.

Answer: D

Diff: 1 Type: MC

Topic: Appendix: Graphing Data

2) Refer to Figure 1A.1.5. Which graph or graphs indicates a positive relationship between  $x$  and  $y$ ?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (a) and (d)

Answer: A

Diff: 2 Type: MC

Topic: Appendix: Graphing Data

3) Refer to Figure 1A.1.5. Which graph or graphs indicates a negative relationship between  $x$  and  $y$ ?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (b) and (d)

Answer: B

Diff: 2 Type: MC

Topic: Appendix: Graphing Data

4) Refer to Figure 1A.1.5. Which graph or graphs indicates no relationship between  $x$  and  $y$ ?

- A) (a)
- B) (b)
- C) (c)
- D) (c) and (d)
- E) (a) and (b)

Answer: D

Diff: 3 Type: MC

Topic: Appendix: Graphing Data

5) Consider graph (a) of Figure 1A.1.5. Which one of the following statements is *true*?

- A)  $x$  and  $y$  are negatively related.
- B)  $x$  and  $y$  are unrelated.
- C)  $x$  and  $y$  are positively related.
- D)  $x$  and  $y$  move in opposite directions.
- E) both A and D are correct.

Answer: C

Diff: 2 Type: MC

Topic: Appendix: Graphing Data

6) Consider graph (b) of Figure 1A.1.5. Which one of the following statements is *true*?

- A)  $x$  and  $y$  are negatively related.
- B)  $x$  and  $y$  are unrelated.
- C)  $x$  and  $y$  are positively related.
- D)  $x$  and  $y$  move in opposite directions.
- E) both A and D are correct.

Answer: E

Diff: 3 Type: MC

Topic: Appendix: Graphing Data

7) Consider graph (d) of Figure 1A.1.5. Which one of the following statements is *true*?

- A)  $x$  and  $y$  are negatively related.
- B)  $x$  and  $y$  are unrelated.
- C)  $x$  and  $y$  are positively related.
- D)  $x$  and  $y$  move in opposite directions.
- E) both A and D.

Answer: B

Diff: 3 Type: MC

Topic: Appendix: Graphing Data

## 1.6 Appendix: Graphs Used in Economic Models

1) If variables  $x$  and  $y$  move up and down together, they are

- A) positively related.
- B) negatively related.
- C) conversely related.
- D) unrelated.
- E) trendy.

Answer: A

Diff: 2 Type: MC

Topic: Appendix: Graphs Used in Economic Models

Source: Study Guide

2) Two variables are positively related if

- A) increases in one are associated with decreases in the other.
- B) increases in one are associated with increases in the other.
- C) decreases in one are associated with increases in the other.
- D) any change in one causes an increase in the other.
- E) any change in one causes a decrease in the other.

Answer: B

Diff: 2 Type: MC

Topic: Appendix: Graphs Used in Economic Models

3) Two variables are negatively related if

- A) increases in one are associated with decreases in the other.
- B) increases in one are associated with increases in the other.
- C) both variables are less than zero.
- D) any change in one causes an increase in the other.
- E) any change in one causes a decrease in the other.

Answer: A

Diff: 2 Type: MC

Topic: Appendix: Graphs Used in Economic Models

4) The relationship between two variables that are positively related is shown graphically by a line that

- A) slopes upward to the right.
- B) is horizontal.
- C) slopes downward to the right.
- D) is vertical.
- E) is above the  $x$ -axis and to the right of the  $y$ -axis.

Answer: A

Diff: 2 Type: MC

Topic: Appendix: Graphs Used in Economic Models

5) The relationship between two variables that are negatively related is shown graphically by a line that

- A) slopes upward to the right.
- B) is horizontal.
- C) slopes downward to the right.
- D) is vertical.
- E) is below the  $x$ -axis and to the left of the  $y$ -axis.

Answer: C

Diff: 2 Type: MC

Topic: Appendix: Graphs Used in Economic Models

Use the figure below to answer the following question.

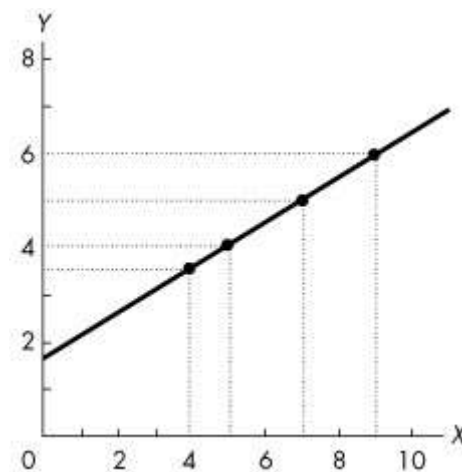


Figure 1A.2.1

6) Refer to Figure 1A.2.1. The variables  $x$  and  $y$

- A) are negatively related.
- B) have a nonlinear relationship.
- C) have a negative linear relationship.
- D) are unrelated.
- E) are positively related.

Answer: E

Diff: 2 Type: MC

Topic: Appendix: Graphs Used in Economic Models

7) In Figure 1A.2.1, the value of  $y$  is 5 when  $x$  is

- A) 4.
- B) 5.
- C) 6.
- D) 7.
- E) 8.

Answer: D

Diff: 1 Type: MC

Topic: Appendix: Graphs Used in Economic Models

- 8) Refer to Figure 1A.2.1. If  $x$  decreases from 5 to 4,  $y$
- A) decreases from 4 to 3.
  - B) decreases from 4 to  $3\frac{1}{2}$ .
  - C) decreases from 4 to 2.
  - D) increases from 4 to 5.
  - E) increases from  $3\frac{1}{2}$  to 4.

Answer: B

Diff: 1 Type: MC

Topic: Appendix: Graphs Used in Economic Models

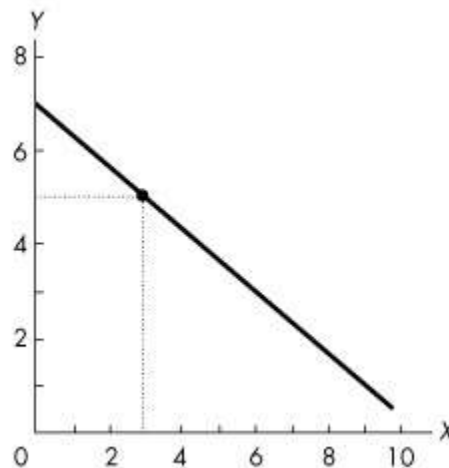
- 9) Refer to Figure 1A.2.1. When  $y$  increases from 5 to 6,  $x$
- A) increases from 5 to 6.
  - B) increases from 7 to 8.
  - C) increases from 7 to 9.
  - D) decreases from 9 to 7.
  - E) increases from 7 to  $7\frac{1}{2}$ .

Answer: C

Diff: 1 Type: MC

Topic: Appendix: Graphs Used in Economic Models

*Use the figure below to answer the following question.*



**Figure 1A.2.2**

- 10) In Figure 1A.2.2, the variables  $x$  and  $y$
- A) move in the same direction.
  - B) are negatively related.
  - C) are always equal.
  - D) are unrelated
  - E) are positively related.

Answer: B

Diff: 1 Type: MC

Topic: Appendix: Graphs Used in Economic Models

11) The relationship between two variables that move in opposite directions is shown graphically by a line that is

A) positively sloped.

B) relatively steep.

C) relatively flat.

D) negatively sloped.

E) curved.

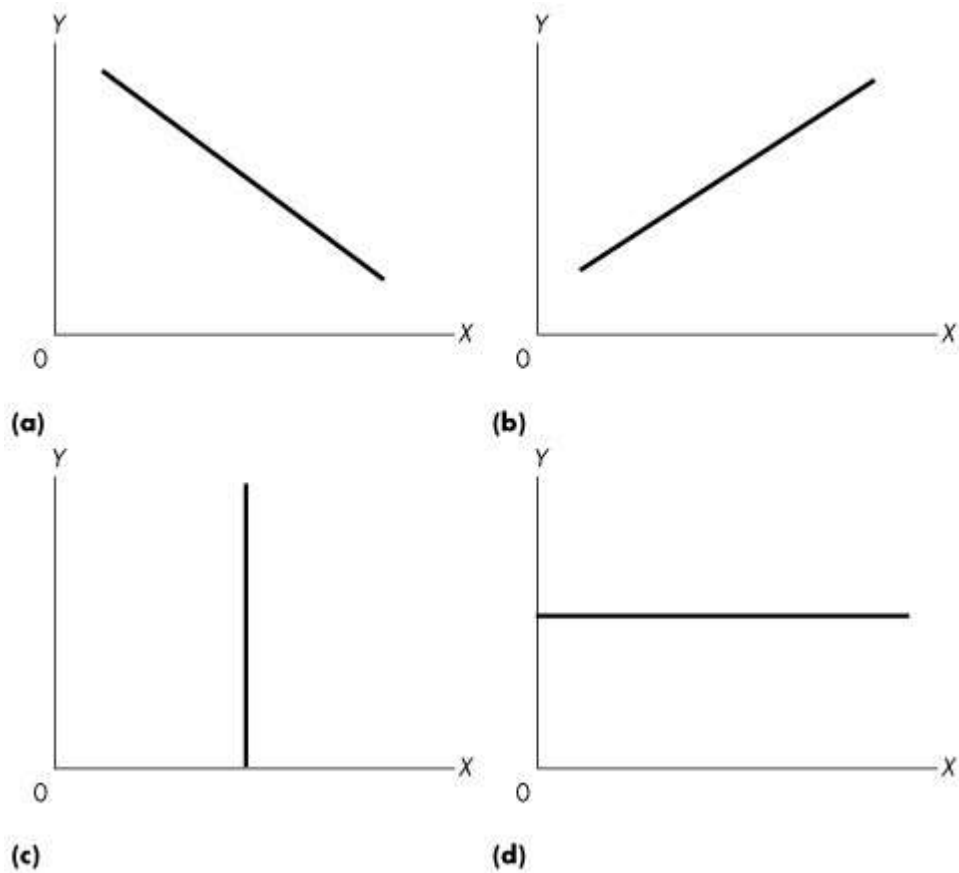
Answer: D

Diff: 1 Type: MC

Topic: Appendix: Graphs Used in Economic Models

Source: Study Guide

Use the figure below to answer the following questions.



**Figure 1A.2.3**

12) Refer to Figure 1A.2.3. If you were told that economic theory predicts that higher levels of the rate of interest ( $x$ ) lead to lower levels of sales of houses ( $y$ ), which graph would you pick to represent this economic relationship?

- A) (a) or (d)
- B) (d)
- C) (b)
- D) (c)
- E) (a)

Answer: E

Diff: 2 Type: MC

Topic: Appendix: Graphs Used in Economic Models

13) Refer to Figure 1A.2.3. If your theory predicted that a rise in the wage rate ( $x$ ) leads to a rise in the amount of labour supplied in the economy ( $y$ ), which graph would you use to represent this relationship?

- A) (a) or (c)
- B) (d)
- C) (c)
- D) (b)
- E) (a)

Answer: D

Diff: 2 Type: MC

Topic: Appendix: Graphs Used in Economic Models

14) Refer to Figure 1A.2.3. Which of the graphs shows a positive relationship between  $x$  and  $y$ ?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) both (b) and (d)

Answer: B

Diff: 1 Type: MC

Topic: Appendix: Graphs Used in Economic Models

15) Refer to Figure 1A.2.3. Which one of the graphs shows a negative relationship between  $x$  and  $y$ ?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) both (a) and (d)

Answer: A

Diff: 1 Type: MC

Topic: Appendix: Graphs Used in Economic Models

16) Refer to Figure 1A.2.3. Suppose our theory predicted that for low levels of quantity produced ( $x$ ) a firm's profits ( $y$ ) were low, for medium levels of output their profits were high, and for high levels of output their profits were low again. Which one of the graphs would represent this relationship?

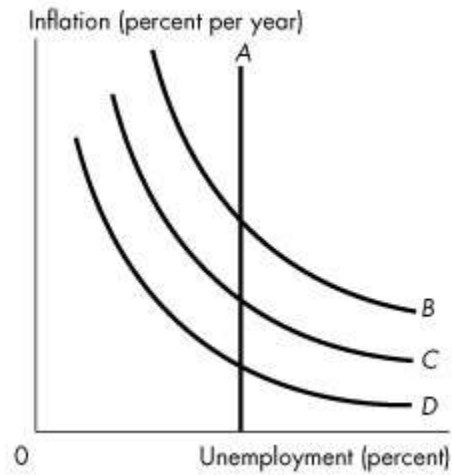
- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) none of the graphs

Answer: E

Diff: 2 Type: MC

Topic: Appendix: Graphs Used in Economic Models

Use the figure below to answer the following questions.



**Figure 1A.2.4**

17) Which curve or curves in Figure 1A.2.4 shows a positive relationship between unemployment and inflation?

- A) *A*
- B) *A* and *B*
- C) *B*, *C*, and *D*
- D) *A* and *C*
- E) none of the curves.

Answer: E

Diff: 1 Type: MC

Topic: Appendix: Graphs Used in Economic Models

18) Which curve or curves in Figure 1A.2.4 shows no relationship between unemployment and inflation?

- A) *A*
- B) *A* and *B*
- C) *B*, *C*, and *D*
- D) *A* and *C*
- E) *B* and *D*

Answer: A

Diff: 1 Type: MC

Topic: Appendix: Graphs Used in Economic Models

19) Which curve or curves in Figure 1A.2.4 shows a negative relationship between unemployment and inflation?

- A) *A*
- B) *A* and *B*
- C) *B*, *C*, and *D*
- D) *A* and *D*
- E) *B* and *C*

Answer: C

Diff: 1 Type: MC

Topic: Appendix: Graphs Used in Economic Models

*Use the table below to answer the following question.*

**Table 1A.2.1**

Year	<i>x</i>	<i>y</i>
2000	6.2	143
2001	5.7	156
2002	5.3	162

20) The data in Table 1A.2.1 shows that

- A) *x* and *y* have a negative relationship.
- B) *x* and *y* have a positive relationship.
- C) there is no relationship between *x* and *y*.
- D) there is first a negative and then a positive relationship between *x* and *y*.
- E) there is first a positive and then a negative relationship between *x* and *y*.

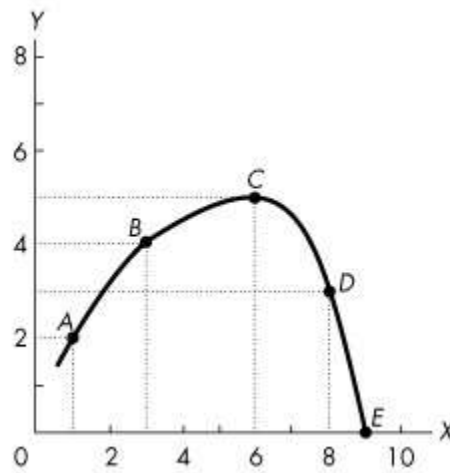
Answer: A

Diff: 2 Type: MC

Topic: Appendix: Graphs Used in Economic Models

Source: Study Guide

Use the figure below to answer the following questions.



**Figure 1A.2.5**

21) Refer to Figure 1A.2.5. Which one of the following statements is true?

- A)  $x$  and  $y$  are positively related at all points between  $A$  and  $D$ .
- B)  $x$  and  $y$  are negatively related at all points between points  $B$  and  $D$ .
- C)  $y$  reaches a maximum at point  $C$ .
- D)  $y$  reaches a minimum at point  $C$ .
- E)  $x$  and  $y$  are unrelated.

Answer: C

Diff: 1 Type: MC

Topic: Appendix: Graphs Used in Economic Models

Use the table below to answer the following question.

**Table 1A.2.2**

$y$	4	6	8	10	12
$z$	1	2	3	4	5

22) Refer to Table 1A.2.2. What type of relationship exists between  $y$  and  $z$ ?

- A) negative
- B) positive
- C) inverse
- D) No consistent relationship exists.
- E) first a positive relationship, then a negative one

Answer: B

Diff: 2 Type: MC

Topic: Appendix: Graphs Used in Economic Models

Use the table below to answer the following questions.

**Table 1A.2.3**

$w$	2	4	6	8	10
$u$	15	12	9	6	3

23) Refer to Table 1A.2.3. What type of relationship exists between  $w$  and  $u$ ?

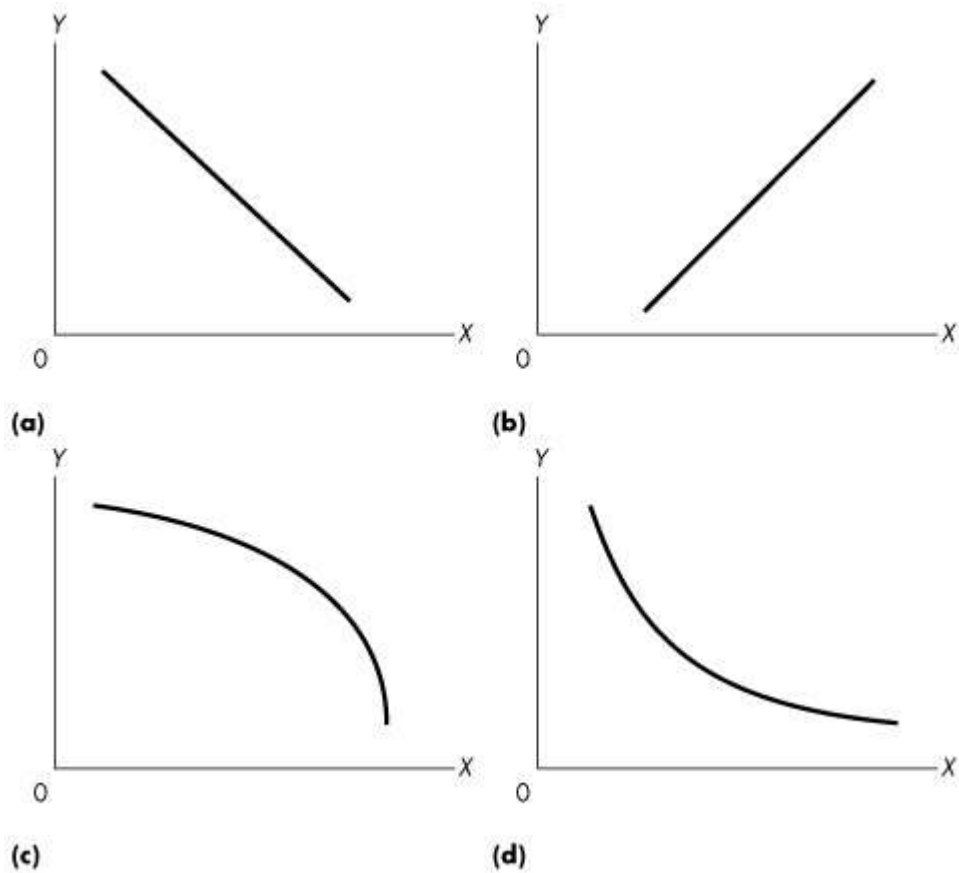
- A) positive
- B) negative
- C) direct
- D) No consistent relationship exists.
- E) first a positive relationship, then a negative one

Answer: B

Diff: 2 Type: MC

Topic: Appendix: Graphs Used in Economic Models

Use the figure below to answer the following question.



**Figure 1A.2.6**

24) Refer to Figure 1A.2.6. Consider the values for  $x$  and  $y$  given in the following table:

$x$	2	4	6	8	10
$y$	12	8	5	3	2

Which one of the graphs in Figure A1.13 represents the relationship between  $x$  and  $y$ ?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (a) and (b)

Answer: D

Diff: 1 Type: MC

Topic: Appendix: Graphs Used in Economic Models

## 1.7 Appendix: The Slope of a Relationship

1) The change in the value of the variable measured on the  $y$ - axis divided by the change in the value of the variable measures on the  $x$ -axis is

- A) increasing.
- B) slope.
- C) decreasing.
- D) constant.
- E) a maximum or minimum.

Answer: B

Diff: 1 Type: MC

Topic: Appendix: The Slope of a Relationship

2) The slope of a horizontal line is

- A) positive.
- B) negative.
- C) zero.
- D) infinite.
- E) initially positive and then negative.

Answer: C

Diff: 1 Type: MC

Topic: Appendix: The Slope of a Relationship

3) The slope of a straight line

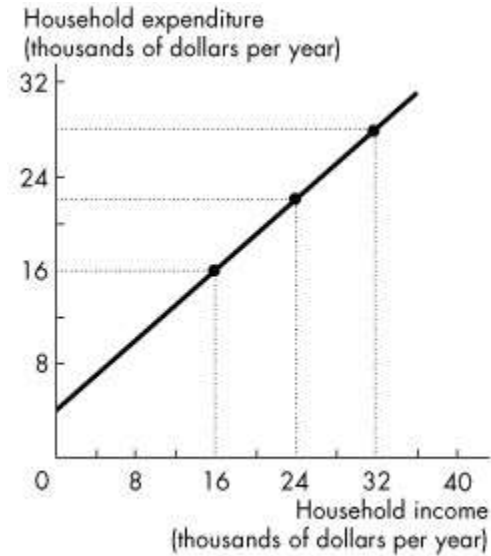
- A) is the same at every point.
- B) increases as the variable on the  $x$ -axis increases if the slope is positive.
- C) decreases as the variable on the  $x$ -axis increases if the slope is negative.
- D) is the same at every point only if the line is horizontal.
- E) depends on where you measure the slope.

Answer: A

Diff: 1 Type: MC

Topic: Appendix: The Slope of a Relationship

Use the figure below to answer the following questions.



**Figure 1A.3.1**

4) In Figure 1A.3.1, if household income increases by \$1 000, household expenditure will

- A) increase by \$1 333.
- B) decrease by \$1 333.
- C) remain unchanged.
- D) increase by \$1 000.
- E) increase by \$750.

Answer: E

Diff: 2 Type: MC

Topic: Appendix: The Slope of a Relationship

Source: Study Guide

5) The slope of the line in Figure 1A.3.1 is

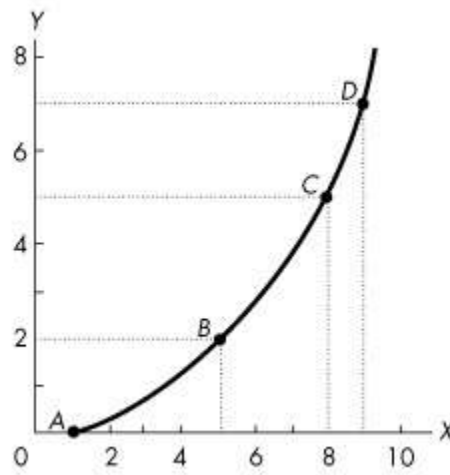
- A) 0.50.
- B) 0.75.
- C) 1.00
- D) 1.25.
- E) 1.50.

Answer: B

Diff: 2 Type: MC

Topic: Appendix: The Slope of a Relationship

Use the figure below to answer the following question.



**Figure 1A.3.2**

6) Refer to Figure 1A.3.2. The slope across the arc between A and B is

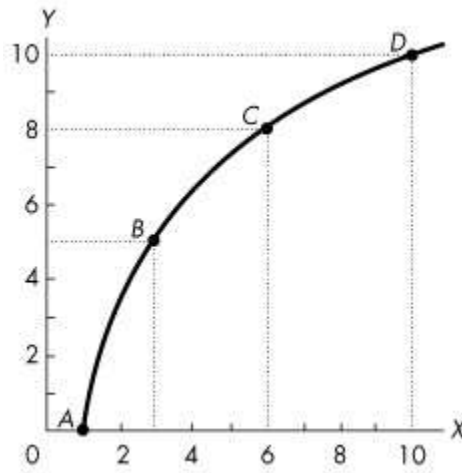
- A)  $1/2$ .
- B)  $2/3$ .
- C) 1.
- D) 2.
- E) 3.

Answer: A

Diff: 2 Type: MC

Topic: Appendix: The Slope of a Relationship

Use the figure below to answer the following questions.



**Figure 1A.3.3**

- 7) Figure 1A.3.3 illustrates two variables,  $x$  and  $y$ , which are
- A) negatively related, with a decreasing slope as  $x$  increases.
  - B) negatively related, with an increasing slope as  $x$  increases.
  - C) positively related, with a decreasing slope as  $x$  increases.
  - D) positively related, with an increasing slope as  $x$  increases.
  - E) positively related, with slope first increasing then decreasing.

Answer: C

Diff: 2 Type: MC

Topic: Appendix: The Slope of a Relationship

- 8) In Figure 1A.3.3, the slope across arc  $AB$  is

- A)  $1/2$ .
- B) 1.
- C)  $3/2$ .
- D)  $5/2$ .
- E)  $5/3$ .

Answer: D

Diff: 2 Type: MC

Topic: Appendix: The Slope of a Relationship

9) In Figure 1A.3.3 the relationship between  $x$  and  $y$  as  $x$  increases is

- A) positive with decreasing slope.
- B) negative with decreasing slope.
- C) negative with increasing slope.
- D) positive with increasing slope.
- E) positive with slope first increasing then decreasing.

Answer: A

Diff: 3 Type: MC

Topic: Appendix: The Slope of a Relationship

Source: Study Guide

10) What is the slope across the arc between  $B$  and  $C$  in Figure 1A.3.3?

- A)  $1/2$ .
- B)  $2/3$
- C) 1
- D) 2
- E) 3

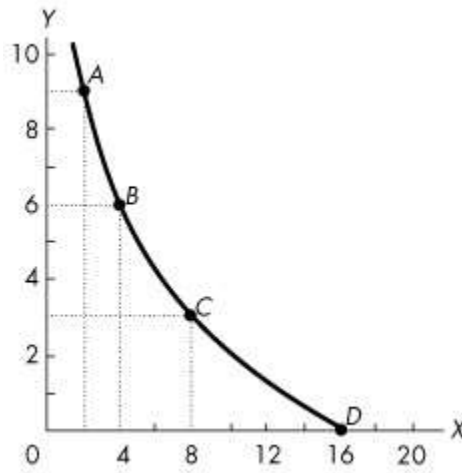
Answer: C

Diff: 2 Type: MC

Topic: Appendix: The Slope of a Relationship

Source: Study Guide

Use the figure below to answer the following questions.



**Figure 1A.3.4**

- 11) Figure 1A.3.4 illustrates two variables,  $x$  and  $y$ , which are
- A) negatively related, with slope becoming closer to 0 as  $x$  increases from 2 to 16.
  - B) negatively related, with slope becoming farther from 0 as  $x$  increases from 2 to 16.
  - C) positively related, with slope becoming closer to 0 as  $x$  increases from 2 to 16.
  - D) positively related, with slope becoming farther from 0 as  $x$  increases from 2 to 16.
  - E) positively related, with the slope unchanging as  $x$  increases from 2 to 16.

Answer: A

Diff: 2 Type: MC

Topic: Appendix: The Slope of a Relationship

- 12) In Figure 1A.3.4, the slope across arc  $AB$  is

- A)  $2/3$ .
- B)  $-1$ .
- C)  $-3/2$ .
- D)  $-3$ .
- E)  $-9/4$ .

Answer: C

Diff: 2 Type: MC

Topic: Appendix: The Slope of a Relationship

- 13) In Figure 1A.3.4, the slope across arc  $BC$  is

- A)  $-2/3$ .
- B)  $-3/2$ .
- C)  $-2$ .
- D)  $-4/3$ .
- E)  $-3/4$ .

Answer: E

Diff: 2 Type: MC

Topic: Appendix: The Slope of a Relationship

14) Refer to Figure 1A.3.4. In Figure 1A.3.4, the slope at point  $B$

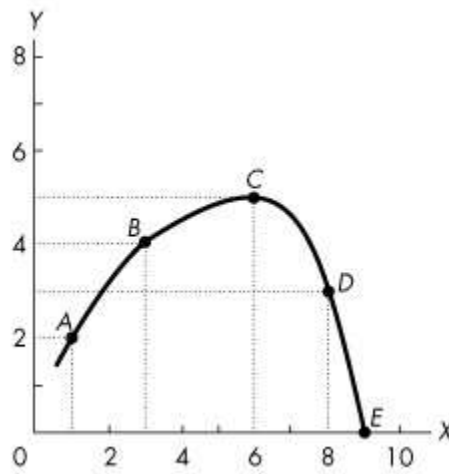
- A) lies between  $-2/3$  and  $-1$ .
- B) lies between  $-3/4$  and  $-3/2$ .
- C) lies between  $-2/3$  and  $-4/3$ .
- D) lies between  $1$  and  $3/2$ .
- E) is greater than  $3/2$ .

Answer: B

Diff: 2 Type: MC

Topic: Appendix: The Slope of a Relationship

Use the figure below to answer the following questions.



**Figure 1A.3.5**

15) Refer to Figure 1A.3.5. Which one of the following statements is true?

- A) The slope is less between points  $A$  and  $B$  than between points  $B$  and  $C$ .
- B) The slope is greater between points  $B$  and  $C$  than between points  $A$  and  $B$ .
- C) The slope at  $C$  is 0.
- D) The slope at  $C$  is 1.
- E) The slope at  $C$  is negative.

Answer: C

Diff: 2 Type: MC

Topic: Appendix: The Slope of a Relationship

- 16) Refer to Figure 1A.3.5. In Figure 1A.3.5, the slope across arc  $BC$  is
- A)  $1/3$ .
  - B)  $1/2$ .
  - C) 1.
  - D) 2.
  - E)  $5/6$ .

Answer: A

Diff: 2 Type: MC

Topic: Appendix: The Slope of a Relationship

- 17) Refer to Figure 1A.3.5. In Figure 1A.3.5, the slope across arc  $CD$  is
- A)  $1/2$ .
  - B) 1.
  - C)  $-1/2$ .
  - D) -1.
  - E)  $-5/8$ .

Answer: D

Diff: 2 Type: MC

Topic: Appendix: The Slope of a Relationship

*Use the table below to answer the following question.*

**Table 1A.3.1**

$y$	4	6	8	10	12
$z$	1	2	3	4	5

- 18) Refer to Table 1A.3.1. Assuming  $y$  is plotted on the vertical axis, the slope of the line is
- A) constant at -2.
  - B) -2 when  $x$  is between 1 and 3.
  - C) -2 when  $x$  is between 1 and 3, and then +2 when  $x$  is between 4 and 5.
  - D) -2 when  $x$  is between 4 and 5.
  - E) constant at +2.

Answer: E

Diff: 2 Type: MC

Topic: Appendix: The Slope of a Relationship

Use the table below to answer the following questions.

**Table 1A.3.2**

$w$	2	4	6	8	10
$u$	15	12	9	6	3

19) In Table 1A.3.2, suppose that  $w$  is measured along the  $x$ -axis. The slope of the line relating  $w$  and  $u$  is

- A) positive with a decreasing slope.
- B) negative with a decreasing slope.
- C) positive with an increasing slope.
- D) negative with a constant slope.
- E) positive with a constant slope.

Answer: D

Diff: 2 Type: MC

Topic: Appendix: The Slope of a Relationship

Source: Study Guide

20) Refer to Table 1A.3.2. Suppose that  $w$  is measured along the  $x$ -axis. The slope of the line relating  $w$  and  $u$  is

- A) +3.
- B) -3.
- C)  $-2/3$ .
- D)  $+3/2$ .
- E)  $-3/2$ .

Answer: E

Diff: 2 Type: MC

Topic: Appendix: The Slope of a Relationship

Source: Study Guide

Use the table below to answer the following questions.

**Table 1A.3.3**

$x$	0	1	2	3	4	5	6	7	9	9
$y$	10	8	6	4	2	0	2	4	6	8

21) Refer to Table 1A.3.3. If we were to draw a graph of this relationship, when would the slope be positive?

- A) never
- B) only if  $x$  is less than 5
- C) only if  $x$  equals 5
- D) only if  $x$  is greater than 5
- E) We do not have enough information to tell.

Answer: D

Diff: 3 Type: MC

Topic: Appendix: The Slope of a Relationship

22) Refer to Table 1A.3.3. When  $x$  equals 5, the slope is

- A) 5.
- B) -2.
- C) +2.
- D) 0.
- E) infinite.

Answer: D

Diff: 3 Type: MC

Topic: Appendix: The Slope of a Relationship

23) Refer to Table 1A.3.3. When  $x$  equals 5,

- A)  $y$  is at a maximum.
- B)  $y$  is at a minimum.
- C) the slope is positive.
- D) the slope is negative.
- E) the slope is first positive and then becomes negative.

Answer: B

Diff: 2 Type: MC

Topic: Appendix: The Slope of a Relationship

24) At all points along a straight line, slope is

- A) positive.
- B) negative.
- C) constant.
- D) zero.
- E) infinity.

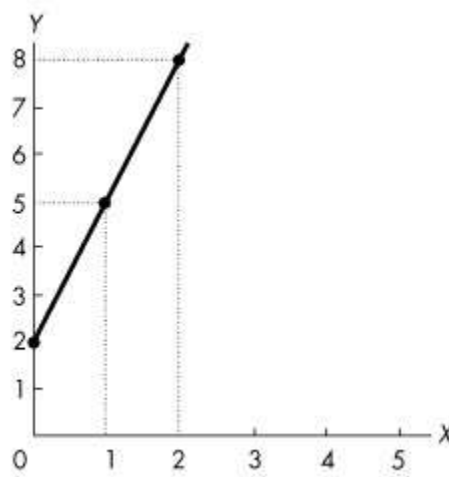
Answer: C

Diff: 1 Type: MC

Topic: Appendix: The Slope of a Relationship

Source: Study Guide

Use the figure below to answer the following question.



**Figure 1A.3.6**

25) What is the slope of the line in Figure A1.3.6?

- A) 2
- B)  $1/2$ .
- C) 3
- D)  $1/3$
- E) -3

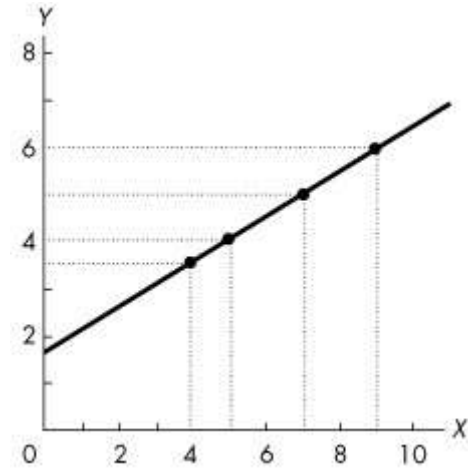
Answer: C

Diff: 1 Type: MC

Topic: Appendix: The Slope of a Relationship

Source: Study Guide

Use the figure below to answer the following question.



**Figure 1A.3.7**

26) The slope of the line in Figure 1A.3.7 is

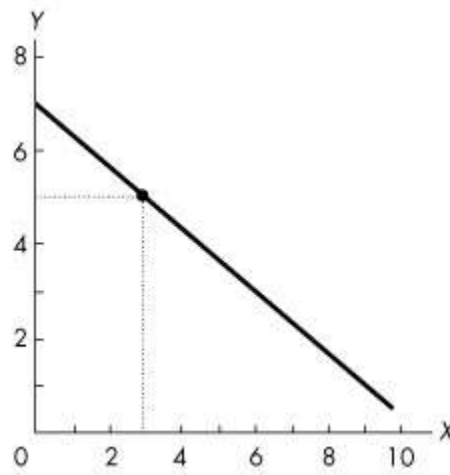
- A) 1.
- B) -1.
- C)  $1/2$ .
- D) 2.
- E) dependent on where you measure it.

Answer: C

Diff: 1 Type: MC

Topic: Appendix: The Slope of a Relationship

Use the figure below to answer the following question.



**Figure 1A.3.8**

27) The slope of the line in Figure 1A.3.8 is

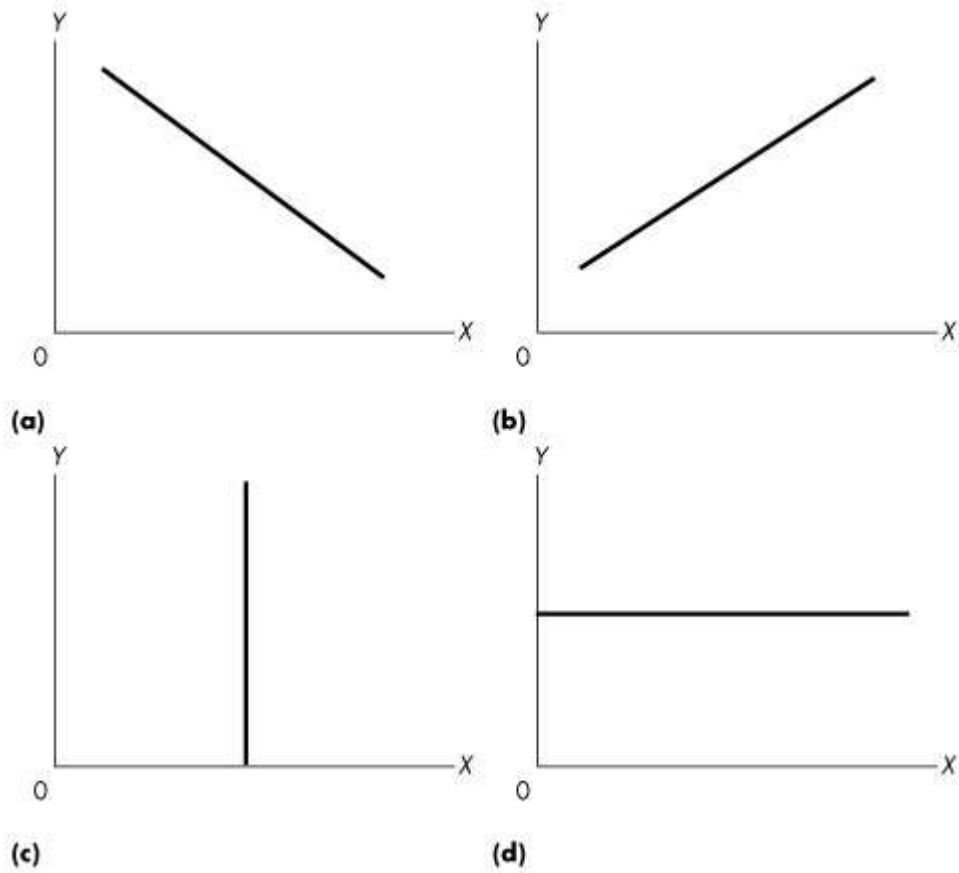
- A)  $3/2$ .
- B)  $2/3$ .
- C)  $-3/2$ .
- D)  $-2/3$ .
- E) none of the above.

Answer: D

Diff: 1 Type: MC

Topic: Appendix: The Slope of a Relationship

Use the figure below to answer the following questions.



**Figure 1A.3.9**

28) Refer to Figure 1A.3.9. Which one of the graphs shows a line with a zero slope?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (a), (b), and (c)

Answer: D

Diff: 1 Type: MC

Topic: Appendix: The Slope of a Relationship

29) Refer to Figure 1A.3.9. Which one of the graphs shows a line with an infinite slope?

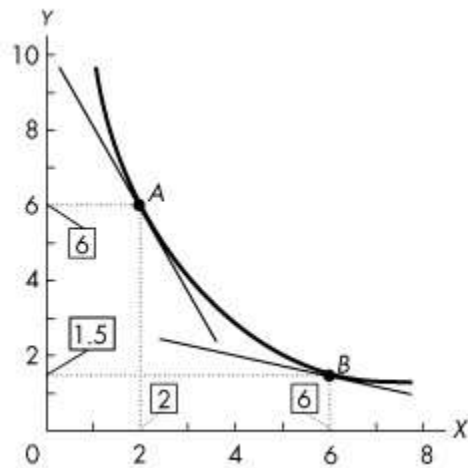
- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (b) and (c)

Answer: C

Diff: 1 Type: MC

Topic: Appendix: The Slope of a Relationship

Use the figure below to answer the following questions.



**Figure 1A.3.10**

30) Refer to Figure 1A.3.10. The figure shows a relationship between two variables,  $x$  and  $y$ . The slope at point A is

- A) 2
- B) -2
- C) 0.25
- D) -0.25
- E) -4

Answer: B

Diff: 1 Type: MC

Topic: Appendix: The Slope of a Relationship

Source: MyEconLab

31) Refer to Figure 1A.3.10. The figure shows a relationship between two variables,  $x$  and  $y$ . The slope at point  $B$  is

- A) 2
- B) -2
- C) 0.25
- D) -0.25
- E) 0.5

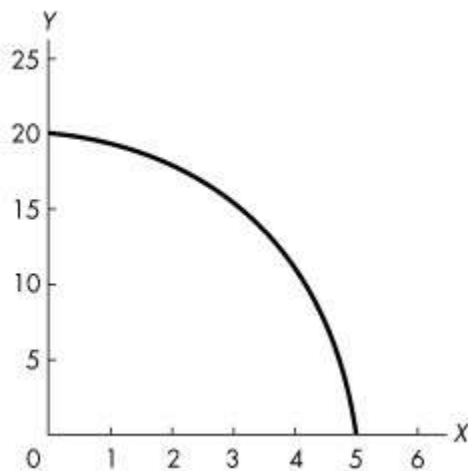
Answer: D

Diff: 1 Type: MC

Topic: Appendix: The Slope of a Relationship

Source: MyEconLab

Use the figure below to answer the following question.



**Figure 1A.3.11**

32) Refer to Figure 1A.3.11. The graph shows a \_\_\_\_\_ relationship. The absolute value of the slope of the relationship \_\_\_\_\_ as the value of  $x$  increases.

- A) positive; increases
- B) positive; decreases
- C) negative; decreases
- D) negative; increases
- E) negative; does not change

Answer: D

Diff: 1 Type: MC

Topic: Appendix: The Slope of a Relationship

Source: MyEconLab

## 1.8 Appendix: Graphing Relationships Among More Than Two Variables

- 1) To graph a relationship among three variables we
- A) hold two variables constant to graph the third variable.
  - B) hold one variable constant and graph the relationship between the other two variables.
  - C) graph each of the three variables using a separate set of axes.
  - D) must be able to draw in three dimensions.
  - E) must be able to allow all three variables to vary simultaneously in one graph.

Answer: B

Diff: 2 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

*Use the table below to answer the following questions.*

**Table 1A.4.1**

$x$	120	100	80	140	120	100	160	140	120
$y$	10	12	14	10	12	14	10	12	14
$z$	4	4	4	5	5	5	6	6	6

- 2) Given the data in Table 1A.4.1, holding  $z$  constant, the graph of  $x$  and  $y$
- A) is a negatively sloped line.
  - B) is a positively sloped line.
  - C) reaches a maximum.
  - D) reaches a minimum.
  - E) does not have a constant slope.

Answer: A

Diff: 3 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

- 3) Given the data in Table 1A.4.1, holding  $y$  constant, the graph of  $x$  and  $z$
- A) is a negatively sloped line.
  - B) is a positively sloped line.
  - C) reaches a maximum.
  - D) reaches a minimum.
  - E) shows that  $x$  and  $z$  are not related.

Answer: B

Diff: 3 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

4) Consider the data in Table 1A.4.1. Suppose  $z$  increases from 4 to 5. What will happen to the graph of the relationship between  $x$  and  $y$ ?

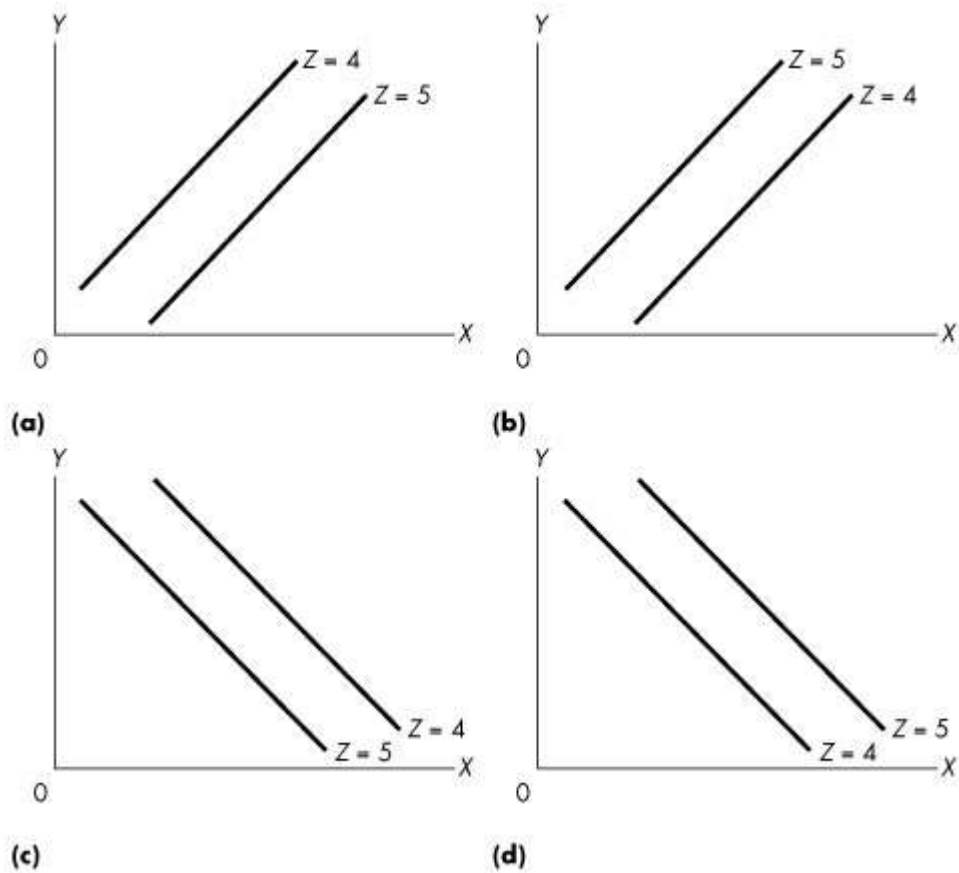
- A) It will shift to the right.
- B) It will shift to the left.
- C) It will become positively sloped.
- D) both A and C
- E) both B and C

Answer: A

Diff: 3 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

Use the figure below to answer the following question.



**Figure 1A.4.1**

5) Given the data in the following table, which one of the graphs in Figure 1A.4.1 correctly represents the relationship among  $x$ ,  $y$ , and  $z$ ?

$x$	120	100	80	140	120	100	160	140	120
$y$	10	12	14	10	12	14	10	12	14
$z$	4	4	4	5	5	5	6	6	6

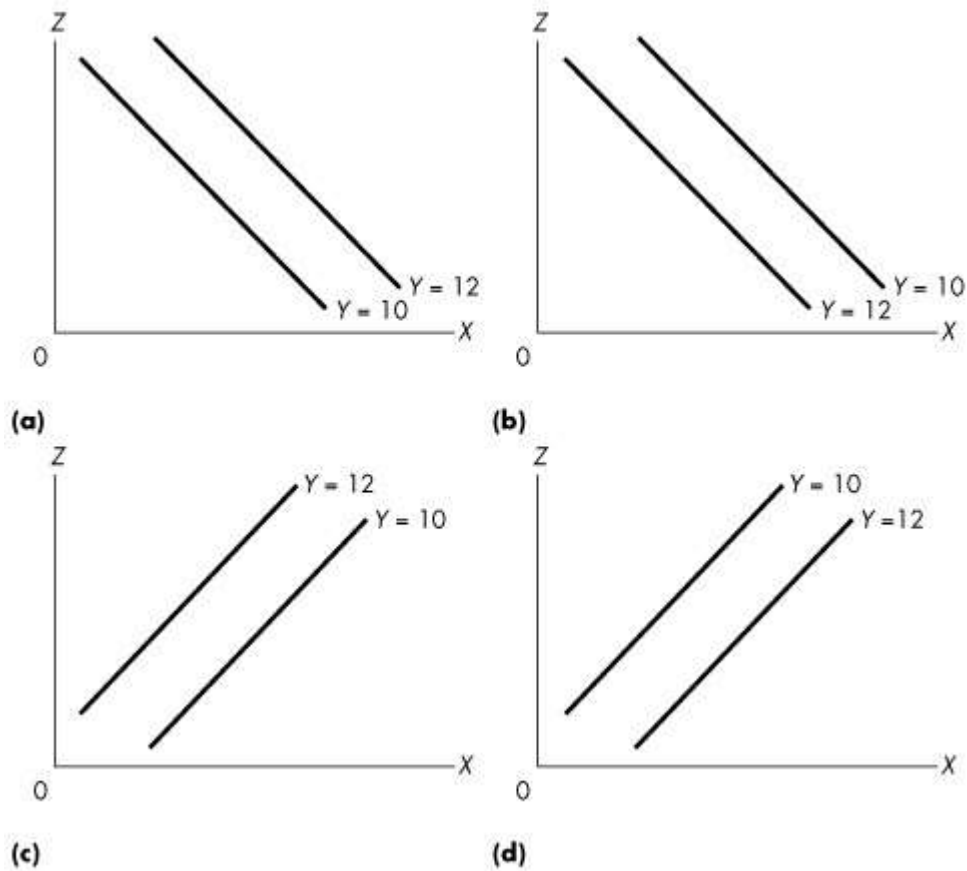
- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (b) and (c)

Answer: D

Diff: 3 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

Use the figure below to answer the following question.



**Figure 1A.4.2**

6) Given the data in the following table, which one of the graphs in Figure 1A.4.2 correctly represents the relationship among  $x$ ,  $y$ , and  $z$ ?

$x$	120	100	80	140	120	100	160	140	120
$y$	10	12	14	10	12	14	10	12	14
$z$	4	4	4	5	5	5	6	6	6

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (a) and (d)

Answer: C

Diff: 3 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

Use the table below to answer the following questions.

**Table 1A.4.2**

Family income (dollars per week)	Price of strawberries (dollars per box)	Number of boxes purchased per week
300	1.00	5
300	1.25	3
300	1.50	2
400	1.00	7
400	1.25	5
400	1.50	4

7) Table 1A.4.2 shows that,

- A) the number of boxes of strawberries purchased is negatively related to the price of strawberries, holding income constant.
- B) the number of boxes of strawberries purchased is negatively related to income, holding the price of strawberries constant.
- C) the price of strawberries is negatively related to family income, holding purchases of strawberries constant.
- D) B and C.
- E) A and B.

Answer: A

Diff: 3 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

8) Given the data in Table 1A.4.2, holding income constant, the graph relating the price of strawberries, measured on the  $y$ -axis and the purchases of strawberries, measured on the  $x$ -axis

- A) is a vertical line.
- B) is a horizontal line.
- C) is a positively sloped line.
- D) is a negatively sloped line.
- E) reaches a minimum.

Answer: D

Diff: 3 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

Source: Study Guide

9) Given the data in Table 1A.4.2, suppose family income decreases from \$400 to \$300 per week. Then the graph relating the price of strawberries, measured on the  $y$ -axis and the number of boxes of strawberries purchased, measured on the  $x$ -axis will

- A) become negatively sloped.
- B) become positively sloped.
- C) shift rightward.
- D) shift leftward.
- E) no longer exist.

Answer: D

Diff: 3 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

Source: Study Guide

10) Given the data in Table 1A.4.2, holding price constant, the graph of the purchases of strawberries, measured on the  $x$ -axis and family income, measured on the  $y$ -axis is a

- A) vertical line.
- B) horizontal line.
- C) positively sloped line.
- D) negatively sloped line.
- E) positively or negatively sloped line, depending on the price that is held constant.

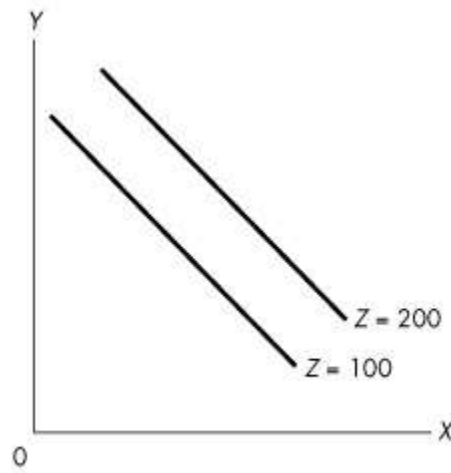
Answer: C

Diff: 3 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

Source: Study Guide

Use the figure below to answer the following question.



**Figure 1A.4.3**

11) In Figure 1A.4.3,  $x$  is

- A) positively related to  $y$  and negatively related to  $z$ .
- B) positively related to both  $y$  and  $z$ .
- C) negatively related to  $y$  and positively related to  $z$ .
- D) negatively related to both  $y$  and  $z$ .
- E) greater than  $z$ .

Answer: C

Diff: 3 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

Source: Study Guide

12) In Figure 1A.4.3, a decrease in the value of  $z$  results in, *ceteris paribus*,

- A) a decrease in the value of  $x$ .
- B) an increase in the value of  $x$ .
- C) an increase in the value of  $y$ .
- D) no change in the value of  $y$ .
- E) no change in the value of  $x$ .

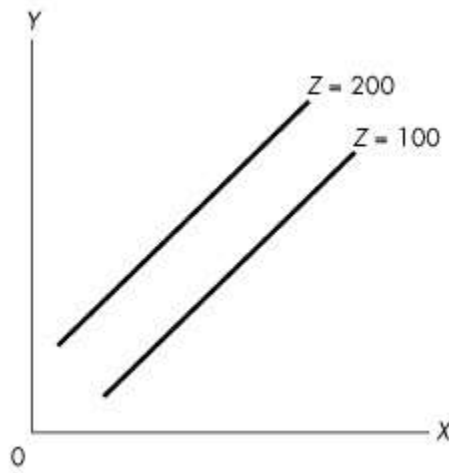
Answer: A

Diff: 3 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

Source: Study Guide

Use the figure below to answer the following question.



**Figure 1A.4.4**

13) Complete the following sentence. In Figure 1A.4.4,  $z$  is

- A) positively related to  $x$  and negatively related to  $y$ .
- B) negatively related to  $x$  and positively related to  $y$ .
- C) positively related to both  $x$  and  $y$ .
- D) negatively related to both  $x$  and  $y$ .
- E) related to  $y$  but not related to  $x$ .

Answer: B

Diff: 3 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

14) To graph a relationship among more than two variables, what assumption is necessary?

- A) normative
- B) positive
- C) linear
- D) independence of variables
- E) *ceteris paribus*

Answer: E

Diff: 1 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

Source: Study Guide

15) Consider the following information on cola sales by number of cases for a typical university residence floor:

Temp. (°C)	Price (dollars per case)			
	10.00	12.50	15.00	17.50
15	50	40	30	20
20	60	50	40	30
25	70	60	50	40
30	80	70	60	50
35	90	80	70	60

Cola sales and cola prices are

- A) inversely related.
- B) positively related.
- C) not affected by the temperature.
- D) unrelated.
- E) negatively related at low temperatures, but positively related at high temperatures.

Answer: A

Diff: 2 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

16) Consider the following information on cola sales by number of cases for a typical university residence floor:

Temp. (°C)	Price (dollars per case)			
	10.00	12.50	15.00	17.50
15	50	40	30	20
20	60	50	40	30
25	70	60	50	40
30	80	70	60	50
35	90	80	70	60

Cola sales and temperature are

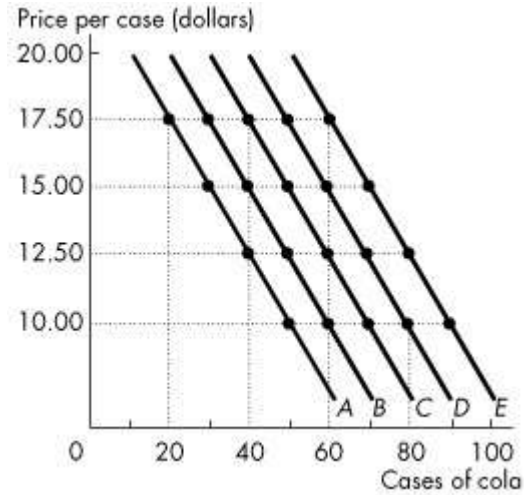
- A) inversely related.
- B) positively related.
- C) not affected by the price.
- D) unrelated.
- E) negatively related at low prices, but positively related at high prices.

Answer: B

Diff: 2 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

Use the figure below to answer the following questions.



**Figure 1A.4.5**

17) Consider the following information on cola sales by number of cases for a typical university residence floor:

Temp. (°C)	Price (dollars per case)			
	10.00	12.50	15.00	17.50
15	50	40	30	20
20	60	50	40	30
25	70	60	50	40
30	80	70	60	50
35	90	80	70	60

Refer to Figure 1A.4.5. Which line shows the relationship of cola sales and its price when the temperature is 30°C?

- A) A
- B) B
- C) C
- D) D
- E) E

Answer: D

Diff: 2 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

18) Consider the following information on cola sales by number of cases for a typical university residence floor:

Temp. (°C)	Price (dollars per case)			
	10.00	12.50	15.00	17.50
15	50	40	30	20
20	60	50	40	30
25	70	60	50	40
30	80	70	60	50
35	90	80	70	60

Refer to Figure 1A.4.5. Which line shows the relationship of cola sales and the temperature when the price of a case is \$15.00?

- A) *A*
- B) *B*
- C) *C*
- D) *D*
- E) none of the above.

Answer: E

Diff: 3 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

19) Consider the following information on cola sales by number of cases for a typical university residence floor:

Temp. (°C)	Price (dollars per case)			
	10.00	12.50	15.00	17.50
15	50	40	30	20
20	60	50	40	30
25	70	60	50	40
30	80	70	60	50
35	90	80	70	60

Refer to Figure 1A.4.5. Which one of the following represents what happens when the temperature rises from 20°C to 25°C?

- A) The curve shifts from *A* to *B*.
- B) The curve shifts from *C* to *B*.
- C) The curve shifts from *B* to *C*.
- D) The curve shifts along line *B*.
- E) The curve shifts along line *C*.

Answer: C

Diff: 3 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

- 20) The Latin term *ceteris paribus* means
- A) "Innocent until proven guilty."
  - B) "Fallacies are composed."
  - C) "Compositions are fallacious."
  - D) "The whole is not the sum of the parts."
  - E) "If all other relevant things remain the same."

Answer: E

Diff: 1 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

Source: Study Guide

Use the table below to answer the following question.

**Table 1A.4.3**

Price (dollars per scoop)	Ice cream consumption (litres per day)			
	0 degrees	10 degrees	20 degrees	30 degrees
<b>0.50</b>	<b>12</b>	<b>18</b>	<b>25</b>	<b>50</b>
<b>1.00</b>	<b>10</b>	<b>12</b>	<b>18</b>	<b>37</b>
<b>1.50</b>	<b>7</b>	<b>10</b>	<b>13</b>	<b>27</b>
<b>2.00</b>	<b>5</b>	<b>7</b>	<b>10</b>	<b>20</b>
<b>2.50</b>	<b>3</b>	<b>5</b>	<b>7</b>	<b>14</b>

21) Refer to Table 1A.4.3. The table shows some data on the quantity of ice cream consumed at different prices and in different weather conditions. To draw a graph of the relationship between the quantity of the ice cream consumed and the price of ice cream, we must \_\_\_\_\_.

- A) decrease the temperature as the price rises
- B) pick the temperature that prevailed when the price was \$1.00.
- C) increase the temperature as the price rises
- D) hold the temperature constant at any of the four levels shown
- E) hold the price constant at any of the five levels shown

Answer: D

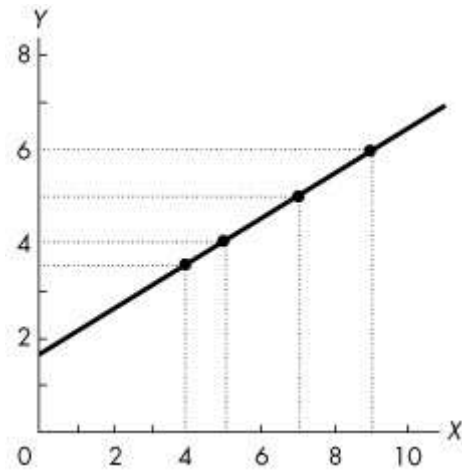
Diff: 3 Type: MC

Topic: Appendix: Graphing Relationships Among More Than Two Variables

Source: MyEconLab

1.9 Appendix: Mathematical Note

Use the figure below to answer the following question.



**Figure 1A.5.1**

1) The equation of the line in Figure 1A.5.1 is

A)  $y = 1.5 - 0.5x$ .

B)  $y = 1.5 + 2x$ .

C)  $y = 1.5 + 0.5x$ .

D)  $y = -3 + 2x$ .

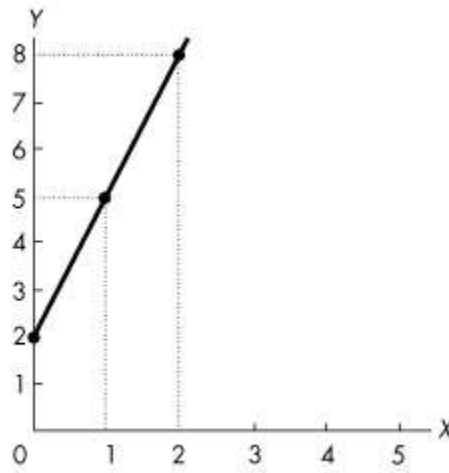
E) dependent on where you measure it.

Answer: C

Diff: 1 Type: MC

Topic: Appendix: Mathematical Note

Use the figure below to answer the following question.



**Figure 1A.5.2**

2) If the line in Figure 1A.5.2 were to continue down to the  $x$ -axis, what would the value of  $x$  be when  $y$  is zero?

- A) 0
- B) 2
- C)  $2/3$
- D)  $-2/3$
- E)  $-3/2$ .

Answer: D

Diff: 2 Type: MC

Topic: Appendix: Mathematical Note

Source: Study Guide

3) If the equation of a straight line is  $y = 6 + 3x$ , then the slope is

- A) -3 and the  $y$ -intercept is 6.
- B) -3 and the  $y$ -intercept is -2.
- C) 3 and the  $y$ -intercept is 6.
- D) 3 and the  $y$ -intercept is -2.
- E) 3 and the  $y$ -intercept is -6.

Answer: C

Diff: 1 Type: MC

Topic: Appendix: Mathematical Note

Source: Study Guide

4) If the equation of a straight line is  $y = 8 - 2x$ , then the slope is

- A) -2 and the  $x$ -intercept is -4.
- B) -2 and the  $x$ -intercept is 4.
- C) -2 and the  $x$ -intercept is 8.
- D) 2 and the  $x$ -intercept is -4.
- E) 2 and the  $x$ -intercept is 4.

Answer: B

Diff: 1 Type: MC

Topic: Appendix: Mathematical Note

Source: Study Guide

5) The equation of a line is  $y = 4 + 2x$ . What is the  $y$ -intercept of this line?

- A) 4
- B) -2
- C)  $-1/2$
- D)  $1/4$
- E) 0

Answer: A

Diff: 1 Type: MC

Topic: Appendix: Mathematical Note

6) The equation of a line is  $y = 4 + 2x$ . What is the  $x$ -intercept of this line?

- A) 4
- B) -2
- C)  $-1/2$
- D)  $1/4$
- E) 0

Answer: B

Diff: 2 Type: MC

Topic: Appendix: Mathematical Note

7) The equation of a line is  $y = 4 + 2x$ . What is the slope of this line?

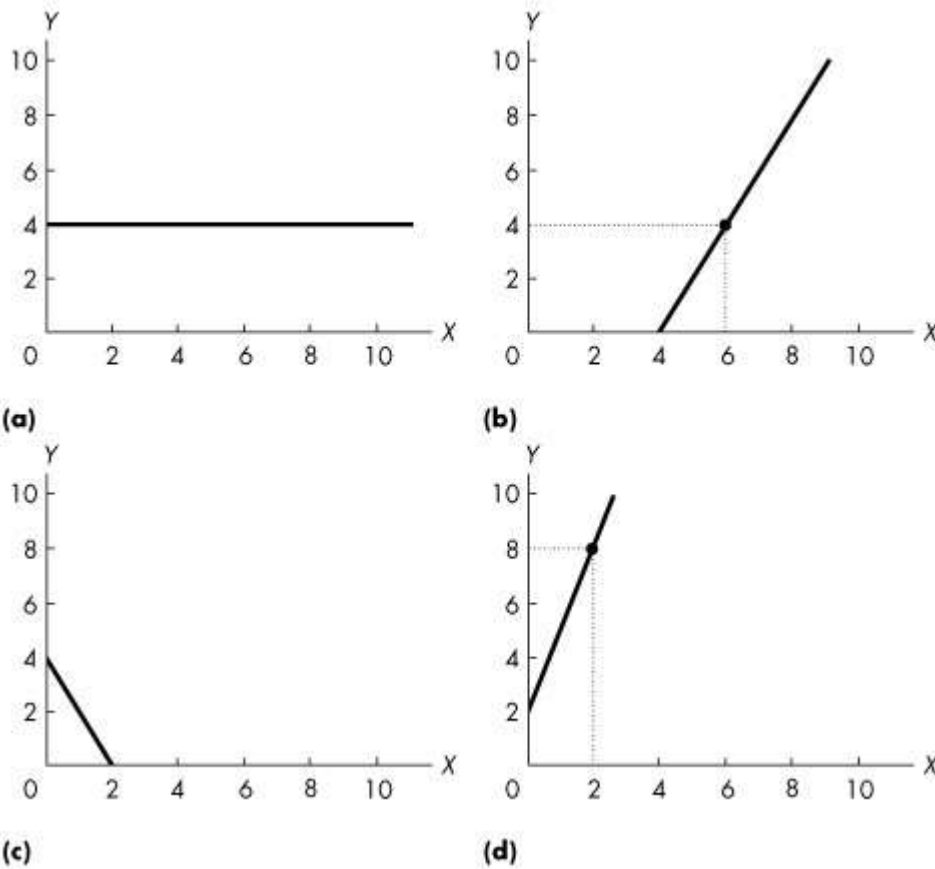
- A) 4
- B) 2
- C)  $1/2$
- D)  $1/4$
- E) 0

Answer: B

Diff: 1 Type: MC

Topic: Appendix: Mathematical Note

Use the figure below to answer the following questions.



**Figure 1A.5.3**

8) The equation of a line is  $y = 4 + 2x$ . Which one of the graphs in Figure 1A.5.3 represents this line?

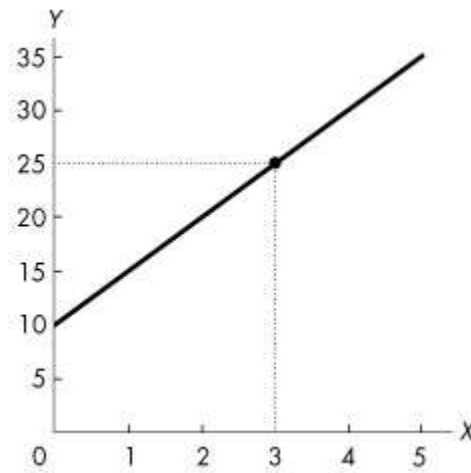
- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) none of the graphs

Answer: E

Diff: 2 Type: MC

Topic: Appendix: Mathematical Note

Use the figure below to answer the following question.



**Figure 1A.5.4**

9) Refer to Figure 1A.5.4. The graph shows the relationship between two variables,  $x$  and  $y$ . This relationship is described by the equation \_\_\_\_\_.

- A)  $y = 5x^2 + 10$
- B)  $y = 10x + 5$
- C)  $y = -5x + 10$
- D)  $y = 5x + 10$
- E)  $x = 10 + 5y$

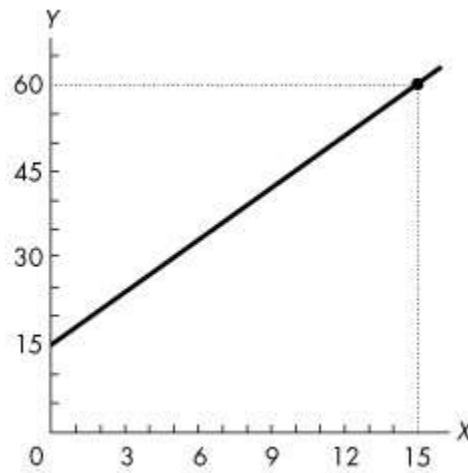
Answer: D

Diff: 2 Type: MC

Topic: Appendix: Mathematical Note

Source: MyEconLab

Use the figure below to answer the following question.



**Figure 1A.5.5**

10) Refer to Figure 1A.5.5. The graph shows the relationship between two variables,  $x$  and  $y$ . Which of the following equations describes this relationship?

- A)  $y = 3x + 15$
- B)  $y = -3x + 15$
- C)  $y = -3x^2 + 15$
- D)  $y = 15x + 3$
- E)  $x = 15y + 3$

Answer: A

Diff: 2 Type: MC

Topic: Appendix: Mathematical Note

Source: MyEconLab

11) Which of the following equations describes a straight line with a  $y$ -intercept of  $-2$  and a slope of  $-5$ ?

- A)  $y = -5 - 2x$
- B)  $y = -2$
- C)  $y = -2 - 5x$
- D)  $y = -5x$
- E)  $x = -2 - 5y$

Answer: C

Diff: 2 Type: MC

Topic: Appendix: Mathematical Note

Source: MyEconLab

## **Chapter 2 The Economic Problem**

### **2.1 Production Possibilities and Opportunity Cost**

#### **1) The production possibilities frontier**

- A) is the boundary between attainable and unattainable levels of production.
- B) is the boundary between what we want to consume and what we want to produce.
- C) shows how production increases as prices rise.
- D) shows prices at which production is possible and impossible.
- E) illustrates why there need not be any scarcity in the world.

Answer: A

Diff: 1 Type: MC

Topic: Production Possibilities and Opportunity Cost

2) Which one of the following concepts is *not* illustrated by a production possibilities frontier?

- A) scarcity
- B) monetary exchange
- C) opportunity cost
- D) attainable and unattainable points
- E) the tradeoff between producing one good versus another

Answer: B

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

3) A point inside a production possibilities frontier

- A) indicates some unused or misallocated resources.
- B) is unattainable.
- C) is preferred to a point on the production possibilities frontier.
- D) indicates a point of production efficiency.
- E) illustrates the idea of opportunity cost.

Answer: A

Diff: 1 Type: MC

Topic: Production Possibilities and Opportunity Cost

4) Which one of the following concepts is illustrated by a production possibilities frontier?

- A) profit
- B) consumption
- C) investment
- D) monetary exchange
- E) the tradeoff between producing one good versus another

Answer: E

Diff: 1 Type: MC

Topic: Production Possibilities and Opportunity Cost

- 5) If Sam is producing at a point inside his production possibilities frontier, then he
- A) can increase production of both goods with zero opportunity cost.
  - B) is fully using all his resources and allocating his resources to their best use.
  - C) must be doing the best he can with limited resources.
  - D) is unaffected by costs and technology.
  - E) has a high opportunity cost of moving from this point.

Answer: A

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

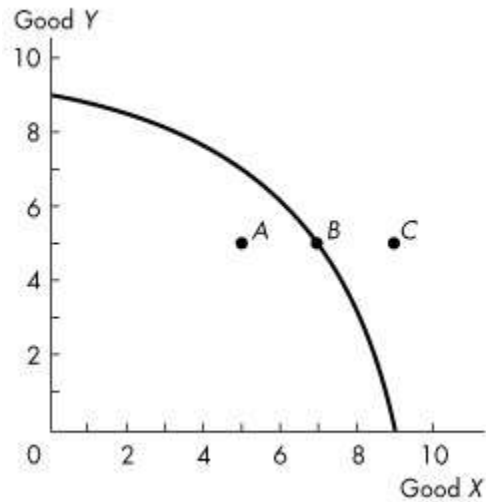
- 6) If Sam is producing at a point on his production possibilities frontier, then he
- A) cannot produce any more of either good.
  - B) is unaffected by costs and technology.
  - C) can produce more of both goods.
  - D) is not subject to scarcity.
  - E) can increase the production of one good only by decreasing the production of the other.

Answer: E

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

Use the figure below to answer the following questions.



**Figure 2.1.1**

7) Refer to the production possibilities frontier in Figure 2.1.1. Which one of the following is true about point A?

- A) It is unattainable.
- B) While no more of good Y can be produced, more of good X can be produced.
- C) It is preferred to point B.
- D) Resources are either unused or misallocated or both.
- E) It is attainable only if the amount of capital goods is increased.

Answer: D

Diff: 1 Type: MC

Topic: Production Possibilities and Opportunity Cost

8) Complete the following sentence. In Figure 2.1.1,

- A) movement from A to B would require a technological advance.
- B) point B is a point of production efficiency.
- C) some resources must be unused at point C.
- D) the concept of decreasing opportunity cost is illustrated.
- E) movement from C to B would require a technological improvement.

Answer: B

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

9) Refer to the production possibilities frontier in Figure 2.1.1, which one of the following is true about point *C*?

- A) It is attainable only if we consume more of good *X*.
- B) It is unattainable.
- C) It is attainable only if we consume less of good *Y*.
- D) It is attainable only if we consume less of good *X*.
- E) It is attainable only if we consume more of good *Y*.

Answer: B

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

10) If Harold can increase production of good *X* without decreasing production of any other good, then Harold

- A) is producing on his production possibilities frontier.
- B) is producing outside his production possibilities frontier.
- C) is producing inside his production possibilities frontier.
- D) must have a linear production possibilities frontier.
- E) must prefer good *X* to any other good.

Answer: C

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

Source: Study Guide

11) If Harold must decrease production of some other good to increase production of good *X*, then Harold

- A) is producing on his production possibilities frontier.
- B) is producing outside his production possibilities frontier.
- C) is producing inside his production possibilities frontier.
- D) must prefer good *X* to any other good.
- E) has too few capital goods.

Answer: A

Type: MC

Topic: Production Possibilities and Opportunity Cost

12) A situation in which resources are either unused or misallocated or both is represented in a production possibilities frontier diagram by

- A) any point on either the horizontal or the vertical axis.
- B) a point above or to the right of the production possibilities frontier.
- C) a point outside the production possibilities frontier.
- D) a point inside the production possibilities frontier.
- E) a point on or inside the production possibilities frontier.

Answer: D

Diff: 1 Type: MC

Topic: Production Possibilities and Opportunity Cost

13) A production possibilities frontier is negatively sloped because

- A) more goods are purchased as price falls.
- B) of opportunity cost.
- C) some resources are unused.
- D) there is not enough capital in the economy.
- E) of increasing consumption.

Answer: B

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

14) Ted chooses to study for his economics exam instead of going to the concert. The concert he will miss is Ted's \_\_\_\_\_ of studying for the exam.

- A) monetary cost
- B) absolute cost
- C) opportunity cost
- D) discretionary cost
- E) comparative cost

Answer: C

Diff: 1 Type: MC

Topic: Production Possibilities and Opportunity Cost

15) Opportunity cost of an action is

- A) the best choice that can be made.
- B) the highest-valued alternative forgone.
- C) the money cost.
- D) the comparative cost.
- E) the absolute cost.

Answer: B

Diff: 1 Type: MC

Topic: Production Possibilities and Opportunity Cost

16) The concept of opportunity cost

- A) cannot be explained by using a production possibilities frontier.
- B) explains that goods are swapped for other goods.
- C) implies that when a person is more efficient in the production of one good, he should produce that good and exchange it for some good that he is relatively less efficient at producing.
- D) implies that a double coincidence of wants must be present for exchange to take place.
- E) implies that because productive resources are scarce, we must give up some of one good to acquire more of another.

Answer: E

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

- 17) On a graph of a production possibilities frontier, opportunity cost is represented by
- A) a point on the horizontal axis.
  - B) a point on the vertical axis.
  - C) a ray through the origin.
  - D) the slope of the production possibilities frontier.
  - E) the  $x$ -axis intercept.

Answer: D

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

- 18) Production efficiency is achieved when
- A) the production possibilities frontier shifts outward at an even pace.
  - B) there are no more tradeoffs.
  - C) all resources are equally productive in all activities.
  - D) resources are not equally productive in all activities.
  - E) we produce goods and services at the lowest possible cost.

Answer: E

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

- 19) A tradeoff exists when
- A) we move from a point within the production possibilities frontier (*PPF*) to a point on the *PPF*.
  - B) we move from a point on the *PPF* to a point within the *PPF*.
  - C) the *PPF* shifts outward.
  - D) we move along the *PPF*.
  - E) the *PPF* shifts towards the origin.

Answer: D

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

- 20) Which of the following quotations best illustrates a tradeoff?
- A) "If the firm reorganized its production process, it could produce more widgets *and* more gadgets."
  - B) "The firm should sell more gadgets, even if it means less widget sales."
  - C) "The more and more gadgets the firm produces, the bigger the fall in widget production."
  - D) "If the firm invests more in capital equipment, it can expand sales next year."
  - E) "The firm has been able to lower costs due to its extensive experience in building widgets."

Answer: C

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

21) A medical clinic has 10 workers. Each worker can produce a maximum of either 2 units of medical services or 5 units of secretarial services a day. The production possibilities frontier of this firm would show

- A) increasing opportunity cost.
- B) decreasing opportunity cost.
- C) constant opportunity cost.
- D) zero opportunity cost.
- E) infinite opportunity cost.

Answer: C

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

22) A medical clinic has 10 workers. Each worker can produce a maximum of either 2 units of medical services or 5 units of secretarial services a day. The opportunity cost of one more unit of medical services is

- A) 2 units of secretarial services.
- B) 5 units of secretarial services.
- C) 0.4 units of secretarial services.
- D) 2.5 units of secretarial services
- E) dependent on the level of services.

Answer: D

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

23) A medical clinic has 10 workers. Each worker can produce a maximum of either 2 units of medical services or 5 units of secretarial services a day. One day, the firm decides it would like to produce 10 units of medical services and 30 units of secretarial services. This output level is

- A) efficient.
- B) unattainable.
- C) inefficient.
- D) costless.
- E) is attainable if the firm reduces the number of its workers.

Answer: B

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

24) A medical clinic has 10 workers. Each worker can produce a maximum of either 2 units of medical services or 5 units of secretarial services a day. One day, the firm decides it would like to produce 16 units of medical services and 5 units of secretarial services. This output level is

- A) efficient.
- B) unattainable.
- C) inefficient.
- D) costless.
- E) attainable and efficient.

Answer: C

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

25) The bowed-out (concave) shape of a production possibilities frontier

- A) is due to the equal usefulness of resources in all activities.
- B) is due to capital accumulation.
- C) is due to technological change.
- D) reflects the existence of increasing opportunity cost.
- E) reflects the existence of decreasing opportunity cost.

Answer: D

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

Source: Study Guide

26) If opportunity costs are increasing, then the production possibilities frontier

- A) will be bowed out and have a positive slope.
- B) will be positively sloped.
- C) will be linear and have a negative slope.
- D) will be bowed out and have a negative slope.
- E) reflects the fact that available resources are equally useful in all production activities.

Answer: D

Diff: 1 Type: MC

Topic: Production Possibilities and Opportunity Cost

27) The fact that resources are not equally productive in all activities

- A) implies that a production possibilities frontier will be bowed outward.
- B) implies that gains from specialization and trade are unlikely.
- C) follows from the law of demand.
- D) implies a linear production possibilities frontier.
- E) implies that an economy should not produce certain goods.

Answer: A

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

28) If additional units of any good could be produced at a *constant* opportunity cost, the production possibilities frontier would be

- A) bowed inward.
- B) bowed outward.
- C) positively sloped.
- D) negatively sloped.
- E) linear.

Answer: E

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

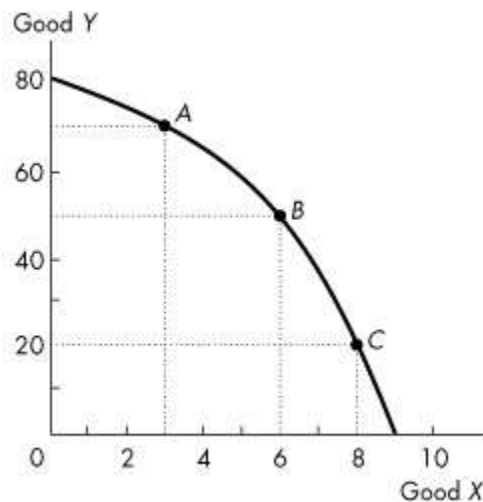
- 29) The existence of *increasing* opportunity cost
- A) explains why specialization is frequently useful.
  - B) explains why resources are scarce.
  - C) explains the bowed-out shape of the production possibilities frontier.
  - D) follows from the existence of property rights.
  - E) explains why some societies produce inside their production possibilities frontier.

Answer: C

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

Use the figure below to answer the following questions.



**Figure 2.1.2**

- 30) Refer to the production possibilities frontier in Figure 2.1.2. If 6 units of X are currently being produced, then
- A) 40 units of Y cannot be produced unless production of X is decreased.
  - B) 40 units of Y cannot be produced unless production of X is increased.
  - C) 60 units of Y can be produced with some resources *not* fully used.
  - D) 50 units of Y must be produced, regardless of resource utilization.
  - E) 50 units of Y can be produced if all resources are used and assigned to the task for which they are the best match.

Answer: E

Diff: 1 Type: MC

Topic: Production Possibilities and Opportunity Cost

31) Refer to the production possibilities frontier in Figure 2.1.2. Suppose that 50 units of *Y* are currently being produced. Then

A) 7 units of *X* are being produced.

B) 6 units of *X* can be produced if all resources are used and assigned to the task for which they are the best match.

C) 9 units of *X* can be produced if all resources are used and assigned to the task for which they are the best match.

D) resources are not being fully utilized.

E) 6 units of *X* are being produced.

Answer: B

Diff: 1 Type: MC

Topic: Production Possibilities and Opportunity Cost

32) Refer to the production possibilities frontier in Figure 2.1.2. At point *A*, the opportunity cost of producing 3 more units of *X*

A) is 30 units of *Y*.

B) is 3 units of *X*.

C) is 20 units of *Y*.

D) is 10 units of *Y*.

E) cannot be determined from the diagram.

Answer: C

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

33) Refer to the production possibilities frontier in Figure 2.1.2. At point *A*, the opportunity cost of increasing production of *Y* to 80 units is

A) 10 units of *Y*.

B) 80 units of *Y*.

C) 2 units of *X*.

D) 3 units of *X*.

E) 1 unit of *X*.

Answer: D

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

34) Refer to the production possibilities frontier in Figure 2.1.2. At point *C*, the opportunity cost of producing one more unit of *X* is

A) 1 unit of *Y*.

B) 1 unit of *X*.

C) 8 units of *X*.

D) 20 units of *X*.

E) 20 units of *Y*.

Answer: E

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

35) Refer to the production possibilities frontier in Figure 2.1.2. At point C, what is the opportunity cost of increasing the production of Y from 20 to 50 units?

- A) 6 units of X
- B) 2 units of X
- C) 8 units of X
- D) 20 units of Y
- E) 30 units of Y

Answer: B

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

36) Consider the production possibilities frontier in Figure 2.1.2, and assume that everything that is produced is also consumed. Which of the following statements is *false*?

- A) Resources are not equally useful in all activities.
- B) Points inside the frontier indicate unused or misallocated resources.
- C) Starting at point A, an increase in the production of Y will shift the frontier outward.
- D) The opportunity cost of producing Y increases as production of Y increases.
- E) The opportunity cost of producing X increases as production of X increases.

Answer: C

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

37) As we increase the production of X, we find we must give up larger and larger amounts of Y per unit of X. Select the best statement.

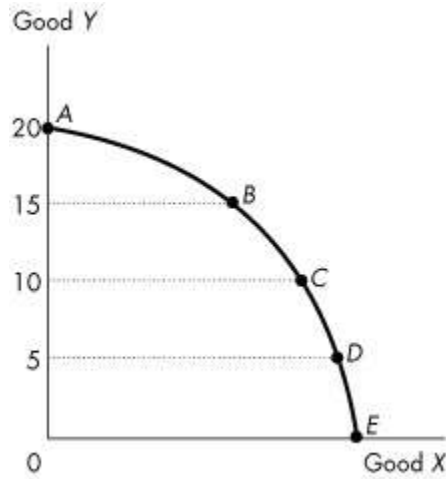
- A) This illustrates increasing opportunity cost.
- B) As a result, we should not specialize in the production of X.
- C) The production possibilities frontier for X and Y is a straight line.
- D) Good Y will be more highly regarded by consumers than good X.
- E) We must be inside the production possibilities frontier.

Answer: A

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

Use the figure below to answer the following questions.



**Figure 2.1.3**

38) Figure 2.1.3 illustrates Mary's production possibilities frontier. If Mary wants to move from point *B* to point *C*,

- A) it will be necessary to improve technology.
- B) it will be necessary to increase the accumulation of capital.
- C) it will be necessary to give up some of good *X* to obtain more of good *Y*.
- D) it will be necessary to give up some of good *Y* to obtain more of good *X*.
- E) she can accomplish this without any opportunity cost.

Answer: D

Diff: 1 Type: MC

Topic: Production Possibilities and Opportunity Cost

39) Figure 2.1.3 illustrates Mary's production possibilities frontier. If Mary wants to move from point *D* to point *C*,

- A) it will be necessary to improve technology.
- B) it will be necessary to increase the accumulation of capital.
- C) it will be necessary to give up some of good *X* to obtain more of good *Y*.
- D) it will be necessary to give up some of good *Y* to obtain more of good *X*.
- E) she can accomplish this without any opportunity cost.

Answer: C

Diff: 1 Type: MC

Topic: Production Possibilities and Opportunity Cost

40) Refer to the production possibilities frontier in Figure 2.1.3. The opportunity cost of moving from *C* to *B* will be

- A) greater than moving from *D* to *C* but less than moving from *B* to *A*.
- B) less than moving from *D* to *C* but greater than moving from *B* to *A*.
- C) the same as moving from *D* to *C* or moving from *B* to *A*.
- D) greater than moving either from *D* to *C* or from *B* to *A*.
- E) neither greater than moving from *D* to *C* nor moving from *B* to *A*.

Answer: A

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

41) Refer to the production possibilities frontier in Figure 2.1.3. The fact that less of *X* must be given up when moving from *D* to *C* than when moving from *B* to *A* indicates

- A) decreasing opportunity cost.
- B) increasing opportunity cost.
- C) comparative advantage in the production of *X*.
- D) the consequences of technological improvement.
- E) unemployed resources at *D*.

Answer: B

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

*Use the table below to answer the following questions.*

**Table 2.1.1**

The following table gives points on the production possibilities frontier for goods *X* and *Y*.

Point	Production of <i>X</i>	Production of <i>Y</i>
<i>A</i>	0	40
<i>B</i>	4	36
<i>C</i>	8	28
<i>D</i>	12	16
<i>E</i>	16	0

42) Refer to Table 2.1.1. What does point *C* mean?

- A) If 8 units of *X* are produced, then at least 28 units of *Y* can be produced.
- B) If 8 units of *X* are produced, then at most 28 units of *Y* can be produced.
- C) If 28 units of *Y* are produced, then more than 8 units of *X* can be produced.
- D) If 8 units of *X* are produced, then only 36 units of *Y* can be produced.
- E) There is unemployment at this point.

Answer: B

Diff: 1 Type: MC

Topic: Production Possibilities and Opportunity Cost

43) Refer to Table 2.1.1. The opportunity cost of increasing the production of  $X$  from 8 to 12 units is

- A) 4 units of  $X$ .
- B) 4 units of  $Y$ .
- C) 8 units of  $Y$ .
- D) 12 units of  $Y$ .
- E) 16 units of  $Y$ .

Answer: D

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

44) Refer to Table 2.1.1. The opportunity cost of increasing the production of  $Y$  from 16 to 36 units is

- A) 4 units of  $X$ .
- B) 8 units of  $X$ .
- C) 12 units of  $X$ .
- D) 16 units of  $X$ .
- E) 20 units of  $Y$ .

Answer: B

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

45) The economy illustrated by the data in Table 2.1.1 exhibits

- A) decreasing opportunity cost.
- B) constant opportunity cost in the production of  $X$ .
- C) constant opportunity cost in the production of  $Y$ .
- D) increasing opportunity cost.
- E) initially increasing, then decreasing opportunity cost.

Answer: D

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

46) From the data in Table 2.1.1, the production of 7 units of  $X$  and 28 units of  $Y$  is

- A) unattainable.
- B) attainable but leaves some resources unused or misallocated or both.
- C) on the *PPF* between points  $C$  and  $D$ .
- D) on the *PPF* between points  $B$  and  $C$ .
- E) outside the *PPF*.

Answer: B

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

- 47) Refer to Table 2.1.1. As we increase the production of  $X$ ,
- A) the amount of  $Y$  that is given up for each additional unit of  $X$  decreases.
  - B) the output of  $Y$  increases.
  - C) the opportunity cost of each additional unit of  $X$  increases.
  - D) unemployment increases.
  - E) the amount of  $X$  increases at an increasing rate.

Answer: C

Diff: 1 Type: MC

Topic: Production Possibilities and Opportunity Cost

- 48) From the data in Table 2.1.1 we can infer that
- A) the economy illustrated has a comparative advantage in the production of  $Y$ .
  - B) the economy illustrated has a comparative advantage in the production of  $X$ .
  - C) the opportunity cost of producing an additional unit of  $Y$  increases as the production of  $Y$  increases.
  - D) the opportunity cost of producing an additional unit of  $Y$  decreases as the production of  $Y$  increases.
  - E) none of the above.

Answer: C

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

- 49) The diagram of the production possibilities frontier corresponding to the data in Table 2.1.1 would be
- A) negatively sloped and linear.
  - B) negatively sloped and bowed inward.
  - C) negatively sloped and bowed outward.
  - D) positively sloped for  $X$  and negatively sloped for  $Y$ .
  - E) a horizontal line.

Answer: C

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

- 50) From the data in Table 2.1.1, the production of 10 units of  $X$  and 28 units of  $Y$  is
- A) unattainable.
  - B) attainable but leaves some resources misallocated.
  - C) on the production possibilities frontier between points  $C$  and  $D$ .
  - D) inside the  $PPF$ .
  - E) possible if we reduce the amount of capital goods.

Answer: A

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

Use the table below to answer the following questions.

**Table 2.1.2**  
Production Possibilities

Possibility	Kilograms of Butter	Guns
A	8	0
B	6	1
C	0	3

51) Refer to Table 2.1.2. In moving from combination B to combination C, the opportunity cost of producing *one* additional unit of guns is

- A) 2 kilograms of butter.
- B) 1/2 kilogram of butter.
- C) 6 kilograms of butter.
- D) 1/6 kilogram of butter.
- E) 3 kilograms of butter.

Answer: E

Diff: 3 Type: MC

Topic: Production Possibilities and Opportunity Cost

52) Refer to Table 2.1.2. According to this production possibilities frontier,

- A) a combination of 6 kilograms of butter and 1 gun leaves some resources unused.
- B) a combination of 0 butter and 4 guns is attainable.
- C) resources are equally useful in all activities.
- D) the opportunity cost of producing guns increases as more guns are produced.
- E) the opportunity cost of producing guns decreases as more guns are produced.

Answer: D

Diff: 1 Type: MC

Topic: Production Possibilities and Opportunity Cost

Use the table below to answer the following questions.

**Table 2.1.3**  
Production possibilities for a society that produces only two goods — hockey sticks and maple leaves.

Possibility	Units of Hockey Sticks	Units of Maple Leaves
A	3	0
B	2	3
C	0	9

53) Refer to Table 2.1.3. In moving from combination C to combination B, the opportunity cost of producing *one* additional hockey stick is

- A) 2 maple leaves.
- B) 1/2 maple leaves.
- C) 6 maple leaves.
- D) 1/6 maple leaves.
- E) 3 maple leaves.

Answer: E

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

Source: Study Guide

Use the table below to answer the following question.

**Table 2.1.4**  
Consider the following production possibilities for A. Student for the typical week:

Possibility	Beer	Pizza
a	14 cases	0
b	12 cases	6
c	9 cases	11
d	5 cases	14
e	0 cases	15

54) Refer to Table 2.1.4. Complete the following sentence. The production possibilities frontier in the table shows

- A) increasing opportunity cost.
- B) learning-by-doing.
- C) constant opportunity cost.
- D) under-utilization of resources.
- E) decreasing opportunity cost.

Answer: A

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

55) The slope of the production possibilities frontier curve indicates

- A) opportunity cost.
- B) comparative advantage.
- C) absolute advantage.
- D) marginal benefit.
- E) preferences.

Answer: A

Diff: 2 Type: MC

Topic: Production Possibilities and Opportunity Cost

56) As we move down the bowed-out production possibilities frontier, opportunity cost

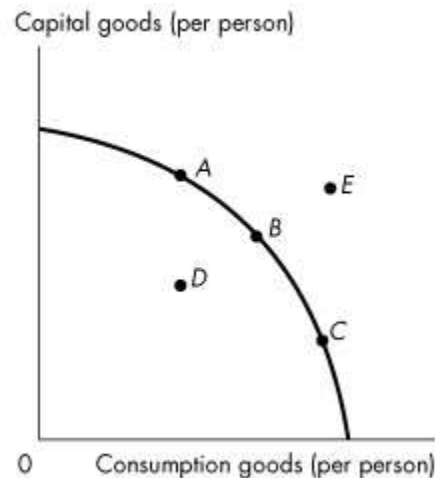
- A) increases.
- B) decreases.
- C) remains constant.
- D) initially decreases, then increases.
- E) decreases but at an increasing rate.

Answer: A

Diff: 1 Type: MC

Topic: Production Possibilities and Opportunity Cost

Use the figure below to answer the following questions.



**Figure 2.1.4**

57) Refer to the production possibilities frontier in Figure 2.1.4. Which point is unattainable?

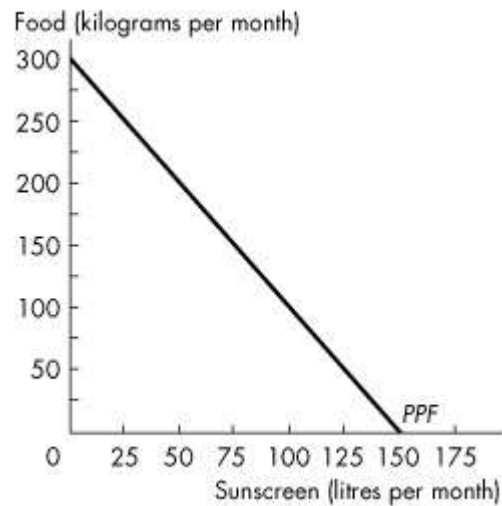
- A) A
- B) B
- C) C
- D) D
- E) E

Answer: E

Diff: 1 Type: MC

Topic: Production Possibilities and Opportunity Cost

Use the figure below to answer the following question.



**Figure 2.1.5**

58) The graph in Figure 2.1.5 shows Sunland's *PPF* for food and sunscreen. Sunland faces \_\_\_\_\_ opportunity cost of food and \_\_\_\_\_ opportunity of sunscreen, which can be seen by the shape of the *PPF*.

- A) an increasing; a decreasing
- B) a constant; a constant
- C) a decreasing; an increasing
- D) an increasing; an increasing
- E) a decreasing; a decreasing

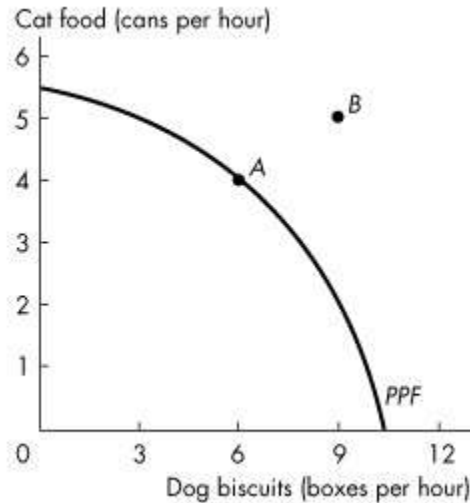
Answer: B

Type: MC

Topic: Production Possibilities and Opportunity Cost

Source: MyEconLab

Use the figure below to answer the following question.



**Figure 2.1.6**

59) Figure 2.1.6 shows the production possibilities frontier for a firm that produces pet food. Point A is \_\_\_\_\_ and point B is \_\_\_\_\_. This *PPF* \_\_\_\_\_ illustrate scarcity because \_\_\_\_\_.

- A) unattainable; attainable; does; because the firm cannot attain the points outside the frontier
- B) attainable; unattainable; does not; the firm can produce any quantity it wants if it is willing to pay a high enough price
- C) unattainable; attainable; does not; the firm can produce any quantity it wants if it is willing to pay a high enough price
- D) attainable; unattainable; does; the firm cannot produce points outside the frontier and as the firm moves along the *PPF*, it cannot produce more dog biscuits without producing less cat food
- E) attainable; unattainable; does not; it is downward sloping

Answer: D

Type: MC

Topic: Production Possibilities and Opportunity Cost

Source: MyEconLab

60) When producing at a point of production efficiency, \_\_\_\_\_.

- A) our choice of goods to produce can be either on or inside the production possibilities frontier
- B) we can satisfy all our wants
- C) the opportunity cost of producing goods other than those measured on the axes of the production possibilities frontier is zero
- D) we face a tradeoff and incur an opportunity cost
- E) resources are either unused or misallocated

Answer: D

Type: MC

61) Jane produces only corn and cloth. If her preferences for corn and cloth change, then

- \_\_\_\_\_.
- A) her *PPF* becomes steeper
  - B) her *PPF* becomes flatter
  - C) her *PPF* becomes straighter
  - D) the world *PPF* shifts outward
  - E) her *PPF* does not change

Answer: E

Type: MC

## 2.2 Using Resources Efficiently

1) Complete the following sentence. Marginal cost

- A) is the opportunity cost of producing one more unit of a good or service.
- B) is unrelated to the production possibilities frontier.
- C) always equals marginal benefit.
- D) remains constant.
- E) is always greater than marginal benefit.

Answer: A

Diff: 1 Type: MC

Topic: Using Resources Efficiently

2) The quantity of shoes produced is measured along the  $x$ -axis of a bowed-outward production possibilities frontier and the quantity of shirts produced is measured along the  $y$ -axis. As you move down towards the right along the production possibilities frontier, the marginal cost of

- A) a pair of shoes decreases.
- B) a pair of shoes increases.
- C) a shirt remains constant.
- D) a shirt increases or decreases but we don't know for sure.
- E) a pair of shoes and a shirt is equal at the midpoint between the  $x$ -axis and the  $y$ -axis.

Answer: B

Diff: 2 Type: MC

Topic: Using Resources Efficiently

3) Which of the following is true regarding marginal benefit?

- I. The marginal benefit curve shows the benefit firms receive by producing another unit of a good.
- II. Marginal benefit increases as more and more of a good is consumed.
- III. Marginal benefit is the maximum amount a person is willing to pay to obtain one more unit of a good.

- A) I only
- B) I and II
- C) I and III
- D) III only
- E) I, II, and III

Answer: D

Diff: 3 Type: MC

Topic: Using Resources Efficiently

4) To describe preferences, economists use the concept of

- A) opportunity cost.
- B) scarcity.
- C) marginal benefit.
- D) marginal cost.
- E) none of the above.

Answer: C

Diff: 1 Type: MC

Topic: Using Resources Efficiently

- 5) Complete the following sentence. As you consume more and more of a good,
- A) marginal benefit increases.
  - B) marginal benefit decreases.
  - C) marginal benefit always equals marginal cost.
  - D) marginal benefit increases or decreases depending on where you are on the production possibilities frontier.
  - E) the price of the good falls.

Answer: B

Diff: 1 Type: MC

Topic: Using Resources Efficiently

- 6) The marginal benefit curve for a good
- A) shows the benefit a firm receives from producing one more unit of that good.
  - B) shows the most a consumer is willing to pay for one more unit of that good.
  - C) is upward-sloping.
  - D) is bowed outward.
  - E) none of the above.

Answer: B

Diff: 1 Type: MC

Topic: Using Resources Efficiently

Source: Study Guide

Use the figure below to answer the following questions.

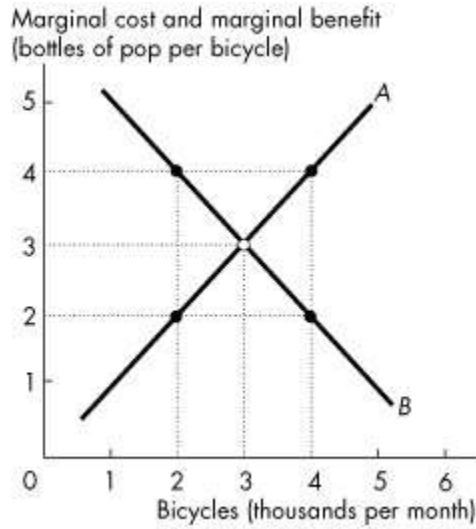


Figure 2.2.1

7) In Figure 2.2.1, the curve labeled *B* shows

- A) the bottles of pop that people are *willing* to forgo to get another bicycle.
- B) the bicycles that people are *willing* to forgo to get another bottle of pop.
- C) the bottles of pop that people *must* forgo to get another bicycle.
- D) that the benefits of producing more bicycles is greater than the benefits of producing more pop.
- E) that the benefits of producing more pop is greater than the benefits of producing more bicycles.

Answer: A

Diff: 1 Type: MC

Topic: Using Resources Efficiently

8) In Figure 2.2.1, when 2,000 bicycles are produced each month

- A) the marginal benefit from another bicycle is greater than the marginal cost of another bicycle.
- B) more bicycles must be produced to reach the efficient level of output.
- C) fewer bicycles must be produced to reach the efficient level of output.
- D) the economy is efficient at this level of production of bicycles.
- E) both A and B.

Answer: E

Diff: 2 Type: MC

Topic: Using Resources Efficiently

9) In Figure 2.2.1, the curve labelled *A* is the \_\_\_\_\_ curve and the curve labelled *B* is the \_\_\_\_\_ curve.

- A) marginal cost; marginal benefit
- B) marginal cost; trade
- C) marginal benefit; trade
- D) production possibilities; trade
- E) marginal benefit; marginal cost

Answer: A

Diff: 1 Type: MC

Topic: Using Resources Efficiently

10) In Figure 2.2.1, when 4,000 bicycles are produced each month

- A) the marginal benefit from another bicycle is greater than the marginal cost of another bicycle.
- B) more bicycles must be produced to reach the efficient level of output.
- C) fewer bicycles must be produced to reach the efficient level of output.
- D) the economy is very efficient at this level of production of bicycles.
- E) both A and B.

Answer: C

Diff: 2 Type: MC

Topic: Using Resources Efficiently

11) A marginal benefit curve measures

- A) comparative advantage.
- B) willingness to pay.
- C) absolute advantage.
- D) opportunity cost.
- E) expenditure.

Answer: B

Diff: 1 Type: MC

Topic: Using Resources Efficiently

12) Allocative efficiency refers to a situation where

- A) opportunity costs are equal.
- B) we cannot produce more of any one good without giving up some other good.
- C) goods and services are produced at the lowest possible cost and in the quantities that provide the greatest possible benefit.
- D) opportunity cost is zero.
- E) none of the above.

Answer: C

Diff: 1 Type: MC

Topic: Using Resources Efficiently

13) As production of food increases, marginal benefit from food

- A) increases and marginal cost increases.
- B) increases and marginal cost decreases.
- C) decreases and marginal cost increases.
- D) decreases and marginal cost decreases.
- E) decreases and marginal cost is zero.

Answer: C

Diff: 1 Type: MC

Topic: Using Resources Efficiently

Source: Study Guide

14) Suppose the production possibilities frontier for skirts and pants is a straight line. As the production of skirts increases, the marginal benefit from skirts

- A) increases and marginal cost is constant.
- B) is constant and marginal cost decreases.
- C) decreases and marginal cost increases.
- D) decreases and marginal cost decreases.
- E) decreases and marginal cost is constant.

Answer: E

Diff: 1 Type: MC

Topic: Using Resources Efficiently

Source: Study Guide

15) With allocative efficiency, for each good produced,

- A) marginal benefit equals marginal cost.
- B) marginal benefit is at its maximum.
- C) marginal benefit exceeds marginal cost by as much as possible.
- D) marginal cost exceeds marginal benefit by as much as possible.
- E) marginal cost is at its minimum.

Answer: A

Diff: 1 Type: MC

Topic: Using Resources Efficiently

Source: Study Guide

16) Marginal benefit from a good or service is the benefit received from consuming \_\_\_\_\_. It is measured by the most that people are willing to pay for \_\_\_\_\_.

- A) goods that you prefer; an additional unit of it
- B) goods that you prefer; more of it
- C) one more unit of it; an additional unit of it
- D) one more unit of it; more of it
- E) as much as is available; the total amount consumed

Answer: C

Type: MC

Topic: Using Resources Efficiently

Source: MyEconLab

Use the table below to answer the following questions.

**Table 2.2.1**

<i>Ethanol</i> (barrels per day)		<b>Food crops</b> (tonnes per day)
<i>70</i>	<i>and</i>	<i>0</i>
<i>64</i>	<i>and</i>	<i>1</i>
<i>54</i>	<i>and</i>	<i>2</i>
<i>40</i>	<i>and</i>	<i>3</i>
<i>22</i>	<i>and</i>	<i>4</i>
<i>0</i>	<i>and</i>	<i>5</i>

17) Refer to Table 2.2.1. Marginal benefit from food crops

A) equals the marginal cost of food crops.

B) remains constant as the quantity of food crops increases from 1 tonne a day to 2 tonnes a day.

C) cannot be calculated from the table.

D) increases as the quantity of food crops increases from 1 tonne a day to 2 tonnes a day.

E) equals 70 barrels of ethanol.

Answer: C

Type: MC

Topic: Using Resources Efficiently

Source: MyEconLab

18) The principle of decreasing marginal benefit implies that the \_\_\_\_\_.

A) additional benefit from obtaining one more unit of a good or service decreases as more of that good or service is consumed

B) additional benefit from obtaining one more unit of a good or service increases as more of that good or service is consumed

C) total benefit from obtaining more of a good or service decreases as more is consumed

D) total benefit from obtaining more of a good or service remains the same as more is consumed

E) additional benefit from producing one more unit of a good or service decreases as more of that good or service is produced

Answer: A

Type: MC

19) The most anyone is willing to pay for another purse is \$30. Currently the price of a purse is \$40, and the cost of producing another purse is \$50. The marginal benefit from a purse is \_\_\_\_\_.

A) \$40

B) \$50

C) \$10

D) \$20

E) \$30

Answer: E

Type: MC

### 2.3 Economic Growth

- 1) A technological improvement is represented by
- A) an outward shift of the production possibilities frontier.
  - B) a movement along the production possibilities frontier.
  - C) a point inside the production possibilities frontier.
  - D) a point outside the production possibilities frontier.
  - E) a movement from a point inside the production possibilities frontier to a point on the production possibilities frontier.

Answer: A

Diff: 1 Type: MC

Topic: Economic Growth

- 2) In general, if country *A* is accumulating capital at a faster rate than country *B*, then country *A*
- A) will soon have a comparative advantage in the production of most goods.
  - B) is using a larger proportion of resources to produce consumption goods.
  - C) will have a production possibilities frontier that is shifting out faster than country *B*'s.
  - D) will have a higher rate of inflation than country *B*.
  - E) will have more unemployment than country *B*.

Answer: C

Diff: 2 Type: MC

Topic: Economic Growth

- 3) The principal reason that production possibilities have grown more rapidly in Hong Kong than in Canada over the last 50 years is because
- A) of cheap Hong Kong labour.
  - B) of foreign aid to Hong Kong.
  - C) Hong Kong has fewer workers.
  - D) Hong Kong has more natural resources.
  - E) Hong Kong has devoted a larger proportion of its resources to capital accumulation.

Answer: E

Diff: 2 Type: MC

Topic: Economic Growth

- 4) Which one of the following would cause a production possibilities frontier to shift *outward*?
- A) an increase in the stock of capital
  - B) an increase in the production of consumption goods
  - C) bad weather
  - D) a decision to fully utilize unemployed resources
  - E) a decrease in the population

Answer: A

Diff: 1 Type: MC

Topic: Economic Growth

- 5) The development of new goods and better ways of producing goods and services is
- A) capital accumulation.
  - B) technological change.
  - C) the big tradeoff.
  - D) allocative efficiency.
  - E) none of the above.

Answer: B

Diff: 1 Type: MC

Topic: Economic Growth

- 6) The growth of capital resources, including human capital is
- A) technological change.
  - B) capital accumulation.
  - C) depreciation.
  - D) opportunity cost.
  - E) none of the above.

Answer: B

Diff: 1 Type: MC

Topic: Economic Growth

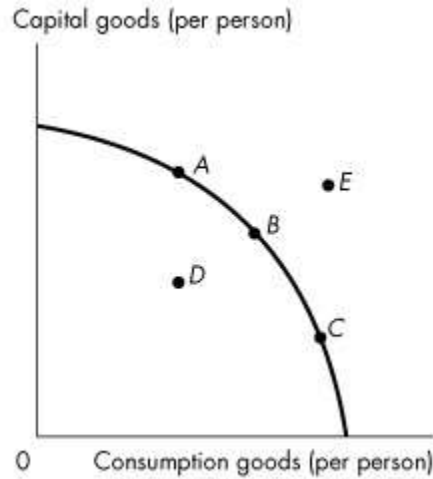
- 7) Which one of the following would likely shift a production possibilities frontier *inward*?
- A) technological change.
  - B) a drought.
  - C) a decrease in the price of natural resources.
  - D) all of the above
  - E) None of the above, because production possibilities frontiers do not shift inward.

Answer: B

Diff: 2 Type: MC

Topic: Economic Growth

Use the figure below to answer the following questions.



**Figure 2.3.1**

8) Refer to the production possibilities frontier in Figure 2.3.1. The production possibilities frontier will shift rightward most rapidly if current production is at

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

Answer: A

Diff: 2 Type: MC

Topic: Economic Growth

9) A production possibilities frontier will shift outward FOR ALL OF THE FOLLOWING REASONS *EXCEPT*

- A) a technological improvement.
- B) an increase in the stock of capital.
- C) an increase in the labour force.
- D) opportunity cost is increasing.
- E) none of the above.

Answer: D

Diff: 1 Type: MC

Topic: Economic Growth

10) A movement *along* the production possibilities frontier will result from

- A) technological change.
- B) change in the stock of capital.
- C) change in the labour force.
- D) all of the above.
- E) none of the above.

Answer: E

Diff: 1 Type: MC

Topic: Economic Growth

Source: Study Guide

11) The opportunity cost of pushing the production possibilities frontier outward is

- A) capital accumulation.
- B) technological change.
- C) reduced current consumption.
- D) the gain in future consumption.
- E) all of the above.

Answer: C

Diff: 2 Type: MC

Topic: Economic Growth

Source: Study Guide

12) In general, the higher the proportion of resources devoted to technological research in an economy, the

- A) greater will be current consumption.
- B) faster the production possibilities frontier will shift outward.
- C) faster the production possibilities frontier will shift inward.
- D) closer it will come to having a comparative advantage in the production of all goods.
- E) more bowed out will be the shape of the production possibilities frontier.

Answer: B

Diff: 2 Type: MC

Topic: Economic Growth

Source: Study Guide

13) Consider a country that has two industries. In the north, they grow wild rice, which requires a lot of rainfall. In the south, they grow wheat, which requires just a moderate amount of rainfall (too much rainfall is bad for wheat production). One year, there is a record rainfall. This will result in

- A) a parallel shift inward of the production possibilities frontier.
- B) a parallel shift outward of the production possibilities frontier.
- C) the production possibilities frontier swiveling, with the wild rice intercept increasing, and the wheat intercept decreasing.
- D) the production possibilities frontier swiveling, with the wild rice intercept decreasing, and the wheat intercept increasing.
- E) none of the above.

Answer: C

Diff: 3 Type: MC

Topic: Economic Growth

14) Suppose a hurricane causes extensive devastation, destroying houses, roads, schools and factories. What would be the effect of this hurricane on a production possibilities frontier consisting of consumption goods and capital goods?

- A) It would shift outward at all points.
- B) It would shift inward at all points.
- C) There would be a movement along the existing production possibilities frontier towards a less capital-intensive point.
- D) There would be a movement along the existing production possibilities frontier towards a more capital-intensive point.
- E) There would be a movement from the existing production possibilities frontier inwards towards a point with unused or misallocated resources.

Answer: B

Diff: 2 Type: MC

Topic: Economic Growth

15) The depletion of fish stocks in Eastern Canada, with its accompanying unemployment, will lead to a

- A) movement from the existing production possibilities frontier to a point inside the production possibilities frontier.
- B) shift inward of the existing production possibilities frontier and production at a point on the new *PPF*.
- C) shift outward of the existing production possibilities frontier.
- D) movement along the existing production possibilities frontier to a point of less fish production.
- E) shift inward of the existing production possibilities frontier plus a movement to a point inside the new production possibilities frontier.

Answer: E

Diff: 3 Type: MC

Topic: Economic Growth

16) Which of the following quotations illustrates economic growth?

- A) "The firm should lower the price it charges for widgets and gadgets."
- B) "The firm should sell more gadgets, even if it means less widget sales."
- C) "The more and more gadgets the firm produces, the bigger the fall in widget production."
- D) "If the firm invests more in capital equipment, it can expand production next year."
- E) "The firm has been able to lower costs due to its extensive experience in building widgets."

Answer: D

Diff: 2 Type: MC

Topic: Economic Growth

17) Economic growth \_\_\_\_\_ overcome scarcity because \_\_\_\_\_.

- A) does; with economic growth the *PPF* rotates outward and eventually becomes a horizontal line
- B) does; we will eventually reach the point where we have too much
- C) does not; we can produce more goods and services but it is still impossible to satisfy all our wants
- D) does not; economic growth requires capital accumulation and technological change
- E) does; with economic growth the *PPF* rotates outward and eventually becomes a vertical line

Answer: C

Type: MC

Topic: Economic Growth

Source: MyEconLab

18) In 1960, the production possibilities per person in Canada were \_\_\_\_\_ than those in Hong Kong. Canada devoted \_\_\_\_\_ of its resources to accumulating capital and the remainder to consumption. Hong Kong devoted \_\_\_\_\_ of its resources to accumulating capital and the remainder to consumption. Because Hong Kong devoted a \_\_\_\_\_ fraction of its resources to accumulating capital, its production possibilities have \_\_\_\_\_.

- A) smaller; one-fifth; one-third; greater; expanded more quickly
- B) smaller; one-third; one-fifth; smaller; not expanded as quickly
- C) greater; one-third; one-fifth; smaller; not expanded as quickly
- D) greater; one-fifth; one-third; greater; expanded more quickly
- E) greater; one-half; one-quarter; smaller; not expanded as quickly

Answer: D

Type: MC

Topic: Economic Growth

Source: MyEconLab

19) The production possibilities frontier shifts outward when \_\_\_\_\_.

- A) tastes and preferences change
- B) the quantity of money in the economy grows
- C) prices rise
- D) human capital accumulates
- E) the political party in power changes

Answer: D

Type: MC

20) Consider a production possibilities frontier with corn production measured on the vertical axis and car production measured on the horizontal axis. Unusually good weather for growing corn shifts \_\_\_\_\_.

A) the horizontal intercept of the *PPF* rightward and the vertical intercept of the *PPF* upward

B) the horizontal intercept of the *PPF* rightward but does not shift the vertical intercept of the *PPF*

C) the vertical intercept of the *PPF* upward but does not shift the horizontal intercept of the *PPF*

D) neither the horizontal intercept nor the vertical intercept of the *PPF*

E) the vertical intercept of the *PPF* downward and the horizontal intercept of the *PPF* leftward

Answer: C

Type: MC

## 2.4 Gains from Trade

1) Individuals *A* and *B* can both produce good *X*. We say that *A* has a comparative advantage in the production of good *X* if

- A) *A* has a lower opportunity cost of producing *X* than *B*.
- B) *A* has a higher opportunity cost of producing *X* than *B*.
- C) *A* can produce more units of *X* in a given time period than *B*.
- D) *A* can produce *X* using newer technology than *B*.
- E) *A* can produce less units of *X* in a given time period than *B*.

Answer: A

Diff: 3 Type: MC

Topic: Gains from Trade

2) Individuals *A* and *B* can both produce goods *X* and *Y*. Individual *A* has a comparative advantage in the production of *X* if

- A) *A* is faster than *B* at producing *X*.
- B) the amount by which *A* must reduce production of *Y* is less than the amount by which *B* must reduce production of *Y* to produce an additional unit of *X*.
- C) *B* has superior knowledge about how to produce *X*.
- D) *A* has a preference to consume *X*.
- E) the amount by which *A* must reduce production of *Y* is more than the amount by which *B* must reduce production of *Y* to produce an additional unit of *X*.

Answer: B

Diff: 2 Type: MC

Topic: Gains from Trade

3) Debra has an absolute advantage in producing a good when she

- A) has a comparative advantage in producing that good.
- B) can produce the good at lower opportunity cost than anyone else.
- C) can produce more of that good than anyone else, using the same quantity of inputs.
- D) has exclusive rights to sell that good.
- E) has better technology than anyone else.

Answer: C

Diff: 2 Type: MC

Topic: Gains from Trade

4) A person who has an absolute advantage in the production of all goods will

- A) also have a comparative advantage in the production of all goods.
- B) not be able to gain from specialization and trade.
- C) produce all goods at the lowest opportunity cost.
- D) not have a comparative advantage in the production of any goods.
- E) have a comparative advantage in the production of only some goods and not others.

Answer: E

Diff: 2 Type: MC

Topic: Gains from Trade

Use the information below to answer the following questions.

**Fact 2.4.1**

In an eight-hour day, Andy can produce either 24 loaves of bread or 8 kilograms of butter. In an eight-hour day, Rolfe can produce either 8 loaves of bread or 8 kilograms of butter.

5) Given Fact 2.4.1, the opportunity cost of producing 1 loaf of bread is

- A) 20 minutes (1/3 hour) for Andy and 1 hour for Rolfe.
- B) 1/3 kilogram of butter for Andy and 1 kilogram of butter for Rolfe.
- C) 3 kilograms of butter for Andy and 1 kilogram of butter for Rolfe.
- D) 8 kilograms of butter for both Andy and Rolfe.
- E) not calculable from the given information.

Answer: B

Diff: 2 Type: MC

Topic: Gains from Trade

6) From Fact 2.4.1, we know that

- A) Andy has the lower opportunity cost of producing bread, while Andy and Rolfe have equal opportunity costs of producing butter.
- B) Andy has the lower opportunity cost of producing both bread and butter.
- C) Andy has the lower opportunity cost of producing bread, while Rolfe has the lower opportunity cost of producing butter.
- D) Andy has the lower opportunity cost of producing butter, while Rolfe has the lower opportunity cost of producing bread.
- E) Andy has the higher opportunity cost of producing both bread and butter.

Answer: C

Diff: 3 Type: MC

Topic: Gains from Trade

7) Refer to Fact 2.4.1. Which one of the following statements is true?

- A) Andy has an absolute advantage in butter production.
- B) Rolfe has an absolute advantage in butter production.
- C) Andy has a comparative advantage in bread production.
- D) Andy has a comparative advantage in butter production.
- E) Rolfe has a comparative advantage in bread production.

Answer: C

Diff: 3 Type: MC

Topic: Gains from Trade

8) Refer to Fact 2.4.1. The opportunity cost of producing 1 kilogram of butter is

- A) 20 minutes (1/3 hour) for Andy and 1 hour for Rolfe.
- B) 1 hour for Andy and 1 hour for Rolfe.
- C) 3 loaves of bread for Andy and 1/3 loaf of bread for Rolfe.
- D) 3 loaves of bread for Andy and 1 loaf of bread for Rolfe.
- E) 8 loaves of bread for Rolfe and 24 loaves of bread for Andy.

Answer: D

Diff: 2 Type: MC

Topic: Gains from Trade

9) Given Fact 2.4.1, Andy and Rolfe

- A) can gain from trade if Andy specializes in butter production and Rolfe specializes in bread production.
- B) can gain from trade if Andy specializes in bread production and Rolfe specializes in butter production.
- C) cannot gain from trade.
- D) can trade, but only Rolfe will gain.
- E) can trade, but only Andy will gain.

Answer: B

Diff: 3 Type: MC

Topic: Gains from Trade

Source: Study Guide

10) Consider Fact 2.4.1. After specialization, *total* consumption will

- A) depend on the preferences of Andy and Rolfe.
- B) be 8 loaves of bread and 24 kilograms of butter.
- C) be 32 loaves of bread and 16 kilograms of butter.
- D) be 8 loaves of bread and 8 kilograms of butter.
- E) be 24 loaves of bread and 8 kilograms of butter.

Answer: E

Diff: 2 Type: MC

Topic: Gains from Trade

Use the information below to answer the following questions.

**Fact 2.4.2**

Agnes can produce either 1 unit of  $X$  or 1 unit of  $Y$  in an hour, while Brenda can produce either 2 units of  $X$  or 4 units of  $Y$  in an hour.

11) Refer to Fact 2.4.2. Which one of the following statements is true?

- A) Brenda has an absolute advantage over Agnes in the production of both goods.
- B) Agnes has a comparative advantage in the production of  $Y$ .
- C) Brenda has a comparative advantage in the production of  $X$ .
- D) Brenda will not gain from trade.
- E) Agnes will not gain from trade.

Answer: A

Diff: 3 Type: MC

Topic: Gains from Trade

12) Given Fact 2.4.2, the opportunity cost of producing a unit of  $X$  is

- A) 1 unit of  $Y$  for Agnes and 2 units of  $Y$  for Brenda.
- B) 1 unit of  $Y$  for Agnes and  $1/2$  unit of  $Y$  for Brenda.
- C) 1 hour for Agnes and  $1/2$  hour for Brenda.
- D) 1 hour for Agnes and 2 hours for Brenda.
- E) 1 hour for Agnes and  $1/4$  hour for Brenda.

Answer: A

Diff: 2 Type: MC

Topic: Gains from Trade

13) Given Fact 2.4.2, the opportunity cost of producing a unit of  $Y$  is

- A) 1 unit of  $Y$  for Agnes and 2 units of  $Y$  for Brenda.
- B) 1 unit of  $Y$  for Agnes and  $1/2$  unit of  $Y$  for Brenda.
- C) 1 hour for Agnes and  $1/2$  hour for Brenda.
- D) 1 hour for Agnes and 2 hours for Brenda.
- E) 1 unit of  $X$  for Agnes and  $1/2$  unit of  $X$  for Brenda.

Answer: E

Diff: 2 Type: MC

Topic: Gains from Trade

14) Complete the following sentence. Given Fact 2.4.2,

- A) there will be gains from trade, no matter what Brenda and Agnes specialize in, as long as they specialize.
- B) there will be gains from trade only if Agnes specializes in the production of *Y* and Brenda in *X*.
- C) there will be gains from trade only if Agnes becomes faster at producing *X*.
- D) there will be no gains from trade because Agnes has an absolute advantage.
- E) there will be gains from trade if Agnes specializes in the production of *X* and Brenda in *Y*.

Answer: E

Diff: 2 Type: MC

Topic: Gains from Trade

15) Given Fact 2.4.2, what would be the total output of *X* and *Y* in an eight-hour day if Agnes and Brenda each specialized in producing the good in which they have a comparative advantage?

- A) 3 units of *X* and 5 units of *Y*
- B) 8 units of *X* and 16 units of *Y*
- C) 8 units of *X* and 32 units of *Y*
- D) 24 units of *X* and 40 units of *Y*
- E) 16 units of *X* and 8 units of *Y*

Answer: C

Diff: 3 Type: MC

Topic: Gains from Trade

16) Any two individuals will gain from exchange

- A) unless one has an absolute advantage in producing all goods.
- B) if each specializes in the production of the good for which he has the higher opportunity cost.
- C) unless they have the same opportunity costs for producing all goods.
- D) unless they have different opportunity costs for producing all goods.
- E) unless they have the same absolute advantage in producing all goods.

Answer: C

Diff: 3 Type: MC

Topic: Gains from Trade

Use the figure below to answer the following questions.

**Table 2.4.1**

The planets of Vulcan and Romulus each produce goods X and Y.  
The following table gives points on their production possibilities frontiers.

Vulcan		Romulus	
Good X	Good Y	Good X	Good Y
0	16	0	12
2	12	2	9
4	8	4	6
6	4	6	3
8	0	8	0

17) Refer to Table 2.4.1. Which one of the following is true?

- A) Romulus has both an absolute advantage and a comparative advantage in the production of Y.
- B) Romulus has both an absolute advantage and a comparative advantage in the production of X.
- C) Vulcan has a comparative advantage in the production of X.
- D) Romulus has a comparative advantage in the production of X.
- E) Vulcan should specialize in the production of X.

Answer: D

Diff: 3 Type: MC

Topic: Gains from Trade

18) Refer to Table 2.4.1. Which one of the following is true?

- A) The opportunity cost of producing more of good X is the same for both planets.
- B) The opportunity cost of producing more of good Y is the same for both planets.
- C) The opportunity cost of producing more of good X is lower in Vulcan.
- D) The opportunity cost of producing more of good Y is lower in Vulcan.
- E) Vulcans are smarter than Romulans.

Answer: D

Diff: 3 Type: MC

Topic: Gains from Trade

19) Refer to Table 2.4.1. For Vulcan, the opportunity cost of producing an additional unit of X is

- A) 4 units of Y.
- B) 2 units of Y.
- C)  $\frac{2}{3}$  units of Y.
- D) 1 unit of Y.
- E) dependent upon how many units of X are already produced.

Answer: B

Diff: 2 Type: MC

Topic: Gains from Trade

20) Refer to Table 2.4.1. For Romulus, the opportunity cost of producing an additional unit of  $X$  is

- A) 4 units of  $Y$ .
- B) 2 units of  $Y$ .
- C)  $2/3$  units of  $Y$ .
- D) 1 unit of  $Y$ .
- E)  $3/2$  units of  $Y$ .

Answer: E

Diff: 2 Type: MC

Topic: Gains from Trade

21) Refer to Table 2.4.1. For Romulus, the opportunity cost of producing an additional unit of  $Y$  is

- A)  $2/3$  units of  $X$ .
- B)  $1/2$  unit of  $X$ .
- C) 2 units of  $X$ .
- D) 3 units of  $X$ .
- E)  $3/2$  units of  $Y$ .

Answer: A

Diff: 2 Type: MC

Topic: Gains from Trade

22) Refer to Table 2.4.1. For Vulcan, the opportunity cost of producing an additional unit of  $Y$  is

- A)  $2/3$  units of  $X$ .
- B)  $1/2$  units of  $X$ .
- C) 2 units of  $X$ .
- D) 3 units of  $X$ .
- E) 4 units of  $X$ .

Answer: B

Diff: 2 Type: MC

Topic: Gains from Trade

23) Refer to Table 2.4.1. Each country will gain from trade if

- A) Romulus specializes in both goods.
- B) Vulcan specializes in both goods.
- C) they both continue to produce both goods.
- D) Vulcan specializes in good  $X$  and Romulus specializes in good  $Y$ .
- E) Romulus specializes in good  $X$  and Vulcan specializes in good  $Y$ .

Answer: E

Diff: 3 Type: MC

Topic: Gains from Trade

24) If individuals *A* and *B* can both produce only goods *X* and *Y* and *A* does *not* have a comparative advantage in the production of either *X* or *Y*, then we know

- A) *B* has an absolute advantage in the production of *X* and *Y*.
- B) *A* and *B* have the same opportunity costs for *X* and for *Y*.
- C) *B* has a comparative advantage in the production of both *X* and *Y*.
- D) the gains from trade will be large but only in one direction.
- E) *A* must have lower opportunity costs of production for both goods.

Answer: B

Diff: 3 Type: MC

Topic: Gains from Trade

25) Consider the following household. In 5 hours, Bob can cook 5 meals or clean 6 rooms. In 5 hours, Mary can cook 30 meals or clean 10 rooms. Select the best statement.

- A) Bob has an absolute advantage in the production of both goods.
- B) Since Mary is better at producing both goods, she should produce both.
- C) Bob has a comparative advantage in cooking.
- D) Mary should specialize in cooking.
- E) none of the above

Answer: D

Diff: 3 Type: MC

Topic: Gains from Trade

*Use the table below to answer the following questions.*

**Table 2.4.2**  
Production for one week by Sheila and Bruce

Sheila		Bruce	
Good X	Good Y	Good X	Good Y
8	0	20	0
6	1	15	2
4	2	10	4
2	3	5	6
0	4	0	8

26) Given the information in Table 2.4.2, can Sheila and Bruce gain by specialization?

- A) Yes, but only if Bruce gets paid more than Sheila.
- B) No, not under the given circumstances.
- C) It depends on the wages each earns.
- D) Only if they are married to each other.
- E) Yes, if each specializes in the good in which he has a comparative advantage.

Answer: E

Diff: 2 Type: MC

Topic: Gains from Trade

27) Given the information in Table 2.4.2, which one of the following is true?

- A) Sheila should specialize in good X.
- B) Bruce should specialize in good X.
- C) The opportunity cost to Bruce of an additional unit of X is 0.4 units of Y.
- D) A and B.
- E) B and C.

Answer: E

Diff: 3 Type: MC

Topic: Gains from Trade

28) Suppose John and Joe each have different production possibility frontiers; John specializes in cloth and Joe specializes in corn. John's island unexpectedly has exceptionally good weather, and suddenly he is twice as productive in the production of *both* corn and cloth. Select the best statement.

- A) This is an example of unemployed resources becoming employed.
- B) As a result, John will have an absolute advantage in both corn and cloth.
- C) As a result, it is possible that John and Joe will switch what they specialize in.
- D) There will be no change in what John and Joe specialize in, because John's comparative advantage has not changed.
- E) There will be a change in what John and Joe specialize in, because John's opportunity cost of production will have risen.

Answer: D

Diff: 3 Type: MC

Topic: Gains from Trade

29) It pays for people to specialize and trade with each other because

- A) otherwise they would not survive.
- B) they can take advantage of the fact they have an absolute advantage in the production of something.
- C) this way they can consume outside their production possibilities frontier.
- D) this way the strong can exploit the weak.
- E) all of the above.

Answer: C

Diff: 2 Type: MC

Topic: Gains from Trade

30) There are two goods, X and Y. If the opportunity cost of producing good X is lower for Pam than for Gino, then

- A) Pam has an absolute advantage in the production of X.
- B) Gino has an absolute advantage in the production of Y.
- C) Pam has a comparative advantage in the production of X.
- D) Gino has a comparative advantage in the production of Y.
- E) C and D.

Answer: E

Diff: 3 Type: MC

Topic: Gains from Trade

31) Mexico and Canada produce both oil and apples using labour only. A barrel of oil is produced with 4 hours of labour in Mexico and 8 hours of labour in Canada. A bushel of apples is produced with 8 hours of labour in Mexico and 12 hours of labour in Canada. Canada has

- A) an absolute advantage in oil production.
- B) an absolute advantage in apple production.
- C) a comparative advantage in oil production.
- D) a comparative advantage in apple production.
- E) none of the above.

Answer: D

Diff: 3 Type: MC

Topic: Gains from Trade

Source: Study Guide

32) In Portugal, the opportunity cost of a bale of wool is 3 bottles of wine. In England, the opportunity cost of 1 bottle of wine is 3 bales of wool. Given this information,

- A) England has an absolute advantage in wine production.
- B) Portugal has an absolute advantage in wool production.
- C) Portugal has a comparative advantage in wine production.
- D) Portugal has a comparative advantage in wool production.
- E) no trade will occur.

Answer: C

Diff: 3 Type: MC

Topic: Gains from Trade

Source: Study Guide

33) To gain from comparative advantage, countries must not only trade, they must also

- A) save.
- B) invest.
- C) engage in research and development.
- D) engage in capital accumulation.
- E) specialize.

Answer: E

Diff: 1 Type: MC

Topic: Gains from Trade

Source: Study Guide

34) In one hour, Sue can produce 50 caps or 10 jackets and Tessa can produce 70 caps or 7 jackets. Sue's opportunity cost of producing a cap is \_\_\_\_\_ jackets and Tessa's opportunity cost of producing a cap is \_\_\_\_\_ jackets.

\_\_\_\_\_ has a comparative advantage in producing caps.

If Sue and Tessa each specialize in producing the good in which they have a comparative advantage and trade 1 jacket for 7 caps, \_\_\_\_\_.

- A) 0.2; 0.10; Sue; Tessa gains but Sue loses
- B) 5.0; 10.0; Tessa; Sue loses but Tessa gains
- C) 5.0; 10.0; Sue; both Sue and Tessa gain
- D) 0.2; 0.10; Tessa; both Sue and Tessa gain
- E) 0.2; 0.10; Sue; both Sue and Tessa gain

Answer: D

Type: MC

Topic: Gains from Trade

Source: MyEconLab

35) Tom takes 20 minutes to cook an egg and 5 minutes to make a sandwich. Jerry takes 15 minutes to cook an egg and 3 minutes to make a sandwich. If Tom and Jerry specialize and trade eggs and sandwiches with each other \_\_\_\_\_.

- A) Tom benefits but Jerry does not
- B) Jerry benefits but Tom does not
- C) neither Tom nor Jerry benefit
- D) either Tom or Jerry benefit but we don't have enough information to know which one benefits
- E) both of them benefit

Answer: E

Type: MC

36) Tom takes 20 minutes to cook an egg and 5 minutes to make a sandwich. Jerry takes 15 minutes to cook an egg and 3 minutes to make a sandwich. Both individuals gain if \_\_\_\_\_.

- A) Jerry produces eggs and trades them to Tom for sandwiches
- B) Jerry produces sandwiches and trades them to Tom for eggs
- C) they trade with each other regardless of who produces sandwiches and who produces eggs
- D) the opportunity cost of producing an egg is greater than the opportunity cost of producing a sandwich
- E) the opportunity cost of producing a sandwich is greater than the opportunity cost of producing an egg

Answer: B

Type: MC

## 2.5 Economic Coordination

1) Trade is organized using the social institutions of

- A) firms.
- B) property rights.
- C) money.
- D) markets.
- E) all of the above.

Answer: E

Diff: 3 Type: MC

Topic: Economic Coordination

Source: Study Guide

2) Markets

- I. enable buyers and sellers to get information
- II. are defined by economists as geographical locations where trade occurs.
- III. have evolved because they facilitate trade.

Which of the above statements are correct?

- A) I only
- B) III only
- C) I and III only
- D) II and III only
- E) I, II and III

Answer: C

Type: MC

Topic: Economic Coordination

Source: Study Guide

3) A property right is

- A) any commodity or token that is generally acceptable as a means of payment.
- B) an economic unit that hires factors of production and organizes those factors to produce and sell goods and services.
- C) any arrangement that enables buyers and sellers to get information and to do business with each other.
- D) a social arrangement that governs the ownership, use, and disposal of anything that people value.
- E) a medium of exchange.

Answer: D

Type: MC

Topic: Economic Coordination

Source: MyEconLab

- 4) The flows in the market economy that go from firms to households are \_\_\_\_\_.  
The flows in the market economy that go from households to firms are \_\_\_\_\_.
- A) all flowing through goods markets; all flowing through factor markets
  - B) the real flows of goods and services and the income flows of wages, rent, interest and profits; the real flows of labour, land, capital and entrepreneurship and the flow of expenditure on goods and services
  - C) the income flows of wages, rent, interest, and profits and the flow of expenditure on goods and services; the real flows of goods and services and the real flows of labour, land, capital and entrepreneurship
  - D) the real flows of goods and services and the real flows of labour, land, capital and entrepreneurship; the income flows of wages, rent, interest, and profits and the flow of expenditure on goods and services
  - E) all flowing through factor markets; all flowing through goods markets

Answer: B

Type: MC

Topic: Economic Coordination

Source: MyEconLab

- 5) The main functions of markets include
- A) promoting the social interest, but not the self-interest.
  - B) selling goods but not factors of production.
  - C) enabling buyers and sellers to get information about each other.
  - D) establishing a physical location for business transactions.
  - E) promoting the self-interest but not the social interest.

Answer: C

Type: MC

Topic: Economic Coordination

Source: MyEconLab

- 6) In an economy lacking property rights, it would be \_\_\_\_\_ to realize the gains from trade and there would be \_\_\_\_\_ specialization compared to an economy with property rights.
- A) more difficult; less
  - B) more difficult; more
  - C) easier; less
  - D) easier; more
  - E) none of the above

Answer: A

Type: MC

- 7) Intellectual property \_\_\_\_\_.
- A) includes land and buildings
  - B) includes stocks and bonds and money in the bank
  - C) is the intangible product of creative effort
  - D) is protected by copyrights and patents
  - E) both C and D are correct

Answer: E

Type: MC

## Chapter 3 Demand and Supply

### 3.1 Markets and Prices

1) The relative price of a good is all of the following *except*

- A) the ratio of one price to another.
- B) an opportunity cost.
- C) the money price of the good divided by a price index.
- D) the same as the money price of a good.
- E) determined in a market.

Answer: D

Diff: 2 Type: MC

Topic: Markets and Prices

2) How many sides does a market have?

- A) one side - buyers
- B) one side - sellers
- C) two sides - buyers and sellers
- D) three sides - buyers, sellers, and the government
- E) two sides - domestic and foreign

Answer: C

Diff: 1 Type: MC

Topic: Markets and Prices

3) Which market is an example of a market for goods?

- A) labour market
- B) haircut market
- C) manufactured input market
- D) apple market
- E) energy market

Answer: D

Diff: 1 Type: MC

Topic: Markets and Prices

4) Which market is an example of a market for services?

- A) orange market
- B) tennis lessons market
- C) manufactured input market
- D) energy market
- E) labour market

Answer: B

Diff: 1 Type: MC

Topic: Markets and Prices

5) Which market is an example of a resource market?

- A) furniture market
- B) apple market
- C) automobile market
- D) haircut market
- E) labour market

Answer: E

Diff: 1 Type: MC

Topic: Markets and Prices

6) The demand and supply model determines

- A) relative prices.
- B) money prices.
- C) supply prices.
- D) demand prices.
- E) absolute prices.

Answer: A

Diff: 1 Type: MC

Topic: Markets and Prices

*Use the table below to answer the following questions.*

**Table 3.1.1**

Year	Coffee Price	Tea Price	Cola Price
2010	\$1.25	\$1.10	\$0.80
2011	\$1.50	\$1.00	\$1.00
2012	\$1.25	\$1.20	\$1.00

7) Refer to Table 3.1.1. In 2010, the relative price of coffee in terms of tea is

- A) 1.25.
- B) 1.10.
- C) 1.00.
- D) 0.88.
- E) 1.14.

Answer: E

Diff: 2 Type: MC

Topic: Markets and Prices

- 8) Refer to Table 3.1.1. In 2012, the relative price of coffee in terms of cola is
- A) 1.25.
  - B) 1.00.
  - C) 0.67.
  - D) 1.56.
  - E) unknown without more information.

Answer: A

Diff: 2 Type: MC

Topic: Markets and Prices

- 9) Refer to Table 3.1.1. In 2012, the relative price of cola in terms of tea is
- A) 1.00.
  - B) 1.20.
  - C) 0.83.
  - D) 1.25.
  - E) unknown without more information.

Answer: C

Diff: 2 Type: MC

Topic: Markets and Prices

- 10) Refer to Table 3.1.1. Between 2010 and 2011, the price of coffee relative to the price of tea \_\_\_\_\_ while the price of coffee relative to the price of cola \_\_\_\_\_.

- A) rose; rose
- B) rose; fell
- C) fell; rose
- D) fell; fell
- E) fell; stayed constant

Answer: B

Diff: 2 Type: MC

Topic: Markets and Prices

- 11) Refer to Table 3.1.1. Between 2011 and 2012, the price of coffee relative to the price of tea \_\_\_\_\_ while the price of coffee relative to the price of cola \_\_\_\_\_.

- A) rose; rose
- B) rose; fell
- C) fell; rose
- D) fell; fell
- E) fell; stayed constant

Answer: D

Diff: 2 Type: MC

Topic: Markets and Prices

12) A market where no single buyer or seller can influence the price is

- A) a buyer's market.
- B) a seller's market.
- C) a competitive market.
- D) an output market.
- E) an input market.

Answer: C

Diff: 1 Type: MC

Topic: Markets and Prices

13) A relative price is

- A) the ratio of one price to another.
- B) an opportunity cost.
- C) a quantity of a "basket" of goods and services forgone.
- D) determined by demand and supply.
- E) all of the above.

Answer: E

Diff: 2 Type: MC

Topic: Markets and Prices

Source: Study Guide

14) William Gregg owned a mill in South Carolina. In December 1862, he placed a notice in the *Edgehill Advertiser* announcing his willingness to exchange cloth for food and other items. Here is an extract:

- 1 yard of cloth for 1 pound of bacon
- 2 yards of cloth for 1 pound of butter
- 4 yards of cloth for 1 pound of wool
- 8 yards of cloth for 1 bushel of salt

If the money price of bacon was 20¢ a pound and the money price of salt was \$2.00 a bushel, people would \_\_\_\_\_.

- A) buy bacon and trade it for cloth because they could buy 8 yards of cloth for only \$1.60, and use that cloth to obtain a bushel of salt
- B) not buy bacon and trade it for cloth because they would have to buy 8 yards of cloth for \$1.60 and then give Mr. Gregg an extra \$0.40 to buy a bushel of salt
- C) buy bacon and trade it for cloth and then trade the cloth for salt because salt is more important for life than either cloth or bacon
- D) not buy bacon and trade it for cloth because the relative price of 1 bushel of salt is only 1/8 yard of cloth
- E) buy bacon and trade it for cloth because cloth is more expensive than bacon

Answer: A

Diff: 2 Type: MC

Topic: Markets and Prices

Source: MyEconLab

- 15) The opportunity cost of good A in terms of good B is equal to the
- A) money price of good A minus the money price of good B.
  - B) money price of good B minus the money price of good A.
  - C) ratio of the money price of good A to the money price of good B.
  - D) ratio of the money price of good B to the money price of good A.
  - E) money price of good A plus the money price of good B.

Answer: C

Type: MC

- 16) Suppose the price of a football is \$20.00 and the price of a basketball is \$10.00. The \_\_\_\_\_ of a football is \_\_\_\_\_.

- A) relative price; 2 basketballs per football
- B) relative price; 1/2 basketball per football
- C) opportunity cost; \$15.00
- D) opportunity cost; \$10.00
- E) relative price; \$10

Answer: A

Type: MC

### 3.2 Demand

- 1) The law of demand states that, other things remaining the same,  
A) the higher the price of a good, the smaller is the quantity demanded.  
B) the higher the price of a good, the smaller is the quantity supplied.  
C) price and quantity supplied are positively related.  
D) as income increases, willingness to pay for the last unit increases.  
E) the higher the price of a good, the greater is the quantity demanded.

Answer: A

Diff: 1 Type: MC

Topic: Demand

- 2) Which one of the following events shifts the demand curve for grape jelly to the right?  
A) an increase in income if grape jelly is a normal good  
B) a decrease in the price of strawberry preserves, a substitute for grape jelly  
C) a decrease in the price of grape jelly  
D) an increase in the price of peanut butter, a complement of grape jelly  
E) a decrease in the population

Answer: A

Diff: 2 Type: MC

Topic: Demand

- 3) The demand curve slopes downward to the right because  
A) an increase in income leads to increased consumption.  
B) of the law of supply.  
C) of the law of demand.  
D) of comparative advantage.  
E) as income rises, the quantity demanded increases.

Answer: C

Diff: 1 Type: MC

Topic: Demand

- 4) An increase in the price of ground beef  
A) increases the demand for chicken, a substitute for ground beef.  
B) increases the demand for hamburger buns, a complement of ground beef.  
C) increases the quantity demanded of ground beef.  
D) decreases the quantity demanded of ground beef.  
E) both A and D.

Answer: E

Diff: 2 Type: MC

Topic: Demand

5) An increase in income

- A) increases the demand for turnips if a turnip is an inferior good.
- B) increases the demand for turnips if a turnip is a normal good.
- C) increases the supply of turnips.
- D) decreases the demand for turnips if turnips have a very low price.
- E) decreases the supply of turnips.

Answer: B

Diff: 2 Type: MC

Topic: Demand

6) A turnip is an inferior good if

- A) an increase in the price of a turnip decreases the quantity of turnips that consumers want to buy.
- B) an increase in income decreases the demand for turnips.
- C) an increase in income increases the demand for turnips.
- D) turnips violate the law of demand.
- E) turnips are a low quality good.

Answer: B

Diff: 2 Type: MC

Topic: Demand

7) If a turnip is an inferior good, then, *ceteris paribus*, an increase in the price of a turnip will

- A) decrease the demand for turnips.
- B) increase the demand for turnips.
- C) decrease the supply of turnips.
- D) increase the supply of turnips.
- E) none of the above.

Answer: E

Diff: 3 Type: MC

Topic: Demand

8) Suppose income increases. Choose the correct statement.

- A) The equilibrium price of turnips falls if a turnip is an inferior good.
- B) The equilibrium price of turnips rises if a turnip is an inferior good.
- C) The equilibrium quantity of turnips decreases if a turnip is an inferior good.
- D) The supply of turnips decreases whether or not a turnip is an inferior good.
- E) Both A and C.

Answer: E

Diff: 3 Type: MC

Topic: Demand

Use the figure below to answer the following questions.



**Figure 3.2.1**

9) Point A in Figure 3.2.1 indicates that

- A) \$1 is the least that consumers are willing to pay for the 4,000th apple.
- B) consumers will not be in equilibrium if the price of an apple is \$1.
- C) consumers will only pay \$1 for any apple.
- D) if the price is \$1, consumers will plan to buy 4,000 apples.
- E) if the price is more than \$1, consumers will buy 9,000 apples.

Answer: D

Diff: 2 Type: MC

Topic: Demand

10) Which one of the following statements best characterizes point B in Figure 3.2.1?

- A) Producers would be unwilling to sell the 9,000th apple for less than \$0.50.
- B) The most that consumers would be willing to pay for the 9,000th apple is \$0.50.
- C) At a price of \$0.50, consumers will be unwilling to buy any apples.
- D) At a price of \$0.50, there will be an apple shortage.
- E) At point B, the market is in equilibrium.

Answer: B

Diff: 2 Type: MC

Topic: Demand

11) Given Figure 3.2.1, under what condition are consumers willing to buy more than 9,000 apples per week?

- A) if the price is above \$1
- B) if the price is between \$1 and \$0.50
- C) if the price is below \$0.50
- D) if the price is between \$1 and \$1.50
- E) if the price is \$0.75

Answer: C

Diff: 2 Type: MC

Topic: Demand

12) Which one of the following would result in a movement from point *A* to point *B* in Figure 3.2.1?

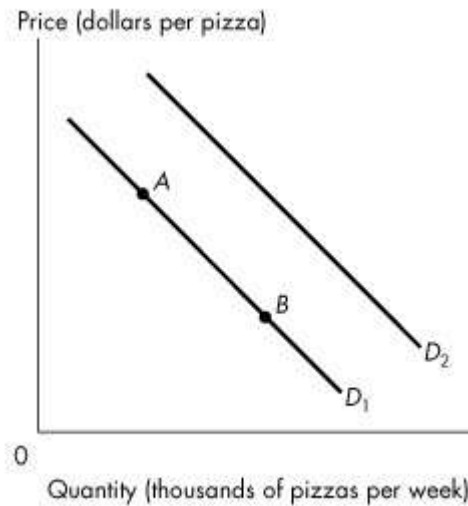
- A) a fall in the price of apples
- B) a rise in the price of oranges
- C) an increase in population size
- D) public concern about chemicals sprayed on apples
- E) a rise in the price of bananas

Answer: A

Diff: 2 Type: MC

Topic: Demand

Use the figure below to answer the following questions.



**Figure 3.2.2**

13) Which one of the following would result in the demand curve shifting from  $D_1$  to  $D_2$  in Figure 3.2.2?

- A) an increase in the supply of pizza
- B) a rise in the price of hamburgers, a substitute for pizza
- C) a rise in the price of pizza
- D) a fall in the price of pizza
- E) a rise in the price of Coke, a complement of pizza

Answer: B

Diff: 2 Type: MC

Topic: Demand

14) Refer to Figure 3.2.2. Which one of the following represents a decrease in quantity demanded?

- A) a shift from  $D_1$  to  $D_2$
- B) a shift from  $D_2$  to  $D_1$
- C) a movement from A to B
- D) a movement from B to A
- E) none of the above

Answer: D

Diff: 2 Type: MC

Topic: Demand

- 15) Refer to Figure 3.2.2. If consumers' income increases,
- A) the quantity of pizzas demanded increases.
  - B) the demand curve for pizzas shifts from  $D_1$  to  $D_2$  if a pizza is a normal good.
  - C) the supply of pizzas increases.
  - D) the quantity of pizzas supplied decreases.
  - E) a movement from point  $A$  to point  $B$  on  $D_1$  occurs.

Answer: B

Diff: 2 Type: MC

Topic: Demand

- 16) The price of good  $A$  rises, and the demand curve for good  $B$  shifts leftward. We can conclude that

- A)  $A$  and  $B$  are substitutes.
- B)  $A$  and  $B$  are complements.
- C)  $A$  and  $B$  are complements in production.
- D)  $B$  is an inferior good.
- E)  $B$  is a normal good.

Answer: B

Diff: 2 Type: MC

Topic: Demand

- 17) The price of good  $X$  falls and the demand for good  $Y$  decreases. We can conclude that

- A)  $X$  and  $Y$  are complements.
- B)  $X$  and  $Y$  are independent of each other.
- C)  $X$  is an inferior good.
- D)  $X$  is a normal good.
- E)  $X$  and  $Y$  are substitutes.

Answer: E

Diff: 2 Type: MC

Topic: Demand

- 18) Which one of the following would lead to an increase in the demand for hamburgers?

- A) a new fad hamburger diet
- B) a decrease in population size
- C) a rise in the price of French fries, a complement of hamburgers
- D) a decrease in consumer income if hamburgers are a normal good
- E) a news report that hamburgers can cause skin diseases

Answer: A

Diff: 2 Type: MC

Topic: Demand

19) Which of the following "other things" are *not* held constant along a demand curve?

- A) income
- B) prices of related goods
- C) the price of the good itself
- D) preferences
- E) expected future income and credit

Answer: C

Diff: 1 Type: MC

Topic: Demand

Source: Study Guide

20) Good A is a normal good if

- A) a rise in the price of a complement causes the demand for A to decrease.
- B) income and the demand for A are negatively related.
- C) a rise in the price of a substitute causes the demand for A to increase.
- D) the demand for A increases when income rises.
- E) good A satisfies the law of demand.

Answer: D

Diff: 1 Type: MC

Topic: Demand

21) A decrease in quantity demanded is represented by a

- A) rightward shift of the supply curve.
- B) rightward shift of the demand curve.
- C) leftward shift of the demand curve.
- D) movement upward and to the left along the demand curve.
- E) movement downward and to the right along the demand curve.

Answer: D

Diff: 1 Type: MC

Topic: Demand

Source: Study Guide

22) Some sales managers are talking shop. Which of the following quotations refers to a movement along the demand curve?

- A) "Since our competitors raised their prices, our sales have doubled."
- B) "It has been an unusually mild winter; our sales of wool scarves are down from last year."
- C) "We decided to cut our prices, and the increase in our sales has been remarkable."
- D) "The Green movement has sparked an increase in our sales of biodegradable products."
- E) None of the above.

Answer: C

Diff: 2 Type: MC

Topic: Demand

Source: Study Guide

23) Some sales managers are talking shop. Which one of the following quotations refers to a rightward shift of the demand curve?

- A) "Since our competitors raised their prices, our sales have doubled."
- B) "It has been an unusually harsh winter; our sales of wool scarves are up from last year."
- C) "We decided to cut our prices, and the increase in our sales has been remarkable."
- D) "The Green movement has sparked an increase in our sales of biodegradable products."
- E) All of the above *except* C.

Answer: E

Diff: 2 Type: MC

Topic: Demand

24) Some sales managers are talking shop. Which one of the following quotations refers to a leftward shift of the demand curve?

- A) "Since our competitors raised their prices, our sales have doubled."
- B) "It has been an unusually mild winter; our sales of wool scarves are down from last year."
- C) "We decided to cut our prices, and the increase in our sales has been remarkable."
- D) "The Green movement has sparked an increase in our sales of biodegradable products."
- E) None of the above.

Answer: B

Diff: 2 Type: MC

Topic: Demand

25) If Hamburger Helper is an inferior good, then, *ceteris paribus*, a decrease in income will lead to

- A) a leftward shift of the demand curve for Hamburger Helper.
- B) a rightward shift of the demand curve for Hamburger Helper.
- C) a movement up along the demand curve for Hamburger Helper.
- D) a movement down along the demand curve for Hamburger Helper.
- E) an initial movement up and then down along the demand curve for Hamburger Helper.

Answer: B

Diff: 2 Type: MC

Topic: Demand

Source: Study Guide

26) Consider the market for cell phones. Suppose the price of a cell phone falls. Explain the effect of this event on the quantity of cell phones demanded and on the demand for cell phones.

- A) The quantity of cell phones demanded is unchanged and the demand for cell phones increases.
- B) The quantity of cell phones demanded decreases and the demand for cell phones is unchanged.
- C) The quantity of cell phones demanded increases and the demand for cell phones is unchanged.
- D) The quantity of cell phones demanded increases and the demand for cell phones also increases.
- E) The quantity of cell phones demanded is unchanged and the demand for cell phones decreases.

Answer: C

Diff: 2 Type: MC

Topic: Demand

Source: MyEconLab

27) People buy more of good 1 when the price of good 2 rises. Good 1 and good 2 are

- A) complements.
- B) substitutes.
- C) normal goods.
- D) inferior goods.
- E) substitutes in production

Answer: B

Type: MC

28) Oatmeal is a normal good and cold cereal is a substitute for oatmeal. Raisins are a complement of oatmeal. Which of the following increases the demand for oatmeal?

- A) an increase in the price of raisins
- B) a decrease in income
- C) a decrease in population
- D) an increase in the price of cold cereal
- E) an increase in the supply of oatmeal

Answer: D

Type: MC

### 3.3 Supply

- 1) The law of supply tells us that other things remaining the same, as the
- A) price of gasoline falls, the quantity of gasoline supplied decreases.
  - B) price of gasoline rises, the quantity of gasoline supplied decreases.
  - C) supply of gasoline increases, the price of gasoline falls.
  - D) cost of producing gasoline falls, the supply of gasoline will increase.
  - E) cost of producing gasoline increases, the price of gasoline rises.

Answer: A

Diff: 2 Type: MC

Topic: Supply

- 2) The supply curve of a good slopes upward to the right because of
- A) technological improvements over time.
  - B) the law of supply.
  - C) the law of demand.
  - D) the existence of substitutes in production.
  - E) the fact that prices tend to rise over time.

Answer: B

Diff: 1 Type: MC

Topic: Supply

- 3) An increase in supply is shown by
- A) a movement down along the supply curve.
  - B) a movement up along the supply curve.
  - C) a rightward shift of the supply curve.
  - D) a leftward shift of the supply curve.
  - E) an initial movement up and then down along the same supply curve.

Answer: C

Diff: 1 Type: MC

Topic: Supply

- 4) If goods  $X$  and  $Y$  are substitutes in production, then a rise in the price of good  $X$
- A) increases the demand for good  $Y$ .
  - B) decreases the demand for good  $Y$ .
  - C) increases the supply of good  $Y$ .
  - D) decreases the supply of good  $Y$ .
  - E) might change the supply of  $Y$ ; it depends on whether  $X$  and  $Y$  are also substitutes.

Answer: D

Diff: 2 Type: MC

Topic: Supply

5) If a producer can use its factors of production to produce either good *A* or good *B*, then a rise in the price of *A*

- A) increases the supply of *B*.
- B) decreases the supply of *A*.
- C) increases the supply of *A*.
- D) decreases the supply of *B*.
- E) both C and D.

Answer: D

Diff: 3 Type: MC

Topic: Supply

6) The fact that a fall in the price of a good results in a decrease in the quantity of the good supplied illustrates

- A) the law of supply.
- B) the law of demand.
- C) a change in supply.
- D) the nature of an inferior good.
- E) technological improvement.

Answer: A

Diff: 1 Type: MC

Topic: Supply

Source: Study Guide

7) Which one of the following would *not* shift the supply curve of good *X* to the right?

- A) a fall in the price of the factors of production used in producing *X*
- B) an improvement in technology used in the production of *X*
- C) a rise in the price of *X*
- D) an increase in the price of *Y*, a complement in production of *X*
- E) a fall in the price of *Y*, a substitute in production of *X*

Answer: C

Diff: 2 Type: MC

Topic: Supply

8) A decrease in the quantity supplied is shown by a

- A) movement down along the supply curve.
- B) movement up along the supply curve.
- C) rightward shift of the supply curve.
- D) leftward shift of the supply curve.
- E) rightward shift of the demand curve.

Answer: A

Diff: 1 Type: MC

Topic: Supply

9) Which one of the following will shift the supply curve of good *X* leftward?

- A) a decrease in the wages of workers employed to produce *X*
- B) an increase in the cost of machinery used to produce *X*
- C) a technological improvement in the production of *X*
- D) a situation where quantity demanded exceeds quantity supplied
- E) a decrease in the cost of capital used to produce *X*

Answer: B

Diff: 2 Type: MC

Topic: Supply

Source: Study Guide

10) Which of the following will shift the supply curve of good *X* rightward?

- A) a decrease in the wages of workers employed to produce good *X*
- B) an increase in the cost of capital used to produce good *X*
- C) an increase in the price of energy
- D) a decrease in the number of suppliers of good *X*
- E) the price of *Y*, a substitute in production for good *X*, rises

Answer: A

Diff: 2 Type: MC

Topic: Supply

11) If a factor of production can be used to produce either good *A* or good *B*, then *A* and *B* are

- A) substitutes in production.
- B) complements in production.
- C) substitutes.
- D) complements.
- E) normal goods.

Answer: A

Diff: 1 Type: MC

Topic: Supply

Source: Study Guide

12) A rise in the price of a good

- A) decreases demand for the good.
- B) creates a movement up along the supply curve.
- C) creates a movement down along the demand curve.
- D) increases the supply of the good.
- E) increases preferences for the good.

Answer: B

Diff: 1 Type: MC

Topic: Supply

- 13) If the number of suppliers of good *Y* increases, then
- A) a movement up along the supply curve of good *Y* will occur.
  - B) a movement down along the supply curve of good *Y* will occur.
  - C) the supply curve of good *Y* shifts rightward.
  - D) the supply curve of good *Y* shifts leftward.
  - E) the supply curve of good *Y* will remain unchanged.

Answer: C

Diff: 1 Type: MC

Topic: Supply

- 14) A shift of the supply curve for rutabagas occurs if there is
- A) a change in preferences for rutabagas.
  - B) a change in the price of a related good that is a substitute for rutabagas.
  - C) a change in income.
  - D) a change in the price of rutabagas.
  - E) none of the above.

Answer: E

Diff: 2 Type: MC

Topic: Supply

Source: Study Guide

- 15) Some producers are chatting over a beer. Which one of the following quotations refers to a movement along the supply curve?

- A) "Wage increases have forced us to raise our prices."
- B) "Our new, sophisticated equipment will enable us to undercut our competitors."
- C) "Raw material prices have sky-rocketed; we will have to pass the cost on to our customers."
- D) "We anticipate a big increase in demand. Our product price should rise, so we are planning for an increase in output."
- E) "New competitors in the industry are causing prices to fall."

Answer: D

Diff: 2 Type: MC

Topic: Supply

Source: Study Guide

- 16) Some producers are chatting over a beer. Which one of the following quotations refers to a rightward shift of the supply curve?

- A) "Wage increases have forced us to raise our prices."
- B) "Our new, sophisticated equipment will enable us to undercut our competitors."
- C) "Raw material prices have sky-rocketed; we will have to pass the cost on to our customers."
- D) "We anticipate a big increase in demand. Our product price should rise, so we are planning for an increase in output."
- E) Both A and C.

Answer: B

Diff: 2 Type: MC

Topic: Supply

17) Some producers are chatting over a beer. Which one of the following quotations refers to a leftward shift of the supply curve?

- A) "Wage increases have forced us to raise our prices."
- B) "Our new, sophisticated equipment will enable us to undercut our competitors."
- C) "Raw material prices have sky-rocketed; we will have to pass the cost on to our customers."
- D) "We anticipate a big increase in demand. Our product price should rise, so we are planning for an increase in output."
- E) Both A and C.

Answer: E

Diff: 2 Type: MC

Topic: Supply

18) A decrease in the quantity supplied of a good is shown by

- A) a movement down along the supply curve.
- B) a leftward shift of the supply curve.
- C) a movement up along the supply curve.
- D) a rightward shift of the supply curve.
- E) an initial rightward shift and then leftward shift of the supply curve.

Answer: A

Diff: 1 Type: MC

Topic: Supply

19) Which of the following decreases the supply of popcorn?

- A) a decrease in the price of popcorn
- B) an increase in the price of popcorn
- C) a technological advance in the production of popcorn
- D) a decrease in the demand for popcorn
- E) a decrease in the number of popcorn producers

Answer: E

Type: MC

20) Which of the following shifts the supply curve for good X leftward?

- A) a situation in which the quantity demanded of X exceeds the quantity supplied of X
- B) an increase in the cost of the machinery used to produce X
- C) a technological advance in the production of X
- D) a decrease in the wages of workers employed to produce X
- E) a situation in which the quantity supplied of X exceeds the quantity demanded of X

Answer: B

Type: MC

### 3.4 Market Equilibrium

Use the table below to answer the following questions.

**Table 3.4.1**

Price (dollars per unit)	Quantity Demanded (units)	Quantity Supplied (units)
1	1,100	50
2	800	200
3	600	420
4	500	500
5	420	580
6	350	640
7	320	680
8	300	700

1) Refer to Table 3.4.1. At a price of \$3 a unit

- A) the market is in equilibrium.
- B) there is a 180-unit surplus.
- C) there is a 180-unit shortage.
- D) there is a tendency for the price to rise.
- E) C and D.

Answer: E

Diff: 2 Type: MC

Topic: Market Equilibrium

2) In Table 3.4.1, the equilibrium price is

- A) \$7 a unit.
- B) \$5 a unit.
- C) \$4 a unit.
- D) \$3 a unit.
- E) \$1 a unit.

Answer: C

Diff: 1 Type: MC

Topic: Market Equilibrium

3) In Table 3.4.1, the equilibrium quantity is

- A) 200 units.
- B) 320 units.
- C) 420 units.
- D) 500 units.
- E) none of the above; there is no equilibrium.

Answer: D

Diff: 1 Type: MC

Topic: Market Equilibrium

4) Refer to Table 3.4.1. The equilibrium quantity is 420 units if

- A) the price is fixed at \$3 a unit.
- B) the price is fixed at \$4 a unit.
- C) the price is fixed at \$5 a unit.
- D) both A and C are correct.
- E) none of the above.

Answer: E

Diff: 2 Type: MC

Topic: Market Equilibrium

5) Refer to Table 3.4.1. A shortage occurs if

- A) the price is \$7 a unit.
- B) the price is \$4 a unit.
- C) the price is \$5 a unit.
- D) the price is below \$4 a unit.
- E) the price is \$6 a unit.

Answer: D

Diff: 1 Type: MC

Topic: Market Equilibrium

6) Refer to Table 3.4.1. A surplus occurs if

- A) the price is \$2 a unit.
- B) the price is \$3 a unit.
- C) the price is above \$4 a unit.
- D) the price is \$1 a unit.
- E) the price is \$4 a unit.

Answer: C

Diff: 1 Type: MC

Topic: Market Equilibrium

7) Refer to Table 3.4.1. If the price is \$7, then the surplus is

- A) 360 units.
- B) 400 units.
- C) 160 units.
- D) zero units.
- E) 290 units.

Answer: A

Diff: 1 Type: MC

Topic: Market Equilibrium

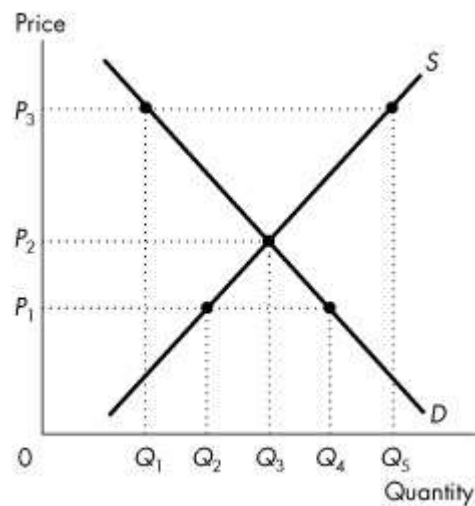
- 8) Refer to Table 3.4.1. If the price is \$3, then the shortage is
- A) zero units.
  - B) 1,050 units.
  - C) 180 units.
  - D) 600 units.
  - E) 160 units.

Answer: C

Diff: 1 Type: MC

Topic: Market Equilibrium

Use the figure below to answer the following questions.



**Figure 3.4.1**

- 9) At price  $P_3$  in Figure 3.4.1,
- A) this market is in equilibrium.
  - B) there is a shortage in the amount of  $Q_5 - Q_1$ .
  - C) there is a tendency for the price to rise.
  - D) equilibrium quantity is  $Q_5$ .
  - E) there is a surplus in the amount of  $Q_5 - Q_1$ .

Answer: E

Diff: 3 Type: MC

Topic: Market Equilibrium

10) At price  $P_2$  in Figure 3.4.1, which one of the following is *not* true?

- A) This market is in equilibrium.
- B) The quantity demanded is equal to the quantity supplied.
- C) The quantity demanded is  $Q_1$ .
- D) There is no surplus.
- E) The quantity supplied is  $Q_3$ .

Answer: C

Diff: 1 Type: MC

Topic: Market Equilibrium

11) At price  $P_1$  in Figure 3.4.1

- A) there is a surplus in the amount of  $Q_4 - Q_2$ .
- B) there is a shortage in the amount of  $Q_4 - Q_2$ .
- C) there is a tendency for the price to fall.
- D) the equilibrium quantity is  $Q_2$ .
- E) the equilibrium quantity is  $Q_4$ .

Answer: B

Diff: 2 Type: MC

Topic: Market Equilibrium

12) At price  $P_1$  in Figure 3.4.1,

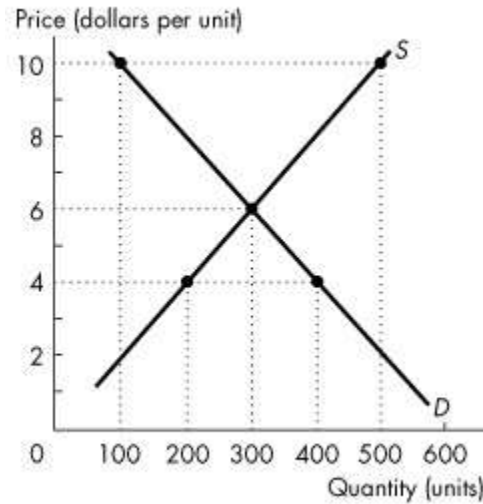
- A) producers can sell all they plan to sell.
- B) consumers can buy all they want.
- C) producers are unwilling to sell any goods.
- D) a surplus exists.
- E) both sides of the market are able to carry out their desired transactions.

Answer: A

Diff: 2 Type: MC

Topic: Market Equilibrium

Use the figure below to answer the following questions.



**Figure 3.4.2**

13) The equilibrium price in the market illustrated by Figure 3.4.2 is

- A) \$2 a unit.
- B) \$4 a unit.
- C) \$6 a unit.
- D) \$8 a unit.
- E) \$10 a unit.

Answer: C

Diff: 1 Type: MC

Topic: Market Equilibrium

14) Refer to Figure 3.4.2. When the price is \$10 a unit

- A) consumers will buy only 100 units of output.
- B) consumers will buy 500 units of output.
- C) consumers will buy nothing.
- D) a shortage occurs.
- E) the surplus is zero.

Answer: A

Diff: 1 Type: MC

Topic: Market Equilibrium

15) At a price of \$10 a unit in Figure 3.4.2

- A) there is a surplus of 200 units.
- B) there is a shortage of 200 units.
- C) there is a surplus of 400 units.
- D) there is a shortage of 400 units.
- E) quantity will rise.

Answer: C

Diff: 1 Type: MC

Topic: Market Equilibrium

16) At a price of \$4 a unit in Figure 3.4.2

- A) the equilibrium quantity is 400 units.
- B) there is a surplus of 200 units.
- C) the quantity supplied is 400 units.
- D) there is a shortage of 200 units.
- E) the quantity demanded is 200 units.

Answer: D

Diff: 1 Type: MC

Topic: Market Equilibrium

17) Which one of the following correctly describes how price adjustment eliminates a surplus?

- A) As the price rises, the quantity demanded decreases and the quantity supplied increases.
- B) As the price rises, the quantity demanded increases and the quantity supplied decreases.
- C) As the price falls, the quantity demanded decreases and the quantity supplied increases.
- D) As the price falls, the quantity demanded increases and the quantity supplied decreases.
- E) As the price falls, the demand for substitutes decreases, which eliminates the surplus.

Answer: D

Diff: 2 Type: MC

Topic: Market Equilibrium

18) Which one of the following correctly describes how price adjustment eliminates a shortage?

- A) As the price rises, the quantity demanded decreases and the quantity supplied increases.
- B) As the price rises, the quantity demanded increases and the quantity supplied decreases.
- C) As the price falls, the quantity demanded decreases and the quantity supplied increases.
- D) As the price falls, the quantity demanded increases and the quantity supplied decreases.
- E) As the price falls, the quantity demanded increases and the quantity supplied increases.

Answer: A

Diff: 2 Type: MC

Topic: Market Equilibrium

19) If the price is above the equilibrium price, then

- A) none of the good will be sold.
- B) the price must rise further to reach the new market equilibrium.
- C) a surplus exists.
- D) a shortage exists.
- E) price will not change; producers will cut back production until the market is in equilibrium.

Answer: C

Diff: 1 Type: MC

Topic: Market Equilibrium

20) A shortage will exist if

- A) the price is above the equilibrium price.
- B) the price is below the equilibrium price.
- C) there are not enough producers.
- D) there are not enough consumers.
- E) demand decreases.

Answer: B

Diff: 1 Type: MC

Topic: Market Equilibrium

21) The price of a good will tend to fall if

- A) there is a surplus at the current price.
- B) the current price is below the equilibrium price.
- C) the quantity supplied exceeds the quantity demanded at the current price.
- D) both A and C are true.
- E) none of the above are true.

Answer: D

Diff: 2 Type: MC

Topic: Market Equilibrium

22) If the market for Twinkies is in equilibrium, then

- A) Twinkies must be a normal good.
- B) producers would like to sell more at the current price.
- C) consumers would like to buy more at the current price.
- D) there is a surplus.
- E) the equilibrium quantity equals the quantity demanded.

Answer: E

Diff: 1 Type: MC

Topic: Market Equilibrium

Source: Study Guide

23) A shortage is the amount by which quantity

- A) demanded exceeds quantity supplied.
- B) supplied exceeds quantity demanded.
- C) demanded increases when the price rises.
- D) demanded exceeds the equilibrium quantity.
- E) supplied exceeds the equilibrium quantity.

Answer: A

Diff: 1 Type: MC

Topic: Market Equilibrium

Source: Study Guide

24) Complete the following sentence. A surplus

- A) exists if the price is above the equilibrium price.
- B) is the amount by which the quantity demanded exceeds the quantity supplied.
- C) is the amount by which the quantity demanded exceeds the equilibrium quantity.
- D) is the amount by which the quantity supplied exceeds the equilibrium quantity.
- E) will lead to rising prices.

Answer: A

Diff: 2 Type: MC

Topic: Market Equilibrium

25) When a shortage occurs, there is a tendency for the

- A) price to fall.
- B) price to remain unchanged.
- C) price to rise.
- D) quantity demanded to increase.
- E) quantity supplied to decrease.

Answer: C

Diff: 1 Type: MC

Topic: Market Equilibrium

Refer to the table below for the following question.

**Table 3.4.2**

Price (dollars per bottle)	Quantity demanded (bottles per week)	Quantity supplied (bottles per week)
2	180	60
6	140	100
10	100	140
14	60	180
18	20	220

26) Refer to Table 3.4.2. The table shows the demand and supply schedules for shampoo. If the price is \$6 a bottle, there is a \_\_\_\_\_ of shampoo. So the price of a bottle of shampoo \_\_\_\_\_, the quantity demanded \_\_\_\_\_ and the quantity supplied \_\_\_\_\_. The market moves to equilibrium.

- A) shortage; rises; decreases; increases
- B) shortage; falls; decreases; increases
- C) surplus; rises; increases; decreases
- D) surplus; falls; increases; decreases
- E) shortage; rises; increases; decreases

Answer: A

Diff: 1 Type: MC

Topic: Market Equilibrium

Source: MyEconLab

27) If the quantity of textbooks supplied is 10,000 per year and the quantity of textbooks demanded is 8,000 per year, there is a \_\_\_\_\_ in the market and the price will \_\_\_\_\_.

- A) shortage; rise
- B) shortage; fall
- C) surplus; rise
- D) surplus; fall
- E) surplus; either rise or fall depending on whether supply increases to meet the surplus

Answer: D

Type: MC

28) If the market for Twinkies is in equilibrium, then

- A) Twinkies must be a normal good.
- B) producers would like to sell more at the current price.
- C) consumers would like to buy more at the current price.
- D) the quantity supplied equals the quantity demanded.
- E) the supply of Twinkies will never increase and the demand for Twinkies will never decrease.

Answer: D

Type: MC

### 3.5 Predicting Changes in Price and Quantity

1) Since 1980, there has been a dramatic increase in the number of working mothers. Based on this information alone, we can predict that the market for child care services has experienced

- A) an increase in demand.
- B) a decrease in demand.
- C) an increase in quantity demanded.
- D) a decrease in quantity supplied.
- E) an increase in supply.

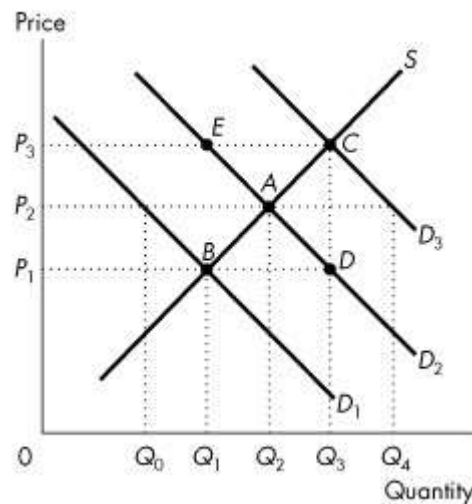
Answer: A

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

Source: Study Guide

Use the figure below to answer the following questions.



**Figure 3.5.1**

2) If the demand curve is  $D_2$  in Figure 3.5.1,

- A) the equilibrium price is  $P_2$  and the equilibrium quantity is  $Q_2$ .
- B) the equilibrium price is  $P_2$  and the equilibrium quantity is  $Q_0$ .
- C) there is a shortage in the amount of  $Q_2 - Q_0$ .
- D) a rise in price will shift the demand curve to  $D_3$ .
- E) price will rise.

Answer: A

Diff: 1 Type: MC

Topic: Predicting Changes in Price and Quantity

3) Initially, the demand curve for good  $A$  is  $D_2$  in Figure 3.5.1. Suppose good  $B$  is a substitute for good  $A$ . If the price of  $B$  falls

- A) the price of  $A$  will rise.
- B) there will be a surplus of good  $A$  at  $P_2$ .
- C) the demand curve for good  $A$  will shift from  $D_2$  to  $D_3$ .
- D) the equilibrium quantity of good  $A$  will increase.
- E) all of the above are true *except* B.

Answer: B

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

4) Initially, the demand curve for good  $A$  is  $D_2$  in Figure 3.5.1. If income increases and  $A$  is a normal good, we would expect to see a movement from point  $A$  to point

- A)  $B$ .
- B)  $C$ .
- C)  $D$ .
- D)  $E$ .
- E)  $C$  and back to point  $A$ .

Answer: B

Diff: 1 Type: MC

Topic: Predicting Changes in Price and Quantity

5) The price of a good will rise if

- A) demand for the good decreases.
- B) supply of the good decreases.
- C) there is a surplus of the good.
- D) the price of a substitute for the good decreases.
- E) the good is an inferior good and income increases.

Answer: B

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

6) The price of a good will fall if

- A) there is a shortage of the good.
- B) if demand for the good increases.
- C) there is a surplus of the good.
- D) if the supply of the good decreases.
- E) if demand for the good does not change.

Answer: C

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

- 7) The price of a good will fall if
- A) demand for the good increases.
  - B) supply of the good decreases.
  - C) supply of the good increases.
  - D) demand for the good remains constant.
  - E) supply of the good remains constant.

Answer: C

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

8) Suppose we observe a rise in the price of good A and an increase in the quantity of good A bought and sold. Which one of the following is a likely explanation?

- A) The law of demand is violated.
- B) The demand for A decreased.
- C) The demand for A increased.
- D) The supply of A increased.
- E) The supply of A decreased.

Answer: C

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

9) Suppose we observe a rise in the price of good A and a decrease in the quantity of good A bought and sold. Which one of the following is a likely explanation?

- A) The law of supply is violated.
- B) The demand for A decreased.
- C) The demand for A increased.
- D) The supply of A increased.
- E) The supply of A decreased.

Answer: E

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

10) Suppose we observe a fall in the price of good A and an increase in the quantity of good A bought and sold. Which one of the following is a likely explanation?

- A) The law of supply is violated.
- B) The demand for A decreased.
- C) The demand for A increased.
- D) The supply of A increased.
- E) The supply of A decreased.

Answer: D

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

11) Suppose we observe a fall in the price of good *A* and a decrease in the quantity of good *A* bought and sold. Which one of the following is a likely explanation?

- A) The law of demand is violated.
- B) The demand for *A* decreased.
- C) The demand for *A* increased.
- D) The supply of *A* increased.
- E) The supply of *A* decreased.

Answer: B

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

12) When the demand for good *A* increases,

- A) the equilibrium price and equilibrium quantity will increase.
- B) the equilibrium price will rise but the equilibrium quantity will decrease.
- C) the equilibrium price and equilibrium quantity will decrease.
- D) the equilibrium price will decrease but the equilibrium quantity will increase.
- E) a surplus will result.

Answer: A

Diff: 1 Type: MC

Topic: Predicting Changes in Price and Quantity

13) When the supply of good *A* decreases,

- A) the equilibrium price and the equilibrium quantity will increase.
- B) the equilibrium price will increase but the equilibrium quantity will decrease.
- C) the equilibrium price and the equilibrium quantity will decrease.
- D) the equilibrium price will decrease but the equilibrium quantity will increase.
- E) a surplus will result.

Answer: B

Diff: 1 Type: MC

Topic: Predicting Changes in Price and Quantity

14) If *A* is an inferior good and consumer income rises, the demand for *A*

- A) increases and the equilibrium price and the equilibrium quantity increase.
- B) increases and the equilibrium price rises but the equilibrium quantity decreases.
- C) decreases and the equilibrium price and the equilibrium quantity decrease.
- D) decreases and the equilibrium price falls but the equilibrium quantity increases.
- E) decreases and the equilibrium price rises; as a result, the equilibrium quantity decreases.

Answer: C

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

- 15) If  $A$  and  $B$  are substitutes and the price of  $A$  rises, we will observe
- A) an increase in the equilibrium price and the equilibrium quantity of  $B$ .
  - B) a decrease in the equilibrium price and the equilibrium quantity of  $B$ .
  - C) an increase in the equilibrium price but a decrease in the equilibrium quantity of  $B$ .
  - D) a decrease in equilibrium price but an increase in the equilibrium quantity of  $B$ .
  - E) none of the above.

Answer: A

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

- 16) If  $A$  and  $B$  are substitutes and the cost of a factor of production used in the production of  $A$  increases, then the price of
- A)  $B$  falls but the price of  $A$  rises.
  - B)  $B$  rises but the price of  $A$  falls.
  - C)  $A$  falls, and the price of  $B$  will stay unchanged.
  - D)  $A$  and  $B$  fall.
  - E)  $A$  and  $B$  rise.

Answer: E

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

- 17) If  $A$  and  $B$  are substitutes in production and the price of  $A$  falls, the supply of  $B$
- A) increases and the price of  $B$  rises.
  - B) increases and the price of  $B$  falls.
  - C) decreases and the price of  $B$  falls.
  - D) decreases and the price of  $B$  rises.
  - E) does not change.

Answer: B

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

- 18) If  $A$  and  $B$  are complements in production and the price of  $A$  falls, the supply of  $B$
- A) increases and the price of  $B$  rises.
  - B) increases and the price of  $B$  falls.
  - C) decreases and the price of  $B$  falls.
  - D) decreases and the price of  $B$  rises.
  - E) does not change.

Answer: D

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

19) Crude oil is a very important factor of production used in the production of gasoline. If the price of crude oil rises, we would expect the

- A) price of gasoline to rise due to an increase in demand.
- B) price of gasoline to fall due to an increase in demand.
- C) price of gasoline to rise due to a decrease in supply.
- D) equilibrium quantity of gasoline to fall due to an increase in supply.
- E) equilibrium quantity of gasoline to rise due to an increase in demand.

Answer: C

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

20) If demand increases and supply decreases, then the

- A) equilibrium quantity increases but the effect on the equilibrium price is unknown.
- B) equilibrium quantity decreases but the effect on the equilibrium price is unknown.
- C) equilibrium price falls but the effect on the equilibrium quantity is unknown.
- D) equilibrium price rises but the effect on the equilibrium quantity is unknown.
- E) effect on both equilibrium price and quantity is unknown.

Answer: D

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

21) If demand decreases and supply increases, then the

- A) equilibrium quantity increases but the effect on the equilibrium price is unknown.
- B) equilibrium quantity decreases but the effect on the equilibrium price is unknown.
- C) equilibrium price falls but the effect on equilibrium quantity is unknown.
- D) equilibrium price rises but the effect on equilibrium quantity is unknown.
- E) effect on both equilibrium price and quantity is unknown.

Answer: C

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

22) If we observe a rise in the equilibrium price of good A, we know that either the demand for A has

- A) increased or the supply of A has decreased or both.
- B) increased or the supply of A has increased or both.
- C) decreased or the supply of A has increased or both.
- D) decreased or the supply of A has decreased or both.
- E) none of the above.

Answer: A

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

23) If we observe a fall in the equilibrium price of good A, we know that either the demand for A has

- A) increased or the supply of A has decreased or both.
- B) increased or the supply of A has increased or both.
- C) decreased or the supply of A has increased or both.
- D) decreased or the supply of A has decreased or both.
- E) none of the above.

Answer: C

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

24) If we observe an increase in the equilibrium quantity of good A, we know that

- A) either the demand for A has increased or the supply of A has decreased or both.
- B) either the demand for A has increased or the supply of A has increased or both.
- C) either the demand for A has decreased or the supply of A has increased or both.
- D) either the demand for A has decreased or the supply of A has decreased or both.
- E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

25) If we observe a decrease in the equilibrium quantity of good A, we know that

- A) either the demand for A has increased or the supply of A has decreased or both.
- B) either the demand for A has increased or the supply of A has increased or both.
- C) either the demand for A has decreased or the supply of A has increased or both.
- D) either the demand for A has decreased or the supply of A has decreased or both.
- E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

26) Which of the following will definitely result in an increase in the equilibrium price?

- A) an increase in both demand and supply
- B) a decrease in both demand and supply
- C) an increase in demand combined with a decrease in supply
- D) a decrease in demand combined with an increase in supply
- E) an increase in supply combined with a decrease in demand

Answer: C

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

Source: Study Guide

27) Which one of the following will definitely lower the equilibrium price?

- A) an increase in both demand and supply
- B) a decrease in both demand and supply
- C) an increase in demand combined with a decrease in supply
- D) a decrease in demand combined with an increase in supply
- E) a decrease in supply combined with an increase in demand

Answer: D

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

28) Which one of the following will definitely decrease the equilibrium quantity?

- A) an increase in both demand and supply
- B) a decrease in both demand and supply
- C) an increase in demand combined with a decrease in supply
- D) a decrease in demand combined with an increase in supply
- E) none of the above

Answer: B

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

29) A technological improvement in the production of good A

- A) decreases the supply of A.
- B) increases the demand for A.
- C) decreases the equilibrium price of A and decreases the equilibrium quantity.
- D) decreases the quantity demanded of A.
- E) increases the supply of A.

Answer: E

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

30) Which of the following events leads to a rise in the price of oranges?

- A) a rise in the price of apples if apples and oranges are substitutes
- B) a scientific discovery that oranges cause hair loss
- C) a decrease in income if oranges are a normal good
- D) good growing weather in Florida
- E) a technological improvement in the production of oranges

Answer: A

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

31) If *A* and *B* are complements and the cost of a factor of production used in the production of *A* decreases, then the price of

- A) both *A* and *B* will rise.
- B) both *A* and *B* will fall.
- C) *A* will fall and the price of *B* will rise.
- D) *A* will rise and the price of *B* will fall.
- E) *A* will fall and the price of *B* will remain unchanged.

Answer: C

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

Source: Study Guide

32) If both demand and supply increase, then the equilibrium price

- A) and equilibrium quantity increases.
- B) falls but the equilibrium quantity increases.
- C) could either rise or fall, but the equilibrium quantity increases.
- D) rises and the equilibrium quantity could either increase or decrease.
- E) falls and the equilibrium quantity could either increase or decrease.

Answer: C

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

33) There have been severe problems in the Atlantic fishing industry, with large falls in the fish stocks. As a result,

- A) the price of fish will fall.
- B) the quantity of fish sold will increase as fishermen will catch more to make up for the shortage.
- C) the equilibrium price and the equilibrium quantity will fall or rise depending on how large the fall in fish stocks.
- D) both the equilibrium price and the equilibrium quantity will rise, as consumers will desire even more fish, because they are scarce.
- E) the fall in the fish stocks will lead to a shortage, and a rise in the equilibrium price and a decrease in the equilibrium quantity.

Answer: E

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

34) There have been severe falls in the fish stocks in the Atlantic fishing industry. As a result, we would expect

- A) an increase in the demand for meat (e.g., beef), because meat is a complement of fish.
- B) a fall in the price of fish, leading to a decrease in the demand for meat, because meat and fish are substitutes.
- C) a fall in the price of fish, leading to an increase in the demand for meat, because meat and fish are substitutes.
- D) an increase in the demand for meat, because meat is a substitute for fish.
- E) a rise in the price of fish, leading to a decrease in the demand for meat, because meat and fish are complements.

Answer: D

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

35) If Canadians suddenly develop a strong urge to escape the cold winter by taking vacations in Hawaii, the

- A) price of a vacation in Hawaii rises and the quantity demanded of Hawaiian vacations decreases.
- B) price of a skiing vacation in the mountains rises.
- C) initial result of the change is a surplus of vacations in Hawaii, leading to a price rise.
- D) price of airline tickets falls as ticket agents make deals in response to this change.
- E) price of luggage will rise, because luggage and vacations are complements.

Answer: E

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

36) The Genius Software Company has developed an amazing new software package to be used only with Einstein Computers. As a result, the equilibrium price of

- A) all computers rises.
- B) rival software packages falls leading to an overall increase in the equilibrium quantity of these packages.
- C) all software packages rises.
- D) Einstein computers rises, accompanied by an increase in the equilibrium quantity.
- E) Einstein computers rises, leading to a decrease in the equilibrium quantity.

Answer: D

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

Use the information below to answer the following questions.

**Fact 3.5.1**

The market for coffee is initially in equilibrium. Pepsi is a substitute for coffee; cream is a complement of coffee. Consider the market for coffee. Assume that all *ceteris paribus* assumptions continue to hold *except* for the event listed.

37) Refer to Fact 3.5.1. If coffee is a normal good, then a decrease in income will

- A) increase the price and the quantity demanded of coffee.
- B) increase the price and the quantity supplied of coffee.
- C) decrease the price and the quantity demanded of coffee.
- D) decrease the price and the quantity supplied of coffee.
- E) cause none of the above.

Answer: D

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

Source: Study Guide

38) Refer to Fact 3.5.1. An increase in the price of Pepsi, a substitute for coffee will

- A) increase the price and the quantity demanded of coffee.
- B) increase the price and the quantity supplied of coffee.
- C) decrease the price and the quantity demanded of coffee.
- D) decrease the price and the quantity supplied of coffee.
- E) cause none of the above.

Answer: B

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

Source: Study Guide

39) Refer to Fact 3.5.1. A technological improvement lowers the cost of producing coffee. At the same time, preferences for coffee decrease. The equilibrium quantity of coffee

- A) increases.
- B) decreases.
- C) remains the same.
- D) increases or decreases depending on whether the price of coffee falls or rises.
- E) increases, decreases, or remains the same depending on the relative shifts of the demand and supply curves.

Answer: E

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

Source: Study Guide

40) Refer to Fact 3.5.1. If there is an increase in the wages of farm workers who harvest coffee beans, the equilibrium quantity of coffee

- A) increases.
- B) decreases.
- C) remains the same.
- D) increases or decreases depending on the slope of the supply and demand curves.
- E) increases or decreases depending on the relative shifts of the supply and demand curves.

Answer: B

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

41) Refer to Fact 3.5.1. The price of cream falls. Simultaneously, there is an increase in the wages of farm workers who harvest coffee beans. The equilibrium quantity of coffee

- A) increases.
- B) decreases.
- C) remains the same.
- D) increases or decreases depending on the slope of the supply and demand curves.
- E) increases, decreases, or remains the same depending on the relative shifts of the supply and demand curves.

Answer: E

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

42) Refer to Fact 3.5.1. A new study comes out, revealing that drinking Pepsi increases your ability to study. The equilibrium quantity of coffee

- A) increases.
- B) decreases.
- C) remains the same.
- D) increases or decreases depending on the slope of the supply and demand curves.
- E) increases or decreases depending on the relative shifts of the supply and demand curves.

Answer: B

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

43) Farm land can be used to produce either cattle or corn. If the demand for cattle increases, then the

- A) demand for corn increases.
- B) supply of corn increases.
- C) demand for corn decreases.
- D) supply of corn decreases.
- E) both B and C.

Answer: D

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

44) When the price of good *A* rises, the supply curve of good *B* shifts rightward. Which of the following statements are true?

- A) *A* and *B* are substitutes.
- B) *A* and *B* are complements.
- C) *A* and *B* are substitutes in production.
- D) *A* and *B* are complements in production.
- E) *A* is a factor used in the production of *B*.

Answer: D

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

45) "As domestic car prices have increased, consumers have found foreign cars to be a better bargain. Consequently, domestic car sales have fallen and foreign car sales have risen." Based on this information alone, there has been a

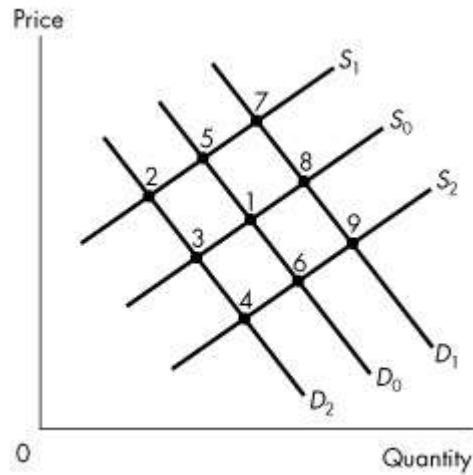
- A) shift in the demand curves for both domestic and foreign cars.
- B) shift in the supply curves for both domestic and foreign cars.
- C) movement along the demand curves for both domestic and foreign cars.
- D) movement along the demand curve for domestic cars and a shift of the demand curve for foreign cars.
- E) shift of the demand curve for domestic cars and a movement along the demand curve for foreign cars.

Answer: D

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

Use the figure below to answer the following questions.



**Figure 3.5.2**

Original equilibrium at 1.

46) Refer to Figure 3.5.2, which represents the market for beans. If the price of peas, a substitute for beans rises, what is the new *beans* equilibrium, *ceteris paribus*?

- A) 8
- B) 3
- C) 9
- D) 5
- E) 6

Answer: A

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

47) Refer to Figure 3.5.2, which represents the market for beer. If the price of pizza, a complement of beer rises, what is the new *beer* equilibrium, *ceteris paribus*?

- A) 8
- B) 3
- C) 9
- D) 5
- E) 6

Answer: B

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

48) Refer to Figure 3.5.2, which represents the market for beans. If the price of peas, a substitute for beans in production, rises, what is the new *beans* equilibrium, *ceteris paribus*?

- A) 8
- B) 3
- C) 9
- D) 5
- E) 6

Answer: D

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

49) Refer to Figure 3.5.2, which represents the market for cow manure. If the price of milk, a complement in production of manure, rises, what is the new manure equilibrium, *ceteris paribus*?

- A) 8
- B) 3
- C) 9
- D) 5
- E) 6

Answer: E

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

50) Refer to Figure 3.5.2, which represents the market for beans. If the price of peas, a substitute for beans *and* a substitute in production, rises, what is the new *beans* equilibrium, *ceteris paribus*?

- A) 2
- B) 3
- C) 9
- D) 4
- E) 7

Answer: E

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

51) Refer to Figure 3.5.2, which represents the market for beans. If the price of peas, a substitute for beans, rises, *and* the cost of producing beans decreases, what is the new *beans* equilibrium, *ceteris paribus*?

- A) 2
- B) 3
- C) 9
- D) 4
- E) 7

Answer: C

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

52) Refer to Figure 3.5.2, which represents the market for tacos. A new scientific study reveals that tacos cause bad breath. Simultaneously, the cost of producing tacos decreases. What is the new equilibrium, *ceteris paribus*?

- A) 2
- B) 3
- C) 9
- D) 4
- E) 7

Answer: D

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

53) Refer to Figure 3.5.2, which represents the market for tacos. A new scientific study reveals that tacos cause bad breath. Simultaneously, the cost of producing tacos increases. What is the new equilibrium, *ceteris paribus*?

- A) 2
- B) 3
- C) 9
- D) 4
- E) 7

Answer: A

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

Use the table below to answer the following questions.

**Table 3.5.1**  
The Market for Car-Seat Heaters

Price (dollars per heater)	Quantity Demanded (heaters per month)	Quantity Supplied (heaters per month)
40	500	300
50	450	350
60	400	400
70	350	450
80	300	500
90	250	550
100	200	600

54) Refer to Table 3.5.1. The equilibrium price is \$\_\_\_\_\_ and the equilibrium quantity is \_\_\_\_\_ heaters per month.

- A) 80; 500
- B) 80; 300
- C) 50; 450
- D) 50; 350
- E) 60; 400

Answer: E

Diff: 1 Type: MC

Topic: Predicting Changes in Price and Quantity

55) Refer to Table 3.5.1. If the price is set at \$80, there will be a

- A) shortage of 200 units and price will rise.
- B) shortage of 200 units and demand will fall.
- C) surplus of 200 units and demand will rise.
- D) surplus of 200 units and supply will fall.
- E) surplus of 200 units and price will fall.

Answer: E

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

56) Refer to Table 3.5.1. Suppose the cost of production rises, causing supply to decrease by 100 units at each price. The new equilibrium price is \$\_\_\_\_\_ and equilibrium quantity is \_\_\_\_\_ units.

- A) 70; 450
- B) 70; 350
- C) 50; 450
- D) 50; 350
- E) 60; 400

Answer: B

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

57) Refer to Table 3.5.1. Suppose a problem develops with car-seat heaters - they malfunction and occasionally cause serious burns. As a result, demand decreases by 100 heaters at each price. The new equilibrium price is \$\_\_\_\_\_ and the new equilibrium quantity is \_\_\_\_\_ heaters per month.

- A) 70; 450
- B) 70; 350
- C) 50; 450
- D) 50; 350
- E) 60; 400

Answer: D

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

58) Refer to Table 3.5.1. Suppose a problem develops with car-seat heaters - they malfunction and occasionally cause serious burns. As a result, demand decreases by 100 heaters at each price. Simultaneously, the cost of production rises, and supply decreases by 100 heaters at each price. The new equilibrium price is \$\_\_\_\_\_ and the new equilibrium quantity is \_\_\_\_\_ heaters per month.

- A) 70; 450
- B) 70; 350
- C) 50; 450
- D) 50; 350
- E) 60; 300

Answer: E

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

Use the figure below to answer the following questions.

**Table 3.5.2**  
Demand and Supply Schedules for Cups of Coffee each day at CoolU

Price (dollars per cup)	Quantity Demanded (cups of coffee per day)	Quantity Supplied (cups of coffee per day)
0.70	1,200	0
0.80	1,100	200
0.90	1,000	400
1.00	900	600
1.10	800	800
1.20	700	1,000
1.30	600	1,200
1.40	500	1,400
1.50	400	1,600

59) Refer to Table 3.5.2. The equilibrium price is \$\_\_\_\_\_ and the equilibrium quantity is \_\_\_\_\_ cups a day.

- A) 1.30; 1200
- B) 0.90; 1000
- C) 1.10; 900
- D) 1.10; 800
- E) 1.00; 800

Answer: D

Diff: 1 Type: MC

Topic: Predicting Changes in Price and Quantity

60) Refer to Table 3.5.2. If the price is set at \$0.80 per cup, there is a \_\_\_\_\_ leading to a price \_\_\_\_\_.

- A) shortage; rise
- B) shortage; fall
- C) surplus; rise
- D) surplus; fall
- E) equilibrium; rise

Answer: A

Diff: 1 Type: MC

Topic: Predicting Changes in Price and Quantity

61) Refer to Table 3.5.2. If the price is set at \$1.30 per cup, there is a \_\_\_\_\_ leading to a price \_\_\_\_\_.

- A) shortage; rise
- B) shortage; fall
- C) surplus; rise
- D) surplus; fall
- E) equilibrium; rise

Answer: D

Diff: 1 Type: MC

Topic: Predicting Changes in Price and Quantity

62) Refer to Table 3.5.2. A premature frost destroys half the coffee trees. This change would be represented as a

- A) leftward shift of the demand curve.
- B) rightward shift of the demand curve.
- C) leftward shift of the supply curve.
- D) rightward shift of the supply curve.
- E) movement down along the supply curve.

Answer: C

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

63) Refer to Table 3.5.2. A premature frost destroys half the coffee trees and the supply of coffee is cut in half. The new equilibrium price is \$\_\_\_\_\_ and the new equilibrium quantity is \_\_\_\_\_ cups a day.

- A) 1.30; 600
- B) 1.50; 400
- C) 0.90; 400
- D) 1.20; 700
- E) 1.30; 500

Answer: A

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

64) Refer to Table 3.5.2. Professor Hyper publishes a new study, showing that coffee raises the test performance of students. Students double their demand for coffee. This change would be represented as a

- A) leftward shift of the demand curve.
- B) rightward shift of the demand curve.
- C) leftward shift of the supply curve.
- D) rightward shift of the supply curve.
- E) movement up along the demand curve.

Answer: B

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

65) Refer to Table 3.5.2. Professor Hyper publishes a new study, showing that coffee raises the test performance of students. Students double their demand for coffee and the quantity of coffee demanded at each price doubles. The new equilibrium price is \$\_\_\_\_\_, and the new equilibrium quantity is \_\_\_\_\_ cups a day.

- A) 1.20; 1,000
- B) 1.30; 1,200
- C) 1.50; 1,600
- D) 1.40; 1,400
- E) none of the above

Answer: B

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

66) Refer to Table 3.5.2. Professor Hyper publishes a new study, showing that coffee raises the test performance of students. Students double their demand for coffee and the quantity of coffee demanded at each price doubles. In addition, a premature frost destroys half the coffee trees and the supply of coffee is cut in half. The new equilibrium price is \$\_\_\_\_\_ and the new equilibrium quantity is \_\_\_\_\_ cups a day.

- A) 1.10; 400
- B) 1.10; 1,600
- C) 1.10; 800
- D) 1.50; 800
- E) 1.50; 400.

Answer: D

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

Use the table below to answer the following questions.

**Table 3.5.3**  
Demand and supply schedules for designer sport t-shirts at CoolU

Price (dollars per t-shirt)	Quantity Supplied (t-shirts per month)	Quantity Demanded (t-shirts per month)
3	150	300
4	160	280
5	170	260
6	180	240
7	190	220
8	200	200
9	210	180
10	220	160
11	230	140
12	240	120

67) Refer to Table 3.5.3. The equilibrium price is \$\_\_\_\_\_ and the equilibrium quantity is \_\_\_\_\_ t-shirts per month.

- A) 6; 200
- B) 7; 220
- C) 8; 180
- D) 8; 220
- E) 8; 200

Answer: E

Diff: 1 Type: MC

Topic: Predicting Changes in Price and Quantity

68) Refer to Table 3.5.3. Suppose that the price of a designer sport t-shirt is \$6. The market has \_\_\_\_\_ leading to \_\_\_\_\_.

- A) an equilibrium; no change in the price
- B) a shortage; a fall in the price
- C) a shortage; a rise in the price
- D) a surplus; a fall in the price
- E) a surplus; a rise in the price

Answer: C

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

69) Refer to Table 3.5.3. Suppose that the price of a designer sport t-shirt is \$10. The market has \_\_\_\_\_ leading to \_\_\_\_\_.

- A) an equilibrium; no change in the price
- B) a shortage; a fall in the price
- C) a shortage; a rise in the price
- D) a surplus; a fall in the price
- E) a surplus; a rise in the price

Answer: D

Diff: 1 Type: MC

Topic: Predicting Changes in Price and Quantity

70) Refer to Table 3.5.3. In a television interview, Joe Cool shows off his designer sport t-shirt, setting off a new craze that doubles business at the sportswear establishments. This would be represented as a

- A) movement up along the demand curve.
- B) rightward shift of the demand curve.
- C) leftward shift of the demand curve.
- D) rightward shift of the supply curve.
- E) leftward shift of the supply curve.

Answer: B

Diff: 1 Type: MC

Topic: Predicting Changes in Price and Quantity

71) Refer to Table 3.5.3. In a television interview, Joe Cool shows off his designer sport t-shirt, setting off a new craze that doubles business at the sportswear establishments. The quantity of t-shirts demanded doubles at each price. The new equilibrium price is \$\_\_\_\_\_ and the new equilibrium quantity is \_\_\_\_\_ t-shirts per month.

- A) 12; 240
- B) 8; 400
- C) 16; 400
- D) 12; 120
- E) 16; 200

Answer: A

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

72) Refer to Table 3.5.3. A new store opens up on the edge of campus, Great Wild North Sportswear, which has the capacity to do as much business as all the existing businesses. The quantity of t-shirts supplied doubles at each price. This would be represented as a

- A) movement up along the demand curve.
- B) rightward shift of the demand curve.
- C) leftward shift of the demand curve.
- D) rightward shift of the supply curve.
- E) leftward shift of the supply curve.

Answer: D

Diff: 2 Type: MC

Topic: Predicting Changes in Price and Quantity

73) Refer to Table 3.5.3. A new store opens up on the edge of campus, Great Wild North Sportswear, which has the capacity to do as much business as all the existing businesses. The quantity of t-shirts supplied doubles at each price. The new equilibrium price is \$\_\_\_\_\_ and the new equilibrium quantity is \_\_\_\_\_ t-shirts per month.

- A) 8; 400
- B) 3; 300
- C) 0; 400
- D) 16; 200
- E) 4; 400

Answer: B

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

74) Refer to Table 3.5.3. A new store opens up on the edge of campus, Great Wild North Sportswear, which has the capacity to do as much business as all the existing businesses. The quantity of t-shirts supplied doubles at each price. In addition, in a television interview, Joe Cool shows off his designer sport t-shirt, setting off a new craze that doubles business at the local sportswear establishments. The quantity of t-shirts demanded doubles at each price. The new equilibrium price is \$\_\_\_\_\_ and the new equilibrium quantity is \_\_\_\_\_ t-shirts per month.

- A) 8; 400
- B) 8; 200
- C) 3; 400
- D) 12; 240
- E) 16; 400

Answer: A

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

Use the table below to answer the following questions.

**Table 3.5.4**  
Quantities demanded and supplied in equilibrium  
before and after a drought strikes potato farms

	<u>Potatoes</u>		<u>Hamburgers</u>		<u>Rice</u>	
	<u>before</u>	<u>after</u>	<u>before</u>	<u>after</u>	<u>before</u>	<u>after</u>
Region 1	100	30	50	20	3	50
Region 2	10	5	4	50	50	60

75) Refer to Table 3.5.4. In Region 1, potatoes and hamburgers are

- A) substitutes.
- B) complements.
- C) normal goods.
- D) unrelated goods.
- E) inferior goods.

Answer: B

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

76) In Table 3.5.4 potatoes and rice are

- A) substitutes in Region 1 and complements in Region 2.
- B) substitutes in Region 2 and complements in Region 1.
- C) complements in both regions.
- D) substitutes in both regions.
- E) unrelated goods in both regions.

Answer: D

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

77) "As fewer people buy computers, the demand for Internet service will decrease and the price of Internet service will increase. The rise in the price of Internet service will increase the supply of Internet service." This statement is \_\_\_\_\_ because \_\_\_\_\_.

- A) false; the decrease in the demand for Internet service creates a surplus and to eliminate the surplus, supply increases
- B) true; when the demand for Internet service increases, the supply of Internet service increases so that the price of Internet service does not increase
- C) true, when the demand for Internet service increases, the supply of Internet service increases too so that no surplus occurs
- D) true; the increase in the price of Internet service increases the supply of Internet service to eliminate the shortage
- E) false; a decrease in demand for Internet service does not increase the price of Internet service and an increase in the price of Internet service does not increase the supply of Internet service

Answer: E

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

Source: MyEconLab

78) The following events occur one at a time:

- I. The price of crude oil rises.
- II. The price of a car rises.
- III. All speed limits on highways are abolished.
- IV. Robots cut car production costs.

The quantity of gasoline supplied \_\_\_\_\_.

- A) increases when all speed limits on highways are abolished
- B) increases when the price of crude oil rises
- C) decreases when robots cut car production costs
- D) increases when the price of a car rises
- E) decreases when the price of crude oil rises

Answer: A

Diff: 3 Type: MC

Topic: Predicting Changes in Price and Quantity

Source: MyEconLab

79) What will happen to the equilibrium price and quantity of coffee if it is discovered to help prevent colds and, at the same time, Brazil and Vietnam emerge in the global market as massive producers of coffee?

- A) The equilibrium price will fall and the effect on the equilibrium quantity is uncertain.
- B) The equilibrium price will rise and the effect on the equilibrium quantity is uncertain.
- C) The equilibrium quantity will decrease and the equilibrium price will rise.
- D) The equilibrium quantity will increase and the equilibrium price will remain unchanged.
- E) The equilibrium quantity will increase and the effect on the equilibrium price is uncertain.

Answer: E

Type: MC

80) All shredded wheat producers have decided to add a new ingredient, the "crunch enhancer" to shredded wheat. Crunch enhancer keeps cereals crisper longer in milk and, as a result, consumers decide they like shredded wheat more than before. What happens to the supply and demand curves for shredded wheat now that it costs more to produce and consumers like it better?

- A) The supply and demand curves both shift rightward.
- B) The supply curve shifts rightward and the demand curve remains unchanged.
- C) The supply curve shifts leftward and the demand curve shifts rightward.
- D) The supply curve shifts leftward and the demand curve remains unchanged.
- E) Neither curve changes but a movement occurs up along the demand curve and a movement occurs up along the supply curve.

Answer: C

Type: MC

### 3.6 Mathematical Note

1) The demand curve for knobs is  $P = 75 - 6Q_D$  and the supply curve for knobs is  $P = 35 + 2Q_S$ .

What is the equilibrium price of a knob?

- A) \$5
- B) \$10
- C) \$40
- D) \$45
- E) None of the above.

Answer: D

Diff: 2 Type: MC

Topic: Mathematical Note: Demand, Supply, and Equilibrium

Source: Study Guide

2) The y- axis intercept of the supply curve is 40 and the slope is 6. The equation of the supply curve is \_\_\_\_\_.

- A)  $P = 3 + 40Q_S$
- B)  $P = 40 + 6Q_S$
- C)  $P = 40 - 6Q_S$
- D)  $Q_S = 40 + 6P$
- E)  $Q_S = 40 - 6P$

Answer: B

Diff: 2 Type: MC

Topic: Mathematical Note: Demand, Supply, and Equilibrium

Source: MyEconLab

3) The y- axis intercept of the demand curve is 60 and the slope is - 8. The equation of the demand curve is \_\_\_\_\_.

- A)  $P = 8 - 60Q_D$
- B)  $P = 60 - 8Q_D$
- C)  $Q_D = 60 - 8P$
- D)  $P = 60 + 8Q_D$
- E)  $Q_D = 60 + 8P$

Answer: B

Diff: 2 Type: MC

Topic: Mathematical Note: Demand, Supply, and Equilibrium

Source: MyEconLab

4) The demand curve is  $P = 700 - 10Q_D$ . The supply curve is  $P = 400 + 5Q_S$ . At market equilibrium, the equilibrium quantity is \_\_\_\_\_ and the equilibrium price is \_\_\_\_\_.

- A) 20; 500
- B) 5; 0.05
- C) 0.05; 5
- D) 500; 20
- E) 300; 15

Answer: A

Diff: 2 Type: MC

Topic: Mathematical Note: Demand, Supply, and Equilibrium

Source: MyEconLab

5) The demand curve is  $P = 700 - 20Q_D$ . The supply curve is  $P = 300 + 20Q_S$ . At market equilibrium, the equilibrium quantity is \_\_\_\_\_ and the equilibrium price is \_\_\_\_\_.

- A) 10; 500
- B) 500; 10
- C) 0.10; 20
- D) 20; 0.10
- E) 400; 40

Answer: A

Diff: 2 Type: MC

Topic: Mathematical Note: Demand, Supply, and Equilibrium

Source: MyEconLab

6) The demand curve is  $P = 800 - 25Q_D$ . The supply curve is  $P = 500 + 25Q_S$ . At market equilibrium, the equilibrium quantity is \_\_\_\_\_ and the equilibrium price is \_\_\_\_\_.

- A) 25; 0.17
- B) 650; 6.0
- C) 0.17; 25
- D) 6.0; 650
- E) 1,300; zero

Answer: D

Diff: 2 Type: MC

Topic: Mathematical Note: Demand, Supply, and Equilibrium

Source: MyEconLab

## Chapter 4 Elasticity

### 4.1 Price Elasticity of Demand

1) A price elasticity of demand of 2 means that a 10 percent increase in price will result in a

- A) 2 percent decrease in quantity demanded.
- B) 20 percent decrease in quantity demanded.
- C) 5 percent decrease in quantity demanded.
- D) 2 percent increase in quantity demanded.
- E) 20 percent increase in quantity demanded.

Answer: B

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

2) The price elasticity of demand is a units-free measure of the responsiveness of the \_\_\_\_\_ when all other influences on buying plans remain the same.

- A) quantity demanded to a change in the price of a substitute or complement
- B) quantity demanded to a change in income
- C) quantity demanded of a good to a change in its price
- D) price to a change in quantity demanded
- E) none of the above

Answer: C

Diff: 1 Type: MC

Topic: Price Elasticity of Demand

3) The concept used by economists to indicate the responsiveness of the quantity demanded of a good to a change in its price is the

- A) cross elasticity of demand.
- B) income elasticity of demand.
- C) substitute elasticity of demand.
- D) price elasticity of demand.
- E) elasticity of supply.

Answer: D

Diff: 1 Type: MC

Topic: Price Elasticity of Demand

4) If a 10 percent rise in price leads to an 8 percent decrease in quantity demanded, the price elasticity of demand is

- A) 0.8.
- B) 1.25.
- C) 8.
- D) 0.125.
- E) 80.

Answer: A

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

5) If a large percentage drop in the price level results in a small percentage increase in the quantity demanded,

- A) demand is inelastic.
- B) demand is elastic.
- C) demand is unit elastic.
- D) the price elasticity of demand is close to infinity.
- E) the price elasticity of demand is zero.

Answer: A

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

6) The price of apples falls by 5 percent and quantity of apples demanded increases by 6 percent. We conclude that the demand for apples is

- A) perfectly elastic.
- B) unit elastic.
- C) elastic.
- D) perfectly inelastic.
- E) inelastic.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

7) The price of oranges rises by 3 percent and quantity of oranges demanded decreases by 3 percent. We conclude that the demand for oranges is

- A) inelastic.
- B) elastic.
- C) perfectly inelastic.
- D) perfect elastic.
- E) unit elastic.

Answer: E

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

8) The price of plums falls by 7 percent and quantity of plums demanded increases by 6.75 percent. We conclude that the demand for plums is

- A) inelastic.
- B) perfectly elastic.
- C) perfectly inelastic.
- D) elastic.
- E) unit elastic.

Answer: A

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

9) The price of good A falls by 10 percent and quantity of good A demanded does not change. We conclude that the demand for good A is

- A) perfectly elastic.
- B) inelastic.
- C) perfectly inelastic.
- D) elastic.
- E) unit elastic.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

10) Which one of the following illustrates an inelastic demand?

- A) A 10 percent rise in price leads to a 5 percent decrease in quantity demanded.
- B) A 10 percent rise in price leads to a 20 percent decrease in quantity demanded.
- C) A price elasticity of demand equal to infinity.
- D) A price elasticity of demand equal to 1.0.
- E) A price elasticity of demand equal to 2.0.

Answer: A

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

11) Which one of the following illustrates an elastic demand?

- A) A 10 percent rise in price leads to a 5 percent decrease in quantity demanded.
- B) A 10 percent rise in price leads to a 20 percent decrease in quantity demanded.
- C) A price elasticity of demand equal to 0.2.
- D) A price elasticity of demand equal to 1.0.
- E) A price elasticity of demand equal to zero.

Answer: B

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

12) If a 12 percent fall in price results in an 8 percent increase in quantity demanded, the price elasticity of demand equals

- A) 0.96.
- B) 0.12.
- C) 0.67.
- D) 1.5.
- E) 0.8.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

13) The demand for good *A* is unit elastic if

A) a 5 percent fall in the price of *A* results in an infinite increase in the quantity of *A* demanded.

B) a 5 percent rise in the price of *A* results in a 10 percent decrease in the quantity of *A* demanded.

C) any increase in the price of *A* results in a 1 percent decrease in the quantity of *A* demanded.

D) a 5 percent rise in the price of *A* results in no change in the quantity of *A* demanded.

E) a 5 percent rise in the price of *A* results in a 5 percent decrease in the quantity of *A* demanded.

Answer: E

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

14) Demand is inelastic if

A) a small change in price results in a large change in quantity demanded.

B) the quantity demanded is very responsive to a change in price.

C) the price elasticity of demand is 0.2.

D) the price does not change when supply increases.

E) a 10 percent change in price results in a 1 percent change in the quantity supplied.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

15) If the demand curve for a good is a horizontal line, then the good has

A) zero income elasticity.

B) price elasticity of demand equal to zero.

C) infinite price elasticity of demand.

D) a price elasticity of demand that is likely to rise in the short run.

E) a price elasticity of demand that is likely to fall in the short run.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

16) If a 10 percent rise in the price of goods leads to a 10 percent decrease in quantity demanded, the demand curve for this good

A) is vertical.

B) is horizontal.

C) has slope equal to 1.

D) is a straight line with slope equal to 10.

E) none of the above.

Answer: E

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

17) A unit elastic demand

A) means that the ratio of a change in quantity demanded to a change in price is equal to 1.

B) means that the ratio of a percentage change in quantity demanded to a percentage change in price is equal to 1.

C) means that the ratio of a change in price to a change in quantity demanded is equal to 1.

D) is illustrated by a horizontal demand curve.

E) is illustrated by a vertical demand curve.

Answer: B

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

18) Suppose a rise in the price of a good from \$6.50 to \$7.50 leads to a decrease in the quantity demanded from 10,500 to 9,500 units. In this range of demand, the price elasticity of demand is

A) 14.

B) 7.

C) 1,000.

D) 1.

E) 0.7.

Answer: E

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

19) A fall in the price of a good from \$11.50 to \$8.50 results in an increase in the quantity demanded from 19,200 to 20,800 units. The price elasticity of demand is

A) 0.27.

B) 3.75.

C) 0.08.

D) 8.0.

E) 30.

Answer: A

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

20) A fall in the price of a good from \$10.50 to \$9.50 results in an increase in the quantity demanded from 18,800 to 21,200 units. The price elasticity of demand is

A) 0.8.

B) 1.25.

C) 1.2.

D) 8.0.

E) 2.4.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

21) Suppose the quantity of root beer demanded decreases from 105,000 litres per week to 95,000 litres per week when the price rises by 5 percent. The price elasticity of demand

A) is 2.0.

B) is 0.5.

C) is 10.

D) is inelastic.

E) cannot be computed unless we know the original price and the new price.

Answer: A

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

22) Suppose that the price elasticity of demand for bottled water in Sackville, New Brunswick is 1.5, while the price elasticity of demand for bottled water in Prince Albert, Saskatchewan is 0.93. This implies that the demand in Sackville is \_\_\_\_\_ and demand in Prince Albert is \_\_\_\_\_.

A) unit elastic; unit elastic

B) perfectly elastic; inelastic

C) inelastic; elastic

D) elastic; inelastic

E) elastic; unit elastic

Answer: D

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

23) Suppose the government of Nova Scotia wants to reduce the consumption of electricity by 5 percent. The price elasticity of demand for electricity is 0.40. You advise the Nova Scotia government to

A) raise the price of electricity by 12.5 percent.

B) raise the price of electricity by 2 percent.

C) lower the price of electricity by 12.5 percent.

D) stay away from the market for electricity and let the market mechanism fix the problem.

E) lower the price of electricity by 2 percent.

Answer: A

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

24) Suppose the Lethbridge Computer Company decides to increase the quantity of computers it sells by 6 percent. If the price elasticity of demand is 3.5, the company must

A) raise the price of a computer by 1.714 percent.

B) raise the price of a computer by 0.21 percent.

C) lower the price of a computer by 0.21 percent.

D) lower the price of a computer by 1.714 percent.

E) lower the price of a computer by 0.58 percent.

Answer: D

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

25) If the demand for salmon in Cape Breton Nova Scotia is unit elastic, the price elasticity of demand for salmon equals

- A) 1.0.
- B) 100.0.
- C) 0.10.
- D) zero.
- E) 10.0.

Answer: A

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

26) At a price of \$15, Jack's quantity demanded of good A is the same as when the price rises to \$16. Jack's demand for good A is

- A) elastic.
- B) inelastic.
- C) perfectly elastic.
- D) unit elastic.
- E) perfectly inelastic.

Answer: E

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

27) Which one of the following will yield a measured price elasticity of demand of 5.0? A 10 percent rise in price results in a

- A) 10 percent decrease in quantity demanded.
- B) 5 percent decrease in quantity demanded.
- C) 2 percent decrease in quantity demanded.
- D) 50 percent decrease in quantity demanded.
- E) 0.5 percent decrease in quantity demanded.

Answer: D

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

Use the table below to answer the following questions.

**Table 4.1.1**  
Demand schedule for good A.

Price (dollars per unit)	Quantity demanded (units)
9.00	0
8.00	2,000
7.00	4,000
6.00	6,000
5.00	8,000
4.00	10,000
3.00	12,000
2.00	14,000
1.00	16,000
0	18,000

28) Refer to Table 4.1.1. The price elasticity of demand when the price rises from \$6 a unit to \$7 a unit is

- A) 1.0.
- B) 2.0.
- C) 2.6.
- D) 0.5.
- E) 1.3.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

29) Refer to Table 4.1.1. Demand is unit elastic when the price falls from

- A) \$8 to \$7.
- B) \$7 to \$6.
- C) \$6 to \$5.
- D) \$5 to \$4.
- E) \$4 to \$3.

Answer: D

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

30) Refer to Table 4.1.1. If the price of good A falls from \$4 to \$3,

- A) total revenue will increase.
- B) total revenue will remain constant.
- C) demand is elastic in this range.
- D) demand is unit elastic in this range.
- E) demand is inelastic in this range.

Answer: E

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

31) For which one of the following will demand be the most price inelastic?

- A) milk
- B) Happy Cow brand milk
- C) Happy Cow brand milk in Regina
- D) Happy Cow brand milk at Ralph's Grocery Store in Regina
- E) All of the above will exhibit the same price elasticity of demand

Answer: A

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

32) For which one of the following is demand likely to be most inelastic?

- A) diamonds
- B) insulin for a diabetic
- C) potatoes
- D) gasoline
- E) books

Answer: B

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

33) Demand will be more inelastic the

- A) higher the income level.
- B) lower the income level.
- C) longer the passage of time after a price increase.
- D) fewer good substitutes that are available.
- E) larger the fraction of income spent on the good.

Answer: D

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

34) Demand will be more elastic the

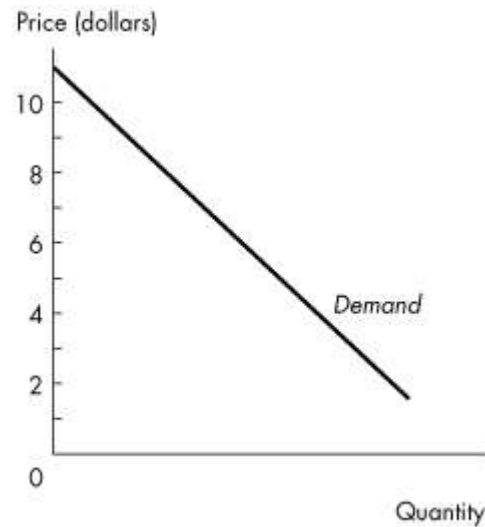
- A) higher the income level.
- B) lower the income level.
- C) longer the passage of time after a price increase.
- D) fewer substitutes are available.
- E) smaller the fraction of income spent on the good.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

Use the figure below to answer the following question.



**Figure 4.1.1**

35) Figure 4.1.1 illustrates a linear demand curve. Comparing the price elasticity in the \$2 to \$3 price range with the elasticity in the \$8 to \$9 range, we can conclude

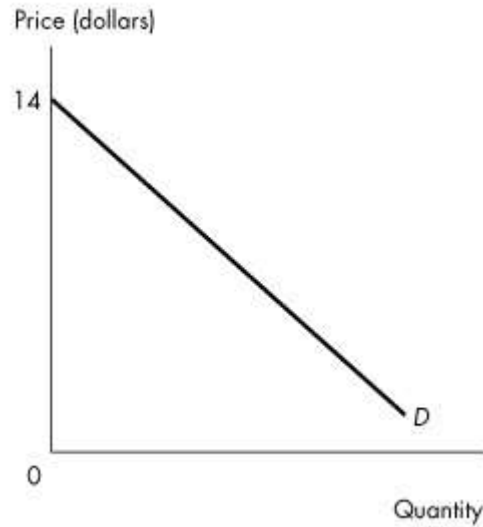
- A) that demand is more elastic in the \$8 to \$9 price range.
- B) that demand is more elastic in the \$2 to \$3 price range.
- C) that the price elasticity of demand is the same in both price ranges.
- D) nothing without numerical information about quantities.
- E) that the price elasticity of demand is zero in both price ranges because the demand curve is a straight-line demand curve.

Answer: A

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

Use the figure below to answer the following questions.



**Figure 4.1.2**

36) Figure 4.1.2 illustrates a linear demand curve. If the price falls from \$13 to \$11,

- A) total revenue increases.
- B) total revenue decreases.
- C) total revenue remains unchanged.
- D) total revenue initially increases then decreases.
- E) total revenue initially decreases then increases.

Answer: A

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

37) Figure 4.1.2 illustrates a linear demand curve. If the price falls from \$4 to \$2,

- A) total revenue increases.
- B) total revenue decreases.
- C) total revenue remains unchanged.
- D) the quantity demanded increases by more than 10 percent.
- E) the percentage change in quantity demanded is more than the percentage change in price.

Answer: B

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

38) The quantity of apples demanded decreases by 8 percent when the price rises by 8 percent. The demand for apples is

- A) unit elastic.
- B) inelastic.
- C) elastic.
- D) perfectly elastic.
- E) perfectly inelastic.

Answer: A

Diff: 1 Type: MC

Topic: Price Elasticity of Demand

39) A perfectly vertical demand curve indicates that the price elasticity of demand for the good is

- A) zero.
- B) greater than zero but less than 1.
- C) 1.
- D) greater than 1.
- E) negative.

Answer: A

Diff: 1 Type: MC

Topic: Price Elasticity of Demand

Source: Study Guide

40) Factors that influence the elasticity of demand include

- A) the closeness of substitutes.
- B) the price of complements but not the price of substitutes.
- C) income.
- D) preferences.
- E) the price of substitutes and complements.

Answer: A

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

41) A given percentage rise in the price of a good is likely to result in a larger percentage decrease in the quantity of the good demanded

- A) the shorter the passage of time.
- B) the larger the proportion of income spent on it.
- C) the harder it is to obtain good substitutes.
- D) all of the above.
- E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

Source: Study Guide

42) Suppose a fall in the price of a good from \$10 to \$8 leads to an increase in quantity demanded from 20 to 24 units. The price elasticity of demand is

- A) 1.
- B) 9/11.
- C) 11/9.
- D) 2.0.
- E) 4.5/11.

Answer: B

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

43) For which one of the following will demand be the most price elastic?

- A) daily newspapers
- B) Ontario newspapers
- C) Toronto newspapers
- D) The *Toronto Star*
- E) Each of the above will exhibit the same price elasticity of demand

Answer: D

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

44) Suppose this coming winter France will have unusually bad weather, and that next year's wine crop will be substantially reduced. Select the best statement.

- A) The French wine supply will increase as price rises.
- B) If the demand for French wine is elastic, wine producers will experience an increase in total revenue.
- C) The initial change in the market will create a surplus of French wine.
- D) In the final equilibrium, price and quantity will be higher.
- E) none of the above

Answer: E

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

Use the table below to answer the following question.

**Table 4.1.2**

<b>Price per Volleyball</b>	<b>Quantity Demanded</b>
\$19	55
\$21	45

45) Refer to Table 4.1.2. The table shows two points on the demand curve for volleyballs. What is the price elasticity of demand between these two points?

- A) 2.5.
- B) 2.0.
- C) 0.5.
- D) 0.4.
- E) none of the above

Answer: B

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

Source: Study Guide

46) If the price elasticity of demand is 2, then a 1 percent fall in price

- A) doubles the quantity demanded.
- B) decreases the quantity demanded by half.
- C) increases the quantity demanded by 2 percent.
- D) decreases the quantity demanded by 2 percent.
- E) increases the quantity demanded by 0.5 percent.

Answer: C

Diff: 1 Type: MC

Topic: Price Elasticity of Demand

Source: Study Guide

47) The demand for a good will be more price inelastic,

- A) the higher is its price.
- B) the larger is the percentage of income spent on it.
- C) the longer is the passage of time.
- D) the smaller the supply of the good.
- E) the fewer substitutes are available for the good.

Answer: E

Diff: 1 Type: MC

Topic: Price Elasticity of Demand

48) A union leader who claims that "higher wages increase living standards without causing unemployment" believes that the demand for labour is

- A) income elastic.
- B) income inelastic.
- C) perfectly elastic.
- D) perfectly inelastic.
- E) unit elastic.

Answer: D

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

Source: Study Guide

49) Business people speak about price elasticity of demand without using the actual term. Which one of the following statements reflects elastic demand for a good?

- A) "A price cut won't help me. It won't increase sales, and I'll just get less money for each unit."
- B) "I don't think a price cut will make any difference to my bottom line. What I may gain from selling more I would lose on the lower price."
- C) "My customers are real bargain hunters. Since I set my prices just a few cents below my competitors, customers have flocked to the store, and sales are booming."
- D) "With the recent economic recovery, people have more income to spend and sales are booming, even at the previous prices."
- E) none of the above

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

Source: Study Guide

50) If a rise in price results in a decrease in total revenue, then the price elasticity of demand is

- A) negative.
- B) zero.
- C) greater than zero but less than 1.
- D) equal to 1.
- E) greater than 1.

Answer: E

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

51) Suppose that Simon Fraser University decides to raise tuition fees to increase the total revenue it receives from students. This policy works only if the demand for a Simon Fraser University education is

- A) unit elastic.
- B) inelastic.
- C) elastic.
- D) greater than the demand for a University of Western Ontario education.
- E) perfectly elastic.

Answer: B

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

52) The demand for a good is perfectly elastic when the price elasticity of demand is

- A) equal to infinity.
- B) between infinity and 1.
- C) equal to 1.
- D) between 1 and zero.
- E) equal to zero.

Answer: A

Diff: 1 Type: MC

Topic: Price Elasticity of Demand

53) When the price elasticity of demand is \_\_\_\_\_, demand for the good is perfectly inelastic.

- A) equal to infinity
- B) greater than 1
- C) equal to 1
- D) between 1 and zero
- E) equal to zero

Answer: E

Diff: 1 Type: MC

Topic: Price Elasticity of Demand

54) When the price elasticity of demand is \_\_\_\_\_, demand for the good is elastic.

- A) equal to infinity
- B) greater than 1
- C) equal to 1
- D) between 1 and zero
- E) equal to zero

Answer: B

Diff: 1 Type: MC

Topic: Price Elasticity of Demand

55) When the price elasticity of demand is \_\_\_\_\_, demand for the good is unit elastic.

- A) equal to infinity
- B) greater than 1
- C) equal to 1
- D) between 1 and zero
- E) equal to zero.

Answer: C

Diff: 1 Type: MC

Topic: Price Elasticity of Demand

56) When the price elasticity of demand is \_\_\_\_\_, demand for the good is inelastic.

- A) equal to infinity
- B) greater than 1
- C) equal to 1
- D) between 1 and zero
- E) equal to zero

Answer: D

Diff: 1 Type: MC

Topic: Price Elasticity of Demand

57) The price elasticity of demand for airplane travel one year in advance of the departure date is most likely to be

- A) equal to infinity.
- B) equal to zero.
- C) between zero and 1.
- D) equal to 1.
- E) greater than 1.

Answer: E

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

58) The price elasticity of demand for airplane travel one week in advance of the departure date is most likely to be

- A) equal to infinity.
- B) equal to zero.
- C) between zero and 1.
- D) equal to 1.
- E) greater than 1.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

59) If a price decrease results in an increase in total revenue, then demand is

- A) inelastic.
- B) unit elastic.
- C) perfectly inelastic.
- D) equal to supply.
- E) elastic.

Answer: E

Diff: 1 Type: MC

Topic: Price Elasticity of Demand

60) Suppose Swiss Chalet in Moncton knows that the demand for their half-chicken meals is elastic. If the manager wants to increase total revenue from half-chicken meal sales, he should

- A) lower the price of a half-chicken meal.
- B) not change the price of a half-chicken meal.
- C) raise the price of a half-chicken meal.
- D) decrease the supply of half-chicken meals.
- E) hire fewer employees.

Answer: A

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

61) As a result of a poor growing season, the supply curve of apples shifted leftward, the equilibrium price of apples rose, and total revenue fell. This suggests that the price elasticity of demand for apples is

- A) perfectly inelastic.
- B) elastic.
- C) inelastic.
- D) unit elastic.
- E) perfectly elastic.

Answer: B

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

62) Suppose the Nunavut government decides to repair Iqaluit roads. One way to generate sufficient funds for this plan is to increase taxes on gasoline. The government will be able to raise total revenue from gasoline sales only if the demand for gasoline is

- A) perfectly elastic.
- B) equal to the supply of gasoline.
- C) unit elastic.
- D) inelastic.
- E) elastic.

Answer: D

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

63) Which of the following will have the most elastic demand?

- A) frozen desserts
- B) ice cream
- C) strawberry ice cream
- D) a banana split made with strawberry and chocolate ice cream
- E) a banana split with with Nestle strawberry and chocolate ice cream

Answer: E

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

64) Suppose your annual income is \$65 000 and your favourite TV Guide magazine costs you \$28 a year. Your demand for the TV Guide magazine is likely to be

- A) perfectly elastic.
- B) inelastic.
- C) unit elastic.
- D) elastic.
- E) elastic -- the same as your demand for all other goods.

Answer: B

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

65) The longer the time that has elapsed since a price change the more time consumers will have to respond to price changes. As a result, demand becomes

- A) zero.
- B) more inelastic.
- C) more elastic.
- D) perfectly inelastic.
- E) unit elastic.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

66) The price of gasoline rises by 25 percent and remains fixed at the new higher level. Choose the correct statement.

- A) The demand for gasoline will increase after consumers adjust their consumption behaviour to the new higher price.
- B) The demand for gasoline will decrease after consumers adjust their consumption behaviour to the new higher price.
- C) Initially after the price change, the price elasticity of demand will be less elastic than it will be a few years after the price change.
- D) The price elasticity of demand for gasoline will decrease in the future.
- E) Initially after the price change, the price elasticity of demand will be more elastic than it will be a few years after the price change.

Answer: C

Diff: 3 Type: MC

Topic: Price Elasticity of Demand

- 67) The demand for a good is price elastic if
- A) a rise in price results in an increase in total revenue.
  - B) a fall in price results in a decrease in total revenue.
  - C) a rise in price results in a decrease in total revenue.
  - D) the good is a necessity.
  - E) the demand for the good is very insensitive to changes in price.

Answer: C

Diff: 1 Type: MC

Topic: Price Elasticity of Demand

- 68) The demand for a good is price inelastic if
- A) a rise in price results in an increase in total revenue.
  - B) a rise in price results in a decrease in total revenue.
  - C) an increase in income results in a decrease in total revenue.
  - D) an increase in income results in an increase in total revenue.
  - E) the good is a luxury.

Answer: A

Diff: 1 Type: MC

Topic: Price Elasticity of Demand

- 69) If the demand for a good is unit elastic, then a 5 percent increase in price results in
- A) a 5 percent increase in total revenue.
  - B) a 5 percent decrease in total revenue.
  - C) no change in total revenue.
  - D) an increase in total revenue greater than 5 percent.
  - E) an increase in total revenue less than 5 percent.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

- 70) Total revenue from the sale of a good will decrease if
- A) income increases and the good is normal.
  - B) its price rises and demand is elastic.
  - C) its price rises and demand is inelastic.
  - D) income falls and the good is an inferior good.
  - E) its price falls and demand is elastic.

Answer: B

Diff: 1 Type: MC

Topic: Price Elasticity of Demand

71) If Saudi Arabia argues that an increase in the supply of oil will decrease total revenue, then Saudi Arabia believes the demand for oil is

- A) income inelastic.
- B) income elastic.
- C) elastic.
- D) inelastic.
- E) unit elastic.

Answer: D

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

72) Suppose there is an increase in the cost of resources used in the production of good A. Then

- A) if the price of A rises, we know the demand for A is elastic.
- B) if the total revenue from sales of A rises, we know the demand for A is elastic.
- C) if the total revenue from sales of A falls, we know the demand for A is elastic.
- D) total revenue will increase because the price of A must rise.
- E) total revenue must fall because the quantity bought and sold of A must fall.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

73) When the price of peanut butter rises by 4 percent, total revenue decreases by 8 percent. The demand for peanut butter

- A) is elastic.
- B) is inelastic.
- C) is unit elastic.
- D) has a price elasticity equal to  $1/2$ .
- E) has a price elasticity equal to 2.

Answer: A

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

Source: Study Guide

74) If price elasticity of demand is zero, then as the price falls

- A) total revenue does not change.
- B) quantity demanded does not change.
- C) quantity demanded falls to zero.
- D) total revenue increases from zero.
- E) None of the above occurs.

Answer: B

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

Source: Study Guide

75) A technological breakthrough lowers the cost of photocopiers. If the demand for photocopiers is price inelastic, we predict that photocopier sales

- A) fall and total revenue increases.
- B) fall and total revenue decreases.
- C) rise and total revenue increases.
- D) rise and total revenue decreases.
- E) rise, but changes in total revenue will depend on elasticity of supply.

Answer: D

Diff: 1 Type: MC

Topic: Price Elasticity of Demand

Source: Study Guide

76) A decrease in tuition fees will decrease the university's total revenue if the price elasticity of demand for university education is

- A) negative.
- B) greater than zero but less than 1.
- C) equal to 1.
- D) greater than 1.
- E) less than the elasticity of supply.

Answer: B

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

Source: Study Guide

77) The demand for orange juice is price elastic. A severe frost, which destroys large quantities of oranges will

- A) lower the equilibrium price but increase total consumer spending on juice.
- B) decrease the equilibrium quantity and decrease total consumer spending on juice.
- C) decrease both the equilibrium quantity and the price of juice.
- D) raise the equilibrium price as well as total consumer spending for juice.
- E) raise the equilibrium price but leave total consumer spending for juice constant.

Answer: B

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

Source: Study Guide

78) Tina and Brian work for the same recording company. Tina claims they would be better off by raising the price of their CDs, while Brian claims they would be better off by lowering the price. We can conclude that

A) Tina thinks the demand for CDs has price elasticity of demand zero and Brian thinks price elasticity of demand equals 1.

B) Tina thinks the demand for CDs has price elasticity of demand equal to 1 and Brian thinks price elasticity of demand equals zero.

C) Tina thinks the demand for CDs is price elastic and Brian thinks it is price inelastic.

D) Tina thinks the demand for CDs is price inelastic and Brian thinks it is price elastic.

E) Tina and Brian should stick to singing and forget about economics.

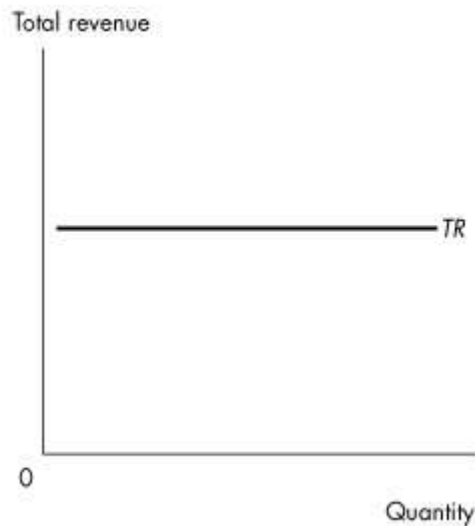
Answer: D

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

Source: Study Guide

Use the figure below to answer the following question.



**Figure 4.1.3**

79) Given the relationship shown in Figure 4.1.3 between total revenue from the sale of a good and the quantity of the good sold, then

A) this is an inferior good.

B) this is a normal good.

C) the price elasticity of demand is zero.

D) demand for this good is perfectly elastic.

E) the price elasticity of demand is 1.

Answer: E

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

Source: Study Guide

80) If the Canucks lower ticket prices and find that total revenue does not change, then the price elasticity of demand for tickets is

- A) zero.
- B) greater than zero but less than 1.
- C) equal to 1.
- D) greater than 1.
- E) negative.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

81) A good has a price elasticity of demand equal to 2. If new imports lower its price from \$1.20 to \$0.80, the percentage change in quantity demanded will be

- A) an increase of 80 percent.
- B) a decrease of 80 percent.
- C) a decrease of 40 percent.
- D) an increase of 2 percent.
- E) an increase of 40 percent.

Answer: A

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

82) Total revenue is more likely to rise when the price rises if

- A) there are few substitutes for the good.
- B) a high proportion of income is spent on the good.
- C) some extended period of time passes.
- D) all of the above.
- E) none of the above.

Answer: A

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

83) Total revenue is more likely to rise when the price falls if

- A) there are few substitutes for the good.
- B) a low proportion of income is spent on the good.
- C) some extended period of time passes.
- D) all of the above.
- E) none of the above.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

84) If the demand for good Z is perfectly inelastic, then the demand curve for good Z is

- A) vertical.
- B) horizontal.
- C) upward sloping.
- D) downward sloping.
- E) initially upward sloping and then downward sloping.

Answer: A

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

85) Suppose the demand curve for good X is horizontal. This shows that the demand for good X is

- A) unit elastic.
- B) inelastic.
- C) perfectly elastic.
- D) perfect inelastic.
- E) elastic.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

86) If the price elasticity of demand is zero, then demand is

- A) elastic.
- B) inelastic.
- C) perfectly inelastic.
- D) perfectly elastic.
- E) unit elastic.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

Use the table below to answer the following question.

**Table 4.1.3**

	Price of Jolt	Price of Coke	Income Level	Jolt Sales
2000	\$1.00/can	\$1.00/can	\$25,000	15,000 cases
2001	\$1.00/can	\$1.40/can	\$25,000	25,000 cases
2002	\$1.00/can	\$1.40/can	\$35,000	15,000 cases
2003	\$1.40/can	\$1.40/can	\$35,000	5,000 cases

87) Refer to Table 4.1.3. The price elasticity of demand for Jolt is

- A) 1.
- B) 2.5.
- C) 3.0.
- D) 0.33.
- E) cannot be calculated because income is not constant.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

88) Suppose a rise of 8 percent in the price of bison meat in Saskatchewan reduces the consumption of bison meat by 24 percent. Such a price rise will induce consumers to spend

- A) more of their income on bison.
- B) the same amount of their income on bison as before.
- C) less of their income on bison.
- D) more on products that are complements of bison.
- E) zero dollars on bison meat.

Answer: C

Diff: 2 Type: MC

Topic: Price Elasticity of Demand

Use the table below to answer the following question.

**Table 4.1.4**

<b>Price</b> (dollars per chip)	<b>Quantity Demanded</b> (millions of chips per year)
<b>200</b>	<b>50</b>
<b>250</b>	<b>45</b>
<b>300</b>	<b>40</b>
<b>350</b>	<b>35</b>
<b>400</b>	<b>30</b>

89) Refer to Table 4.1.4. The table shows the demand schedule for computer chips. As the price rises from \$200 a chip to \$300 a chip, total revenue \_\_\_\_\_. So at a price of \$250 a chip, demand is \_\_\_\_\_.

- A) falls; inelastic
- B) rises; inelastic
- C) falls; rises
- D) rises; elastic
- E) rises; unit elastic

Answer: B

Type: MC

Topic: Price Elasticity of Demand

Source: MyEconLab

Use the table below to answer the following question.

**Table 4.1.5**

<b>Price</b> (dollars per night)	<b>Quantity demanded</b> (rooms per night)
<b>200</b>	<b>10,000</b>
<b>250</b>	<b>8,000</b>
<b>400</b>	<b>5,000</b>
<b>500</b>	<b>4,000</b>
<b>800</b>	<b>2,500</b>

90) Refer to Table 4.1.5. The demand for hotel rooms is \_\_\_\_\_ because \_\_\_\_\_.

- A) inelastic; if the price is set low enough, total revenue will decrease
- B) elastic; if the price is set high enough, total revenue will decrease
- C) unit elastic; a price cut leaves total revenue unchanged. Total revenue never reaches a maximum
- D) decreasing as the price falls; the demand curve for hotel rooms is a straight-line demand curve
- E) inelastic; if the price is set low enough, total revenue will increase

Answer: C

Type: MC

Topic: Price Elasticity of Demand

Source: MyEconLab

91) When the price of a good increased by 5 percent, the quantity demanded of it decreased 10 percent. The price elasticity of demand is \_\_\_\_\_. A price rise will \_\_\_\_\_ total revenue.

- A) 2.0; decrease
- B) 0.5; decrease
- C) 2.0; increase
- D) 0.5; increase
- E) -2.0; decrease

Answer: A

Type: MC

Topic: Price Elasticity of Demand

Source: MyEconLab

92) When the price of a good increased by 6 percent, the quantity demanded of it decreased 3 percent. Most likely, this good \_\_\_\_\_ and \_\_\_\_\_.

- A) is a necessity; has poor substitutes
- B) has poor substitutes; is a luxury
- C) is a necessity; has good substitutes
- D) is a luxury; is narrowly defined
- E) is a luxury; has experienced a recent price change

Answer: A

Type: MC

Topic: Price Elasticity of Demand

Source: MyEconLab

93) The price elasticity of demand for purses is measured in

- A) dollars.
- B) purses.
- C) dollars per purse.
- D) purses per dollar.
- E) none of the above.

Answer: E

Type: MC

94) The price elasticity of demand depends on

- A) the units used to measure price and the units used to measure quantity.
- B) the units used to measure price but not the units used to measure quantity.
- C) the units used to measure quantity but not the units used to measure price.
- D) neither the units used to measure price nor the units used to measure quantity.
- E) the relative price of the good.

Answer: D

Type: MC

95) When the quantity of coal is measured in kilograms instead of pounds, the demand for coal becomes

- A) more elastic.
- B) less elastic.
- C) neither more nor less elastic.
- D) perfectly elastic.
- E) perfectly inelastic.

Answer: C

Type: MC

96) The price elasticity of demand for oranges \_\_\_\_\_ if the quantity is measured in pounds instead of kilograms and \_\_\_\_\_ if the price is measured in dollars instead of cents.

- A) changes; changes
- B) changes; does not change
- C) does not change; changes
- D) does not change; does not change
- E) increases; decreases

Answer: D

Type: MC

## 4.2 More Elasticities of Demand

Use the table below to answer the following questions.

**Table 4.2.1**

Year	Quantity Demanded (units)	Price (dollars)	Income (dollars)
2007	25,000	1	4,000
2008	15,000	3	4,000
2009	5,000	3	6,000

1) Consider the information in Table 4.2.1. Select the best statement.

- A) The income elasticity of demand is -2.5.
- B) The income elasticity of demand is 2.5.
- C) The income elasticity of demand is -3.33.
- D) The income elasticity of demand is 3.33.
- E) We cannot calculate the income elasticity of demand because both income and price are changing at the same time.

Answer: A

Diff: 2 Type: MC

Topic: More Elasticities of Demand

2) The income elasticity of demand equals the percentage change in \_\_\_\_\_ other things remaining the same.

- A) price divided by the percentage change in income
- B) price divided by the percentage change in quantity demanded
- C) income divided by the percentage change in quantity demanded
- D) quantity demanded divided by the percentage change in price
- E) quantity demanded divided by the percentage change in income

Answer: E

Diff: 1 Type: MC

Topic: More Elasticities of Demand

3) If the quantity of carrots demanded increases by a small percentage when income increases by a large amount, we know that the demand for carrots is

- A) price elastic.
- B) price inelastic.
- C) income inferior.
- D) income elastic.
- E) income inelastic.

Answer: E

Diff: 1 Type: MC

Topic: More Elasticities of Demand

4) If the quantity of carrots demanded increases by a large percentage when income increases by a small amount, we know that the demand for carrots is

- A) price elastic.
- B) price inelastic.
- C) income inferior.
- D) income inelastic.
- E) income elastic.

Answer: E

Diff: 1 Type: MC

Topic: More Elasticities of Demand

5) Which one of the following must be true if demand is income inelastic?

- A) A large percentage increase in income will result in a small percentage increase in quantity demanded.
- B) A small percentage increase in income will result in a large percentage increase in quantity demanded.
- C) An increase in income will decrease the quantity demanded.
- D) The good is an inferior good.
- E) A percentage rise in price increases the quantity demanded by a smaller percentage.

Answer: A

Diff: 1 Type: MC

Topic: More Elasticities of Demand

6) Which one of the following must be true if demand is income elastic?

- A) A large percentage increase in income will result in a small percentage increase in quantity demanded.
- B) A small percentage increase in income will result in a large percentage increase in quantity demanded.
- C) An increase in income will decrease the quantity demanded.
- D) The good is an inferior good.
- E) A percentage change in price will lead to a larger percentage change in quantity demanded.

Answer: B

Diff: 1 Type: MC

Topic: More Elasticities of Demand

7) If a turnip is an inferior good then

- A) a small decrease in income decreases the quantity of turnips demanded at the current price by a large amount.
- B) a large decrease in income decreases the quantity of turnips demanded at the current price by a small amount.
- C) an increase in income increases the quantity demanded at the current price.
- D) an increase in income decreases the quantity demanded at the current price.
- E) turnips taste awful.

Answer: D

Diff: 2 Type: MC

Topic: More Elasticities of Demand

8) If a turnip is a normal good then

- A) a small decrease in income increases the quantity of turnips demanded at the current price by a large amount.
- B) a large decrease in income increases the quantity of turnips demanded at the current price by a small amount.
- C) an increase in income increases the quantity demanded at the current price.
- D) an increase in income decreases the quantity demanded at the current price.
- E) an increase in price decreases the quantity demanded.

Answer: C

Diff: 2 Type: MC

Topic: More Elasticities of Demand

9) Fred's income increases from \$1,950 per week to \$2,050 per week. As a result, he decides to increase the number of movies he attends each month by 10 percent. Fred's demand for movies is

- A) price elastic.
- B) price inelastic.
- C) income elastic.
- D) income inelastic.
- E) income inferior.

Answer: C

Diff: 2 Type: MC

Topic: More Elasticities of Demand

10) Fred's income increases from \$840 per week to \$1,160 per week. As a result, he decides to purchase 24 percent more bubble gum each week. The income elasticity of Fred's demand for bubble gum is

- A) 0.32.
- B) 1.33.
- C) 24.
- D) 0.24.
- E) 0.75.

Answer: E

Diff: 2 Type: MC

Topic: More Elasticities of Demand

11) Fred's income increases from \$800 per week to \$1,200 per week. As a result, he decides to purchase 40 percent more bubble gum each week. The income elasticity of Fred's demand for bubble gum is

- A) 0.40.
- B) 40.
- C) 1.0.
- D) 0.12.
- E) 10.

Answer: C

Diff: 2 Type: MC

Topic: More Elasticities of Demand

12) Suppose that a 20 percent increase in income increases the quantity of good A demanded from 19,200 to 20,800 units. The income elasticity of demand for good A is

- A) 0.05.
- B) 0.8.
- C) 0.4.
- D) 1.2.
- E) 2.0.

Answer: C

Diff: 2 Type: MC

Topic: More Elasticities of Demand

13) If a 10 percent increase in income results in a 5 percent increase in quantity demanded, what is the income elasticity of demand?

- A) 0.5
- B) -0.5
- C) 2.0
- D) -2.0
- E) 1.5

Answer: A

Diff: 1 Type: MC

Topic: More Elasticities of Demand

Source: Study Guide

14) If a 10 percent *increase* in income results in a 10 percent *decrease* in the consumption of widgets, then

- A) the price elasticity of demand for widgets equals 1.
- B) the income elasticity of demand for widgets is negative.
- C) the income elasticity of demand for widgets equals 1.
- D) widgets are a normal good.
- E) the price elasticity demand for widgets is negative.

Answer: B

Diff: 2 Type: MC

Topic: More Elasticities of Demand

15) Luxury goods tend to have income elasticities of demand that are

- A) greater than 1.
- B) greater than zero but less than 1.
- C) less than the income elasticities of demand for necessary goods.
- D) negative.
- E) first positive and then negative as income increases.

Answer: A

Diff: 2 Type: MC

Topic: More Elasticities of Demand

Source: Study Guide

16) If a 4 percent decrease in income (at a constant price) results in a 2 percent decrease in the consumption of dweedles then

- A) the income elasticity of demand for dweedles is negative.
- B) dweedles are a necessity and a normal good.
- C) dweedles are a luxury and a normal good.
- D) dweedles are an inferior good.
- E) both A and D.

Answer: B

Diff: 2 Type: MC

Topic: More Elasticities of Demand

Source: Study Guide

17) The cross elasticity of demand between any two goods is defined as the

- A) percentage change in the quantity demanded of one good divided by the percentage change in the price of the other good.
- B) change in the price elasticity of demand for one good divided by the change in the price elasticity of demand for the other good.
- C) percentage change in the quantity of a good demanded divided by the percentage change in its price.
- D) percentage change in the quantity of a good demanded divided by the percentage change in income.
- E) percentage change in the price of one good divided by the percentage change in the price of the other good.

Answer: A

Diff: 1 Type: MC

Topic: More Elasticities of Demand

18) If the cross elasticity of demand between goods *A* and *B* is positive, then

- A) the demands for *A* and *B* are both price elastic.
- B) the demands for *A* and *B* are both price inelastic.
- C) *A* and *B* are complements.
- D) *A* and *B* are substitutes.
- E) *A* and *B* are independent goods.

Answer: D

Diff: 1 Type: MC

Topic: More Elasticities of Demand

19) If the cross elasticity of demand between goods *A* and *B* is negative, then

- A) the demands for *A* and *B* are both price elastic.
- B) the demands for *A* and *B* are both price inelastic.
- C) *A* and *B* are complements.
- D) *A* and *B* are substitutes.
- E) *A* and *B* are independent goods.

Answer: C

Diff: 1 Type: MC

Topic: More Elasticities of Demand

20) If the cross elasticity of demand between beef and bison is 1.5, then a 3 percent increase in the price of beef will lead to

- A) a 4.5 percent increase in the quantity of bison demanded.
- B) a 4.5 percent decrease in the quantity of bison demanded.
- C) a 2 percent increase in the quantity of bison demanded.
- D) a 2 percent decrease in the quantity of bison demanded.
- E) a 0.5 percent increase in the quantity of bison demanded.

Answer: A

Diff: 2 Type: MC

Topic: More Elasticities of Demand

21) If the quantity of chicken demanded increases by 1.25 percent when the price of beef increases by 2.5 percent, the cross elasticity of demand between chicken and beef is

- A) 3.125.
- B) -3.125.
- C) -0.5.
- D) 2.0.
- E) 0.5.

Answer: E

Diff: 2 Type: MC

Topic: More Elasticities of Demand

22) An economic measure that indicates when the demands for two or more goods are related is

- A) the income elasticity of demand.
- B) the price elasticity of demand.
- C) the substitute elasticity of demand.
- D) the cross elasticity of demand.
- E) the normal elasticity of demand.

Answer: D

Diff: 1 Type: MC

Topic: More Elasticities of Demand

23) If a rise in the price of good *B* increases the demand for good *A*, then

- A) *A* and *B* are substitutes.
- B) *A* and *B* are complements.
- C) the cross elasticity of demand between *A* and *B* is negative.
- D) *A* is a resource used in the production of *B*.
- E) the demand for *A* is price elastic.

Answer: A

Diff: 2 Type: MC

Topic: More Elasticities of Demand

24) If an increase in the supply of good *A* increases the demand for good *B*, then  
A) the demands for *A* and *B* are independent.  
B) the elasticity of supply for good *A* is greater than 1.  
C) *A* and *B* are complements.  
D) *A* and *B* are substitutes.  
E) the demand for *A* is price elastic.

Answer: C

Diff: 2 Type: MC

Topic: More Elasticities of Demand

25) If an increase in the supply of good *A* decreases the demand for good *B*, then  
A) the demands for *A* and *B* are independent.  
B) the elasticity of supply for good *A* is greater than 1.  
C) *A* and *B* are complements.  
D) *A* and *B* are substitutes.  
E) the demand for *A* is price elastic.

Answer: D

Diff: 2 Type: MC

Topic: More Elasticities of Demand

26) A rise in the price of good *A* shifts the  
A) demand curve for good *B* rightward if the cross elasticity of demand between *A* and *B* is negative.  
B) demand curve for good *B* rightward if the cross elasticity of demand between *A* and *B* is positive.  
C) supply curve of *B* rightward if the cross elasticity of demand between *A* and *B* is negative.  
D) supply curve of *B* rightward if the cross elasticity of demand between *A* and *B* is positive.  
E) demand curve for *B* rightward if the income elasticity of demand for *B* is positive.

Answer: B

Diff: 2 Type: MC

Topic: More Elasticities of Demand

27) If the cross elasticity of demand between peanut butter and jelly is negative, then  
A) a rise in the price of peanut butter results in a rise in the equilibrium price of jelly.  
B) a rise in the price of peanut butter results in a fall in the equilibrium price of jelly.  
C) a rise in the price of peanut butter has no effect on the equilibrium price of jelly.  
D) a fall in the price of peanut butter results in a fall in the equilibrium price of jelly.  
E) peanut butter and jelly are substitutes.

Answer: B

Diff: 3 Type: MC

Topic: More Elasticities of Demand

28) Suppose a fall from \$110 to \$90 in the price of playing golf on a public golf course results in an increase in the quantity of golf balls demanded (at the current price of golf balls) from 9,950 units to 10,050 units. The cross elasticity of demand of playing golf with respect to the price of golf balls is

- A) -0.05.
- B) -0.1.
- C) 0.01.
- D) 0.08.
- E) 0.05.

Answer: A

Diff: 2 Type: MC

Topic: More Elasticities of Demand

29) A fall in the price of  $X$  from \$6 to \$4 results in an increase in the quantity of  $Y$  demanded (at the current price of  $Y$ ) from 900 to 1,100 units. What is the cross elasticity of demand between  $X$  and  $Y$ ?

- A) 0.5
- B) -0.5
- C) 2
- D) -2
- E) Either A or B, depending on whether  $X$  and  $Y$  are substitutes or complements.

Answer: B

Diff: 2 Type: MC

Topic: More Elasticities of Demand

30) If good  $A$  is a substitute for good  $B$ , then the cross elasticity of demand is

- A) 12.
- B) infinity.
- C) positive.
- D) zero.
- E) less than zero.

Answer: C

Diff: 2 Type: MC

Topic: More Elasticities of Demand

31) If good  $A$  is a complement of good  $B$ , then the cross elasticity of demand is

- A) 12.
- B) infinity.
- C) positive.
- D) zero.
- E) negative.

Answer: E

Diff: 2 Type: MC

Topic: More Elasticities of Demand

Use the table below to answer the following questions.

**Table 4.2.2**

	Price of Jolt	Price of Coke	Income Level	Jolt Sales
2006	\$1.00/can	\$1.00/can	\$25,000	15,000 cases
2007	\$1.00/can	\$1.40/can	\$25,000	25,000 cases
2008	\$1.00/can	\$1.40/can	\$35,000	15,000 cases
2009	\$1.40/can	\$1.40/can	\$35,000	5,000 cases

32) Refer to Table 4.2.2. The cross elasticity of demand for Jolt with respect to the price of Coke is

- A) 0.75.
- B) 1.5.
- C) 0.40.
- D) 10.
- E) cannot be calculated because income is not constant.

Answer: B

Diff: 3 Type: MC

Topic: More Elasticities of Demand

33) Refer to Table 4.2.2. The income elasticity of demand for Jolt is

- A) +0.67.
- B) -0.67.
- C) +1.5.
- D) -1.5.
- E) cannot be calculated because the price of Coke is not constant.

Answer: D

Diff: 2 Type: MC

Topic: More Elasticities of Demand

34) Refer to Table 4.2.2. All of the following statements regarding Jolt are true *except*

- A) it has an elastic demand.
- B) it is an inferior good.
- C) it is a substitute for Coke.
- D) it has a negative cross elasticity of demand with respect to Coke.
- E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: More Elasticities of Demand

35) The cross elasticity of demand for good A with respect to the price of good B is -1.5. A 10 percent rise in the price of good B will lead to

- A) an increase of 1.5 percent in the quantity of A demanded.
- B) an increase of 15 percent in the quantity of A demanded.
- C) a decrease of 15 percent in the quantity of A demanded.
- D) an increase of 6.7 percent in the quantity of A demanded.
- E) a decrease of 6.7 percent in the quantity of A demanded.

Answer: C

Diff: 2 Type: MC

Topic: More Elasticities of Demand

36) A good has an income elasticity of +0.5. An increase in income from \$15,000 to \$25,000 will lead to a

- A) 2.5 percent increase in the quantity demanded of the good.
- B) 5 percent increase in the quantity demanded of the good.
- C) 5 percent decrease in the quantity demanded of the good.
- D) 25 percent decrease in the quantity demanded of the good.
- E) 25 percent increase in the quantity demanded of the good.

Answer: E

Diff: 2 Type: MC

Topic: More Elasticities of Demand

37) Business people speak about cross elasticity of demand without using the actual term.

Which one of the following statements reflects cross elasticity of demand?

- A) "A price cut won't help me. It won't increase sales, and I'll just get less money for each unit."
- B) "I don't think a price cut will make any difference to my bottom line. What I may gain from selling more I would lose on the lower price."
- C) "My customers are real bargain hunters. Since I set my prices just a few cents below my competitors, customers have flocked to the store and sales are booming."
- D) "With the recent economic recovery, people have more income to spend and sales are booming, even at the previous prices."
- E) "Since the price of gasoline fell at the neighbouring station, my milk sales have been booming."

Answer: E

Diff: 2 Type: MC

Topic: More Elasticities of Demand

38) Business people speak about income elasticity of demand without using the actual term. Which one of the following statements reflects income elasticity of demand?

- A) "A price cut won't help me. It won't increase sales, and I'll just get less money for each unit."
- B) "I don't think a price cut will make any difference to my bottom line. What I may gain from selling more I would lose on the lower price."
- C) "My customers are real bargain hunters. Since I set my prices just a few cents below my competitors, customers have flocked to the store and sales are booming."
- D) "With the recent economic recovery, people have more income to spend and sales are booming, even at the previous prices."
- E) both A and B

Answer: D

Diff: 2 Type: MC

Topic: More Elasticities of Demand

39) A negative value for

- A) price elasticity of supply implies an upward-sloping supply curve.
- B) cross elasticity of demand implies that the goods are complements.
- C) price elasticity of demand implies an inferior good.
- D) income elasticity of demand implies a normal good.
- E) income elasticity of demand implies an error in your calculation.

Answer: B

Diff: 2 Type: MC

Topic: More Elasticities of Demand

Source: Study Guide

40) If Mr. Brown's income increases by 12 percent and as a result his quantity demanded of music downloads increases by 4 percent, Mr. Brown's income elasticity of demand for music downloads is

- A) 3.0.
- B) 0.33.
- C) -0.33.
- D) -3.0.
- E) 48.0.

Answer: B

Diff: 2 Type: MC

Topic: More Elasticities of Demand

- 41) When the price of a bicycle falls from \$220 to \$180 and other things remain the same
- I. the quantity of bicycles demanded increases from 150 to 250 an hour.
  - II. the quantity of skateboards demanded decreases from 125 to 75 an hour.
  - III. the quantity of bicycle helmets demanded increases from 170 to 230 an hour.

Bicycle helmets and bicycles are \_\_\_\_\_ because a fall in the price of a bicycle brings \_\_\_\_\_ in the quantity demanded of bicycle helmets. The cross elasticity of demand for bicycle helmets with respect to bicycles is \_\_\_\_\_.

- A) complements; an increase; -1.5
- B) substitutes; a decrease; 1.5
- C) substitutes; an increase; -0.67
- D) complements; a decrease; 0.67
- E) complements; an increase; 1.5

Answer: A

Type: MC

Topic: More Elasticities of Demand

Source: MyEconLab

- 42) When Erika's income increases by 6 percent, her demand for tickets to professional hockey games increases by 3 percent. Erika's demand for tickets is income \_\_\_\_\_. For Erika, hockey tickets are \_\_\_\_\_ good.

- A) elastic; a normal
- B) inelastic; an inferior
- C) elastic; an inferior
- D) inelastic; a normal
- E) inelastic; a normative

Answer: D

Type: MC

Topic: More Elasticities of Demand

Source: MyEconLab

- 43) When the price of a bicycle falls from \$220 to \$180 and other things remain the same
- I. the quantity demanded of bicycles increases from 150 to 250 an hour
  - II. the quantity demanded of skateboards decreases from 125 to 75 an hour
  - III. the quantity demanded of bicycle helmets increases from 170 to 230 an hour.

Skateboards and bicycles are \_\_\_\_\_ because a fall in the price of a bicycle brings \_\_\_\_\_ in the quantity demanded of skateboards. The cross elasticity of demand for skateboards with respect to bicycles is \_\_\_\_\_.

- A) complements; an increase; -0.4
- B) complements; a decrease; 0.4
- C) substitutes; an increase; -2.5
- D) substitutes; a decrease; 2.5
- E) substitutes; a decrease; 0.4

Answer: D

Type: MC

Topic: More Elasticities of Demand

Source: MyEconLab

44) Suppose Clyde always eats ice cream and chocolate syrup together. If the price of syrup increases by 10 percent, and the cross elasticity of demand is -2, the quantity of ice cream demanded

- A) increases by 5 percent.
- B) increases by 20 percent.
- C) decreases by 5 percent.
- D) decreases by 20 percent.
- E) decreases by 2 percent.

Answer: D

Type: MC

45) If the cross elasticity of demand between two goods is -0.56, then a fall in the price of one good leads to a \_\_\_\_\_ shift in the \_\_\_\_\_ curve of the other good.

- A) rightward; demand
- B) rightward; supply
- C) leftward; demand
- D) leftward; supply
- E) rightward; demand curve and the supply

Answer: A

Type: MC

46) In the nation of Transporta, the income elasticity of demand for used cars is -2.66. If incomes in this nation increase by 10 percent,

- A) the quantity of used cars demanded increase by 26.6 percent.
- B) used cars will be normal goods.
- C) the quantity of used cars demanded decrease by 26.6 percent.
- D) the demand curve for used cars shifts rightward.
- E) the supply curve of used cars shifts rightward.

Answer: C

Type: MC

47) All normal goods have

- A) an income elasticity of demand greater than 1.0.
- B) a price elasticity of demand greater than 1.0.
- C) a negative price elasticity of demand.
- D) a positive income elasticity of demand.
- E) a negative cross elasticity of demand

Answer: A

Type: MC

### 4.3 Elasticity of Supply

1) The elasticity of supply is a units-free measure of the responsiveness of the

- A) quantity demanded to a change in supply.
- B) quantity supplied to a change in demand.
- C) quantity supplied to a change in price.
- D) price of one good to a change in the quantity supplied of a second good.
- E) quantity supplied of one good to a change in the price of another good.

Answer: C

Diff: 1 Type: MC

Topic: Elasticity of Supply

2) Supply is elastic if

- A) a small percentage change in price results in a large percentage change in quantity supplied.
- B) a large percentage change in price results in a small percentage change in quantity supplied.
- C) a small percentage change in demand results in a large percentage change in quantity supplied.
- D) the good is an inferior good.
- E) the good is a normal good.

Answer: A

Diff: 1 Type: MC

Topic: Elasticity of Supply

3) If a large percentage fall in the price of good A results in a small percentage decrease in the quantity supplied, then

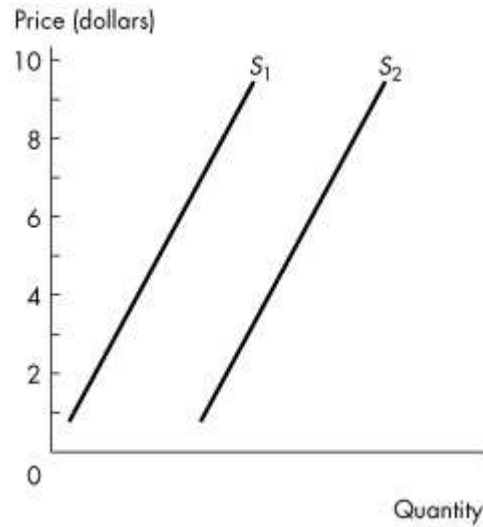
- A) demand is elastic.
- B) demand is inelastic.
- C) demand is income inelastic.
- D) supply is inelastic.
- E) supply is elastic.

Answer: D

Diff: 1 Type: MC

Topic: Elasticity of Supply

Use the figure below to answer the following question.



**Figure 4.3.1**

- 4) The two supply curves in Figure 4.3.1 are parallel. Between \$7 to \$8,
- A)  $S_1$  is more elastic than  $S_2$ .
  - B)  $S_1$  is more inelastic than  $S_2$ .
  - C)  $S_1$  and  $S_2$  have the same elasticity.
  - D)  $S_1$  is steeper than  $S_2$ .
  - E)  $S_1$  is flatter than  $S_2$ .

Answer: A

Diff: 3 Type: MC

Topic: Elasticity of Supply

- 5) If a rise in the price of good A from \$9 to \$11 results in an increase from 9,500 to 10,500 units supplied, then
- A) supply is elastic.
  - B) supply is inelastic.
  - C) supply is unit elastic.
  - D) demand is elastic.
  - E) supply is perfectly inelastic.

Answer: B

Diff: 2 Type: MC

Topic: Elasticity of Supply

6) If a rise in the price of good A from \$9 to \$11 results in an increase in quantity supplied from 4,000 to 6,000 units, the elasticity of supply is

- A) 0.5.
- B) 0.8.
- C) 1.0.
- D) 2.0.
- E) 20.0.

Answer: D

Diff: 2 Type: MC

Topic: Elasticity of Supply

7) If a 10 percent increase in price results in a 9 percent increase in quantity supplied,

- A) the good is a normal good.
- B) the good is an inferior good.
- C) supply is unit elastic.
- D) supply is inelastic.
- E) supply is elastic.

Answer: D

Diff: 2 Type: MC

Topic: Elasticity of Supply

8) If a 10 percent increase in price results in an 18 percent increase in quantity supplied, the elasticity of supply is

- A) 0.3.
- B) 0.6.
- C) 1.2.
- D) 1.8.
- E) 9.0.

Answer: D

Diff: 2 Type: MC

Topic: Elasticity of Supply

9) Suppose the price of a television set rises by 10 percent. Which one of the following would we expect to be the most elastic following such a price change?

- A) the momentary supply of television sets
- B) the short-run supply of television sets
- C) the long-run supply of television sets
- D) the momentary demand for television sets
- E) the normal demand for television sets

Answer: C

Diff: 1 Type: MC

Topic: Elasticity of Supply

10) A vertical supply curve

- A) is impossible except in the long run.
- B) implies an elasticity of supply equal to zero.
- C) implies an elasticity of supply equal to infinity.
- D) indicates that suppliers are unwilling to produce the good.
- E) indicates a shortage of the good.

Answer: B

Diff: 2 Type: MC

Topic: Elasticity of Supply

11) A horizontal supply curve

- A) is impossible except in the long run.
- B) implies an elasticity of supply equal to zero.
- C) implies an elasticity of supply equal to infinity.
- D) indicates that suppliers are unwilling to produce the good.
- E) indicates there is a fixed quantity of the good that can be supplied.

Answer: C

Diff: 1 Type: MC

Topic: Elasticity of Supply

12) Short-run supply is

- A) more elastic than momentary supply but less elastic than long-run supply.
- B) less elastic than momentary supply but more elastic than long-run supply.
- C) less elastic than both momentary and long-run supply.
- D) more elastic than both momentary and long-run supply.
- E) as elastic as either the momentary or the long-run supply.

Answer: A

Diff: 1 Type: MC

Topic: Elasticity of Supply

13) Supply is inelastic if

- A) a small percentage change in price results in a large percentage change in quantity supplied.
- B) a large percentage change in price results in a small percentage change in quantity supplied.
- C) the good is a normal good.
- D) the good is an inferior good.
- E) the good has many substitutes.

Answer: B

Diff: 2 Type: MC

Topic: Elasticity of Supply

14) If a rise in the price of good A from \$100 to \$120 results in an increase in quantity supplied from 10,000 to 12,000 units, then the elasticity of supply is

- A) 0.625.
- B) 0.8.
- C) 1.25.
- D) 0.2.
- E) 1.0.

Answer: E

Diff: 1 Type: MC

Topic: Elasticity of Supply

15) Long-run supply is

- A) more elastic than momentary supply but less elastic than short-run supply.
- B) less elastic than momentary supply but more elastic than short-run supply.
- C) less elastic than both momentary and short-run supply.
- D) more elastic than both momentary and short-run supply.
- E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: Elasticity of Supply

Source: Study Guide

16) A sudden, end-of-summer heat wave increases the demand for air conditioners and catches suppliers with no reserve inventories. The momentary supply for air conditioners is

- A) perfectly elastic.
- B) perfectly inelastic.
- C) elastic.
- D) shown by an upward-sloping curve.
- E) shown by a horizontal curve.

Answer: B

Diff: 2 Type: MC

Topic: Elasticity of Supply

Source: Study Guide

17) When price rises from \$1.50 to \$2.50, quantity supplied increases from 9,000 to 11,000 units. What is the price elasticity of supply?

- A) 0.4
- B) 0.8
- C) 2.5
- D) 4.0
- E) -0.4

Answer: A

Diff: 2 Type: MC

Topic: Elasticity of Supply

Source: Study Guide

18) Preferences for brussels sprouts increase. The price of brussels sprouts will not change if the price elasticity of

- A) demand is 0.
- B) demand is 1.
- C) supply is 0.
- D) supply is 1.
- E) supply is infinity.

Answer: E

Diff: 3 Type: MC

Topic: Elasticity of Supply

Source: Study Guide

19) The elasticity of supply for airplane travel one year in advance of the departure date is most likely to be

- A) substantially lower than -1.
- B) between -1 and zero.
- C) between zero and 1.
- D) around 1.
- E) substantially greater than 1.

Answer: E

Diff: 2 Type: MC

Topic: Elasticity of Supply

20) The elasticity of supply for airplane travel one day in advance of the departure date is most likely to be

- A) substantially lower than -1.
- B) between -1 and zero.
- C) between zero and 1.
- D) around 1.
- E) substantially greater than 1.

Answer: C

Diff: 2 Type: MC

Topic: Elasticity of Supply

21) Goods that can be produced using rare productive resources have a \_\_\_\_\_ elasticity of supply. The greater the amount of time available after a price change, the \_\_\_\_\_ is the elasticity of supply.

- A) low; smaller
- B) high; greater
- C) high; smaller
- D) low; greater
- E) high; more inelastic

Answer: D

Type: MC

Topic: Elasticity of Supply

Source: MyEconLab

22) You are told that a 5 percent increase in the price of a good increases the quantity supplied by 10 percent after one month. Supply of this good is \_\_\_\_\_. This good is most likely produced using productive resources that are \_\_\_\_\_.

- A) inelastic; plentiful or easily obtained
- B) decreasing; unique or rare
- C) elastic; plentiful or easily obtained
- D) unit elastic; unique or rare
- E) elastic; unique or rare

Answer: C

Type: MC

Topic: Elasticity of Supply

Source: MyEconLab

23) In the market for farm crops momentary supply is \_\_\_\_\_. In the market for farm crops, short-run supply is \_\_\_\_\_.

- A) less elastic than short-run supply; less elastic than long-run supply
- B) more elastic than short-run supply; more elastic than long-run supply
- C) negative; positive
- D) positive; negative
- E) perfectly elastic; perfectly inelastic

Answer: A

Type: MC

Topic: Elasticity of Supply

Source: MyEconLab

24) The demand for corn increases. As a result, the price of corn \_\_\_\_\_, and the less elastic the supply of corn, the \_\_\_\_\_ will be the effect on the price.

- A) falls; smaller
- B) falls; greater
- C) rises; smaller
- D) rises; greater
- E) None of the above because the change in the price is effected by the price elasticity of demand.

Answer: D

Type: MC

25) If the supply curve passes through the origin, then the price elasticity of supply is \_\_\_\_\_.

- A) zero
- B) 1
- C) -1
- D) greater than 1
- E) less than 1 but greater than zero

Answer: B

Type: MC

## Chapter 5 Efficiency and Equity

## 5.1 Resource Allocation Methods

1) When a market price allocates a scarce resource

- A) everyone in the economy can use the resource.
- B) only those who show interest can use the resource.
- C) willingness-to-pay is not an issue.
- D) ability to pay for the resource is less important than willingness-to-pay.
- E) only those who are willing and able to pay get the resource.

Answer: E

Diff: 1 Type: MC

Topic: Resource Allocation Methods

2) In a command system, resources are allocated by

- A) people who show interest to use the resources.
- B) people who are able to pay for the resources.
- C) market price.
- D) the order of someone in authority.
- E) those people who come first in line.

Answer: D

Diff: 1 Type: MC

Topic: Resource Allocation Methods

3) In the Canadian economy, the command system

- A) is not used at all.
- B) is used occasionally inside firms and government departments.
- C) is used only by private companies.
- D) is used extensively in place of markets.
- E) is used extensively inside firms and government departments.

Answer: E

Diff: 1 Type: MC

Topic: Resource Allocation Methods

4) Majority rule allocates resources in the way that

- A) politicians choose.
- B) a majority of voters choose.
- C) democracies choose.
- D) all voters choose.
- E) the military chooses.

Answer: B

Diff: 1 Type: MC

Topic: Resource Allocation Methods

- 5) A contest allocates resources to
- A) a winner or a group of winners.
  - B) an athlete.
  - C) a gambler.
  - D) the government.
  - E) private firms.

Answer: A

Diff: 1 Type: MC

Topic: Resource Allocation Methods

- 6) Contests do a good job in resource allocation
- A) under any circumstances.
  - B) when the efforts of the players are easy to monitor and reward directly.
  - C) when the efforts of the players are hard to monitor and reward directly.
  - D) when the first-come, first-served allocation method has failed.
  - E) only under a command system.

Answer: C

Diff: 1 Type: MC

Topic: Resource Allocation Methods

- 7) The first-come, first-served method of resource allocation allocates resources to
- A) the wealthiest.
  - B) people who are willing to take risks.
  - C) people who are not willing to take risks.
  - D) the first in line.
  - E) honest, hard-working people.

Answer: D

Diff: 1 Type: MC

Topic: Resource Allocation Methods

- 8) Lotteries allocate resources to
- A) those who work for the government.
  - B) those who come up lucky in a gaming system.
  - C) those who work for private firms.
  - D) people who are employed by gaming corporations.
  - E) those who are in command.

Answer: B

Diff: 1 Type: MC

Topic: Resource Allocation Methods

9) Lotteries work best

- A) under any circumstances.
- B) under the first-come, first served allocation method.
- C) when there is no effective way to distinguish among potential users of a scarce resource.
- D) when potential users of scarce resources are unknown.
- E) under a command system.

Answer: C

Diff: 1 Type: MC

Topic: Resource Allocation Methods

10) When a scarce resource is allocated to someone who is the winner, the method of resource allocation is

- A) a lottery.
- B) a contest.
- C) first-come, first-served.
- D) force.
- E) personal characteristics.

Answer: B

Diff: 1 Type: MC

Topic: Resource Allocation Methods

11) What method of resource allocation depends on willingness-to-pay and ability-to-pay?

- A) command
- B) lottery
- C) market price
- D) first-come, first-served
- E) force

Answer: C

Diff: 1 Type: MC

Topic: Resource Allocation Methods

12) At West, recognized as the "jewel in Vancouver's culinary crown", reservations are essential. At Le Bistro Chez Michel, a restaurant in North Vancouver, reservations are recommended. At Vij's, a restaurant not too far from the University of British Columbia, reservations are not accepted.

West allocates scarce table resources by \_\_\_\_\_, Le Bistro Chez Michel allocates scarce table resources by \_\_\_\_\_, and Vij's allocates scarce table resources by \_\_\_\_\_.

- A) market price; market price and force; force
- B) personal characteristics; personal characteristics and first-come, first-served; first-come, first-served
- C) a command system; a combination of a command system and first-come, first-served; first-come, first-served
- D) first-come, first-served; first-come, first-served; first-come, first-served
- E) personal characteristics; personal characteristics; first-come, first-served

Answer: D

Diff: 1 Type: MC

Topic: Resource Allocation Methods

Source: MyEconLab

13) Restaurants don't use market price to allocate their tables because \_\_\_\_\_.

- A) they would have to watch the price of a table at other restaurants to keep competitive
- B) restaurants would have to advertise the price
- C) the price of a table would fluctuate hourly, customer uncertainty would deter patrons, and lower demand would bring lower profit
- D) they would have to continually change the supply of tables to keep the price constant
- E) the price of a table would eventually fall to zero and restaurants would incur a loss

Answer: C

Diff: 1 Type: MC

Topic: Resource Allocation Methods

Source: MyEconLab

14) Which of the following is true?

- A) When resources are allocated on the basis of personal characteristics, all people who are willing and able to pay the price get the resource.
- B) When the range of activities to be monitored is large and complex, a command system allocates resources better than a market price.
- C) When a market price allocates resources, some people who are willing and able to pay that price don't get the resource.
- D) Force provides the state with an effective method of transferring wealth from the rich to the poor.
- E) When resources are allocated by force, people with the "right" characteristics get the resources.

Answer: D

Type: MC

- 15) As a method of resource allocation, force
- A) plays a crucial negative role but not a positive role.
  - B) plays a crucial positive role but not a negative role.
  - C) plays a crucial role for both good and ill.
  - D) is always better than majority rule.
  - E) is always better than first-come, first-served.

Answer: C

Type: MC

16) If the owner of an apartment building rents only to married couples over the age of 30, the method of resource allocation is

- A) majority rule.
- B) contest.
- C) personal characteristics.
- D) market price.
- E) force.

Answer: C

Type: MC

## 5.2 Benefit, Cost, and Surplus

1) Choose the statement or statements that are correct.

- I. The value of one more unit of a good or service is its marginal benefit.
- II. Marginal benefit equals the total amount we spend on a good or service.
- III. Marginal benefit is the maximum amount willingly paid for another unit of a good or service.

- A) I only.
- B) II only.
- C) I and III.
- D) III only.
- E) I, II, and III.

Answer: C

Diff: 3 Type: MC

Topic: Benefit, Cost, and Surplus

2) The demand curve for a good is the same as the

- A) marginal cost curve of that good.
- B) marginal benefit curve for that good.
- C) consumer surplus curve of that good.
- D) production possibilities frontier (*PPF*).
- E) none of the above.

Answer: B

Diff: 1 Type: MC

Topic: Benefit, Cost, and Surplus

3) What is the consumer surplus for the market from the production of the 100th unit of a good?

- A) the marginal social cost of the 100th unit
- B) the marginal social benefit from the 100th unit
- C) the opportunity cost of producing the 100th unit
- D) the marginal social benefit from the 100th unit minus the marginal social cost of the 100th unit
- E) the marginal social benefit from the 100th unit minus the price paid for the 100th unit

Answer: E

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

4) Except for the very last unit of a good sold, the price paid by consumers of that good for an additional unit is

- A) less than the marginal social benefit from that unit.
- B) more than the marginal social benefit from that unit.
- C) less than the marginal social cost of producing that unit.
- D) less than the opportunity cost of producing that unit.
- E) equal to consumer surplus.

Answer: A

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

5) A new car has a sticker price of \$35,000. Fred decided that he would pay no more than \$32,000 for this car. He bought the car for \$31,000. Fred obtained a consumer surplus of

- A) \$35,000.
- B) \$32,000.
- C) \$4,000.
- D) \$3,000.
- E) \$1,000.

Answer: E

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

6) A used truck has a sticker price of \$21,000. Arthur decided that he would pay no more than \$19,500 for this truck. He bought the truck for \$19,250. Arthur obtained a consumer surplus of

- A) \$21,000.
- B) \$19,500.
- C) \$19,250.
- D) \$1,750.
- E) \$250.

Answer: E

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

7) Charlene is willing to pay \$5.00 for a sandwich. If the price of a sandwich is \_\_\_\_\_, Charlene \_\_\_\_\_.

- A) \$4.00; does not receive any consumer surplus
- B) \$4.00; receives a consumer surplus
- C) \$6.00; receives a consumer surplus
- D) \$6.00; receives a marginal cost
- E) \$4.00; receives a producer surplus

Answer: B

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

8) Consumer surplus is

- A) the difference between the maximum price consumers are willing to pay and the minimum price producers are willing to accept.
- B) the excess of the benefit received from a good over the amount paid for it.
- C) the total value to consumers of a good.
- D) equal to the area under the demand curve.
- E) the total amount paid for a good.

Answer: B

Diff: 1 Type: MC

Topic: Benefit, Cost, and Surplus

Source: Study Guide

9) An oil painting has an opportunity cost of \$1,000. The painting was purchased for \$1,500. How much consumer surplus did the *buyer* obtain?

- A) \$1,500
- B) \$1,000
- C) \$500
- D) zero
- E) cannot be determined from the information given

Answer: E

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

10) The maximum price a consumer is willing to pay for a good is the

- A) consumer surplus.
- B) value of the good.
- C) opportunity cost of producing the good.
- D) minimum supply-price.
- E) marginal cost of the good.

Answer: B

Diff: 1 Type: MC

Topic: Benefit, Cost, and Surplus

Source: Study Guide

11) The market for strawberries is perfectly competitive. Joe and Haley are consuming the same amount of strawberries, but Joe's demand is much more elastic than Haley's. Which statement is true?

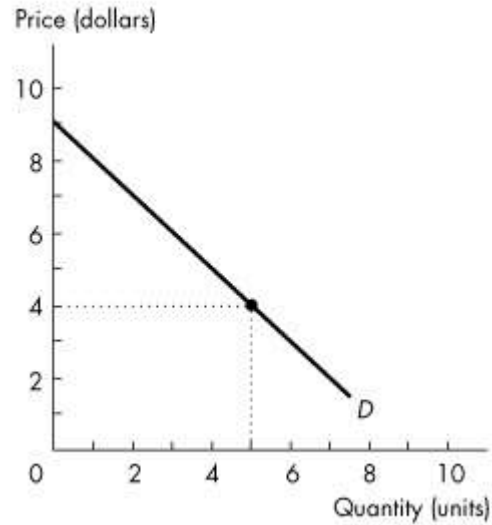
- A) Joe's consumer surplus exceeds Haley's.
- B) Haley's consumer surplus equals Joe's.
- C) Haley's consumer surplus exceeds Joe's.
- D) In comparing consumer surpluses, no statement can be made.
- E) Any comparison of consumer surplus depends on the price of strawberries.

Answer: C

Diff: 3 Type: MC

Topic: Benefit, Cost, and Surplus

Use the figure below to answer the following questions.



**Figure 5.2.1**

12) Consider the demand curve in Figure 5.2.1. What is the value of the first unit of the good?

- A) \$10
- B) \$9
- C) \$8
- D) \$5
- E) \$4

Answer: C

Diff: 1 Type: MC

Topic: Benefit, Cost, and Surplus

Source: Study Guide

13) Consider the demand curve in Figure 5.2.1. If the price of the good is \$4, what is the consumer surplus?

- A) \$32.50
- B) \$25.00
- C) \$20.00
- D) \$12.50
- E) none of the above

Answer: D

Diff: 1 Type: MC

Topic: Benefit, Cost, and Surplus

Source: Study Guide

14) Consider Figure 5.2.1. If the price is \$4, what is the consumer surplus from the third unit of the good?

- A) \$0
- B) \$1
- C) \$2
- D) \$3
- E) \$4

Answer: C

Diff: 1 Type: MC

Topic: Benefit, Cost, and Surplus

15) Consider Figure 5.2.1. When the price is \$4, what is the consumer surplus from the second unit of the good?

- A) \$7
- B) \$3
- C) \$4
- D) \$1
- E) \$10

Answer: B

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

16) Bill and Ted each consume 15 chocolate bars at the current price. If Bill's demand for chocolate bars is more elastic than Ted's demand, then

- A) Bill's willingness to pay for the last chocolate bar is greater than Ted's.
- B) Ted's willingness to pay for the last chocolate bar is greater than Bill's.
- C) Bill's consumer surplus is greater than Ted's.
- D) Ted's consumer surplus is greater than Bill's.
- E) Bill's consumer surplus equals Ted's.

Answer: D

Diff: 3 Type: MC

Topic: Benefit, Cost, and Surplus

17) When demand is perfectly elastic, then consumer surplus is

- A) infinite.
- B) zero.
- C) 1.00.
- D) -1.00.
- E) between zero and 1.00.

Answer: B

Diff: 3 Type: MC

Topic: Benefit, Cost, and Surplus

18) Consumer surplus is

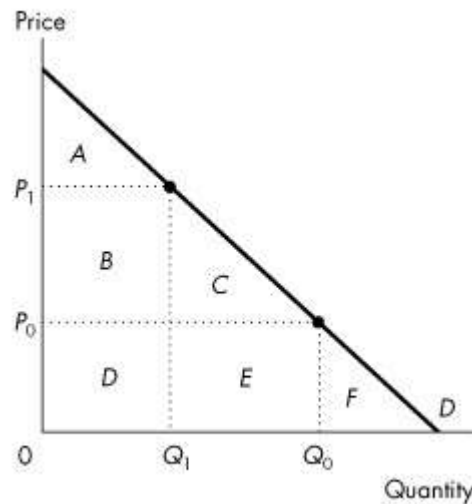
- A) the difference between the market price of the good and the cost of the good.
- B) greater on the last unit sold than on the first unit sold.
- C) greater on the first unit sold than on the last unit sold.
- D) equal to price multiplied by quantity sold.
- E) equal to the area below the demand curve.

Answer: C

Diff: 1 Type: MC

Topic: Benefit, Cost, and Surplus

Use the figure below to answer the following questions.



**Figure 5.2.2**

19) Refer to Figure 5.2.2. If the price is  $P_0$ , consumer surplus is

- A) A.
- B) B plus C.
- C) D plus E.
- D) A plus B plus C.
- E) A plus B plus C plus D plus E.

Answer: D

Diff: 1 Type: MC

Topic: Benefit, Cost, and Surplus

20) Refer to Figure 5.2.2 If the price is  $P_1$ , consumer surplus is

- A) A.
- B) B plus C.
- C) D plus E.
- D) A plus B plus C.
- E) A plus B plus C plus D plus E.

Answer: A

Diff: 1 Type: MC  
Topic: Benefit, Cost, and Surplus

21) Refer to Figure 5.2.2. If the price rises from  $P_0$  to  $P_1$ , the change in consumer surplus is

- A)  $A$ .
- B)  $B$  plus  $C$ .
- C)  $D$  plus  $E$ .
- D)  $A$  plus  $B$  plus  $C$ .
- E)  $A$  plus  $B$  plus  $C$  plus  $D$  plus  $E$ .

Answer: B

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

22) Refer to Figure 5.2.2 If the price falls from  $P_1$  to  $P_0$ , then the change in consumer surplus is

- A)  $A$ .
- B)  $A + B$ .
- C)  $A + B + C$ .
- D)  $B + C$ .
- E)  $A + B + D$ .

Answer: D

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

23) Refer to Figure 5.2.2. If the price is  $P_0$ , then the value of the last unit consumed is

- A)  $P_0$ .
- B)  $P_1$ .
- C) equal to area  $A + B + C$ .
- D) 0.
- E)  $P_1 - P_0$ .

Answer: A

Diff: 1 Type: MC

Topic: Benefit, Cost, and Surplus

24) Consumer surplus

- A) will definitely be low for inexpensive goods.
- B) will definitely be high for inexpensive goods.
- C) will definitely be low for expensive goods.
- D) will definitely be high for expensive goods.
- E) may be low or high for any type of good, expensive or inexpensive, depending on the characteristics of demand.

Answer: E

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

25) Market demand is the

- A) sum of the prices that each individual is willing to pay for each quantity demanded.
- B) sum of the quantity demanded by each individual at each price.
- C) sum of the consumer surplus of each individual.
- D) difference between the maximum amount each individual is willing to pay for a good and the market price.
- E) difference between the market price and the maximum amount each individual is willing to pay for a good.

Answer: B

Diff: 1 Type: MC

Topic: Benefit, Cost, and Surplus

Source: Study Guide

26) Sally and Eric are the only people in an economy. Sally buys 3 bottles of water when the price is \$2 a bottle and 4 bottles of water when the price is \$1 a bottle. Eric buys 10 bottles of water when the price is \$0.50 a bottle and 5 bottles of water when the price is \$1 a bottle. In the market for water, the quantity demanded \_\_\_\_\_.

- A) increases as the price rises
- B) is 4 bottles at a price of \$1 a bottle
- C) increases as the price falls
- D) is 8 bottles at a price of \$2 a bottle
- E) is 15 bottles at a price of \$0.50 a bottle

Answer: C

Diff: 1 Type: MC

Topic: Benefit, Cost, and Surplus

Source: MyEconLab

27) If we produce one more bottle of water

- A) we cannot be acting efficiently.
- B) we incur a marginal cost.
- C) we must move away from market equilibrium.
- D) the price of a bottle of water must rise.
- E) the marginal social benefit from bottled water increases.

Answer: B

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

28) Marginal cost

- A) is always less than price.
- B) can be negative.
- C) is the minimum price a producer must receive to induce him to offer one more unit of a good or service for sale.
- D) is greater than price.
- E) decreases as more of a good or service is produced.

Answer: C

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

- 29) A supply curve is
- A) the same as a production possibilities frontier.
  - B) a marginal social benefit curve.
  - C) a marginal benefit curve.
  - D) a marginal cost curve.
  - E) a downward-sloping curve.

Answer: D

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

- 30) A market supply curve is
- A) the horizontal sum of the individual supply curves.
  - B) downward sloping.
  - C) the vertical sum of the individual supply curves.
  - D) is downward sloping initially, and then upward sloping.
  - E) is represented by a line with a constant slope.

Answer: A

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

- 31) What is the producer surplus for the market from the production of the 100th unit of a good?
- A) the marginal cost of producing the 100th unit
  - B) the marginal benefit from the 100th unit
  - C) the opportunity cost of producing the 100th unit
  - D) the marginal social benefit from the 100th unit minus the marginal cost of producing the 100th unit
  - E) the price paid for the 100th unit minus the marginal social cost of producing the 100th unit

Answer: E

Diff: 3 Type: MC

Topic: Benefit, Cost, and Surplus

- 32) Suppose that the Hot Dog House can produce hotdogs at a constant cost of \$0.25 each. If the Hot Dog House sells hotdogs for \$0.50 each, then the Hot Dog House
- A) receives a producer surplus.
  - B) will raise the price of hot dogs.
  - C) will allow consumers to receive a consumer surplus.
  - D) has no producer surplus.
  - E) has an opportunity cost of \$0.50 a hot dog.

Answer: A

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

33) An oil painting has a marginal cost of \$1,000. The painting was bought for \$1,500. How much producer surplus did the painter obtain?

- A) \$1,500
- B) \$1,000
- C) \$500
- D) zero
- E) cannot be determined from the information given

Answer: C

Diff: 1 Type: MC

Topic: Benefit, Cost, and Surplus

34) Producer surplus is

- A) the difference between the maximum price consumers are willing to pay and the minimum price producers are willing to accept.
- B) the excess of the amount received from the sale of a good or service over the cost of producing it.
- C) equal to the marginal cost of production.
- D) equal to the area under the supply curve.
- E) the total amount paid for the good.

Answer: B

Diff: 1 Type: MC

Topic: Benefit, Cost, and Surplus

35) The marginal cost of producing an additional basket of tomatoes is \$5.00. The consumer is willing to pay a maximum of \$9.00 for an additional basket. A farmer sells a basket of tomatoes for \$6.00 each. The farmer receives a producer surplus from selling an additional basket of tomatoes equal to

- A) \$1.00.
- B) \$3.00.
- C) \$4.00.
- D) \$5.00.
- E) \$9.00.

Answer: A

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

36) The marginal cost of producing one more hot dog is \$1.00. The price of a hot dog is \$1.50. The producer surplus from selling one more hotdog is

- A) \$1.00.
- B) \$1.50.
- C) \$0.50.
- D) zero.
- E) \$2.50.

Answer: C

Diff: 1 Type: MC

Topic: Benefit, Cost, and Surplus

37) Producer surplus is

- A) the value producers place on a good minus the price of the good.
- B) the price of the good minus the value producers place on it.
- C) zero if price equals marginal cost.
- D) greater the more elastic the supply of the good.
- E) none of the above.

Answer: C

Diff: 1 Type: MC

Topic: Benefit, Cost, and Surplus

Use the table below to answer the following questions.

**Table 5.2.1**

Quantity (units)	Marginal Cost (dollars)
1	2
2	3
3	4
4	5

38) Table 5.2.1 gives information on marginal cost for the XYZ firm. If XYZ sells the first unit at a price of \$6, what is the producer surplus on that unit?

- A) \$4
- B) \$6
- C) \$9
- D) \$12
- E) \$7

Answer: A

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

39) Refer to Table 5.2.1. If the price is \$6 a unit, the producer surplus on the third unit is

- A) \$3.
- B) \$6.
- C) \$5.
- D) \$4.
- E) \$2.

Answer: E

Diff: 1 Type: MC

Topic: Benefit, Cost, and Surplus

40) The marginal cost for Morgan's Marvellous Movies is given in the following table:

**Table 5.2.2**

Quantity (number of movies)	Marginal Cost (dollars)
1	4.00
2	4.50
3	5.00
4	5.50
5	6.00

If the firm sells the fifth movie at a price of \$7, what is the producer surplus on that movie?

- A) \$28
- B) \$3
- C) \$7
- D) \$6
- E) \$1

Answer: E

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

41) The marginal cost for Morgan's Marvellous Movies is given in the following table:

**Table 5.2.3**

Quantity (number of movies)	Marginal Cost (dollars)
1	4.00
2	4.50
3	5.00
4	5.50
5	6.00

If the firm sells the first movie at a price of \$7, what is the producer surplus on that movie?

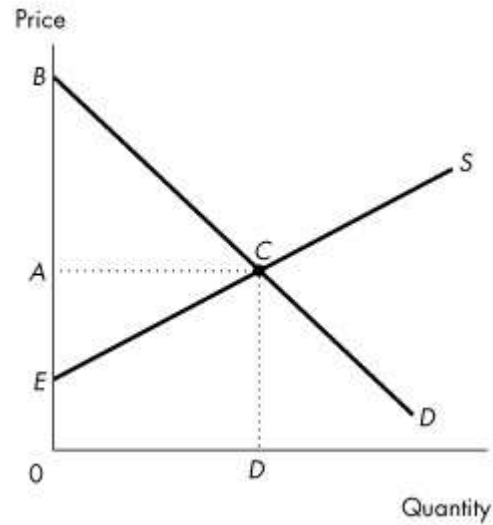
- A) \$28
- B) \$3
- C) \$7
- D) \$6
- E) \$1

Answer: B

Diff: 2 Type: MC

Topic: Benefit, Cost, and Surplus

Use the information below to answer the following question.



**Figure 5.2.3**

42) Consider the demand and supply curves in Figure 5.2.3. If the market is at the competitive equilibrium, which area in the diagram indicates the cost of producing the quantity sold?

- A) *ABC*
- B) *AEC*
- C) *EBC*
- D) *OBCD*
- E) *OECD*

Answer: E

Diff: 1 Type: MC

Topic: Benefit, Cost, and Surplus

Source: Study Guide

43) Sal likes to eat pizza. The \_\_\_\_\_ is the maximum amount that Sal is willing to pay for one more slice of pizza.

- A) market price
- B) marginal cost
- C) consumer surplus
- D) marginal benefit
- E) producer surplus

Answer: D

Type: MC

Table 5.2.4

Price (dollars per slice)	Abby's quantity demanded (slices per month)	Barry's quantity demanded (slices per month)
2.50	25	50
3.00	20	40
3.50	15	30
4.00	10	20
4.50	5	10
5.00	0	0

Table 5.2.4 shows the demand schedules for pizza for Abby and Barry who are the only buyers in the market.

44) Refer to Table 5.2.4. What is the marginal social benefit from the 45th slice of pizza?

- A) \$3.50
- B) \$4.00
- C) \$2.50
- D) \$5.00
- E) \$4.50

Answer: A

Type: MC

45) If you increase your consumption of pop by one additional can a week, your marginal benefit from this last can is \$1.00. For you, the \_\_\_\_\_ this last can of pop is \$1.00

- A) price of
- B) marginal cost of
- C) value from
- D) consumer surplus from
- E) producer surplus

Answer: C

Type: MC

46) A market demand curve is constructed by

A) adding the prices all consumers are willing to pay for any given quantity.

B) determining the quantity supplied by all producers at all possible prices.

C) subtracting the quantity supplied by all producers from the quantity demanded by all individuals at each price.

D) adding the quantities demanded by all individuals at each price.

E) subtracting the quantity demanded by all individuals from the quantity supplied by all producers at each price.

Answer: D

Type: MC

### 5.3 Is the Competitive Market Efficient?

1) When the efficient quantity is produced

- A) total consumer surplus is zero.
- B) total producer surplus is zero.
- C) consumer surplus exceeds producer surplus by the greatest possible amount.
- D) producer surplus exceeds consumer surplus by the greatest possible amount.
- E) the sum of consumer surplus and producer surplus is maximized.

Answer: E

Diff: 2 Type: MC

Topic: Is the Competitive Market Efficient?

2) When the efficient quantity is produced

- A) marginal social benefit equals marginal social cost.
- B) the quantity demanded equals the quantity supplied.
- C) resources are used in the activities in which they are most highly valued.
- D) the sum of consumer surplus and producer surplus is maximized.
- E) all of the above.

Answer: E

Diff: 2 Type: MC

Topic: Is the Competitive Market Efficient?

Use the figure below to answer the following questions.

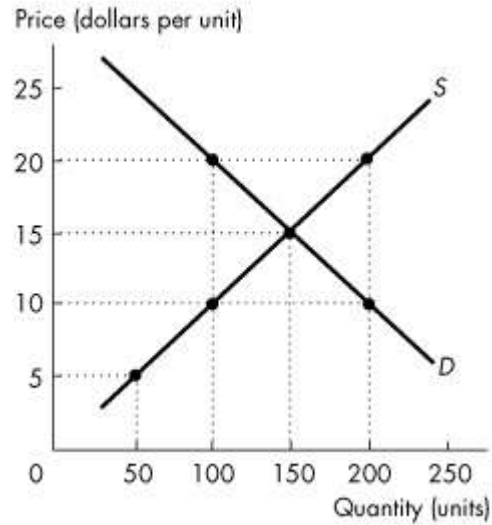


Figure 5.3.1

3) Refer to Figure 5.3.1. The efficient quantity is

- A) 250 units.
- B) 200 units.
- C) 150 units.
- D) 100 units.
- E) 50 units.

Answer: C

Diff: 1 Type: MC

Topic: Is the Competitive Market Efficient?

4) Refer to Figure 5.3.1. At the efficient quantity, the price is

- A) \$20 a unit.
- B) \$15 a unit.
- C) \$10 a unit.
- D) \$5 a unit.
- E) zero.

Answer: B

Diff: 2 Type: MC

Topic: Is the Competitive Market Efficient?

- 5) Refer to Figure 5.3.1. If the quantity produced is 200,
- A) a deadweight loss exists.
  - B) the sum of consumer surplus and producer surplus is maximized.
  - C) production is efficient.
  - D) the sum of consumer surplus and producer surplus is zero.
  - E) deadweight loss is minimized.

Answer: A

Diff: 3 Type: MC

Topic: Is the Competitive Market Efficient?

- 6) Refer to Figure 5.3.1. If the quantity produced is 100,
- A) marginal social benefit exceeds marginal social cost.
  - B) marginal social cost exceeds marginal social benefit.
  - C) production is efficient.
  - D) marginal social benefit is minimized.
  - E) deadweight loss is zero.

Answer: A

Diff: 3 Type: MC

Topic: Is the Competitive Market Efficient?

- 7) Refer to Figure 5.3.1. If the price is \$15 a unit,
- A) production is efficient.
  - B) marginal social benefit equals marginal social cost.
  - C) deadweight loss is zero.
  - D) the sum of consumer surplus and producer surplus is maximized.
  - E) all of the above.

Answer: E

Diff: 2 Type: MC

Topic: Is the Competitive Market Efficient?

- 8) A negative externality results in
- A) underproduction.
  - B) zero production.
  - C) overproduction.
  - D) efficient production.
  - E) zero deadweight loss.

Answer: C

Diff: 2 Type: MC

Topic: Is the Competitive Market Efficient?

9) Which of the following can lead to an inefficient outcome?

- I. Price regulations
- II. Increasing marginal cost
- III. Monopoly

- A) I only
- B) II only
- C) I and III
- D) III only
- E) I, II, and III

Answer: C

Diff: 3 Type: MC

Topic: Is the Competitive Market Efficient?

10) A monopoly leads to

- A) overproduction.
- B) underproduction.
- C) efficient production.
- D) maximization of consumer surplus.
- E) zero deadweight loss.

Answer: B

Diff: 2 Type: MC

Topic: Is the Competitive Market Efficient?

11) Which of the following lead to an inefficient outcome?

- I. Decreasing marginal social benefit
- II. Taxes
- III. High transactions cost

- A) I only
- B) II only
- C) I and III
- D) II and III
- E) I, II and III

Answer: D

Diff: 3 Type: MC

Topic: Is the Competitive Market Efficient?

12) Choose the correct statement.

- A) Producer surplus is an external cost.
- B) Consumer surplus is an external benefit.
- C) A government subsidy paid to a producer is an external benefit.
- D) Consumer surplus is an external cost.
- E) Subsidies lead to overproduction.

Answer: E

Diff: 3 Type: MC

Topic: Is the Competitive Market Efficient?

- 13) Suppose the market for diamonds is a monopoly. We can expect
- A) underproduction of diamonds.
  - B) overproduction of diamonds.
  - C) marginal social benefit to equal marginal social cost in the diamond market.
  - D) an efficient quantity of diamonds.
  - E) the allocation of diamonds to be first-come, first-served.

Answer: A

Diff: 3 Type: MC

Topic: Is the Competitive Market Efficient?

- 14) Consider the market for hot dogs. If this market becomes a monopoly, then there will be
- A) underproduction of hot dogs.
  - B) overproduction of hot dogs.
  - C) a deadweight loss in the market for hot dogs.
  - D) an efficient quantity of hot dogs.
  - E) both A and C are correct.

Answer: E

Diff: 3 Type: MC

Topic: Is the Competitive Market Efficient?

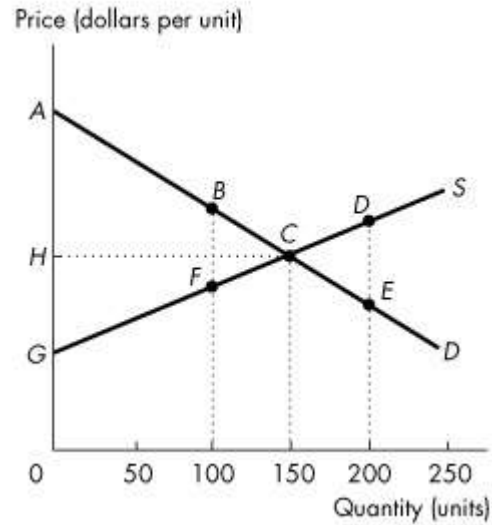
- 15) When a deadweight loss occurs in a market, we can be certain that
- A) taxes have been imposed in the market.
  - B) the market is a monopoly.
  - C) there is underproduction in the market.
  - D) the entire economy experiences a loss.
  - E) both A and C.

Answer: D

Diff: 2 Type: MC

Topic: Is the Competitive Market Efficient?

Use the figure below to answer the following questions.



**Figure 5.3.2**

16) Refer to Figure 5.3.2. If the level of output is 150 units, the consumer surplus is area

- A) *BCF*.
- B) *ACG*.
- C) *DCE*.
- D) *ACH*.
- E) *HCG*.

Answer: D

Diff: 2 Type: MC

Topic: Is the Competitive Market Efficient?

17) Refer to Figure 5.3.2. If the level of output is 150 units, the producer surplus is area

- A) *BCF*.
- B) *ACG*.
- C) *DCE*.
- D) *ACH*.
- E) *HCG*.

Answer: E

Diff: 2 Type: MC

Topic: Is the Competitive Market Efficient?

18) Refer to Figure 5.3.2. If the level of output is 100 units, the deadweight loss is area

- A) *BCF*.
- B) *ACG*.
- C) *DCE*.
- D) *ACH*.
- E) *HCG*.

Answer: A

Diff: 3 Type: MC

Topic: Is the Competitive Market Efficient?

19) Refer to Figure 5.3.2. If the level of output is 200 units, the deadweight loss is area

- A) *BCF*.
- B) *ACG*.
- C) *DCE*.
- D) *ACH*.
- E) *HCG*.

Answer: C

Diff: 3 Type: MC

Topic: Is the Competitive Market Efficient?

20) An external cost

- A) is a marginal benefit.
- B) results in underproduction.
- C) is a payment from the government to a producer.
- D) is a cost that affects someone other than the seller.
- E) is a payment from a producer to the government.

Answer: D

Diff: 1 Type: MC

Topic: Is the Competitive Market Efficient?

21) If production is not at an efficient level, which of the following *must* be true?

- A) Marginal social benefit exceeds marginal social cost.
- B) Marginal social cost exceeds marginal social benefit.
- C) Production will increase.
- D) Production will decrease.
- E) none of the above

Answer: E

Diff: 1 Type: MC

Topic: Is the Competitive Market Efficient?

Source: Study Guide

22) In competitive equilibrium, which of the following statements is *false*?

- A) Marginal social benefit equals marginal social cost.
- B) Willingness to pay equals marginal cost of production.
- C) The sum of consumer surplus and producer surplus is maximized.
- D) Deadweight loss is maximized.
- E) Resources are used efficiently to produce goods and services that people value most highly.

Answer: D

Diff: 1 Type: MC

Topic: Is the Competitive Market Efficient?

Source: Study Guide

23) If resources are allocated efficiently,

- A) consumer surplus exceeds producer surplus.
- B) producer surplus exceeds consumer surplus.
- C) the sum of consumer surplus and producer surplus is maximized.
- D) marginal social benefit is maximized.
- E) marginal social cost is minimized.

Answer: C

Diff: 1 Type: MC

Topic: Is the Competitive Market Efficient?

Source: Study Guide

24) Markets may not achieve an efficient allocation of resources when there are

- A) public goods.
- B) external benefits.
- C) monopolies.
- D) subsidies.
- E) all of the above.

Answer: E

Diff: 1 Type: MC

Topic: Is the Competitive Market Efficient?

Source: Study Guide

25) Overproduction of a good means that

- A) deadweight loss has been eliminated.
- B) the sum of consumer surplus and producer surplus is greater than the sum for an efficient allocation.
- C) marginal social cost exceeds marginal social benefit.
- D) marginal social benefit exceeds marginal social cost.
- E) this is a public good.

Answer: C

Diff: 1 Type: MC

Topic: Is the Competitive Market Efficient?

Source: Study Guide

- 26) Deadweight loss is
- A) borne entirely by consumers.
  - B) gained by producers.
  - C) the social loss from inefficiency.
  - D) not a problem with overproduction.
  - E) all of the above.

Answer: C

Diff: 1 Type: MC

Topic: Is the Competitive Market Efficient?

Source: Study Guide

- 27) At current output, the marginal social benefit from Furbys is greater than marginal social cost. To achieve an efficient allocation, which of the following must occur? (1) Furby output must increase. (2) Furby output must decrease. (3) the marginal social benefit of Furbys will rise. (4) the marginal social cost of Furbys will fall.

- A) 1 and 3
- B) 1 and 4
- C) 2 and 3
- D) 2 and 4
- E) 1 only

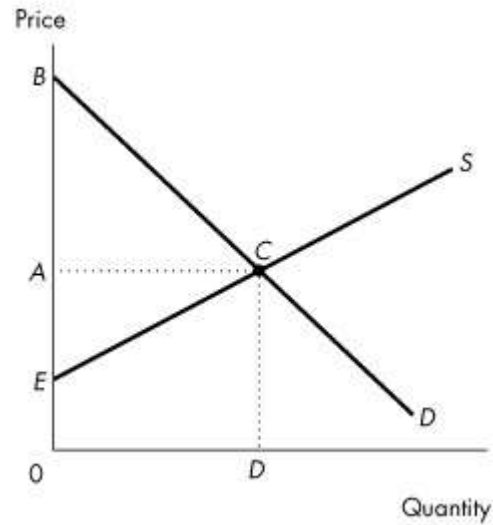
Answer: E

Diff: 1 Type: MC

Topic: Is the Competitive Market Efficient?

Source: Study Guide

Use the information below to answer the following question.



**Figure 5.3.3**

28) Consider the demand and supply curves in Figure 5.3.3. If the market is at the competitive equilibrium, which area in the diagram indicates producer surplus?

- A) *ABC*
- B) *AEC*
- C) *EBC*
- D) *OBCD*
- E) *OECD*

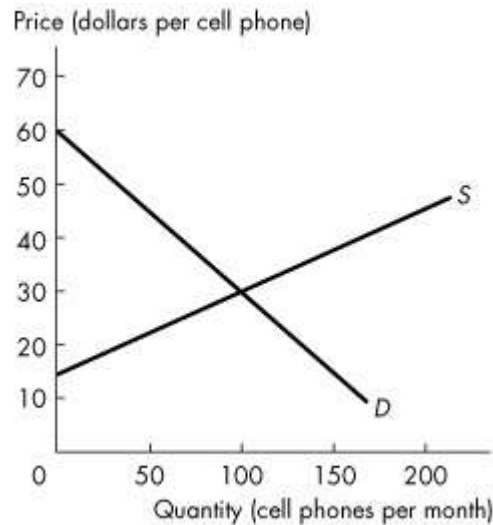
Answer: B

Diff: 1 Type: MC

Topic: Is the Competitive Market Efficient?

Source: Study Guide

Use the figure below to answer the following question.



**Figure 5.3.4**

29) Refer to Figure 5.3.4. The graph shows the market for cell phones. When production is efficient, total surplus is \_\_\_\_\_ and the cost of producing the cell phones sold is \_\_\_\_\_.

- A) \$2,250; \$2,250
- B) \$2,250; \$3,000
- C) \$1,500; \$750
- D) \$750; \$1,500
- E) \$1,500; \$2,250

Answer: A

Diff: 1 Type: MC

Topic: Is the Competitive Market Efficient?

Source: MyEconLab

30) Choose the correct statement.

- A) The competitive market pushes the quantity produced to its efficient level.
- B) When the efficient quantity is produced in a competitive market, consumer surplus is maximized.
- C) Competitive equilibrium occurs when demand equals supply.
- D) When the efficient quantity is produced in a competitive market, producer surplus is maximized.
- E) When the efficient quantity is produced in a competitive market, producer surplus is minimized.

Answer: A

Diff: 1 Type: MC

Topic: Is the Competitive Market Efficient?

Source: MyEconLab

31) All of the following statements are true *except* \_\_\_\_\_.

- A) an externality is a cost or a benefit that affects someone other than the seller or the buyer of a good
- B) when an electric utility does not consider the cost of pollution when it decides how much power to produce, the result is overproduction
- C) an electric utility creates an external cost by burning coal
- D) all externalities create overproduction
- E) an external cost creates overproduction

Answer: D

Diff: 1 Type: MC

Topic: Is the Competitive Market Efficient?

Source: MyEconLab

32) It is efficient to produce an additional shirt if the

- A) marginal social benefit from producing the shirt exceeds zero.
- B) marginal social benefit of producing the shirt equals zero.
- C) consumer surplus from the additional shirt exceeds its producer surplus.
- D) marginal social benefit from producing the shirt is greater than the marginal social cost of producing it.
- E) producer surplus from the additional shirt exceeds its consumer surplus.

Answer: D

Type: MC

33) When 2,000 hamburgers a day are produced, the marginal social benefit from the 2000<sup>th</sup> hamburger is \$1.50 and its marginal social cost is \$1.00. And when 7,500 hamburgers a day are produced, the marginal social benefit from the 2000<sup>th</sup> hamburger is \$1.00 and its marginal social cost is \$1.50. The efficient quantity of hamburgers is \_\_\_\_\_ a day

- A) less than 2,000
- B) between 2,000 and 7,500
- C) more than 7,500
- D) zero
- E) 2,000

Answer: B

Type: MC

#### 5.4 Is the Competitive Market Fair?

1) Which of the following ideas describes the concept of "utilitarianism"?

I. Utilitarianism was introduced in the 1930s.

II. Utilitarians believed that a society should strive to make as many people as happy as possible.

III. Utilitarians claimed that taking money from rich people and giving it to poorer people would not make an economy better off.

A) I only

B) II only

C) I and III

D) II and III

E) I, II, and III

Answer: B

Diff: 2 Type: MC

Topic: Is the Competitive Market Fair?

2) The symmetry principle is based on

A) the idea that income should be redistributed from the rich to the poor.

B) the idea that people in similar situations should be treated similarly.

C) the fact that taxes create a deadweight loss.

D) the idea that markets operate fairly.

E) the idea that there is symmetry between buyers and sellers in a market.

Answer: B

Diff: 1 Type: MC

Topic: Is the Competitive Market Fair?

3) When the cost of making income transfers is recognized, we recognize the big tradeoff between

A) efficiency and fairness.

B) marginal benefit and marginal cost.

C) value and marginal benefit.

D) producer surplus and consumer surplus.

E) deadweight loss and utilitarianism.

Answer: A

Diff: 2 Type: MC

Topic: Is the Competitive Market Fair?

4) A modified version of utilitarianism proposed by John Rawls could be summarized as

A) transfer everything to the poor.

B) transfer everything to the rich.

C) expand the size of government.

D) minimize the size of government.

E) make the poorest as well off as possible.

Answer: E

Diff: 1 Type: MC

Topic: Is the Competitive Market Fair?

5) The essence of philosopher Robert Nozick's proposal is that

- A) fairness works on the basis of fair outcomes.
- B) fairness must be based on fairness of rules.
- C) involuntary exchange is fair.
- D) all of the above.
- E) none of the above.

Answer: B

Diff: 1 Type: MC

Topic: Is the Competitive Market Fair?

6) One big problem with the utilitarian ideal is that it

- A) ignores fairness.
- B) ignores equality.
- C) ignores the costs of making income transfers.
- D) all of the above.
- E) none of the above.

Answer: C

Diff: 2 Type: MC

Topic: Is the Competitive Market Fair?

7) An idea of fairness that emphasizes equality of opportunity is

- A) fair results.
- B) fair rules.
- C) fair incomes.
- D) utilitarianism.
- E) modified utilitarianism.

Answer: B

Diff: 1 Type: MC

Topic: Is the Competitive Market Fair?

Source: Study Guide

8) According to the "big tradeoff,"

- A) income transfers reduce efficiency.
- B) efficiency requires income transfers.
- C) a more equally shared pie results in a larger pie.
- D) property rights and voluntary exchange insure equality of opportunity.
- E) income transfers should make the poorest person as well off as possible.

Answer: A

Diff: 1 Type: MC

Topic: Is the Competitive Market Fair?

Source: Study Guide

- 9) According to John Rawls' modified utilitarianism, income should be redistributed until
- A) incomes are equal.
  - B) opportunities are equal.
  - C) the poorest person is as well off as possible.
  - D) the poorest person is as well off as possible, after incorporating the costs of income transfers.
  - E) the big tradeoff is eliminated.

Answer: D

Diff: 1 Type: MC

Topic: Is the Competitive Market Fair?

Source: Study Guide

- 10) Economists tend to
- A) agree about efficiency and about fairness.
  - B) agree about efficiency but disagree about fairness.
  - C) disagree about efficiency but agree about fairness.
  - D) be more agreeable than philosophers about fairness.
  - E) be more disagreeable than philosophers about fairness.

Answer: B

Diff: 1 Type: MC

Topic: Is the Competitive Market Fair?

Source: Study Guide

- 11) The two big approaches to thinking about fairness are \_\_\_\_\_.
- A) it's not fair if my income is less than yours and it's not fair if my opportunities in life are less than yours
  - B) it's not fair if the result isn't fair and it's not fair if the rules aren't fair
  - C) the fairness of democracy and the fairness of central planning
  - D) the fairness of income equality and the fairness of educational equality
  - E) it's not fair if you are treated unkindly and it's not fair if you treat someone unkindly

Answer: B

Diff: 1 Type: MC

Topic: Is the Competitive Market Fair?

Source: MyEconLab

- 12) The idea of fairness that has been developed to deal with the big tradeoff is the idea that \_\_\_\_\_.

- A) fair distribution of the economic pie is the one that costs the richest person the least amount of money
- B) fair distribution of the economic pie is the one that makes everyone equal
- C) we should treat other people as we would like to be treated
- D) fair distribution of the economic pie is the one that makes the poorest person as well off as possible
- E) we need to make a bigger economic pie

Answer: D

Diff: 1 Type: MC

Topic: Is the Competitive Market Fair?

Source: MyEconLab

- 13) The main idea of fairness is based on which of the following rules?
- a. The state must enforce laws that establish and protect private property.
  - b. Goods and services that produce externalities must be owned by the state, monopolies must be eliminated, and common resources must follow the rules of the competitive market.
  - c. The state must enforce tax laws so that after taxes are paid and benefits are received, the gap between rich and poor is as small as possible.
  - d. Private property may be transferred from one person to another only by voluntary exchange.
- A) Rules a and d.
  - B) Rules b and d.
  - C) Rules b and c.
  - D) Rules a and c.
  - E) The main idea of fairness is not based on any of these rules.

Answer: A

Diff: 1 Type: MC

Topic: Is the Competitive Market Fair?

Source: MyEconLab

14) Sunscreen factories are required to limit production to 100 bottles a day, which is less than the efficient quantity. The 100 bottles could be allocated to beachgoers by \_\_\_\_\_, which is \_\_\_\_\_ by the fair rules idea of fairness and \_\_\_\_\_ by the fair results idea of fairness.

- A) first-come first-served; fair; unfair
- B) personal characteristics; fair; fair
- C) force; unfair; fair
- D) majority rule; fair; fair
- E) first-come first-served; fair; fair

Answer: A

Diff: 1 Type: MC

Topic: Is the Competitive Market Fair?

Source: MyEconLab

15) Suppose the government places a tax on business profits so that businesses decrease production and generate a deadweight loss. Revenues from the tax are used to boost the incomes of the poor. The decision to levy the tax implies that in this case the government

- A) values people but not businesses.
- B) values efficiency more than its view of fairness.
- C) profits from collecting taxes.
- D) values its view of fairness more than efficiency.
- E) is unaware of the deadweight loss it is creating.

Answer: D

Type: MC

## Chapter 6 Government Actions in Markets

### 6.1 A Housing Market with a Rent Ceiling

- 1) The time spent looking for someone with whom to do business is called

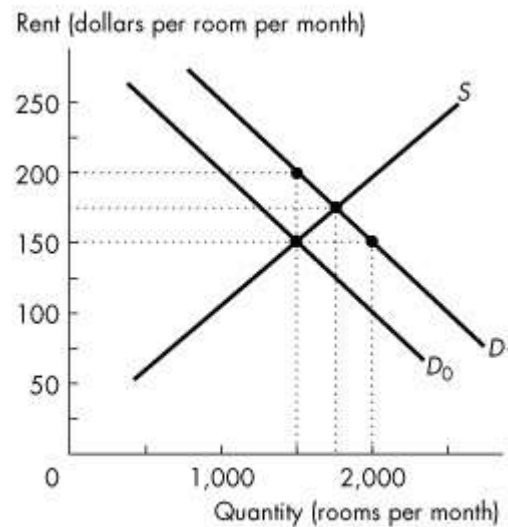
- A) elasticity of time.
- B) market time.
- C) search activity.
- D) opportunity time.
- E) development time.

Answer: C

Diff: 1 Type: MC

Topic: A Housing Market with a Rent Ceiling

Use the figure below to answer the following questions.



**Figure 6.1.1**

2) Consider the market for rental housing illustrated in Figure 6.1.1 when the demand curve is  $D_0$ . The equilibrium in an unregulated market is

- A) 1,500 rooms rented at \$150 a month.
- B) 1,500 rooms rented at \$200 a month.
- C) 1,750 rooms rented at \$175 a month.
- D) 1,750 rooms rented at \$200 a month.
- E) 2,000 rooms rented at \$150 a month.

Answer: A

Diff: 1 Type: MC

Topic: A Housing Market with a Rent Ceiling

3) Refer to Figure 6.1.1. If the demand for rental housing increases and the demand curve shifts rightward from  $D_0$  to  $D_1$ , and the market is unregulated, the number of rooms rented is

- A) 1,500, and the rent rises to \$200 a month.
- B) 2,000, and the rent is at its initial level.
- C) 1,750, and the rent rises to \$175 a month.
- D) 2,000, and the rent rises to \$200 a month.
- E) 1,750, and the rent rises to \$200 a month.

Answer: C

Diff: 1 Type: MC

Topic: A Housing Market with a Rent Ceiling

4) Refer to Figure 6.1.1. If the demand for rental housing increases and the demand curve shifts rightward from  $D_0$  to  $D_1$ , and there is a strictly enforced rent ceiling of \$150 per room,

- A) the number of rooms rented will increase to 2,000.
- B) the number of rooms rented is 1,500.
- C) there is a housing shortage of 500 rooms.
- D) both B and C.
- E) the number of rooms rented decreases to 1,000.

Answer: D

Diff: 2 Type: MC

Topic: A Housing Market with a Rent Ceiling

5) Refer to Figure 6.1.1. Suppose the demand for rental housing is shown by demand curve  $D_1$ , and there is a rent ceiling of \$150 per room. What is the highest rent that would be charged in a black market?

- A) \$150 a month
- B) \$175 a month
- C) \$200 a month
- D) \$100 a month
- E) cannot be determined from the graph, but we know it is greater than \$200

Answer: C

Diff: 3 Type: MC

Topic: A Housing Market with a Rent Ceiling

6) Refer to Figure 6.1.1. Suppose the demand for rental housing is shown by demand curve  $D_1$ , and there is a rent ceiling of \$150 per room. What is the highest amount that would be expended on search activity?

- A) \$200.
- B) \$150.
- C) \$100.
- D) \$50.
- E) \$0.

Answer: D

Diff: 3 Type: MC

Topic: A Housing Market with a Rent Ceiling

7) An illegal market in which the equilibrium price exceeds the price ceiling is

- A) a rental market.
- B) a capital market.
- C) a black market.
- D) an efficient market.
- E) a housing market.

Answer: C

Diff: 1 Type: MC

Topic: A Housing Market with a Rent Ceiling

8) If the government imposes a maximum rent for housing that is above the equilibrium price, then you predict that

- A) the law will have no effect in the market for housing.
- B) the law will generate a shortage of housing.
- C) the law will create a surplus of housing.
- D) the demand curve for housing shifts rightward.
- E) the supply curve of housing shifts leftward.

Answer: A

Diff: 2 Type: MC

Topic: A Housing Market with a Rent Ceiling

9) When a price ceiling is set below the equilibrium price,

- A) the demand curve shifts leftward.
- B) the quantity supplied exceeds the quantity demanded.
- C) the quantity supplied equals the quantity demanded.
- D) the supply curve shifts rightward.
- E) the quantity demanded exceeds the quantity supplied.

Answer: E

Diff: 2 Type: MC

Topic: A Housing Market with a Rent Ceiling

Use the figure below to answer the following questions.



**Figure 6.1.2**

10) Refer to Figure 6.1.2. If a rigorously enforced price ceiling is set at \$10, then

- A) 100 units will be sold at a price of \$20 each.
- B) 100 units will be sold at a price of \$15 each.
- C) 150 units will be sold at a price of \$15 each.
- D) 200 units will be sold at a price of \$10 each.
- E) 100 units will be sold at a price of \$10 each.

Answer: E

Diff: 2 Type: MC

Topic: A Housing Market with a Rent Ceiling

11) Refer to Figure 6.1.2. What would be the maximum black market price of the good if a price ceiling is set at \$10 a unit?

- A) \$10
- B) \$15
- C) \$20
- D) 50 goods sold at \$10 and 50 goods sold at \$20
- E) 50 goods sold at \$10 and 50 goods sold at \$15

Answer: C

Diff: 3 Type: MC

Topic: A Housing Market with a Rent Ceiling

12) Which one of the following is *not* likely to be an outcome of a rent ceiling?

- A) a black market for rent-controlled housing
- B) long waiting lists of potential renters for rent-controlled housing
- C) a short-run shortage of housing
- D) a black market price below the rent ceiling
- E) increased search activity for rent-controlled housing

Answer: D

Diff: 2 Type: MC

Topic: A Housing Market with a Rent Ceiling

Source: Study Guide

13) If a rent ceiling imposed by the government is greater than the equilibrium rent for housing, then

- A) the supply of rental housing will increase.
- B) a shortage of housing will occur.
- C) a surplus of housing will occur.
- D) the equilibrium rent will prevail as long as all else remains constant.
- E) the equilibrium rent will rise.

Answer: D

Diff: 2 Type: MC

Topic: A Housing Market with a Rent Ceiling

14) Which one of the following is likely to be the outcome of a rent ceiling imposed below the equilibrium rent?

- A) a black market for rent-controlled housing
- B) long waiting lists of potential suppliers for rent-controlled housing
- C) a surplus of housing
- D) no search activity
- E) Both A and B are correct.

Answer: E

Diff: 2 Type: MC

Topic: A Housing Market with a Rent Ceiling

15) A price ceiling set below the equilibrium price will result in

- A) excess supply.
- B) excess demand.
- C) the equilibrium price.
- D) an increase in supply.
- E) a decrease in demand.

Answer: B

Diff: 1 Type: MC

Topic: A Housing Market with a Rent Ceiling

Source: Study Guide

16) Daisy and Donald live in a community with rent ceilings. Both are looking for an apartment to rent. Daisy has a job paying \$10 per hour and Donald has a job paying \$8 per hour. Both value an apartment equally. What is the most likely outcome?

- A) Daisy will spend more time than Donald searching for an apartment.
- B) Donald will spend more time than Daisy searching for an apartment.
- C) Both of them will spend the same amount of time searching for an apartment.
- D) Daisy will find the apartment.
- E) Donald will find the apartment.

Answer: B

Diff: 2 Type: MC

Topic: A Housing Market with a Rent Ceiling

17) In an unregulated housing market with no rent ceiling, the rent is determined by the

- A) landlords only.
- B) tenants only.
- C) government only.
- D) market.
- E) landlords, tenants, and the government.

Answer: D

Diff: 2 Type: MC

Topic: A Housing Market with a Rent Ceiling

18) An effective rent ceiling

- A) increases consumer surplus.
- B) increases producer surplus.
- C) creates a deadweight loss.
- D) decreases the supply of housing.
- E) increases the supply of housing.

Answer: C

Diff: 3 Type: MC

Topic: A Housing Market with a Rent Ceiling

19) In an unregulated housing market with no rent ceiling,

- A) scarce housing resources are allocated inefficiently.
- B) scarce housing resources are allocated efficiently.
- C) tenants pay a lower rent compared to what they pay in a market with an effective rent ceiling.
- D) landlords receive less compared to what they receive in a market with an effective rent ceiling.
- E) consumer surplus equals producer surplus.

Answer: B

Diff: 2 Type: MC

Topic: A Housing Market with a Rent Ceiling

- 20) In an unregulated housing market, with no rent ceiling,
- A) marginal social cost is greater than marginal social benefit.
  - B) marginal social benefit is greater than marginal social cost.
  - C) marginal social benefit equals marginal social cost.
  - D) marginal social benefit is negative.
  - E) marginal social cost is negative.

Answer: C

Diff: 2 Type: MC

Topic: A Housing Market with a Rent Ceiling

- 21) According to the *fair result* view of fairness, a fair outcome in the housing market
- A) is the one that blocks voluntary exchange of housing.
  - B) cannot be created in the housing industry.
  - C) is one that allocates scarce housing resources to those who are willing and able to pay.
  - D) is one that allocates scarce housing resources by lottery.
  - E) is one that allocates scarce housing resources to the poorest.

Answer: E

Diff: 3 Type: MC

Topic: A Housing Market with a Rent Ceiling

- 22) According to the *fair rules* view of fairness, a fair outcome in the housing market
- A) is one that does not block voluntary exchanges of housing.
  - B) cannot be created in housing industry.
  - C) is one that allocates scarce housing resources to those who are willing and able to pay.
  - D) is one that allocates scarce housing resources by lottery.
  - E) is one that allocates scarce housing resources to the poorest.

Answer: A

Diff: 3 Type: MC

Topic: A Housing Market with a Rent Ceiling

- 23) When rent is not permitted to allocate scarce housing, what other mechanisms are available?
- A) a lottery
  - B) first-come, first-served
  - C) discrimination
  - D) both A and B are correct
  - E) A, B and C are correct

Answer: E

Diff: 1 Type: MC

Topic: A Housing Market with a Rent Ceiling

- 24) A lottery allocates housing to those
- A) who are poor.
  - B) who share similar views to the owner of the housing.
  - C) who are rich.
  - D) whose names are on waiting lists.
  - E) who are lucky.

Answer: E

Diff: 1 Type: MC

Topic: A Housing Market with a Rent Ceiling

- 25) First-come, first-served allocates housing to those
- A) whose names are on waiting lists.
  - B) who share similar views to the owner of the housing.
  - C) who are rich.
  - D) who are poor.
  - E) who are lucky.

Answer: A

Diff: 1 Type: MC

Topic: A Housing Market with a Rent Ceiling

- 26) Discrimination allocates scarce housing
- A) to those who are poor.
  - B) based on the self-interest of landlords.
  - C) to those who are lucky.
  - D) to those whose names are on waiting lists.
  - E) to those who are willing and able to pay.

Answer: B

Diff: 1 Type: MC

Topic: A Housing Market with a Rent Ceiling

27) Suppose the government introduces a ceiling on the fees that lawyers are permitted to charge. If the fee ceiling is set \_\_\_\_\_ the equilibrium wage rate, the amount of work done by lawyers \_\_\_\_\_, the consumer surplus of people who hire lawyers \_\_\_\_\_, and the producer surplus of law firms \_\_\_\_\_.

- A) below; increases; increases; increases
- B) above; decreases; decreases; decreases
- C) below; decreases; decreases; decreases
- D) above; increases; increases; increases
- E) below; decreases; increases; decreases

Answer: C

Type: MC

Topic: A Housing Market with a Rent Ceiling

Source: MyEconLab

28) Suppose the government introduces a ceiling on the fees that lawyers are permitted to charge. This fee ceiling

- A) is always inefficient.
- B) results in an inefficient use of resources when the ceiling is above the equilibrium fee.
- C) results in an efficient use of resources when the ceiling is above the equilibrium fee.
- D) results in an efficient use of resources when the ceiling is below the equilibrium fee.
- E) is always efficient.

Answer: C

Type: MC

Topic: A Housing Market with a Rent Ceiling

Source: MyEconLab

29) An effective rent ceiling

- A) increases producer surplus.
- B) results in a producer surplus of zero.
- C) sometimes increases producer surplus and sometimes decreases producer surplus.
- D) decreases producer surplus.
- E) decreases the supply of housing.

Answer: D

Type: MC

30) A rent ceiling

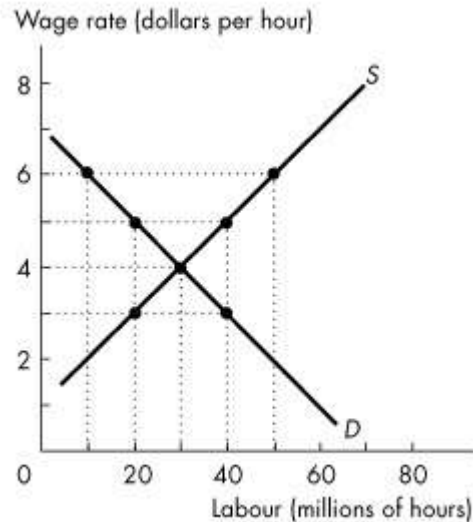
- A) results in a shortage of housing if the rent ceiling is below the equilibrium rent.
- B) results in a surplus of housing if the rent ceiling is above the equilibrium rent.
- C) always results in a shortage of housing.
- D) always results in a surplus of housing.
- E) Both A and B are correct.

Answer: A

Type: MC

## 6.2 A Labour Market with a Minimum Wage

Use the figure below to answer the following questions.



**Figure 6.2.1**

1) Refer to Figure 6.2.1. What is the equilibrium wage rate per hour in an unregulated market?

- A) \$2
- B) \$3
- C) \$4
- D) \$5
- E) \$30

Answer: C

Diff: 1 Type: MC

Topic: A Labour Market with a Minimum Wage

2) Refer to Figure 6.2.1. Suppose a \$5 per hour minimum wage is in force. What is the lowest wage per hour an unemployed person would be willing to accept?

- A) \$2
- B) \$3
- C) \$4
- D) \$5
- E) \$1

Answer: B

Diff: 2 Type: MC

Topic: A Labour Market with a Minimum Wage

3) Refer to Figure 6.2.1. If the minimum wage is set at \$2 per hour, what is the level of unemployment in millions of hours?

- A) 50
- B) 40
- C) 20
- D) 10
- E) 0

Answer: E

Diff: 2 Type: MC

Topic: A Labour Market with a Minimum Wage

Source: Study Guide

4) Refer to Figure 6.2.1. If the minimum wage is set at \$6 per hour, what is the level of unemployment in millions of hours?

- A) 50
- B) 40
- C) 20
- D) 10
- E) 0

Answer: B

Diff: 2 Type: MC

Topic: A Labour Market with a Minimum Wage

Source: Study Guide

5) Suppose a minimum wage of \$4 an hour is in force, resulting in unemployment of 10 million hours. Then the demand for labour increases such that supply and demand intersect at a wage rate of \$5 per hour. What will happen to the equilibrium wage rate and employment?

- A) The wage rate is \$5 an hour and there will be no unemployment.
- B) The wage rate is \$5 an hour and there will be a surplus of labour.
- C) The wage rate is \$4 an hour and there will be a surplus of labour.
- D) The wage rate is \$4 an hour and there will be no unemployment.
- E) The wage rate is \$4 an hour and there will be unemployment.

Answer: A

Diff: 1 Type: MC

Topic: A Labour Market with a Minimum Wage

Use the table below to answer the following questions.

**Table 6.2.1**

Wage Rate (dollars per hour)	Quantity Supplied (hours per week)	Quantity Demanded (hours per week)
7	1,000	200
6	800	400
5	600	600
4	400	800

6) Table 6.2.1 gives the supply and demand schedules for teenage labour in Genoa City. In an unregulated market,

- A) there is no teenage unemployment and the wage rate is \$6 per hour.
- B) there is no teenage unemployment and the wage rate is \$5 per hour.
- C) teenage unemployment is 400 hours and the wage rate is \$6 per hour.
- D) teenage unemployment is 400 hours and the wage rate is \$5 per hour.
- E) the minimum wage is \$7 per hour.

Answer: B

Diff: 2 Type: MC

Topic: A Labour Market with a Minimum Wage

7) Table 6.2.1 gives the supply and demand schedules for teenage labour in Genoa City. Suppose the Genoa City Council sets a minimum wage of \$6 per hour. Teenage unemployment is

- A) 800 hours.
- B) 600 hours.
- C) 400 hours.
- D) 200 hours.
- E) zero hours.

Answer: C

Diff: 2 Type: MC

Topic: A Labour Market with a Minimum Wage

8) Table 6.2.1 gives the supply and demand schedules for teenage labour in Genoa City. Suppose the Genoa City Council sets a minimum wage of \$4 per hour. Teenage unemployment is

- A) 800 hours.
- B) 600 hours.
- C) 400 hours.
- D) 200 hours.
- E) zero hours.

Answer: E

Diff: 2 Type: MC

Topic: A Labour Market with a Minimum Wage

- 9) Table 6.2.1 gives the supply and demand schedules for teenage labour in Genoa City. There is a minimum wage set at \$6 per hour. Suppose a new fast food restaurant opens and increases the quantity demanded of teenage labour by 400 hours per week at each wage rate. The result is
- A) elimination of teenage unemployment and a wage rate of \$7 per hour.
  - B) elimination of teenage unemployment, but the wage rate remains at \$6 per hour.
  - C) some teenage unemployment with the wage rate remaining at \$6 per hour.
  - D) no change in teenage unemployment because the wage rate rises to \$7 per hour.
  - E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: A Labour Market with a Minimum Wage

- 10) Table 6.2.1 gives the supply and demand schedules for teenage labour in Genoa City. Suppose a new fast food restaurant opens and increases the quantity demanded of teenage labour by 400 hours per week at each wage rate. If the teenage labour market is unregulated, there is an increase in teenage employment to
- A) 1,000 hours per week and a wage of \$5 per hour.
  - B) 1,000 hours per week and a wage of \$7 per hour.
  - C) 800 hours per week and a wage of \$6 per hour.
  - D) 600 hours per week and a wage of \$7 per hour.
  - E) 400 hours per week and a wage of \$7 per hour.

Answer: C

Diff: 2 Type: MC

Topic: A Labour Market with a Minimum Wage

- 11) Which one of the following statements is *false*?
- A) An effective minimum wage sets the wage rate above the equilibrium wage rate.
  - B) An effective rent ceiling sets the rent below the equilibrium rent.
  - C) An effective rent ceiling leads to a housing shortage.
  - D) An effective minimum wage is inefficient.
  - E) A minimum wage is a price ceiling in the labour market.

Answer: E

Diff: 2 Type: MC

Topic: A Labour Market with a Minimum Wage

Use the table below to answer the following questions.

**Table 6.2.2**

Wage Rate (dollars per hour)	Quantity Supplied (millions of hours)	Quantity Demanded (millions of hours)
7	60	30
6	50	40
5	40	50
4	30	60
3	20	70

12) Refer to Table 6.2.2. What is the level of unemployment in millions of hours if the minimum wage is set at \$3 per hour?

- A) 70
- B) 40
- C) 30
- D) 20
- E) zero

Answer: E

Diff: 2 Type: MC

Topic: A Labour Market with a Minimum Wage

13) Refer to Table 6.2.2. What is the level of unemployment in millions of hours if the minimum wage is set at \$7 per hour?

- A) 40
- B) 30
- C) 20
- D) 10
- E) zero

Answer: B

Diff: 2 Type: MC

Topic: A Labour Market with a Minimum Wage

14) Refer to Table 6.2.2. What is the equilibrium wage rate in an unregulated market?

- A) \$5.00 per hour
- B) \$5.50 per hour
- C) \$6.00 per hour
- D) \$6.50 per hour
- E) \$7.50 per hour

Answer: B

Diff: 2 Type: MC

Topic: A Labour Market with a Minimum Wage

15) Suppose the minimum wage is \$4 per hour, and 1,100 units of labour are hired. Then the government raises the minimum wage to \$6 per hour, and 900 units are now hired. Choose the correct statement.

- A) Total wages paid to workers has fallen.
- B) The price elasticity of demand for labour is 0.5.
- C) There is unemployment in this labour market.
- D) The quantity of labour supplied is greater at the higher minimum wage.
- E) all of the above except A

Answer: E

Diff: 3 Type: MC

Topic: A Labour Market with a Minimum Wage

16) Complete the following sentence. A price floor set below the equilibrium price results in

- A) a surplus.
- B) a shortage.
- C) the equilibrium price.
- D) an increase in supply.
- E) a decrease in demand.

Answer: C

Diff: 2 Type: MC

Topic: A Labour Market with a Minimum Wage

17) When a minimum wage is set above the equilibrium wage rate,

- A) unemployment decreases.
- B) job search activity decreases.
- C) the supply of workers decreases.
- D) unemployment increases.
- E) the supply of workers increases.

Answer: D

Type: MC

Topic: A Labour Market with a Minimum Wage

Source: MyEconLab

18) The government sets a price floor for corn, which is above the equilibrium price of corn. As a result

- A) the market for corn is efficient.
- B) a shortage of corn occurs.
- C) consumer surplus is maximized.
- D) a deadweight loss is created.
- E) B, C, and D are correct.

Answer: D

Type: MC

19) Suppose the equilibrium wage is \$10 an hour. A minimum wage is a price \_\_\_\_\_ and that will change the quantity of employment if it is set at \_\_\_\_\_ an hour.

- A) floor; \$12
- B) ceiling; \$12
- C) floor; \$8
- D) ceiling; \$8
- E) floor; \$10

Answer: A

Type: MC

### 6.3 Taxes

1) Suppose the demand for gasoline is inelastic, but not perfectly inelastic, and the supply is elastic, but not perfectly elastic. A tax on gasoline is paid

- A) mostly by buyers.
- B) mostly by sellers.
- C) equally by buyers and sellers.
- D) totally by buyers.
- E) totally by sellers.

Answer: A

Diff: 3 Type: MC

Topic: Taxes

2) Suppose the demand for CDs is elastic, but not perfectly elastic, and the supply is inelastic, but not perfectly inelastic. A tax on CDs is paid

- A) equally by buyers and sellers.
- B) mostly by sellers.
- C) mostly by buyers.
- D) by neither buyers nor sellers.
- E) totally by sellers.

Answer: B

Diff: 3 Type: MC

Topic: Taxes

Use the figure below to answer the following questions.

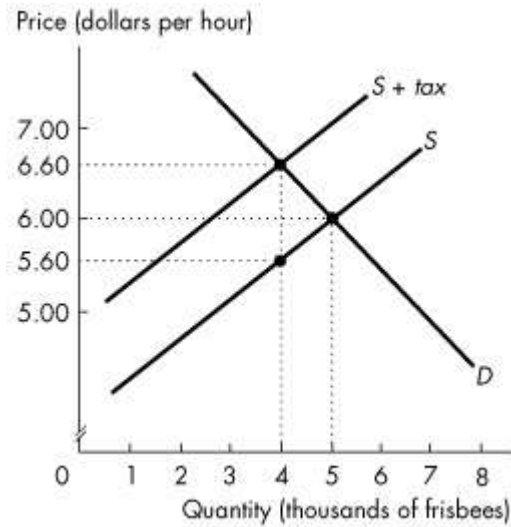


Figure 6.3.1

3) Refer to Figure 6.3.1 showing the market for frisbees before and after a tax is imposed. The tax on each frisbee is

- A) \$0.40.
- B) \$0.60.
- C) \$1.00.
- D) \$5.60.
- E) \$6.60.

Answer: C

Diff: 2 Type: MC

Topic: Taxes

Source: Study Guide

4) Refer to Figure 6.3.1 showing the market for frisbees before and after a tax is imposed. On each frisbee, the sellers' share of the tax is

- A) \$0.40.
- B) \$0.60.
- C) \$1.00.
- D) \$5.60.
- E) \$6.60.

Answer: A

Diff: 3 Type: MC

Topic: Taxes

Source: Study Guide

5) Refer to Figure 6.3.1 showing the market for frisbees before and after a tax is imposed. On each frisbee, the buyers' share of the tax is

- A) \$0.40.
- B) \$0.60.
- C) \$1.00.
- D) \$5.60.
- E) \$6.60.

Answer: B

Diff: 3 Type: MC

Topic: Taxes

Source: Study Guide

6) Refer to Figure 6.3.1 showing the market for frisbees before and after a tax is imposed. Government revenue from the tax is

- A) \$4,000.
- B) \$5,000.
- C) \$22,400.
- D) \$26,400.
- E) \$30,000.

Answer: A

Diff: 2 Type: MC

Topic: Taxes

Source: Study Guide

7) Refer to Figure 6.3.1 showing the market for frisbees before and after a tax is imposed. We can determine that between 4,000 and 5,000 frisbees, supply is

- A) inelastic.
- B) unit elastic.
- C) elastic.
- D) perfectly elastic.
- E) perfectly inelastic.

Answer: C

Diff: 2 Type: MC

Topic: Taxes

8) If the price of a good is not affected by a tax, then

- A) supply is perfectly elastic.
- B) demand is perfectly elastic.
- C) the elasticity of supply is greater than elasticity of demand.
- D) demand is unit elastic.
- E) supply is unit elastic.

Answer: B

Diff: 3 Type: MC

Topic: Taxes

Source: Study Guide

9) The burden of the tax on buyers is greater the more

- (1) elastic is demand
- (2) inelastic is demand
- (3) elastic is supply
- (4) inelastic is supply

- A) (2) only
- B) (1) and (3)
- C) (1) and (4)
- D) (2) and (3)
- E) (2) and (4)

Answer: D

Diff: 3 Type: MC

Topic: Taxes

10) The burden of tax on sellers is greater the more

- (1) elastic is demand
- (2) inelastic is demand
- (3) elastic is supply
- (4) inelastic is supply

- A) (2) only
- B) (1) and (3)
- C) (1) and (4)
- D) (2) and (3)
- E) (2) and (4)

Answer: C

Diff: 3 Type: MC

Topic: Taxes

11) Suppose your province raises the provincial sales tax by 1 percent. You predict that the prices of taxed goods (including the tax) will

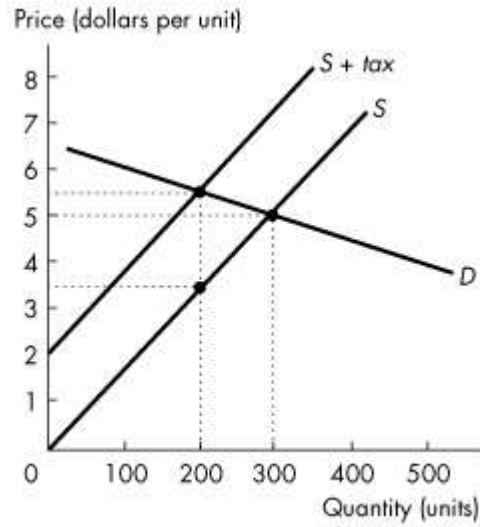
- A) rise by 1 percent.
- B) rise by more than 1 percent.
- C) rise by an amount between zero and 1 percent.
- D) not change at all.
- E) fall by an amount between zero and 1 percent.

Answer: C

Diff: 2 Type: MC

Topic: Taxes

Use the figure below to answer the following questions.



**Figure 6.3.2**

12) Refer to Figure 6.3.2. The amount of the tax per unit is

- A) zero.
- B) \$0.50.
- C) \$1.00.
- D) \$1.50.
- E) \$2.00.

Answer: E

Diff: 2 Type: MC

Topic: Taxes

13) Refer to Figure 6.3.2. The buyers' share of the tax is

- A) zero.
- B) \$0.50.
- C) \$1.00.
- D) \$1.50.
- E) \$2.00.

Answer: B

Diff: 3 Type: MC

Topic: Taxes

14) Refer to Figure 6.3.2. The seller's share of the tax is

- A) zero.
- B) \$0.50.
- C) \$1.00.
- D) \$1.50.
- E) \$2.00.

Answer: D

Diff: 3 Type: MC

Topic: Taxes

15) Refer to Figure 6.3.2. Government revenue from the tax is

- A) zero.
- B) \$100.
- C) \$300.
- D) \$400.
- E) \$600.

Answer: D

Diff: 2 Type: MC

Topic: Taxes

16) Refer to Figure 6.3.2. The deadweight loss from the sales tax is

- A) \$50.
- B) \$100.
- C) \$200.
- D) \$1,000.
- E) \$150.

Answer: B

Diff: 3 Type: MC

Topic: Taxes

17) Refer to Figure 6.3.2. Between 200 and 300 units, demand is

- A) inelastic.
- B) unit elastic.
- C) elastic.
- D) perfectly inelastic.
- E) perfectly elastic.

Answer: C

Diff: 2 Type: MC

Topic: Taxes

18) The seller pays most of a tax if demand is relatively elastic because

- A) the buyer can easily substitute to other markets.
- B) the seller can easily substitute to other markets.
- C) the government forces the seller to bear the burden of the tax.
- D) there is a black market for this good.
- E) the seller cannot easily substitute to other goods.

Answer: A

Diff: 2 Type: MC

Topic: Taxes

19) The buyer pays most of a tax if demand is relatively inelastic because

- A) the buyer cannot easily substitute to other markets.
- B) the buyer can easily substitute to other markets.
- C) the government forces the seller to bear the burden of the tax.
- D) there is a black market for this good.
- E) the seller cannot easily substitute to other goods.

Answer: A

Diff: 2 Type: MC

Topic: Taxes

20) The buyer pays most of a tax if supply is relatively elastic because

- A) the buyer cannot easily substitute to other markets.
- B) the seller can easily substitute to other markets.
- C) the government forces the seller to bear the burden.
- D) there is a black market for this good.
- E) the seller cannot easily substitute to other goods.

Answer: B

Diff: 2 Type: MC

Topic: Taxes

21) If a sales tax is imposed on food, who is likely to pay most of the tax?

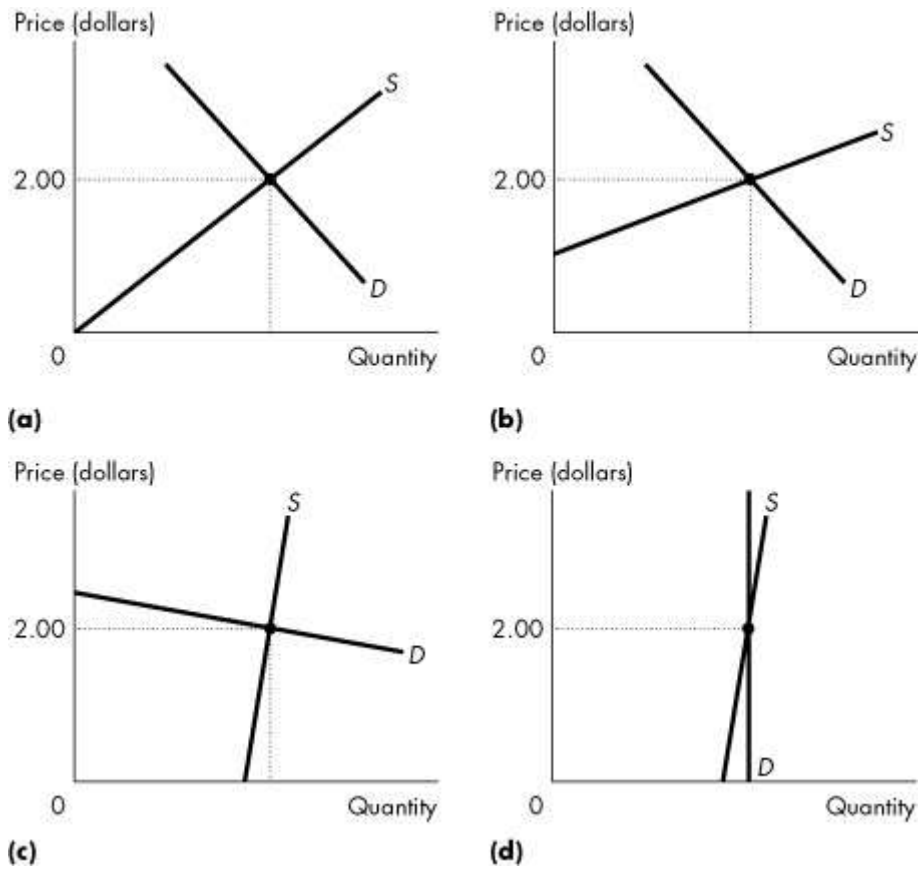
- A) mostly the buyer
- B) mostly the seller
- C) neither the seller nor the buyer
- D) the buyer and the seller equally
- E) the burden of the tax depends on the size of the tax

Answer: A

Diff: 3 Type: MC

Topic: Taxes

Use the figure below to answer the following questions.



**Figure 6.3.3**

22) Refer to Figure 6.3.3. Suppose a tax of \$1 is imposed. In which market would the seller pay the highest portion of the tax?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) all markets equally

Answer: C

Diff: 3 Type: MC

Topic: Taxes

23) Refer to Figure 6.3.3. Suppose a tax of \$1 is imposed. In which market would the buyer pay the highest portion of the tax?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) all markets equally

Answer: D

Diff: 3 Type: MC

Topic: Taxes

24) Refer to Figure 6.3.3. Suppose a tax of \$1 is imposed. In which market would tax revenue be the lowest?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) all markets equally

Answer: C

Diff: 3 Type: MC

Topic: Taxes

25) Refer to Figure 6.3.3. Suppose a tax of \$1 is imposed. In which market would tax revenue be the highest?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) all markets equally

Answer: D

Diff: 3 Type: MC

Topic: Taxes

26) Governments tend to tax items with inelastic demand because

- A) governments wish to avoid big rises in after-tax prices.
- B) sellers pay most of the tax in these cases.
- C) buyers pay most of the tax in these cases.
- D) these goods yield the most tax revenues.
- E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: Taxes

27) If the supply of a good is perfectly elastic, then a tax on the good will be paid

- A) completely by the buyers.
- B) completely by the sellers.
- C) equally by the buyers and sellers.
- D) mostly but not completely by the buyers.
- E) mostly but not completely by the sellers.

Answer: A

Diff: 2 Type: MC

Topic: Taxes

28) If the supply of a good is perfectly inelastic, then a tax on the good will be paid

- A) completely by the buyers.
- B) completely by the sellers.
- C) equally by the buyers and sellers.
- D) mostly but not completely by the buyers.
- E) mostly but not completely by the sellers.

Answer: B

Diff: 2 Type: MC

Topic: Taxes

29) If the demand for a good is perfectly elastic, then a tax on the good will be paid

- A) completely by the buyers.
- B) completely by the sellers.
- C) equally by the buyers and sellers.
- D) mostly but not completely by the buyers.
- E) mostly but not completely by the sellers.

Answer: B

Diff: 2 Type: MC

Topic: Taxes

30) If the demand for a good is perfectly inelastic, then a tax on the good will be paid

- A) completely by the buyers.
- B) completely by the sellers.
- C) equally by the buyers and sellers.
- D) mostly but not completely by the buyers.
- E) mostly but not completely by the sellers.

Answer: A

Diff: 2 Type: MC

Topic: Taxes

31) A \$10 per-unit tax on MP3 players raises the equilibrium price paid by consumers by \$5. The quantity sold before the tax was 5,000 per year. The revenue from the tax is

- A) zero.
- B) positive but less than \$50,000 per year.
- C) \$50,000 per year.
- D) more than \$50,000 per year.
- E) greater the more elastic is demand.

Answer: B

Diff: 3 Type: MC

Topic: Taxes

32) A 3 cents per-unit tax on bread leads to no change in the quantity bought and sold. The tax is paid

- A) completely by the sellers.
- B) completely by the buyers.
- C) equally by the buyers and sellers.
- D) mostly but not completely by the buyers.
- E) completely by either the sellers or the buyers; we cannot tell without more information.

Answer: E

Diff: 3 Type: MC

Topic: Taxes

*Use the table below to answer the following questions.*

**Table 6.3.1**

Price (dollars per unit)	Quantity Demanded (units)	Quantity Supplied (units)
3	900	300
4	800	400
5	700	500
6	600	600
7	500	700
8	400	800
9	200	900

33) Refer to Table 6.3.1. Suppose a sales tax of \$2 a unit is imposed on the good described in the table. The new price paid by consumers is \$ \_\_\_\_\_ and \_\_\_\_\_ units are sold.

- A) \$6; 400
- B) \$7; 700
- C) \$7; 500
- D) \$6.50; 500
- E) \$6.50; 700

Answer: C

Diff: 3 Type: MC

Topic: Taxes

34) Refer to Table 6.3.1. Suppose a sales tax of \$2 a unit is imposed on the good described in the table. The buyers' share of the tax is

- A) \$2.00.
- B) \$1.50.
- C) \$1.00.
- D) zero.
- E) \$2.50.

Answer: C

Diff: 3 Type: MC

Topic: Taxes

35) Refer to Table 6.3.1. Suppose a sales tax of \$2 a unit is imposed on the good described in the table. The sellers' share of the tax is

- A) \$2.00.
- B) \$1.50.
- C) \$1.00.
- D) \$0.
- E) \$2.50.

Answer: C

Diff: 3 Type: MC

Topic: Taxes

36) Refer to Table 6.3.1. Suppose a sales tax of \$2 a unit is imposed on the good described in the table. Government revenue from the tax is

- A) \$1,200.
- B) \$1,000.
- C) \$800.
- D) \$600.
- E) zero.

Answer: B

Diff: 3 Type: MC

Topic: Taxes

37) The \_\_\_\_\_ principle is the proposition that people should pay taxes equal to the benefits they receive from the services provided by government.

The \_\_\_\_\_ principle is the proposition that people should pay taxes according to how easily they can bear the burden of the tax.

- A) benefits; ability-to-pay
- B) equality; fairness
- C) services; burden
- D) ability-to-pay; benefits
- E) efficient; inefficient

Answer: A

Type: MC

Topic: Taxes

Source: MyEconLab

38) When a sales tax is imposed on sellers, the supply curve shifts so that the vertical distance between the original supply curve and supply plus tax curve equals the

- A) sales tax multiplied by the price elasticity of demand.
- B) sales tax multiplied by the price elasticity of supply.
- C) sales tax divided by the price elasticity of demand.
- D) amount of the sales tax per unit.
- E) sales tax divided by the price elasticity of supply.

Answer: D

Type: MC

39) The demand for a good and the supply of a good are each neither perfectly elastic nor perfectly inelastic. If a sales tax on sellers of the good is imposed, the tax is paid by

- A) the buyers only.
- B) both the buyers and the sellers.
- C) the sellers only.
- D) the buyers only if demand for the good increases.
- E) the suppliers only if the supply of the good increases.

Answer: B

Type: MC

## 6.4 Production Quotas and Subsidies

1) A subsidy is a

- A) tax imposed by the government on imported goods.
- B) payment made by the government to a producer.
- C) tax imposed by the government on a producer.
- D) payment made by a consumer to a producer.
- E) payment made by foreign governments to domestic farmers.

Answer: B

Diff: 2 Type: MC

Topic: Production Quotas and Subsidies

2) A subsidy

- A) lowers the price received by farmers.
- B) decreases the quantity supplied in the market.
- C) raises the price received by farmers.
- D) prevents the deadweight loss from underproduction.
- E) decreases total revenue received by farmers.

Answer: C

Diff: 2 Type: MC

Topic: Production Quotas and Subsidies

3) A subsidy

- A) raises marginal social benefit above marginal social cost.
- B) makes marginal social cost equal marginal social benefit.
- C) results in efficient production.
- D) raises marginal social cost above marginal social benefit.
- E) makes world prices higher than domestic prices.

Answer: D

Diff: 2 Type: MC

Topic: Production Quotas and Subsidies

4) A production quota

- A) is a lower limit to the quantity of a good that can be produced in a specified period.
- B) is an upper limit to the quantity of a good that can be produced in a specified period.
- C) is a payment made by a consumer to a producer.
- D) is a payment made by a producer to a consumer.
- E) is a payment made by the government to a producer.

Answer: B

Diff: 2 Type: MC

Topic: Production Quotas and Subsidies

5) Suppose the Canadian Dairy Commission sets a production quota for dairy production above the equilibrium quantity. Then,

- A) the policy will increase the quantity of milk produced in Canada.
- B) the policy will raise the price of milk in the international market.
- C) the policy will have no impact on the dairy industry.
- D) the policy will increase revenue received by dairy producers.
- E) the policy will decrease revenue received by dairy producers.

Answer: C

Diff: 2 Type: MC

Topic: Production Quotas and Subsidies

6) A production quota

- A) increases the marginal social cost of production.
- B) lowers the price and increases the marginal social cost of production.
- C) increases demand for the good.
- D) raises the price and decreases the marginal social cost of production.
- E) makes production more efficient.

Answer: D

Diff: 2 Type: MC

Topic: Production Quotas and Subsidies

7) An effective production quota

- A) is efficient because it results in overproduction.
- B) is efficient because it results in underproduction.
- C) is inefficient because it results in underproduction.
- D) is inefficient because it results in overproduction.
- E) is efficient for quantities below the equilibrium quantity and is inefficient for quantities above the equilibrium quantity.

Answer: C

Diff: 2 Type: MC

Topic: Production Quotas and Subsidies

8) In a market with an effective production quota

- A) marginal social benefit exceeds marginal social cost.
- B) marginal social benefit equals marginal social cost.
- C) marginal social cost exceeds marginal social benefit.
- D) marginal social cost is greater than the equilibrium price.
- E) marginal social benefit is less than the equilibrium price.

Answer: A

Diff: 2 Type: MC

Topic: Production Quotas and Subsidies

9) When an effective production quota is applied in the market for wheat, the quantity produced \_\_\_\_\_ and the price \_\_\_\_\_. The marginal social benefit \_\_\_\_\_ marginal social cost.

- A) increases; rises; exceeds
- B) decreases; falls; is less than
- C) decreases; rises; exceeds
- D) increases; falls; is less than
- E) decreases; rises; is less than

Answer: C

Type: MC

Topic: Production Quotas and Subsidies

Source: MyEconLab

Use the figure below to answer the following question.

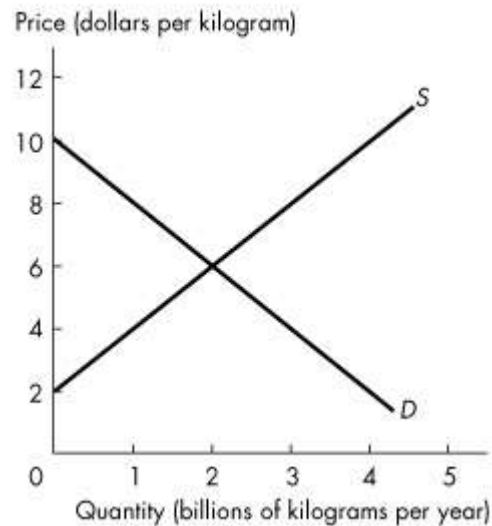


Figure 6.4.1

10) Refer to Figure 6.4.1. The graph shows the market for tomatoes. When the government introduces a subsidy for tomatoes at \$4 a kilogram, the quantity produced is \_\_\_\_\_ because \_\_\_\_\_.

- A) efficient; marginal social cost is less than marginal social benefit
- B) efficient; marginal social benefit equals marginal social cost
- C) inefficient; marginal social cost is less than marginal social benefit
- D) inefficient; marginal social benefit is less than marginal social cost
- E) inefficient; marginal social cost is zero

Answer: D

Type: MC

Topic: Production Quotas and Subsidies

Source: MyEconLab

Use the table below to answer the following question.

**Table 6.4.1**

Price (dollars per box)	Quantity Demanded (boxes per week)	Quantity Supplied (boxes per week)
1.00	3,500	500
1.10	3,250	1,000
1.20	3,000	1,500
1.30	2,750	2,000
1.40	2,500	2,500
1.50	2,250	3,000
1.60	2,000	3,500

11) Refer to Table 6.4.1. The table shows the demand and supply schedules for rice. The market for rice is in equilibrium. With a subsidy of \$0.30 a box, the price of a box of rice is \_\_\_\_\_, the marginal cost of producing rice is \_\_\_\_\_ a box, and the quantity of rice produced is \_\_\_\_\_ boxes.

- A) \$1.40; \$1.40; 2,500
- B) \$1.20; \$1.50; 2,500
- C) \$1.20; \$1.50; 3,000
- D) \$1.50; \$1.20; 3,000
- E) \$1.50; \$1.20; 2,500

Answer: C

Type: MC

Topic: Production Quotas and Subsidies

Source: MyEconLab

12) Refer to Table 6.4.1. The table shows the demand and supply schedules for rice. With a production quota of 2,000 boxes a week, the price of a box of rice is \_\_\_\_\_, the marginal cost of producing rice is \_\_\_\_\_ a box, and the quantity of rice produced is \_\_\_\_\_ boxes a week.

- A) \$1.30; \$1.60; 2,000
- B) \$1.60; \$1.30; 2,000
- C) \$1.40; \$1.40; 2,500
- D) \$1.40; \$1.40; 2,000
- E) \$1.60; \$1.30; 2,500

Answer: B

Type: MC

Topic: Production Quotas and Subsidies

Source: MyEconLab

13) A production quota is set below the equilibrium quantity. At the quota quantity, marginal social benefit is \_\_\_\_\_ marginal social cost and the level of production is \_\_\_\_\_.

- A) less than; efficient
- B) greater than; efficient
- C) less than; efficient
- D) less than; inefficient
- E) equal to; efficient

Answer: D

Type: MC

14) A production quota is set equal to the equilibrium quantity. At the quota quantity, marginal social benefit is \_\_\_\_\_ marginal social cost and the level of production is \_\_\_\_\_.

- A) less than; efficient
- B) greater than; efficient
- C) less than; efficient
- D) less than; inefficient
- E) equal to; efficient

Answer: E

Type: MC

## 6.5 Markets for Illegal Goods

- 1) If enforcement is aimed at sellers of an illegal good, the
- A) price and quantity bought decrease.
  - B) price and quantity bought increase.
  - C) price rises and quantity bought decreases.
  - D) price falls and quantity bought increases.
  - E) price change is uncertain and quantity bought decreases.

Answer: C

Diff: 3 Type: MC

Topic: Markets for Illegal Goods

Source: Study Guide

- 2) If enforcement is aimed at buyers of an illegal good, the
- A) price and quantity bought decrease.
  - B) price and quantity bought increase.
  - C) price rises and quantity bought decreases.
  - D) price falls and quantity bought increases.
  - E) price change is uncertain and quantity bought decreases.

Answer: A

Diff: 3 Type: MC

Topic: Markets for Illegal Goods

- 3) Which one of the following statements about illegal goods is *true*?
- A) Taxes are more effective in changing preferences than prohibition.
  - B) Prohibition is more effective in generating revenue than an equivalent tax.
  - C) Taxes and penalties cannot be set to yield equivalent outcomes.
  - D) Taxes generate revenues while prohibition sends a signal that might influence preferences.
  - E) none of the above

Answer: D

Diff: 2 Type: MC

Topic: Markets for Illegal Goods

Source: Study Guide

- 4) Consider a market for an illegal good. If the government imposes the cost of breaking the law on the buyer of the good, then price will be
- A) higher and quantity lower compared to imposing the same cost on the seller.
  - B) higher and quantity higher compared to imposing the same cost on the seller.
  - C) lower and quantity lower compared to imposing the same cost on the seller.
  - D) lower and quantity the same compared to imposing the same cost on the seller.
  - E) higher and quantity the same compared to imposing the same cost on the seller.

Answer: D

Diff: 3 Type: MC

Topic: Markets for Illegal Goods

5) Suppose the cost of breaking the law is imposed on the buyers of an illegal good. This action will have its biggest impact on quantity if the demand for the good is

- A) inelastic or the supply is inelastic.
- B) elastic or the supply is elastic.
- C) elastic or the supply is inelastic.
- D) inelastic or the supply is elastic.
- E) perfectly inelastic.

Answer: B

Diff: 3 Type: MC

Topic: Markets for Illegal Goods

6) Suppose the cost of breaking the law is imposed on the sellers of an illegal good. This action will have its biggest impact on quantity if the demand for the good is

- A) inelastic or the supply is inelastic.
- B) elastic or the supply is elastic.
- C) elastic or the supply is inelastic.
- D) inelastic or the supply is elastic.
- E) perfectly inelastic.

Answer: B

Diff: 3 Type: MC

Topic: Markets for Illegal Goods

*Use the table below to answer the following questions.*

**Table 6.5.1**  
The Market for a Prohibited Good.

Price (dollars)	Quantity Demanded (units)	Quantity Supplied (units)
5	700	100
6	600	200
7	500	300
8	400	400
9	300	500
10	200	600
11	100	700

7) Refer to Table 6.5.1. Which one of the following costs of breaking the law imposed on the buyers of the good would reduce the quantity to zero?

- A) \$1
- B) \$2
- C) \$4
- D) \$6
- E) \$8

Answer: E

Diff: 3 Type: MC

Topic: Markets for Illegal Goods



8) Refer to Table 6.5.1. If a \$2-per-unit cost of breaking the law is imposed on buyers, the new price is \_\_\_\_\_ and the new equilibrium quantity is \_\_\_\_\_ units.

- A) \$8; 400
- B) \$8; 300
- C) \$7; 300
- D) \$9; 300
- E) \$8; 200

Answer: C

Diff: 3 Type: MC

Topic: Markets for Illegal Goods

9) Refer to Table 6.5.1. If a \$2-per-unit cost of breaking the law is imposed on sellers, the new price is \_\_\_\_\_ and the new equilibrium quantity is \_\_\_\_\_ units.

- A) \$8; 400
- B) \$8; 300
- C) \$7; 300
- D) \$9; 300
- E) \$8; 200

Answer: D

Diff: 3 Type: MC

Topic: Markets for Illegal Goods

10) Refer to Table 6.5.1. If a \$2-per-unit cost of breaking the law is imposed on sellers, the price received by sellers (net of the cost of breaking the law) would be

- A) \$8.
- B) \$7.
- C) \$9.
- D) \$10.
- E) \$6.

Answer: B

Diff: 3 Type: MC

Topic: Markets for Illegal Goods

11) Refer to Table 6.5.1. If a \$2-per-unit cost of breaking the law is imposed on both the buyers and the sellers, the new price is \_\_\_\_\_ and the new equilibrium quantity is \_\_\_\_\_ units.

- A) \$8; 400
- B) \$8; 300
- C) \$7; 300
- D) \$9; 300
- E) \$8; 200

Answer: E

Diff: 3 Type: MC

Topic: Markets for Illegal Goods

12) If enforcement of the law is aimed at buyers of an illegal good, the result will be

- A) an increase in the supply of the good.
- B) a decrease in the supply of the good.
- C) a decrease in the demand for the good.
- D) a rise in the price of the good.
- E) no change in the equilibrium quantity.

Answer: C

Diff: 2 Type: MC

Topic: Markets for Illegal Goods

13) Provincial governments across Canada recently started legalizing and then heavily taxing gambling at casinos. The new taxes are lower than the cost of breaking the law was to the sellers of the previously illegal casino services. The costs of breaking the law to the buyers of these services also fell to zero. This change will likely lead to

- A) a rise in the equilibrium price, and a decrease in the equilibrium quantity.
- B) a rise in the equilibrium price, and an increase in the equilibrium quantity.
- C) a fall in the equilibrium price, and an increase in the equilibrium quantity.
- D) a fall in the equilibrium price, and a decrease in the equilibrium quantity.
- E) an unknown change in equilibrium price and equilibrium quantity.

Answer: B

Diff: 3 Type: MC

Topic: Markets for Illegal Goods

14) All of the following statements about legalizing and taxing drugs are true *except*

- A) legalizing and taxing drugs would eliminate the black market in drugs.
- B) the quantity of a drug bought could be decreased if the drug was legalized and taxed.
- C) a sufficiently high tax could be imposed to decrease supply, raise the price, and achieve the same decrease in the quantity bought as with a prohibition of drugs.
- D) an extremely high tax rate would be needed to cut the quantity of drugs bought to the level prevailing with a prohibition.
- E) tax revenue can be used to make law enforcement more effective.

Answer: A

Type: MC

Topic: Markets for Illegal Goods

Source: MyEconLab

15) A fact that argues in favour of prohibition and against taxes on illegal drugs is that

- A) prohibition sends a signal that might influence preferences.
- B) penalties for illegal activities with prohibition are less than the penalties for tax evasion.
- C) a black market is easier to maintain under prohibition than under the tax code.
- D) search activity decreases with prohibition.
- E) all of the above.

Answer: A

Type: MC

Topic: Markets for Illegal Goods

Source: MyEconLab

16) Suppose that buying and selling a certain good is made illegal. In the market for this good, the demand curve shifts \_\_\_\_\_ and the supply curve shifts \_\_\_\_\_.

- A) rightward; rightward
- B) leftward; leftward
- C) rightward; leftward
- D) leftward; rightward
- E) None of the above. Neither the demand curve nor the supply curve shift.

Answer: B

Type: MC

17) If the penalty on sellers of an illegal good is less than the penalty on buyers of an illegal good, then supply of the good will \_\_\_\_\_ by \_\_\_\_\_ demand and the price of the good will \_\_\_\_\_.

- A) decrease; more than; rise
- B) decrease; less than; rise
- C) decrease; less than; fall
- D) decrease; more than; fall
- E) increase; less than; rise

Answer: C

Type: MC

## Chapter 7 Global Markets in Action

### 7.1 How Global Markets Work

1) Goods and services that we buy from other countries are our

- A) balance of payments.
- B) exports.
- C) imports.
- D) terms of trade.
- E) comparative goods and services.

Answer: C

Type: MC

Topic: How Global Markets Work

Skill: Recognition

AACSB: Reflective Thinking

2) The goods and services we sell to people in other countries are our

- A) tariffs.
- B) quotas.
- C) exports.
- D) imports.
- E) investment goods and services.

Answer: C

Type: MC

Topic: How Global Markets Work

Skill: Recognition

AACSB: Reflective Thinking

3) The fundamental force that drives international trade is

- A) absolute advantage.
- B) importation duties.
- C) the advantage of execution.
- D) export advantage.
- E) comparative advantage.

Answer: E

Type: MC

Topic: How Global Markets Work

Skill: Recognition

AACSB: Reflective Thinking

4) The fundamental force that drives international trade is

- A) comparative advantage.
- B) absolute advantage.
- C) a countries' desire to increase their trade surplus.
- D) cheap labour in countries like China and India.
- E) unemployment of factors of production.

Answer: A

Diff: 2 Type: MC

Topic: How Global Markets Work

Skill: Recognition

AACSB: Reflective Thinking

5) A country

- A) imports those goods in which it has a comparative advantage.
- B) exports those goods in which it has a comparative advantage.
- C) imports goods produced in countries with lower wage rates.
- D) exports goods produced by domestic industries with low wages relative to its trading partners.
- E) B and D are correct.

Answer: B

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

AACSB: Reflective Thinking

6) Canada has a comparative advantage in producing airplanes if

- A) it can produce them at a lower dollar cost than another country.
- B) it can produce a larger quantity than another country.
- C) it has a larger quantity of skilled workers than another country.
- D) it can produce them at a higher opportunity cost than another country.
- E) it can produce them at a lower opportunity cost than another country.

Answer: E

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

AACSB: Reflective Thinking

7) Prior to international trade, if the price of good X is lower in country A than in country B,

- A) country B has an absolute advantage in the production of good X.
- B) country B has a comparative advantage in the production of good X.
- C) country A has an absolute advantage in the production of good X.
- D) country A has a comparative advantage in the production of good X.
- E) country B should stop producing good X.

Answer: D

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

AACSB: Reflective Thinking

8) Which of the following statements about Canada's international trade in 2010 is correct?

- A) The value of Canada's imports exceeded the value of Canada's exports.
- B) The value of Canada's exports was about 45 percent of the value of total expenditure in Canada.
- C) Canada imported only goods.
- D) Canada was the world's second largest trader.
- E) Canada exported only goods.

Answer: A

Type: MC

Topic: How Global Markets Work

Skill: Recognition

AACSB: Reflective Thinking

9) Canada has a comparative advantage in producing hardwood if the Canadian price of hardwood before international trade is \_\_\_\_\_ the world price.

- A) equal to
- B) greater than
- C) not comparable to
- D) at least double
- E) less than

Answer: E

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

AACSB: Reflective Thinking

10) Compared to the situation before international trade, after Canada exports a good, production in Canada \_\_\_\_\_ and consumption in Canada \_\_\_\_\_.

- A) increases; increases
- B) increases; decreases
- C) decreases; increases
- D) decreases; decreases
- E) increases; does not change

Answer: B

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

AACSB: Analytical Skills

11) Compared to the situation before international trade, after Canada imports a good, production in Canada \_\_\_\_\_ and consumption in Canada \_\_\_\_\_.

- A) increases; increases
- B) increases; decreases
- C) decreases; increases
- D) decreases; decreases
- E) does not change; increases

Answer: C

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

AACSB: Analytical Skills

12) Which of the following is a Canadian service export?

- A) a Canadian buys dinner while travelling in Switzerland
- B) a Swiss buys dinner while travelling in Canada
- C) a Canadian buys a clock made in Switzerland
- D) a Swiss buys a computer made in Canada
- E) a Canadian buys a Canadian computer in Switzerland

Answer: B

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

Refer to the table below to answer the following questions.

**Table 7.1.1**  
Glazeland's Doughnut Market

Price (dollars per doughnut)	Glazeland's Supply (millions)	Glazeland's Demand (millions)
0.20	1	10
0.30	2	8
0.40	3	6
0.50	4	4
0.60	5	2
0.70	6	0

13) Table 7.1.1 shows Glazeland's doughnut market before international trade. Glazeland opens up to international trade. If the world price is \$0.60, then Glazeland will produce \_\_\_\_\_ doughnuts and will \_\_\_\_\_ doughnuts.

- A) 2 million; import 3 million
- B) 4 million; import 1 million
- C) 4 million; export 1 million
- D) 5 million; import 3 million
- E) 5 million; export 3 million

Answer: E

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

14) Table 7.1.1 shows Glazeland's doughnut market before international trade. Glazeland opens up to international trade. If the world price is \$0.40, then Glazeland will produce \_\_\_\_\_ doughnuts and will \_\_\_\_\_ doughnuts.

- A) 3 million; import 3 million
- B) 3 million; export 3 million
- C) 4 million; import 1 million
- D) 4 million; export 1 million
- E) 6 million; export 3 million

Answer: A

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

15) Canada produces both lumber and wine. Canada exports lumber and imports wine. The rest of the world imports Canadian lumber and exports wine to Canada. If Canada did *not* trade with the rest of the world, then the equilibrium price of lumber would be \_\_\_\_\_ in Canada than the rest of the world, and the equilibrium price of wine would be \_\_\_\_\_ in Canada than the rest of the world.

- A) lower; higher
- B) higher; lower
- C) higher; higher
- D) lower; lower
- E) the same or lower; the same or higher

Answer: A

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

Source: MyEconLab

AACSB: Analytical Skills

16) Canada produces both lumber and wine. Canada exports lumber and imports wine. The rest of the world imports Canadian lumber and exports wine to Canada. Canada has a comparative advantage in producing \_\_\_\_\_. The rest of the world has a comparative advantage in producing \_\_\_\_\_.

- A) lumber; wine
- B) wine; lumber
- C) wine; wine
- D) lumber; lumber
- E) a good other than lumber or wine; wine

Answer: A

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

Source: MyEconLab

AACSB: Analytical Skills

17) In one year, Brazil exported more than 1.8 billion kilograms of coffee to the rest of the world. We can conclude that

- A) Brazil has comparative advantage in coffee production.
- B) Brazil has an absolute advantage in coffee production.
- C) the rest of the world has a comparative advantage in coffee production.
- D) the rest of the world has an absolute advantage in coffee production.
- E) Brazil's government has placed a tariff on coffee.

Answer: A

Type: MC

18) Choose the correct statement.

- A) Exports include goods and services.
- B) Imports include goods but not services.
- C) Imports include services but not goods.
- D) Exports include goods but not services.
- E) Exports include services but not goods.

Answer: A

Type: MC

## 7.2 Winners, Losers, and the Net Gain from Trade

1) Consider a country that sells some of its goods as exports. Who does *NOT* benefit?

- A) domestic consumers
- B) domestic producers
- C) workers in the industry
- D) foreign consumers
- E) everyone benefits

Answer: A

Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Conceptual

AACSB: Analytical Skills

2) Who benefits from imports?

- A) domestic consumers
- B) domestic producers
- C) foreign consumers
- D) domestic workers in the industry
- E) everyone benefits

Answer: A

Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Conceptual

AACSB: Analytical Skills

3) A country opens up to trade and becomes an importer of some good. Consumer surplus \_\_\_\_\_, producer surplus \_\_\_\_\_, and total surplus \_\_\_\_\_.

- A) increases; decreases; decreases
- B) decreases; decreases; decreases
- C) decreases; increases; increases
- D) increases; increases; increases
- E) increases; decreases; increases

Answer: E

Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Conceptual

AACSB: Analytical Skills

- 4) A country opens up to trade. In an import industry, surplus has been redistributed from
- A) producers to consumers.
  - B) consumers to producers.
  - C) government to consumers.
  - D) producers to government.
  - E) none of the above.

Answer: A

Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Conceptual

AACSB: Analytical Skills

*Refer to the table below to answer the following questions.*

**Table 7.2.1**

Price (dollars)	Quantity demanded (units)	Quantity supplied (units)
2	100	70
4	95	75
6	90	80
8	85	85
10	80	90
12	75	95

- 5) The table shows a country's demand and supply schedules. Based on Table 7.2.1, at what world price would the country import?

- A) at exactly \$8 a unit
- B) any price above \$8 a unit
- C) a price of \$10 a unit
- D) a price of \$20 a unit
- E) a price below \$8 a unit

Answer: E

Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

AACSB: Analytical Skills

6) The table shows a country's demand and supply schedules. Based on Table 7.2.1, suppose the world price is \$4 a unit. The country

- A) imports 20 units.
- B) exports 20 units.
- C) imports 10 units.
- D) exports 10 units.
- E) imports 30 units.

Answer: A

Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

AACSB: Analytical Skills

7) A market is open to international trade. At the world price, the quantity demanded is 150 units and the quantity supplied is 200 units. This country will

- A) import 50 units.
- B) export 200 units.
- C) import 150 units.
- D) import 200 units.
- E) export 50 units.

Answer: E

Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Conceptual

AACSB: Analytical Skills

8) A country opens up to trade and becomes an exporter of a good. Consumer surplus \_\_\_\_\_, producer surplus \_\_\_\_\_, and total surplus \_\_\_\_\_.

- A) decreases; increases; increases
- B) increases; decreases; increases
- C) decreases; increases; decreases
- D) remains unchanged; increases; increases
- E) decreases; decreases; decreases

Answer: A

Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Conceptual

AACSB: Analytical Skills

- 9) A country opens up to trade. In an export industry, surplus has been redistributed from
- A) consumers to producers.
  - B) producers to consumers.
  - C) producers to government.
  - D) government to consumers.
  - E) none of the above.

Answer: A

Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Conceptual

AACSB: Communication

*Refer to the table below to answer the following question.*

**Table 7.2.2**

Price (dollars)	Quantity demanded (units)	Quantity supplied (units)
2	100	70
4	95	75
6	90	80
8	85	85
10	80	90
12	75	95

- 10) The table shows a country's demand and supply schedules. Based on Table 7.2.2, at what world price would the country export?

- A) at only \$8 a unit
- B) any price below \$8
- C) a price of \$6 a unit
- D) a price of \$4 a unit
- E) any price above \$8 a unit

Answer: E

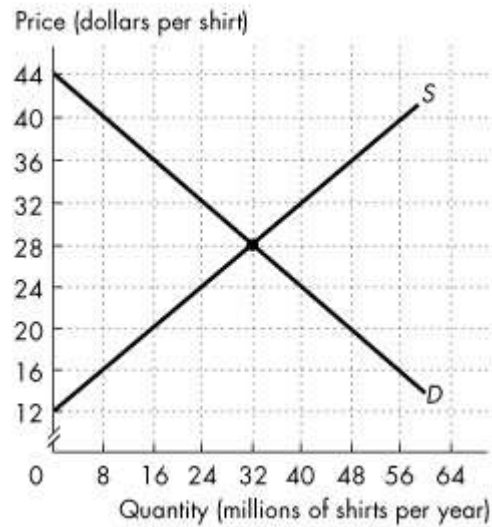
Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

AACSB: Analytical Skills

Refer to the figure below to answer the following questions.



The figure shows the market for shirts in Canada, where  $D$  is the domestic demand curve and  $S$  is the domestic supply curve. The world price is \$20 per shirt.

**Figure 7.2.1**

11) In Figure 7.2.1, with international trade Canadians buy \_\_\_\_\_ million shirts per year.

- A) 48
- B) 32
- C) 16
- D) 24
- E) 56

Answer: A

Diff: 2 Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

AACSB: Analytical Skills

12) In Figure 7.2.1, with international trade \_\_\_\_\_ million shirts per year are produced in Canada.

- A) 48
- B) 32
- C) 20
- D) 56
- E) 16

Answer: E

Diff: 2 Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

AACSB: Analytical Skills

13) In Figure 7.2.1, with international trade Canada \_\_\_\_\_ million shirts per year.

- A) imports 32
- B) imports 48
- C) exports 16
- D) exports 32
- E) imports 16

Answer: A

Diff: 2 Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

AACSB: Analytical Skills

14) In Figure 7.2.1, international trade \_\_\_\_\_ consumer surplus in Canada by \_\_\_\_\_.

- A) increases; \$320 million
- B) decreases; \$192 million
- C) increases; \$192 million
- D) decreases; \$320 million
- E) increases; \$576 million

Answer: A

Diff: 3 Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

AACSB: Analytical Skills

15) In Figure 7.2.1, international trade \_\_\_\_\_ producer surplus in Canada by \_\_\_\_\_.

- A) increases; \$320 million
- B) decreases; \$192 million
- C) increases; \$192 million
- D) decreases; \$320 million
- E) decreases; \$256 million

Answer: B

Diff: 3 Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

AACSB: Analytical Skills

16) In Figure 7.2.1, international trade \_\_\_\_\_ total surplus in Canada by \_\_\_\_\_.

- A) increases; \$128 million
- B) decreases; \$192 million
- C) increases; \$320 million
- D) decreases; \$256 million
- E) decreases; \$128 million

Answer: A

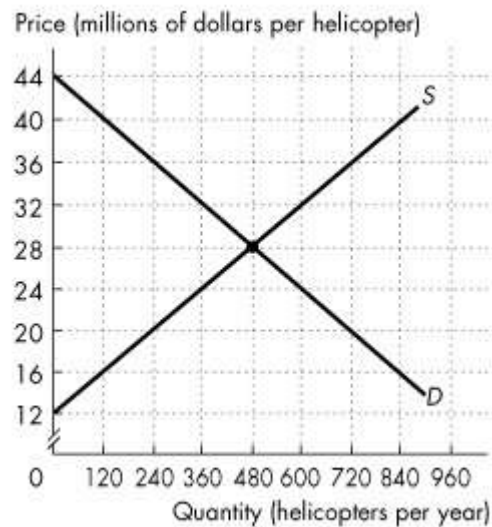
Diff: 3 Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

AACSB: Analytical Skills

Refer to the figure below to answer the following questions.



The figure shows the market for helicopters in Canada, where  $D$  is the domestic demand curve and  $S$  is the domestic supply curve. Canada trades helicopters with the rest of the world at a price of \$36 million per helicopter.

**Figure 7.2.2**

17) In Figure 7.2.2, with international trade Canadian firms buy \_\_\_\_\_ helicopters per year.

- A) 240
- B) 480
- C) 720
- D) 360
- E) 600

Answer: A

Diff: 2 Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

AACSB: Analytical Skills

18) In Figure 7.2.2, with international trade \_\_\_\_\_ helicopters per year are produced in Canada.

- A) 360
- B) 480
- C) 720
- D) 240
- E) 600

Answer: C

Diff: 2 Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

AACSB: Analytical Skills

19) In Figure 7.2.2, Canada \_\_\_\_\_ helicopters per year.

- A) exports 480
- B) exports 720
- C) imports 480
- D) imports 240
- E) exports 240

Answer: A

Diff: 2 Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

AACSB: Analytical Skills

20) In Figure 7.2.2, international trade \_\_\_\_\_ consumer surplus in Canada by \_\_\_\_\_.

- A) decreases; \$2.88 billion
- B) decreases; \$1.92 billion
- C) increases; \$2.88 billion
- D) increases; \$4.8 billion
- E) increases; \$1.92 billion

Answer: A

Diff: 3 Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

AACSB: Analytical Skills

21) In Figure 7.2.2, international trade \_\_\_\_\_ producer surplus in Canada by \_\_\_\_\_.

- A) decreases; \$2.88 billion
- B) decreases; \$1.92 billion
- C) increases; \$4.8 billion
- D) increases; \$3.6 billion
- E) decreases; \$4.8 billion

Answer: C

Diff: 3 Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

AACSB: Analytical Skills

22) In Figure 7.2.2, international trade \_\_\_\_\_ total surplus in Canada by \_\_\_\_\_.

- A) decreases; \$2.56 billion
- B) increases; \$4.8 billion
- C) decreases; \$3.6 billion
- D) decreases; \$1.92 billion
- E) increases; \$1.92 billion

Answer: E

Diff: 3 Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

AACSB: Analytical Skills

23) Canada's producer surplus \_\_\_\_\_ when Canada imports a good and Canada's producer surplus \_\_\_\_\_ when Canada exports a good.

- A) increases; increases
- B) increases; decreases
- C) decreases; increases
- D) decreases; decreases
- E) does not change; does not change

Answer: C

Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Conceptual

AACSB: Analytical Skills

24) When Canada exports a good, Canada's consumer surplus \_\_\_\_\_ and Canada's total surplus \_\_\_\_\_.

- A) increases; increases
- B) increases; decreases
- C) decreases; increases
- D) decreases; decreases
- E) decreases and Canada's producer surplus increases; does not change

Answer: C

Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Conceptual

AACSB: Analytical Skills

25) When Canada exports a good, the amount of the \_\_\_\_\_ in Canada's consumer surplus is \_\_\_\_\_ the amount of the \_\_\_\_\_ in Canada's producer surplus.

- A) increase; smaller than; increase
- B) increase; larger than; decrease
- C) decrease; smaller than; increase
- D) decrease; equal to; decrease
- E) decrease; equal to; increase

Answer: C

Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

AACSB: Analytical Skills

26) Canada exports athletic coaching services and imports computer tech support. The price of athletic coaching services in Canada is \_\_\_\_\_ with international trade than without international trade. As a result of trade in athletic coaching services, the Canadian producer surplus from athletic coaching services \_\_\_\_\_ and the Canadian consumer surplus from athletic coaching services \_\_\_\_\_.

- A) higher; increases; increases
- B) lower; decreases; decreases
- C) lower; decreases; increases
- D) higher; increases; decreases
- E) higher; decreases; increases

Answer: D

Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

Source: MyEconLab

AACSB: Analytical Skills

27) Canada exports athletic coaching services and imports computer tech support. The price of computer tech support in Canada is \_\_\_\_\_ with international trade than without international trade. As a result of trade in computer tech support, the Canadian producer surplus from computer tech support \_\_\_\_\_ and the Canadian consumer surplus from computer tech support \_\_\_\_\_.

- A) higher; increases; increases
- B) lower; decreases; increases
- C) lower; decreases; decreases
- D) higher; increases; decreases
- E) lower; increases; increases

Answer: B

Type: MC

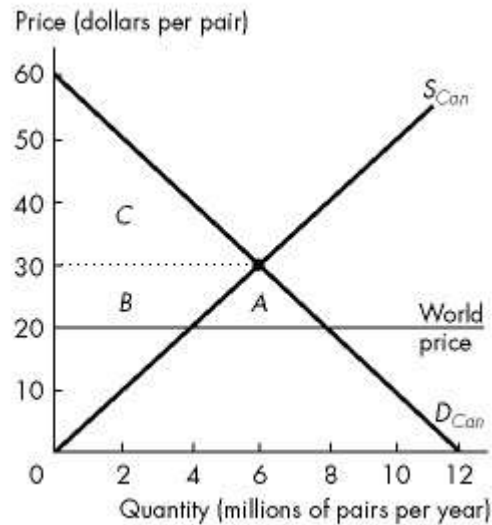
Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

Source: MyEconLab

AACSB: Analytical Skills

Refer to the figure below to answer the following question.



**Figure 7.2.3**

28) Refer to Figure 7.2.3. The graph shows the market for shoes in Canada. The world price of a pair of shoes is \$20. With free international trade, Canadian consumer surplus \_\_\_\_\_ and Canadian producer surplus \_\_\_\_\_.

- A) increases by area  $A + B$ ; decreases by area  $B$
- B) increases by area  $B$ ; decreases by area  $B$
- C) increases by area  $A$ ; decreases by area  $B$
- D) decreases by area  $A + B$ ; increases by area  $B$
- E) decreases by area  $B$ ; increases by area  $A$

Answer: A

Type: MC

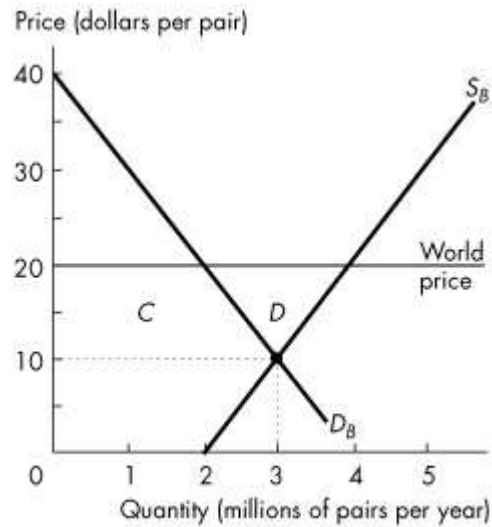
Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

Source: MyEconLab

AACSB: Analytical Skills

Refer to the figure below to answer the following question.



**Figure 7.2.4**

29) Refer to Figure 7.2.4. The graph shows the demand for shoes in Brazil,  $D_B$ , the supply of shoes produced in Brazil,  $S_B$ , and the market equilibrium in Brazil when it does not trade internationally. If the world price of a pair of shoes is \$20 and Brazil opens up and trades internationally, producer surplus in Brazil \_\_\_\_\_ and consumer surplus in Brazil \_\_\_\_\_.

- A) increases by area  $C + D$ ; decreases by area  $C$
- B) increases by area  $C$ ; decreases by area  $C$  and a deadweight loss equal to area  $D$  arises
- C) increases by area  $D$ ; decreases by area  $D$
- D) decreases by area  $C$ ; increases by area  $C + D$
- E) decreases by area  $C + D$ ; increases by area  $C$

Answer: A

Type: MC

Topic: Winners, Losers, and the Net Gain from Trade

Skill: Analytical

Source: MyEconLab

AACSB: Analytical Skills

30) In one year, Brazil exported more than 1.8 billion kilograms of coffee to the rest of the world. We can conclude that

- A) Brazil's coffee producers lose from this trade.
- B) coffee consumers in the rest of the world lose from this trade.
- C) Brazil's coffee consumers lose from this trade.
- D) coffee producers in the rest of the world gain from this trade.
- E) the deadweight loss in Brazil's coffee market is large and growing.

Answer: C

Type: MC

31) In a market that moves from a situation of no trade to a situation where a good is exported, the price of the good \_\_\_\_\_, the quantity produced by the domestic industry \_\_\_\_\_, and producer surplus \_\_\_\_\_.

- A) rises; increases; increases
- B) falls; decreases; decreases
- C) does not change; increases; increases
- D) does not change; decreases; decreases
- E) rises; increases; decreases

Answer: A

Type: MC

32) In a market that moves from a situation of no trade to a situation where a good is imported, the price of the good \_\_\_\_\_, the quantity produced by the domestic industry \_\_\_\_\_, and producer surplus \_\_\_\_\_.

- A) rises; increases; increases
- B) falls; decreases; decreases
- C) does not change; increases; increases
- D) does not change; decreases; decreases
- E) rises; increases; decreases

Answer: B

Type: MC

### 7.3 International Trade Restrictions

1) A tariff is a tax that is imposed by the \_\_\_\_\_ country when an \_\_\_\_\_ good crosses its international boundary.

- A) exporting; imported
- B) importing; exported
- C) exporting; exported
- D) importing; imported
- E) importing or exporting; imported or exported

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Reflective Thinking

2) A tax that is imposed by the importing country when an imported good crosses its international boundary is called

- A) an import quota.
- B) dumping.
- C) a voluntary export restraint.
- D) a tariff.
- E) a sales tax.

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Reflective Thinking

3) Tariffs and import quotas differ in that

- A) one is a form of trade restriction, while the other is not.
- B) one is a tax, while the other is a limit.
- C) one is imposed by the government, while the other is imposed by the private sector.
- D) one is legal, while the other is not.
- E) one increases imports, while the other decreases imports.

Answer: B

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Reflective Thinking

- 4) Tariffs and import quotas both result in
- A) lower levels of domestic production.
  - B) the domestic government gaining revenue.
  - C) lower levels of imports.
  - D) higher levels of domestic consumption.
  - E) the elimination of deadweight loss.

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

- 5) If Canada imposes a tariff on imported cars,
- A) Canada's demand curve for cars shifts rightward.
  - B) Canada's demand curve for cars shifts leftward.
  - C) Canada's supply curve of cars shifts rightward.
  - D) Canada's supply curve of cars shifts leftward.
  - E) the price in Canada rises but neither Canada's demand curve nor Canada's supply curve shifts.

Answer: E

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Analytical Skills

- 6) Which of the following statements concerning tariffs is *NOT* true?

- A) A tariff results in a deadweight loss.
- B) A tariff creates revenue for the government.
- C) A tariff decreases international trade.
- D) A tariff leaves the price of imports unchanged.
- E) A tariff decreases consumer surplus.

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Communication

7) If a country imposes a tariff on an imported good, the tariff \_\_\_\_\_ the price in the importing country and \_\_\_\_\_ the quantity of imports.

- A) raises; increases
- B) raises; does not change
- C) lowers; does not change
- D) lowers; increases
- E) raises; decreases

Answer: E

Type: MC

Topic: International Trade Restrictions

Skill: Analytical

AACSB: Analytical Skills

8) A tariff imposed by Canada on Japanese cars \_\_\_\_\_ the price of cars in Canada and \_\_\_\_\_ the quantity of Japanese cars imported into Canada.

- A) raises; increases
- B) raises; decreases
- C) lowers; increases
- D) lowers; decreases
- E) raises; does not change

Answer: B

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

9) If Canada imposes a tariff of \$1 per imported shirt, the tariff

- A) raises the price of a shirt paid by Canadian consumers.
- B) benefits Canadian shirt producers.
- C) decreases imports of shirts into Canada.
- D) creates a deadweight loss.
- E) all of the above.

Answer: E

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Communication

- 10) If Canada imposes a tariff on imported steel, the tariff
- A) raises the Canadian price of imported steel.
  - B) decreases the Canadian production of steel.
  - C) increases the total Canadian consumption of steel.
  - D) decreases employment in the Canadian steel industry.
  - E) all of the above.

Answer: A

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

- 11) Suppose the country of Mooland imposes tariffs on imported beef from the country of Aqualand. As a result of the tariffs, the
- A) price of beef in Mooland falls.
  - B) quantity of beef exported by Mooland increases.
  - C) quantity of beef imported by Mooland decreases.
  - D) quantity of beef imported by Mooland increases.
  - E) price of beef in Mooland does not change.

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

- 12) Reducing a tariff \_\_\_\_\_ the domestic production of the good and \_\_\_\_\_ the total domestic consumption of the good.
- A) increases; increases
  - B) increases; decreases
  - C) decreases; increases
  - D) decreases; decreases
  - E) does not change; increases

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

13) Increasing a tariff \_\_\_\_\_ the domestic quantity consumed of the good and \_\_\_\_\_ the domestic production of the good.

- A) increases; increases
- B) increases; decreases
- C) decreases; increases
- D) decreases; decreases
- E) decreases; does not change

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

14) Tariffs

- A) generate revenue for consumers.
- B) generate revenue for the government.
- C) encourage domestic consumers to buy more imports.
- D) encourage domestic producers to produce less.
- E) lower prices for consumers.

Answer: B

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Reflective Thinking

15) Canada imports cars from Japan. If Canada imposes a tariff on cars imported from Japan, Canadian

- A) consumers will lose and Japanese producers will gain.
- B) tariff revenue will equal the loss of Canadian consumer surplus.
- C) consumers will lose and Canadian producers will gain.
- D) car manufacturers will gain revenue equal to the revenue lost by Japanese car manufacturers.
- E) producers will lose and Japanese consumers will gain.

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Analytical

AACSB: Analytical Skills

16) A Canadian tariff imposed on items that can be produced more cheaply abroad

- A) benefits Canadians by making these goods cheaper.
- B) makes the goods more expensive in foreign markets.
- C) creates a deadweight loss.
- D) equalizes the cost of production between Canada and foreign producers.
- E) All of the above.

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Reflective Thinking

17) A tariff is imposed on imports. Surplus will be redistributed from

- A) consumers to producers only.
- B) consumers to government only.
- C) government to producers only.
- D) government to consumers only.
- E) consumers to producers and government.

Answer: E

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Reflective Thinking

18) The winners from a tariff on imports are

- A) producers and government.
- B) producers only.
- C) consumers only.
- D) consumers, producers, and government.
- E) government only.

Answer: A

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Ethical Reasoning

19) A tariff is imposed on a good. This \_\_\_\_\_ the quantity supplied, \_\_\_\_\_ the quantity demanded, and \_\_\_\_\_ the price in the home country.

- A) increases; decreases; raises
- B) increases; does not change; does not change
- C) increases; increases; raises
- D) increases; decreases; lowers
- E) decreases; increases; lowers

Answer: A

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Reflective Thinking

20) A tariff is imposed on a good. This \_\_\_\_\_ producer surplus, \_\_\_\_\_ consumer surplus, and \_\_\_\_\_ total surplus in the home country.

- A) increases; decreases; increases
- B) increases; does not change; increases
- C) increases; increases; increases
- D) decreases; decreases; decreases
- E) increases; decreases; decreases

Answer: E

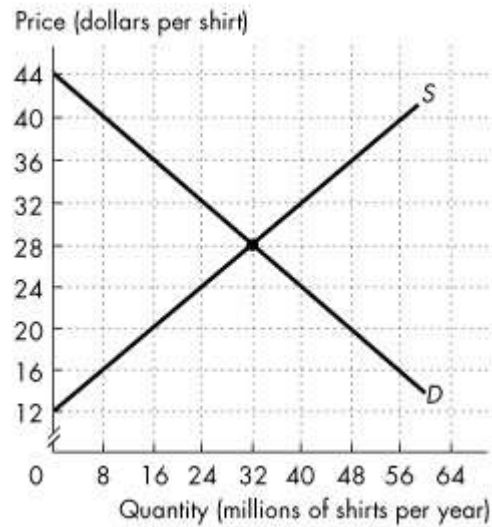
Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Reflective Thinking

Refer to the figure below to answer the following questions.



The figure shows the market for shirts in Canada, where D is the domestic demand curve and S is the domestic supply curve. The world price is \$20 per shirt. Canada imposes a tariff on imported shirts of \$4 per shirt.

**Figure 7.3.1**

21) Refer to Figure 7.3.1, with the tariff Canadians buy \_\_\_\_\_ million shirts per year.

- A) 48
- B) 32
- C) 16
- D) 24
- E) 40

Answer: E

Diff: 2 Type: MC

Topic: International Trade Restrictions

Skill: Analytical

AACSB: Analytical Skills

22) Refer to Figure 7.3.1, with the tariff Canada imports \_\_\_\_\_ million shirts per year.

- A) 24
- B) 8
- C) 32
- D) 16
- E) 40

Answer: D

Diff: 2 Type: MC

Topic: International Trade Restrictions

Skill: Analytical

AACSB: Analytical Skills

23) Refer to Figure 7.3.1, the tariff \_\_\_\_\_ Canada's imports of shirts by \_\_\_\_\_ million shirts per year.

- A) decreases; 16
- B) decreases; 8
- C) increases; 8
- D) increases; 4
- E) increases; 16

Answer: A

Diff: 2 Type: MC

Topic: International Trade Restrictions

Skill: Analytical

AACSB: Analytical Skills

24) Refer to Figure 7.3.1, the tariff \_\_\_\_\_ the domestic production of shirts in Canada by \_\_\_\_\_ per year.

- A) increases; 8 million
- B) decreases; 16 million
- C) increases; 4 million
- D) decreases; 8 million
- E) increases; 24 million

Answer: A

Diff: 2 Type: MC

Topic: International Trade Restrictions

Skill: Analytical

AACSB: Analytical Skills

25) Refer to Figure 7.3.1, the Canadian government's revenue from the tariff is \_\_\_\_\_.

- A) \$64 million
- B) \$32 million
- C) \$128 million
- D) \$48 million
- E) \$480 million

Answer: A

Diff: 2 Type: MC

Topic: International Trade Restrictions

Skill: Analytical

AACSB: Analytical Skills

26) Refer to Figure 7.3.1, Canadian consumers' \_\_\_\_\_ from the tariff is \_\_\_\_\_.

- A) loss; \$176 million
- B) gain; \$64 million
- C) loss; \$80 million
- D) gain; \$128 million
- E) gain; \$176 million

Answer: A

Diff: 3 Type: MC

Topic: International Trade Restrictions

Skill: Analytical

AACSB: Analytical Skills

27) Refer to Figure 7.3.1, Canadian producers' \_\_\_\_\_ from the tariff is \_\_\_\_\_.

- A) loss; \$32 million
- B) loss; \$64 million
- C) gain; \$80 million
- D) gain; \$128 million
- E) gain; \$64 million

Answer: C

Diff: 3 Type: MC

Topic: International Trade Restrictions

Skill: Analytical

AACSB: Analytical Skills

28) Refer to Figure 7.3.1, the deadweight loss from the tariff is \_\_\_\_\_.

- A) \$80 million
- B) \$16 million
- C) zero
- D) \$64 million
- E) \$32 million

Answer: E

Diff: 3 Type: MC

Topic: International Trade Restrictions

Skill: Analytical

AACSB: Analytical Skills

29) Of the following, in which decade were Canada's tariffs at their lowest level?

- A) 2000s
- B) 1970s
- C) 1950s
- D) 1930s
- E) 1890s

Answer: A

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Reflective Thinking

30) An import quota is

- A) a tariff that is a fixed percentage of the price of a good.
- B) a tariff that is a fixed dollar amount per unit of a good.
- C) an agreed upon price for a good to be imported at a specified future date.
- D) a restriction that specifies the maximum quantity of a good that may be imported in a given time period.
- E) the same as an export subsidy.

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Reflective Thinking

31) \_\_\_\_\_ specifies the maximum quantity of a good that may be imported in a given period of time.

- A) An import restriction
- B) A legislative restriction
- C) A trade restriction
- D) An import quota
- E) An import subsidy

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Reflective Thinking

32) Import quotas

- A) are the same as tariffs.
- B) are not used by Canada.
- C) set the minimum percentage of the value of a product that must consist of imported components.
- D) benefit society.
- E) set the maximum number of units of a good that can be imported in a given time period.

Answer: E

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Reflective Thinking

33) An import quota is a

- A) tariff imposed on goods that are dumped in the country.
- B) law that prevents ecologically damaging goods from being imported into a country.
- C) market-imposed balancing factor that keeps prices of imports and exports in equilibrium.
- D) government-imposed restriction on the quantity of a specific good that can be imported.
- E) tax in an international market.

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Reflective Thinking

34) An import quota directly restricts \_\_\_\_\_ and are designed to protect domestic \_\_\_\_\_.

- A) exports; consumers only
- B) exports; producers only
- C) imports; consumers only
- D) imports; producers only
- E) imports; producers and consumers

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

35) Import quotas \_\_\_\_\_ the price of imported goods and \_\_\_\_\_ the quantity consumed in the country imposing the quota.

- A) raise; increase
- B) raise; decrease
- C) lower; increase
- D) lower; decrease
- E) raise; do not change

Answer: B

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

36) If a government imposes a quota on imports of a popular doll, the price of the doll in the importing country \_\_\_\_\_ and the quantity purchased in the importing country \_\_\_\_\_.

- A) rises; increases
- B) rises; decreases
- C) falls; increases
- D) falls; decreases
- E) rises; does not change

Answer: B

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

37) A key difference between tariffs and import quotas is that

- A) consumers are hurt with import quotas but not with tariffs.
- B) consumers are hurt with tariffs but not with import quotas.
- C) the government receives revenue with a tariff, but the importer makes a profit with an import quota.
- D) the government receives revenue with an import quota, but the importer makes a profit with a tariff.
- E) producer surplus increases with a tariff and decreases with an import quota.

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Reflective Thinking

38) Import quotas and tariffs both

- A) decrease deadweight loss.
- B) cause a loss of revenue to domestic producers.
- C) lower prices on imported goods.
- D) decrease producer surplus.
- E) restrict foreign trade.

Answer: E

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Reflective Thinking

- 39) A difference between a quota and a tariff is that
- A) a tariff generates a higher price than does an import quota.
  - B) a tariff generates a greater reduction in exports than does an import quota.
  - C) an import quota increases profits of domestic producers more than a tariff.
  - D) the government collects revenue from a tariff but does not collect revenue from an import quota.
  - E) an import quota generates a deadweight loss and a tariff does not.

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Reflective Thinking

- 40) A tariff \_\_\_\_\_ consumer surplus and an import quota \_\_\_\_\_ consumer surplus.
- A) decreases; decreases
  - B) increases; increases
  - C) decreases; increases
  - D) increases; decreases
  - E) does not change; does not change

Answer: A

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

- 41) A tariff \_\_\_\_\_ the domestic price of the good and an import quota \_\_\_\_\_ the domestic price of the good.
- A) lowers; lowers
  - B) lowers; raises
  - C) raises; lowers
  - D) raises; raises
  - E) does not change; does not change

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

- 42) A tariff \_\_\_\_\_ a deadweight loss and an import quota \_\_\_\_\_ a deadweight loss.
- A) creates; creates
  - B) does not create; creates
  - C) creates; does not create
  - D) does not create; does not create
  - E) sometimes creates; always creates

Answer: A

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

*Refer to the table below to answer the following questions.*

**Table 7.3.1**  
Canada's Market for Widgets

Price (dollars per widgets)	Canadian Supply (millions)	Canadian Demand (millions)
5	12	52
6	16	48
7	20	44
8	24	40
9	28	36
10	32	32
12	36	28

- 43) Table 7.3.1 shows the Canadian supply of and demand for widgets. Widgets are available on the world market for \$7. If the Canadian government imposes a tariff of \$1, the domestic selling price will be \_\_\_\_\_ and quantity bought will be \_\_\_\_\_.

- A) \$6; 48 million
- B) \$7; 44 million
- C) \$8; 16 million
- D) \$8; 24 million
- E) \$8; 40 million

Answer: E

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

44) Table 7.3.1 shows the Canadian supply of and demand for widgets. Widgets are available on the world market for \$7. If the Canadian government imposes a tariff of \$1, how many widgets will Canada import?

- A) 32 million
- B) 24 million
- C) 16 million
- D) 28 million
- E) 40 million

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

45) Table 7.3.1 shows the Canadian supply of and demand for widgets. Widgets are available on the world market for \$7. Canadian widget producers convince the government to protect the domestic industry from cheap imports. If the Canadian government sets an import quota of 8 million widgets, the resulting price of a widget in Canada will be \_\_\_\_\_, and domestic production will be \_\_\_\_\_.

- A) \$6; 40 million
- B) \$7; 36 million
- C) \$8; 32 million
- D) \$9; 28 million
- E) \$10; 32 million

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

46) A tariff on watches which are imported by Atlantis \_\_\_\_\_ the price of watches in Atlantis and \_\_\_\_\_.

- A) lowers; imports of watches increase
- B) raises; watch production in Atlantis increases
- C) raises; watch production in Atlantis decreases
- D) lowers; watch production in Atlantis increases
- E) lowers; watch production in Atlantis decreases

Answer: B

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

47) The introduction of a tariff \_\_\_\_\_ consumer surplus, \_\_\_\_\_ producer surplus, and \_\_\_\_\_ total surplus.

- A) increases; decreases; decreases
- B) increases; increases; decreases
- C) decreases; decreases; decreases
- D) decreases; increases; decreases
- E) decreases; increases; increases

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

Refer to the figure below to answer the following question.

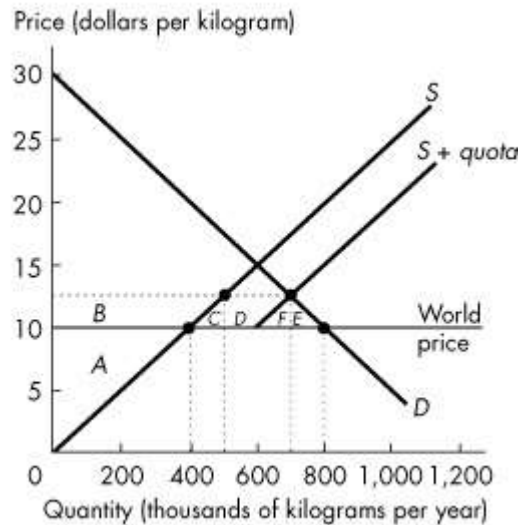


Figure 7.3.2

48) Refer to Figure 7.3.2. The supply of peanuts in Canada is made up of Canadian grown peanuts and imported peanuts. Initially, Canada engages in free trade in the peanut market. Then Canada puts a quota on peanut imports. The graph shows the Canadian market for peanuts when the Canadian government puts a quota on peanut imports. The Canadian consumer surplus that is redistributed to Canadian producers is \_\_\_\_\_ and the quota creates a deadweight loss equal to \_\_\_\_\_.

- A) area  $B + C + D + E$ ; zero
- B) area  $B + C + F$ ; area  $D$
- C) area  $B$ ; area  $D + E$
- D) area  $B$ ; area  $C + E$
- E) area  $B + C + D$ ; area  $E + F$

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

Source: MyEconLab

AACSB: Analytical Skills

49) Among the following, the domestic government gains the most revenue when it

- A) imposes an import quota.
- B) eliminates an import quota.
- C) encourages freer trade.
- D) imposes a tariff.
- E) increases the demand for a domestically-produced good.

Answer: D

Type: MC

- 50) If a quota is set at the same quantity of imports that results from a tariff,
- A) the deadweight loss from the tariff is greater than the deadweight loss from the import quota.
  - B) the deadweight loss from the tariff equals the deadweight loss from the import quota.
  - C) the deadweight loss from the import quota is greater than the deadweight loss from the tariff.
  - D) the government tariff revenue is greater than the importers' profit from the import quota.
  - E) the government tariff revenue is less than the importers' profit from the import quota.

Answer: B

Type: MC

## 7.4 The Case Against Protection

1) Economists usually agree with which of the following arguments that favour protectionism?

- A) the competition with cheap foreign labour defence
- B) the job protection defence
- C) the dumping defence
- D) the infant-industry defence
- E) None of the above. Economists generally agree that arguments in favor of protection are flawed.

Answer: E

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Ethical Reasoning

2) Which of the following are valid reasons advanced by almost all economists? Protection

- A) saves jobs.
- B) prevents rich countries from exploiting developing countries.
- C) is a good way for governments in developed nations to raise revenue.
- D) penalizes lax environmental standards.
- E) Economists would not support any of the above reasons.

Answer: E

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Ethical Reasoning

3) Which of the following are reasons economists consider valid for trade protection?

- I. Protection penalizes countries that have weak environmental standards.
- II. Protection limits dumping of low-wage jobs into the domestic economy.
- III. Protection prevents low-wage jobs in foreign countries from lowering wages in Canada.

- A) I and II
- B) II and III
- C) I, II, and III
- D) I and III
- E) None of the above

Answer: E

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Ethical Reasoning

4) The idea of comparative advantage changes is the basis for which of the following arguments for protection from foreign competition?

- A) the cheap foreign labour argument
- B) the infant-industry argument
- C) the dumping argument
- D) the saves jobs argument
- E) the prevents rich countries from exploiting developing countries argument

Answer: B

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Reflective Thinking

5) The most efficient way to encourage the growth of an infant-industry is through

- A) a voluntary export restraint.
- B) a tariff.
- C) a subsidy.
- D) an import quota.
- E) none of the above.

Answer: C

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Reflective Thinking

6) The proposition that protection is necessary to allow an infant industry to grow into a mature industry so that it can compete in world markets is the \_\_\_\_\_.

- A) infant-maturity argument
- B) infant-industry argument
- C) new industry proposition
- D) growth proposition
- E) dynamic comparative advantage argument

Answer: B

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Reflective Thinking

7) Dumping occurs when a foreign firm \_\_\_\_\_.

- A) pollutes international waters
- B) disposes of waste material internationally
- C) sells inferior output to foreigners
- D) sells its exports at a lower price than its cost of production
- E) sells its output at a lower price in a foreign country than in the country where it produces the good

Answer: D

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Reflective Thinking

8) \_\_\_\_\_ occurs when a foreign firm sells its exports at a lower price than its cost of production.

- A) Comparative advantage
- B) Learning-by-doing
- C) A tariff
- D) An infant industry
- E) Dumping

Answer: E

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Reflective Thinking

9) Suppose that the country of Pacifica sold its cars in Atlantica for less than it costs to produce the cars. Pacifica could be accused of

- A) avoiding import quotas.
- B) increasing its gains from trade.
- C) dumping.
- D) engaging in learning-by-doing.
- E) exploiting a comparative advantage.

Answer: C

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Reflective Thinking

- 10) When a firm "dumps" some of its output in another country, it
- A) creates an environmental hazard in the receiving country.
  - B) sells its output abroad at a price lower than it costs to produce the output.
  - C) increases the total level of employment in the importing country.
  - D) is specializing according to comparative advantage.
  - E) creates for itself an absolute advantage.

Answer: B

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Reflective Thinking

- 11) In poorer countries, free trade \_\_\_\_\_ the demand for labour in these countries and \_\_\_\_\_ the wages paid in these countries.

- A) decreases; lowers
- B) decreases; raises
- C) increases; lowers
- D) increases; raises
- E) increases the supply and decreases; lowers

Answer: D

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Reflective Thinking

- 12) Which of the following statements is true?

- A) International trade raises wages in developing countries.
- B) International trade with rich industrial countries forces people in the developing countries to work for lower wages.
- C) International trade leads to job losses in both import competing industries and exporting industries.
- D) Unlike other types of international trade, offshoring does not bring any gains from trade.
- E) All of the above.

Answer: A

Diff: 2 Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Reflective Thinking

- 13) The argument that protection \_\_\_\_\_.
- A) penalizes poor environmental standards is true
  - B) allows us to compete with cheap foreign wages is true
  - C) is necessary for infant industries is true
  - D) saves jobs is flawed
  - E) prevents rich countries from exploiting poor countries is true.

Answer: D

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Reflective Thinking

- 14) Which of the following is an explanation for the existence of trade restrictions?

- A) tariffs generate revenue for the government
- B) rent seeking
- C) inefficient quotas
- D) both A and B
- E) both A and C

Answer: D

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Reflective Thinking

- 15) In industrial countries, there is more reliance on \_\_\_\_\_, as opposed to \_\_\_\_\_ for government revenue.

- A) tariffs; tax collection
- B) import quotas; tariffs
- C) tariffs; import quotas
- D) import quotas; tax collection
- E) tax collection; tariffs

Answer: E

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Reflective Thinking

16) In developing countries, there is more reliance on \_\_\_\_\_ as opposed to \_\_\_\_\_ for government revenue.

- A) tariffs; tax collection
- B) import quotas; tariffs
- C) tax collection; tariffs
- D) tariffs; import quotas
- E) import quotas; tax collection

Answer: A

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Reflective Thinking

17) Of the groups listed below, which is most likely to lobby for protection?

- A) workers in the import industry
- B) workers in the export industry
- C) consumers in the import industry
- D) producers in the export industry
- E) All of the above.

Answer: A

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Ethical Reasoning

18) Rent seeking is one reason why countries choose to

- A) export and import the same goods.
- B) work for freer trade.
- C) follow the theory of comparative advantage.
- D) hire foreign labour.
- E) restrict trade.

Answer: E

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Reflective Thinking

19) When considering rent seeking, which of the following is *TRUE*?

- A) The anti-free trade group generally will lobby more than the pro-free trade group.
- B) The pro-free trade group generally will lobby more than the anti-free trade group.
- C) Usually only the anti-free trade group is concerned about what is best for society at large.
- D) Only the pro-free trade group is concerned about the government's revenue from tariffs.
- E) None of the above.

Answer: A

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Reflective Thinking

20) One reason that international trade is restricted is that

- A) the individual gain to parties who benefit from the protection will be much larger than the individual loss to parties who lose.
- B) the government completely pays the losers from international trade for their losses.
- C) protectionism benefits consumers.
- D) the government cannot measure the cost of protectionism.
- E) tariff revenue raises more income than income taxes in industrial countries.

Answer: A

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Ethical Reasoning

21) Usually the *removal* of trade barriers affecting a particular good benefits \_\_\_\_\_ people domestically, each of whom gains a \_\_\_\_\_.

- A) a few; little
- B) a few; lot
- C) many; little
- D) many; lot
- E) We can't determine the relative benefits from the removal of trade barriers.

Answer: C

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Ethical Reasoning

22) Usually the *imposition* of trade barriers affecting a particular good benefits \_\_\_\_\_ people domestically, each of whom gains a \_\_\_\_\_.

- A) a few; little
- B) a few; lot
- C) many; little
- D) many; lot
- E) We can't determine the relative benefits from the imposition of trade barriers.

Answer: B

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Ethical Reasoning

23) The gains from free trade are enjoyed by a \_\_\_\_\_ number of people and the costs of free trade are imposed on a \_\_\_\_\_ number of people.

- A) small; large
- B) large; small
- C) small; small
- D) large; large
- E) We can't determine the relative number of people who benefit and lose from free trade.

Answer: B

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Reflective Thinking

24) The effects of offshoring from opening up call centres in India are similar to the effects from

- A) free trade.
- B) tariffs.
- C) import quota.
- D) voluntary export restraints.
- E) export subsidies.

Answer: A

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

Source: Study Guide

AACSB: Reflective Thinking

25) Offshore outsourcing occurs when a firm in Canada \_\_\_\_\_.

- A) hires foreign labour and produces in other countries
- B) buys finished goods, components, or services from other firms in other countries
- C) buys finished goods, components, or services from other firms in Canada
- D) hires Canadian labour and produces in Canada
- E) hires foreign workers who work in Canada

Answer: B

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

Source: MyEconLab

AACSB: Reflective Thinking

26) When a firm implements offshore outsourcing, consumers in Canada \_\_\_\_\_, workers in Canada in the industry that is being outsourced \_\_\_\_\_ and workers in the foreign country in the industry that is being outsourced \_\_\_\_\_.

- A) gain; lose; lose
- B) lose; lose; gain
- C) lose; gain; lose
- D) gain; lose; gain
- E) gain; gain; gain

Answer: D

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

Source: MyEconLab

AACSB: Reflective Thinking

27) The infant industry argument is based on the idea of

- A) global comparative advantage.
- B) global absolute advantage.
- C) tariff maximization.
- D) learning-by-doing.
- E) tariff minimization.

Answer: D

Type: MC

28) Offshoring occurs when a firm in Canada

- A) hires foreign labour and produces in other countries.
- B) buys finished goods, components, or services from other firms in other countries.
- C) hires Canadian labour and produces in Canada.
- D) buys finished goods, components, or services from other firms in Canada.
- E) both A and B are correct

Answer: E

Type: MC

29) Outsourcing occurs when a firm in Canada

- A) hires foreign labour and produces in other countries.
- B) buys finished goods, components, or services from other firms in other countries.
- C) hires Canadian labour and produces in Canada.
- D) buys finished goods, components, or services from other firms in Canada.
- E) Both B and D are correct.

Answer: E

Type: MC

## Chapter 8 Utility and Demand

### 8.1 Consumption Choices

1) The change in total utility that results from a one-unit increase in the quantity of a good

consumed is

- A) additional utility.
- B) marginal utility.
- C) average utility.
- D) marginal utility per dollar.
- E) fractional utility.

Answer: B

Type: MC

Topic: Consumption Choices

2) Utility is

- A) the value of a good.
- B) the additional satisfaction received from consuming another unit of a good.
- C) the benefit or satisfaction from consuming goods and services.
- D) the practical usefulness of a good.
- E) equal to the price of a good.

Answer: C

Diff: 1 Type: MC

Topic: Consumption Choices

3) Diminishing marginal utility means that

- A) Ralph will enjoy his second hamburger less than the first one.
- B) the utility from one hamburger is greater than the utility from two hamburgers.
- C) the price of two hamburgers is less than twice the price of one.
- D) the utility from eating two hamburgers will be more than twice the utility from eating the first one.
- E) hamburgers seem smaller as you eat more of them.

Answer: A

Diff: 1 Type: MC

Topic: Consumption Choices

4) As more of a good is consumed its

- A) marginal utility increases.
- B) marginal utility decreases.
- C) marginal utility remains unchanged.
- D) total utility decreases.
- E) total utility increases at an increasing rate.

Answer: B

Diff: 1 Type: MC

Topic: Consumption Choices

5) What is marginal utility?

- A) The change in total utility divided by the price of a good.
- B) The maximum amount of satisfaction from consuming a good.
- C) The total satisfaction received from consuming as much of the good that is available for consumption.
- D) The additional satisfaction received from consuming one more unit of a good.
- E) The change in the price of a good divided by the change in total utility.

Answer: D

Diff: 1 Type: MC

Topic: Consumption Choices

6) John likes to eat apples, oranges, and pears. If John increases his consumption of oranges, *ceteris paribus*, marginal utility theory tell us that John's marginal utility of

- A) oranges decreases.
- B) apples decreases.
- C) pears decreases.
- D) oranges remains constant.
- E) oranges, apples, and pears all decrease.

Answer: A

Diff: 2 Type: MC

Topic: Consumption Choices

7) The fact that your fourth slice of pizza does not generate as much satisfaction as your third slice is an example of

- A) consumer surplus.
- B) diminishing total utility.
- C) diminishing marginal utility.
- D) the paradox of value.
- E) the law of demand.

Answer: C

Diff: 2 Type: MC

Topic: Consumption Choices

Use the table below to answer the following questions.

**Table 8.1.1**

Quantity	Total Utility	Marginal Utility
0	0	
1	30	30
2	A	12
3	B	5
4	50	C

8) Refer to Table 8.1.1. The value of  $B$  is

- A) 30.
- B) 47.
- C) 42.
- D) 18.
- E) 0.

Answer: B

Diff: 2 Type: MC

Topic: Consumption Choices

9) Refer to Table 8.1.1. The value of  $C$  is

- A) 0.
- B) 13.
- C) 17.
- D) 50.
- E) 3.

Answer: E

Diff: 3 Type: MC

Topic: Consumption Choices

10) Total utility is always

- A) greater than marginal utility.
- B) less than marginal utility.
- C) decreasing when marginal utility is decreasing.
- D) decreasing when marginal utility is increasing.
- E) increasing when marginal utility is positive.

Answer: E

Diff: 2 Type: MC

Topic: Consumption Choices

Source: Study Guide

11) Marginal utility equals

- A) total utility divided by price.
- B) total utility divided by the total number of units consumed.
- C) the slope of the total utility curve.
- D) the inverse of total utility.
- E) the area below the demand curve but above market price.

Answer: C

Diff: 2 Type: MC

Topic: Consumption Choices

12) Total utility equals

- A) the sum of the marginal utilities of each unit consumed.
- B) the area below the demand curve but above the market price.
- C) the slope of the marginal utility curve.
- D) the marginal utility of the last unit divided by price.
- E) the marginal utility of the last unit consumed multiplied by the total number of units consumed.

Answer: A

Diff: 2 Type: MC

Topic: Consumption Choices

Source: Study Guide

13) According to the principle of diminishing marginal utility, as consumption of a good increases, total utility

- A) decreases and then eventually increases.
- B) decreases at an increasing rate.
- C) decreases at a decreasing rate.
- D) increases at an increasing rate.
- E) increases at a decreasing rate.

Answer: E

Diff: 1 Type: MC

Topic: Consumption Choices

14) When total utility is increasing, marginal utility

- A) is negative.
- B) must be between zero and one.
- C) is either increasing or decreasing.
- D) is either positive or negative.
- E) is also increasing.

Answer: C

Diff: 2 Type: MC

Topic: Consumption Choices

15) The first can of Sprite Jack drinks give him 22 units of utility and the second can gives him an additional 12 units of utility. How much units of utility do the two cans of Sprite give Jack?

- A) 17
- B) 46
- C) 34
- D) 2
- E) 36

Answer: C

Diff: 2 Type: MC

Topic: Consumption Choices

16) The first can of Coke gives 15 units of utility to Witney, while the second can of Coke increases her total utility to 23. What is the marginal utility of the second can of Coke?

- A) 24 units
- B) 8 units
- C) 38 units
- D) 11.5 units
- E) 7.5 units

Answer: B

Diff: 2 Type: MC

Topic: Consumption Choices

*Use the table below to answer the following question.*

**Table 8.1.2**

Units Consumed	Jim's Total Utility	Sally's Total Utility
1	12	16
2	22	26
3	30	34
4	36	40

17) Table 8.1.2 gives total utilities for Jim and Sally. Which one of the following statements is true?

- A) Jim has increasing marginal utility.
- B) For Sally, the marginal utility of the third unit consumed is 6.
- C) If Jim consumes 2 units, his total utility is 34 units.
- D) Jim and Sally receive the same marginal utility from the third unit consumed.
- E) If Sally consumes 2 units, her total utility is 10 units.

Answer: D

Diff: 2 Type: MC

Topic: Consumption Choices

18) A budget line is drawn with

- A) quantity of one good on the vertical axis and the quantity of the second good on the horizontal axis.
- B) price of one good on the vertical axis and the price of the second good on the horizontal axis.
- C) quantity of one good on the vertical axis and its price on the horizontal axis.
- D) quantity of one good on the horizontal axis and its price on the vertical axis.
- E) quantity of one good on the horizontal axis and its total utility on the vertical axis.

Answer: A

Type: MC

19) The budget line

- A) shows the limits to a household's consumption choices.
- B) shows the household's total utility.
- C) is downward sloping because it illustrates decreasing marginal utility.
- D) shows how a household's consumption choices change as income changes.
- E) Both A and D are correct.

Answer: A

Type: MC

20) The budget line shows the boundary between those combinations of goods and services that

- A) have positive marginal utility and those that have negative marginal utility.
- B) are available and those that are unavailable.
- C) are desirable and those that are undesirable.
- D) are affordable and those that are unaffordable.
- E) are normal goods and those that are inferior goods.

Answer: D

Type: MC

21) Sam buys gasoline and coffee each week. To draw his budget line for gasoline and coffee, Sam needs to know

- A) if his income is expected to rise in the future.
- B) if the price of gasoline is expected to rise in the future.
- C) if the price of coffee is expected to fall in the future.
- D) the goods that he considers to be substitutes for gasoline and for coffee.
- E) how much income he has to spend and the prices of one litre of gasoline and one cup of coffee.

Answer: E

Type: MC

## 8.2 Utility-Maximizing Choice

1) Sarah can consume either pizzas or hamburgers. The price of a hamburger is \$1 and the price of a pizza is \$5. Let  $MU_h$  be the marginal utility of hamburgers and  $MU_p$  be the marginal utility of pizzas. In consumer equilibrium, what must the ratio  $MU_h/MU_p$  equal?

- A) 1/5
- B) 5/1
- C) 1/1
- D) 1/6
- E) 4

Answer: A

Diff: 1 Type: MC

Topic: Utility-Maximizing Choices

Use the table below to answer the following questions.

**Table 8.2.1**

Hours Spent	Total Utility from Sailing	Total Utility from Skiing
1	100	70
2	140	110
3	170	140
4	190	150

2) Refer to Table 8.2.1. Consider Sam's utility from sailing and skiing. If the price of sailing is \$10 per hour and the price of skiing is \$20 per hour, Sam will choose to spend

- A) all his time sailing.
- B) all his time skiing.
- C) more time sailing than skiing.
- D) more time skiing than sailing.
- E) the same amount of time sailing and skiing, since they give the same amount of utility.

Answer: C

Diff: 3 Type: MC

Topic: Utility-Maximizing Choices

3) Refer to Table 8.2.1. Consider Sam's utility from sailing and skiing. The price of sailing is \$10 per hour and the price of skiing is \$20 per hour; Sam's income to spend on these activities is \$80. In consumer equilibrium, Sam will sail for

- A) 3 hours and ski for 2 hours.
- B) 2 hours and ski for 4 hours.
- C) 4 hours.
- D) 4 hours and ski for 2 hours.
- E) 8 hours.

Answer: D

Diff: 3 Type: MC

Topic: Utility-Maximizing Choices

- 4) If a consumer spends all his income and his marginal utility per dollar is equal for all goods, then
- A) marginal utility is maximized.
  - B) total utility is maximized.
  - C) he cannot be better off even with more income.
  - D) the proportion of income spent on each good must be equal.
  - E) the number of units bought of each good must be equal.

Answer: B

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

- 5) Which one of the following is *not* true in consumer equilibrium?
- A) The total utilities of all goods are equal.
  - B) The consumer is maximizing utility, given her income and the prices of goods and services.
  - C) The marginal utility per dollar is equal for all goods.
  - D) Given prices and her income, the consumer finds that any other choice of goods to consume would lower her utility.
  - E) The consumer will not change her choices unless prices or income change.

Answer: A

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

*Use the table below to answer the following questions.*

**Table 8.2.2**

Bags of Popcorn	Marginal Utility	Bottles of Pop	Marginal Utility
1	120	1	120
2	100	2	70
3	80	3	60
4	70	4	40

- 6) Refer to Table 8.2.2. Henry is maximizing his utility by consuming 3 bags of popcorn and 3 bottles of pop. What is the ratio of the price of popcorn to the price of pop?
- A) 1/2
  - B) 1
  - C) 3/4
  - D) 4/3
  - E) 6/5

Answer: D

Diff: 1 Type: MC

Topic: Utility-Maximizing Choices

7) Refer to Table 8.2.2. What is the total utility if 3 bags of popcorn and 2 bottles of pop are consumed?

- A) 150
- B) 310
- C) 490
- D) 660
- E) 100.

Answer: C

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

8) Let  $MU_A$  and  $MU_B$  stand for the marginal utility of goods  $A$  and  $B$ , respectively. Let  $P_A$  and  $P_B$  stand for the price of goods  $A$  and  $B$ , respectively. Which statement must hold for consumer equilibrium?

- A)  $MU_A = MU_B$
- B)  $MU_A = MU_B$  and  $P_A = P_B$
- C)  $MU_A/MU_B = P_B/P_A$
- D)  $MU_A/MU_B = P_A/P_B$
- E)  $MU_A P_A = MU_B P_B$

Answer: D

Diff: 1 Type: MC

Topic: Utility-Maximizing Choices

9) Let  $MU_A$  and  $MU_B$  stand for the marginal utility of goods  $A$  and  $B$ , respectively. Let  $P_A$  and  $P_B$  stand for the price of goods  $A$  and  $B$ , respectively. Assume that for a given consumer  $MU_A$  and  $MU_B$  are equal to each other, and  $P_A$  is greater than  $P_B$ . In this case, the consumer is better off if he consumes

- A) more of good  $A$  and less of good  $B$ .
- B) less of good  $A$  and more of good  $B$ .
- C) equal amount of goods  $A$  and  $B$ .
- D) good  $B$  only.
- E) neither good  $A$  nor good  $B$ .

Answer: B

Diff: 3 Type: MC

Topic: Utility-Maximizing Choices

10) Advise Sarah how to maximize her utility if  $MU_A=8$ ,  $MU_B=20$ ,  $P_A=4$  and  $P_B=5$ .

- A) Consume equal amounts of both goods.
- B) Consume more of good  $A$  and less of good  $B$ .
- C) Consume more of good  $B$  and less of good  $A$ .
- D) Lower the price of good  $B$ .
- E) Raise the price of good  $A$ .

Answer: C

Diff: 3 Type: MC

Topic: Utility-Maximizing Choices



11) To determine consumer equilibrium we need to know only

- A) prices and income.
- B) total utility and income.
- C) marginal utility and income.
- D) prices, income, and marginal utility.
- E) prices and marginal utility.

Answer: D

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

12) Harold can consume either pens or milkshakes. The price of a pen is \$1, and the price of a milkshake is \$1. Harold figures that when his income is spent, his marginal utility from pens will be 10 and his marginal utility from milkshakes will be 8. Harold is better off

- A) by consuming more pens and fewer milkshakes.
- B) by consuming more pens and more milkshakes.
- C) by consuming fewer pens and fewer milkshakes.
- D) by consuming fewer pens and more milkshakes.
- E) only if he makes more income.

Answer: A

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

13) According to the marginal utility theory, consumers

- A) maximize utility and minimize marginal utility.
- B) maximize utility and equalize marginal utility per dollar across all goods.
- C) save part of their income for future consumption.
- D) maximize utility by spending the most on the least expensive good.
- E) maximize utility by spending the least on the least expensive good.

Answer: B

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

14) In consumer equilibrium

- A) total utility is maximized given the consumer's income and the prices of goods.
- B) marginal utility is maximized given the consumer's income and the prices of goods.
- C) marginal utility per dollar is maximized given the consumer's income and the prices of goods.
- D) the marginal utility from each good is equal.
- E) marginal utility per dollar is zero.

Answer: A

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

Source: Study Guide

15) Samir consumes apples and bananas and is in consumer equilibrium. The marginal utility from his last apple is 10 and the marginal utility from his last banana is 5. If the price of an apple is \$0.50, then what is the price of a banana?

- A) \$0.05
- B) \$0.10
- C) \$0.25
- D) \$0.50
- E) \$1.00

Answer: C

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

Source: Study Guide

16) Suppose a consumer spends all his income. His marginal utility per dollar on  $X$  is 4 and marginal utility per dollar on  $Y$  is 2. We know that

- A) utility can be increased by increasing the consumption of  $X$  and decreasing the consumption of  $Y$ .
- B) utility can be increased by decreasing the consumption of  $X$  and increasing the consumption of  $Y$ .
- C) the price of  $Y$  must be eight times the price of  $X$ .
- D) utility is maximized.
- E) the price of  $Y$  must be one-third the price of  $X$ .

Answer: A

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

Use the table below to answer the following questions.

**Table 8.2.3**

Good X (\$2 each)		Good Y (\$1 each)	
Quantity	Utility	Quantity	Utility
1	20	1	14
2	32	2	24
3	42	3	32
4	48	4	37
5	52	5	40
6	54	6	42
7	55	7	43

17) Refer to Table 8.2.3. To attain consumer equilibrium, the first \$4 of income is used to purchase

- A) 2 units of good X.
- B) 3 units of good X.
- C) 4 units of good Y.
- D) an amount of X and Y that cannot be determined from the table.
- E) 2 units of good Y and 1 unit of X.

Answer: E

Diff: 3 Type: MC

Topic: Utility-Maximizing Choices

18) Refer to Table 8.2.3. If income is \$13, then utility is maximized when consumption is

- A) 6 units of X and 1 unit of Y.
- B) 5 units of X and 3 units of Y.
- C) 4 units of X and 5 units of Y.
- D) 3 units of X and 7 units of Y.
- E) 2 units of X and 9 units of Y.

Answer: C

Diff: 3 Type: MC

Topic: Utility-Maximizing Choices

19) For a consumer to maximize utility from a given income,

- A) the marginal utility from each good must be maximized.
- B) the total utility from each good must be maximized.
- C) the marginal utilities of all goods and services consumed must be equal.
- D) the marginal utility per dollar from all goods and services consumed must be equal.
- E) the amount of each good consumed per dollar must be equal.

Answer: D

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

20) Suppose you are consuming hot dogs and Cokes and believe you are receiving maximum total utility from the meal for your entire budget of \$12. The price of a hot dog is \$2 and the price of a Coke is \$2. Which one of the following can you conclude?

- A) The total utility from hot dogs is maximized.
- B) The marginal utilities from hot dogs and Cokes divided by the quantity of each good must be equal.
- C) The total utilities from hot dogs and Cokes must be equal.
- D) You are purchasing three hot dogs and three Cokes.
- E) The marginal utilities from hot dogs and Cokes must be equal.

Answer: E

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

*Use the table below to answer the following question.*

**Table 8.2.4**

Units of X	Total Utility (X)	Units of Y	Total Utility (Y)
0	0	0	0
1	9	1	49
2	17	2	90
3	24	3	110
4	30	4	118
5	35	5	124
6	39	6	129
7	42	7	132
8	44	8	133

21) Refer to Table 8.2.4. Suppose the price of X is \$1 and the price of Y is \$1. How much of each should you purchase to maximize utility from a total expenditure of \$11?

- A) 3 units of X and 8 units of Y
- B) 4 units of X and 7 units of Y
- C) 5 units of X and 6 units of Y
- D) 6 units of X and 5 units of Y
- E) 7 units of X and 4 units of Y

Answer: C

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

22) If Ms. Petersen is maximizing her utility in the consumption of goods A and B, which one of the following statements must be true?

- A)  $MU_A = MU_B$
- B)  $MU_A/P_A = MU_B/P_B$
- C)  $MU_A/P_B = MU_B/P_A$
- D)  $TU_A = TU_B$
- E)  $TU_A/P_A = TU_B/P_B$

Answer: B

Diff: 1 Type: MC

Topic: Utility-Maximizing Choices

Source: Study Guide

23) Which one of the following is *not* an assumption of marginal utility theory?

- A) People derive utility from their consumption.
- B) More consumption yields more total utility.
- C) Utility can be measured.
- D) Marginal utility diminishes with more consumption.
- E) Consumers maximize total utility.

Answer: C

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

24) If Soula is maximizing her utility, and two goods have the same marginal utility, she

- A) buys only one.
- B) buys equal quantities of both.
- C) is paying the same price for each good.
- D) receives the same total utility from each good.
- E) none of the above.

Answer: C

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

Source: Study Guide

25) A consumer maximizes his utility by purchasing 2 units of good X at \$5 per unit and 3 units of good Y at \$7 per unit. What is the ratio of the marginal utility from X to the marginal utility from Y?

- A) 5/7
- B) 7/5
- C) 2/3
- D) 3/2
- E) 10/21

Answer: A

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

26) Shelley is maximizing utility in her consumption of mansions and Porsches. If the marginal utility of her last purchased mansion is twice the marginal utility of her last purchased Porsche, then we know

- A) Shelley buys twice as many mansions as Porsches.
- B) Shelley buys twice as many Porsches as mansions.
- C) Shelley buys more Porsches than mansions, but we do not know how many more.
- D) the price of a mansion is twice the price of a Porsche.
- E) the price of a Porsche is twice the price of a mansion.

Answer: D

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

27) Sergio is maximizing utility in his consumption of beer and bubblegum. If the price of beer is greater than the price of bubblegum, then we know

- A) Sergio buys more beer than bubblegum.
- B) Sergio buys more bubblegum than beer.
- C) the marginal utility from the last purchased beer is greater than the marginal utility from the last purchased bubblegum.
- D) the marginal utility from the last purchased bubblegum is greater than the marginal utility from the last purchased beer.
- E) the marginal utilities from the last purchased beer and bubblegum are equal.

Answer: C

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

Source: Study Guide

28) In consumer equilibrium, a consumer equates the

- A) total utility from each good.
- B) marginal utility from each good.
- C) total utility per dollar on each good.
- D) marginal utility per dollar on each good.
- E) total income spent on each good with total utility from each good.

Answer: D

Diff: 1 Type: MC

Topic: Utility-Maximizing Choices

Source: Study Guide

29) If the marginal utilities from two goods are not equal, then the consumer

- A) cannot be in equilibrium.
- B) should increase consumption of the good with the lower marginal utility.
- C) should decrease consumption of the good with the lower marginal utility.
- D) may possibly be in equilibrium.
- E) will definitely be in equilibrium.

Answer: D

Diff: 3 Type: MC

Topic: Utility-Maximizing Choices

- 30) Geneva is not at her consumer equilibrium for movies and music downloads. Why?
- A) Her average utility from movies does not equal her average utility from music downloads.
  - B) Her total utility from movies does not equal her total utility from music downloads.
  - C) Her marginal utility from the last movie she attended does not equal her marginal utility from the last music download she downloaded.
  - D) Her average utility from movies does not equal her total utility from music downloads.
  - E) Her marginal utility per dollar from the last movie she attended does not equal her marginal utility per dollar from the last music download she downloaded.

Answer: E

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

- 31) Martha and Sarah have the same preferences, face the same prices, and have the same income. Sarah's utility is measured in units while Martha's is measured in units squared. Select the best response.

- A) Martha and Sarah will choose to consume the same set of goods.
- B) Martha's and Sarah's marginal utility per dollar will be equal.
- C) Martha's and Sarah's marginal utilities will be equal.
- D) Martha and Sarah will have equal total utility.
- E) Martha and Sarah will not choose to consume the same set of goods.

Answer: A

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

- 32) John and Sally have identical preferences except Sally's utility units are exactly 10 times that of John's. Both have the same income and face the same prices. Choose the best response.

- A) John consumes 10 times the amount that Sally consumes.
- B) John receives 1/10 the satisfaction that Sally receives.
- C) Both will consume the same amount of all goods.
- D) John and Sally will have equal total utility.
- E) John and Sally will have equal marginal utility.

Answer: C

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

- 33) Billy likes candy bars and popcorn. Candy bars sell for \$0.50 each and popcorn sells for \$1 a bag. Currently he is in consumer equilibrium with marginal utility per dollar on popcorn equal to 100. What is the marginal utility per dollar on candy bars?

- A) 50
- B) 100
- C) 200
- D) 25
- E) 0.5

Answer: B

Diff: 1 Type: MC

Topic: Utility-Maximizing Choices

34) The relative price of beer to back bacon is 2:1. If Bob's current consumption is at a level where

$MU_{beer}/MU_{back\ bacon}$  is 1:2, then to maximize total utility Bob must

- A) consume more beer and less back bacon.
- B) not change his current consumption of beer and back bacon.
- C) consume less beer and more back bacon.
- D) raise the price of beer.
- E) consume twice as much beer and half as much back bacon.

Answer: C

Diff: 2 Type: MC

Topic: Utility-Maximizing Choices

Source: Study Guide

35) Max has \$35 a day to spend, and he can spend as much time as he likes on his leisure pursuits. Windsurfing equipment rents for \$10 an hour, and snorkeling equipment rents for \$5 an hour. If Max equalizes the marginal utility *per hour* from windsurfing and from snorkeling, he

- A) maximizes his total utility.
- B) can increase his total utility by spending less time windsurfing and more time snorkeling.
- C) can increase his total utility only if the price of windsurfing equipment rentals decreases.
- D) can increase his total utility by spending more time windsurfing and less time snorkeling.
- E) maximizes his marginal utility per dollar.

Answer: B

Type: MC

Topic: Utility-Maximizing Choices

Source: MyEconLab

Use the table below to answer the following question.

**Table 8.2.5**

<b>Hours per month</b>	<b>Marginal utility from golf</b>	<b>Marginal utility from tennis</b>
1	80	40
2	60	36
3	40	30
4	30	10
5	20	5
6	10	2
7	6	1

36) Refer to Table 8.2.5. Cindy enjoys golf and tennis. The table shows the marginal utility she gets from each activity.

Cindy has \$70 a month to spend, and she can spend as much time as she likes on her leisure pursuits. The price of an hour of golf is \$10, and the price of an hour of tennis is \$5.

Cindy decides to golf for 5 hours a month and play tennis for 4 hours a month.

If Cindy spends a dollar more on golf and a dollar less on tennis, her total utility \_\_\_\_\_.

If Cindy spends a dollar less on golf and a dollar more on tennis, her total utility \_\_\_\_\_.

- A) decreases; decreases
- B) increases; decreases
- C) decreases; increases
- D) increases; increases
- E) does not change; does not change

Answer: A

Type: MC

Topic: Utility-Maximizing Choices

Source: MyEconLab

37) Danny has \$12 to spend on two goods: pies and pop. The price of a pie is \$4, and the price of a can of pop is \$2. To maximize his utility, Danny buys

- A) 2 pies and 2 cans of pop.
- B) 3 pies and no pop.
- C) the combination that gives him the same marginal utility per dollar on pies as on pop.
- D) 6 cans of pop and no pie.
- E) the combination that gives him the same total utility from pies as from pop.

Answer: C

Type: MC

- 38) When Kathryn is at her consumer equilibrium, she is
- A) consuming the combination of goods that is at the midpoint of her budget line.
  - B) consuming a combination of goods that is located inside her budget line.
  - C) consuming a combination of goods that is located outside her budget line.
  - D) consuming a combination such that the marginal utility from good  $X$  divided by the marginal utility from good  $Y$  equals the price of good  $X$  divided by the price of good  $Y$ .
  - E) on the midpoint of her demand curve.

Answer: D

Type: MC

- 39) If Katie purchases two slices of pizza and six breadsticks to maximize her total utility, then
- A) a slice of pizza costs three times as much as a breadstick.
  - B) her marginal utility from the second slice of pizza divided by the price of a slice of pizza is equal to her marginal utility from the sixth breadstick divided by the price of a breadstick.
  - C) a breadstick costs three times as much as a slice of pizza.
  - D) she spends more on pizza than she spends on breadsticks.
  - E) B and D are both correct.

Answer: B

Type: MC

### 8.3 Predictions of Marginal Utility Theory

1) Chuck and Barry have identical total utility schedules but Chuck has a much higher income. If each is maximizing his total utility, then

- A) they will have equal total utilities.
- B) Chuck will have lower total utility than Barry.
- C) Chuck will have lower marginal utility than Barry for each normal good consumed.
- D) Chuck will have higher marginal utility than Barry for each normal good consumed.
- E) they will have equal marginal utilities for each normal good consumed.

Answer: C

Diff: 3 Type: MC

Topic: Predictions of Marginal Utility Theory

Source: Study Guide

2) Harold can consume apples and oranges. He likes them equally well and currently is in consumer equilibrium. Then the price of oranges rises, while his income remains the same. What will happen to his consumption?

- A) consumption of oranges increases; consumption of apples decreases
- B) consumption of oranges increases; consumption of apples increases
- C) consumption of oranges decreases; consumption of apples decreases
- D) consumption of oranges decreases; consumption of apples increases
- E) consumption of oranges decreases; consumption of apples could either increase or decrease

Answer: E

Diff: 3 Type: MC

Topic: Predictions of Marginal Utility Theory

3) As a consumer's income decreases, marginal utility theory predicts that

- A) the price of normal goods falls.
- B) the demand for normal goods decreases.
- C) the demand for all goods decreases.
- D) the demand for normal goods increases.
- E) total utility increases.

Answer: B

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

4) Billy likes candy bars and popcorn. Candy bars sell for \$0.50 each and popcorn sells for \$1 per bag. Currently he is in consumer equilibrium. Then the price of a candy bar rises to \$1. Which statement is true in the new consumer equilibrium?

- A) The marginal utility from popcorn will increase.
- B) Marginal utility per dollar on candy bars will be equal to 2.
- C) Total utility will increase.
- D) The marginal utility from candy will decrease.
- E) The marginal utility from candy will be equal to the marginal utility from popcorn.

Answer: E

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

Use the table below to answer the following questions.

**Table 8.2.1**

Windsurfing equipment rents for \$10 per hour, snorkeling equipment for \$5 per hour.

Hours per Month	Total Utility from Windsurfing	Total Utility from Snorkeling
1	60	20
2	110	38
3	150	53
4	180	64
5	200	70

5) Devon enjoys windsurfing and snorkeling. His total utility from each activity is summarized in Table 8.2.1. Devon has \$35 to spend. How long will Devon choose to windsurf and to snorkel?

- A) 1 hour windsurfing and 5 hours snorkeling
- B) 2 hours windsurfing and 3 hours snorkeling
- C) 3 hours windsurfing and 1 hour snorkeling
- D) 4 hours windsurfing and no hours snorkeling
- E) 2 hour windsurfing and 4 hours snorkeling

Answer: C

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

6) Consider Devon's utility from snorkeling and windsurfing in Table 8.2.1. Devon has \$55 to spend. What are Devon's choices for time spent on the two activities?

- A) 1 hour of windsurfing and 9 hours of snorkeling
- B) 2 hours of windsurfing and 7 hours of snorkeling
- C) 3 hours of windsurfing and 5 hours of snorkeling
- D) 4 hours of windsurfing and 3 hours of snorkeling
- E) 5 hours of windsurfing and 1 hour of snorkeling

Answer: D

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

7) Consider Devon's total utility from snorkeling and windsurfing in Table 8.2.1. Suppose that Devon's total income rises from \$35 to \$55, *ceteris paribus*. Given that Devon changes his choice of windsurfing and snorkeling, what is his income elasticity for windsurfing?

- A) zero
- B) 28.6
- C) 44.4
- D) 0.64
- E) 1.55

Answer: D

Diff: 3 Type: MC

Topic: Predictions of Marginal Utility Theory

8) Consider Devon's total utility from snorkeling and windsurfing in Table 8.2.1. Suppose Devon's total income is \$35. If the price of windsurfing rises to \$20 per hour, how long does Devon choose to windsurf and to snorkel?

- A) 1 hour of windsurfing and 3 hours of snorkeling
- B) 2 hour of windsurfing and 7 hours of snorkeling
- C) 3 hours of windsurfing and 5 hours of snorkeling
- D) 4 hours of windsurfing and 3 hours of snorkeling
- E) 5 hours of windsurfing and 1 hour of snorkeling

Answer: A

Diff: 3 Type: MC

Topic: Predictions of Marginal Utility Theory

9) Consider Devon's total utility from snorkeling and windsurfing in Table 8.2.1. Suppose Devon's total income is \$35. If the price of windsurfing rises to \$20 per hour, what is Devon's elasticity of demand for windsurfing?

- A) 1.0
- B) 0.67
- C) 1.5
- D) 10
- E) 1.33

Answer: C

Diff: 3 Type: MC

Topic: Predictions of Marginal Utility Theory

10) Consider Devon's total utility from snorkeling and windsurfing in Table 8.2.1. Suppose Devon's total income is \$35. If the price of windsurfing rises to \$20 per hour, what is Devon's cross elasticity of demand of snorkeling with respect to the price of windsurfing?

- A) 1.0
- B) 0.67
- C) 1.5
- D) 10
- E) 1.33

Answer: C

Diff: 3 Type: MC

Topic: Predictions of Marginal Utility Theory

11) Bikes and roller blades are substitutes. Marginal utility theory predicts that when the price of a bike rises, the quantity of bikes demanded

- A) decreases and the demand curve for roller blades shifts rightward.
- B) decreases and the demand curve for roller blades shifts leftward.
- C) decreases and a movement occurs down along the demand curve for roller blades.
- D) increases and the demand curve for roller blades shifts rightward.
- E) increases and the demand curve for roller blades shifts leftward.

Answer: A

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

Source: Study Guide

12) Beverly is currently in consumer equilibrium. An increase in her income

- A) increases her total utility.
- B) decreases her total utility.
- C) increases her marginal utility from all goods.
- D) decreases her marginal utility from all goods.
- E) increases her consumption of all goods.

Answer: A

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

Source: Study Guide

13) Ron starts out in consumer equilibrium, consuming two goods,  $X$  and  $Y$ . The price of  $Y$  rises. Immediately after the rise in price

- A)  $MU_X/P_X > MU_Y/P_Y$ , and then Ron increases his consumption of  $Y$ .
- B)  $MU_X/P_X > MU_Y/P_Y$ , and then Ron decreases his consumption of  $Y$ .
- C)  $MU_X/P_X < MU_Y/P_Y$ , and then Ron increases his consumption of  $Y$ .
- D)  $MU_X/P_X < MU_Y/P_Y$ , and then Ron decreases his consumption of  $Y$ .
- E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

14) Ron starts out in consumer equilibrium, consuming two goods,  $X$  and  $Y$ . The price of  $X$  rises. Immediately after the rise in price

- A)  $MU_X/P_X > MU_Y/P_Y$ , and then Ron increases his consumption of  $X$ .
- B)  $MU_X/P_X > MU_Y/P_Y$ , and then Ron decreases his consumption of  $X$ .
- C)  $MU_X/P_X < MU_Y/P_Y$ , and then Ron increases his consumption of  $X$ .
- D)  $MU_X/P_X < MU_Y/P_Y$ , and then Ron decreases his consumption of  $X$ .
- E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

15) Ron starts out in consumer equilibrium, consuming two goods,  $X$  and  $Y$ . Ron's income rises. At this point, we can definitely conclude that

- A)  $MU_X/P_X > MU_Y/P_Y$ , and then Ron increases his consumption of  $X$ .
- B)  $MU_X/P_X > MU_Y/P_Y$ , and then Ron decreases his consumption of  $X$ .
- C)  $MU_X/P_X < MU_Y/P_Y$ , and then Ron increases his consumption of  $X$ .
- D)  $MU_X/P_X < MU_Y/P_Y$ , and then Ron decreases his consumption of  $X$ .
- E) none of the above.

Answer: E

Diff: 3 Type: MC

Topic: Predictions of Marginal Utility Theory

16) If the price of a good rises, then in the new consumer equilibrium all of the following are true *except*

- A) the marginal utility from consuming the good will be higher than before the price rise.
- B) the quantity of the good consumed decreases.
- C) the quantity of substitutes consumed increases.
- D) the marginal utility from substitutes will be lower than before the price rise.
- E) the marginal utility from the good equals its new higher price.

Answer: E

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

17) If the price of a good falls, then in the new consumer equilibrium

- A) the marginal utility from consuming the good will be higher than before.
- B) the quantity of the good consumed decreases.
- C) the quantity of substitutes consumed increases.
- D) the marginal utility from substitutes will be lower than before the fall in price.
- E) none of the above.

Answer: E

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

18) If income rises, then in the new consumer equilibrium

- A) the marginal utility from normal goods increases.
- B) the marginal utility from normal goods decreases.
- C) the marginal utility from inferior goods increases.
- D) total utility from inferior goods increases.
- E) both B and C.

Answer: E

Diff: 3 Type: MC

Topic: Predictions of Marginal Utility Theory

19) If income falls, then in the new consumer equilibrium

- A) the marginal utility from normal goods increases.
- B) the marginal utility from normal goods decreases.
- C) the marginal utility from inferior goods increases.
- D) total utility from normal goods increases.
- E) both B and C.

Answer: A

Diff: 3 Type: MC

Topic: Predictions of Marginal Utility Theory

- 20) Utility is similar to temperature because
- A) both are positive.
  - B) both are negative.
  - C) both have units of measurement that are arbitrary.
  - D) both are observable.
  - E) both are measured in the same scale.

Answer: C

Diff: 3 Type: MC

Topic: Predictions of Marginal Utility Theory

- 21) Other things remaining the same, marginal utility theory implies that a rise in the price of a good
- A) increases the consumer surplus.
  - B) decreases the consumer surplus.
  - C) leaves consumer surplus unchanged.
  - D) has an effect on consumer surplus that cannot be determined.
  - E) decreases consumer surplus by the amount equal to the total utility of all goods consumed before the price rise but not after the price rise.

Answer: B

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

- 22) The paradox of value as it applies to diamonds and water can be explained by
- A) distinguishing between utility and price.
  - B) water having a high level of marginal utility relative to diamonds.
  - C) water having a low price relative to diamonds.
  - D) the fact that utility can't be measured.
  - E) distinguishing between total utility and marginal utility.

Answer: E

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

- 23) The high price of diamonds relative to the price of water reflects the fact that, at typical levels of consumption,
- A) the total utility of water is relatively low.
  - B) the total utility of diamonds is relatively high.
  - C) the marginal utility of water is high.
  - D) the marginal utility of diamonds is relatively low.
  - E) None of the above is true.

Answer: E

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

Source: Study Guide

24) Which one of the following statements is true?

- A) Since consumers of a good consume this good until the price equals the value of the last unit, they clearly get no benefit from consuming this good.
- B) Consumers choosing between goods  $X$  and  $Y$  will set  $MU_X = MU_Y$ .
- C) The value of a good to a consumer is measured by the price.
- D) Consumer surplus on a unit of a good will never be zero.
- E) If the marginal utility per dollar of good  $X$  is less than the marginal utility per dollar of good  $Y$ , then the consumer should shift some spending from  $X$  to  $Y$ .

Answer: E

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

25) The paradox of value

- A) is that values are the same for different people.
- B) is that economists can calculate marginal utility, even though utility is unmeasurable.
- C) is resolved by an appeal to the law of diminishing total utility.
- D) remains unresolved by economists.
- E) is resolved by an appeal to the difference between marginal utility and total utility.

Answer: E

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

26) Childcare workers often get paid fairly low wages, yet it is said that they have "the most important job in the world." This paradox can be resolved by

- A) distinguishing between price and value.
- B) distinguishing between marginal utility and total utility.
- C) noting that childcare yields no utility since it is a service.
- D) noting that marginal utility does not diminish for childcare.
- E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

27) With respect to water and diamonds, water

- A) has a higher marginal utility.
- B) has a lower marginal utility.
- C) has a lower total utility.
- D) is cheaper than diamonds because it has a lower total utility.
- E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

- 28) The value of a good relates to
- A) total utility, while price relates to consumer surplus.
  - B) consumer surplus, while price relates to total utility.
  - C) marginal utility, while price relates to consumer surplus.
  - D) marginal utility, while price relates to total utility.
  - E) total utility, while price relates to marginal utility.

Answer: E

Diff: 2 Type: MC

Topic: Predictions of Marginal Utility Theory

Source: Study Guide

- 29) Which of the following is *not* a prediction of marginal utility theory?
- A) Other things remaining the same, the higher the price of a good, the smaller the quantity demanded.
  - B) Other things remaining the same, the lower the price of a good, the greater the quantity demanded.
  - C) Other things remaining the same, the lower the price of a good, the smaller is the consumption of substitutes for that good.
  - D) The law of demand.
  - E) Diminishing marginal utility.

Answer: E

Type: MC

Topic: Predictions of Marginal Utility Theory

- 30) You are consuming hot dogs and Cokes and believe you are maximizing utility for your entire budget of \$12. The price of a hot dog is \$2 and the price of a Coke is \$2. Suppose the price of hot dogs rises to \$4 and the price of a Coke remains at \$2. You adjust your consumption of hot dogs and Cokes and believe you are once again receiving maximum total utility from the meal. Which one of the following can you conclude?
- A) The total utility from hot dogs is maximized.
  - B) The marginal utilities from hot dogs and Cokes must be equal.
  - C) The marginal utility from hot dogs must rise compared to the marginal utility from Cokes.
  - D) You are purchasing 2 hot dogs and 2 Cokes.
  - E) You are purchasing 1 hot dog and 4 Cokes.

Answer: C

Type: MC

Topic: Predictions of Marginal Utility Theory

- 31) If a consumer's income increases and if all goods are normal goods,
- A) the quantity bought of each good decreases.
  - B) the quantity bought of some normal goods increases and of other normal goods decreases, but we can't make an accurate prediction.
  - C) some goods become inferior because it isn't possible to buy all goods.
  - D) the quantity bought of each good increases.
  - E) the supply of all goods increases and the marginal utility from all goods decreases.

Answer: D

Type: MC

Topic: Predictions of Marginal Utility Theory

Source: MyEconLab

- 32) Ben consumes only movies and video games and he is in consumer equilibrium. For Ben, movies and video games are substitutes.

The price of a movie falls which \_\_\_\_\_ the marginal utility per dollar from movies.

To return to consumer equilibrium, Ben \_\_\_\_\_ the number of movies he sees and \_\_\_\_\_ the number of video games he plays.

His marginal utility per dollar for movies \_\_\_\_\_ and his marginal utility per dollar for video games \_\_\_\_\_ as he returns to consumer equilibrium.

- A) increases; decreases; increases; decreases; increases
- B) decreases; increases; decreases; decreases; increases
- C) increases; increases; decreases; decreases; increases
- D) decreases; decreases; increases; increases; decreases
- E) increases; increases; decreases; increases; increases

Answer: C

Type: MC

Topic: Predictions of Marginal Utility Theory

Source: MyEconLab

- 33) The paradox of value asks why

- A) bad things happen to good people.
- B) the price of water is low and the price of a diamond is high, but water is essential to life while diamonds are not.
- C) the good die young.
- D) total utility is greater than marginal utility.
- E) the standard of living is higher in North America than in South America.

Answer: B

Type: MC

Topic: Predictions of Marginal Utility Theory

Source: MyEconLab

34) Ben spends \$50 a year on 2 bunches of flowers and \$50 a year on 10,000 litres of tap water. Ben is maximizing utility. His marginal utility from water is 0.5 units per litre. \_\_\_\_\_ more valuable to Ben than \_\_\_\_\_.

Ben's expenditure on flowers and water illustrates the paradox of value because Ben's marginal utility from flowers is \_\_\_\_\_ than his marginal utility from water and his total utility from flowers is \_\_\_\_\_ than his total utility from water.

- A) Water is; flowers; greater; less
- B) Water is; flowers; less; greater
- C) Flowers are; water; greater; less
- D) Flowers are; water; less; greater
- E) None of the above because Ben values flowers and water equally

Answer: A

Type: MC

Topic: Predictions of Marginal Utility Theory

Source: MyEconLab

35) Marginal utility theory predicts that a rise in the price of a banana results in

- A) the demand curve for bananas shifting rightward.
- B) the demand curve for bananas shifting leftward.
- C) a movement upward along the demand curve for bananas.
- D) a movement downward along the demand curve for bananas.
- E) the demand curve for bananas shifting rightward and the supply curve for bananas shifting rightward.

Answer: C

Type: MC

Topic: Predictions of Marginal Utility Theory

Skill: Conceptual

AACSB: Reflective Thinking

36) Which of the following statements is true?

- A) Marginal utility theory predicts that an increase in a consumer's income increases consumption of *all* goods.
- B) It is possible to derive the law of demand — that a higher price decreases the quantity demanded — using marginal utility theory.
- C) Marginal utility theory makes no prediction about a consumer's responses to hikes in the prices of the goods and services he or she consumes.
- D) Marginal utility theory predicts that all goods are normal goods and that all goods are substitutes for each other.
- E) None of the above.

Answer: B

Type: MC

Topic: Predictions of Marginal Utility Theory

Skill: Conceptual

AACSB: Reflective Thinking

37) Bianca consumes pizza. Marginal utility theory predicts that when the price of pizza increases,

- A) Bianca's total utility from pizza will increase.
- B) Bianca's marginal utility from pizza will not change.
- C) Bianca's demand curve for pizza will shift leftward.
- D) Bianca will buy less pizza.
- E) C and D are correct.

Answer: D

Type: MC

38) Lucy buys only magazines and CDs. Both are normal goods. Lucy's income decreases, but the prices of magazines and CDs do not change. Marginal utility theory predicts that

- A) Lucy buys more magazines and more CDs.
- B) Lucy buys fewer magazines and fewer CDs.
- C) Lucy's demand curve for magazines shifts leftward.
- D) Lucy's demand curve for CDs shifts leftward.
- E) B, C, and D are correct.

Answer: E

Type: MC

## 8.4 New Ways of Explaining Consumer Choices

1) Which of the following barriers to rational choices are studied by behavioural economics?

- A) bounded rationality
- B) bounded will-power
- C) bounded self-interest
- D) the endowment effect
- E) all of the above.

Answer: E

Diff: 1 Type: MC

Topic: New Ways of Explaining Consumer Choices

Source: Study Guide

2) Neuroeconomics studies all of the following concepts *except*

- A) the prefrontal cortex.
- B) the hippocampus.
- C) the production possibilities frontier.
- D) dopamine.
- E) anxiety and fear.

Answer: C

Diff: 1 Type: MC

Topic: New Ways of Explaining Consumer Choices

Source: Study Guide

3) The three limitations on human rationality that behavioural economics emphasizes are

- A) bounded rationality, bounded utility, and bounded self-interest.
- B) bounded rationality, bounded will-power, and bounded self-interest.
- C) bounded utility, bounded will-power, and bounded self-interest.
- D) bounded rationality, bounded will-power, and bounded utility.
- E) bounded rationality, bounded surplus, and bounded utility.

Answer: B

Diff: 1 Type: MC

Topic: New Ways of Explaining Consumer Choices

Source: MyEconLab

4) Behavioural economics and neuroeconomics seek to achieve

- A) the reason why we do not always make rational economic decisions.
- B) a method of using will-power and self-interest to gain utility maximization.
- C) a theory in which consumers are always utility-maximizers.
- D) a new method for the human brain to work out rational choice.
- E) the rational concepts that support the law of demand and the law of supply.

Answer: A

Diff: 1 Type: MC

Topic: New Ways of Explaining Consumer Choices

Source: MyEconLab

5) Behavioural economics

- A) studies the activity of the human brain when a person makes an economic decision.
- B) studies psychology by using the economist's toolbox.
- C) studies the ways in which limits on the human brain's ability to compute and implement rational decisions influences economic behaviour.
- D) was used extensively in the development of marginal utility theory.
- E) all of the above.

Answer: C

Diff: 1 Type: MC

Topic: New Ways of Explaining Consumer Choices

Source: MyEconLab

6) Billy Jean loves to read and she has decided that she will buy all of her books at the bookstore at the outlet mall. One day she is in Chapters and sees a book from the *Globe and Mail* Best Sellers list that she wants to read and she decides to buy it.

Buying the book means that she will not be able to take her Mom out for coffee this week.

Billy Jean's decision is an example of

- A) bounded economics.
- B) bounded self-interest.
- C) bounded will-power.
- D) bounded rationality.
- E) all of the above.

Answer: C

Diff: 2 Type: MC

Topic: New Ways of Explaining Consumer Choices

Source: MyEconLab

7) A behavioural economist will explain Tom's donation to charity by saying that Tom is displaying

- A) the endowment effect.
- B) bounded rationality.
- C) bounded self-interest.
- D) bounded will-power.
- E) the neuro effect.

Answer: C

Type: MC

Topic: New Ways of Explaining Consumer Choices

Skill: Conceptual

AACSB: Reflective Thinking

8) If Sean thinks that the choice between going to Olive Garden or Red Lobster is simply too confusing, a behavioural economist will explain that Sean is showing

- A) the endowment effect.
- B) bounded rationality.
- C) bounded self-interest.
- D) bounded will-power.
- E) irrational behaviour.

Answer: B

Type: MC

Topic: New Ways of Explaining Consumer Choices

Skill: Conceptual

AACSB: Reflective Thinking

9) According to a behavioural economist, a person who is unwilling to sell the last kilogram of rice he purchased for the same price that he paid for it is displaying

- A) the endowment effect.
- B) bounded rationality.
- C) bounded self-interest.
- D) bounded will-power.
- E) rational behaviour.

Answer: A

Type: MC

Topic: New Ways of Explaining Consumer Choices

Skill: Conceptual

AACSB: Reflective Thinking

10) Gene plays another hour of computer games rather than study for the hour even though he knows that the next day when he takes his test he will regret his decision. Gene is showing

- A) the endowment effect.
- B) bounded rationality.
- C) bounded self-interest.
- D) bounded will-power.
- E) bad judgment.

Answer: D

Type: MC

Topic: New Ways of Explaining Consumer Choices

Skill: Conceptual

AACSB: Reflective Thinking

- 11) Lucky buys hats for \$20 but Lucky will not sell one of her hats for less than \$35. Lucky is
- A) displaying the endowment effect.
  - B) making decisions using her prefrontal cortex.
  - C) exhibiting bounded self-interest.
  - D) showing unbounded will-power.
  - E) a behavioural economist.

Answer: A

Type: MC

Topic: New Ways of Explaining Consumer Choices

Skill: Conceptual

AACSB: Reflective Thinking

12) Bounded self-interest

- A) is limited by the computing power of the human brain.
- B) prevents us from making a decision that we know, at the time of implementing the decision, we will later regret.
- C) is the tendency for people to value something more highly simply because they own it.
- D) results in sometimes suppressing our own interests to help others.
- E) is the tendency for people to value something more highly simply because a friend owns it.

Answer: D

Type: MC

## Chapter 9 Possibilities, Preferences, and Choices

### 9.1 Consumption Possibilities

1) Guy has an income ( $Y$ ) of \$50 with which he can purchase DVDs ( $D$ ) at \$10 each and haircuts ( $H$ ) at \$20 each. Which one of the following represents Guy's budget line?

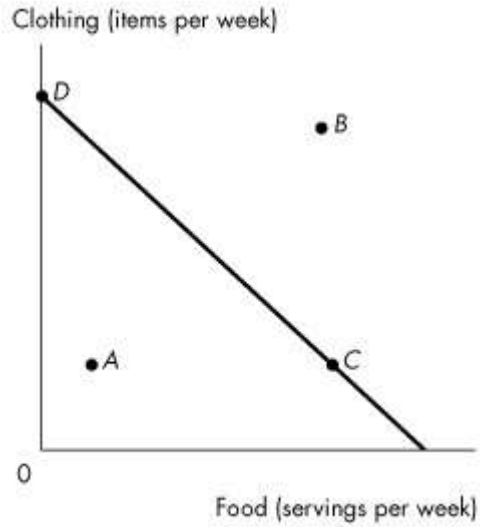
- A)  $Y = 10Q_D - 20Q_H$
- B)  $50 = Q_D + Q_H$
- C)  $Y = 50 + Q_D + Q_H$
- D)  $20Y = Q_D + 10Q_H$
- E)  $50 = 10Q_D + 20Q_H$

Answer: E

Diff: 2 Type: MC

Topic: Consumption Possibilities

*Use the figure below to answer the following questions.*



**Figure 9.1.1**

2) Shelly's budget line is shown in Figure 9.1.1 Which point is unaffordable given her income and current prices?

- A) *A* and *B*
- B) *B* only
- C) *C* only
- D) *C* and *D* only
- E) All points are unattainable.

Answer: B

Diff: 1 Type: MC

Topic: Consumption Possibilities

3) Shelly's budget line is shown in Figure 9.1.1. Which points are affordable given her income and current prices?

- A) *A* only
- B) *B* only
- C) *C* only
- D) *D* only
- E) *A*, *C*, and *D*

Answer: E

Diff: 2 Type: MC

Topic: Consumption Possibilities

4) David has an income of \$30 to buy movie tickets and bus tickets. The price of a movie ticket is \$6 and the price of a bus ticket is \$2. What is David's real income?

- A) \$30
- B) 5 movie tickets or 15 bus tickets
- C) 15 movie tickets or 5 bus tickets
- D) \$38
- E) \$32

Answer: B

Diff: 2 Type: MC

Topic: Consumption Possibilities

5) David has an income of \$30 to buy movie tickets and bus tickets. The price of a movie ticket is \$6 and the price of a bus ticket is \$2. What is the relative price of a bus ticket in terms of movie tickets?

- A) 2 movie tickets
- B) 15 movie tickets
- C) \$3
- D)  $\frac{1}{3}$  movie tickets
- E) \$6

Answer: D

Diff: 2 Type: MC

Topic: Consumption Possibilities

6) Real income in terms of a good is defined as

- A) income divided by the quantity consumed of a good.
- B) the income of a producer of that good.
- C) the price of one good divided by the price of another good.
- D) dollar income.
- E) income divided by the price of a good.

Answer: E

Diff: 1 Type: MC

Topic: Consumption Possibilities

7) Marie-Louise has an income of \$10 to buy peanuts and popcorn. The price of a bag of peanuts is \$1 and the price of a bag of popcorn is \$2. What is Marie-Louise's real income in terms of popcorn?

- A) 1/2 bag of popcorn
- B) 1 bag of popcorn
- C) 2 bags of popcorn
- D) 5 bags of popcorn
- E) 10 bags of popcorn

Answer: D

Diff: 2 Type: MC

Topic: Consumption Possibilities

8) The price of one good divided by the price of another good is

- A) an absolute price.
- B) a relative price.
- C) a marginal price.
- D) a demand price.
- E) a money price.

Answer: B

Diff: 1 Type: MC

Topic: Consumption Possibilities

9) The price of a cup of coffee is \$2.00. The price of a cup of tea is \$1.20. The relative price of a cup of tea with respect to a cup of coffee is

- A) 0.6 cups of coffee.
- B) 1.67 cups of coffee.
- C) 1.0 cup of coffee.
- D) 1.25 cups of coffee.
- E) 0.75 cups of coffee.

Answer: A

Diff: 1 Type: MC

Topic: Consumption Possibilities

10) The magnitude of the slope of the budget line is the

- A) relative price of the good measured on the vertical axis.
- B) relative price of the good measured on the horizontal axis.
- C) absolute price of the good measured on the horizontal axis.
- D) real price of the good measured on the vertical axis.
- E) price of the good measured on the vertical axis.

Answer: B

Diff: 3 Type: MC

Topic: Consumption Possibilities

11) When speaking of the price of the good measured on the horizontal axis relative to the price of the good measured on the vertical axis, which statement is true?

- A) The steeper the slope of the budget line, the more expensive the good measured on the horizontal axis.
- B) The steeper the slope of the budget line, the less expensive the good measured on the horizontal axis.
- C) The steeper the slope of the budget line, the more expensive the good measured on the vertical axis.
- D) The slope of the budget line is independent of relative prices.
- E) The flatter the slope of the budget line, the more expensive the good measured on the horizontal axis.

Answer: A

Diff: 3 Type: MC

Topic: Consumption Possibilities

12) Suppose all prices double and income also doubles. Which statement is true?

- A) The budget line does not change.
- B) The slope of the budget line increases.
- C) The slope of the budget line decreases.
- D) The budget line shifts rightward.
- E) The budget line shifts leftward.

Answer: A

Diff: 3 Type: MC

Topic: Consumption Possibilities

13) The budget line depends on

- A) income only.
- B) prices only.
- C) income and prices.
- D) preferences only.
- E) preferences and prices.

Answer: C

Diff: 1 Type: MC

Topic: Consumption Possibilities

Source: Study Guide

14) If the price of the good measured on the vertical axis increases, the budget line

- A) becomes steeper.
- B) becomes flatter.
- C) shifts leftward and parallel to the original budget line.
- D) shifts rightward and parallel to the original budget line.
- E) shifts leftward and becomes steeper.

Answer: B

Diff: 2 Type: MC

Topic: Consumption Possibilities

Source: Study Guide

15) If the price of the good measured on the horizontal axis increases, the budget line

- A) becomes steeper.
- B) shifts leftward and becomes steeper.
- C) shifts leftward and parallel to the original budget line.
- D) shifts rightward and parallel to the original budget line.
- E) becomes flatter.

Answer: A

Diff: 2 Type: MC

Topic: Consumption Possibilities

16) If income increases, the budget line

- A) becomes steeper.
- B) becomes flatter.
- C) shifts leftward and parallel to the original budget line.
- D) shifts rightward and parallel to the original budget line.
- E) shifts parallel either leftward or rightward depending on whether the goods measured on the axes are normal or inferior.

Answer: D

Diff: 2 Type: MC

Topic: Consumption Possibilities

Source: Study Guide

17) If income decreases, the budget line

- A) becomes steeper.
- B) becomes flatter.
- C) shifts leftward and parallel to the original budget line.
- D) shifts rightward and parallel to the original budget line.
- E) shifts parallel either leftward or rightward depending on whether the goods measured on the axes are normal or inferior.

Answer: C

Diff: 2 Type: MC

Topic: Consumption Possibilities

18) Martha consumes cake and muffins. Suppose Martha's income doubles and the prices of cake and muffins also double. Martha's budget line

- A) shifts leftward but the slope does not change.
- B) remains unchanged.
- C) shifts rightward but the slope does not change.
- D) shifts rightward and becomes steeper.
- E) shifts rightward and becomes flatter.

Answer: B

Diff: 2 Type: MC

Topic: Consumption Possibilities

19) Let  $Y = \$100$ ,  $Q_X$  = quantity of good X, and  $Q_W$  = quantity of good W,  $P_X = \$4$  and  $P_W = \$5$ . The budget equation is

- A)  $100 = 4Q_X + 5Q_W$ .
- B)  $100 = Q_X + (4/5)Q_W$ .
- C)  $Q_X = 100 + (4/5)Q_W$ .
- D)  $Q_X = Q_W + (4/5)Y$ .
- E)  $Q_W = Q_X + (4/5)Y$ .

Answer: A

Diff: 2 Type: MC

Topic: Consumption Possibilities

20) Sarah has an income of \$100. She purchases 5 pizzas at \$10 each and 10 subs at \$5 each. Then the government taxes subs, and the price rises to \$10 each. Simultaneously, the government gives Sarah a grant of \$50 in income to make up for this change. As a result, Sarah's budget line

- A) becomes steeper.
- B) becomes flatter.
- C) shifts leftward and parallel to the original budget line.
- D) shifts rightward and parallel to the original budget line.
- E) swivels around the original consumption choice.

Answer: E

Diff: 3 Type: MC

Topic: Consumption Possibilities

21) Bill consumes apples and bananas. Apples are measured on the vertical axis and bananas are measured on the horizontal axis. Bill's income doubles, the price of apples doubles, and the price of bananas triples. Bill's budget line

- A) remains unchanged.
- B) shifts rightward and the slope does not change.
- C) shifts rightward and becomes steeper.
- D) shifts rightward and becomes flatter.
- E) becomes steeper.

Answer: E

Diff: 3 Type: MC

Topic: Consumption Possibilities

22) The initial budget equation for pop ( $p$ ) and movies ( $m$ ) is  $Q_p = 20 - 4Q_m$ , and the price of a pop is \$5. If the price of a pop falls to \$4, what is the new budget equation?

- A)  $Q_p = 25 - 2Q_m$
- B)  $Q_p = 25 - 4Q_m$
- C)  $Q_p = 25 - 5Q_m$
- D)  $Q_p = 20 - 5Q_m$
- E) none of the above

Answer: C

Diff: 3 Type: MC

Topic: Consumption Possibilities

Source: Study Guide

23) Which one of the following statements about the budget line is *false*? The budget line

- A) separates affordable consumption points from unaffordable consumption points.
- B) is based on fixed prices.
- C) is based on fixed income.
- D) is based on fixed quantities.
- E) constrains consumer choices.

Answer: D

Diff: 2 Type: MC

Topic: Consumption Possibilities

24) Zarina can afford to buy 3 tomatoes and no toothbrushes, or 2 toothbrushes and no tomatoes.

The relative price of a toothbrush is

- A)  $\frac{2}{3}$  of a tomato.
- B)  $\frac{3}{2}$  tomatoes.
- C) 6 tomatoes.
- D)  $\frac{1}{6}$  of a tomato.
- E) impossible to calculate without additional information.

Answer: B

Diff: 2 Type: MC

Topic: Consumption Possibilities

Source: Study Guide

25) A change in the price of the good measured on the horizontal axis changes \_\_\_\_\_ of the budget line.

- A) the slope and  $y$ -intercept
- B) the slope and  $x$ -intercept
- C) the  $x$ - and  $y$ -intercepts but not the slope
- D) only the slope
- E) only the  $y$ -intercept

Answer: B

Diff: 2 Type: MC

Topic: Consumption Possibilities

26) A change in the price of the good measured on the vertical axis changes \_\_\_\_\_ of the budget line.

- A) the slope and  $y$ -intercept
- B) the slope and  $x$ -intercept
- C) the  $x$ - and  $y$ -intercepts but not the slope
- D) only the slope
- E) only the  $y$ -intercept

Answer: A

Diff: 2 Type: MC

Topic: Consumption Possibilities

27) A change in income changes \_\_\_\_\_ of the budget line.

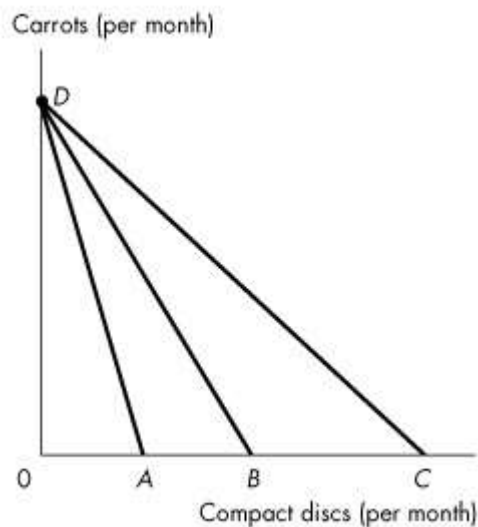
- A) the slope and y-intercept
- B) the slope and x-intercept
- C) the x- and y-intercepts but not the slope
- D) only the slope
- E) only the y-intercept

Answer: C

Diff: 2 Type: MC

Topic: Consumption Possibilities

Use the figure below to answer the following questions.



**Figure 9.1.2**

28) Refer to Figure 9.1.2. Which budget line shows the greatest real income in terms of compact discs?

- A) *AD*
- B) *BD*
- C) *CD*
- D) Real income is equal for all three budget lines.
- E) Cannot be determined without studying the indifference curves.

Answer: C

Diff: 2 Type: MC

Topic: Consumption Possibilities

29) Refer to Figure 9.1.2. Which budget line shows the greatest real income in terms of carrots?

A) *AD*

B) *BD*

C) *CD*

D) Real income is equal for all three budget lines.

E) Cannot be determined without studying the indifference curves.

Answer: D

Diff: 2 Type: MC

Topic: Consumption Possibilities

30) Refer to Figure 9.1.2. Which budget line has the lowest relative price for compact discs?

A) *DA*

B) *DB*

C) *DC*

D) The relative price is equal for all three budget lines.

E) Cannot be determined without studying the indifference curves.

Answer: C

Diff: 2 Type: MC

Topic: Consumption Possibilities

31) Refer to Figure 9.1.2. Which budget line has the lowest relative price for carrots?

A) *AD*

B) *BD*

C) *CD*

D) The relative price is equal for all three budget lines.

E) Cannot be determined without studying the indifference curves.

Answer: A

Diff: 2 Type: MC

Topic: Consumption Possibilities

32) Larry consumes only beer (*B*) and chips (*C*). The equation of his budget line (with beer measured on the vertical axis) is

A)  $QB = Y/PB - (PC/PB)QC$ .

B)  $QB = Y - (PC/PB)QC$ .

C)  $QB = Y/PC - (PB/PC)QC$ .

D)  $QB = Y/PB - (PC/PB)QB$ .

E)  $QC = Y/PC - (PB/PC)QB$ .

Answer: A

Diff: 2 Type: MC

Topic: Consumption Possibilities

33) Larry consumes only beer ( $B$ ) and chips ( $C$ ). The magnitude of the slope of his budget line (with beer measured on the vertical axis) is

- A)  $P_C/Y$ .
- B)  $P_C \times P_B$ .
- C)  $Y/P_C$ .
- D)  $Y/P_B$ .
- E)  $P_C/P_B$ .

Answer: E

Diff: 2 Type: MC

Topic: Consumption Possibilities

34) Larry consumes only beer ( $B$ ) and chips ( $C$ ). His real income in terms of beer is

- A)  $P_C/Y$ .
- B)  $P_C \times P_B$ .
- C)  $Y/P_C$ .
- D)  $Y/P_B$ .
- E)  $P_C/P_B$ .

Answer: D

Diff: 2 Type: MC

Topic: Consumption Possibilities

35) Larry consumes only beer ( $B$ ) and chips ( $C$ ). His real income in terms of chips is

- A)  $P_C/Y$ .
- B)  $P_C \times P_B$ .
- C)  $Y/P_C$ .
- D)  $Y/P_B$ .
- E)  $P_C/P_B$ .

Answer: C

Diff: 2 Type: MC

Topic: Consumption Possibilities

36) Larry consumes only beer ( $B$ ) and chips ( $C$ ). If beer is measured on the vertical axis, the relative price of chips in terms of beer is all of the following *except*

- A)  $P_C/P_B$
- B) the magnitude of the slope of the budget line
- C) equal to the opportunity cost of 1 bag of chips
- D) the real income in terms of beer
- E) the inverse of the relative price of beer in terms of chips

Answer: D

Diff: 2 Type: MC

Topic: Consumption Possibilities

37) Sara's income is \$12 a week. The price of popcorn is \$3 a bag, and the price of a smoothie is \$3. The opportunity cost of a smoothie is \_\_\_\_\_.

- A) \$3
- B) 4 bags of popcorn
- C) 1.00 smoothie
- D) 1.0 bag of popcorn
- E) \$1

Answer: D

Diff: 2 Type: MC

Topic: Consumption Possibilities

Source: MyEconLab

38) Goods that can be bought in any quantity desired are called

- A) divisible goods.
- B) invisible goods.
- C) inferior goods.
- D) services.
- E) normal goods.

Answer: A

Type: MC

39) Junkfood Jill spends all of her income on jellybeans and Jolt cola. Suppose that Jill's income is \$30, the price of a bag of jellybeans is \$6, and the price of a bottle of Jolt cola is \$2. Which of the following combinations of jellybeans and Jolt cola lies inside Jill's budget line?

- A) 2 bags of jellybeans and 8 bottles of Jolt
- B) 5 bags of jellybeans and 0 bottles of Jolt
- C) 4 bags of jellybeans and 4 bottles of Jolt
- D) 3 bags of jellybeans and 6 bottles of Jolt
- E) 5 bags of jellybeans and 15 bottles of Jolt

Answer: A

Type: MC

40) Which of the following is *not* relevant when calculating the budget line?

- A) the price of good *X*
- B) income
- C) the price of good *Y*
- D) preferences
- E) the relative price of good *X* in terms of good *Y*

Answer: D

Type: MC

- 41) The number of pizza slices is plotted on the horizontal axis and number of hot dogs is plotted on the vertical axis. If the price of a hot dog rises the
- A)  $x$ -intercept and the slope of the budget line increase.
  - B)  $y$ -intercept and the slope of the budget line increase.
  - C)  $x$ -intercept and the slope of the budget line decrease.
  - D)  $y$ -intercept decreases and the slope of the budget line does not change.
  - E)  $y$ -intercept and the slope of the budget line decrease.

Answer: E

Type: MC

## 9.2 Preferences and Indifference Curves

1) An indifference curve is

- A) the boundary between what can be produced and what cannot be produced.
- B) the boundary between what a consumer can afford and what he cannot afford.
- C) a line that shows combinations of goods among which a consumer is indifferent.
- D) the boundary between normal goods and inferior goods.
- E) a line with a positive slope.

Answer: C

Diff: 1 Type: MC

Topic: Preferences and Indifference Curves

2) A preference map is

- A) a series of points that represent levels of equal satisfaction.
- B) a series of demand curves.
- C) a series of supply curves.
- D) a map that shows contour lines.
- E) a series of indifference curves.

Answer: E

Diff: 2 Type: MC

Topic: Preferences and Indifference Curves

3) The marginal rate of substitution

- A) is the amount of good  $Y$  substituted for good  $X$  as a consumer moves along his budget line.
- B) is the rate at which a person gives up the good measured on the  $y$ -axis to get an additional unit of the good measured on the  $x$ -axis while remaining on the same indifference curve.
- C) increases as a consumer consumes more of the good measured on the  $x$ -axis.
- D) is greater than the magnitude of the slope of the budget line.
- E) is equal to the slope of the budget line.

Answer: B

Diff: 1 Type: MC

Topic: Preferences and Indifference Curves

4) Which one of the following statements is *false*?

- A) If the indifference curve is steep, the marginal rate of substitution is high.
- B) A low marginal rate of substitution implies a flat indifference curve.
- C) A flat indifference curve implies a consumer must receive a large amount of good X to compensate for a small decrease in good Y.
- D) A high marginal rate of substitution implies a consumer must receive a large amount of good X to compensate for a small decrease in good Y.
- E) A high marginal rate of substitution implies a consumer must receive a small amount of good X to compensate for a large decrease in good Y.

Answer: D

Diff: 3 Type: MC

Topic: Preferences and Indifference Curves

5) The magnitude of the slope of an indifference curve is

- A) the marginal rate of substitution.
- B) the marginal rate of transformation.
- C) the marginal propensity to consume.
- D) the marginal propensity to substitute.
- E) the relative price of good Y.

Answer: A

Diff: 1 Type: MC

Topic: Preferences and Indifference Curves

Use the figure below to answer the following questions.

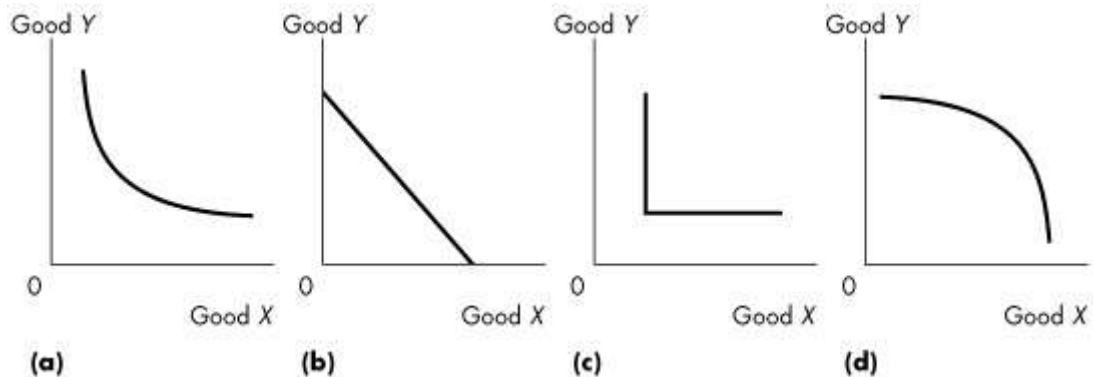


Figure 9.2.1

6) Which one of the graphs in Figure 9.2.1 shows perfect substitutes?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (c) and (d)

Answer: B

Diff: 2 Type: MC

Topic: Preferences and Indifference Curves

7) Which of the graphs in Figure 9.2.1 shows perfect complements?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (c) and (d)

Answer: C

Diff: 2 Type: MC

Topic: Preferences and Indifference Curves

8) A constant marginal rate of substitution between two goods implies

- A) the goods are perfect complements.
- B) the goods are imperfect substitutes.
- C) the goods are both inferior.
- D) one good is normal and one good is inferior.
- E) the goods are perfect substitutes.

Answer: E

Diff: 2 Type: MC

Topic: Preferences and Indifference Curves

9) What is a distinguishing characteristic of goods that are perfect complements?

- A) straight-line indifference curves
- B) upward-sloping demand curves
- C) L-shaped indifference curves
- D) upward-sloping indifference curves
- E) curved indifference curves, bowed away from the origin

Answer: C

Diff: 2 Type: MC

Topic: Preferences and Indifference Curves

10) A consumer always has a cup of coffee with a tablespoon of sugar. What would the consumer's indifference curves for these two goods look like?

- A) upward sloping
- B) horizontal along the entire length
- C) downward sloping with a constant slope
- D) vertical along the entire length
- E) L-shaped

Answer: E

Diff: 2 Type: MC

Topic: Preferences and Indifference Curves

11) A consumer considers Coke and Pepsi to be perfect substitutes for each other. What would the consumer's indifference curves for these two goods look like?

- A) L-shaped
- B) horizontal along the entire length
- C) vertical along the entire length
- D) upward sloping
- E) downward sloping with a constant slope

Answer: E

Diff: 2 Type: MC

Topic: Preferences and Indifference Curves

12) Which one of the following statements is *false*?

- A) Indifference curves are negatively sloped.
- B) A preference map consists of a series of indifference curves.
- C) Indifference curves are bowed out from the origin.
- D) The marginal rate of substitution is the magnitude of the slope of an indifference curve.
- E) The marginal rate of substitution increases as a consumer moves up along an indifference curve for ordinary goods.

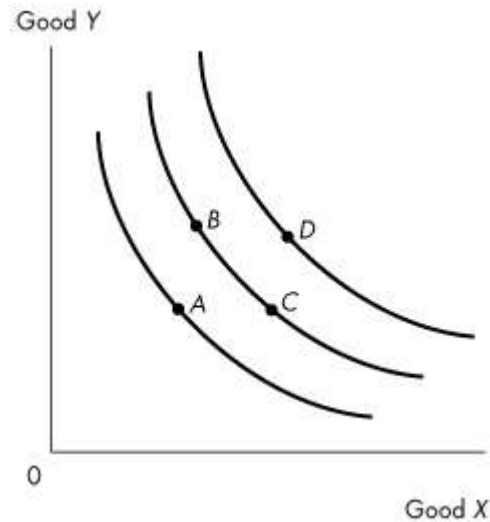
Answer: C

Diff: 2 Type: MC

Topic: Preferences and Indifference Curves

Source: Study Guide

Use the figure below to answer the following question.



**Figure 9.2.2**

13) Figure 9.2.2 shows three indifference curves for Brenda. Which one of the following is *not* true?

- A) Brenda would be equally happy consuming at either point *B* or point *C*.
- B) Brenda prefers consuming at point *B* to consuming at point *A*.
- C) Brenda prefers consuming at point *D* to consuming at either point *B* or point *C*.
- D) The marginal rate of substitution is higher at point *C* than at point *B*.
- E) Brenda prefers consuming at point *D* to consuming at point *A*.

Answer: D

Diff: 3 Type: MC

Topic: Preferences and Indifference Curves

14) Good *X* is measured on the horizontal axis and good *Y* is measured on the vertical axis. The marginal rate of substitution is

- A) the relative price of good *X* in terms of good *Y*.
- B) the relative price of good *Y* in terms of good *X*.
- C) the rate at which a consumer will give up good *Y* to obtain an additional unit of good *X* while remaining indifferent.
- D) the rate at which a consumer will give up good *X* to obtain an additional unit of good *Y* while remaining indifferent.
- E) equal to the magnitude of the slope of the budget line.

Answer: C

Diff: 2 Type: MC

Topic: Preferences and Indifference Curves

15) Which one of the following statements is *true* about the indifference curves for two goods that are perfect substitutes?

- A) The indifference curves are negatively-sloped straight lines.
- B) The indifference curves are L-shaped.
- C) The marginal rate of substitution is zero.
- D) The indifference curves are positively-sloped straight lines.
- E) The marginal rate of substitution is infinity.

Answer: A

Diff: 2 Type: MC

Topic: Preferences and Indifference Curves

16) Which one of the following statements is *true* about the indifference curves for two goods that are close but not perfect substitutes?

- A) The indifference curves are negatively-sloped straight lines.
- B) The indifference curves are L-shaped.
- C) The marginal rate of substitution is constant.
- D) The marginal rate of substitution decreases as more of the good measured on the  $x$ -axis and less of the good measured on the  $y$ -axis are consumed.
- E) both A and C

Answer: D

Diff: 3 Type: MC

Topic: Preferences and Indifference Curves

17) The shape of a person's indifference curves between two goods depends on

- A) the prices of the two goods.
- B) the person's income.
- C) the degree of substitutability between the two goods.
- D) the level of satisfaction for the person.
- E) all of the above.

Answer: C

Diff: 2 Type: MC

Topic: Preferences and Indifference Curves

Source: Study Guide

18) If two goods are perfect substitutes, then their

- A) indifference curves are positively-sloped straight lines.
- B) indifference curves are negatively-sloped straight lines.
- C) indifference curves are L-shaped.
- D) marginal rate of substitution is zero.
- E) marginal rate of substitution is infinity.

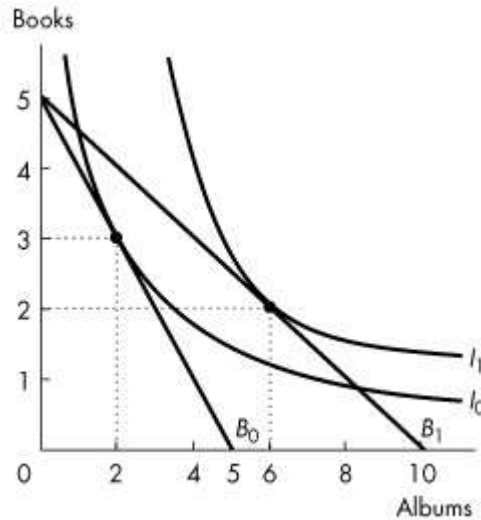
Answer: B

Diff: 2 Type: MC

Topic: Preferences and Indifference Curves

Source: Study Guide

Use the figure below to answer the following questions.



**Figure 9.2.3**

19) Refer to Figure 9.2.3. Rashid buys only books and albums. The figure shows his preferences. When Rashid chooses the consumption point of 3 books and 2 albums, his marginal rate of substitution is \_\_\_\_\_.

- A) 1 book per album
- B) zero
- C) 3/2 books per album
- D) 2/3 books per album
- E) 0.5 books per album

Answer: A

Diff: 2 Type: MC

Topic: Preferences and Indifference Curves

Source: MyEconLab

20) Refer to Figure 9.2.3. When Rashid chooses the consumption point of 2 books and 6 albums, his marginal rate of substitution is \_\_\_\_\_.

- A) 1/3 books per album
- B) 0.5 books per album
- C) 3 books per album
- D) 1 book per album
- E) 2 books per album

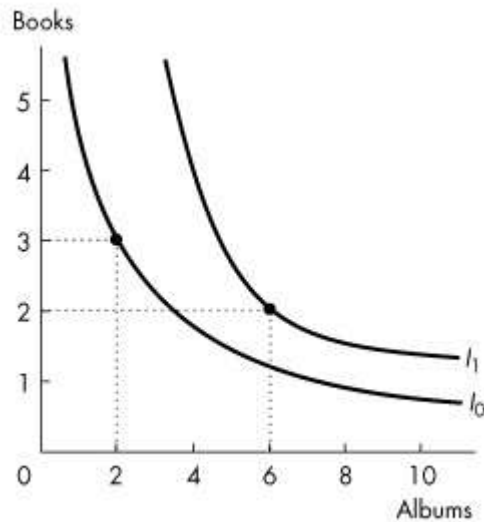
Answer: B

Diff: 2 Type: MC

Topic: Preferences and Indifference Curves

Source: MyEconLab

Use the figure below to answer the following question.



**Figure 9.2.4**

21) Refer to Figure 9.2.4. Rashid buys only books and albums. The figure shows his preferences. Rashid's indifference curves \_\_\_\_\_ display diminishing marginal rate of substitution because \_\_\_\_\_.

- A) do; Rashid is indifferent between consuming 6 albums and 2 books and consuming 2 albums and 3 books
- B) do not; the magnitude of the slope of both indifference curves decreases as Rashid consumes more albums and fewer books
- C) do not; Rashid is indifferent between consuming 6 albums and 2 books and consuming 2 albums and 3 books
- D) do; the magnitude of the slope of both indifference curves decreases as Rashid consumes more albums and fewer books
- E) do; the price of an album decreases as Rashid increases the quantity he buys

Answer: D

Diff: 2 Type: MC

Topic: Preferences and Indifference Curves

Source: MyEconLab

Use the figure below to answer the following question.

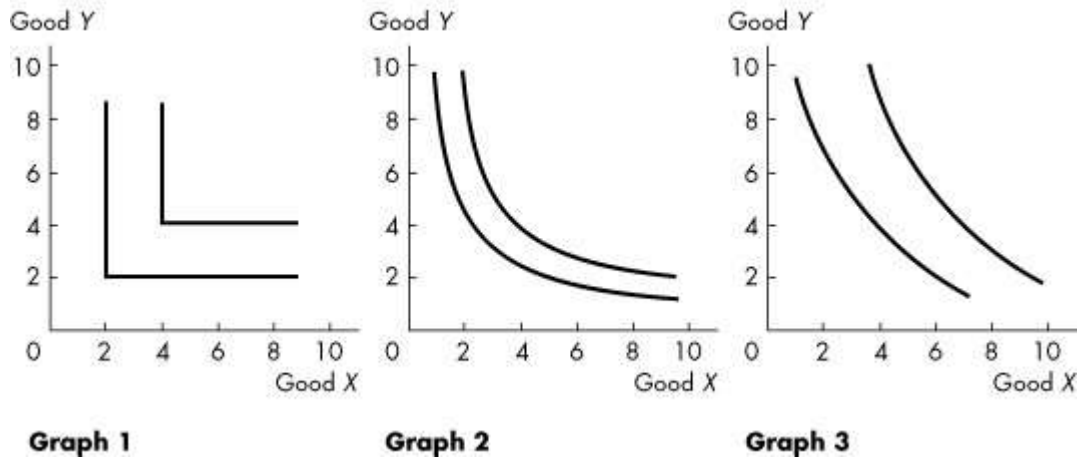


Figure 9.2.5

22) Refer to Figure 9.2.5. The graphs show indifference curves for various goods. Graph \_\_\_\_\_ best describes the pair of goods baseballs and baseball bats. Graph \_\_\_\_\_ best describes the pair of goods desktop computers and laptop computers.

- A) 2; 3
- B) 2; 1
- C) 1; 1
- D) 1; 3
- E) 3; 2

Answer: A

Diff: 2 Type: MC

Topic: Preferences and Indifference Curves

Source: MyEconLab

23) An indifference curve slopes downward because \_\_\_\_\_.

- A) it shows that people are only happy when they increase consumption of all goods
- B) it shows that when a person gives up some of good X they must increase their consumption of good Y to remain indifferent
- C) it shows that when a person gives up some of good X they can afford to increase their consumption of good Y
- D) it is a demand curve without prices
- E) the quantity demanded increases as the price falls

Answer: B

Diff: 2 Type: MC

Topic: Preferences and Indifference Curves

Source: MyEconLab

24) Which of the following statements is FALSE?

A) A consumer possesses a preference map.

B) An indifference curve is a line that shows combinations of goods among which a consumer is indifferent.

C) A consumer has only one indifference curve.

D) The marginal rate of substitution is the rate at which a consumer will give up good  $y$  to get an additional unit of good  $x$  and remain on the same indifference curve.

E) If the indifference curve is steep, the marginal rate of substitution is high.

Answer: C

Type: MC

25) Which of the following results in a rightward shift of your indifference curves for gasoline and movie rentals?

A) an increase in the price of a litre of gasoline with no change in the price of a movie rental

B) an increase in the price of a movie rental with no change in the price of a litre of gasoline

C) an increase in income if gasoline and movie rentals are normal goods

D) a decrease in the price of a litre of gasoline or a decrease in the price of a movie rental

E) none of the above

Answer: E

Type: MC

26) If two consumption points are on different indifference curves, then one point is

A) a substitute for the other.

B) preferred to the other.

C) a complement of the other.

D) a normal good and the other point is an inferior good.

E) more expensive than the other.

Answer: B

Type: MC

### 9.3 Predicting Consumer Choices

1) Leah consumes at a point on her budget line where her marginal rate of substitution is less than the magnitude of the slope of her budget line. As Leah moves towards her best affordable point, she will move to

- A) a lower budget line.
- B) a higher budget line.
- C) a lower indifference curve.
- D) a higher indifference curve.
- E) a tangent point on the same indifference curve.

Answer: D

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

2) Leah consumes at a point on her budget line where her marginal rate of substitution is less than the magnitude of the slope of her budget line. As Leah moves along her budget line toward her best affordable point, she will move

- A) down and left.
- B) down and right.
- C) up and left.
- D) up and right.
- E) straight up.

Answer: C

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

3) A consumer's best affordable point occurs

- A) inside the budget line.
- B) outside the budget line.
- C) on the budget line.
- D) at a point that cannot be determined.
- E) at a corner on the budget line, with only one good consumed.

Answer: C

Diff: 1 Type: MC

Topic: Predicting Consumer Choices

4) At the best affordable point, what is the relationship between the indifference curve and the budget line?

- A) The budget line and the indifference curve are identical.
- B) The slope of the indifference curve exceeds the slope of the budget line.
- C) The slope of the budget line exceeds the slope of the indifference curve.
- D) The slope of the indifference curve equals the slope of the budget line.
- E) None of the above.

Answer: D

Diff: 2 Type: MC

Topic: Predicting Consumer Choices

5) Jay has an income of \$10 to buy peanuts and popcorn. The price of peanuts is \$1 a bag and the price of popcorn is \$2 a bag. He chooses to consume 5 bags of peanuts and 2 bags of popcorn. What can we say about this consumption choice?

A) It is not the best affordable choice. He should consume more peanuts, more popcorn, or more of both.

B) It is the best affordable choice, and his marginal rate of substitution equals the slope of the budget line.

C) The consumption choice is on the budget line.

D) The consumption choice is outside the budget line.

E) both B and C

Answer: A

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

6) Which one of the following is true at the best affordable choice of a consumer?

A) Marginal rate of substitution exceeds the slope of the budget line.

B) Marginal rate of substitution is less than the relative price of the good measured on the  $x$ -axis.

C) All income is spent.

D) The consumption choice is outside the budget line.

E) Other consumption points along the consumer's budget line lie on higher indifference curves.

Answer: C

Diff: 2 Type: MC

Topic: Predicting Consumer Choices

7) At the best affordable point, which statement is true?

A) The slope of the indifference curve equals the slope of the budget line.

B) The marginal rate of substitution between two goods equals their absolute price.

C) The highest affordable indifference curve has the same intercept as the budget line.

D) Other points on the same indifference curve are affordable but not preferred.

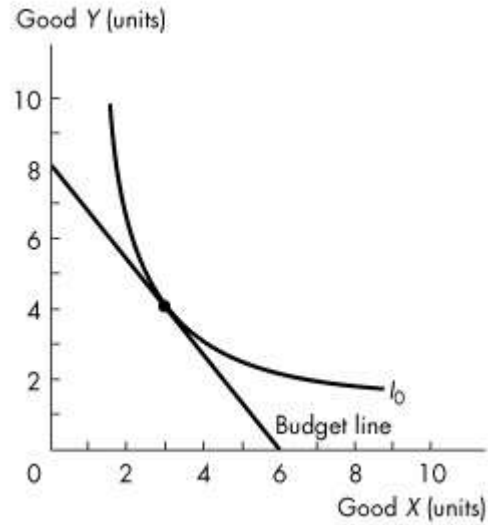
E) Some income is not spent.

Answer: A

Diff: 2 Type: MC

Topic: Predicting Consumer Choices

Use the figure below to answer the following questions.



**Figure 9.3.1**

8) Consider the budget line and indifference curve in Figure 9.3.1. If the price of good X is \$1 a unit, then the price of good Y is

- A) \$0.75 a unit.
- B) \$1 a unit.
- C) \$1.25 a unit.
- D) \$2 a unit.
- E) \$1.33 a unit.

Answer: A

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

9) Consider the budget line and indifference curve in Figure 9.3.1. At the best affordable point, the marginal rate of substitution is

- A)  $1/2$ .
- B) 2.
- C)  $4/3$ .
- D)  $3/4$ .
- E) 4.

Answer: C

Diff: 2 Type: MC

Topic: Predicting Consumer Choices

10) Consider the budget line and indifference curve in Figure 9.3.1. If the price of good X is \$2 a unit, what is the price of good Y?

- A) \$0.37 a unit
- B) \$0.67 a unit
- C) \$1.50 a unit
- D) \$2.67 a unit
- E) impossible to calculate without additional information

Answer: C

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

Use the figure below to answer the following question.

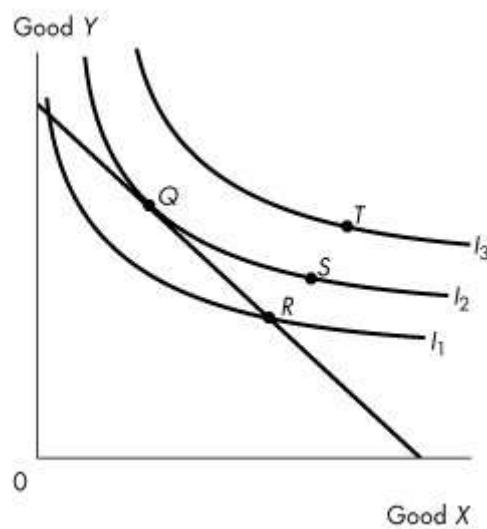


Figure 9.3.2

11) Which one of the following statements about Figure 9.3.2 is *true*?

- A) Point S is preferred to point Q, but S is not affordable.
- B) Point R is not affordable.
- C) Point T is preferred to point Q, but T is not affordable.
- D) Points Q and S cost the same, but Q is preferred to S.
- E) Point R is the best affordable point.

Answer: C

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

Source: Study Guide

12) Peter's income increases and so does his consumption of both movies and pop, but his consumption of pop increases by less than his consumption of movies increases. Which one of the following statements is true for Peter?

- A) A movie is an inferior good; pop is a normal good.
- B) A movie is a normal good; pop is an inferior good.
- C) A movie is an inferior good; pop is an inferior good.
- D) Movies and pop are both normal goods.
- E) A movie is a normal good; we cannot tell whether pop is a normal good or an inferior good.

Answer: D

Diff: 2 Type: MC

Topic: Predicting Consumer Choices

13) A consumer choosing between apples and oranges is at her best affordable point. Then the price of apples decreases. If both apples and oranges are normal goods, which one of the following statements is true about her new best affordable point?

- A) She will consume more apples and more oranges.
- B) She will consume more apples and fewer oranges.
- C) She will consume fewer apples and more oranges.
- D) She will consume fewer apples and fewer oranges.
- E) She will consume more apples, and we cannot tell whether she will consume more or less oranges.

Answer: E

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

14) Which statement is true for a normal good?

- A) The income effect dominates the substitution effect.
- B) The income effect reinforces the substitution effect.
- C) As income increases, consumption decreases.
- D) As income increases, consumption remains constant.
- E) As price falls, we cannot tell whether consumption increases or decreases.

Answer: B

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

15) Which statement is true for an inferior good?

- A) The substitution effect is positive; as price rises, consumption increases.
- B) The income effect is absent; as income increases, consumption remains constant.
- C) The income effect works in the opposite direction to the substitution effect.
- D) The good is of poor workmanship.
- E) The income effect works in the same direction as the substitution effect.

Answer: C

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

16) The effect of a change in income on buying plans is called the

- A) income effect.
- B) substitution effect.
- C) normal effect.
- D) inferior effect.
- E) price effect.

Answer: A

Diff: 2 Type: MC

Topic: Predicting Consumer Choices

17) What is the relationship between goods and the income effect?

- A) An inferior good has a positive income effect.
- B) A normal good has a positive income effect.
- C) An inferior good has no income effect.
- D) A normal good has no income effect.
- E) A normal good has a negative income effect.

Answer: B

Diff: 2 Type: MC

Topic: Predicting Consumer Choices

18) What is a distinguishing characteristic of an inferior good?

- A) a negative price effect
- B) a positive income effect
- C) a positive substitution effect
- D) a negative income effect
- E) an upward-sloping demand curve

Answer: D

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

19) The substitution effect is the effect of

- A) a change in income on the quantity bought.
- B) a change in price on the quantity bought when the consumer moves to a higher indifference curve.
- C) a change in income on the quantity bought when the consumer moves to a higher indifference curve.
- D) a change in the best affordable point.
- E) a change in price on the quantity bought when the consumer hypothetically remains on the same indifference curve.

Answer: E

Diff: 2 Type: MC

Topic: Predicting Consumer Choices

- 20) A change in the price of a good has
- A) an income effect only.
  - B) a substitution effect only.
  - C) a substitution effect and an income effect.
  - D) an income effect that exceeds the substitution effect.
  - E) a substitution effect that exceeds the income effect.

Answer: C

Diff: 2 Type: MC

Topic: Predicting Consumer Choices

- 21) Suppose the price of potatoes falls and there is a decrease in the purchases of potatoes, what can we infer?

- A) The income effect is negative and exceeds the substitution effect.
- B) The income effect is negative and reinforces the substitution effect.
- C) The income effect is positive and exceeds the substitution effect.
- D) The income effect is positive and reinforces the substitution effect.
- E) The income effect is negative and just about offsets the substitution effect.

Answer: A

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

- 22) Which one of the following statements is always true of the substitution effect?

- A) It leads to a positive income effect.
- B) It is positive.
- C) It decreases consumption.
- D) It leads to a negative income effect.
- E) It is negative.

Answer: E

Diff: 2 Type: MC

Topic: Predicting Consumer Choices

- 23) Which one of the following is always true of the price effect?

- A) It leads to a positive income effect.
- B) It is positive.
- C) It decreases consumption.
- D) It leads to a negative income effect.
- E) None of the above.

Answer: E

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

24) Which one of the following is always true of the income effect?

- A) It leads to a positive income effect.
- B) It is positive.
- C) It decreases consumption.
- D) It leads to a negative income effect.
- E) None of the above.

Answer: E

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

25) The price of a good increases relative to other goods. Which one of the following statements must be true? The resulting

- A) income effect is negative.
- B) income effect is positive.
- C) substitution effect is negative.
- D) substitution effect is positive.
- E) income effect is zero.

Answer: C

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

26) When the price of a good changes, the change in consumption that leaves the consumer indifferent between the two choices is called the

- A) normal effect.
- B) substitution effect.
- C) income effect.
- D) price effect.
- E) inferior effect.

Answer: B

Diff: 2 Type: MC

Topic: Predicting Consumer Choices

27) If the price of a normal good rises, the income effect

- A) will increase consumption of the good and the substitution effect will decrease consumption.
- B) will decrease consumption of the good and the substitution effect will increase consumption.
- C) and the substitution effect will both increase consumption of the good.
- D) and the substitution effect will both decrease consumption of the good.
- E) is always larger than the substitution effect.

Answer: D

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

28) If the price of the good measured on the horizontal axis falls, the substitution effect is indicated by movement to a

- A) higher indifference curve.
- B) lower indifference curve.
- C) steeper part of the same indifference curve.
- D) flatter part of the same indifference curve.
- E) flatter part of a higher indifference curve.

Answer: D

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

Source: Study Guide

Use the figure below to answer the following questions.

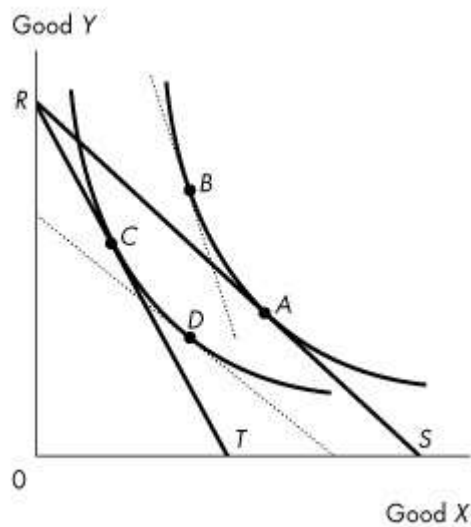


Figure 9.3.3

29) Consider an initial budget line labelled  $RS$  in Figure 9.3.3. The budget line becomes  $RT$  with

- A) a rise in the price of good  $X$ .
- B) a fall in the price of good  $X$ .
- C) a rise in the price of good  $Y$ .
- D) a decrease in the preference for good  $X$ .
- E) an increase in real income.

Answer: A

Diff: 2 Type: MC

Topic: Predicting Consumer Choices

Source: Study Guide

30) Consider an initial budget line labelled *RS* in Figure 9.3.3. If the budget line becomes *RT*, the substitution effect is illustrated by the move from point

- A) *A* to *B*.
- B) *A* to *C*.
- C) *A* to *D*.
- D) *B* to *D*.
- E) *D* to *C*.

Answer: A

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

Source: Study Guide

31) Consider an initial budget line labelled *RS* in Figure 9.3.3. If the budget line becomes *RT*, the income effect is illustrated by the move from point

- A) *A* to *B*.
- B) *A* to *C*.
- C) *A* to *D*.
- D) *B* to *C*.
- E) *B* to *D*.

Answer: D

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

Source: Study Guide

32) Consider an initial budget line labelled *RT* in Figure 9.3.3. What would rotate the budget line to *RS*?

- A) a rise in the price of good *X*
- B) a fall in the price of good *X*
- C) a rise in the price of good *Y*
- D) a decrease in the preference for good *X*
- E) an increase in real income

Answer: B

Diff: 2 Type: MC

Topic: Predicting Consumer Choices

33) Consider an initial budget line labelled *RT* in Figure 9.3.3. If the budget line becomes *RS*, the substitution effect is illustrated by the move from point

- A) *A* to *C*.
- B) *A* to *D*.
- C) *B* to *D*.
- D) *B* to *A*.
- E) *C* to *D*.

Answer: E

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

34) Consider an initial budget line labelled  $RT$  in Figure 9.3.3. If the budget line becomes  $RS$ , the income effect is illustrated by the move from point

- A)  $A$  to  $B$ .
- B)  $A$  to  $C$ .
- C)  $B$  to  $D$ .
- D)  $C$  to  $B$ .
- E)  $D$  to  $A$ .

Answer: E

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

35) If the price of an inferior good rises, the income effect

- A) will have an uncertain effect on consumption of the good, and the substitution effect will decrease consumption.
- B) will decrease consumption of the good, and the substitution effect will decrease consumption.
- C) and the substitution effect will both increase consumption of the good.
- D) and the substitution effect will both decrease consumption of the good.
- E) will increase consumption of the good and the substitution effect will decrease consumption.

Answer: E

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

*Use the information below to answer the following questions.*

### **Fact 9.3.1**

Marc has an income of \$20 and spends it on two goods, root beer (measured on the vertical axis) and chips (measured on the horizontal axis). The price of root beer is \$1 a can. The price of chips is \$0.50 a bag. Initially, Marc chooses to consume 10 cans of root beer and 20 bags of chips. Then the price of root beer rises to \$1.50 per can and the price of chips falls to \$0.25 a bag.

36) Refer to Fact 9.3.1. Marc's initial marginal rate of substitution was

- A) not calculable with the information given.
- B) equal to 2 cans of root beer given up for each bag of chips gained.
- C) equal to 1 can of root beer given up for each bag of chips gained.
- D) equal to 10 cans of root beer given up for each bag of chips gained.
- E) equal to 1/2 can of root beer given up for each bag of chips gained.

Answer: E

Diff: 2 Type: MC

Topic: Predicting Consumer Choices

- 37) Refer to Fact 9.3.1. When the price of a bag of chips falls, Marc
- A) will consume more beer, more chips, and be better off.
  - B) will consume less beer, more chips, and be better off.
  - C) will consume less beer, more chips, and be worse off.
  - D) will consume less beer, less chips, and be worse off.
  - E) consume more beer, less chips, and be better off.

Answer: B

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

- 38) When price rises, the substitution effect
- A) always increases consumption.
  - B) increases consumption for normal goods only.
  - C) decreases consumption for normal goods only.
  - D) decreases consumption for inferior goods only.
  - E) does none of the above.

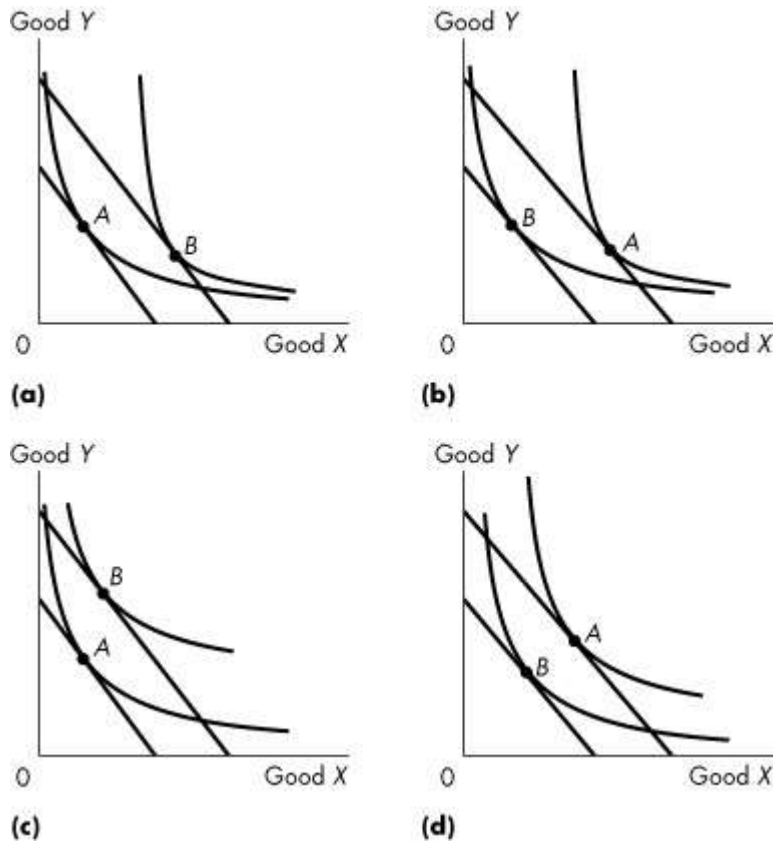
Answer: E

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

Source: Study Guide

Use the figure below to answer the following questions.



**Figure 9.3.4**

Original equilibrium at *A*, new equilibrium at *B*

39) Refer to Figure 9.3.4. Which graphs show the case where good *Y* is an inferior good?

- A) (a) and (b)
- B) (c) and (d)
- C) (a) and (c)
- D) (b) and (d)
- E) none of the graphs

Answer: A

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

40) Refer to Figure 9.3.4. Which graphs show the case where good  $Y$  is a normal good?

- A) (a) and (b)
- B) (c) and (d)
- C) (a) and (c)
- D) (b) and (d)
- E) none of the graphs

Answer: B

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

41) Karen consumes chocolate and candles. When Karen is at her best affordable point, she is \_\_\_\_\_.

- A) on or inside her budget line, on her highest attainable indifference curve, and has a marginal rate of substitution between chocolate and candles that is equal to the relative price of chocolate and candles
- B) on the indifference curve that is closest to the origin and minimizing the marginal rate of substitution
- C) on the indifference curve that is farthest from the origin and maximizing the marginal rate of substitution
- D) on her budget line, on her highest attainable indifference curve, and has a marginal rate of substitution between chocolate and candles that is equal to the relative price of chocolate and candles
- E) on her budget line, on her highest attainable indifference curve, and maximizing the marginal rate of substitution

Answer: D

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

Source: MyEconLab

42) The substitution effect is the effect of a change in \_\_\_\_\_ on \_\_\_\_\_. The income effect is the effect of a change in \_\_\_\_\_ on \_\_\_\_\_.

- A) income; quantity bought of a substitute; income; quantity bought
- B) income; consumption; price; quantity bought
- C) price; quantity bought; income; quantity bought
- D) the price of a substitute; quantity bought; income; the number of labour hours
- E) none of the above

Answer: C

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

Source: MyEconLab

- 43) For a normal good, the income effect \_\_\_\_\_.
- A) is negative and the substitution effect is positive
  - B) reinforces the substitution effect
  - C) is positive and the substitution effect is negative
  - D) is equal and opposite to the substitution effect
  - E) is zero

Answer: B

Diff: 3 Type: MC

Topic: Predicting Consumer Choices

Source: MyEconLab

- 44) When Jim is at his best affordable point, the budget line
- A) is steeper than the highest attainable indifference curve.
  - B) is flatter than the highest attainable indifference curve.
  - C) does not touch the highest attainable indifference curve.
  - D) is tangent to the highest attainable indifference curve.
  - E) intersects the highest attainable indifference curve.

Answer: D

Type: MC

- 45) Albert is consuming at a point where his budget line is not as steep as indifference curve. To reach consumer equilibrium, Albert

- A) consumes less of the good that is measured on the horizontal axis.
- B) consumes none of the good that is measured on the horizontal axis.
- C) must increase his income.
- D) must shop at stores that have lower prices.
- E) consumes more of the good that is measured on the horizontal axis.

Answer: E

Type: MC

- 46) The substitution effect

- A) always dominates the income effect.
- B) is always dominated by the income effect.
- C) results in an increase in the quantity of the good consumed when the price rises.
- D) results in a decrease in the quantity of the good consumed when the price falls.
- E) is greater than the price effect.

Answer: D

Type: MC

## Chapter 10 Organizing Production

### 10.1 The Firm and Its Economic Problem

- 1) A firm's goal is to

- A) maximize revenue.
- B) maximize cost while minimizing revenue.

- C) maximize profit.
- D) minimize costs.
- E) minimize risk.

Answer: C

Diff: 1 Type: MC

Topic: The Firm and Its Economic Problem

2) A firm's total opportunity cost of production is the sum of the cost of using resources

- A) bought in the market.
- B) owned by the firm.
- C) supplied by the firm's owner.
- D) bought in the market and supplied by the firm's owner.
- E) bought in the market, owned by the firm, and supplied by the firm's owner.

Answer: E

Diff: 1 Type: MC

Topic: The Firm and Its Economic Problem

3) The implicit rental rate

- A) is the firm's opportunity cost of using the capital it owns.
- B) is paid with cash.
- C) has two components: economic depreciation and foregone interest.
- D) both A and C are correct.
- E) both B and C are correct.

Answer: D

Diff: 1 Type: MC

Topic: The Firm and Its Economic Problem

4) Which one of the following is included in the implicit rental rate of capital?

- A) economic depreciation
- B) the cost of electricity
- C) the cost of raw materials
- D) the cost of low-skilled labour
- E) the cost of heating

Answer: A

Diff: 2 Type: MC

Topic: The Firm and Its Economic Problem

5) Which one of the following statements about the implicit rental rate of capital is true?

- A) It is the market value of capital.
- B) It is the opportunity cost to a firm of using its own capital.
- C) It includes normal profit.
- D) It is the amount paid for the use of land or buildings.
- E) It is the depreciated value of capital.

Answer: B

Diff: 1 Type: MC

Topic: The Firm and Its Economic Problem

6) The difference in the market value of a new car and the market value of the same car one year later is

- A) economic depreciation.
- B) physical depreciation.
- C) economic deterioration.
- D) physical deterioration.
- E) conventional depreciation.

Answer: A

Diff: 1 Type: MC

Topic: The Firm and Its Economic Problem

7) Economic depreciation is

- A) the same as depreciation calculated by an accountant.
- B) equal to economic profit minus normal profit.
- C) the change in the market value of capital over a given period.
- D) the deterioration of the physical appearance of a capital.
- E) paid in cash.

Answer: C

Diff: 1 Type: MC

Topic: The Firm and Its Economic Problem

8) Marc bought a new car last year for \$10,000. He can now sell the car for \$8,500. To buy this year's model of the same car he would have to pay \$11,000. What is the one-year amount of economic depreciation?

- A) \$2,500
- B) \$1,500
- C) \$1,000
- D) \$10,000
- E) \$3,500

Answer: B

Diff: 2 Type: MC

Topic: The Firm and Its Economic Problem

9) Marc bought a new car last year for \$10,000. He can now sell the car for \$8,500. To buy this year's model of the same car he would have to pay \$11,000. What is the implicit rental rate using the car for one year at a zero percent interest rate?

- A) \$2,500
- B) \$3,500
- C) \$1,000
- D) \$10,000
- E) \$1,500

Answer: E

Diff: 2 Type: MC

Topic: The Firm and Its Economic Problem

10) Marc bought a new car last year for \$10,000. He can now sell the car for \$8,500. To buy this year's model he would have to pay \$11,000. Marc also had to take out a \$9,000 loan to buy the car, which had to be paid back in yearly installments of \$3,300 per year over three years. What is the implicit rental rate of the first year's use of the car?

- A) \$2,800
- B) \$1,300
- C) \$1,800
- D) \$13,300
- E) \$4,800

Answer: C

Diff: 3 Type: MC

Topic: The Firm and Its Economic Problem

11) The implicit rental rate to a firm of owning a building is

- A) the sum of economic depreciation and foregone interest.
- B) economic depreciation only.
- C) foregone interest only.
- D) the cost of using an alternative building.
- E) the rent paid on the building.

Answer: A

Diff: 2 Type: MC

Topic: The Firm and Its Economic Problem

12) Gerald is a freelance writer who could work for a newspaper at \$25,000 a year but instead runs his own business making revenue of \$40,000 a year. His only business expenses are \$1,000 for writing materials and \$12,000 for rent. What is Gerald's economic profit from working as a freelance writer?

- A) \$2,000
- B) \$28,000
- C) \$15,000
- D) \$25,000
- E) \$27,000

Answer: A

Diff: 2 Type: MC

Topic: The Firm and Its Economic Problem

- 13) Economic profit equals total revenue minus
- A) the cost of resources bought in the market.
  - B) the implicit rental rate.
  - C) the opportunity cost of production.
  - D) the cost of resources supplied by the owner.
  - E) the cost of resources owned by the firm.

Answer: C

Diff: 2 Type: MC

Topic: The Firm and Its Economic Problem

- 14) In general,
- (1) opportunity cost is greater than accounting cost.
  - (2) opportunity cost is less than accounting cost.
  - (3) economic profit is greater than accounting profit.
  - (4) economic profit is less than accounting profit.
- A) 1 only
  - B) 1 and 3
  - C) 1 and 4
  - D) 2 and 3
  - E) 2 and 4

Answer: C

Diff: 2 Type: MC

Topic: The Firm and Its Economic Problem

Source: Study Guide

- 15) A profit-maximizing firm is constrained by
- A) demand for its product.
  - B) limited resources.
  - C) available technology.
  - D) limited information.
  - E) all of the above.

Answer: E

Diff: 2 Type: MC

Topic: The Firm and Its Economic Problem

Source: Study Guide

16) Normal profit is the \_\_\_\_\_. Normal profit \_\_\_\_\_ part of a firm's opportunity cost because \_\_\_\_\_.

- A) return that an entrepreneur can expect to receive on the average; is; it is the cost of a foregone alternative, which is running another firm
- B) profit used by the Canada Revenue Agency to calculate tax owing; is; part of it must be paid to the government and is no longer available to the entrepreneur
- C) profit used by the Canada Revenue Agency to calculate tax owing; is; it is paid in cash
- D) return that an entrepreneur can expect to receive on the average; is not; it is not paid in cash
- E) profit used by the Canada Revenue Agency to calculate tax owing; is; it includes depreciation

Answer: A

Type: MC

Topic: The Firm and Its Economic Problem

Source: MyEconLab

17) A firm's opportunity cost includes

- A) the cost of using resources bought in the market and owned by the firm only.
- B) the cost of using resources bought in the market, owned by the firm, and supplied by the firm's owner.
- C) only costs that are paid in cash or by cheque.
- D) the cost of using resources supplied by the firm's owner only.
- E) economic profit.

Answer: B

Type: MC

Topic: The Firm and Its Economic Problem

Source: MyEconLab

18) Which of the following is part of a firm's opportunity cost of production?

- I. wages
  - II. utility costs
  - III. interest on a bank loan
  - IV. interest forgone on funds used to buy capital equipment
- A) I only
  - B) II only
  - C) III only
  - D) IV only
  - E) I, II, III, and IV

Answer: E

Type: MC

19) If economic profit is equal to zero then the firm is making

- A) a normal profit.
- B) zero profit as recorded by accountants.
- C) negative profit as recorded by accountants.
- D) zero taxable income.
- E) an amount equal to the implicit rental rate.

Answer: A

Type: MC

## 10.2 Technological and Economic Efficiency

1) Firm *A* can produce a unit of output with 10 hours of labour and 5 units of capital. Firm *B* can produce a unit of output with 5 hours of labour and 10 units of capital. Firm *C* can produce a unit of output with 10 hours of labour and 10 units of capital. If the prices of labour and material are \$10 and \$5, respectively which firm is *technologically* efficient?

- A) *A* only
- B) *B* only
- C) *C* only
- D) *A* and *B*
- E) *A* and *C*

Answer: D

Diff: 3 Type: MC

Topic: Technological and Economic Efficiency

2) To produce a unit of output, Alphaworks uses 10 hours of labour and 5 kilograms of material. Betaworks uses 5 hours of labour and 10 kilograms of material, and Gammaworks uses 10 hours of labour and 10 kilograms of material. If labour costs \$10 per hour and material costs \$5 per kilogram, which firm is *economically* efficient?

- A) Alphaworks only
- B) Betaworks only
- C) Gammaworks only
- D) Alphaworks and Betaworks
- E) Alphaworks and Gammaworks

Answer: B

Diff: 2 Type: MC

Topic: Technological and Economic Efficiency

Source: Study Guide

3) Which one of the following statements is *not* true?

- A) A production process is technologically efficient only if it is producing a given output at the lowest possible cost.
- B) If a process is economically efficient, it must be technologically efficient as well.
- C) Economic efficiency depends on the relative price of inputs, while technological efficiency does not.
- D) Economically efficient firms will be more likely to survive than economically inefficient firms.
- E) Technologically efficient firms are more likely to survive than technologically inefficient firms.

Answer: A

Diff: 2 Type: MC

Topic: Technological and Economic Efficiency

Use the information below to answer the following questions.

**Fact 10.2.1**

Consider the following three methods of preparing your tax return. Method *A* uses a personal computer (cost equal to \$1,000) and 1 hour of your time. Method *B* uses a calculator (cost equal to \$30) and 12 hours of your time. Method *C* uses pen and paper (cost equal to \$1) and 2 days (16 hours) of your time.

4) Consider Fact 10.2.1. Which production method is *technologically* inefficient?

- A) *A*
- B) *B*
- C) *C*
- D) all of the above
- E) none of the above

Answer: E

Diff: 3 Type: MC

Topic: Technological and Economic Efficiency

5) Consider Fact 10.2.1. Choose the best statement.

- A) When your wage rate is \$5 per hour, the economically efficient method is method *C*.
- B) When your wage rate is \$50 per hour, the economically efficient method is method *B*.
- C) When your wage rate is \$500 per hour, the economically efficient method is method *A*.
- D) all of the above
- E) B and C only

Answer: D

Diff: 2 Type: MC

Topic: Technological and Economic Efficiency

Use the table below to answer the following questions.

**Table 10.2.1**

Method	Quantity of Labour	Quantity of Capital
1	5	10
2	10	7
3	15	5

6) Refer to Table 10.2.1, which shows three methods for making photon torpedoes. Which method is *technologically* efficient?

- A) 1 only
- B) 2 only
- C) 3 only
- D) all of the methods
- E) 1 and 3 only

Answer: D

Diff: 2 Type: MC

Topic: Technological and Economic Efficiency

Source: Study Guide

7) Refer to Table 10.2.1. If the price of labour is \$10 per unit and the price of capital is \$20 per unit, which method is *economically* efficient?

- A) 1 only
- B) 2 only
- C) 3 only
- D) all of the above
- E) 1 and 3 only

Answer: B

Diff: 2 Type: MC

Topic: Technological and Economic Efficiency

Source: Study Guide

8) Which one of the following statements is *true*?

- A) All technologically efficient methods are also economically efficient.
- B) All economically efficient methods are also technologically efficient.
- C) Technological efficiency changes with changes in relative input prices.
- D) Technologically efficient firms will be more likely to survive than economically efficient firms.
- E) none of the above

Answer: B

Diff: 2 Type: MC

Topic: Technological and Economic Efficiency

Source: Study Guide

Use the table below to answer the following questions.

**Table 10.2.2**  
Three methods of making one medical hologram

Method	Labour	Capital
1	5	10
2	10	15
3	15	5

9) In Table 10.2.2, which method of making a medical hologram is *technologically* efficient?

- A) 1 only
- B) 2 only
- C) 3 only
- D) all of the above
- E) 1 and 3 only

Answer: E

Diff: 2 Type: MC

Topic: Technological and Economic Efficiency

10) Refer to Table 10.2.2. If the price of labour is \$20 per unit and the price of capital is \$10 per unit, which method is *economically* efficient?

- A) 1 only
- B) 2 only
- C) 3 only
- D) 2 and 3 only
- E) 1 and 3 only

Answer: A

Diff: 2 Type: MC

Topic: Technological and Economic Efficiency

11) A firm that uses the latest technology \_\_\_\_\_ technologically efficient because \_\_\_\_\_.

- A) is not necessarily; the firm might not use the least amount of inputs to produce a given output
- B) is not necessarily; new technology is more expensive than old technology
- C) is; efficiency is about costs rather than when the technology was developed
- D) is; new technology isn't developed unless it is efficient
- E) is; most consumers want access to the latest technology

Answer: A

Type: MC

Topic: Technological and Economic Efficiency

Source: MyEconLab

12) Some firms use large amounts of capital and small amounts of labour, while others use small amounts of capital and large amounts of labour to

A) use surpluses of labour and capital and eliminate unemployment of these resources.

B) use the best available technology.

C) use the resources that are most readily available.

D) maximize profit.

E) maximize production.

Answer: D

Type: MC

Topic: Technological and Economic Efficiency

Source: MyEconLab

13) Emma owns a firm that produces umbrellas. Currently, Emma produces 2,500 umbrellas a day. Emma cannot produce more umbrellas in a day unless she purchases another machine or else hires more workers. Emma is \_\_\_\_\_ efficient.

A) economically

B) economically and technologically

C) technologically

D) not

E) capital and labour

Answer: C

Type: MC

14) A firm that is technologically efficient

A) always makes an economic profit.

B) *must* be economically efficient, but a firm that is economically efficient is not always technologically efficient.

C) *must* be economically efficient, and a firm that is economically efficient *must* always be technologically efficient.

D) is not always economically efficient, and a firm that is economically efficient is not always technologically efficient.

E) is not always economically efficient, but a firm that is economically efficient *must* always be technologically efficient.

Answer: E

Type: MC

### 10.3 Information and Organization

- 1) In the relationship between the owner of a bakery and the baker, the owner is
- A) an agent, as is the baker.
  - B) an agent and the baker is a principal.
  - C) a principal and the baker is an agent.
  - D) a principal, as is the baker.
  - E) neither a principal nor an agent, but the baker is an agent.

Answer: C

Diff: 1 Type: MC

Topic: Information and Organization

- 2) A firm with a single owner who has unlimited liability is
- A) a corporation.
  - B) a sole proprietorship.
  - C) a limited partnership.
  - D) an unlimited partnership.
  - E) a cooperative.

Answer: B

Diff: 1 Type: MC

Topic: Information and Organization

- 3) The legal responsibility for debts incurred by a sole proprietorship falls upon
- A) the shareholders.
  - B) the partners of the sole proprietorship.
  - C) the owner.
  - D) the creditors.
  - E) the managers.

Answer: C

Diff: 1 Type: MC

Topic: Information and Organization

- 4) The profits of a sole proprietorship are
- A) taxed twice.
  - B) subject to a corporate tax.
  - C) not taxed.
  - D) exempt from taxation.
  - E) treated as the owner's income.

Answer: E

Diff: 1 Type: MC

Topic: Information and Organization

5) Typical examples of a partnership would include which one of the following?

- A) a law firm
- B) a corner drugstore
- C) an automobile manufacturer
- D) a bank
- E) a freelance writer

Answer: A

Diff: 1 Type: MC

Topic: Information and Organization

6) In a partnership, each partner is legally liable for

- A) all the debts of the partnership.
- B) the fraction of the debts corresponding to the fraction of ownership.
- C) 50 percent of the debt.
- D) all debts of the partnership limited by the personal wealth of the partner.
- E) an amount of debt limited to the amount of the partner's investment in the partnership.

Answer: D

Diff: 1 Type: MC

Topic: Information and Organization

7) Most establishments in Canada

- A) employ between 5 and 99 people.
- B) employ more than 100 people.
- C) employ fewer than 5 people.
- D) employ more than 500 people.
- E) are partnerships.

Answer: C

Diff: 1 Type: MC

Topic: Information and Organization

8) Susan invests \$1,000 to buy shares of TooNew stock. The company declares bankruptcy, leaving many debts unpaid, including Susan's \$1,000 investment. Susan has a personal net worth of \$50,000. What will be Susan's final net worth if TooNew has total unpaid debts of \$30,000?

- A) \$19,000
- B) \$21,000
- C) \$49,000
- D) \$51,000
- E) \$20,000

Answer: C

Diff: 2 Type: MC

Topic: Information and Organization

9) Mr. Brown opens his restaurant as a sole proprietorship. After a year of disastrous reviews, he has gone deeply into debt. His liability is

- A) zero; he has already lost all his money.
- B) the amount of his original investment.
- C) limited only by his entire wealth.
- D) limited to assets owned by the restaurant.
- E) depends upon how much money he has in his savings account.

Answer: C

Diff: 2 Type: MC

Topic: Information and Organization

10) A firm with two or more owners who have unlimited liability is

- A) a sole proprietorship.
- B) a partnership.
- C) a conglomerate.
- D) a corporation.
- E) a public company.

Answer: B

Diff: 1 Type: MC

Topic: Information and Organization

Source: Study Guide

11) A firm with one or more owners of limited liability is

- A) a sole proprietorship.
- B) a partnership.
- C) a conglomerate.
- D) a corporation.
- E) a public company.

Answer: D

Diff: 1 Type: MC

Topic: Information and Organization

12) What is a *disadvantage* of a corporation relative to a sole proprietorship or partnership?

- A) Owners have unlimited liability.
- B) Profits are taxed twice; as corporate profits and as dividend income and capital gains to stockholders.
- C) high cost of capital
- D) perpetual life
- E) None of the above.

Answer: B

Diff: 2 Type: MC

Topic: Information and Organization

Source: Study Guide

13) Which one of the following is an *advantage* of a corporation relative to a proprietorship or partnership?

- A) Owners have limited liability.
- B) Profits are taxed once.
- C) difficult to raise money
- D) no principal-agent problems
- E) None of the above.

Answer: A

Diff: 2 Type: MC

Topic: Information and Organization

14) A sole proprietorship

- A) dies with the owner.
- B) is the same as a partnership.
- C) always bring a higher return to its owner than a corporation brings to its owners.
- D) is a not-for-profit firm.
- E) has a complex management structure.

Answer: A

Diff: 1 Type: MC

Topic: Information and Organization

15) Firms organize production by using

- A) command systems only.
- B) incentive systems only.
- C) command and incentive systems.
- D) market systems only.
- E) principal-agent systems only.

Answer: C

Diff: 2 Type: MC

Topic: Information and Organization

Source: Study Guide

16) Firm strategies for coping with the principal-agent problem are

- A) ownership, incentive pay, and long-term contracts.
- B) sole proprietorship, partnership, and the corporation.
- C) economies of scale, scope, and team production.
- D) technology, information, and the market.
- E) ownership, scope, and the market.

Answer: A

Diff: 2 Type: MC

Topic: Information and Organization

Source: Study Guide

17) Firms cope with uncertainty and incomplete information by using

- A) sole proprietorship, limited liability, and market coordination.
- B) ownership, incentive pay, and long-term contracts.
- C) team production, economies of scale, and transactions costs.
- D) the market, the firm, and internal organization.
- E) team production, economies of scale, and transaction costs.

Answer: B

Diff: 2 Type: MC

Topic: Information and Organization

18) The possibility that an employee may not work hard is an example of the

- A) limited liability problem.
- B) principal-agent problem.
- C) transactions cost problem.
- D) technological efficiency problem.
- E) partnership problem.

Answer: B

Diff: 2 Type: MC

Topic: Information and Organization

Source: Study Guide

19) The principal-agent problem exists when

- A) there is no command system in place.
- B) firms operate as sole proprietorships.
- C) agents do not act in the best interest of principals.
- D) principals do not act in the best interest of agents.
- E) the future value of money is more than its current value.

Answer: C

Diff: 1 Type: MC

Topic: Information and Organization

20) Federal Express enters into contracts with independent truck operators who offer FedEx service and who are rewarded by the volume (cubic feet) of packages they carry.

FedEx does not hire more independent drivers because

- A) it is concerned about a possible downturn in the economy and the effects of overexpansion.
- B) it cannot afford more trucks and more drivers.
- C) of the principal-agent problem.
- D) it is a corporation, so it wants to have a limited number of independent truck owners operating as proprietorships.
- E) trucks are not a technologically efficient method of transporting parcels.

Answer: C

Type: MC

Topic: Information and Organization

Source: MyEconLab

21) It is a disadvantage of \_\_\_\_\_ that retained profits are taxed twice.  
It is a disadvantage of \_\_\_\_\_ that bad decisions are not checked by the need for consensus.  
A) a sole proprietorship; both a partnership and a sole proprietorship  
B) a corporation; a sole proprietorship  
C) both a partnership and a sole proprietorship; a partnership  
D) a corporation; both a partnership and a sole proprietorship  
E) both a corporation and a partnership; a sole proprietorship  
Answer: B  
Type: MC  
Topic: Information and Organization  
Source: MyEconLab

22) A golf club manufacturer pays its workers based on the number of sets of clubs they produce.  
This firm  
A) organizes production based on a command system.  
B) does not have a principal-agent problem.  
C) is a sole proprietorship.  
D) organizes production based on an incentive system.  
E) is a corporation.  
Answer: D  
Type: MC

23) An example of the principal-agent problem occurs when  
A) an agent is more motivated than the principle to provide a high-quality good or service.  
B) managers try to cope with employees that are inefficient.  
C) sole proprietors don't receive any money payment for their entrepreneurial skills.  
D) managers devise penalties that eliminate employee waste.  
E) managers devise incentives that encourage employees to act in the owner's behalf.  
Answer: E  
Type: MC

## 10.4 Markets and the Competitive Environment

Use the table below to answer the following questions.

**Table 10.4.1**

Taco Stands		Pizza Sellers	
Firm	Sales (dollars)	Firm	Sales (dollars)
Burning Belly	150	Prairie Pizza	600
Fire Mouth	70	Pizza Condo	400
Taco Taco	50	Inferior Pizza	140
Taco Hut	30	McDaisy's	60
Top 4 sales	300	Top 4 sales	1,200
Total Sales	900	Total Sales	1,500

1) Refer to Table 10.4.1. The four-firm concentration ratio for taco stands is

- A) 15 percent.
- B) 100 percent.
- C) 80 percent.
- D) 33 percent.
- E) 30 percent.

Answer: D

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

2) Refer to Table 10.4.1. The four-firm concentration ratio for the pizza sellers is

- A) 40 percent.
- B) 100 percent.
- C) 80 percent.
- D) 33 percent.
- E) 12.5 percent.

Answer: C

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

3) Which one of the following statements describes a market that is monopolistically competitive?

- A) The presence of significant barriers to entry.
- B) The products produced by the firms are identical.
- C) Many firms compete by making similar but slightly different products.
- D) There is a small number of large firms.
- E) The product produced by one firm has no close substitutes.

Answer: C

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment



- 4) One difference between perfect competition and monopolistic competition is
- A) firms in a perfectly competitive market produce similar but slightly different products.
  - B) in perfect competition, the product produced has no close substitutes.
  - C) monopolistic competition has barriers to entry, whereas perfect competition has none.
  - D) firms in monopolistic competition have some degree of market power.
  - E) a small number of firms compete in a monopolistically competitive market and a large number of firms compete in a perfectly competitive market.

Answer: D

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

- 5) One difference between oligopoly and monopolistic competition is
- A) there is a smaller number of firms in a monopolistically competitive market than in an oligopoly.
  - B) in oligopolies firms make slightly different products whereas in monopolistic competition the products are identical.
  - C) monopolistic competition has barriers to entry, whereas oligopoly has none.
  - D) fewer firms compete in an oligopoly than in a monopolistically competitive market.
  - E) in oligopolies, firms are typically smaller in size.

Answer: D

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

- 6) The four-firm concentration ratio measures the share of the largest four firms in total industry
- A) profit.
  - B) sales.
  - C) cost.
  - D) capital.
  - E) loss.

Answer: B

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

Source: Study Guide

- 7) The purpose of calculating the concentration ratio is
- A) to obtain the firm's total profit.
  - B) to obtain the firm's production cost.
  - C) to measure the losses the firm incurred.
  - D) to measure the extent to which the market is dominated by a small number of firms.
  - E) to distinguish between the firm's total profit and production cost.

Answer: D

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

8) In a perfectly competitive market, the four-firm concentration ratio is

- A) almost zero.
- B) 50 percent.
- C) 100 percent.
- D) 75 percent.
- E) 25 percent.

Answer: A

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

9) In a monopoly, the four-firm concentration ratio is

- A) 75 percent.
- B) 100 percent.
- C) almost zero.
- D) 25 percent.
- E) 50 percent.

Answer: B

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

10) A four-firm concentration ratio of less than 60 percent indicates

- A) a monopoly.
- B) a market that is dominated by a few firms.
- C) a competitive market.
- D) an oligopoly.
- E) an absence of competition.

Answer: C

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

11) A four-firm concentration ratio that exceeds 60 percent indicates

- A) a perfectly competitive market.
- B) a monopolistically competitive market.
- C) a monopoly.
- D) an oligopoly.
- E) a competitive market.

Answer: D

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

12) The Herfindahl-Hirschman Index (HHI) is the square of the percentage market share of each firm summed over the \_\_\_\_\_ firms in a market.

- A) largest 60
- B) largest 50
- C) smallest 50
- D) largest 75
- E) smallest 60

Answer: B

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

13) In a perfectly competitive market, the Herfindahl-Hirschman Index (HHI)

- A) is small.
- B) is usually greater than 5,000.
- C) is greater than 1,000 but less than 2,000.
- D) lies between 1,200 and 1,500.
- E) is greater than 10,000.

Answer: A

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

14) A market in which the Herfindahl-Hirschman Index (HHI) lies between 1,000 and 1,800 is regarded as being

- A) a monopoly.
- B) an oligopoly.
- C) a perfectly competitive market.
- D) a moderately competitive market.
- E) a potential matter of concern for regulators.

Answer: D

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

15) When the Herfindahl-Hirschman Index (HHI) is greater than 1,800,

- A) the market is very competitive.
- B) a monopoly exists.
- C) there are many producers in the market.
- D) the market is moderately competitive.
- E) the market is uncompetitive.

Answer: E

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

- 16) An industry with a high four-firm concentration ratio may have little monopoly power if
- A) its production is geographically concentrated.
  - B) its barriers to entry are low.
  - C) its barriers to entry are high.
  - D) there are no international producers of the product.
  - E) there are no close substitutes for its product.

Answer: B

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

- 17) The four-firm concentration ratio tells us the percentage of \_\_\_\_\_ for the four largest firms in an industry.
- A) employment
  - B) accounting profit
  - C) economic profit
  - D) the value of sales
  - E) physical output

Answer: D

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

- 18) A provincial phone company like SaskTel likely has
- A) a high four-firm concentration ratio in the province, but a low one nationally.
  - B) a low four-firm concentration ratio in the province, but a high one nationally.
  - C) a low four-firm concentration ratio in the province and nationally.
  - D) a high four-firm concentration ratio in the province and nationally.
  - E) a four-firm concentration ratio of zero.

Answer: A

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

- 19) What is the maximum value of the Herfindahl-Hirschman Index?
- A) 1
  - B) 1,000,000
  - C) 100,000
  - D) 10,000
  - E) 1,000

Answer: D

Diff: 3 Type: MC

Topic: Markets and the Competitive Environment

20) The Herfindahl-Hirschman Index is calculated as

- A) the cube of the percentage market share of each firm summed over the largest 100 firms.
- B) the square of the percentage market share of each firm summed over the largest 50 firms or summed over all the firms if there are fewer than 50.
- C) the square of the percentage market share of each firm summed over the largest 20 firms.
- D) double the market share of the five largest firms.
- E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

21) If a market is shared equally by four firms, the Herfindahl-Hirschman Index is

- A) 1/4.
- B) 4.
- C) 25.
- D) 100.
- E) 2,500.

Answer: E

Diff: 3 Type: MC

Topic: Markets and the Competitive Environment

22) Where the Herfindahl-Hirschman Index is less than 1,000, the market is regarded as

- A) a monopoly.
- B) an oligopoly.
- C) competitive.
- D) regulated.
- E) none of the above.

Answer: C

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

23) A market structure where a small number of firms compete occurs in

- A) perfect competition.
- B) monopolistic competition.
- C) the worldwide market for wheat, corn, and rice.
- D) oligopoly.
- E) monopoly.

Answer: D

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

Source: Study Guide

24) Which of the following industries in Canada has the highest four-firm concentration ratio?

- A) audio and video equipment
- B) clothing
- C) bakery items
- D) fabrics
- E) tobacco products

Answer: E

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

25) Which of the following industries in Canada has the lowest four-firm concentration ratio?

- A) tires
- B) soft drinks and ice
- C) textiles
- D) sugar
- E) wooden windows and doors

Answer: C

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

26) The Herfindahl-Hirschman Index (HHI) for a local water supplier is

- A) less than 100.
- B) between 101 and 999.
- C) more than 1,000 but less than 2,000.
- D) 10,000.
- E) between 2,000 and 5,000.

Answer: D

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

27) If a market is shared equally by 100 firms, the Herfindahl-Hirschman Index is

- A) 1/100.
- B) 1/50.
- C) 1.
- D) 50.
- E) 100.

Answer: D

Diff: 3 Type: MC

Topic: Markets and the Competitive Environment

28) Product differentiation is always a feature in

- A) perfect competition.
- B) monopolistic competition.
- C) oligopoly.
- D) monopoly.
- E) all of the above.

Answer: B

Diff: 2 Type: MC

Topic: Markets and the Competitive Environment

Source: Study Guide

29) The North American economy is \_\_\_\_\_ and is becoming \_\_\_\_\_ competitive.

- A) uncompetitive; less
- B) competitive; more
- C) competitive; less
- D) uncompetitive; more
- E) currently an oligopolistic market; more

Answer: B

Type: MC

Topic: Markets and the Competitive Environment

Source: MyEconLab

30) The four-firm concentration ratio in an industry is 75 percent.

Total sales in the industry are \$800 million and total economic profit in the industry is \$500 million. Normal profit for each firm is zero.

From this information we know that

- A) economic profit of any four firms is at least \$667 million.
- B) total sales from the four largest firms is \$600 million.
- C) economic profit of the four largest firms is \$375 million.
- D) total sales from any four firms is at least \$1,067 million.
- E) economic profit of the four largest firms is \$500 million.

Answer: B

Type: MC

Topic: Markets and the Competitive Environment

Source: MyEconLab

31) Which of the following pairs of market types are both characterized by having a large number of firms?

- A) oligopoly and monopolistic competition
- B) monopoly and oligopoly
- C) perfect competition and monopolistic competition
- D) monopoly and monopolistic competition
- E) perfect competition and oligopoly

Answer: C

Type: MC

32) The correct ranking of the four basic market structures from low HHI (Herfindahl-Hirschman Index) to high HHI is

- A) monopolistic competition, perfect competition, oligopoly, monopoly.
- B) perfect competition, oligopoly, monopolistic competition, monopoly.
- C) monopoly, oligopoly, monopolistic competition, perfect competition.
- D) perfect competition, monopolistic competition, oligopoly, monopoly.
- E) monopoly, monopolistic competition, oligopoly, perfect competition.

Answer: D

Type: MC

## 10.5 Produce or Outsource? Firms and Markets

1) Which one of the following is not generally a transactions cost?

- A) the fee to a broker for buying stocks
- B) the cost of a lawyer who drafts a contract
- C) the cost of hiring someone to find you a supplier of raw materials
- D) the cost of the owner's time in a sole proprietorship
- E) the cost of phone calls made to find a buyer

Answer: D

Diff: 2 Type: MC

Topic: Produce or Outsource? Firms and Markets

2) When the cost of producing a unit of a good falls as its output rate increases,

- A) economies of scale exist.
- B) economies of scope exist.
- C) transactions costs are zero.
- D) market coordination is unnecessary.
- E) the firm is a partnership.

Answer: A

Diff: 1 Type: MC

Topic: Produce or Outsource? Firms and Markets

3) Which one of the following would *not* likely be a firm with economies of scale?

- A) an electrical production plant
- B) a steel mill
- C) a telephone company
- D) a firm that produces handmade cabinetry
- E) a multi-store dry-cleaning firm

Answer: D

Diff: 2 Type: MC

Topic: Produce or Outsource? Firms and Markets

4) A firm with a sales department, a production department, and a marketing department is an example of

- A) team production.
- B) joint production.
- C) economies of scale.
- D) economies of scope.
- E) transactions costs.

Answer: A

Diff: 1 Type: MC

Topic: Produce or Outsource? Firms and Markets

5) Team production is

- A) a production process with decreasing costs per unit as production increases.
- B) a production process with individuals specializing in mutually supportive tasks.
- C) the production that results from market activity.
- D) the cost of organizing an assembly line.
- E) the lower costs resulting from organizing a firm versus using the market to coordinate production.

Answer: B

Diff: 1 Type: MC

Topic: Produce or Outsource? Firms and Markets

6) Firms coordinate economic activity more efficiently than markets when firms have

- A) lower transactions costs.
- B) economies of scale.
- C) economies of scope.
- D) economies of team production.
- E) all of the above.

Answer: E

Diff: 2 Type: MC

Topic: Produce or Outsource? Firms and Markets

Source: Study Guide

7) Which one of the following statements is *true*?

- A) Firms are markets in and of themselves.
- B) Firms do not organize factors of production to produce goods and services.
- C) Firms are buyers of consumer goods and services.
- D) Efficient firms can eliminate scarcity.
- E) Firms are often more efficient than markets as coordinators of economic activity.

Answer: E

Diff: 1 Type: MC

Topic: Produce or Outsource? Firms and Markets

8) A group of business people are having coffee. Which of the following quotations describes economies of scale?

- A) "The new production process we've installed uses less capital and labour than the old one."
- B) "The new assembly line has higher capital costs, but the fall in workers' hours has lowered overall costs."
- C) "The costs of per-unit production have fallen dramatically as we have increased the length of the production runs."
- D) "Despite the higher costs of negotiating the contracts, hiring the cleaning firm is much cheaper than using our own staff."
- E) "The computer servicing people we have hired work very well as an integrated problem-solving group."

Answer: C

Diff: 2 Type: MC

Topic: Produce or Outsource? Firms and Markets

9) A group of business people are having coffee. Which of the following quotations describes transactions costs?

A) "The new production process we've installed uses less capital and labour than the old one."

B) "The new assembly line has higher capital costs, but the fall in workers' hours has lowered overall costs."

C) "The costs of per-unit production have fallen dramatically as we have increased the length of the production runs."

D) "Despite the higher costs of negotiating the contracts, hiring the cleaning firm is much cheaper than using our own staff."

E) "The computer servicing people we have hired work very well as an integrated problem-solving group."

Answer: D

Diff: 2 Type: MC

Topic: Produce or Outsource? Firms and Markets

10) The major factor determining whether a firm or a market coordinates a particular set of activities is

A) cost.

B) a sale.

C) depreciation.

D) the size of the market.

E) the number of workers.

Answer: A

Diff: 2 Type: MC

Topic: Produce or Outsource? Firms and Markets

11) Which of the following activities is most likely to be coordinated by a firm, instead of a market?

A) a large rock concert in Vancouver

B) producing paperclips

C) running a golf course

D) selling groceries

E) all of the above except A

Answer: E

Diff: 3 Type: MC

Topic: Produce or Outsource? Firms and Markets

12) A firm with a lower unit cost from producing a wider range of goods and services has economies of

A) transactions costs.

B) scale.

C) scope.

D) team production.

E) market coordination.

Answer: C

Diff: 2 Type: MC

Topic: Produce or Outsource? Firms and Markets

Source: Study Guide

Use the information below to answer the following question.

**Fact 10.5.1**

Two leading design firms, Astro Studios of San Francisco and Hers Experimental Design Laboratory, Inc. of Osaka, Japan, worked with Microsoft to design the Xbox 360 video game console. IBM, ATI, and SiS designed the Xbox 360's hardware. Three firms, Flextronics, Wistron, and Celestica, manufacture the Xbox 360 at their plants in China and Taiwan.

- 13) Refer to Fact 10.5.1. Microsoft works with a large number of other firms to bring the Xbox to market, rather than performing all the required tasks at its headquarters in Seattle because
- A) Microsoft wants to control as many firms as possible and by sending Xbox design and production to other firms, Microsoft gains control in a new market.
  - B) this is the method of production with the lowest cost.
  - C) Microsoft employees do not have the expertise to perform the necessary tasks.
  - D) Microsoft already dominates too many markets and the government requires that other firms coordinate Xbox design and production.
  - E) All of the above.

Answer: B

Type: MC

Topic: Produce or Outsource? Firms and Markets

Source: MyEconLab

- 14) All of the following statements are correct *except*
- A) firms coordinate economic activity when they can perform a task more efficiently than markets can.
  - B) Nobel Laureate Ronald Coase stated that firms cannot be more efficient than markets.
  - C) markets can coordinate production.
  - D) firms are often more efficient than markets as coordinators of economic activity because they can achieve lower transactions costs, economies of scale, economies of scope, and economies of team production.
  - E) outsourcing is an example of market coordination.

Answer: A

Type: MC

Topic: Produce or Outsource? Firms and Markets

Source: MyEconLab

- 15) When Jitters Coffee Company, Inc., can lower the cost of packaging a kilogram of coffee by doubling the quantity packaged each day, it is achieving
- A) economies of scope.
  - B) lower transactions costs
  - C) economies of scale.
  - D) efficient team production.
  - E) all of the above

Answer: C

Type: MC

- 16) Team production is a production process in which
- A) an assembly line is used.
  - B) individuals rotate from one task to another.
  - C) competing groups perform identical tasks.
  - D) individuals specialize in mutually supportive tasks.
  - E) pay is based on group output.

Answer: D

Type: MC

## Chapter 11 Output and Costs

### 11.1 Decision Time Frames

- 1) The short run is a time frame in which
- A) the firm is not able to hire more workers.
  - B) the amount of output produced is fixed.
  - C) there is a shortage of most factors of production.
  - D) at least one factor of production is fixed.
  - E) there is not enough time to make all of the decisions necessary to maximize profit.

Answer: D

Diff: 1 Type: MC

Topic: Decision Time Frames

- 2) The long run is a time frame in which
- A) the firm can hire all the workers it wants to employ, but it does not have sufficient time to buy more equipment.
  - B) the firm is able to maximize revenue.
  - C) the firm may want to build a bigger plant, but cannot do so.
  - D) economic efficiency is achieved.
  - E) the quantities of all factors of production can be varied.

Answer: E

Diff: 1 Type: MC

Topic: Decision Time Frames

- 3) Plant refers to those factors of production
- A) that are too expensive for the firm to purchase.
  - B) that must be held in storage for at least one year.
  - C) that are fixed in the short run.
  - D) that have a decreasing marginal product as more of the factor is used.
  - E) which can be purchased only in fixed quantity lots.

Answer: C

Diff: 1 Type: MC

Topic: Decision Time Frames

- 4) The short run refers to a time period

- A) of one year or less.
- B) in which all factors of production are variable.
- C) in which all factors of production are fixed.
- D) in which some factors of production are variable, but at least one factor of production is.
- E) in which all factors of production are variable, but the technology is fixed.

Answer: D

Diff: 1 Type: MC

Topic: Decision Time Frames

Source: Study Guide

- 5) The long run refers to a time period
- A) of one year or less.
  - B) in which all factors of production are variable.
  - C) in which labour is variable, but plant is fixed.
  - D) when there is at least one variable factor of production.
  - E) of at least 5 years.

Answer: B

Diff: 1 Type: MC

Topic: Decision Time Frames

- 6) Choose the correct statement.
- A) The long run is a period of time in which the quantity of at least one input is fixed.
  - B) The short run is a period of time in which the firm has sufficient time to change all its inputs.
  - C) The long run is a time frame that lasts for 10 years.
  - D) In the short run, the firm's plant is fixed.
  - E) A firm always has plenty of time to make decisions about changing its inputs no matter if it is in a short run or long run position.

Answer: D

Diff: 1 Type: MC

Topic: Decision Time Frames

*Use the information below to answer the following questions.*

### **Fact 11.1.1**

**January 31, 2008:** Starbucks will open 75 more stores abroad than originally predicted, for a total of 975.

**February 25, 2008:** For three hours on Tuesday, Starbucks will shut down every single one of its 7,100 stores so that baristas can receive a refresher course.

**June 2, 2008:** Starbucks replaces baristas with vending machines.

**July 18, 2008:** Starbucks is closing 616 stores by the end of March.

- 7) Refer to Fact 11.1.1. The decisions made on \_\_\_\_\_ are short-run decisions because they \_\_\_\_\_.

- A) January 31 and July 18; change the number of stores but not necessarily the number of employees
- B) February 25 and June 2; change a variable factor of production but not a fixed factor of production
- C) February 25, June 2, and July 18; deal with stores located in the United States
- D) June 2 and July 18; are the more recent decisions
- E) None of the above.

Answer: B

Diff: 1 Type: MC

Topic: Decision Time Frames

Source: MyEconLab

8) Refer to Fact 11.1.1. The decisions made on \_\_\_\_\_ are long-run decisions because they \_\_\_\_\_.

- A) June 2; are changes to labour which affect people for the long term
- B) January 31 and July 18; change Starbucks' plant
- C) February 25, June 2, and July 18; all deal with stores located in the United States
- D) January 31 and February 25; are the earliest decisions
- E) None of the above.

Answer: B

Diff: 1 Type: MC

Topic: Decision Time Frames

Source: MyEconLab

9) When the demand for electricity peaks during the hottest days of summer, Hydro One can generate more electricity by using more fuel and increasing the working hours of many of its employees. The company cannot, however, increase electric power production by building additional generating capacity. This means that the company is operating in the

- A) market run.
- B) intermediate run.
- C) long run.
- D) immediate run.
- E) short run.

Answer: E

Type: MC

10) Choose the correct statement.

- A) Expenditure on a plant that has no resale value is a sunk cost.
- B) A sunk cost is irrelevant to a firm's current decisions.
- C) A cost that influences a firm's current decisions is the short-run cost of changing its labour inputs.
- D) A cost that influences a firm's current decisions is the long-run cost of changing its plant.
- E) All of the above.

Answer: E

Type: MC

## 11.2 Short-Run Technology Constraint

- 1) A firm's total product curve describes
- A) the minimum cost of producing a given amount of output.
  - B) the maximum output that a given quantity of labour can produce.
  - C) how the maximum attainable output varies as the size of the firm's plant varies, given the quantity of labour employed.
  - D) how the management of the firm makes decisions over the short run.
  - E) how the amount of labour varies as the amount of output varies.

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

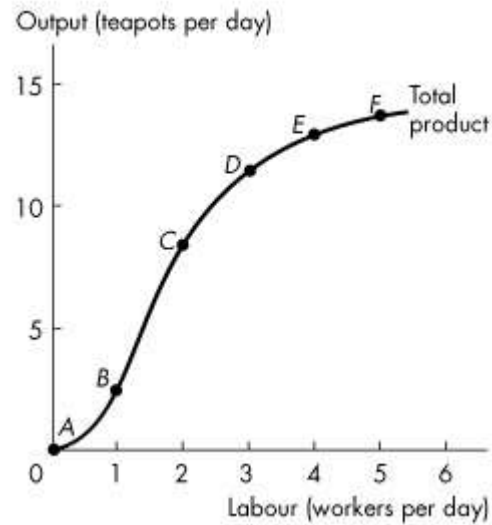
- 2) The total product curve is a graph that shows the
- A) minimum cost of producing a given amount of output using a given technology.
  - B) maximum profit from each unit of output sold.
  - C) maximum output that a given quantity of labour can produce.
  - D) maximum output that can be produced as technology advances.
  - E) change in total product for a given change in marginal product.

Answer: C

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

Use the figure below to answer the following questions.



**Figure 11.2.1**

3) Refer to Figure 11.2.1 which illustrates Tania's total product curve. Which one of the following statements is *false*?

- A) All the points above the curve are unattainable.
- B) All the points below the curve are attainable.
- C) All the points below the curve are inefficient.
- D) The cost of producing at point *B* equals the cost of producing at point *C*.
- E) All the points on the curve are attainable.

Answer: D

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

4) Refer to Figure 11.2.1 which illustrates Tania's total product curve. Which one of the following statements is *true*?

- A) The points above the curve are attainable and inefficient.
- B) The points below the curve are attainable and inefficient.
- C) The points below the curve are inefficient and unattainable.
- D) The points on the curve are efficient and unattainable.
- E) Marginal product is equal at every point on the total product curve.

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

Source: Study Guide

5) Refer to Figure 11.2.1 which illustrates Tania's total product curve. Average product of labour reaches its maximum for the \_\_\_\_\_ worker.

- A) first
- B) second
- C) third
- D) fourth
- E) fifth

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

6) Refer to Figure 11.2.1 which illustrates Tania's total product curve. Marginal product of labour reaches its maximum when the number of workers increases from

- A) zero to 1.
- B) 1 to 2.
- C) 2 to 3.
- D) 3 to 4.
- E) 4 to 5.

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

7) Marginal product of labour is the increase in total product that results from a

- A) one-unit increase in the quantity of labour employed, other inputs remaining the same.
- B) one-unit increase in the quantity of fixed inputs employed, holding the quantity of the variable inputs constant.
- C) one-unit increase in both the quantity of variable and fixed inputs.
- D) change in the cost of labour.
- E) 1 percent change in the quantity of labour and the quantity of capital employed.

Answer: A

Diff: 1 Type: MC

Topic: Short-Run Technology Constraint

Refer to the table below to answer the following questions.

**Table 11.2.1**

Labour (workers per day)	Output (teapots per day)
0	0
1	3
2	12
3	19
4	23
5	25

8) Refer to Table 11.2.1 which gives Tania's total product schedule. The marginal product when the firm increases the number of workers from 3 to 4 per day is

- A) 6 teapots.
- B) 2 teapots.
- C) 9 teapots.
- D) 7 teapots.
- E) 4 teapots.

Answer: E

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

9) Refer to Table 11.2.1 which gives Tania's total product schedule. The marginal product when the number of workers increases from 1 to 2 is

- A) 3 teapots.
- B) 12 teapots.
- C) 7 teapots.
- D) 9 teapots.
- E) 6 teapots.

Answer: D

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

10) Refer to Table 11.2.1 which gives Tania's total product schedule. The average product when the firm hires two workers is

- A) 3 teapots per worker.
- B) 6 teapots per worker.
- C) 7 teapots per worker.
- D) 9 teapots per worker.
- E) 12 teapots per worker.

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

11) Refer to Table 11.2.1 which gives Tania's total product schedule. Average product of labour reaches its maximum for the \_\_\_\_\_ worker.

- A) first
- B) second
- C) third
- D) fourth
- E) fifth

Answer: C

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

12) Refer to Table 11.2.1 which gives Tania's total product schedule. Marginal product of labour reaches its maximum when the number of workers increases from

- A) 0 to 1.
- B) 1 to 2.
- C) 2 to 3.
- D) 3 to 4.
- E) 4 to 5

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

*Use the table below to answer the following questions.*

**Table 11.2.2**

Labour (workers per day)	Output (teapots per day)
0	0
1	2
2	8
3	12
4	15
5	16

13) Refer to Table 11.2.2 which gives Tania's total product schedule. The average product when the firm employs four workers is

- A) 2 teapots per worker.
- B) 8 teapots per worker.
- C) 12 teapots per worker.
- D) 15 teapots per worker.
- E) 3.75 teapots per worker.

Answer: E

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

14) Refer to Table 11.2.2 which gives Tania's total product schedule. The marginal product when the number of workers increases from 2 to 3 is

- A) 1 teapot.
- B) 2 teapots.
- C) 3 teapots.
- D) 4 teapots.
- E) 3.75 teapots.

Answer: D

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

15) Refer to Table 11.2.2 which gives Tania's total product schedule. The average product when the firm hires three workers is

- A) 1 teapot per worker.
- B) 2 teapots per worker.
- C) 3 teapots per worker.
- D) 4 teapots per worker.
- E) 12 teapots per worker.

Answer: D

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

16) Suppose a 1-unit increase in labour, from 2 to 3 workers, increases output from 10 to 15 tea cups. The marginal product from the increase in the quantity of labour is

- A) 1 tea cup.
- B) 3 tea cups.
- C) 4 tea cups.
- D) 5 tea cups.
- E) 15 tea cups.

Answer: D

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

17) Suppose a firm increases the quantity of labour employed from 5 to 6 workers, and as a result, the firm's total output increases from 100 units to 400 units. The marginal product of the sixth worker is

- A) 50 units.
- B) 100 units.
- C) 200 units.
- D) 300 units.
- E) 66.67 units.

Answer: D

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

18) Marginal product

- A) is always negative.
- B) is the slope of the total product curve.
- C) is always zero.
- D) lies between zero and one.
- E) equals average product minus total product.

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

19) If the total product of three workers is 214 and the total product of four workers is 221, then the marginal product of the fourth worker is

- A) 71.3.
- B) 55.25.
- C) 7.
- D) 62.14.
- E) 1.75.

Answer: C

Diff: 1 Type: MC

Topic: Short-Run Technology Constraint

20) If the total product of four workers is 156, calculate the average product of each worker.

- A) 39
- B) 19.5
- C) 78
- D) 152
- E) 624

Answer: A

Diff: 1 Type: MC

Topic: Short-Run Technology Constraint

21) The steeper the slope of the total product curve,

- A) the smaller the average product.
- B) the smaller the marginal product.
- C) the greater the total cost.
- D) the more efficient the technology employed.
- E) the greater the marginal product.

Answer: E

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

Use the figure below to answer the following question.

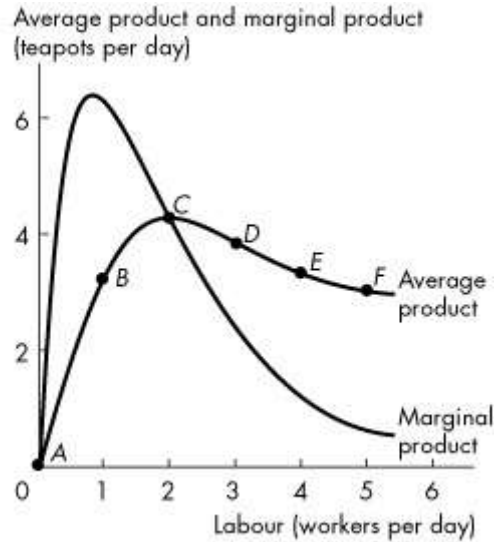


Figure 11.2.2

22) Refer to Figure 11.2.2 which shows Tania's average product curve and marginal product curve. The point of maximum average product is point

- A) B.
- B) C.
- C) D.
- D) E.
- E) F.

Answer: B

Diff: 1 Type: MC

Topic: Short-Run Technology Constraint

23) Which one of the following statements is *true*?

- A) The highest value of average product occurs where average product is greater than marginal product.
- B) When the average product curve is rising, marginal product is less than average product.
- C) When the average product curve is falling, marginal product is greater than average product.
- D) The maximum total product occurs at minimum marginal product.
- E) The highest value of average product occurs where average product equals marginal product.

Answer: E

Diff: 3 Type: MC

Topic: Short-Run Technology Constraint

24) Diminishing marginal returns refers to a situation where the \_\_\_\_\_ of an additional worker is less than the \_\_\_\_\_ of the previous worker.

- A) marginal cost; marginal cost
- B) average cost; average cost
- C) marginal product; marginal product
- D) average product; average product
- E) marginal product; average product

Answer: C

Diff: 1 Type: MC

Topic: Short-Run Technology Constraint

25) The law of diminishing marginal returns states:

- A) As the size of a plant increases, marginal product eventually decreases.
- B) As the size of a firm's plant increases, average cost eventually decreases.
- C) As a firm uses more of a variable factor of production, with a given quantity of the fixed factor of production, the marginal product of the variable factor eventually diminishes.
- D) As a firm uses more of a variable factor of production, its average cost eventually decreases.
- E) As a firm uses more of a variable factor of production, total product eventually decreases.

Answer: C

Diff: 1 Type: MC

Topic: Short-Run Technology Constraint

26) The law of diminishing marginal returns refers to the tendency for \_\_\_\_\_ to eventually decrease as more labour is employed, everything else remaining the same.

- A) average total cost
- B) marginal cost
- C) total product
- D) marginal product of labour
- E) average product of labour

Answer: D

Diff: 1 Type: MC

Topic: Short-Run Technology Constraint

27) When the marginal product of labour is less than the average product of labour,

- A) the average product of labour is increasing.
- B) the marginal product of labour is increasing.
- C) the total product curve is negatively sloped.
- D) the firm is experiencing diminishing marginal returns.
- E) None of the above.

Answer: D

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

Source: Study Guide

28) When the 7th worker is hired, output increases from 100 units per week to 110 units per week. When the 8th worker is hired, output increases from 110 units to 118 units. This is an example of

- A) diminishing marginal returns.
- B) diminishing marginal cost.
- C) decreasing returns to scale.
- D) labour-intensive production.
- E) increasing returns to scale.

Answer: A

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

29) When Coffee 'n' Cream in Victoria, British Columbia hires two students, 64 customers can be served in one hour. Suppose the manager of the restaurant observes that after hiring the third student, 80 customers are being served in one hour. The marginal product of the third student is \_\_\_\_\_ customers per hour.

- A) 4
- B) 16
- C) 8
- D) 26.67
- E) 32

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

30) When the marginal product of labour is greater than the average product of labour,

- A) the average product of labour is increasing.
- B) the marginal product of labour is increasing.
- C) the total product curve is negatively sloped.
- D) the firm is experiencing diminishing marginal returns.
- E) the firm is experiencing constant returns.

Answer: A

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

Use the table below to answer the following questions.

**Table 11.2.3**

Labour (workers per week)	Output (rubbers boats per week)	Marginal Product (rubber boats per worker)	Average Product (rubber boats per worker)
0	0		
1	1	1	1
2	2	1	1
3	4	2	1
4	7	<i>A</i>	<i>C</i>
5	11	4	<i>C</i>
6	14	<i>B</i>	2.2
7	16	2	<i>E</i>
8	17	1	2.28
9	18	1	2.13
10	18	0	2
			1.8

31) Refer to Table 11.2.3. The value of *A* is

A) 1.75.

B) 2.

C) 3.

D) 7.

E) 4.

Answer: C

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

32) Refer to Table 11.2.3. The maximum value of marginal product occurs where output equals \_\_\_\_\_, while the maximum value of average product occurs where output equals \_\_\_\_\_.

- A) 5; 6
- B) 6; 5
- C) 7; 14
- D) 9; 14
- E) 14; 11

Answer: D

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

Use the table below to answer the following question.

**Table 11.2.4**

Number of Workers	Total Product (baskets of corn)
1	0
2	3
3	7
4	10
5	12

33) Refer to Table 11.2.4. The table gives the total product schedule of workers who harvest corn. Diminishing marginal returns begin when the \_\_\_\_\_ is hired.

- A) 1st labourer
- B) 2nd labourer
- C) 3rd labourer
- D) 4th labourer
- E) There are no diminishing marginal returns since total product always rises.

Answer: D

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

34) Which of the following quotes *best* illustrates the idea of marginal product?

- A) "If I have 10 workers on my assembly line, I can produce 13 tables a day."
- B) "If I add an 11th worker, I can produce 1 extra table a day."
- C) "Each worker produces 2 tables a day."
- D) "I find if I add an extra shift at night, table production only rises by 80 percent because I need more maintenance time on the assembly line."
- E) "If I double workers and double the assembly line, I can make 120 percent more tables."

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

35) If the marginal product of the fifth worker is 34, then the total product of five workers

- A) is 35.
- B) is 24.
- C) is 170.
- D) is 6.8.
- E) cannot be calculated with the information given.

Answer: E

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

36) If capital is a variable input in a production process, the law of diminishing marginal returns implies that

- A) total product is minimized.
- B) capital's marginal product is positive and less than one.
- C) total product is maximized.
- D) marginal product of capital eventually decreases.
- E) marginal product of capital is constant.

Answer: D

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

37) If energy (E) is the only input used to produce output (Q), what is the formula for average product of energy?

- A)  $\Delta Q/\Delta E$
- B)  $Q/E$
- C)  $\Delta E/\Delta Q$
- D)  $E/Q$
- E)  $Q \cdot E$

Answer: B

Diff: 1 Type: MC

Topic: Short-Run Technology Constraint

38) If energy (E) is the only input used to produce output (Q), what is the formula for marginal product of energy?

- A)  $Q \cdot E$
- B)  $Q/E$
- C)  $\Delta Q/\Delta E$
- D)  $\Delta E/\Delta Q$
- E)  $E/Q$

Answer: C

Diff: 1 Type: MC

Topic: Short-Run Technology Constraint

39) Suppose the marginal product of energy equals the average product of energy. This implies that

- A) marginal product is negative.
- B) average product is at its maximum value.
- C) marginal product is at its maximum value.
- D) the marginal product curve is upward sloping.
- E) average product is at its minimum value.

Answer: B

Diff: 1 Type: MC

Topic: Short-Run Technology Constraint

40) Which one of the following statements is correct?

- A) When marginal product is increasing, average product is decreasing.
- B) When average product is less than zero, marginal product is positive.
- C) When marginal product is increasing and greater than average product, average product is increasing.
- D) When marginal product is zero, total product is at its minimum.
- E) When average product exceeds marginal product, marginal product is increasing.

Answer: C

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

41) Which of the following quotes *best* illustrates the idea of average product?

- A) "If I have 10 workers on my assembly line, I can produce 13 tables a day."
- B) "If I add an 11th worker, I can produce 1 extra table a day."
- C) "Each worker produces 2 tables a day."
- D) "I find if I add an extra shift at night, table production only rises by 80 percent because I need more maintenance time on the assembly line."
- E) "If I double workers and double the assembly line, I can make 120 percent more tables."

Answer: C

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

42) Which of the following quotes *best* illustrates the idea of total product?

- A) "If I have 10 workers on my assembly line, I can produce 13 tables a day."
- B) "If I add an 11th worker, I can produce 1 extra table a day."
- C) "Each worker produces 2 tables a day."
- D) "I find if I add an extra shift at night, table production only rises by 80 percent because I need more maintenance time on the assembly line."
- E) "If I double workers and double the assembly line, I can make 120 percent more tables."

Answer: A

Diff: 2 Type: MC

Topic: Short-Run Technology Constraint

43) The average product of labour equals

- A) the slope of the total product curve.
- B) the slope of the marginal product curve.
- C) the increase in total product divided by the increase in labour employed.
- D) total product divided by the quantity of labour employed.
- E) the difference between the total product and the marginal product of labour.

Answer: D

Diff: 1 Type: MC

Topic: Short-Run Technology Constraint

Source: Study Guide

44) The average product of energy equals

- A) the increase in total product divided by the increase in energy used.
- B) total product divided by the quantity of energy used.
- C) the slope of the total product curve.
- D) the slope of the marginal product curve.
- E) the difference between the total product and the marginal product of energy.

Answer: B

Diff: 1 Type: MC

Topic: Short-Run Technology Constraint

45) Which of the following statements by a restaurant owner refers to the law of diminishing marginal returns?

- A) "The higher the quality of the ingredients we use, the higher the cost of producing each meal."
- B) "If we double the size of our premises and double everything else — kitchen staff, serving staff, equipment — we can increase the number of meals we serve, but not to double the current levels."
- C) "We can increase the number of meals we serve by just adding more kitchen staff, but each additional worker adds less meals than the previous worker because traffic in the kitchen will get worse."
- D) "We can serve the same number of meals with fewer kitchen staff, but we would have to buy more labour-saving kitchen equipment."
- E) "We can serve the same number of meals with less kitchen equipment, but we would have to hire more kitchen staff."

Answer: C

Diff: 3 Type: MC

Topic: Short-Run Technology Constraint

Source: Study Guide

46) Choose the correct statement.

- A) When marginal product of labour is greater than average product of labour and marginal product is either increasing or decreasing average product of labour is increasing.
- B) When total product is increasing average product of labour and marginal product of labour are both increasing.
- C) When marginal product of labour is greater than or equal to average product of labour, average product of labour is increasing.
- D) When marginal product of labour is increasing, average product of labour is greater than marginal product of labour.
- E) When total product is increasing, average product of labour is decreasing and marginal product of labour is increasing.

Answer: A

Diff: 3 Type: MC

Topic: Short-Run Technology Constraint

Source: MyEconLab

47) The marginal product of labour initially \_\_\_\_\_ and eventually \_\_\_\_\_. The average product of labour initially \_\_\_\_\_ and eventually \_\_\_\_\_.

- A) increases; decreases; increases; decreases
- B) decreases; increases; decreases; increases
- C) increases; decreases; decreases; increases
- D) decreases; increases; increases; decreases
- E) increases; is constant; increases; decreases

Answer: A

Diff: 3 Type: MC

Topic: Short-Run Technology Constraint

Source: MyEconLab

48) The total output produced with any quantity of labour is equal to the sum of the

- A) average products of each of the workers hired.
- B) marginal costs of each of the workers hired.
- C) marginal products of each of the workers hired.
- D) average costs of each of the workers hired.
- E) fixed products of each of the workers hired.

Answer: C

Type: MC

49) The average product of labour is

- A) the inverse of the average product of capital.
- B) the slope of the marginal product of labour curve.
- C) the slope of the total product curve.
- D) greater than the average product of labour.
- E) calculated as total product divided by the total quantity of labour employed.

Answer: E

Type: MC

- 50) At that amount of output where diminishing marginal returns first sets in,
- A) average product begins to decrease.
  - B) total product begins to decrease.
  - C) marginal cost begins to decrease.
  - D) marginal product begins to decrease.
  - E) All of the above.

Answer: D

Type: MC

### 11.3 Short-Run Cost

1) Which of the following are correct? According to the law of diminishing returns,

- (1) marginal product eventually rises.
- (2) marginal product eventually falls.
- (3) marginal cost eventually rises.
- (4) marginal cost eventually falls.

- A) (1) and (3)
- B) (1) and (4)
- C) (2) and (3)
- D) (2) and (4)
- E) (4)

Answer: C

Diff: 2 Type: MC

Topic: Short-Run Cost

Source: Study Guide

*Use the table below to answer the following questions.*

**Table 11.3.1**

Labour (workers per day)	Output (teapots per day)	TFC (dollars per day)	TVC (dollars per day)	TC (dollars per day)
0	0	20	0	20
1	4	20	--	45
2	9	20	--	70
3	13	20	--	95
4	16	20	100	--
5	18	20	125	145

2) Refer to Table 11.3.1, which gives Tania's total cost schedule. The average fixed cost of producing 9 teapots per day is

- A) \$2.22.
- B) \$1.25.
- C) \$10.00.
- D) \$1.11.
- E) \$1.54.

Answer: A

Diff: 2 Type: MC

Topic: Short-Run Cost

3) Refer to Table 11.3.1, which gives Tania's total cost schedule. The average total cost of producing 16 teapots per day is

- A) \$2.
- B) \$5.
- C) \$3.33.
- D) \$7.50.
- E) \$5.51.

Answer: D

Diff: 2 Type: MC

Topic: Short-Run Cost

4) Refer to Table 11.3.1, which gives Tania's total cost schedule. When output increases from 4 to 9 teapots, the marginal cost of one of the 5 teapots is

- A) \$4.25.
- B) \$4.
- C) \$25.
- D) \$6.25.
- E) \$5.

Answer: E

Diff: 2 Type: MC

Topic: Short-Run Cost

*Use the table below to answer the following questions.*

**Table 11.3.2**

Labour (workers per day)	Output (teapots per day)	TFC (dollars per day)	TVC (dollars per day)	TC (dollars per day)
0	0	30	0	30
1	3	30	20	--
2	8	30	40	--
3	12	30	60	--
4	14	30	--	110
5	15	30	--	130

5) Refer to Table 11.3.2, which gives Tania's total cost schedule. The average total cost of producing 14 teapots is

- A) \$7.86.
- B) \$6.75.
- C) \$7.
- D) \$1.75.
- E) \$27.50.

Answer: A

Diff: 2 Type: MC

Topic: Short-Run Cost

6) Refer to Table 11.3.2, which gives Tania's total cost schedule. When output increases from 8 to 12 teapots, the marginal cost of one of the 4 teapots is

- A) \$20.
- B) \$5.
- C) \$1.
- D) \$6.67.
- E) \$2.

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Cost

7) If an increase in output from 5 to 10 teapots increases total cost from \$100 to \$200, the marginal cost of one of those 5 teapots is

- A) \$10.
- B) \$20.
- C) \$22.
- D) \$25.
- E) dependent upon the amount of extra labour used.

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Cost

8) Marginal cost is equal to

- A) total cost divided by output.
- B) the increase in total cost divided by the increase in output.
- C) the increase in total cost divided by the increase in labour input, given the amount of capital.
- D) total variable cost minus total fixed cost.
- E) the increase in total cost divided by the increase in variable cost.

Answer: B

Diff: 1 Type: MC

Topic: Short-Run Cost

9) Choose the correct equation.

- A)  $TFC = TC/Q$
- B)  $TFC = TC - AVC$
- C)  $TFC = TC - TVC$
- D)  $TFC = TVC/Q$
- E)  $TFC = TVC - TC$

Answer: C

Diff: 1 Type: MC

Topic: Short-Run Cost

10) Which one of the following statements is *false*?

- A) Average total cost is total cost per unit of output.
- B) Average fixed cost plus average variable cost equals average total cost.
- C) Marginal cost is the increase in total cost resulting from a one-unit increase in output.
- D) Total cost equals fixed cost plus average cost.
- E) Marginal cost depends on the amount of labour hired.

Answer: D

Diff: 2 Type: MC

Topic: Short-Run Cost

11) Which one of the following statements is *false*?

- A) Total variable cost plus total fixed cost equals total cost.
- B) Marginal cost equals the change in total cost divided by the change in output.
- C) Average total cost is calculated by dividing total cost by the level of output.
- D) The average cost curve is U-shaped.
- E) The total cost curve is U-shaped.

Answer: E

Diff: 2 Type: MC

Topic: Short-Run Cost

12) Which one of the following statements is *false*?

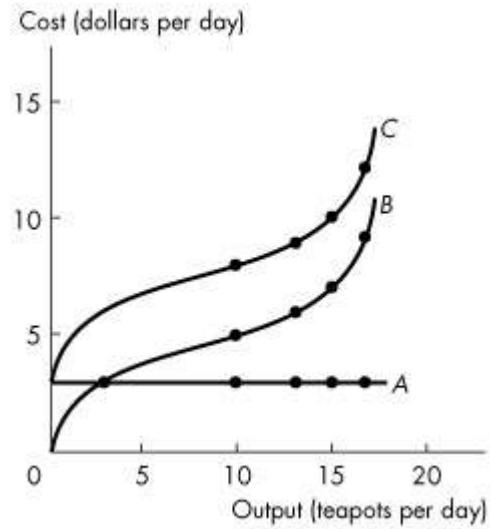
- A) The average total cost curve and average variable cost curve are U-shaped.
- B) The gap between the average total cost curve and the average variable cost curve equals marginal cost.
- C) The gap between the average total cost curve and the average variable cost curve narrows as output increases.
- D) The marginal cost curve intersects the average variable cost curve at minimum average variable cost.
- E) The marginal cost curve intersects the average total cost curve at minimum average total cost.

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Cost

Use the figure below to answer the following question.



**Figure 11.3.1**

13) Refer to Figure 11.3.1. Which one of the following statements is *false*?

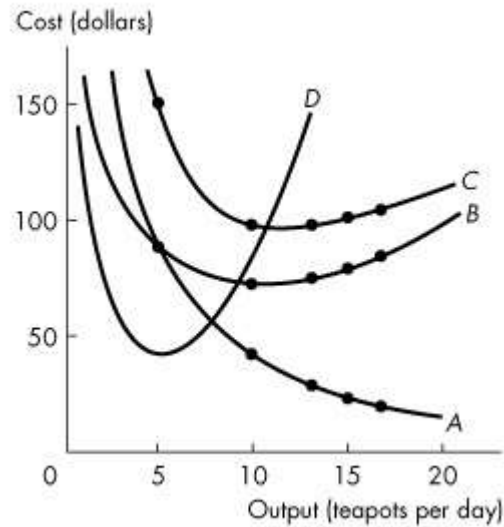
- A) The total fixed cost curve A.
- B) Total variable cost and total cost both increase with output.
- C) The vertical gap between curves B and C is equal to total variable cost.
- D) Marginal cost is equal to the slope of curve C.
- E) Total fixed cost is constant.

Answer: C

Diff: 2 Type: MC

Topic: Short-Run Cost

Use the figure below to answer the following questions.



**Figure 11.3.2**

14) Refer to Figure 11.3.2, which illustrates short-run average and marginal cost curves. Which one of the following statements is *false*?

- A) Average fixed cost decreases with output.
- B) The vertical gap between curves *B* and *C* is equal to average variable cost.
- C) Line *B* comes closer to line *C* as output increases because of a decrease in average fixed cost.
- D) Curve *D* is the marginal cost curve.
- E) The vertical gap between curves *B* and *C* is equal to average fixed cost.

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Cost

15) Refer to Figure 11.3.2, which illustrates the short-run average and marginal cost curves. The average variable cost curve is curve

- A) *A*.
- B) *B*.
- C) *C*.
- D) *D*.
- E) none of the above.

Answer: B

Diff: 1 Type: MC

Topic: Short-Run Cost

16) Refer to Figure 11.3.2, which illustrates the short-run average and marginal cost curves. The marginal cost curve is curve

- A) A.
- B) B.
- C) C.
- D) D.
- E) none of the above.

Answer: D

Diff: 1 Type: MC

Topic: Short-Run Cost

17) Which one of the following is *false*?

- A) The marginal cost curve intersects the average variable cost curve and the average total cost curve at their maximum points.
- B) When marginal cost is greater than average variable cost, average variable cost is increasing.
- C) When marginal cost is greater than average total cost, average total cost is increasing.
- D) The average total cost curve is U-shaped.
- E) The average fixed cost curve is downward sloping.

Answer: A

Diff: 2 Type: MC

Topic: Short-Run Cost

18) As soon as diminishing returns set in, a firm's

- A) marginal product increases.
- B) average fixed cost decreases.
- C) marginal cost decreases.
- D) marginal cost increases.
- E) total cost decreases.

Answer: D

Diff: 2 Type: MC

Topic: Short-Run Cost

19) Average variable cost is at a minimum at the same output at which

- A) average product is at a maximum.
- B) average product is at a minimum.
- C) marginal product is at a maximum.
- D) marginal product is at a minimum.
- E) marginal cost is at a minimum.

Answer: A

Diff: 2 Type: MC

Topic: Short-Run Cost

Source: Study Guide

- 20) The range over which average variable cost is decreasing is the same as the range over which
- A) marginal cost is increasing.
  - B) average fixed cost is decreasing.
  - C) marginal product is decreasing.
  - D) average product is decreasing.
  - E) average product is increasing.

Answer: E

Diff: 2 Type: MC

Topic: Short-Run Cost

- 21) The vertical distance between the  $TC$  and  $TVC$  curves

- A) decreases as output increases.
- B) increases as output increases.
- C) is equal to  $AFC$ .
- D) is equal to  $TFC$ .
- E) is equal to  $MC$ .

Answer: D

Diff: 2 Type: MC

Topic: Short-Run Cost

Source: Study Guide

- 22) The marginal cost ( $MC$ ) curve intersects the

- A)  $ATC$ ,  $AVC$ , and  $AFC$  curves at their minimum points.
- B)  $ATC$  and  $AFC$  curves at their minimum points.
- C)  $AVC$  and  $AFC$  curves at their minimum points.
- D)  $ATC$  and  $AVC$  curves at their minimum points.
- E)  $TC$  and  $TVC$  curves at their minimum points.

Answer: D

Diff: 2 Type: MC

Topic: Short-Run Cost

Source: Study Guide

- 23) If the average variable cost of producing 10 units is \$18 and the average variable cost of producing 11 units is \$20, we know that, between 10 and 11 units of output,

- A) marginal cost is increasing.
- B) average total cost is increasing.
- C) average fixed cost is increasing.
- D) total cost is either increasing or decreasing.
- E) none of the above.

Answer: A

Diff: 3 Type: MC

Topic: Short-Run Cost

- 24) Marginal cost is the amount that
- A) total cost increases when one more labourer is hired.
  - B) fixed cost increases when one more labourer is hired.
  - C) variable cost increases when one more labourer is hired.
  - D) total cost increases when one more unit of output is produced.
  - E) fixed cost increases when one more unit of output is produced.

Answer: D

Diff: 1 Type: MC

Topic: Short-Run Cost

Source: Study Guide

- 25) Marginal cost equals

- A)  $Q/TVC$ .
- B)  $\Delta TFC/\Delta TC$ .
- C)  $\Delta TC/\Delta Q$ .
- D)  $\Delta Q/\Delta TVC$ .
- E)  $(TC-TVC)/Q$ .

Answer: C

Diff: 1 Type: MC

Topic: Short-Run Cost

- 26) Marginal cost equals

- A)  $TC/Q$ .
- B)  $Q/TVC$ .
- C)  $(TC-TVC)/Q$ .
- D)  $TC/\Delta Q$ .
- E)  $\Delta TC/\Delta Q$ .

Answer: E

Diff: 1 Type: MC

Topic: Short-Run Cost

- 27) Given an upward-sloping, straight line total variable cost curve, what does the marginal cost curve look like?

- A) an upward-sloping straight line
- B) a downward-sloping straight line
- C) a U-shaped curve
- D) a horizontal line
- E) a vertical line

Answer: D

Diff: 1 Type: MC

Topic: Short-Run Cost

28) A rise in the price of a fixed input shifts a firm's

- A) average variable cost curve upward.
- B) average total cost curve upward.
- C) average total cost curve downward.
- D) marginal cost curve upward.
- E) marginal cost curve downward.

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Cost

Source: Study Guide

29) Total cost is \$20 at 4 units of output and \$36 at 6 units of output. Between 4 and 6 units of output, marginal cost

- A) is less than average total cost.
- B) is equal to average total cost.
- C) is equal to average variable cost.
- D) is greater than average total cost.
- E) equals average fixed cost.

Answer: D

Diff: 3 Type: MC

Topic: Short-Run Cost

Source: Study Guide

30) A firm's total fixed cost is \$100. If total cost is \$200 for one unit of output and \$310 for two units, what is the marginal cost of the second unit?

- A) \$100
- B) \$110
- C) \$200
- D) \$210
- E) \$310

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Cost

Source: Study Guide

31) If *ATC* is falling, then *MC* must be

- A) rising.
- B) falling.
- C) equal to *ATC*.
- D) above *ATC*.
- E) below *ATC*.

Answer: E

Diff: 2 Type: MC

Topic: Short-Run Cost

Source: Study Guide

32) If  $ATC$  is rising then  $MC$  must be

- A) rising.
- B) falling.
- C) equal to  $ATC$ .
- D) above  $ATC$ .
- E) both A and D.

Answer: E

Diff: 2 Type: MC

Topic: Short-Run Cost

33) If  $AFC$  is falling then  $MC$  must be

- A) rising.
- B) falling.
- C) above  $AFC$ .
- D) below  $AFC$ .
- E) none of the above.

Answer: E

Diff: 2 Type: MC

Topic: Short-Run Cost

34) If  $MC$  is rising then  $ATC$  must be

- A) rising.
- B) falling.
- C) above  $MC$ .
- D) below  $MC$ .
- E) none of the above.

Answer: E

Diff: 3 Type: MC

Topic: Short-Run Cost

35) Which of the following quotes *best* illustrates the idea of fixed cost?

- A) "As we increase output, per-unit costs fall."
- B) "My primary source of overhead cost is the cost of running the head office."
- C) "If I need to, I can negotiate more overtime with my work force to meet unexpected orders."
- D) "If I double the number of workers and trucks, I get only 80 percent more packages delivered."
- E) None of the above.

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Cost

36) The *ATC* curve shifts upward if

- A) factor prices rise.
- B) a new technology is introduced.
- C) more workers are hired.
- D) all of the above.
- E) none of the above.

Answer: A

Diff: 2 Type: MC

Topic: Short-Run Cost

37) The *MC* curve shifts upward if

- A) factor prices rise.
- B) a new technology is introduced.
- C) more workers are hired.
- D) all of the above.
- E) none of the above.

Answer: A

Diff: 2 Type: MC

Topic: Short-Run Cost

38) The *AFC* curve shifts upward if

- A) factor prices rise.
- B) a new technology is introduced.
- C) more workers are hired.
- D) all of the above.
- E) none of the above.

Answer: E

Diff: 2 Type: MC

Topic: Short-Run Cost

39) The marginal cost curve slopes upward due to

- A) diminishing marginal utility.
- B) diminishing marginal returns.
- C) technological inefficiency.
- D) economic inefficiency.
- E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Cost

40) The average fixed cost curve slopes downward due to

- A) diminishing marginal utility.
- B) diminishing marginal returns.
- C) technological inefficiency.
- D) economic inefficiency.
- E) none of the above.

Answer: E

Diff: 2 Type: MC

Topic: Short-Run Cost

41) The average variable cost curve will shift upward if

- A) there is an increase in fixed cost.
- B) there is a technological advance.
- C) the price of the variable input decreases.
- D) the price of the variable input increases.
- E) the price of output increases.

Answer: D

Diff: 2 Type: MC

Topic: Short-Run Cost

Source: Study Guide

42) A technological advance will shift

- (1) TP, AP, and MP curves up.
  - (2) TP, AP, and MP down.
  - (3) TC, ATC, and MC curves up.
  - (4) TC, ATC, and MC curves down.
- A) (1) and (3)
  - B) (1) and (4)
  - C) (2) and (3)
  - D) (2) and (4)
  - E) none of the above

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Cost

Source: Study Guide

43) An increase in the cost of labour shifts the

A) total, average, and marginal product curves upward and total, average, and marginal cost curves upward.

B) total, average, and marginal product curves upward and total, average, and marginal cost curves downward.

C) total, average, and marginal product curves downward and total, average, and marginal cost curves upward.

D) total, average, and marginal product curves downward and total, average, and marginal cost curves downward.

E) none of the above.

Answer: E

Diff: 2 Type: MC

Topic: Short-Run Cost

44) Marginal cost \_\_\_\_\_.

A) is constantly increasing, but as output increases it increases by smaller and smaller amounts

B) decreases at low outputs until it reaches its minimum value, then remains constant

C) decreases at low outputs and increases at high outputs

D) increases at low outputs until it reaches its maximum value, then remains constant

E) is constantly decreasing, but as output increases it decreases by smaller and smaller amounts

Answer: C

Diff: 2 Type: MC

Topic: Short-Run Cost

Source: MyEconLab

45) The marginal cost curve slopes downward at low outputs because of \_\_\_\_\_. The marginal cost curve eventually slopes upward because of \_\_\_\_\_.

A) greater specialization and division of labour; the law of diminishing returns

B) the law of diminishing returns; increasing average fixed cost

C) falling average fixed cost; the law of diminishing returns

D) the law of diminishing returns; greater specialization and division of labour

E) greater specialization and division of labour; rising average fixed cost

Answer: A

Diff: 2 Type: MC

Topic: Short-Run Cost

Source: MyEconLab

46) When the marginal product curve is \_\_\_\_\_, the marginal cost curve is falling. When the average product curve is \_\_\_\_\_, the average variable cost curve is falling. Maximum  $MP$  occurs at the same output as \_\_\_\_\_. Maximum  $AP$  occurs at the same output as \_\_\_\_\_.

- A) rising; rising; maximum  $MC$ ; maximum  $AVC$
- B) falling; falling; minimum  $MC$ ; minimum  $AVC$
- C) rising; rising; minimum  $MC$ ; minimum  $AVC$
- D) falling; falling; maximum  $MC$ ; maximum  $AVC$
- E) rising; rising; minimum  $MC$ ; minimum  $ATC$

Answer: C

Diff: 2 Type: MC

Topic: Short-Run Cost

Source: MyEconLab

47) Sue's Surfboards rents the factory building in which it produces surfboards. The rent is increased by \$200 a week. If other things remain the same, the average fixed cost curve \_\_\_\_\_, the average variable cost curve \_\_\_\_\_, the average total cost curve \_\_\_\_\_, and the marginal cost curve \_\_\_\_\_.

- A) does not change; shifts upward; shifts upward; shifts upward
- B) shifts upward; does not change; shifts upward; does not change
- C) shifts upward; does not change; does not change; shifts upward
- D) shifts upward; does not change; shifts upward; shifts upward
- E) shifts upward; shifts upward; shifts upward; shifts upward

Answer: B

Diff: 2 Type: MC

Topic: Short-Run Cost

Source: MyEconLab

48) Which type of cost does not change as the quantity of output produced changes?

- A) average total cost
- B) marginal cost
- C) average fixed cost
- D) total fixed cost
- E) Both C and D are correct.

Answer: D

Type: MC

49) Ernie's Earmuffs produces 200 earmuffs per year at a total cost of \$2,000 and \$400 of this cost is fixed. What is Ernie's total variable cost?

- A) \$400
- B) \$8
- C) \$2
- D) \$2,400
- E) \$1,600

Answer: E

Type: MC

50) Ernie's Earmuffs produces 200 earmuffs per year at a total cost of \$2,000 and \$400 of this cost is fixed. What is Ernie's average variable cost?

A) \$400

B) \$8

C) \$2

D) \$2,400

E) \$1,600

Answer: B

Type: MC

## 11.4 Long-Run Cost

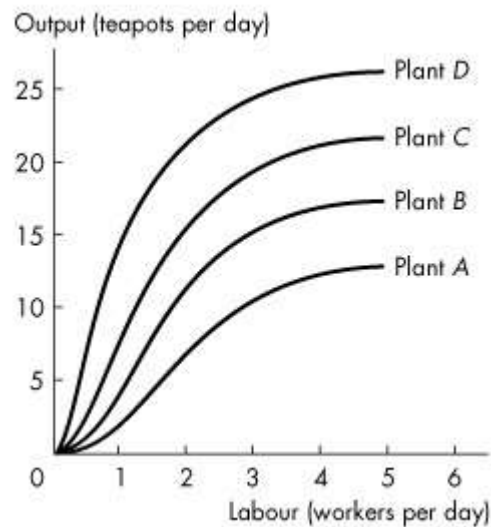
- 1) A production function is the relationship between the maximum output attainable and the
- A) price of output.
  - B) change in technology.
  - C) demand for output.
  - D) quantities of inputs used.
  - E) amount of labour used.

Answer: D

Diff: 1 Type: MC

Topic: Long-Run Cost

Use the figure below to answer the following questions.



**Figure 11.4.1**

- 2) Refer to Figure 11.4.1 which shows the total product curves for four different plant sizes as Tania varies the quantity of capital and workers. The curve that represents the plant using the largest amount of capital is

- A) plant A.
- B) plant B.
- C) plant C.
- D) plant D.
- E) all curves because each plant uses the same number of machines, just different amounts of labour.

Answer: D

Diff: 2 Type: MC

Topic: Long-Run Cost

3) Refer to Figure 11.4.1, which illustrates the total product curves for four different plant sizes. One of the fundamental technological facts reflected in the shape of each of the total product curves is the

- A) price of the inputs.
- B) price of the output.
- C) law of diminishing marginal returns.
- D) law of economies of scale.
- E) fact that capital and labour cannot be substituted for each other.

Answer: C

Diff: 2 Type: MC

Topic: Long-Run Cost

4) The marginal product of capital is the

- A) change in total product resulting from a 1-unit increase in the quantity of labour employed, holding the quantity of the capital constant.
- B) change in total product resulting from a 1-unit increase in the quantity of capital employed, holding the quantity of the labour constant.
- C) total product divided by the total quantity of capital employed, holding the quantity of the labour constant.
- D) total product divided by the total quantity of labour employed, holding the quantity of the capital constant.
- E) change in the quantity of capital used resulting from a 1-unit increase in total product, holding constant the quantity of labour.

Answer: B

Diff: 2 Type: MC

Topic: Long-Run Cost

5) Suppose Honda can triple its production of Civics by tripling its production facility for those cars. This indicates the presence of

- A) constant returns to scale.
- B) economies of scale.
- C) diseconomies of scale.
- D) the law of diminishing returns.
- E) minimum efficient scale.

Answer: A

Diff: 2 Type: MC

Topic: Long-Run Cost

6) Suppose a candy manufacturer can triple its production of fudge by doubling its production facility for making fudge. This indicates the presence of

- A) constant returns to scale.
- B) economies of scale.
- C) diseconomies of scale.
- D) market constraints.
- E) the law of diminishing returns.

Answer: B

Diff: 2 Type: MC

Topic: Long-Run Cost

- 7) Diseconomies of scale are present when
- A) the *LRAC* curve slopes downward.
  - B) average total cost falls as input increases.
  - C) average total cost rises as output increases.
  - D) the *LRAC* curve is horizontal.
  - E) total fixed cost increases.

Answer: C

Diff: 1 Type: MC

Topic: Long-Run Cost

- 8) Economies of scale are present when
- A) the *LRAC* curve slopes downward.
  - B) average total cost remains constant as input increases.
  - C) average total cost rises as output increases.
  - D) the *LRAC* curve is horizontal.
  - E) total fixed cost increases.

Answer: A

Diff: 1 Type: MC

Topic: Long-Run Cost

- 9) If diseconomies of scale are present
- A) average total cost is decreasing.
  - B) the long-run average cost curve has a negative slope.
  - C) economies of scale are also present.
  - D) the long-run average cost curve has a positive slope.
  - E) None of the above.

Answer: D

Diff: 2 Type: MC

Topic: Long-Run Cost

- 10) If constant returns to scale are present
- A) average total cost is decreasing.
  - B) average total cost is increasing.
  - C) the *LRAC* curve is horizontal.
  - D) the *LRAC* curve is downward sloping.
  - E) the *LRAC* curve is upward sloping.

Answer: C

Diff: 2 Type: MC

Topic: Long-Run Cost

Use the table below to answer the following questions.

**Table 11.4.1**  
Swanky's output levels

Labour (workers per day)	Plant Size (knitting machines)		
	1	2	3
1	5	11	14
2	11	16	19
3	14	19	23
4	16	21	25
5	17	22	26

11) Refer to Table 11.4.1, which represents Swanky's production possibilities as the firm varies the quantities of knitting machines and workers per day. If Swanky increases the number of knitting machines from 2 to 3 and increases the number of workers employed from 2 to 3, the factory experiences

- A) economies of scale.
- B) constant returns to scale.
- C) diseconomies of scale.
- D) constant marginal product.
- E) minimum efficient scale.

Answer: C

Diff: 3 Type: MC

Topic: Long-Run Cost

12) Refer to Table 11.4.1, which represents Swanky's production possibilities as the firm varies the quantities of knitting machines and workers per day. If Swanky increases the number of knitting machines from 1 to 2 and increases the number of workers employed from 1 to 2, the factory experiences

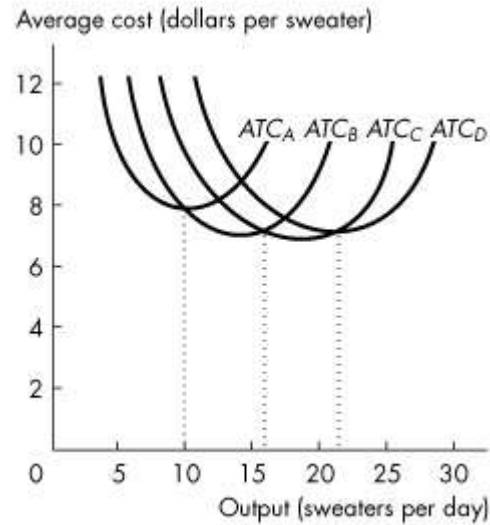
- A) economies of scale.
- B) constant returns to scale.
- C) diseconomies of scale.
- D) constant marginal product.
- E) minimum efficient scale.

Answer: A

Diff: 3 Type: MC

Topic: Long-Run Cost

Use the figure below to answer the following questions.



**Figure 11.4.2**

13) Refer to Figure 11.4.2, which illustrates the short-run average total cost curves for four different plant sizes. Which curve represents the average total cost for the largest of the four plant sizes?

- A)  $ATC_A$
- B)  $ATC_B$
- C)  $ATC_C$
- D)  $ATC_D$
- E) either  $ATC_C$  or  $ATC_D$

Answer: D

Diff: 3 Type: MC

Topic: Long-Run Cost

14) Refer to Figure 11.4.2, which illustrates the short-run average total cost curves for four different plant sizes. Which plant has the lowest average total cost for an output rate of 5 sweaters a day?

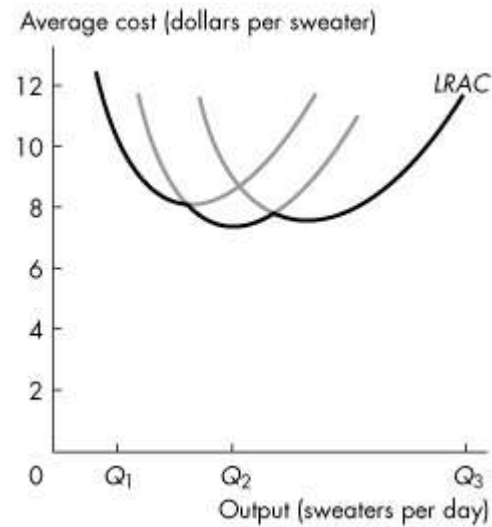
- A) Plant A
- B) Plant B
- C) Plant C
- D) Plant D
- E) none of the above

Answer: A

Diff: 3 Type: MC

Topic: Long-Run Cost

Use the figure below to answer the following question.



**Figure 11.4.3**

15) Refer to Figure 11.4.3 which shows a firm's long-run average total cost curve. An increase in production from  $Q_1$  to  $Q_2$  sweaters per day produces

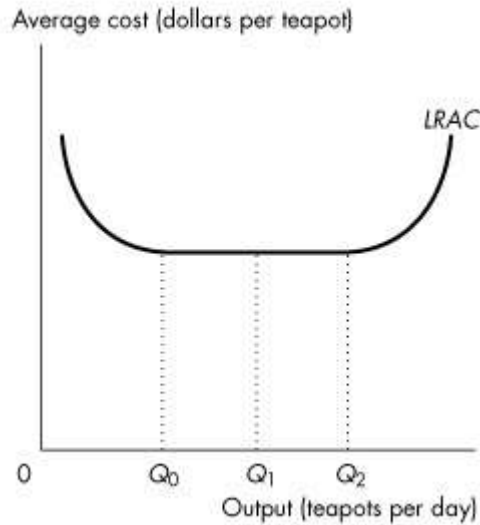
- A) the minimum efficient scale.
- B) economies of scale.
- C) diseconomies of scale.
- D) constant total costs.
- E) constant returns to scale.

Answer: B

Diff: 2 Type: MC

Topic: Long-Run Cost

Use the figure below to answer the following questions.



**Figure 11.4.4**

16) Refer to Figure 11.4.4, which illustrates the long-run average total cost curve. Which one of the following statements is *false*?

- A) Economies of scale exist between 0 and  $Q_0$  units of output.
- B) Diseconomies of scale exist between 0 and  $Q_1$  units of output.
- C) Constant returns to scale exist between  $Q_1$  and  $Q_2$  units of output.
- D) Diseconomies of scale exist at quantities greater than  $Q_2$  units of output.
- E) Constant returns to scale exist between  $Q_0$  and  $Q_1$  units of output.

Answer: B

Diff: 2 Type: MC

Topic: Long-Run Cost

17) Refer to Figure 11.4.4, which illustrates the long-run average total cost curve. Given an increase in output from  $Q_1$  to  $Q_2$ ,

- A) economies of scale exist.
- B) diseconomies of scale exist.
- C) constant returns to scale exist.
- D) average total cost is increasing.
- E) average total cost is decreasing.

Answer: C

Diff: 2 Type: MC

Topic: Long-Run Cost

18) A firm will want to increase its scale of plant if

- A) it is persistently producing on the upward-sloping part of its short-run average total cost curve.
- B) it is persistently producing on the downward-sloping part of its short-run average total cost curve.
- C) it is producing below minimum efficient scale.
- D) marginal cost is below average total cost.
- E) marginal cost is below average variable cost.

Answer: A

Diff: 3 Type: MC

Topic: Long-Run Cost

Source: Study Guide

19) The minimum efficient scale is the smallest quantity of output at which

- A) the long-run average cost curve reaches its lowest level.
- B) the average total cost curve reaches its lowest level.
- C) the average fixed cost curve reaches its lowest level.
- D) economies of scale begin.
- E) diminishing returns begin.

Answer: A

Diff: 2 Type: MC

Topic: Long-Run Cost

Source: Study Guide

20) Diminishing returns to capital \_\_\_\_\_ occur as the quantity of capital increases because for a given quantity of \_\_\_\_\_ each additional unit of \_\_\_\_\_ will result in \_\_\_\_\_ incremental amounts of output.

- A) do not; capital; labour; greater
- B) do; labour; capital; smaller
- C) do not; labour; capital; greater
- D) do; capital; labour; smaller
- E) do not; labour; capital; smaller

Answer: B

Diff: 2 Type: MC

Topic: Long-Run Cost

Source: MyEconLab

21) The long-run average cost curve is the relationship between the lowest attainable average total cost and output, when plant size is \_\_\_\_\_ and labour is \_\_\_\_\_. The long-run average cost curve is made up of the segments of individual average \_\_\_\_\_ cost curves with the lowest average \_\_\_\_\_ cost for a given output.

- A) varied; varied; variable; variable
- B) varied; varied; total; total
- C) varied; held constant; variable; variable
- D) held constant; varied; total; total
- E) held constant; varied; variable; variable

Answer: B

Diff: 2 Type: MC

Topic: Long-Run Cost

Source: MyEconLab

22) Economies of scale refer to the range of output over which

- A) long-run average cost rises as output increases.
- B) marginal cost exceeds average cost.
- C) long-run average cost falls as output increases.
- D) the marginal product of labour decreases.
- E) marginal product equals average product.

Answer: C

Type: MC

23) Diseconomies of scale refer to the range of output over which

- A) long-run average cost rises as output increases.
- B) average cost exceeds marginal cost.
- C) long-run average cost falls as output increases.
- D) the marginal product of labour increases.
- E) marginal product equals average product.

Answer: A

Type: MC

## Chapter 12 Perfect Competition

### 12.1 What Is Perfect Competition?

1) Perfect competition occurs in a market where there are many firms, each selling

- A) an identical product.
- B) a similar product.
- C) a unique product.
- D) a capital-intensive product.
- E) a competitive product.

Answer: A

Diff: 1 Type: MC

Topic: What is Perfect Competition?

2) Which one of the following does *not* occur in perfect competition?

- A) No single firm can exert a significant influence on the market price of the good.
- B) There are many buyers.
- C) There are significant restrictions on entry into the market.
- D) Sellers and buyers are well informed about prices.
- E) Established firms have no advantage over new ones.

Answer: C

Diff: 1 Type: MC

Topic: What is Perfect Competition?

- 3) A price-taking firm faces a
  - A) perfectly inelastic demand.
  - B) downward-sloping marginal revenue curve.
  - C) downward-sloping supply curve.
  - D) perfectly elastic demand.
  - E) downward-sloping demand curve.

Answer: D

Diff: 1 Type: MC

Topic: What is Perfect Competition?

- 4) In a perfectly competitive market, the market demand curve is illustrated by
  - A) a downward-sloping curve.
  - B) a line that is vertical at the market output.
  - C) an upward-sloping curve.
  - D) a line that is horizontal at the market price.
  - E) a curve that is bowed towards the origin.

Answer: A

Diff: 1 Type: MC

Topic: What is Perfect Competition?

5) The slope of a perfectly competitive firm's demand curve is

- A) infinity.
- B) zero.
- C) 1.
- D) greater than 1.
- E) negative.

Answer: B

Diff: 2 Type: MC

Topic: What is Perfect Competition?

6) A price taker is a firm that

- A) must lower its price if it wants to sell more output.
- B) sets the market price.
- C) cannot influence the market price.
- D) is incurring an economic loss.
- E) can raise its price if it lowers output.

Answer: C

Diff: 1 Type: MC

Topic: What is Perfect Competition?

7) If a firm faces a perfectly elastic demand for its product, then

- A) it is not a price taker.
- B) it will want to lower its price to increase sales.
- C) it will want to raise its price to increase total revenue.
- D) its marginal revenue curve is horizontal at the market price.
- E) it will always make zero economic profit.

Answer: D

Diff: 2 Type: MC

Topic: What is Perfect Competition?

Source: Study Guide

8) Marginal revenue is

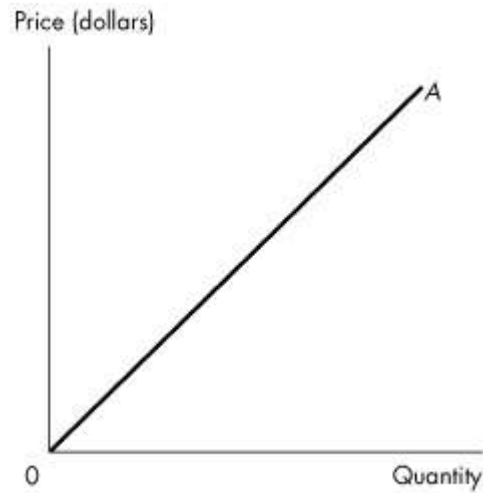
- A) the change in total quantity that results from a one-unit increase in the price of the good.
- B) the change in total revenue that results from a one-unit increase in the quantity sold.
- C) economic profit divided by the quantity sold.
- D) the change in economic profit that results from a one-unit increase in the quantity sold.
- E) total revenue minus total cost.

Answer: B

Diff: 1 Type: MC

Topic: What is Perfect Competition?

Use the figure below to answer the following questions.



**Figure 12.1.1**

9) Refer to Figure 12.1.1. The firm competes in a perfectly competitive market. Curve A represents the firm's

- A) total fixed cost curve.
- B) average fixed cost curve.
- C) average variable cost curve.
- D) total revenue curve.
- E) marginal revenue curve.

Answer: D

Diff: 2 Type: MC

Topic: What is Perfect Competition?

10) Refer to Figure 12.1.1. The firm competes in a perfectly competitive market. Curve A is a straight line because the firm

- A) is a price taker.
- B) faces constant returns to scale.
- C) wants to maximize profits.
- D) has perfect information.
- E) has constant marginal cost.

Answer: A

Diff: 2 Type: MC

Topic: What is Perfect Competition?

Use the table below to answer the following questions.

**Table 12.1.1**

Quantity (units)	Price (dollars)
5	15
6	15
7	15

11) Refer to Table 12.1.1 which gives the demand schedule for a perfectly competitive firm. If the firm sells 5 units of output, total revenue is

- A) \$15.
- B) \$30.
- C) \$75.
- D) \$90.
- E) \$105.

Answer: C

Diff: 1 Type: MC

Topic: What is Perfect Competition?

12) Refer to Table 12.1.1 which gives the demand schedule for a perfectly competitive firm. If the firm sells 6 units of output, marginal revenue is

- A) \$15.
- B) \$30.
- C) \$75.
- D) \$90.
- E) \$105.

Answer: A

Diff: 2 Type: MC

Topic: What is Perfect Competition?

13) Refer to Table 12.1.1 which gives the demand schedule for a perfectly competitive firm. If the quantity sold by the firm rises from 5 to 6, marginal revenue is

- A) \$15.
- B) \$30.
- C) \$75.
- D) \$90.
- E) \$105.

Answer: A

Diff: 2 Type: MC

Topic: What is Perfect Competition?

- 14) For perfect competition to arise, it is necessary that market demand be
- A) inelastic.
  - B) elastic.
  - C) perfectly elastic.
  - D) large relative to the minimum efficient scale of a single firm.
  - E) small relative to the minimum efficient scale of a single firm.

Answer: D

Diff: 2 Type: MC

Topic: What is Perfect Competition?

Source: Study Guide

- 15) Assume that the leather market is a perfectly competitive market. The market demand curve for leather is \_\_\_\_\_ and each individual leather producer's demand curve is \_\_\_\_\_.

- A) vertical; downward sloping
- B) downward sloping; horizontal
- C) downward sloping; vertical
- D) horizontal; horizontal
- E) horizontal; downward sloping

Answer: B

Diff: 2 Type: MC

Topic: What is Perfect Competition?

- 16) An example of a perfectly competitive industry is the

- A) airline industry.
- B) beer industry.
- C) running shoe industry.
- D) fast food industry.
- E) wheat industry.

Answer: E

Diff: 2 Type: MC

Topic: What is Perfect Competition?

- 17) Economic profit equals

- A) total fixed cost plus total variable cost.
- B) total revenue minus marginal cost.
- C) marginal revenue minus marginal cost.
- D) total revenue minus total cost.
- E) total revenue minus total variable cost.

Answer: D

Diff: 1 Type: MC

Topic: What is Perfect Competition?

18) Lin's fortune cookies are identical to the fortune cookies made by dozens of other firms, and there is free entry in the fortune cookie market. Buyers and sellers are well informed about prices. Lin's fortune cookies operates in a \_\_\_\_\_ market.

- A) challenging
- B) monopolistic
- C) perfectly competitive
- D) noncompetitive
- E) perfectly competent

Answer: C

Type: MC

Topic: What is Perfect Competition?

Source: MyEconLab

19) Lin's fortune cookies are identical to the fortune cookies made by dozens of other firms, and there is free entry in the fortune cookie market. Buyers and sellers are well informed about prices. The price of a fortune cookie is determined by \_\_\_\_\_. The marginal revenue of a fortune cookie equals \_\_\_\_\_.

- A) market demand and market supply; price
- B) the ingredients that Lin's uses to produce his fortune cookies; average total cost
- C) the number of cookies that Lin's produces; average variable cost
- D) the freshness of the fortune cookies; average fixed cost
- E) market demand and market supply; the price elasticity of demand

Answer: A

Type: MC

Topic: What is Perfect Competition?

Source: MyEconLab

20) A perfectly competitive market is characterized by

- A) firms that are price setters.
- B) firms that each face a downward-sloping demand curve.
- C) firms that each sell a unique good or service.
- D) buyers who are unaware of the price charged by each firm.
- E) no restrictions on entry into the market.

Answer: E

Type: MC

21) When a firm is a "price taker," the firm

- A) can charge any price that it wants to charge, that is, "take" any price it chooses.
- B) pays a fixed price for all of its fixed inputs.
- C) will accept ("take") the lowest price that its customers offer.
- D) pays a fixed price for all of its variable inputs.
- E) cannot influence the market price of the good that it sells.

Answer: E

Type: MC

## 12.2 The Firm's Output Decision

Use the table below to answer the following questions.

**Table 12.2.1**

Output (units)	Total Revenue (dollars)	Total Cost (dollars)
0	0	25
1	30	49
2	60	69
3	90	86
4	120	100
5	150	114
6	180	128
7	210	170

1) Refer to Table 12.2.1, which gives the total revenue schedule and total cost schedule of a perfectly competitive firm. The short-run equilibrium price of one unit of the good is

- A) \$3.
- B) \$10.
- C) \$15.
- D) \$25.
- E) \$30.

Answer: E

Diff: 3 Type: MC

Topic: The Firm's Output Decision

2) Refer to Table 12.2.1, which gives the total revenue schedule and total cost schedule of a perfectly competitive firm. The marginal revenue received from the sale of the 4th unit of output is

- A) \$3.
- B) \$15.
- C) \$10.
- D) \$120.
- E) \$30.

Answer: E

Diff: 2 Type: MC

Topic: The Firm's Output Decision

3) Refer to Table 12.2.1, which gives the total revenue schedule and total cost schedule of a perfectly competitive firm. The marginal cost of increasing production from 4 units to 5 units is

- A) \$14.
- B) \$128.
- C) \$100.
- D) \$25.
- E) \$30.

Answer: A

Diff: 2 Type: MC

Topic: The Firm's Output Decision

4) Refer to Table 12.2.1, which gives the total revenue schedule and total cost schedule of a perfectly competitive firm. If the firm produces 2 units of output, it

- A) makes an economic profit of \$9.
- B) makes an economic profit of \$60.
- C) incurs an economic loss of \$9.
- D) incurs an economic loss of \$60.
- E) incurs an economic loss of \$69.

Answer: C

Diff: 2 Type: MC

Topic: The Firm's Output Decision

5) Refer to Table 12.2.1, which gives the total revenue schedule and total cost schedule of a perfectly competitive firm. If the firm produces 3 units of output, it will

- A) make an economic profit of \$4.
- B) make an economic profit of \$90.
- C) incur an economic loss of \$4.
- D) break even.
- E) incur an economic loss of \$86.

Answer: A

Diff: 2 Type: MC

Topic: The Firm's Output Decision

6) Refer to Table 12.2.1, which gives the total revenue schedule and total cost schedule of a perfectly competitive firm. Economic profit is maximized when the firm produces \_\_\_\_\_ units of output.

- A) zero
- B) 7
- C) 3
- D) 6
- E) 5

Answer: D

Diff: 2 Type: MC

Topic: The Firm's Output Decision

- 7) A firm shuts down if price is
- A) above minimum average variable cost.
  - B) below minimum average variable cost.
  - C) above minimum average fixed cost.
  - D) less than marginal cost.
  - E) below average total cost.

Answer: B

Diff: 2 Type: MC

Topic: The Firm's Output Decision

Use the table below to answer the following questions.

**Table 12.2.2**

Output (pizzas per hour)	Total Cost (dollars per hour)
0	10
1	12
2	16
3	22
4	30
5	40
6	55

- 8) Refer to Table 12.2.2, which gives the total cost schedule for Chip's Pizza Palace, a perfectly competitive firm. If the price of a pizza is \$7, what is Chip's profit-maximizing output per hour?

- A) zero pizzas
- B) 1 pizza
- C) 2 pizzas
- D) 3 pizzas
- E) 4 pizzas

Answer: D

Diff: 3 Type: MC

Topic: The Firm's Output Decision

- 9) Refer to Table 12.2.2, which gives the total cost schedule for Chip's Pizza Palace, a perfectly competitive firm. If Chip shuts down in the short run, his total cost is

- A) \$0.
- B) \$10 an hour.
- C) \$12 an hour.
- D) \$22 an hour.
- E) \$40 an hour.

Answer: B

Diff: 2 Type: MC

Topic: The Firm's Output Decision

Use the table below to answer the following questions.

**Table 12.2.3**

Output (balloons per hour)	Total Cost (dollars per hour)
0	4.00
1	7.00
2	8.00
3	12.50
4	17.20
5	22.00
6	29.00

10) Refer to Table 12.2.3, which gives the total cost schedule for Brenda's Balloon Shop, a perfectly competitive firm. Brenda's total fixed cost is

- A) \$3 an hour.
- B) \$4 an hour.
- C) \$7 an hour.
- D) \$29 an hour.
- E) zero.

Answer: B

Diff: 2 Type: MC

Topic: The Firm's Output Decision

11) Refer to Table 12.2.3, which gives the total cost schedule for Brenda's Balloon Shop, a perfectly competitive firm. The marginal cost of increasing production from 4 balloons an hour to 5 balloons an hour is

- A) \$1.
- B) \$4.50.
- C) \$4.70.
- D) \$4.80.
- E) \$4.40.

Answer: D

Diff: 2 Type: MC

Topic: The Firm's Output Decision

12) Refer to Table 12.2.3, which gives the total cost schedule for Brenda's Balloon Shop, a perfectly competitive firm. The average fixed cost of producing the 4th balloon is

- A) \$4.30.
- B) \$4.80.
- C) \$4.70.
- D) \$4.50.
- E) \$1.00.

Answer: E

Diff: 3 Type: MC

Topic: The Firm's Output Decision

13) Refer to Table 12.2.3 which gives the total cost schedule for Brenda's Balloon Shop, a perfectly competitive firm. The average variable cost of producing the 1st balloon is

- A) \$1.00
- B) \$4.00
- C) \$2.00
- D) \$4.80.
- E) \$3.00

Answer: E

Diff: 2 Type: MC

Topic: The Firm's Output Decision

14) A firm will shut down temporarily when the price is so low that total revenue is insufficient to cover the

- A) total cost of production.
- B) total variable cost of production.
- C) total fixed cost of production.
- D) marginal cost of production.
- E) none of the above.

Answer: B

Diff: 1 Type: MC

Topic: The Firm's Output Decision

15) A firm that temporarily shuts down and produces no output incurs a loss equal to its

- A) total fixed cost.
- B) total variable cost.
- C) marginal cost.
- D) marginal revenue.
- E) average total cost.

Answer: A

Diff: 2 Type: MC

Topic: The Firm's Output Decision

16) Suppose a firm is trying to decide whether or not to temporarily shut down to minimize total loss. If price equals average variable cost, then

- A) total revenue equals total fixed cost, and the loss equals total variable cost.
- B) total revenue equals total variable cost, and the loss equals total fixed cost.
- C) total fixed cost is zero.
- D) total variable cost equals total fixed cost.
- E) total cost equals total variable cost.

Answer: B

Diff: 3 Type: MC

Topic: The Firm's Output Decision

17) The shutdown point occurs at the point of minimum

- A) marginal cost.
- B) average variable cost.
- C) average fixed cost.
- D) total cost.
- E) average total cost.

Answer: B

Diff: 1 Type: MC

Topic: The Firm's Output Decision

18) A firm maximizes profit by producing the output at which marginal cost equals

- A) marginal revenue.
- B) average total cost.
- C) average variable cost.
- D) average fixed cost.
- E) total revenue.

Answer: A

Diff: 1 Type: MC

Topic: The Firm's Output Decision

19) In a perfectly competitive market, a firm maximizes its profit by producing the quantity of output at which

- A) market price equals average fixed cost.
- B) market price equals marginal cost.
- C) average variable cost equals average fixed cost.
- D) market price equals minimum average variable cost.
- E) market price equals marginal revenue.

Answer: B

Diff: 1 Type: MC

Topic: The Firm's Output Decision

20) If price falls below minimum average variable cost, the best a firm can do is

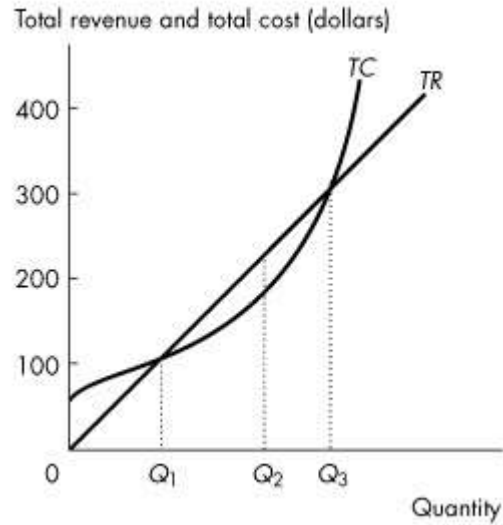
- A) increase production and incur a loss equal to total variable cost.
- B) increase production and incur a loss equal to total fixed cost.
- C) stop production and incur a loss equal to total fixed cost.
- D) stop production and incur a loss equal to total variable cost.
- E) stay at the same production level and incur a loss equal to the difference between total cost and total revenue.

Answer: C

Diff: 2 Type: MC

Topic: The Firm's Output Decision

Use the figure below to answer the following question.



**Figure 12.2.1**

21) Refer to Figure 12.2.1, which shows a perfectly competitive firm's total revenue and total cost curves. Which one of the following statements is *false*?

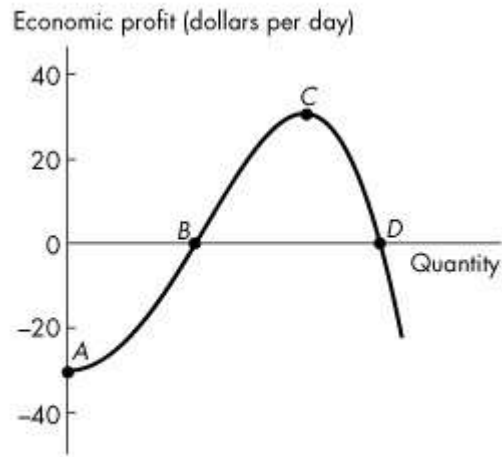
- A) Economic profit is the vertical distance between the total revenue curve and the total cost curve.
- B) At an output of  $Q_1$  units a day, the firm makes zero economic profit.
- C) At an output greater than  $Q_3$  units a day, the firm incurs an economic loss.
- D) At an output of  $Q_2$  units a day, the firm incurs an economic loss.
- E) At an output less than  $Q_1$  units a day, the firm incurs an economic loss.

Answer: D

Diff: 2 Type: MC

Topic: The Firm's Output Decision

Use the figure below to answer the following questions.



**Figure 12.2.2**

22) Refer to Figure 12.2.2, which shows a perfectly competitive firm's economic profit and loss.

The firm is incurring a loss at

- A) point *A*.
- B) point *B*.
- C) point *C*.
- D) point *D*.
- E) both points *B* and *D*.

Answer: A

Diff: 2 Type: MC

Topic: The Firm's Output Decision

23) Refer to Figure 12.2.2, which shows a perfectly competitive firm's economic profit and loss.

The firm is breaking even at points

- A) *A* and *C*.
- B) *A* and *D*.
- C) *B* and *C*.
- D) *B* and *D*.
- E) *C* and *D*.

Answer: D

Diff: 2 Type: MC

Topic: The Firm's Output Decision

24) A perfectly competitive firm's supply curve includes its marginal cost curve at all prices above minimum

- A) average total cost.
- B) average fixed cost.
- C) total cost.
- D) average variable cost.
- E) total variable cost.

Answer: D

Diff: 2 Type: MC

Topic: The Firm's Output Decision

25) A perfectly competitive firm is maximizing profit if

- A) marginal cost equals price and price is not below minimum average variable cost.
- B) marginal cost equals price and price is not below minimum average fixed cost.
- C) total revenue is at a maximum.
- D) average variable cost is at a minimum.
- E) average total cost is at a minimum.

Answer: A

Diff: 3 Type: MC

Topic: The Firm's Output Decision

26) If a perfectly competitive firm is producing an output at which price is equal to average total cost, the firm

- A) should shut down.
- B) is breaking even.
- C) is making an economic profit.
- D) is incurring an economic loss.
- E) is not producing its profit-maximizing quantity.

Answer: B

Diff: 2 Type: MC

Topic: The Firm's Output Decision

27) If a perfectly competitive firm's marginal revenue is less than its marginal cost, the firm

- A) cannot increase its economic profit.
- B) must be making an economic profit.
- C) should decrease its output to increase economic profit.
- D) should increase its output to increase economic profit.
- E) must raise the price.

Answer: C

Diff: 2 Type: MC

Topic: The Firm's Output Decision

28) The maximum loss a firm will experience in the short run equals

- A) zero.
- B) its total fixed cost.
- C) its total variable cost.
- D) its total cost.
- E) its marginal cost.

Answer: B

Diff: 2 Type: MC

Topic: The Firm's Output Decision

29) In the price range below minimum average variable cost, a perfectly competitive firm's supply curve is

- A) horizontal at the market price.
- B) vertical at zero output.
- C) the same as its marginal cost curve.
- D) the same as its average variable cost curve.
- E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: The Firm's Output Decision

Source: Study Guide

30) In the price range above minimum average variable cost, a perfectly competitive firm's supply curve is

- A) horizontal at the market price.
- B) vertical at zero output.
- C) the same as its marginal cost curve.
- D) the same as its average variable cost curve.
- E) none of the above.

Answer: C

Diff: 1 Type: MC

Topic: The Firm's Output Decision

31) If a perfectly competitive firm is producing in the short run at an output where price is less than average total cost, the firm

- A) will shut down.
- B) is breaking even.
- C) is still making a positive economic profit.
- D) is incurring an economic loss but will continue to operate as long as price is above minimum average fixed cost.
- E) is incurring an economic loss but will continue to operate as long as price is above minimum average variable cost.

Answer: E

Diff: 2 Type: MC

Topic: The Firm's Output Decision

- 32) If a perfectly competitive firm's marginal revenue is greater than its marginal cost, the firm
- A) cannot increase its economic profit.
  - B) must be making an economic profit.
  - C) will decrease its output to increase economic profit.
  - D) will increase its output to increase economic profit.
  - E) will lower the price.

Answer: D

Diff: 2 Type: MC

Topic: The Firm's Output Decision

- 33) In a perfectly competitive market, the market price is \$8. An individual firm is producing the output at which  $MC = \$8$ .  $AVC$  at that output is \$10. What should the firm do to maximize its economic profit in the short run?

- A) shut down
- B) expand output
- C) contract output
- D) leave output unchanged
- E) raise the price

Answer: A

Diff: 2 Type: MC

Topic: The Firm's Output Decision

- 34) If a perfectly competitive firm in the short run is able to pay its variable costs and part, but not all, of its fixed costs, then it is operating in the range on its marginal cost curve that is anywhere

- A) above the break-even point.
- B) below the break-even point.
- C) above the shutdown point.
- D) below the shutdown point.
- E) between the shutdown and break-even points.

Answer: E

Diff: 2 Type: MC

Topic: The Firm's Output Decision

Source: Study Guide

- 35) If a perfectly competitive firm in the short run is able to pay its variable costs and all of its fixed costs and more, then it is operating in the range on its marginal cost curve that is

- A) above the break-even point.
- B) below the break-even point.
- C) above the shutdown point.
- D) below the shutdown point.
- E) between the shutdown and break-even points.

Answer: A

Diff: 2 Type: MC

Topic: The Firm's Output Decision

36) In a perfectly competitive industry, the market price is \$5. An individual firm is producing the level of output where marginal cost is \$5 and is increasing, and average total cost is \$25. What should the firm do to maximize its economic profit in the short run?

- A) shut down
- B) expand output
- C) contract output
- D) leave output unchanged
- E) insufficient information to answer

Answer: E

Diff: 3 Type: MC

Topic: The Firm's Output Decision

Use the table below to answer the following question.

**Table 12.2.4**

<i>Price</i> (dollars per box)	<i>Quantity demanded</i> (thousands of boxes per week)
3.65	500
5.20	450
6.80	400
8.40	350
10.00	300
11.60	250
13.20	200

<b>Quantity</b> (boxes per week)	<b>Marginal cost</b> (dollars per additional box)	<b>Average</b> <b>variable cost</b> (dollars per box)	<b>Average</b> <b>total cost</b> (dollars per box)
200	6.40	7.80	12.80
250	7.00	7.00	11.00
300	7.65	7.10	10.43
350	8.40	7.20	10.06
400	10.00	7.50	10.00
450	12.40	8.00	10.22
500	20.70	9.00	11.00

37) Refer to Table 12.2.4. The market is perfectly competitive and there are 1,000 firms that produce paper.

The top table sets out the market demand schedule for paper.

Each producer of paper has the costs shown in the bottom table when it uses its least-cost plant size.

The market price is \_\_\_\_\_ a box, the market output is \_\_\_\_\_ boxes, and the output produced by each firm is \_\_\_\_\_ boxes. Each firm \_\_\_\_\_.

A) \$7.00; 250,000; 250; incurs an economic loss of \$1,000 a week

B) \$8.40; 350,000; 350; makes zero economic profit

C) \$7.65; 300,000; 300; incurs an economic loss of \$834 a week

D) \$8.40; 350,000; 350; incurs an economic loss of \$581 a week

E) \$7.65; 300,000; 300; makes zero economic profit

Answer: D

Type: MC

Topic: The Firm's Output Decision

Source: MyEconLab

38) A firm is producing the profit-maximizing amount of output when it is producing where its \_\_\_\_\_ curve intersects its \_\_\_\_\_ curve.

- A) marginal cost; average total cost
- B) marginal cost; average variable cost
- C) marginal cost; marginal revenue
- D) average total cost; average variable cost
- E) total cost; total revenue

Answer: C

Type: MC

39) As a firm in a perfectly competitive market increases its output, its marginal revenue \_\_\_\_\_ and its marginal cost \_\_\_\_\_.

- A) increases; increases
- B) increases; does not change
- C) does not change; decreases
- D) decreases; increases
- E) does not change; increases

Answer: E

Type: MC

### 12.3 Output, Price and Profit in the Short Run

1) In which one of the following situations will a perfectly competitive firm make an economic profit?

- A)  $MR > AVC$
- B)  $MR > ATC$
- C)  $ATC > MC$
- D)  $ATC > MR$
- E)  $MC > AVC$

Answer: B

Diff: 2 Type: MC

Topic: Output, Price, and Profit in the Short Run

Source: Study Guide

2) In which one of the following situations will a perfectly competitive firm incur an economic loss?

- A)  $MR > AVC$
- B)  $MR > ATC$
- C)  $ATC < MC$
- D)  $ATC > MR$
- E)  $MC > AVC$

Answer: D

Diff: 2 Type: MC

Topic: Output, Price, and Profit in the Short Run

3) A firm in a perfectly competitive industry is maximizing its economic profit by producing 500 units of output. At 500 units of output, which one of the following must be *false*?

- A)  $MC < AVC$
- B)  $MC < ATC$
- C)  $MC > ATC$
- D)  $MR < ATC$
- E)  $MR > AVC$

Answer: A

Diff: 3 Type: MC

Topic: Output, Price, and Profit in the Short Run

4) If a profit-maximizing firm in a perfectly competitive market is making an economic profit, then it must be producing a level of output where

- A) price is greater than marginal cost.
- B) price is greater than marginal revenue.
- C) marginal cost is greater than marginal revenue.
- D) marginal cost is greater than average total cost.
- E) average total cost is greater than marginal cost.

Answer: D

Diff: 3 Type: MC

Topic: Output, Price, and Profit in the Short Run

5) If a profit-maximizing firm in a perfectly competitive market is incurring an economic loss, then it must be producing a level of output where

- A) price is greater than marginal cost.
- B) price is greater than marginal revenue.
- C) marginal cost is greater than marginal revenue.
- D) average total cost is greater than marginal cost.
- E) average total cost is less than marginal cost.

Answer: D

Diff: 3 Type: MC

Topic: Output, Price, and Profit in the Short Run

6) In a perfectly competitive market, the short-run market supply curve is

- A) the horizontal sum of the supply curves of all the individual firms.
- B) the vertical sum of the supply curves of all the individual firms.
- C) vertical at the total level of output being produced by all firms.
- D) horizontal at the current market price.
- E) none of the above.

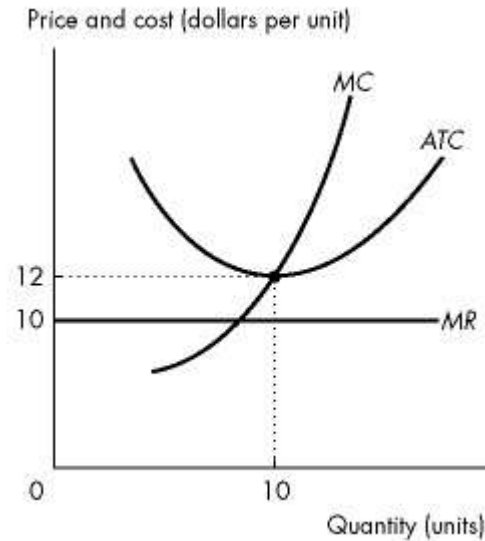
Answer: A

Diff: 1 Type: MC

Topic: Output, Price, and Profit in the Short Run

Source: Study Guide

Use the figure below to answer the following questions.



**Figure 12.3.1**

7) Refer to Figure 12.3.1, which shows the cost curves and marginal revenue curve of a firm in a perfectly competitive industry. In the short run, if the market price of the good is \$10, the firm produces \_\_\_\_\_ units of output and \_\_\_\_\_.

- A) 10; incurs an economic loss of \$20
- B) 10; incurs an economic loss of \$40
- C) less than 10; incurs an economic loss of \$20
- D) 10; makes an economic profit of \$20
- E) less than 10; incurs an economic loss of less than \$20

Answer: E

Diff: 3 Type: MC

Topic: Output, Price, and Profit in the Short Run

8) Refer to Figure 12.3.1 which shows the cost curves and marginal revenue curve of a firm in a perfectly competitive industry. In the short run, the firm will

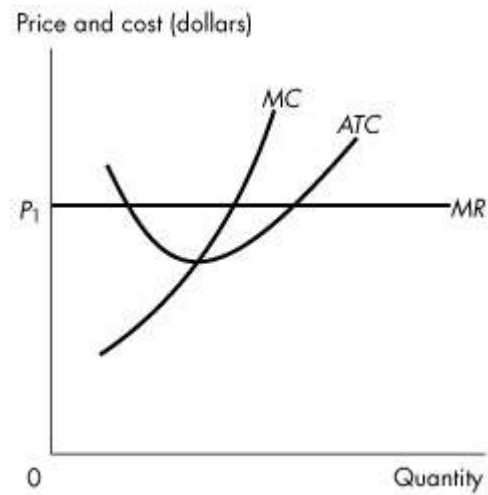
- A) exit from the industry.
- B) break even.
- C) make an economic profit.
- D) incur an economic loss.
- E) close down.

Answer: D

Diff: 2 Type: MC

Topic: Output, Price, and Profit in the Short Run

Use the figure below to answer the following question.



**Figure 12.3.2**

9) Refer to Figure 12.3.2 which shows the cost curves and marginal revenue curve of a firm in a perfectly competitive industry, The firm is

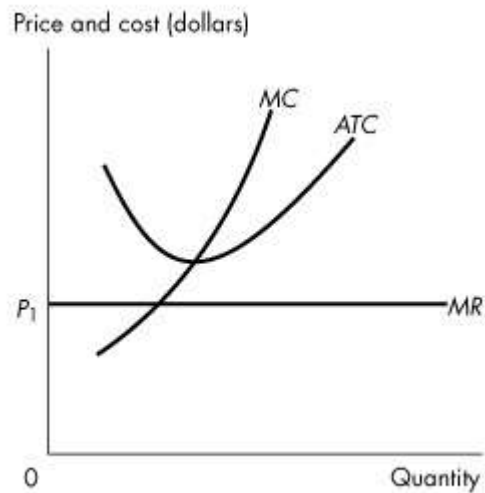
- A) making an economic profit.
- B) incurring an economic loss.
- C) breaking even.
- D) not maximizing economic profit.
- E) going to close down temporarily.

Answer: A

Diff: 2 Type: MC

Topic: Output, Price, and Profit in the Short Run

Use the figure below to answer the following questions.



**Figure 12.3.3**

10) Refer to Figure 12.3.3 which shows the cost curves and marginal revenue curve of a firm in a perfectly competitive industry. The firm is

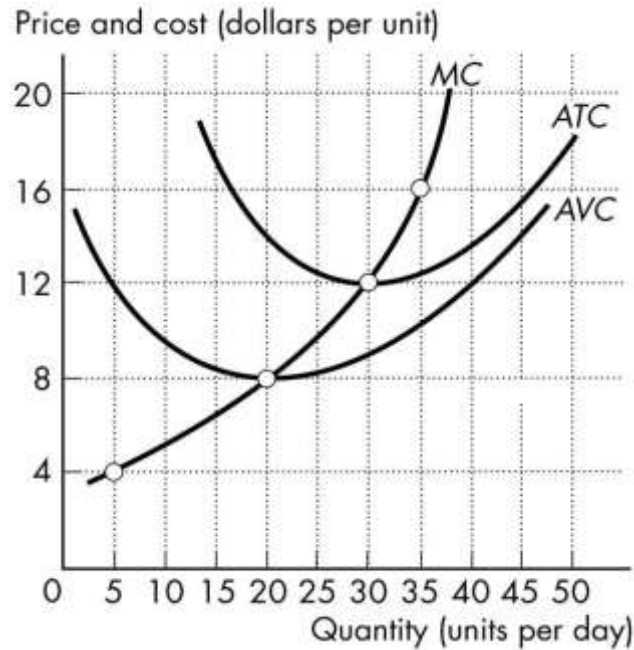
- A) making an economic profit.
- B) incurring an economic loss.
- C) breaking even.
- D) at its shutdown point.
- E) none of the above.

Answer: B

Type: MC

Topic: Output, Price, and Profit in the Short Run

Use the figure below to answer the following questions.



**Figure 12.3.4**

11) Refer to Figure 12.3.4 which shows cost curves of Paul's Picture Frames Inc. The picture frame market is perfectly competitive and the market price is \$30 a frame. Paul produces \_\_\_\_\_ frames each week, makes \_\_\_\_\_ of total revenue, and makes zero \_\_\_\_\_ profit

- A) 200; \$4,000; economic
- B) 300; \$9,000; normal
- C) 200; \$4,000; normal
- D) 300; \$9,000; economic
- E) 300; \$3,000; economic

Answer: D

Type: MC

Use the figure below to answer the following questions.

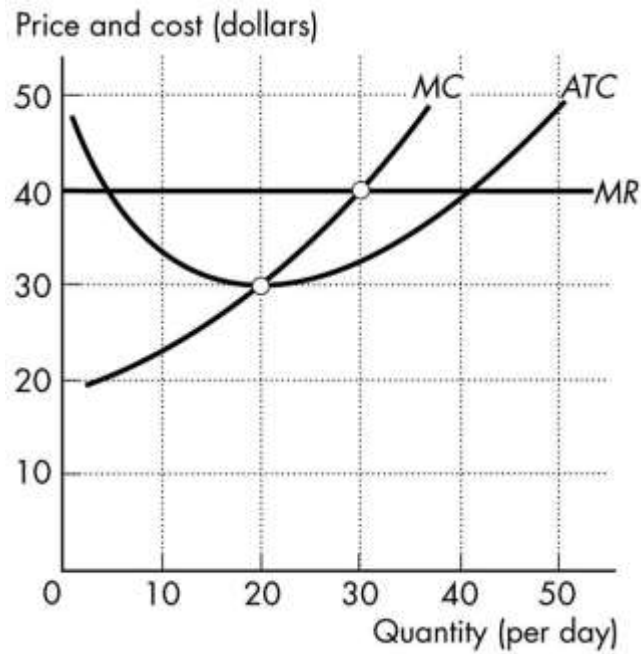


Figure 12.3.5

12) Refer to Figure 12.3.5, which shows the cost curves and the marginal revenue curve for a perfectly competitive firm. To maximize its profit, the firm produces \_\_\_\_\_ units of output and the price is \_\_\_\_\_ a unit.

- A) 30; \$40
- B) 30; \$30
- C) 20; \$40
- D) 20; \$30
- E) 30; \$32.50

Answer: A

Type: MC

## 12.4 Output, Price, and Profit in the Long Run

*Use the information below to answer the following questions.*

### **Fact 12.4.1**

Franklin is a fiddlehead farmer. He sold 10 bags of fiddleheads last month, with total fixed cost of \$100 and total variable cost of \$50.

- 1) Refer to Fact 12.4.1. If the price of fiddleheads last month was \$15 per bag, Franklin
- A) should have shut down because total revenue did not cover total variable cost.
  - B) incurred an economic loss of \$135.
  - C) made zero economic profit.
  - D) made an economic profit of \$50.
  - E) made an economic profit of \$100.

Answer: C

Diff: 2 Type: MC

Topic: Output, Price, and Profit in the Long Run

Source: Study Guide

2) Refer to Fact 12.4.1. Suppose the price of fiddleheads is expected to stay at \$10 per bag for the foreseeable future, and Franklin's production and cost figures are expected to stay the same. His total fixed cost consists entirely of rent on land, and his five-year lease on the land runs out at the end of the month. Should Franklin renew the lease?

- A) Yes, because total revenue will still cover total fixed cost.
- B) Yes, because total revenue will still cover total variable cost and a portion of total fixed cost.
- C) No, because total revenue must cover all costs for factors of production to remain in fiddlehead farming in the long run.
- D) No, because in the long run, zero economic profit is a signal to move factors of production out of fiddlehead farming.
- E) Insufficient information to answer.

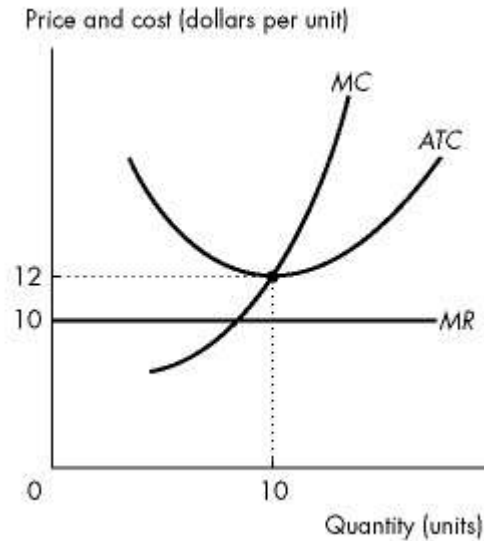
Answer: C

Diff: 3 Type: MC

Topic: Output, Price, and Profit in the Long Run

Source: Study Guide

Use the figure below to answer the following questions.



**Figure 12.4.1**

3) Refer to Figure 12.4.1, which shows the cost curves and marginal revenue curve of a firm in a perfectly competitive market. In the long run, market

- A) demand will increase.
- B) demand will decrease.
- C) supply will increase.
- D) supply will decrease.
- E) supply and market demand will decrease.

Answer: D

Diff: 2 Type: MC

Topic: Output, Price, and Profit in the Long Run

4) Refer to Figure 12.4.1 which shows the cost curves and marginal revenue curve of a firm in a perfectly competitive market. In the long run,

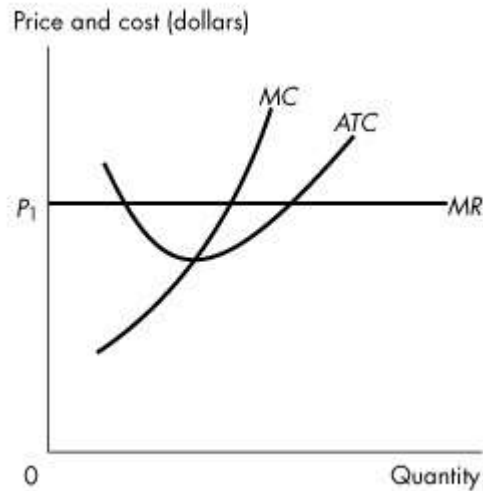
- A) firms that remain in the market will expand production.
- B) market demand will increase.
- C) market supply will increase.
- D) firms will enter the market.
- E) firms that remain in the market will reduce production.

Answer: A

Diff: 3 Type: MC

Topic: Output, Price, and Profit in the Long Run

Use the figure below to answer the following questions.



**Figure 12.4.2**

5) Refer to Figure 12.4.2 which shows the cost curves and marginal revenue curve of a firm in a perfectly competitive market. In the long run, market

- A) demand will increase.
- B) demand will decrease.
- C) supply will increase.
- D) supply will decrease.
- E) supply and market demand will decrease.

Answer: C

Diff: 2 Type: MC

Topic: Output, Price, and Profit in the Long Run

6) Refer to Figure 12.4.2 which shows the cost curves and marginal revenue curve of a firm in a perfectly competitive market. In the long run,

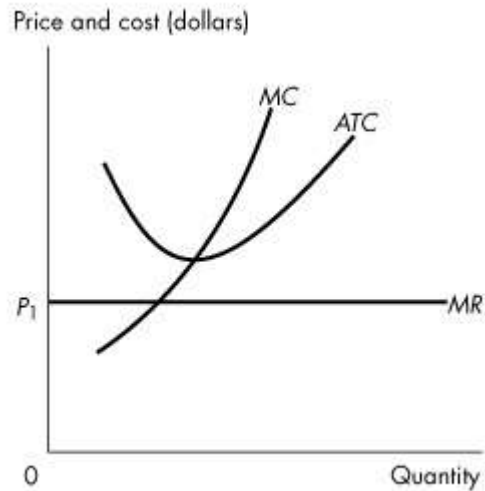
- A) firms that remain in the market will expand production.
- B) market demand will increase.
- C) market supply will decrease.
- D) firms will exit the market.
- E) firms that remain in the market will decrease production.

Answer: E

Diff: 2 Type: MC

Topic: Output, Price, and Profit in the Long Run

Use the figure below to answer the following questions.



**Figure 12.4.3**

7) Refer to Figure 12.4.3. which shows the cost curves and marginal revenue curve of a firm in a perfectly competitive market. In the long run, market

- A) demand will increase.
- B) demand will decrease.
- C) supply will increase.
- D) supply will decrease.
- E) demand and market supply will both increase.

Answer: D

Diff: 2 Type: MC

Topic: Output, Price, and Profit in the Long Run

8) Refer to Figure 12.4.3 which shows the cost curves and marginal revenue curve of a firm in a perfectly competitive market. In the long run,

- A) firms that remain in the market will expand production.
- B) market demand will increase.
- C) firms will adopt labour-saving technology.
- D) industry output will remain constant.
- E) firms will enter the market.

Answer: A

Diff: 2 Type: MC

Topic: Output, Price, and Profit in the Long Run

9) Refer to Figure 12.4.3 which shows the cost curves and marginal revenue curve of a firm in a perfectly competitive market. Firms are

- A) making an economic profit, and some firms leave the market. Market supply decreases.
- B) making an economic profit, and some firms enter the market. Market supply increases.
- C) incurring an economic loss, and some firms leave the market. Market supply decreases.
- D) incurring an economic loss, and some firms enter the market. Market supply increases.
- E) loss, but since they are covering average variable cost, no one will exit the market in the long run.

Answer: C

Diff: 2 Type: MC

Topic: Output, Price, and Profit in the Long Run

10) If firms exit an market, the

- A) market supply curve shifts leftward.
- B) price of the good falls.
- C) economic profit of the remaining firms decrease.
- D) total market output increases.
- E) economic profit of the remaining firms stay the same.

Answer: A

Diff: 2 Type: MC

Topic: Output, Price, and Profit in the Long Run

11) When a perfectly competitive market is in long-run equilibrium

- A) at least one firm makes an economic profit.
- B) all firms make zero economic profit.
- C) firms enter the market if other firms are making an economic profit.
- D) firms exit the market if other firms are incurring an economic loss.
- E) all of the above.

Answer: B

Diff: 2 Type: MC

Topic: Output, Price, and Profit in the Long Run

12) Long-run equilibrium occurs in a competitive market when

- A) economic profit and economic loss have been eliminated.
- B) no barriers to entry exist.
- C) all firms are operating at their shutdown points.
- D) price equals marginal cost.
- E) none of the above.

Answer: A

Diff: 1 Type: MC

Topic: Output, Price, and Profit in the Long Run

13) Which one of the following does *not* occur in the long run when firms in a market make an economic profit?

- A) Firms enter the market.
- B) The market supply curve shifts rightward.
- C) Each firm increases production.
- D) Economic profit of each firm decreases.
- E) Market price falls.

Answer: C

Diff: 2 Type: MC

Topic: Output, Price, and Profit in the Long Run

14) Firms will stop exiting an market only when

- A) marginal revenue equals price.
- B) marginal revenue equals marginal cost.
- C) all remaining firms are making an economic profit.
- D) all remaining firms are making zero economic profit.
- E) marginal revenue equals average fixed cost.

Answer: D

Diff: 2 Type: MC

Topic: Output, Price, and Profit in the Long Run

15) If firms in a perfectly competitive market are making an economic profit, new firms will enter. This entry shifts the market

- A) demand curve leftward, and the market price falls.
- B) demand curve rightward, and the market price rises.
- C) supply curve leftward, and the market price rises.
- D) supply curve rightward, and the market price falls.
- E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: Output, Price, and Profit in the Long Run

16) If firms in a perfectly competitive market are incurring an economic loss, some firms will exit. This exit shifts the market

- A) demand curve leftward, and the market price falls.
- B) demand curve rightward, and the market price rises.
- C) supply curve leftward, and the market price rises.
- D) supply curve rightward, and the market price falls.
- E) none of the above.

Answer: C

Diff: 2 Type: MC

Topic: Output, Price, and Profit in the Long Run

17) A perfectly competitive market is in short-run equilibrium with price below average total cost. Which one of the following is *not* a prediction of the long-run consequences of such a situation?

- A) Price will rise.
- B) Market output will increase.
- C) Firms will exit the market.
- D) The output of each existing firm will increase.
- E) Economic profit will be zero.

Answer: B

Diff: 3 Type: MC

Topic: Output, Price, and Profit in the Long Run

Source: Study Guide

18) Suppose that the market in which bakeries compete is a perfectly competitive market. Which one of the following reasons does *not* explain why it is difficult for a bakery to make an economic profit in the long run?

- A) All bakeries are price takers.
- B) All bakeries are able to set the market price.
- C) The threat of entry by potential bakeries.
- D) The demand facing each bakery is perfectly elastic.
- E) All bakeries produce identical goods.

Answer: B

Type: MC

Topic: Output, Price, and Profit in the Long Run

Use the table below to answer the following question.

**Table 12.4.1**

<i>Price</i> (dollars per box)	<i>Quantity demanded</i> (thousands of boxes per week)
3.65	500
5.20	450
6.80	400
8.40	350
10.00	300
11.60	250
13.20	200

<b>Quantity</b> (boxes per week)	<b>Marginal cost</b> (dollars per additional box)	<b>Average variable cost</b> (dollars per box)	<b>Average total cost</b> (dollars per box)
200	6.40	7.80	12.80
250	7.00	7.00	11.00
300	7.65	7.10	10.43
350	8.40	7.20	10.06
400	10.00	7.50	10.00
450	12.40	8.00	10.22
500	20.70	9.00	11.00

19) Refer to Table 12.4.1. The top table shows the market demand schedule for paper. The market is perfectly competitive and there are 1,000 firms that produce paper. Each firm has the costs shown in the bottom table when it uses its least-cost plant. The market price in the long run is \_\_\_\_\_ a box and the equilibrium quantity produced in the long run is \_\_\_\_\_ boxes a week.

- A) \$11.60; 250,000
- B) \$7.00; a little less than 400,000
- C) \$10.00; 300,000
- D) \$6.40; a little more than 400,000
- E) \$8.40; 350,000

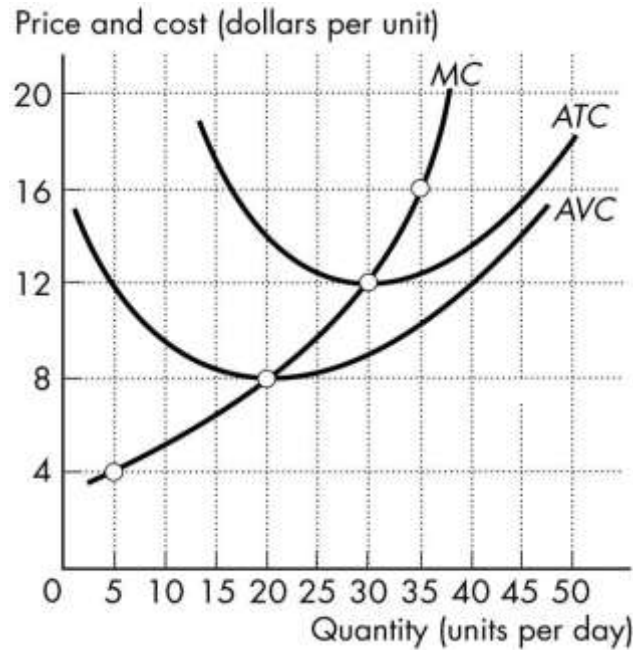
Answer: C

Type: MC

Topic: Output, Price, and Profit in the Long Run

Source: MyEconLab

Use the figure below to answer the following questions.



**Figure 12.4.4**

20) Refer to Figure 12.4.4, which shows the cost curves for a perfectly competitive firm. If all firms in the market have the same cost curves and the price is \$16 per unit,

- A) the market is in long-run equilibrium.
- B) in the long run, firms will leave this market.
- C) in the long run, the price will fall as new firms enter the market.
- D) the firm is making zero economic profit.
- E) none of the above

Answer: C

Type: MC

21) Homer's Holesome Donuts has determined that its profit-maximizing quantity is 10,000 donuts per year. Homer's total revenue from the sale of donuts is \$12,000 a year. Homer's costs are \$16,000 in annual rental payments for its five-year lease on its store and \$5,000 for ingredients. Should Homer's exit the market in the long run?

- A) Yes, because Homer's is incurring an economic loss.
- B) Yes, because all costs are fixed in the long run.
- C) No, because Homer's is covering its variable costs.
- D) No, because Homer's is covering its fixed costs.
- E) No, because all costs are variable in the long run.

Answer: A

Type: MC

## 12.5 Changing Tastes and Advancing Technology

1) Consider a perfectly competitive market with long-run external diseconomies. When demand increases permanently, the equilibrium price

- A) remains constant and the equilibrium quantity increases.
- B) remains constant and the equilibrium quantity decreases.
- C) rises and the equilibrium quantity increases.
- D) falls and the equilibrium quantity decreases.
- E) rises and the equilibrium quantity remains the same.

Answer: C

Diff: 3 Type: MC

Topic: Changing Tastes and Advancing Technology

2) Consider a perfectly competitive market with long-run external economies. When demand increases permanently, the equilibrium price

- A) remains constant and the equilibrium quantity increases.
- B) remains constant and the equilibrium quantity decreases.
- C) rises and the equilibrium quantity decreases.
- D) falls and the equilibrium quantity increases.
- E) falls and the equilibrium quantity remains the same.

Answer: D

Diff: 3 Type: MC

Topic: Changing Tastes and Advancing Technology

3) What is the effect of a permanent increase in demand in a perfectly competitive market, with no external economies or diseconomies?

- A) Market price increases in the long run.
- B) Average cost decreases in the long run.
- C) Market price decreases in the long run.
- D) Average cost increases in the long run.
- E) Market price remains constant in the long run.

Answer: E

Diff: 3 Type: MC

Topic: Changing Tastes and Advancing Technology

4) Technological change spreads through a perfectly competitive market. Choose the statement that is incorrect.

- A) The market price falls and the equilibrium quantity increases.
- B) The technological change brings permanent gains for consumers and producers.
- C) Firms that do not change to the new technology will incur an economic loss and eventually go out of business.
- D) Firms that are quick to adopt to the new technology will make economic profits initially, but in the long run they will make zero economic profit.
- E) Average cost will fall for firms who adopt the new technology.

Answer: B

Diff: 3 Type: MC

Topic: Changing Tastes and Advancing Technology

5) External economies are factors beyond the control of an individual firm which

- A) lower its marginal revenue as market output increases.
- B) raise its costs as market output increases.
- C) lower its costs as market output increases.
- D) lower its economic profit as market output increases.
- E) raise its economic profit as market output increases.

Answer: C

Diff: 2 Type: MC

Topic: Changing Tastes and Advancing Technology

Use the figure below to answer the following question.

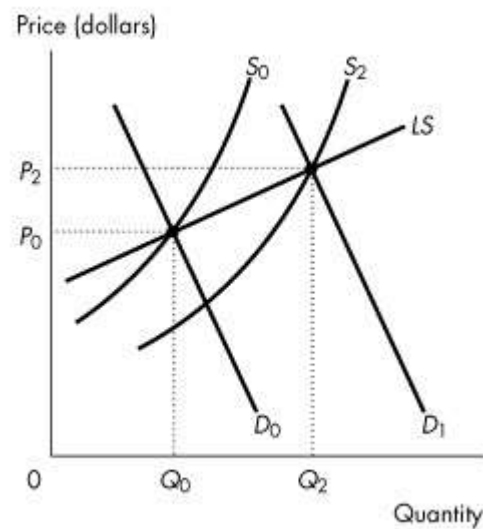


Figure 12.5.1

6) Refer to Figure 12.5.1. Given the increase in market demand from  $D_0$  to  $D_1$ , the graph represents

- A) a constant cost industry.
- B) an increasing cost industry.
- C) a decreasing cost industry.
- D) an inefficient market.
- E) a market experiencing a technological change.

Answer: B

Diff: 2 Type: MC

Topic: Changing Tastes and Advancing Technology

- 7) The long-run market supply curve is positively sloped when
- A) external economies exist.
  - B) external diseconomies exist.
  - C) neither external economies nor diseconomies exist.
  - D) external costs exist.
  - E) external benefits exist.

Answer: B

Diff: 2 Type: MC

Topic: Changing Tastes and Advancing Technology

- 8) The long-run market supply curve is negatively sloped if
- A) external economies exist.
  - B) external diseconomies exist.
  - C) neither external economies nor diseconomies exist.
  - D) external costs exist.
  - E) external benefits exist.

Answer: A

Diff: 2 Type: MC

Topic: Changing Tastes and Advancing Technology

- 9) Which one of the following is *not* true of a new long-run equilibrium which is the result of a new technology in a perfectly competitive market?
- A) The equilibrium price falls.
  - B) Industry output increases.
  - C) Economic profit of each firm remaining in the industry increases.
  - D) All firms in the industry use the new technology.
  - E) Average total cost decreases.

Answer: C

Diff: 2 Type: MC

Topic: Changing Tastes and Advancing Technology

Source: Study Guide

- 10) If a market experiences external economies, the long-run market supply
- A) is perfectly inelastic.
  - B) is perfectly elastic.
  - C) curve has a positive slope.
  - D) curve has a negative slope.
  - E) has allocative inefficiency.

Answer: D

Diff: 2 Type: MC

Topic: Changing Tastes and Advancing Technology

Source: Study Guide

11) If a market experiences external diseconomies, the long-run market supply

- A) is perfectly inelastic.
- B) is perfectly elastic.
- C) curve has a positive slope.
- D) curve has a negative slope.
- E) curve is vertical.

Answer: C

Diff: 2 Type: MC

Topic: Changing Tastes and Advancing Technology

12) A perfectly competitive market, with no external economies or diseconomies, is initially in long-run equilibrium. There is a permanent decrease in demand. After adjustment to the new long-run equilibrium

- A) the remaining firms in the market will each be producing more output than previously.
- B) the remaining firms in the market will each be producing less output than previously.
- C) the remaining firms in the market will each be producing the same output as previously.
- D) the remaining firms in the market may each be producing more output than previously, depending on the size of the change in demand.
- E) the remaining firms in the market will each be producing either the same or more output than previously.

Answer: C

Type: MC

Topic: Changing Tastes and Advancing Technology

13) A perfectly competitive market, with no external economies or diseconomies, is initially in long-run equilibrium. There is a permanent increase in demand. After adjustment to the new long-run equilibrium

- A) the remaining firms in the market will each be producing more output than previously.
- B) the remaining firms in the market will each be producing less output than previously.
- C) the remaining firms in the market will each be producing the same output as previously.
- D) the remaining firms in the market may each be producing more output than previously, depending on the size of the change in demand.
- E) the remaining firms in the market will each be producing either the same or more output than previously.

Answer: C

Type: MC

Topic: Changing Tastes and Advancing Technology

14) A market with constant costs is in long-run equilibrium when it experiences a permanent increase in demand.

In the short run, firms in the market \_\_\_\_\_. In the long run, some firms \_\_\_\_\_ the market.

- A) make zero economic profit; exit
- B) make an economic profit; enter
- C) incur an economic loss; exit
- D) make zero economic profit; enter
- E) none of the above

Answer: B

Type: MC

Topic: Changing Tastes and Advancing Technology

Source: MyEconLab

15) A market with constant costs is in long-run equilibrium when it experiences a permanent increase in demand.

Market supply \_\_\_\_\_ and the market price \_\_\_\_\_.

Market output \_\_\_\_\_ and in the long run each remaining firm makes \_\_\_\_\_ profit.

- A) increases; falls until it reaches each firms' minimum average total cost; increases; zero economic
- B) decreases; rises until it reaches each firms' minimum average variable cost; decreases; zero economic
- C) increases; falls; increases; an economic
- D) decreases; rises until it reaches each firms' minimum average total cost; decreases; an economic
- E) increases; does not change; increases; zero economic

Answer: A

Type: MC

Topic: Changing Tastes and Advancing Technology

Source: MyEconLab

16) A market with constant costs is in long-run equilibrium when it experiences a permanent decrease in demand.

In the short run, firms in the market \_\_\_\_\_.

In the long run, some firms \_\_\_\_\_ the market.

Market supply \_\_\_\_\_ and the market price \_\_\_\_\_.

Market output \_\_\_\_\_ and in the long run each remaining firm makes \_\_\_\_\_ profit.

A) incur an economic loss; exit; decreases; rises until it reaches the firms' minimum average total cost; decreases; zero economic

B) make zero economic profit; enter; increases; falls; increases; an economic

C) incur an economic loss; exit; decreases; rises until it reaches the firms' minimum average total cost; decreases; an economic

D) make zero economic profit; exit; decreases; rises until it reaches the firms' minimum average variable cost; decreases; an economic

E) make an economic profit; enter; increases; falls; increases; economic profit

Answer: A

Type: MC

Topic: Changing Tastes and Advancing Technology

Source: MyEconLab

17) Initially, a perfectly competitive market that has 1,000 firms is in long-run equilibrium. Then 100 firms in the industry adopt a new technology that reduces the average cost of producing the good. In the short run, the price \_\_\_\_\_, firms with the new technology make \_\_\_\_\_ economic profit, and firms with the old technology \_\_\_\_\_.

A) remains the same; zero; incur an economic loss

B) remains the same; positive; break even

C) falls; positive; incur an economic loss

D) remains the same; positive; incur an economic loss

E) falls; break even; incur an economic loss

Answer: C

Type: MC

## 12.6 Competition and Efficiency

1) Which one of the following need *not* be satisfied to achieve allocative efficiency?

- A) Marginal social cost equals marginal social benefit.
- B) The sum of consumer surplus and producer surplus is maximized.
- C) Price equals marginal social benefit.
- D) Price equals marginal social cost.
- E) Only high-quality goods are produced.

Answer: E

Diff: 3 Type: MC

Topic: Competition and Efficiency

2) All of the following statements are true *except*

- A) consumers allocate their budgets to get the most value possible.
- B) we derive a consumer's demand curve by finding how the best budget allocation changes as the price of a good changes.
- C) firms get the most value out of their resources at every point along a consumer's demand curve.
- D) a competitive equilibrium achieves an efficient outcome.
- E) when firms in perfect competition are away from the long-run equilibrium, the market is still efficient.

Answer: C

Diff: 2 Type: MC

Topic: Competition and Efficiency

3) An efficient allocation is achieved when

- A) consumers are selecting points on their demand curves.
- B) producers are selecting points on their supply curves.
- C) the sum of consumer surplus and producer surplus is maximized.
- D) all of the above.
- E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: Competition and Efficiency

4) Resources are used efficiently when

- A) consumers are on their marginal benefit curves.
- B) firms are economically efficient.
- C) price equals marginal social benefit equals marginal social cost.
- D) there are no external benefits or external costs.
- E) all of the above.

Answer: E

Diff: 2 Type: MC

Topic: Competition and Efficiency

Source: Study Guide

5) Producers choose \_\_\_\_\_.

Producers are efficient on the market supply curve because \_\_\_\_\_.

- A) to produce a good or service only if they will receive a producer surplus; every point on the market supply curve maximizes producer surplus
- B) to maximize profit; on the market supply curve scarcity is eliminated
- C) to produce goods and services made with the newest technology; the market supply curve traces out the same path as a firm's marginal cost curve
- D) to maximize profit; we derive the firm's supply curve by finding the profit-maximizing quantity at each price
- E) to produce goods and services made with the newest technology; every point on the market supply curve shows the marginal cost of production using new technology

Answer: D

Type: MC

Topic: Competition and Efficiency

Source: MyEconLab

6) Consumers choose \_\_\_\_\_.

Consumers are efficient on the market demand curve because \_\_\_\_\_.

- A) to maximize profit; they only purchase goods and services that they can afford
- B) to buy a good or service only if they will receive a consumer surplus; every point on the market demand curve maximizes consumer surplus
- C) to purchase goods and services made with the newest technology; the market demand curve traces out the same path as the marginal revenue curve
- D) to allocate their budgets to get the most value possible out of them; we derive a consumer's demand curve by finding how the best budget allocation changes as the price of a good changes
- E) to allocate their budgets to get the most value possible out of them; they only purchase goods and services that they can afford

Answer: D

Type: MC

Topic: Competition and Efficiency

Source: MyEconLab

7) In a competitive market, the market demand curve measures the \_\_\_\_\_ if \_\_\_\_\_ exist.

In a competitive market, the market supply curve measures the \_\_\_\_\_ if \_\_\_\_\_ exist.

- A) marginal social benefit; no external costs; marginal social cost; no external benefits
- B) firms' marginal benefit; external benefits; consumers' marginal cost; external costs
- C) marginal social benefit; no external benefits; marginal social cost; no external costs
- D) marginal social benefit; external benefits; marginal social cost; external costs
- E) consumer surplus; external benefits; producer surplus; external costs

Answer: C

Type: MC

Topic: Competition and Efficiency

Source: MyEconLab

8) Choose the correct statement.

- A) Resources are used efficiently when marginal social benefit equals marginal social cost.
- B) Competitive equilibrium achieves an efficient outcome.
- C) Competitive equilibrium maximizes the gains from trade.
- D) When firms in perfect competition are away from long-run equilibrium, either entry or exit is taking place and the market is still efficient.
- E) All of the above

Answer: E

Type: MC

## Chapter 13 Monopoly

### 13.1 Monopoly and How It Arises

1) An exclusive right granted to a firm to supply a good or service is

- A) a licence.
- B) a patent.
- C) a public franchise.
- D) the essential characteristic of natural monopoly.
- E) an economy of scale.

Answer: C

Diff: 1 Type: MC

Topic: Monopoly and How It Arises

2) A natural monopoly exists when

- A) the government protects the firm by granting an exclusive franchise.
- B) production can take place with constant returns to scale.
- C) there are no rivals in the market.
- D) one firm can supply the entire market at a lower cost than two or more firms.
- E) the average total cost curve is upward sloping.

Answer: D

Diff: 1 Type: MC

Topic: Monopoly and How It Arises

3) In a natural monopoly, the long-run average cost curve

- A) is downward sloping in the relevant range of output levels.
- B) is horizontal in the relevant range of output levels.
- C) is upward sloping in the relevant range of output levels.
- D) may be either upward sloping or downward sloping in the relevant range of output levels.
- E) lies below the marginal cost curve.

Answer: A

Diff: 2 Type: MC

Topic: Monopoly and How It Arises

4) Which one of the following is an example of a natural barrier to entry of new firms into an industry?

- A) licensing of professions

- B) economies of scale
- C) issuing a patent
- D) a public franchise
- E) all of the above

Answer: B

Diff: 2 Type: MC

Topic: Monopoly and How It Arises

Source: Study Guide

- 5) To prevent monopoly from arising, there must be
- A) a single supplier of a good in the market.
  - B) no close substitutes for the good.
  - C) barriers preventing entry of other firms.
  - D) freedom of entry into the market.
  - E) economies of scale.

Answer: D

Diff: 2 Type: MC

Topic: Monopoly and How It Arises

- 6) Suppose in an industry a firm realizes economies of scale over the entire length of its *LRAC* curve. In this situation, the firm is
- A) a natural monopoly.
  - B) a fixed-cost monopoly.
  - C) an output-discriminating monopoly.
  - D) a perfect-price discriminating monopoly.
  - E) a constant total variable cost monopoly.

Answer: A

Diff: 2 Type: MC

Topic: Monopoly and How It Arises

- 7) Which of the following is *least* likely to be a *natural monopoly*?

- A) subway services
- B) electric utilities
- C) water and sewer services
- D) taxicab service
- E) cable television services

Answer: D

Diff: 2 Type: MC

Topic: Monopoly and How It Arises

- 8) A single-price monopoly is a firm that \_\_\_\_\_ each unit of its output \_\_\_\_\_. A \_\_\_\_\_ monopoly sells different units of a good or service for different prices.

- A) produces; at a constant cost; discriminatory
- B) must sell; for the same price to all its customers; price-discriminating
- C) produces; at a constant cost; price-discriminating
- D) must sell; for the same price to all its customers; discriminatory
- E) must sell; at the same price as a perfectly competitive firm; price-discriminating

Answer: B

Diff: 2 Type: MC

Topic: Monopoly and How It Arises

Source: MyEconLab

9) Canada Post has a monopoly on residential mail delivery. Pfizer Inc. makes LIPITOR, a prescription drug that lowers cholesterol. Rogers Communications is the sole provider of cable television service in some parts of Ontario. The monopolies which are legal monopolies are \_\_\_\_\_.

- A) only Pfizer
- B) Canada Post, Pfizer, and Rogers Communications
- C) Canada Post and Pfizer
- D) only Canada Post
- E) none of the above

Answer: C

Diff: 2 Type: MC

Topic: Monopoly and How It Arises

Source: MyEconLab

10) Canada Post has a monopoly on residential mail delivery. Pfizer Inc. makes LIPITOR, a prescription drug that lowers cholesterol. Rogers Communications is the sole provider of cable television service in some parts of Ontario. The monopolies which profit from price discrimination are \_\_\_\_\_.

- A) Canada Post and Rogers Communications
- B) only Pfizer
- C) only Canada Post
- D) all three monopolies
- E) none of the above

Answer: D

Diff: 2 Type: MC

Topic: Monopoly and How It Arises

Source: MyEconLab

11) A monopoly arises for two key reasons, which are \_\_\_\_\_.

- A) barriers to entry and no close substitutes
- B) franchises and barriers to entry
- C) barriers to entry and close substitutes
- D) close substitutes and no barriers to entry
- E) natural and legal

Answer: A

Type: MC

Topic: Monopoly and How It Arises

Skill: Recognition

AACSB: Reflective Thinking

- 12) A monopoly is a market with a single firm that
- A) produces a good or service for which no close substitute exists and which is protected by a barrier that prevents other firms from selling that good or service.
  - B) purchases its factors of production from only one supplier because of a barrier preventing it from buying from other suppliers.
  - C) produces a good or service for which no close substitute exists and that sells all its output to one buyer because there is barrier preventing other buyers from purchasing the good or service.
  - D) cannot control the price it sets for its good or service because there is barrier that prevents the firm from changing the price.
  - E) produces its good or service using labour from a single source, which is usually a union.

Answer: A

Type: MC

Topic: Monopoly and How It Arises

Skill: Recognition

AACSB: Reflective Thinking

- 13) Firms that can price discriminate between customers do so to \_\_\_\_\_.
- A) increase consumer surplus
  - B) increase employment
  - C) increase economic profit
  - D) decrease the quantity they produce
  - E) increase producer surplus and deadweight loss

Answer: C

Type: MC

Topic: Monopoly and How It Arises

Skill: Recognition

AACSB: Reflective Thinking

- 14) Which one of the following is *most* likely to be a natural monopoly?
- A) sandwich shops
  - B) printing services
  - C) welding services
  - D) automotive service
  - E) electric utilities

Answer: E

Diff: 1 Type: MC

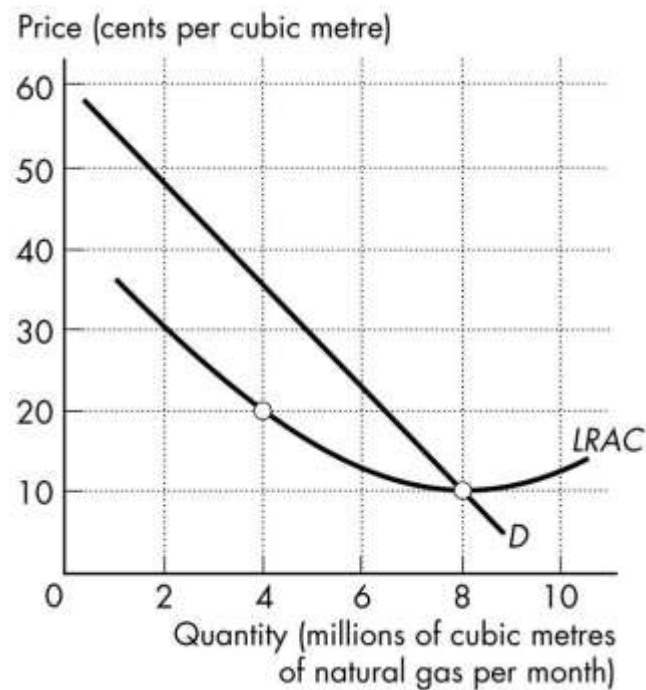
Topic: Monopoly Regulation

15) When Dominant Pizza is willing to sell a pizza to a student who lives on-campus at a lower price than it sells the identical pizza to a student who lives a block away from the campus, the pizza firm is

- A) implementing unfair pricing practices.
- B) incurring a loss on on-campus sales.
- C) eliminating all competition.
- D) located close to the campus.
- E) practising price discrimination.

Answer: E

Type: MC



**Figure 13.1.1**

16) Refer to Figure 13.1.1. The quantity demanded by the market is 8 million cubic metres a month. This market is

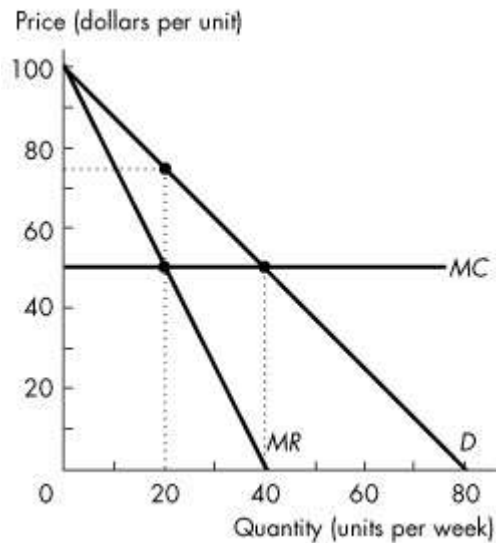
- A) a legal monopoly.
- B) served by a perfect price discriminating monopoly.
- C) served by many firms each making an economic profit.
- D) served by many firms each incurring an economic loss.
- E) a natural monopoly.

Answer: E

Type: MC

## 13.2 A Single-Price Monopoly's Output and Price Decision

Use the figure below to answer the following question.



**Figure 13.2.1**

1) Refer to Figure 13.2.1. This single-price monopoly produces \_\_\_\_\_ units per day and charges a price of \$\_\_\_\_\_ per unit.

- A) zero; 0
- B) 20; 75
- C) 40; 50
- D) 20; 50
- E) 20; 20

Answer: B

Diff: 2 Type: MC

Topic: A Single-Price Monopoly's Output and Price Decision

2) To increase sales from 7 units to 8 units, a single-price monopolist must drop the price from \$7 per unit to \$6 per unit. What is marginal revenue in this range?

- A) \$48
- B) \$6
- C) \$1
- D) -\$1
- E) None of the above.

Answer: D

Diff: 2 Type: MC

Topic: A Single-Price Monopoly's Output and Price Decision

Source: Study Guide

Use the figure below to answer the following questions.

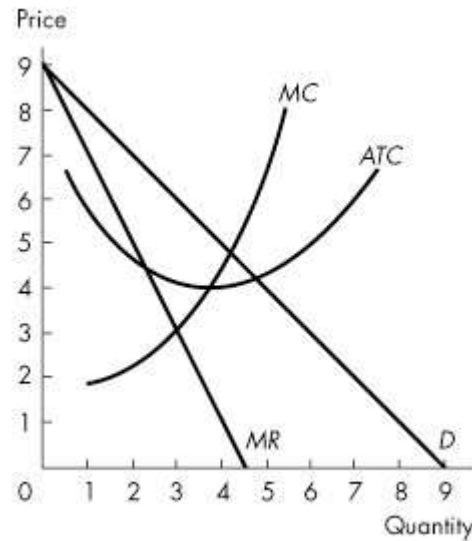


Figure 13.2.2

3) For the single-price monopoly shown in Figure 13.2.2, when profit is maximized, quantity is

- A) 3 and price is \$3.
- B) 3 and price is \$6.
- C) 4 and price is \$4.
- D) 4 and price is \$5.
- E) 5 and price is \$4.

Answer: B

Diff: 2 Type: MC

Topic: A Single-Price Monopoly's Output and Price Decision

Source: Study Guide

4) Refer to Figure 13.2.2. If the single-price monopoly shown in Figure 13.2.2 is maximizing profit, what is total economic profit?

- A) \$3
- B) \$4
- C) \$6
- D) \$9
- E) None of the above.

Answer: C

Diff: 2 Type: MC

Topic: A Single-Price Monopoly's Output and Price Decision

Source: Study Guide

5) If a profit-maximizing monopoly is producing an output at which marginal cost exceeds marginal revenue, it

- A) should raise price and decrease output.
- B) should lower price and increase output.
- C) should lower price and decrease output.
- D) is incurring an economic loss.
- E) is maximizing profit.

Answer: A

Diff: 2 Type: MC

Topic: A Single-Price Monopoly's Output and Price Decision

Source: Study Guide

Use the figure below to answer the following questions.

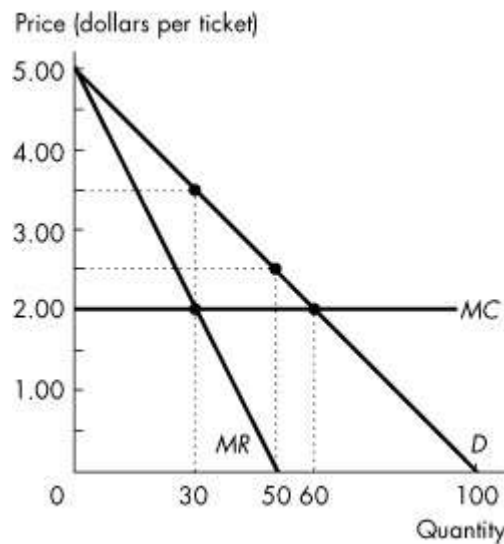


Figure 13.2.3

6) Refer to Figure 13.2.3. Assume this firm is a single-price monopoly. What is the profit-maximizing price to charge for the tickets?

- A) \$5.00
- B) \$4.00
- C) \$3.00
- D) \$2.00
- E) \$3.50

Answer: E

Diff: 2 Type: MC

Topic: A Single-Price Monopoly's Output and Price Decision

7) Refer to Figure 13.2.3. Assume this firm is a single-price monopoly. How many tickets does this monopolist sell to maximize economic profit?

- A) 20 tickets
- B) 30 tickets
- C) 50 tickets
- D) 60 tickets
- E) 100 tickets

Answer: B

Diff: 2 Type: MC

Topic: A Single-Price Monopoly's Output and Price Decision

Use the figure below to answer the following question.

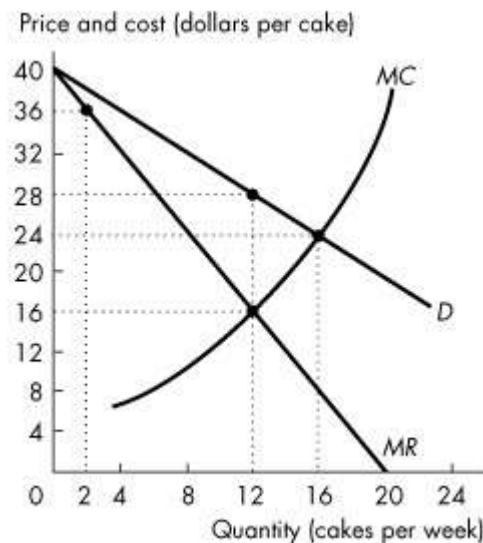


Figure 13.2.4

8) Refer to Figure 13.2.4. Grannie's is the only cake bakery on Coastal Island. The graph shows Grannie's demand curve, marginal revenue curve, and marginal cost curve. Grannie's profit-maximizing price is \_\_\_\_\_ a cake and its profit-maximizing output is \_\_\_\_\_ cakes a week.

- A) \$28; 12
- B) \$16; 12
- C) \$36; 2
- D) \$16; 24
- E) \$24; 16

Answer: A

Diff: 2 Type: MC

Topic: A Single-Price Monopoly's Output and Price Decision

Source: MyEconLab

- 9) A monopoly \_\_\_\_\_ make positive economic profit in the long run because \_\_\_\_\_.
- A) can; barriers to entry prevent other firms from entering the market and sharing the profit
  - B) cannot; eventually demand will decrease and prices will fall
  - C) cannot; other firms will enter the market until all firms are making zero economic profit
  - D) can; new technology constantly lowers costs for the monopoly firm and for its competitors
  - E) can; demand constantly increases and price constantly rises

Answer: A

Diff: 2 Type: MC

Topic: A Single-Price Monopoly's Output and Price Decision

Source: MyEconLab

*Use the table below to answer the following question.*

**Table 13.2.1**

Price (dollars per bottle)	Quantity Demanded (bottles per hour)
10	0
8	1
6	2
4	3
2	4
0	5

- 10) Refer to Table 13.2.1. Minnie's Mineral Springs, a single-price monopoly, faces the market demand schedule given in the table. Minnie will not produce a quantity at which the market demand for water is inelastic because when demand is inelastic she can \_\_\_\_\_ the quantity produced, which \_\_\_\_\_.
- A) increase; increases total revenue, decreases total cost, and increases economic profit
  - B) increase; increases total revenue and increases total cost, but the increase in total cost is less than the increase in total revenue
  - C) decrease; increases total revenue, decreases total cost, and increases economic profit
  - D) decrease; decreases total revenue and decreases total cost, but the decrease in total cost is less than the decrease in total revenue
  - E) decrease; increases total revenue, does not change total cost, and increases economic profit

Answer: C

Diff: 2 Type: MC

Topic: A Single-Price Monopoly's Output and Price Decision

Source: MyEconLab

- 11) A single-price monopolist's demand curve
- A) is its marginal revenue curve.
  - B) shows that demand for the good is perfectly elastic.
  - C) is the same as the market demand curve.
  - D) shows that demand for the good is perfectly inelastic.
  - E) is horizontal.

Answer: C

Type: MC

Topic: A Single-Price Monopoly's Output and Price Decision

Skill: Recognition

AACSB: Reflective Thinking

- 12) For a single-price monopoly, the demand curve is

- A) below the marginal revenue curve.
- B) the same as the marginal revenue curve.
- C) above the marginal revenue curve.
- D) the same as the total revenue curve.
- E) below the average total cost curve.

Answer: C

Type: MC

Topic: A Single-Price Monopoly's Output and Price Decision

Skill: Recognition

AACSB: Reflective Thinking

- 13) The marginal revenue curve for a single-price monopoly

- A) is below its demand curve.
- B) is the same as the demand curve.
- C) lies above its demand curve.
- D) is horizontal.
- E) has a slope equal to the slope of the demand curve.

Answer: A

Type: MC

Topic: A Single-Price Monopoly's Output and Price Decision

Skill: Recognition

AACSB: Reflective Thinking

- 14) If marginal revenue equals zero, then demand at this level of output is

- A) perfectly inelastic.
- B) inelastic.
- C) unit elastic.
- D) elastic.
- E) perfectly elastic.

Answer: C

Type: MC

Topic: A Single-Price Monopoly's Output and Price Decision

Skill: Conceptual

AACSB: Reflective Thinking

15) If the demand for its good or service is elastic, a monopoly's

- A) total revenue is unchanged when the firm lowers its price.
- B) total revenue decreases when the firm lowers its price.
- C) marginal revenue is positive.
- D) marginal revenue is zero.
- E) marginal revenue is negative.

Answer: C

Type: MC

Topic: A Single-Price Monopoly's Output and Price Decision

Skill: Conceptual

AACSB: Reflective Thinking

16) If the demand for its good or service is inelastic, a monopoly's

- A) total revenue increases when the firm lowers its price.
- B) total revenue is unchanged when the firm lowers its price.
- C) marginal revenue is negative.
- D) marginal revenue is equal to zero.
- E) marginal revenue is positive.

Answer: C

Type: MC

Topic: A Single-Price Monopoly's Output and Price Decision

Skill: Conceptual

AACSB: Reflective Thinking

17) A monopoly

- A) faces a perfectly elastic demand.
- B) ignores the demand curve because it is the only seller.
- C) can raise the price it charges only if it decreases the quantity that it sells.
- D) can raise the price it charges only if it increases the quantity that it sells.
- E) faces a perfectly inelastic demand.

Answer: C

Type: MC

18) A single-price monopolist

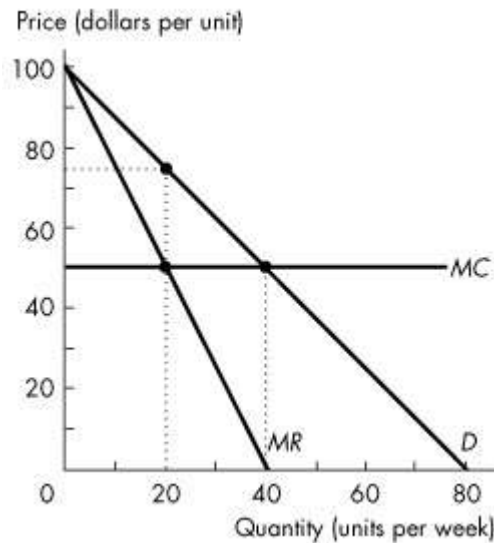
- A) maximizes economic profit by producing the quantity at which marginal revenue equals marginal cost.
- B) maximizes economic profit by producing the quantity at which marginal revenue equals average total cost.
- C) can increase the price and the quantity sold simultaneously.
- D) is not restricted by the law of demand.
- E) can sell as much as it wants at a given price because it is the only seller.

Answer: A

Type: MC

### 13.3 Single-Price Monopoly and Competition Compared

Use the figure below to answer the following questions.



**Figure 13.3.1**

1) Refer to Figure 13.3.1. If this market were perfectly competitive, the output level would exceed the single-price monopoly output level by

- A) 20 units.
- B) 40 units.
- C) 60 units.
- D) zero. The perfectly competitive firm and the single-price monopoly produce the same quantity because marginal cost is constant.
- E) 30 units.

Answer: A

Diff: 3 Type: MC

Topic: Single-Price Monopoly and Competition Compared

2) Refer to Figure 13.3.1. The efficient quantity is

- A) 20 units.
- B) 40 units.
- C) 60 units.
- D) 80 units.
- E) zero units.

Answer: B

Diff: 2 Type: MC

Topic: Single-Price Monopoly and Competition Compared

- 3) Refer to Figure 13.3.1. If this market is a single-price monopoly, then
- A) it is efficient because the monopoly is maximizing economic profit.
  - B) price is equal to marginal cost and the outcome is efficient.
  - C) price is less than marginal cost, and consumer surplus is less than in a perfectly competitive market.
  - D) price is greater than the marginal cost and the outcome is inefficient.
  - E) the outcome is inefficient because the monopoly's costs are too high.

Answer: D

Diff: 2 Type: MC

Topic: Single-Price Monopoly and Competition Compared

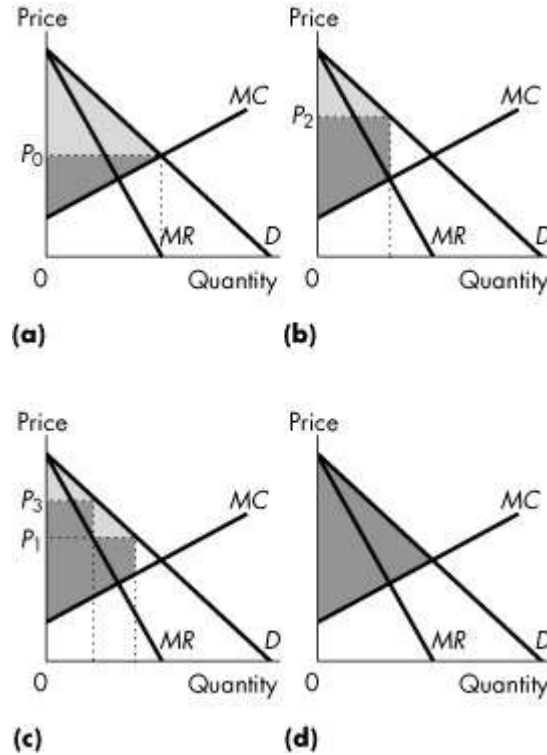
- 4) The pursuit of wealth by capturing economic rent
- A) is rent seeking.
  - B) is illegal in Canada.
  - C) is price discrimination.
  - D) creates a legal monopoly.
  - E) creates a natural monopoly.

Answer: A

Diff: 1 Type: MC

Topic: Single-Price Monopoly and Competition Compared

Use the figure below to answer the following questions.



**Figure 13.3.2**

5) Consider Figure 13.3.2. Consider a perfectly competitive market. If the light grey area shows the consumer surplus, and the dark grey area shows the producer surplus, which graph correctly represents this market?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (b) and (d)

Answer: A

Diff: 3 Type: MC

Topic: Single-Price Monopoly and Competition Compared

6) Consider Figure 13.3.2. Consider a single-price monopoly. If the light grey area shows the consumer surplus, and the dark grey area shows the producer surplus, which graph correctly represents this firm?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (b) and (c)

Answer: B

Diff: 3 Type: MC

Topic: Single-Price Monopoly and Competition Compared

7) Taking competitive rent seeking activity into account, the social cost of monopoly is equal to the

- A) deadweight loss from monopoly.
- B) monopoly's producer surplus.
- C) deadweight loss plus the monopoly's producer surplus.
- D) deadweight loss minus the monopoly's producer surplus.
- E) consumer surplus lost plus producer surplus lost.

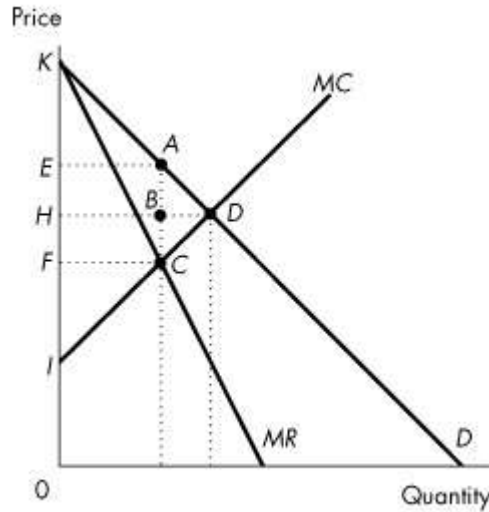
Answer: C

Diff: 3 Type: MC

Topic: Single-Price Monopoly and Competition Compared

Source: Study Guide

Use the figure below to answer the following questions.



**Figure 13.3.3**

8) Consider the market demand curve in Figure 13.3.3. If the market is perfectly competitive, which area indicates consumer surplus?

- A) *AEK*
- B) *DHK*
- C) *DIK*
- D) *DIH*
- E) None of the above.

Answer: B

Diff: 3 Type: MC

Topic: Single-Price Monopoly and Competition Compared

Source: Study Guide

9) Consider the market demand curve in Figure 13.3.3. If the market is perfectly competitive, which area indicates producer surplus?

- A) *AEK*
- B) *DHK*
- C) *DIK*
- D) *DIH*
- E) None of the above.

Answer: D

Diff: 3 Type: MC

Topic: Single-Price Monopoly and Competition Compared

Source: Study Guide

10) Consider the market demand curve in Figure 13.3.3. If the market is perfectly competitive, which area indicates the deadweight loss?

- A) *ABD*
- B) *BCD*
- C) *KDI*
- D) *ADC*
- E) None of the above.

Answer: E

Diff: 3 Type: MC

Topic: Single-Price Monopoly and Competition Compared

11) Consider the revenue and cost curves in Figure 13.3.3. If this is a single-price monopoly, what is consumer surplus?

- A) *EADH*
- B) *EABH*
- C) *ABD*
- D) *ACD*
- E) *KEA*

Answer: E

Diff: 3 Type: MC

Topic: Single-Price Monopoly and Competition Compared

12) Consider the revenue and cost curves in Figure 13.3.3. What is the difference in consumer surplus between a single-price monopoly and a perfectly competitive market?

- A) *EADH*
- B) *EABH*
- C) *ABD*
- D) *ACD*
- E) *FHDC*

Answer: A

Diff: 3 Type: MC

Topic: Single-Price Monopoly and Competition Compared

13) Consider the revenue and cost curves in Figure 13.3.3. If this is a single-price monopoly, what area is producer surplus?

- A) *IHD*
- B) *KHD*
- C) *KEA*
- D) *IEAC*
- E) None of the above.

Answer: D

Diff: 3 Type: MC

Topic: Single-Price Monopoly and Competition Compared

14) Consider the revenue and cost curves in Figure 13.3.3. What is the difference in producer surplus between a single-price monopoly and a perfectly competitive market?

- A)  $EADH$
- B)  $EABH$
- C)  $ABD$
- D)  $ACD$
- E)  $EABH - BCD$

Answer: E

Diff: 3 Type: MC

Topic: Single-Price Monopoly and Competition Compared

15) Refer to Figure 13.3.3. What is the redistribution of surplus from consumers to the producer with a single-price monopoly, as compared to a perfectly competitive market?

- A)  $EADH$
- B)  $EABH$
- C)  $ABD$
- D)  $ACD$
- E)  $EABH - BCD$

Answer: B

Diff: 3 Type: MC

Topic: Single-Price Monopoly and Competition Compared

16) Consider the cost and revenue curves in Figure 13.3.3. Which area indicates the deadweight loss from a single-price monopoly?

- A)  $EACF$
- B)  $ACD$
- C)  $ABD$
- D)  $BCD$
- E) None of the above.

Answer: B

Diff: 3 Type: MC

Topic: Single-Price Monopoly and Competition Compared

Source: Study Guide

17) Rent seeking \_\_\_\_\_.

- A) is a variable cost and with rent seeking the monopoly becomes more efficient
- B) decreases average total cost and with rent seeking the monopoly becomes more efficient
- C) increases deadweight loss above the original monopoly deadweight loss, but the monopoly continues to produce the same inefficient quantity
- D) decreases consumer surplus and with rent seeking the monopoly becomes more efficient
- E) decreases deadweight loss

Answer: C

Diff: 3 Type: MC

Topic: Single-Price Monopoly and Competition Compared

Source: MyEconLab

18) Consumer surplus is

- A) positive in the case of a monopolist practising perfect price discrimination.
- B) equal to price minus marginal cost.
- C) less in the case of a single-price monopoly than in the case of a perfectly competitive industry.
- D) zero for a single-price monopolist.
- E) greater in a single-price monopoly than in a perfectly competitive industry.

Answer: C

Type: MC

Topic: Single-Price Monopoly and Competition Compared

Skill: Recognition

AACSB: Reflective Thinking

19) The creation of a monopoly results in gains to

- A) producers at no expense to consumers.
- B) consumers at no expense to producers.
- C) producers at the expense of consumers.
- D) consumers at the expense of producers.
- E) producers and consumers at the expense of the government.

Answer: C

Type: MC

Topic: Single-Price Monopoly and Competition Compared

Skill: Conceptual

AACSB: Reflective Thinking

20) Rent seeking is best defined as

- A) an attempt by landlords to get tenants.
- B) the pursuit of wealth by capturing economic rent.
- C) an attempt by individuals to avoid paying taxes.
- D) owners of a monopoly selling the firm at the highest possible price.
- E) none of the above.

Answer: B

Type: MC

Topic: Single-Price Monopoly and Competition Compared

Skill: Recognition

AACSB: Reflective Thinking

21) Methods of rent seeking include which of the following?

- I. Buying a monopoly
  - II. Creating a monopoly
  - III. Price discrimination
- A) I and II
  - B) I and III
  - C) II and III
  - D) III only
  - E) II only

Answer: A

Type: MC

Topic: Single-Price Monopoly and Competition Compared

Skill: Recognition

AACSB: Reflective Thinking

22) Which one of the following is *true* for a single-price monopolist but not for a perfectly competitive firm?

- A) The firm maximizes profit by setting marginal cost equal to marginal revenue.
- B) The firm is a price-taker.
- C) The firm can sell any level of output at any price it sets.
- D) The firm's marginal cost is less than price.
- E) The firm's marginal revenue curve is horizontal.

Answer: D

Diff: 2 Type: MC

Topic: Single-Price Monopoly and Competition Compared

Use the figure below to answer the following questions.

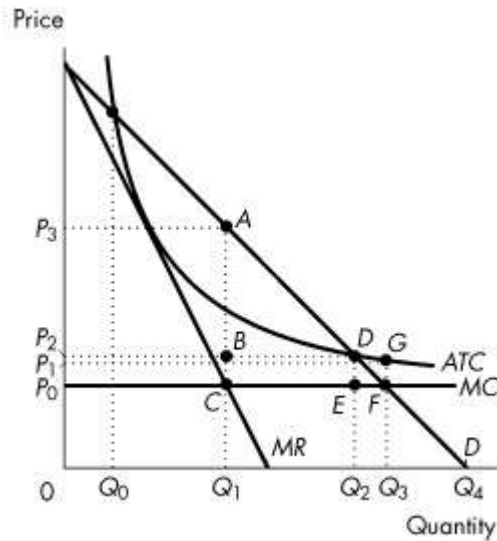


Figure 13.3.4

23) Consider the natural monopoly depicted in Figure 13.3.4. Total surplus is at a maximum when quantity is

- A)  $Q_1$  and price is  $P_1$ .
- B)  $Q_1$  and price is  $P_3$ .
- C)  $Q_2$  and price is  $P_2$ .
- D)  $Q_3$  and price is  $P_0$ .
- E)  $Q_4$  and price is 0.

Answer: D

Diff: 3 Type: MC

Topic: Single-Price Monopoly and Competition Compared

24) Consider the natural monopoly depicted in Figure 13.3.4. What area in the graph represents the deadweight loss arising from an unregulated monopoly?

- A)  $ABD$
- B)  $DGF$
- C)  $DEF$
- D)  $ACF$
- E)  $CBDE$

Answer: D

Diff: 3 Type: MC

Topic: Single-Price Monopoly and Competition Compared

- 25) One difference between perfectly competitive markets and a single-price monopoly is that
- A) marginal revenue equals marginal cost for perfectly competitive firms, but not for single-price monopolists.
  - B) marginal cost equals average variable cost for perfectly competitive firms but not for single-price monopolists.
  - C) price equals minimum average total cost for single-price monopolists but not for perfectly competitive firms.
  - D) marginal revenue equals price for perfectly competitive firms, but not for single-price monopolists.
  - E) none of the above

Answer: D

Type: MC

26) Which of the following markets will have the largest deadweight loss?

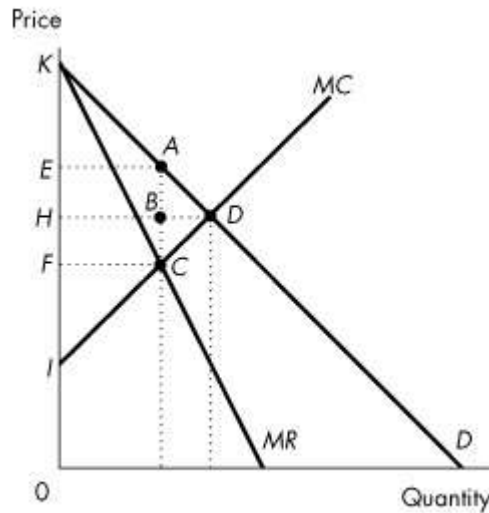
- A) a single-price monopoly
- B) a perfectly competitive market
- C) a perfectly price discriminating monopoly
- D) both B and C
- E) both A and C

Answer: A

Type: MC

## 13.4 Price Discrimination

Use the figure below to answer the following question.



**Figure 13.4.1**

1) Which area in Figure 13.4.1 indicates the deadweight loss from a perfect price-discriminating monopoly?

- A)  $EACF$
- B)  $ACD$
- C)  $ABD$
- D)  $BCD$
- E) None of the above.

Answer: E

Diff: 3 Type: MC

Topic: Price Discrimination

Source: Study Guide

2) When perfect price discrimination occurs, which one of the following statements is *false* ?

- A) Buyers cannot resell the product.
- B) The firm can distinguish between buyers.
- C) The firm sets prices.
- D) The firm captures consumer surplus.
- E) The outcome is less efficient than with single-price monopoly.

Answer: E

Diff: 3 Type: MC

Topic: Price Discrimination

Source: Study Guide

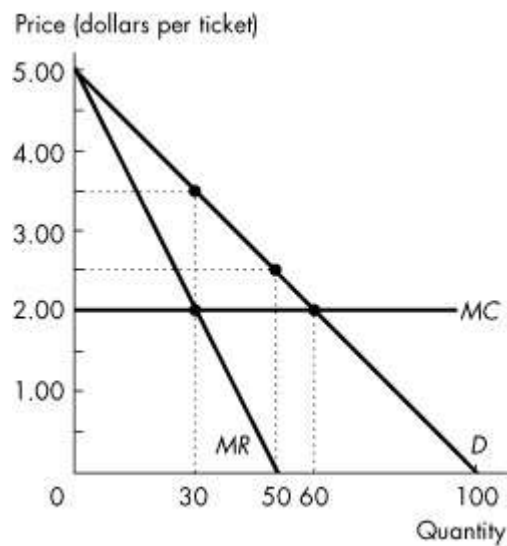
- 3) A monopoly can practise price discrimination when it
- A) can segment the market according to the different prices the consumers are willing to pay.
  - B) is a price taker.
  - C) has different marginal costs of production for different output levels.
  - D) has decreasing average variables cost.
  - E) produces a good with close substitutes.

Answer: A

Diff: 2 Type: MC

Topic: Price Discrimination

Use the figure below to answer the following question.



**Figure 13.4.2**

- 4) Refer to Figure 13.4.2. Assume this monopolist practises perfect price discrimination. This means that
- A) the monopoly's behaviour is illegal.
  - B) one price is charged to young people and a different price to older people.
  - C) a different price can be charged to each buyer.
  - D) price will rise as the number of buyers increases.
  - E) the quantity sold will be less compared to the case of no price discrimination.

Answer: C

Diff: 2 Type: MC

Topic: Price Discrimination

5) Refer to Figure 13.4.2. Assume this monopolist practises perfect price discrimination. What is the lowest price charged for tickets?

- A) \$0
- B) \$1.00
- C) \$3.50
- D) \$3.00
- E) \$2.00

Answer: E

Diff: 3 Type: MC

Topic: Price Discrimination

6) Refer to Figure 13.4.2. Assume this monopolist practises perfect price discrimination. How many tickets are sold?

- A) 20 tickets
- B) 60 tickets
- C) 40 tickets
- D) 100 tickets
- E) 80 tickets

Answer: B

Diff: 3 Type: MC

Topic: Price Discrimination

7) Refer to Figure 13.4.2. Assume this monopolist practises perfect price discrimination. What is total revenue?

- A) \$110
- B) \$210
- C) \$310
- D) \$120
- E) \$105

Answer: B

Diff: 3 Type: MC

Topic: Price Discrimination

8) If a firm practises perfect price discrimination,

- A) its marginal cost curve is horizontal.
- B) it will maximize total revenue.
- C) it does not produce the quantity at which marginal revenue equals marginal cost.
- D) it will produce the quantity at which the marginal revenue curve intersects the average total cost curve.
- E) it will produce the quantity at which the marginal cost curve intersects the demand curve.

Answer: E

Diff: 3 Type: MC

Topic: Price Discrimination

Use the table below to answer the following questions.

**Table 13.4.1**

Price (dollars)	Quantity Demanded (units)
8	0
7	1
6	2
5	3
4	4
3	5
2	6
1	7

9) Refer to Table 13.4.1. If a perfect price-discriminating monopoly faces the demand schedule shown in Table 13.4.1 and if marginal cost is constant at \$3, output is

- A) 2 units.
- B) 3 units.
- C) 4 units.
- D) 5 units.
- E) 6 units.

Answer: D

Diff: 3 Type: MC

Topic: Price Discrimination

10) Table 13.4.1 shows the demand schedule faced by a monopoly. If the monopoly is a perfect price-discriminating monopoly the marginal revenue from the sale of the 3rd unit of output is

- A) \$2.
- B) \$6.
- C) \$4.
- D) \$3.
- E) \$5.

Answer: E

Diff: 3 Type: MC

Topic: Price Discrimination

11) Table 13.4.1 shows the demand schedule faced by a perfect price-discriminating monopoly. If 3 units are sold, total revenue is

- A) \$15.00.
- B) \$16.00.
- C) \$18.00.
- D) \$19.50.
- E) \$5.00.

Answer: C

Diff: 3 Type: MC

Topic: Price Discrimination

12) The output of a (not perfect) price-discriminating monopoly is

- A) less than a single-price monopoly.
- B) more than a single-price monopoly but less than a perfectly competitive industry.
- C) the same amount as a perfectly competitive industry.
- D) more than a perfectly competitive industry.
- E) less than a single-price monopoly but more than a perfectly competitive industry.

Answer: B

Diff: 2 Type: MC

Topic: Price Discrimination

Source: Study Guide

13) A perfect price-discriminating monopoly produces

- A) less than a single-price monopoly.
- B) more than a single-price monopoly but less than a perfectly competitive industry.
- C) less than a monopoly that practices price discrimination but not perfect price discrimination.
- D) more than a perfectly competitive industry.
- E) the same amount as a perfectly competitive industry.

Answer: E

Diff: 2 Type: MC

Topic: Price Discrimination

14) A perfect price-discriminating monopoly

- A) has a demand curve that is also its marginal revenue curve.
- B) maximizes total revenue.
- C) is inefficient.
- D) will produce the quantity at which the marginal cost curve intersects its demand curve.
- E) both A & D are correct.

Answer: E

Diff: 3 Type: MC

Topic: Price Discrimination

Source: Study Guide

15) Which of the following quotes by a store manager describes price discrimination in action?

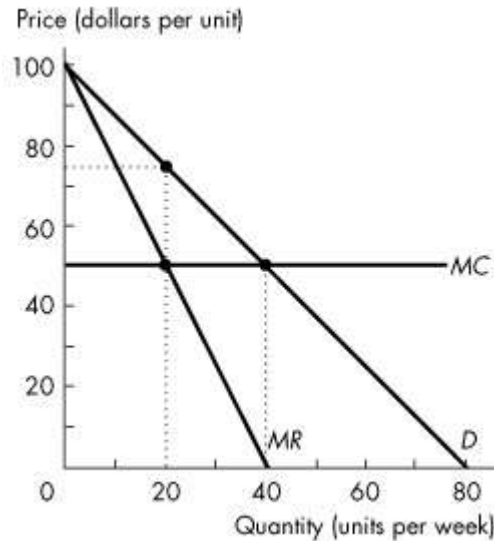
- A) "Since bulk goods are cheaper to package, I can offer a lower price."
- B) "I can get a 4-litre jug of milk from the supplier for less than four 1-litre cartons, so I can sell it for less per litre."
- C) "We offer our employees a 10 percent price discount."
- D) "I offer discounts if you buy 12 apple juices in one box, although it costs me the same as if I split it up and sell them separately."
- E) "We set price equal to average variable cost."

Answer: D

Diff: 2 Type: MC

Topic: Price Discrimination

Use the figure below to answer the following question.



**Figure 13.4.3**

- 16) Refer to Figure 13.4.3. The outcome is efficient if
- A) the monopoly is able to perfectly price discriminate.
  - B) the price consumers pay is equal to average total cost.
  - C) the price consumers pay exceeds minimum average variable cost.
  - D) the quantity produced is 80 units.
  - E) the quantity produced is 20 units.

Answer: A

Diff: 2 Type: MC

Topic: Price Discrimination

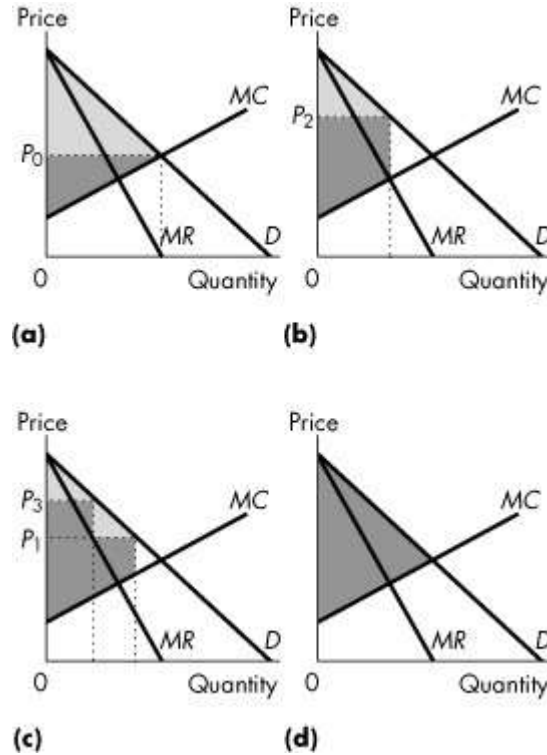
- 17) A perfect price-discriminating monopoly is
- A) less efficient than a single-price monopoly.
  - B) more efficient than a single-price monopoly, but less efficient than a perfectly competitive industry.
  - C) as efficient as a single-price monopoly.
  - D) more efficient than a perfectly competitive industry.
  - E) as efficient as a perfectly competitive industry.

Answer: E

Diff: 3 Type: MC

Topic: Price Discrimination

Use the figure below to answer the following questions.



**Figure 13.4.4**

18) Refer to Figure 13.4.4. Consider a market with a monopoly that distinguishes between two groups of buyers. If the light grey area shows the consumer surplus and the dark grey area shows the producer surplus, which graphs correctly represents this firm?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (b) and (d)

Answer: C

Diff: 3 Type: MC

Topic: Price Discrimination

19) Refer to Figure 13.4.4. Consider a market with a perfect price-discriminating monopolist. If the light grey area shows the consumer surplus and the dark grey area shows the producer surplus, which graph correctly represents this firm?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) none of the graphs

Answer: D

Diff: 3 Type: MC

Topic: Price Discrimination

Use the figure below to answer the following questions.

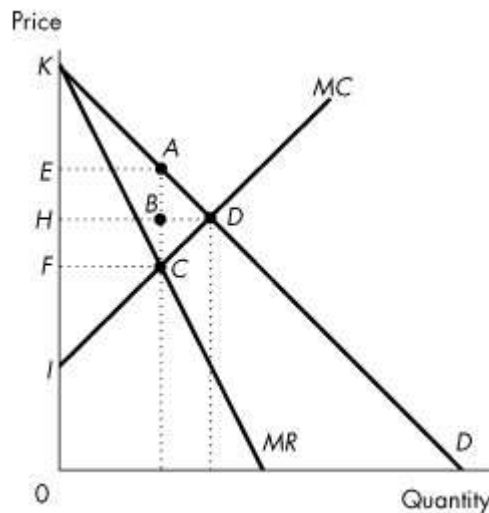


Figure 13.4.5

20) Consider the cost and revenue curves in Figure 13.4.5. If this is a perfect price-discriminating monopoly, what is consumer surplus?

- A) *EADH*
- B) *EABH*
- C) *ABD*
- D) *KEA*
- E) None of the above.

Answer: E

Diff: 3 Type: MC

Topic: Price Discrimination

21) Refer to Figure 13.4.5. What is the redistribution of surplus from consumers to the producer with a perfect price-discriminating monopoly, as compared to a perfectly competitive market?

- A) *EADH*
- B) *EABH*
- C) *ABD*
- D) *ACD*
- E) *KHD*

Answer: E

Diff: 3 Type: MC

Topic: Price Discrimination

22) When a monopoly practices price discrimination \_\_\_\_\_.

- A) it charges different prices to different consumers and transfers some of the consumer surplus to economic profit
- B) it produces a smaller quantity than when it is a single-price monopoly which decreases consumer surplus
- C) new firms enter the industry, so buyers have more goods from which to choose and consumer surplus increases
- D) consumer surplus increases because the monopoly increases the quantity available for sale
- E) firms exit the industry and consumer surplus decreases

Answer: A

Diff: 3 Type: MC

Topic: Price Discrimination

Source: MyEconLab

23) Donna owns the only dog grooming salon on Lonely Island. If Donna can price discriminate between dog owners who are seniors and those who are not, her economic profit will be \_\_\_\_\_ than if she does not price discriminate and the number of dog groomings will be \_\_\_\_\_ if she does not price discriminate.

- A) greater; more than
- B) greater; less than
- C) less; more than
- D) less; less than
- E) greater; the same as

Answer: A

Type: MC

Topic: Price Discrimination

Skill: Conceptual

AACSB: Reflective Thinking

- 24) The more perfectly a monopoly can price discriminate, the
- A) smaller its output and the lower its profit.
  - B) smaller its output and the higher its profit.
  - C) larger its output and the lower its profit.
  - D) larger its output and the higher its profit.
  - E) none of the above.

Answer: D

Type: MC

Topic: Price Discrimination

Skill: Analytical

AACSB: Reflective Thinking

- 25) Which of the following occurs with both perfectly price-discriminating and single-price monopolies?

- A) The amount of output is inefficient.
- B) All consumer surplus goes to the monopoly.
- C) Deadweight loss is created.
- D) There is a redistribution of consumer surplus to the monopoly.
- E) Demand is perfectly elastic.

Answer: D

Type: MC

Topic: Price Discrimination

Skill: Recognition

AACSB: Reflective Thinking

- 26) Which of the following is true for a perfect price-discriminating monopoly?

- A)  $P = MR$  for each unit sold.
- B)  $P = ATC$  for each unit sold.
- C)  $P = MC$  for each unit sold.
- D)  $P > MC$  for each unit sold.
- E)  $P > MR$  for each unit sold.

Answer: A

Type: MC

Topic: Price Discrimination

Skill: Conceptual

AACSB: Reflective Thinking

- 27) If a monopolist can perfectly price discriminate, then
- A) price equals average cost for each unit sold.
  - B) price equals marginal cost for each unit sold.
  - C) price equals marginal cost for the last unit sold.
  - D) the firm can ignore the marginal cost curve.
  - E) price is greater than marginal revenue for each unit sold.

Answer: C

Type: MC

Topic: Price Discrimination

Skill: Conceptual

AACSB: Reflective Thinking

- 28) For a monopoly able to practice perfect price discrimination, the market
- A) supply curve is horizontal.
  - B) supply curve is the same as the marginal revenue curve.
  - C) demand curve is the same as the marginal cost curve.
  - D) demand curve is the same as the marginal revenue curve.
  - E) demand curve is horizontal.

Answer: D

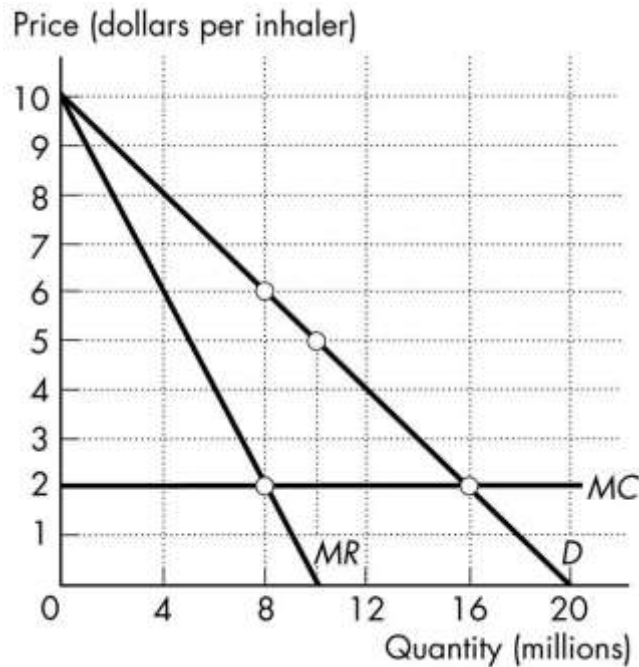
Type: MC

Topic: Price Discrimination

Skill: Conceptual

AACSB: Reflective Thinking

Use the figure below to answer the following questions.



**Figure 13.4.6**

29) Prime Pharmaceuticals has developed a new asthma medicine, for which it has a patent. An inhaler can be produced at a constant marginal cost of \$2 per inhaler. The demand curve, marginal revenue curve, and marginal cost curve for this new asthma inhaler are shown in Figure 13.4.6. The patent gives Prime Pharmaceuticals a monopoly for its new inhaler. If Prime Pharmaceuticals can perfectly price discriminate, then it

- A) sells 16 million inhalers.
- B) charges a price of \$2 for each inhaler it sells.
- C) sells inhalers for \$6 each.
- D) makes zero economic profit.
- E) Both A and B are correct.

Answer: A

Type: MC

30) Prime Pharmaceuticals has developed a new asthma medicine, for which it has a patent. An inhaler can be produced at a constant marginal cost of \$2 per inhaler. The demand curve, marginal revenue curve, and marginal cost curve for this new asthma inhaler are shown in Figure 13.4.6. The patent gives Prime Pharmaceuticals a monopoly for its new inhaler. If Prime Pharmaceuticals can perfectly price discriminate, then consumer surplus is

- A) zero.
- B) \$24 million.
- C) \$64 million.
- D) \$44 million.
- E) \$32 million.

Answer: A

Type: MC

### 13.5 Monopoly Regulation

- 1) Rate of return regulation can end up serving the self-interest of the firm if
- A) there is a great demand for the good.
  - B) there is a competitive struggle to determine which firms will supply the market.
  - C) the regulated firm overstates its costs of production.
  - D) price is set at average total cost.
  - E) the rate is set too low.

Answer: C

Diff: 2 Type: MC

Topic: Monopoly Regulation

- 2) A monopolist under rate of return regulation has an incentive to
- A) pad costs.
  - B) produce more than the efficient quantity of output.
  - C) charge a price equal to marginal cost.
  - D) maximize consumer surplus.
  - E) maximize shareholder profits

Answer: A

Diff: 2 Type: MC

Topic: Monopoly Regulation

Source: Study Guide

- 3) A monopolist under marginal cost pricing has an incentive to
- A) inflate costs.
  - B) produce more than the efficient quantity of output.
  - C) produce less than the efficient quantity of output.
  - D) maximize consumer surplus.
  - E) produce the efficient quantity of output.

Answer: E

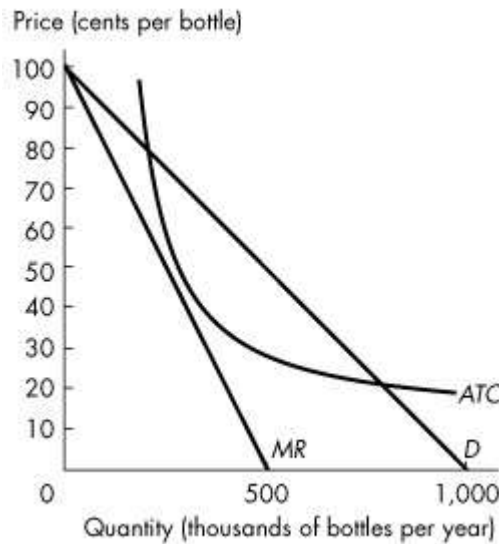
Diff: 3 Type: MC

Topic: Monopoly Regulation

Use the information below to answer the following questions.

**Fact 13.5.1**

Cascade Springs Inc. is a natural monopoly that bottles water from a spring high in the Rocky Mountains. The total fixed cost it incurs is \$80,000, and its marginal cost is 10 cents a bottle. The demand curve for Cascade Springs bottled water is shown in the following figure:



**Figure 13.5.1**

4) Refer to Figure 13.5.1. Suppose the industry is unregulated. In this case, output is

- A) 400,000 bottles per year.
- B) 450,000 bottles per year.
- C) 600,000 bottles per year.
- D) 700,000 bottles per year.
- E) 800,000 bottles per year.

Answer: B

Diff: 2 Type: MC

Topic: Monopoly Regulation

5) Refer to Figure 13.5.1. Suppose the firm is regulated by the government that imposes marginal cost pricing. The price of a bottle of water is

- A) \$0.
- B) \$0.50.
- C) \$0.30.
- D) \$0.10.
- E) \$0.20.

Answer: D

Diff: 3 Type: MC

Topic: Monopoly Regulation

6) Refer to Figure 13.5.1. Suppose the government regulates the firm with average cost pricing. What is the price?

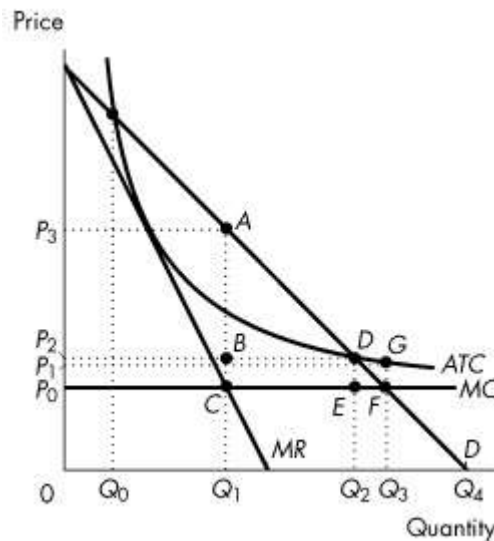
- A) \$0 a bottle
- B) \$0.50 a bottle
- C) \$0.30 a bottle
- D) \$0.10 a bottle
- E) \$0.20 a bottle

Answer: E

Diff: 3 Type: MC

Topic: Monopoly Regulation

Use the figure below to answer the following questions.



**Figure 13.5.2**

7) Consider the natural monopoly depicted in Figure 13.5.2. If a regulator uses a marginal cost pricing rule to set price, what is the quantity produced?

- A) 0
- B)  $Q_0$
- C)  $Q_1$
- D)  $Q_2$
- E)  $Q_3$

Answer: E

Diff: 3 Type: MC

Topic: Monopoly Regulation

8) Consider the natural monopoly depicted in Figure 13.5.2. If a regulatory agency sets a price just sufficient for the firm to make zero economic profit, what output will it produce?

- A)  $Q_4$
- B)  $Q_0$
- C)  $Q_1$
- D)  $Q_2$
- E)  $Q_3$

Answer: D

Diff: 2 Type: MC

Topic: Monopoly Regulation

9) Consider the natural monopoly depicted in Figure 13.5.2. If a regulatory agency sets a price just sufficient for the firm to make zero economic profit, and if the firm inflates its costs as much as possible, the regulated price will be

- A)  $P_0$ .
- B)  $P_1$ .
- C)  $P_2$ .
- D)  $P_3$ .
- E) none of the above.

Answer: D

Diff: 3 Type: MC

Topic: Monopoly Regulation

10) Consider the natural monopoly depicted in Figure 13.5.2. What area in the graph represents the deadweight loss arising from an average cost pricing rule?

- A)  $ABD$
- B)  $DGF$
- C)  $DEF$
- D)  $ACF$
- E)  $CBDE$

Answer: C

Diff: 3 Type: MC

Topic: Monopoly Regulation

11) For the regulated natural monopoly, an average cost pricing rule sets price equal to

- A) marginal cost.
- B) total fixed cost.
- C) average variable cost.
- D) average fixed cost.
- E) average total cost.

Answer: E

Diff: 2 Type: MC

Topic: Monopoly Regulation

- 12) A price cap is a price \_\_\_\_\_. A price cap might be a more effective way of regulating monopoly than rate of return regulation because under rate of return regulation \_\_\_\_\_.
- A) ceiling; a firm incurs an economic loss
  - B) floor; price is set equal to marginal cost
  - C) ceiling; the firm's managers have an incentive to inflate costs
  - D) floor; the firm's managers have an incentive to purchase more than the efficient quantity of capital
  - E) floor; the firm's managers have an incentive to inflate costs

Answer: C

Diff: 2 Type: MC

Topic: Monopoly Regulation

Source: MyEconLab

- 13) An average cost pricing rule sets \_\_\_\_\_ equal to average total cost. An average cost pricing rule is not an efficient way of regulating monopoly because at the quantity produced \_\_\_\_\_.

- A) price; marginal benefit exceeds marginal cost
- B) the return on capital; marginal benefit exceeds marginal cost
- C) marginal cost; marginal cost exceeds marginal benefit
- D) price equal to marginal revenue, which in long-run equilibrium is; marginal cost exceeds marginal benefit
- E) marginal cost; marginal benefit exceeds marginal cost

Answer: A

Diff: 2 Type: MC

Topic: Monopoly Regulation

Source: MyEconLab

- 14) Social interest theory predicts that the political process will seek to minimize

- A) producer surplus.
- B) consumer surplus.
- C) total surplus.
- D) deadweight loss.
- E) average total cost.

Answer: D

Type: MC

Topic: Monopoly Regulation

Skill: Analytical

AACSB: Reflective Thinking

15) The capture theory holds that regulations are supplied to maximize \_\_\_\_\_.

- A) total sales
- B) economic profit
- C) marginal product
- D) consumer surplus
- E) marginal revenue

Answer: B

Type: MC

Topic: Monopoly Regulation

Skill: Recognition

AACSB: Reflective Thinking

16) Under a marginal cost pricing rule, a regulated natural monopoly

- A) makes an economic profit and a deadweight loss arises.
- B) makes an economic profit with no deadweight loss.
- C) incurs an economic loss with no deadweight loss.
- D) incurs an economic loss and a deadweight loss arises.
- E) breaks even.

Answer: C

Type: MC

17) Regulation of a natural monopoly will maximize the sum of consumer surplus and producer surplus if the firm is regulated with

- A) an average cost pricing rule.
- B) a rate of return regulation.
- C) a price cap.
- D) capture theory.
- E) a marginal cost pricing rule.

Answer: E

Type: MC

## Chapter 14 Monopolistic Competition

### 14.1 What Is Monopolistic Competition?

1) In monopolistic competition

- A) firms practice product differentiation.
- B) the goods produced by each firm are identical.
- C) firms do not have any control over the price of their products.
- D) there are barriers to entry.
- E) a small number of firms compete.

Answer: A

Diff: 2 Type: MC

Topic: What Is Monopolistic Competition?

2) Toronto has a large number of retail stores that sell clothes. Each store has its own characteristics which differ from the other stores. The clothing business in Toronto is an example

of

- A) a duopoly.
- B) an oligopoly.
- C) a perfectly competitive market.
- D) a monopoly.
- E) a monopolistically competitive market.

Answer: E

Diff: 2 Type: MC

Topic: What Is Monopolistic Competition?

3) A firm in a monopolistically competitive market

- A) faces an upward-sloping demand curve.
- B) faces a downward-sloping demand curve.
- C) practices product differentiation.
- D) faces a horizontal demand curve.
- E) B and C are correct.

Answer: E

Diff: 2 Type: MC

Topic: What Is Monopolistic Competition?

4) One factor that distinguishes a monopoly from monopolistic competition is that

- A) firms in monopolistic competition practice collusion.
- B) no barriers to entry exist in a monopoly.
- C) barriers to exit exist in monopolistic competition.
- D) close substitutes are available in monopolistic competition.
- E) firms are price-takers in monopolistic competition.

Answer: D

Diff: 2 Type: MC

Topic: What Is Monopolistic Competition?

5) In monopolistic competition

- A) there are two firms in the market.
- B) the size of one firm is small relative to the size of the industry.
- C) the size of one firm is large relative to the size of the industry.
- D) each firm is a price-taker.
- E) there is only one firm in the market.

Answer: B

Diff: 2 Type: MC

Topic: What Is Monopolistic Competition?

6) If some firms in the industry make an economic profit, then

- A) the industry cannot be perfectly competitive.
- B) the industry must be monopolistically competitive.
- C) rival firms will enter if there are no barriers to entry.
- D) the firms must practice product differentiation.
- E) the industry must be an oligopoly.

Answer: C

Diff: 2 Type: MC

Topic: What Is Monopolistic Competition?

7) A monopolistically competitive firm is able to influence the price of what it sells because of

- A) barriers to entry.
- B) economies of scale.
- C) product differentiation.
- D) the fact there are many buyers.
- E) inelastic demand.

Answer: C

Diff: 2 Type: MC

Topic: What Is Monopolistic Competition?

8) In monopolistic competition

- A) firms can collude.
- B) each firm has a small market share.
- C) each firm pays attention to every other firm.
- D) firms make a profit in the long run.
- E) all of the above.

Answer: B

Diff: 2 Type: MC

Topic: What Is Monopolistic Competition?

Source: Study Guide

9) ACME, Inc. operates in a market structure in which there are many other firms that find it easy to enter or exit. ACME is operating in \_\_\_\_\_ market.

- A) definitely a perfectly competitive
- B) a perfectly competitive or a monopolistically competitive
- C) definitely a monopolistically competitive
- D) neither a perfectly competitive nor a monopolistically competitive
- E) a monopolistic

Answer: B

Type: MC

Topic: What Is Monopolistic Competition?

Skill: Recognition

AACSB: Reflective Thinking

10) The existence of a large number of firms in monopolistic competition

- A) means that each firm has a small market share.
- B) makes it possible for each firm's price to deviate by a large amount from the average price of the other firms.
- C) means that a firm must pay attention to the behaviour of all of its competitors.
- D) All of the above answers are correct.
- E) None of the above answers are correct.

Answer: A

Type: MC

Topic: What Is Monopolistic Competition?

Skill: Recognition

AACSB: Reflective Thinking

11) The key feature of monopolistic competition that distinguishes it from perfect competition is

- A) many sellers.
- B) barriers to entry.
- C) perfectly elastic demand.
- D) product differentiation.
- E) none of the above.

Answer: D

Type: MC

Topic: What Is Monopolistic Competition?

Skill: Recognition

AACSB: Reflective Thinking

12) In monopolistic competition, firms compete on the basis of

- A) price only.
- B) price, quality, and marketing.
- C) marketing only.
- D) quality and marketing, but not price.
- E) quality only.

Answer: B

Diff: 1 Type: MC

Topic: What Is Monopolistic Competition?

Skill: Recognition

AACSB: Reflective Thinking

13) In monopolistic competition, each firm supplies a \_\_\_\_\_ part of the total industry output and its actions \_\_\_\_\_ the actions of the other firms.

- A) small; do not directly affect
- B) small; directly affect
- C) large; do not directly affect
- D) large; directly affect
- E) large; may or may not directly affect

Answer: A

Diff: 1 Type: MC

Topic: What Is Monopolistic Competition?

Skill: Recognition

AACSB: Reflective Thinking

14) Monopolistic competition differs from monopoly because in monopolistic competition

- A) firms maximize profits.
- B) firms set marginal revenue equal to marginal cost to maximize profit.
- C) firms are free to enter and exit.
- D) All of the above are differences between monopoly and monopolistically competitive firms.
- E) None of the above are differences between monopoly and monopolistically competitive firms.

Answer: C

Type: MC

Topic: What Is Monopolistic Competition?

Skill: Recognition

AACSB: Reflective Thinking

15) Dole Co. operates in a monopolistically competitive market. Which of the following characterizes Dole Co.'s market?

- A) Dole Co. supplies a small portion of the market's output.
- B) Dole Co.'s product is slightly different from its competitors.
- C) Dole Co. faced no barrier to entry when it decided to enter its market.
- D) Dole Co. is unable to collude with other firms in the market.
- E) All of the above describe Dole Co.'s market.

Answer: E

Type: MC

Topic: What Is Monopolistic Competition?

Skill: Recognition

AACSB: Reflective Thinking

16) Which of the following goods is best described as being sold in a monopolistically competitive market?

- A) batteries
- B) wheat
- C) fast food
- D) postage stamps
- E) the local newspaper

Answer: C

Type: MC

Topic: What Is Monopolistic Competition?

Skill: Conceptual

AACSB: Reflective Thinking

17) Within a monopolistically competitive industry,

- A) firms can freely enter and exit, and economic profit is zero in the long run.
- B) firms can freely enter and exit, and economic profit is greater than zero in the long run.
- C) there are some barriers to entry and exit, and economic profit is zero in the long run.
- D) there are some barriers to entry and exit, and economic profit is greater than zero in the long run.
- E) firms can freely enter and exit, and economic profit is zero in the short run.

Answer: A

Type: MC

Topic: What Is Monopolistic Competition?

Skill: Recognition

AACSB: Reflective Thinking

- 18) When comparing perfect competition and monopolistic competition, we find that
- A) firms in monopolistic competition produce identical products just as do firms in perfect competition.
  - B) firms in monopolistic competition face barriers to entry, unlike firms in perfect competition.
  - C) advertising plays a large role in monopolistic competition, unlike in perfect competition.
  - D) firms in monopolistic competition are price takers just as is the case for firms in perfect competition.
  - E) firms in monopolistic competition each have a large market share.

Answer: C

Type: MC

Topic: What Is Monopolistic Competition?

Skill: Conceptual

AACSB: Reflective Thinking

- 19) Which of the following best explains why firms in monopolistic competition face a downward-sloping demand curve while perfectly competitive firms do not?
- A) Monopolistically competitive industries have only a few firms.
  - B) Monopolistically competitive firms face barriers to entry.
  - C) Only industries with free entry and exit have firms that face horizontal demand curves.
  - D) Firms in monopolistic competition are price takers.
  - E) Firms in monopolistic competition sell a differentiated good.

Answer: E

Type: MC

- 20) Product differentiation exists within an industry when
- A) there are no substitutes for the product.
  - B) the firm can sell all it wants at the given price.
  - C) the market is a monopoly.
  - D) the market is perfectly competitive.
  - E) there are close but not perfect substitutes for the product.

Answer: E

Type: MC

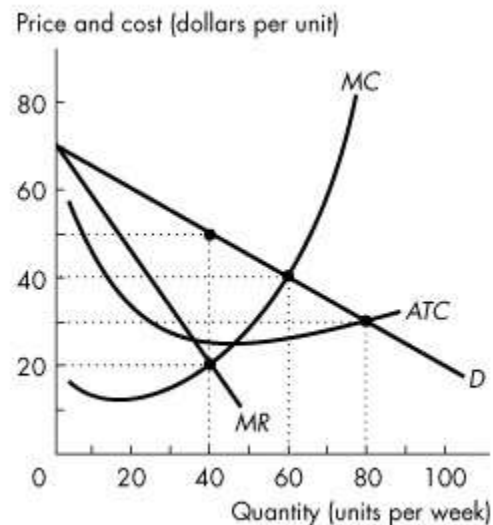
- 21) Firefox, Internet Explorer, and Google Chrome browsers are an example of
- A) goods produced in perfectly competitive markets.
  - B) goods produced by monopolies.
  - C) product differentiation.
  - D) goods that are identical.
  - E) product similarity.

Answer: C

Type: MC

## 14.2 Price and Output in Monopolistic Competition

Use the figure below to answer the following questions.



**Figure 14.2.1**

- 1) Refer to Figure 14.2.1. If this firm is in monopolistic competition, it will produce an output level
- A) of 40 units.
  - B) of 60 units.
  - C) of 80 units.
  - D) that is impossible to determine without information concerning the rival firms.
  - E) that is less than 40 units.

Answer: A

Diff: 1 Type: MC

Topic: Price and Output in Monopolistic Competition

- 2) Refer to Figure 14.2.1. If this firm is in monopolistic competition, then it will charge a price
- A) of \$20 a unit.
  - B) of \$50 a unit.
  - C) of \$40 a unit.
  - D) of \$30 a unit.
  - E) that is impossible to determine without information concerning the behaviour of the rival firms.

Answer: B

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

- 3) Refer to Figure 14.2.1. This firm in monopolistic competition will
- A) make an economic profit in the short run.
  - B) make zero economic profit in the short run.
  - C) incur an economic loss.
  - D) make an economic profit in the long run.
  - E) incur an economic loss in the long run.

Answer: A

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

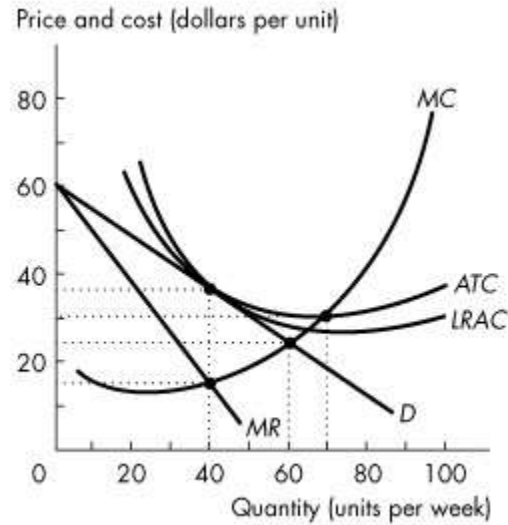
- 4) Refer to Figure 14.2.1. If this firm in monopolistic competition is in short-run equilibrium, then
- A) rival firms will enter the industry.
  - B) all firms will exit the industry.
  - C) economic profit of all firms in the industry is zero.
  - D) it produces 60 units of output to maximize economic profit.
  - E) the firm's profits can be expected to rise over time.

Answer: A

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

Use the figure below to answer the following questions.



**Figure 14.2.2**

5) Refer to Figure 14.2.2. To maximize economic profit, this firm in monopolistic competition will charge a price of

- A) \$15 a unit.
- B) \$25 a unit.
- C) \$20 a unit.
- D) \$32 a unit.
- E) \$35 a unit.

Answer: E

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

6) Refer to Figure 14.2.2. To maximize economic profit, this firm in monopolistic competition produces an output

- A) of 40 units.
- B) of 70 units.
- C) of 60 units.
- D) that cannot be determined without information concerning rival firms.
- E) of less than 40 units.

Answer: A

Diff: 1 Type: MC

Topic: Price and Output in Monopolistic Competition

- 7) Refer to Figure 14.2.2. This firm
- A) is incurring an economic loss.
  - B) is in long-run equilibrium.
  - C) is making an economic profit.
  - D) must raise its price to maximize economic profit.
  - E) will make more economic profit in the long run.

Answer: B

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

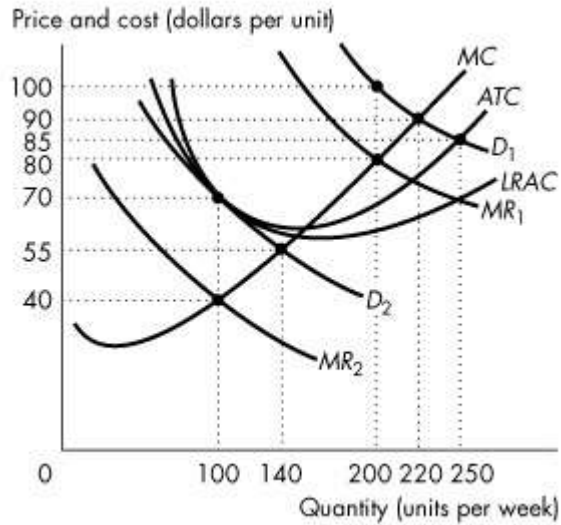
- 8) Refer to Figure 14.2.2. If this firm in monopolistic competition is maximizing economic profit,
- A) there will be entry of rival firms into the industry.
  - B) rival firms will exit the industry.
  - C) its profit will rise over time.
  - D) this firm will exit the industry in the long run.
  - E) none of the above.

Answer: E

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

Use the figure below to answer the following questions.



**Figure 14.2.3**

9) Refer to Figure 14.2.3. Which demand curve does this monopolistically competitive firm face in the long run?

- A) demand curve  $D_1$
- B) demand curve  $D_2$
- C) either demand curve  $D_1$  or  $D_2$
- D) neither demand curve  $D_1$  nor demand curve  $D_2$
- E) Any demand curve is possible, including  $D_1$  or  $D_2$ .

Answer: B

Diff: 3 Type: MC

Topic: Price and Output in Monopolistic Competition

10) Refer to Figure 14.2.3. Assume this firm faces demand curve  $D_1$ . To maximize economic profit, this firm in monopolistic competition will charge a price of \_\_\_\_\_ and produce an output of \_\_\_\_\_ units.

- A) \$100; 200
- B) \$90; 220
- C) \$80; 200
- D) \$70; 100
- E) \$55; 140

Answer: A

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

11) Refer to Figure 14.2.3. Assume this firm faces demand curve  $D_1$ . At the profit-maximizing output level, the firm

- A) incurs an economic loss.
- B) makes zero economic profit.
- C) makes an economic profit.
- D) makes less economic profit than that earned by firms in perfect competition.
- E) makes an unknown economic profit that is impossible to determine without information concerning the price charged by the rival firms.

Answer: C

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

12) Refer to Figure 14.2.3. Assume this firm faces demand curve  $D_1$ . If this firm in monopolistic competition is maximizing profit,

- A) there will be entry of rival firms into the industry.
- B) rival firms will exit the industry.
- C) the market is efficient.
- D) this firm will exit the industry in the long run.
- E) its profit will rise over time.

Answer: A

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

13) Refer to Figure 14.2.3. Assume this firm faces demand curve  $D_1$ . If the firm produced the efficient quantity, it would produce

- A) 100 units.
- B) 220 units.
- C) 200 units.
- D) 250 units.
- E) 140 units.

Answer: B

Diff: 3 Type: MC

Topic: Price and Output in Monopolistic Competition

14) Refer to Figure 14.2.3. Assume this firm faces demand curve  $D_2$ . To maximize economic profit, this firm in monopolistic competition will charge a price of \_\_\_\_\_ and produce an output of \_\_\_\_\_ units.

- A) \$40; 100
- B) \$90; 220
- C) \$80; 200
- D) \$55; 140
- E) \$70; 100

Answer: E

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

15) Refer to Figure 14.2.3. Assume this firm faces demand curve  $D_2$ . At the profit-maximizing output level, the firm

- A) incurs an economic loss.
- B) makes zero economic profit.
- C) makes an economic profit.
- D) is not in a long-run equilibrium.
- E) is producing at its efficient scale.

Answer: B

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

16) Refer to Figure 14.2.3. Assume this firm faces demand curve  $D_2$ . If this firm in monopolistic competition is maximizing economic profit,

- A) there will be entry of rival firms into the industry.
- B) rival firms will exit the industry.
- C) it is producing the efficient quantity.
- D) the number of firms in the industry will remain constant.
- E) economic profit will fall over time.

Answer: D

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

17) Refer to Figure 14.2.3. Assume this firm faces demand curve  $D_2$ . When the firm produces the efficient quantity, it produces

- A) 100 units.
- B) 140 units.
- C) 200 units.
- D) 220 units.
- E) 250 units.

Answer: B

Diff: 3 Type: MC

Topic: Price and Output in Monopolistic Competition

18) Refer to Figure 14.2.3. Assume this firm faces demand curve  $D_2$ . If the firm produces the efficient quantity, it

- A) makes an economic profit.
- B) makes zero economic profit.
- C) incurs an economic loss.
- D) is in a long-run equilibrium.
- E) will face competition from new firms entering the industry.

Answer: C

Diff: 3 Type: MC

Topic: Price and Output in Monopolistic Competition

19) In the long run, all firms in an industry that is monopolistically competitive

- A) produce at their efficient scale.
- B) set price equal to marginal cost.
- C) incur an economic profit.
- D) make an economic profit.
- E) make zero economic profit.

Answer: E

Diff: 1 Type: MC

Topic: Price and Output in Monopolistic Competition

20) In the short-run, the similarity between a monopolist and a monopolistically competitive firm is that

- A) they both make the same decisions about the level of output and output price.
- B) they both face an upward-sloping supply curve for their products.
- C) they both try to maximize their total revenues.
- D) they both try to minimize their average fixed costs.
- E) they set the price such that marginal revenue equals average total cost.

Answer: A

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

21) Mrs. Smith's bakery shop is a firm in monopolistic competition. If in the short-run Mrs. Smith incurs an economic loss, she will keep producing as long as

- A) price is less than average variable cost.
- B) price is equal to marginal cost.
- C) price is greater than or equal to average variable cost.
- D) marginal revenue is greater than or equal to average variable cost.
- E) marginal revenue is less than average variable cost.

Answer: C

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

22) Mrs. Smith's bakery shop is a firm in monopolistic competition. The firm's marginal revenue curve

- A) is upward sloping.
- B) is downward sloping and above the demand curve.
- C) is a horizontal line.
- D) is the same as the demand curve.
- E) is downward sloping and lies below the demand curve.

Answer: E

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

23) Mrs. Smith's bakery shop is a firm in monopolistic competition. She is currently selling a box of bread for \$16. The firm's marginal cost is \$7 and marginal revenue is \$7. To maximize economic profit Mrs. Smith

- A) shuts down.
- B) decreases output so that marginal revenue exceeds marginal cost.
- C) continues to produce the same level of output.
- D) increases output so that marginal cost exceeds marginal revenue.
- E) decreases output so that marginal cost equals the output price.

Answer: C

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

24) What will happen in the long run if firms in monopolistic competition incur economic loss?

- A) Firms will continue producing and endure the losses.
- B) Firms will leave the industry until the remaining firms make positive economic profit.
- C) Firms will ask the government for financial aid.
- D) Firms will leave the industry until the remaining firms make zero economic profit.
- E) The level of investment in this industry will increase to boost the economy.

Answer: D

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

25) A firm has excess capacity if

- A) it produces above its efficient scale.
- B) it produces below its efficient scale.
- C) it produces the same level as its efficient scale.
- D) it sells some of its factors of production.
- E) it improves the quality of its factors of production.

Answer: B

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

26) The real-estate industry is monopolistically competitive, so in this industry

- A) the market demand curve is a horizontal line.
- B) the market demand curve is upward sloping.
- C) there are few realtors in the market.
- D) excess capacity exists.
- E) excess capacity does not exist.

Answer: D

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

- 27) A firm's markup is
- A) the firm's total profit.
  - B) the firm's total cost.
  - C) the amount by which price exceeds marginal cost.
  - D) the amount by which price equals marginal cost.
  - E) the amount by which price is less than marginal cost.

Answer: C

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

- 28) Markup
- A) does not exist in monopoly.
  - B) does not exist in monopolistic competition.
  - C) exists in perfect competition.
  - D) is the difference between price and average total cost.
  - E) exists in both monopoly and monopolistic competition.

Answer: E

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

- 29) In monopolistically competitive industries,
- A) firms compete on quality, price and marketing.
  - B) the range of choice of products is the same as in perfectly competitive industries.
  - C) firms are insensitive to changes in consumer demand.
  - D) all firms produce a quantity at which marginal cost is greater than marginal benefit.
  - E) all firms make an economic profit.

Answer: A

Diff: 1 Type: MC

Topic: Price and Output in Monopolistic Competition

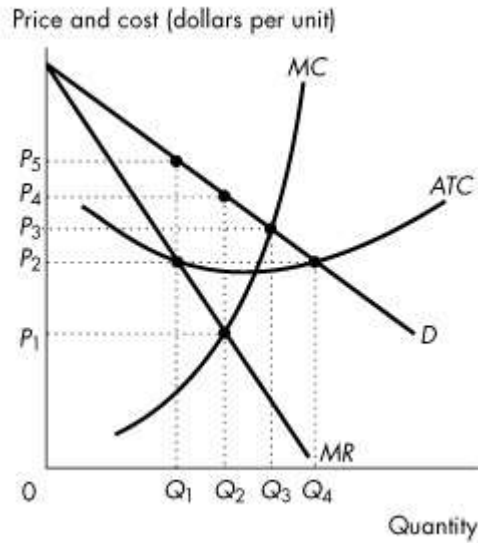
- 30) Excess capacity in monopolistically competitive firms occurs because
- A) each firm faces a demand that is perfectly elastic.
  - B) each firm builds a huge plant.
  - C) the existence of slightly differentiated products, serving almost the same purpose, causes a waste of precious natural resources.
  - D) firms produce an output that is less than the output at minimum average total cost.
  - E) marginal cost is too high.

Answer: D

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

Use the figure below to answer the following questions.



**Figure 14.2.4**

31) Refer to Figure 14.2.4. The figure represents a monopolistically competitive firm in short-run equilibrium. What is the firm's level of output?

- A)  $Q_1$
- B)  $Q_2$
- C)  $Q_3$
- D)  $Q_4$
- E) zero.

Answer: B

Diff: 1 Type: MC

Topic: Price and Output in Monopolistic Competition

Source: Study Guide

32) Refer to Figure 14.2.4. The figure represents a monopolistically competitive firm in short-run equilibrium. What price does the firm charge?

- A)  $P_2$
- B)  $P_1$
- C)  $P_4$
- D)  $P_3$
- E)  $P_5$

Answer: C

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

33) Refer to Figure 14.2.4. The figure represents a monopolistically competitive firm in short-run equilibrium. In the long run,

- A) new firms enter, and each existing firm's demand curve shifts leftward.
- B) new firms enter, and each existing firm's demand curve shifts rightward.
- C) existing firms exit, and each remaining firm's demand curve shifts leftward.
- D) existing firms exit, and each remaining firm's demand curve shifts rightward.
- E) the equilibrium is the same as in the short run.

Answer: A

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

Source: Study Guide

34) In the long run, a monopolistically competitive firm produces the output at which price equals

- A) marginal cost.
- B) marginal revenue.
- C) average variable cost.
- D) average total cost.
- E) B and D.

Answer: D

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

Source: Study Guide

35) Consider a monopolistically competitive industry in long-run equilibrium. Suppose there is a large increase in wages that raises the costs for all firms. What happens within each firm in the short run?

- A) They will be forced to close down due to the excess costs.
- B) They will continue producing as before, cushioned by their previous excess profits.
- C) They will expand output and try to make up for lost profits.
- D) They will lower prices and try to steal customers away from their rivals.
- E) They will decrease production and produce the quantity at which marginal revenue equals the new (higher) marginal cost curve; this means a rise in price.

Answer: E

Diff: 3 Type: MC

Topic: Price and Output in Monopolistic Competition

36) Under monopolistic competition, long-run economic profit is zero because of

- A) product differentiation.
- B) no barriers to entry.
- C) excess capacity.
- D) economic inefficiency.
- E) the downward-sloping demand curve facing each firm.

Answer: B

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

Source: Study Guide

37) In the long run, a monopolistically competitive firm will make the same economic profit as

- A) a monopolistically competitive firm in the short run.
- B) a single-price monopoly.
- C) a price-discriminating monopoly.
- D) a perfectly competitive firm in long-run equilibrium.
- E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

Source: Study Guide

38) Which one of the following is true for perfect competition, monopolistic competition, and single-price monopoly?

- A) Each firm produces an identical good.
- B) Each firm makes zero long-run economic profit.
- C) The profit maximizing quantity occurs at the quantity at which  $MC = MR$ .
- D) Easy entry and exit.
- E) None of the above.

Answer: C

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

Source: Study Guide

39) In the long run, the firm in monopolistic competition

- A) faces a perfectly elastic demand.
- B) produces more than the quantity at minimum  $ATC$ .
- C) produces less than the quantity at minimum  $ATC$ .
- D) produces the quantity at minimum  $ATC$ .
- E) makes an economic profit.

Answer: C

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

Source: Study Guide

40) Which one of the following characteristics is *not* shared by single-price monopoly and monopolistic competition?

- A) Firms face a downward-sloping demand curve.
- B) Profit-maximizing quantity occurs where  $MC = MR$ .
- C) Price charged is the highest consumers are willing to pay.
- D) Firms make an economic profit in the long run.
- E) The marginal revenue curve lies below the demand curve.

Answer: D

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

Source: Study Guide

41) Which one of the following characteristics is shared by perfect competition and monopolistic competition?

- A) Firms face a downward-sloping demand curve.
- B) Profit-maximizing quantity occurs where  $MC = MR$ .
- C) Long-run equilibrium price equals minimum  $ATC$ .
- D) Firms make an economic profit in the long run.
- E) None of the above.

Answer: B

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

42) Which of the following are true? The similarities between perfect competition and monopolistic competition include:

- (1) no barriers to entry.
  - (2) profit-maximizing output occurs where  $MC = MR$ .
  - (3) long-run economic profit equals zero.
- A) (1) only
  - B) (2) only
  - C) (1) and (2) only
  - D) (2) and (3) only
  - E) (1), (2), and (3)

Answer: E

Diff: 3 Type: MC

Topic: Price and Output in Monopolistic Competition

43) Firms in monopolistic competition make zero economic profit in the long run because

- A) their costs rise over time.
- B) the demand they face decreases as rival firms offer slightly differentiated products for sale in the same market.
- C) their marginal cost curves slope upward.
- D) the market eventually becomes perfectly competitive.
- E) both A and B are correct.

Answer: B

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

44) Choose the correct statement about firms in monopolistic competition.

- A) All firms make positive economic profit.
- B) The price is set equal to marginal cost to achieve maximum economic profit.
- C) Price is lower than in perfect competition.
- D) Production always takes place at minimum average total cost.
- E) The price is always greater than the marginal cost.

Answer: E

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

45) Choose the correct statement about firms in monopolistic competition.

- A) A firm must lower its price to sell a greater quantity.
- B) A firm can never incur an economic loss.
- C) Price is never more than marginal cost.
- D) Firms offer identical products.
- E) The most a firm can make is zero economic profit.

Answer: A

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

46) For a monopolistically competitive firm to be making an economic profit,

- A) the production period must be the short run.
- B) the production period must be the long run.
- C) rival firms must not exist.
- D) its rivals must also be making an economic profit.
- E) barriers to entry must exist.

Answer: A

Type: MC

Topic: Price and Output in Monopolistic Competition

47) When firms in monopolistic competition incur an economic loss

- A) firms enter the industry and produce better products.
- B) firms exit the industry, and demand increases for the products of the firms that remain.
- C) firms exit the industry, and demand decreases for the firms that remain in the industry.
- D) firms enter the industry, and demand increases for the firms that were originally in the industry.
- E) the industry will eventually disappear.

Answer: B

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

48) When firms in monopolistic competition make an economic profit

- A) firms enter the industry, which increases demand for the product of the firms originally in the market.
- B) firms exit the industry, and demand increases for the products of the firms that remain.
- C) firms exit the industry, and demand decreases for the firms that remain in the industry.
- D) firms enter the industry, and demand decreases for the firms that were originally in the industry.
- E) eventually the market will become a monopoly.

Answer: D

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

- 49) Firms in monopolistic competition have rivals that
- A) will always match their price increases.
  - B) will always match their price decreases but not their price increases.
  - C) all agree on a common price.
  - D) set their price where the demand curve is tangent to the average cost curve.
  - E) set their price according to the demand they face.

Answer: E

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

50) For a firm in monopolistic competition, the marginal cost curve intersects the average total cost curve

- A) at the minimum average total cost.
- B) to the left of the minimum average total cost.
- C) to the right of the minimum average total cost.
- D) at no point.
- E) at the same quantity at which the marginal cost curve intersects the marginal revenue curve.

Answer: A

Type: MC

Topic: Price and Output in Monopolistic Competition

Skill: Analytical

AACSB: Reflective Thinking

51) Which of the following is *always* true regarding a profit-maximizing monopolistically competitive firm in short-run equilibrium?

- A)  $P = ATC$
- B)  $P = MR$
- C)  $MR = MC$
- D)  $MC = ATC$
- E)  $P = MC$

Answer: C

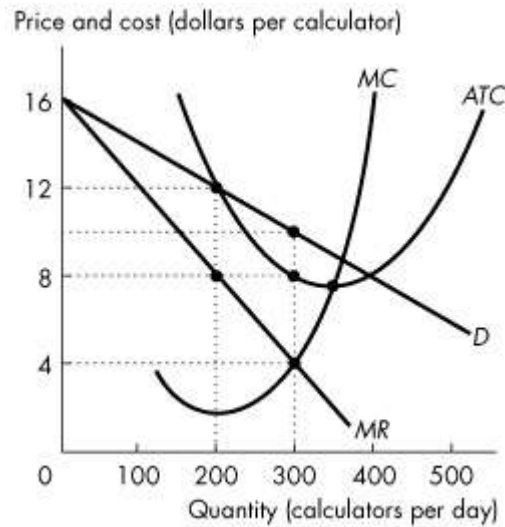
Type: MC

Topic: Price and Output in Monopolistic Competition

Skill: Recognition

AACSB: Reflective Thinking

Use the figure below to answer the following questions.



**Figure 14.2.5**

52) Refer to Figure 14.2.5 The figure shows the situation facing Smart Digit, Inc., a firm in monopolistic competition that produces calculators. What is the firm's economic profit per day?

- A) zero
- B) between \$1 and \$700
- C) between \$701 and \$900
- D) more than \$901
- E) less than zero

Answer: B

Type: MC

Topic: Price and Output in Monopolistic Competition

Skill: Analytical

AACSB: Analytical Skills

53) Refer to Figure 14.2.5. The figure shows the situation facing Smart Digit, Inc., a firm in monopolistic competition that produces calculators. The firm's markup is \_\_\_\_\_ per calculator.

- A) zero
- B) \$2
- C) \$4
- D) \$6
- E) \$10

Answer: D

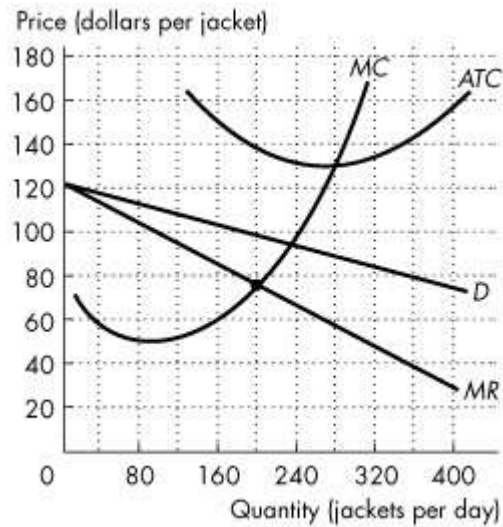
Type: MC

Topic: Price and Output in Monopolistic Competition

Skill: Analytical

AACSB: Analytical Skills

Use the figure below to answer the following questions.



**Figure 14.2.6**

54) Refer to Figure 14.2.6, which shows the demand curve, marginal revenue curve and cost curves faced by Gap. Gap maximizes its profit if it sells \_\_\_\_\_ jackets per day.

- A) 200
- B) 240
- C) 275
- D) 140
- E) 280

Answer: A

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

Skill: Analytical

AACSB: Analytical Skills

55) Refer to Figure 14.2.6, which shows the demand curve, marginal revenue curve and cost curves faced by Gap. Gap maximizes its profit if it charges \_\_\_\_\_ per jacket.

- A) \$100
- B) \$95
- C) \$75
- D) \$120
- E) \$90

Answer: A

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

Skill: Analytical

AACSB: Analytical Skills

56) Refer to Figure 14.2.6, which shows the demand curve, marginal revenue curve and cost curves faced by Gap. Gap's economic \_\_\_\_\_ is \_\_\_\_\_ a day.

- A) loss; \$8,000
- B) loss; \$13,000
- C) profit; \$7,200
- D) profit; \$13,000
- E) loss; \$8,960

Answer: A

Diff: 2 Type: MC

Topic: Price and Output in Monopolistic Competition

Skill: Analytical

AACSB: Analytical Skills

57) Consider a monopolistically competitive industry which is in long-run equilibrium. Which of the following is true?

- A) All firms charge a price equal to average total cost.
- B) All firms charge a price equal to marginal cost.
- C) All firms make an economic profit.
- D) The demand, average total cost, and marginal cost curves all intersect at the same point.
- E) Firms have an incentive to enter the industry.

Answer: A

Type: MC

Topic: Price and Output in Monopolistic Competition

Skill: Conceptual

AACSB: Reflective Thinking

58) In the long-run, a firm in monopolistic competition produces at an output level where

- A)  $P > ATC$  and  $MR = MC$ .
- B)  $P > ATC$  and  $MR > MC$ .
- C)  $P = ATC$  and  $MR = MC$ .
- D)  $P = ATC$  and  $MR > MC$ .
- E)  $P > ATC$  and  $MC > ATC$ .

Answer: C

Type: MC

Topic: Price and Output in Monopolistic Competition

Skill: Recognition

AACSB: Reflective Thinking

Use the figure below to answer the following question.

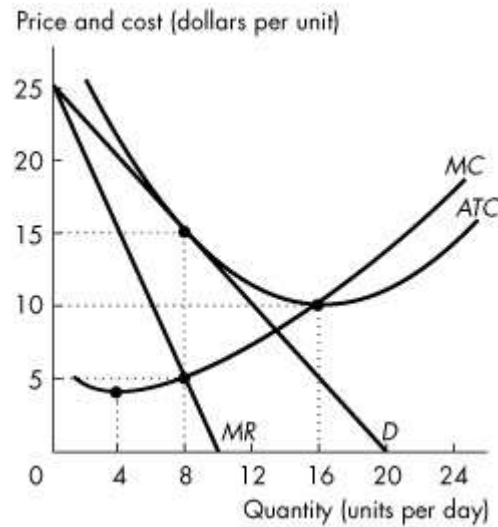


Figure 14.2.7

59) Refer to Figure 14.2.7. The figure shows the demand, marginal revenue, and cost curves for a monopolistically competitive firm in the long run. The firm has excess capacity of

- A) 4 units.
- B) 8 units.
- C) 16 units.
- D) \$10.
- E) \$5.

Answer: B

Type: MC

Topic: Price and Output in Monopolistic Competition

Skill: Analytical

AACSB: Analytical Skills

60) Monopolistic competition might be efficient if

- A) firms invested in technology that decreased the marginal cost of production.
- B) more firms entered the industry.
- C) firms left the industry.
- D) the loss that arises because the quantity produced is less than the efficient quantity is offset by the gain that arises from having a greater degree of product variety.
- E) firms made more use of brand names.

Answer: D

Type: MC

Topic: Price and Output in Monopolistic Competition

Source: MyEconLab

61) A firm's efficient scale is the quantity at which \_\_\_\_\_ is a minimum.  
 A firm has excess capacity if it produces \_\_\_\_\_ its efficient scale.  
 In the long run, a firm in monopolistic competition produces less than the efficient scale and has excess capacity because the firm faces a \_\_\_\_\_ demand curve.

- A) average total cost; below; downward-sloping
- B) marginal cost; above; horizontal
- C) average total cost; above; downward-sloping
- D) marginal cost; below; horizontal
- E) average variable cost; below; downward-sloping

Answer: A

Type: MC

Topic: Price and Output in Monopolistic Competition

Source: MyEconLab

*Use the table below to answer the following question.*

**Table 14.2.1**

<b>Price</b> (dollars per sweatshirt)	<b>Quantity demanded</b> (sweatshirts per week)
<b>0</b>	<b>100</b>
<b>20</b>	<b>80</b>
<b>40</b>	<b>60</b>
<b>60</b>	<b>40</b>
<b>80</b>	<b>20</b>
<b>100</b>	<b>0</b>

62) Refer to Table 14.2.1. Sara is a dot.com entrepreneur who sells sweatshirts. She pays \$1,000 a week for her Web server and Internet connection. She pays the firm that makes the sweatshirts \$20 a sweatshirt. Sara has no other costs. The table sets out the demand schedule for Sara's sweatshirts.

Other firms \_\_\_\_\_ enter the Web sweatshirt business and compete with Sara.

In the long run, the demand for Sara's sweatshirts \_\_\_\_\_ and her economic profit \_\_\_\_\_.

- A) will; decreases; falls to zero
- B) will not; decreases; falls to zero
- C) will; increases; increases
- D) will not; increases; increases
- E) will; increases; falls to zero

Answer: A

Type: MC

Topic: Price and Output in Monopolistic Competition

Source: MyEconLab

63) Firms in monopolistic competition in the short run always

- A) set price above marginal cost.
- B) make an economic profit.
- C) set price equal to marginal cost.
- D) produce at the minimum average total cost.
- E) break even.

Answer: A

Type: MC

64) The profit-maximizing condition for a firm in monopolistic competition is to produce the quantity at which

- A) marginal cost equals price.
- B) price equals marginal revenue.
- C) average total cost equals price.
- D) marginal cost equals marginal revenue.
- E) average variable cost equals price.

Answer: D

Type: MC

65) In monopolistic competition, firms can make an economic profit in

- A) the short run but not in the long run.
- B) the short run and in the long run.
- C) the long run but not in the short run.
- D) neither the short run nor the long run.
- E) always in the short run and sometimes but not frequently in the long run.

Answer: A

Type: MC

66) In long-run equilibrium, a firm in monopolistic competition

- A) makes zero economic profit and operates with excess capacity.
- B) makes zero economic profit and produces above capacity output.
- C) makes a positive economic profit and operates with excess capacity.
- D) makes a positive economic profit and produces above capacity output.
- E) incurs an economic loss and exits the market.

Answer: A

Type: MC

### 14.3 Product Development and Marketing

1) An advantage of monopolistic competition over perfect competition is

- A) economic profit.
- B) product variety.
- C) excess capacity.
- D) efficiency.
- E) economies of scale.

Answer: B

Diff: 1 Type: MC

Topic: Product Development and Marketing

Source: Study Guide

2) Because consumers value product variety,

- A) society must be more efficient with monopolistic competition than with perfect competition.
- B) the inefficiency of monopolistic competition is partially offset.
- C) in the long run, monopolistic competition firms make economic profit.
- D) monopolistically competitive industries are efficient.
- E) no two goods of the same type will have equal prices.

Answer: B

Diff: 2 Type: MC

Topic: Product Development and Marketing

3) Selling costs

- A) are variable costs that increase total cost.
- B) always increase demand for a firm's product.
- C) always decrease demand by increasing competition.
- D) always provide consumers with valuable services.
- E) include marketing expenditures on advertising and packaging.

Answer: E

Diff: 2 Type: MC

Topic: Product Development and Marketing

Source: Study Guide

4) Advertising by firms in monopolistic competition

- A) does not provide consumers with useful information.
- B) increases the marginal cost of production.
- C) is inefficient.
- D) is a waste of valuable resources because firms are forced by the entry of rival firms to be price takers.
- E) generates the perception among consumers that product differentiation exists.

Answer: E

Diff: 1 Type: MC

Topic: Product Development and Marketing

- 5) The decision to undertake product development in monopolistic competition is made by comparing the
- A) marginal benefit of product development to the marginal cost of product development.
  - B) marginal revenue of product development to the average total cost of product development.
  - C) total revenue of product development to the total cost of product development.
  - D) firm's expenditure on product development to expenditures by competing firms.
  - E) none of the above.

Answer: A

Type: MC

Topic: Product Development and Marketing

Skill: Conceptual

AACSB: Reflective Thinking

- 6) In monopolistic competition, advertising costs
- A) are fixed costs.
  - B) can result in the firm producing an amount of output such that its average total cost is lower than if it did not advertise.
  - C) shift the *ATC* curve upward.
  - D) all of the above answers are correct.
  - E) none of the above answers are correct.

Answer: D

Type: MC

Topic: Product Development and Marketing

Skill: Recognition

AACSB: Reflective Thinking

- 7) Advertising costs in monopolistic competition increase a firm's
- A) total fixed cost.
  - B) marginal cost.
  - C) total variable cost.
  - D) average variable cost.
  - E) both A and B are correct.

Answer: A

Type: MC

Topic: Product Development and Marketing

Skill: Conceptual

AACSB: Reflective Thinking

- 8) If a firm spends \$600 on advertising, its
- A) *ATC* and *MC* curves shift upward.
  - B) *MC* curve shifts upward and its *ATC* curve does not shift.
  - C) *ATC* curve shifts upward and its *MC* curve does not shift.
  - D) *ATC* curve shifts upward and its *MC* curve shifts downward.
  - E) *AFC* and *AVC* curves shift upward.

Answer: C

Type: MC

Topic: Product Development and Marketing

Skill: Conceptual

AACSB: Reflective Thinking

- 9) Advertising costs are \_\_\_\_\_ costs and the per unit cost of advertising \_\_\_\_\_ as production increases.

- A) fixed; increases
- B) variable; increases
- C) fixed; decreases
- D) variable; does not change
- E) variable; decreases

Answer: C

Type: MC

Topic: Product Development and Marketing

Skill: Conceptual

AACSB: Reflective Thinking

- 10) Expenditures on advertising

- A) can lower average total cost if the advertising increases the quantity sold by a large enough amount.
- B) cannot lower average total cost because when a firm advertises it increases its costs.
- C) always lower average total cost because whenever a firm advertises, it increases the quantity sold.
- D) are variable costs so do not affect the average total cost.
- E) lower total cost if the advertising increases the quantity sold by a large enough amount.

Answer: A

Type: MC

Topic: Product Development and Marketing

Skill: Conceptual

AACSB: Reflective Thinking

- 11) Advertising costs of a monopolistically competitive firm are
- A) greater than a monopoly and the same as a perfectly competitive firm.
  - B) greater than a perfectly competitive firm.
  - C) less than a perfectly competitive firm.
  - D) the same as a monopoly.
  - E) less than a monopoly.

Answer: B

Type: MC

Topic: Product Development and Marketing

Skill: Conceptual

AACSB: Reflective Thinking

12) A textbook publisher is in monopolistic competition. If the firm spends nothing on advertising, it can sell no books at \$100 a book, but for each \$10 cut in price, the quantity of books it can sell increases by 20 books a day. The firm's total fixed cost is \$2,400 a day. Its average variable cost and marginal cost is a constant \$20 per book. If the firm spends \$1,200 a day on advertising, it can increase the quantity of books sold at each price by 50 percent. If the publisher advertises, its profit maximizing level of output is

- A) 120 books per day.
- B) 80 books per day.
- C) 160 books per day.
- D) 100 books per day.
- E) 240 books per day.

Answer: A

Type: MC

Topic: Product Development and Marketing

Skill: Analytical

AACSB: Analytical Skills

13) A textbook publisher is in monopolistic competition. If the firm spends nothing on advertising, it can sell no books at \$100 a book, but for each \$10 cut in price, the quantity of books it can sell increases by 20 books a day. The firm's total fixed cost is \$2,400 a day. Its average variable cost and marginal cost is a constant \$20 per book. If the firm spends \$1,200 a day on advertising, it can increase the quantity of books sold at each price by 50 percent. If the publisher advertises, its profit maximizing price per book is

- A) \$40.
- B) \$50.
- C) \$60.
- D) \$70.
- E) \$20.

Answer: C

Type: MC

Topic: Product Development and Marketing

Skill: Analytical

AACSB: Analytical Skills

Use the information below to answer the following question.

**Fact 14.3.1**

Suppose that at one of the Talbot's shops, marginal cost of a coat is constant at \$150, and total fixed cost is \$3,000 a day. The shop maximizes its profit by selling 15 coats a day at \$500 per coat. Then the shops nearby increase their advertising. The Talbot shop responds by spending \$1,500 a day more on advertising its coats. As a result, its profit-maximizing number of coats sold increases to 25 a day at \$400 per coat.

14) Refer to Fact 14.3.1. As a result of increased advertising, Talbot's markup

- A) decreases by \$100.
- B) increases by \$50.
- C) increases by \$75.
- D) decreases by \$60.
- E) decreases by an unknown amount.

Answer: A

Diff: 3 Type: MC

Topic: Product Development and Marketing

Skill: Analytical

AACSB: Analytical Skills

15) Other than by adjusting price, the two main ways in which a firm in monopolistic competition competes with other firms are by \_\_\_\_\_ and \_\_\_\_\_.

- A) innovation and product development; advertising
- B) taking surveys to discover the wants of its consumers; opening up new retail outlets
- C) changing its method of production; relocating its factories to areas with lower wage rates
- D) decreasing its workforce; using new technology
- E) advertising; producing the efficient quantity

Answer: A

Type: MC

Topic: Product Development and Marketing

Source: MyEconLab

16) Product innovation and development is efficient if the marginal social cost of a new and improved product \_\_\_\_\_ its marginal social benefit.

In monopolistic competition marginal revenue is less than price, so product innovation is probably \_\_\_\_\_ to its efficient level.

- A) is greater than; not pushed
- B) equals; pushed
- C) is greater than; pushed
- D) equals; not pushed
- E) is less than; not pushed

Answer: D

Type: MC

Topic: Product Development and Marketing

Source: MyEconLab

17) Advertising and brand names

A) are never efficient.

B) can be efficient but are not always efficient.

C) are equally efficient in monopolistically competitive markets and perfectly competitive markets.

D) are always efficient.

E) are more efficient in perfectly competitive markets than in monopolistically competitive markets.

Answer: B

Type: MC

Topic: Product Development and Marketing

Source: MyEconLab

*Use the information below to answer the following questions.*

**Fact 14.3.2**

Suppose that Tommy Hilfiger's marginal cost of a jacket is \$100 (a constant marginal cost) and at one of the firm's shops, total fixed cost is \$2,000 a day.

The profit-maximizing number of jackets sold in this shop is 20 a day.

Then the shops nearby start to advertise their jackets. The Tommy Hilfiger shop now spends \$2,000 a day advertising its jackets, and its profit-maximizing number of jackets sold jumps to 50 a day.

18) Refer to Fact.14.3.2. If advertising decreases demand and makes demand more elastic, the price of a Tommy Hilfiger jacket \_\_\_\_\_. If advertising increases demand and makes demand less elastic, the price of a Tommy Hilfiger jacket \_\_\_\_\_.

If price falls, markup \_\_\_\_\_.

If price rises, markup \_\_\_\_\_.

A) falls; rises; rises; falls

B) rises; falls; falls; rises

C) falls; rises; falls; rises

D) rises; falls; rises; falls

E) falls; rises; does not change; does not change

Answer: C

Type: MC

Topic: Product Development and Marketing

Source: MyEconLab

- 19) Refer to Fact 14.3.2. Tommy Hilfiger uses advertising as a signal because
- A) when Tommy Hilfiger advertises, it forces its competitors to advertise, which raises the competition's average total cost and increases the possibility of the competition incurring an economic loss and leaving the market.
  - B) only firms that can afford advertising have longevity and will be able to honor any future obligations to its customers.
  - C) by spending large sums of advertising Tommy Hilfiger is signaling that its jackets are high quality.
  - D) advertising encourages people to spend regardless of the quality.
  - E) advertising always increases demand and creates a more efficient market.

Answer: C

Type: MC

Topic: Product Development and Marketing

Source: MyEconLab

- 20) Refer to Fact 14.3.2. Having a brand name helps Tommy Hilfiger increase its economic profit because
- A) the goal of a brand name is to encourage people to buy just one good. After the initial purchases, Tommy Hilfiger can decrease quality and produce goods at a lower average total cost, which increases economic profit.
  - B) in every type of market, consumers are most comfortable when buying from a firm with a well-known brand name. And the greater the number of consumers, the greater is the economic profit.
  - C) a brand name provides an incentive to achieve high and consistent quality, and consumers will purchase goods from Tommy Hilfiger rather than from an unknown producer because they know what to expect from Tommy Hilfiger.
  - D) having a brand name usually leads to a monopoly.
  - E) none of the above.

Answer: C

Type: MC

Topic: Product Development and Marketing

Source: MyEconLab

21) Calvin is a custom picture framer. His total fixed cost is \$110 a day, and his average variable cost is \$1 a frame. He is maximizing his profit by selling 22 picture frames a day for \$6 a frame. Few people know about Calvin's Framery. Calvin thinks that if he spends \$10 a day on advertising, he can increase his market and sell 44 picture frames a day for \$6 a frame. If Calvin's belief about the effect of advertising is correct, he

- A) cannot increase his economic profit by advertising because advertising increases his average total cost.
- B) cannot increase his economic profit by advertising because advertising increases his total cost.
- C) can increase his economic profit by advertising.
- D) can increase his economic profit by advertising only if he raises the price of a picture frame.
- E) can increase his economic profit by advertising only if he can lower his total variable cost.

Answer: C

Type: MC

Topic: Product Development and Marketing

Source: MyEconLab

22) Firms in monopolistic competition constantly develop new products in an effort to

- A) increase the demand for their product.
- B) make the demand for their product unit elastic.
- C) increase the marginal cost of their product.
- D) decrease average total cost.
- E) decrease average fixed cost.

Answer: A

Type: MC

23) Excess capacity and high advertising expenditures are encountered in

- A) monopoly.
- B) oligopoly.
- C) monopolistic competition.
- D) perfect competition.
- E) all markets.

Answer: C

Type: MC

24) Monopolistically competitive firms engaging in advertising will definitely achieve which of the following?

- A) an increase in demand
- B) an increase in average total cost
- C) an increase in total cost
- D) Both B and C are correct.
- E) A, B, and C are correct.

Answer: C

Type: MC

## Chapter 15 Oligopoly

### 15.1 What Is Oligopoly

1) The market structure in which natural or legal barriers prevent the entry of new firms and a small number of firms compete is

- A) monopoly.
- B) monopolistic competition.
- C) perfect competition.
- D) oligopoly.
- E) duopoly.

Answer: D

Diff: 1 Type: MC

Topic: What Is Oligopoly?

2) Suppose that industry A consists of four firms who collectively control 96 percent of total sales in the market. We can conclude that industry A is

- A) perfectly competitive.
- B) a duopoly.
- C) monopolistically competitive.
- D) an oligopoly.
- E) a monopoly.

Answer: D

Diff: 2 Type: MC

Topic: What Is Oligopoly?

3) Which one the following industries is the best example of an oligopoly?

- A) the market for wheat
- B) the fast-food industry
- C) the automobile industry
- D) the clothing industry
- E) the restaurant industry

Answer: C

Diff: 1 Type: MC

Topic: What Is Oligopoly?

4) Which one of the following industries is the best example of an oligopoly?

- A) the battery industry
- B) the sporting goods industry
- C) the footwear industry
- D) the cosmetics industry
- E) the power industry

Answer: A

Diff: 1 Type: MC

Topic: What Is Oligopoly?

5) Which one of the following characteristics applies to oligopolistic markets?

- A) There is a large number of firms.
- B) The absence of barriers to entry of firms.
- C) Firms are large relative to the size of the market.
- D) All firms are price takers.
- E) Firms produce only differentiated products.

Answer: C

Diff: 1 Type: MC

Topic: What Is Oligopoly?

6) Which one of the following characteristics applies to oligopolistic markets?

- A) There is free entry of rival firms.
- B) Firms are so large relative to the market that they do not have to consider the behaviour of rival firms.
- C) Firms are mutually independent because there are many firms in the industry.
- D) Firms have to consider the behaviour of their rivals since their rivals are also large relative to the size of the market as a whole.
- E) Economic profit of each firm equals zero.

Answer: D

Diff: 2 Type: MC

Topic: What Is Oligopoly?

7) Why might only a few firms dominate an oligopolistic industry?

- A) A natural or legal barrier to entry exists.
- B) Perfectly elastic demand makes small-scale operation economically inefficient.
- C) Decreasing returns to scale may make small-scale firms more advantageous.
- D) Inelastic market demand leads to the domination of the industry by a few firms.
- E) It is due to the outcome of the prisoners' dilemma.

Answer: A

Diff: 2 Type: MC

Topic: What Is Oligopoly?

8) Firm X is competing in an oligopolistic industry. When firm X increases its price

- A) then rival firm Y will always increase its price.
- B) then rival firm Y will increase its market share if firm Y also increases its price.
- C) then the behaviour of rival firm Y will have no impact on the market share of firm X.
- D) the market as a whole will become less profitable.
- E) the rival firm Y will increase its market share if firm Y keeps a constant price.

Answer: E

Diff: 2 Type: MC

Topic: What Is Oligopoly?

9) Which is *not* a characteristic of oligopoly?

- A) Each firm faces a downward-sloping demand curve.
- B) Firms are profit-maximizers.
- C) The sales of one firm will not have a significant effect on other firms.
- D) There is more than one firm in the industry.
- E) Firms set prices.

Answer: C

Diff: 2 Type: MC

Topic: What Is Oligopoly?

Source: Study Guide

10) If the efficient scale of production only allows three firms to supply a market, the market is a

- A) three-firm monopoly.
- B) cost-based oligopoly.
- C) natural oligopoly.
- D) monopolistic competition.
- E) competitive monopoly.

Answer: C

Diff: 1 Type: MC

Topic: What Is Oligopoly?

Source: Study Guide

11) A cartel is a group of firms which agree to

- A) behave competitively.
- B) raise the price of their products.
- C) lower the price of their products.
- D) increase the amount they produce.
- E) cheat on each other.

Answer: B

Diff: 1 Type: MC

Topic: What Is Oligopoly?

Source: Study Guide

12) Because an oligopoly has a small number of firms

- A) each firm can act like a monopoly.
- B) the firms may legally form a cartel.
- C) the HHI for the industry is small.
- D) the four-firm concentration ratio for the industry is small.
- E) the firms are interdependent.

Answer: E

Diff: 1 Type: MC

Topic: What Is Oligopoly?

Source: Study Guide

13) Complete the following sentence. A duopoly is

- A) a market where three dominant firms collude to decide the profit-maximizing price.
- B) a market where two firms compete for profit and market share.
- C) the same as a monopoly.
- D) not an oligopoly.
- E) a market with two distinct products.

Answer: B

Diff: 1 Type: MC

Topic: What Is Oligopoly?

14) A duopoly occurs when \_\_\_\_\_.

- A) there are only two producers of a particular good competing in the same market
- B) there are two producers of two goods competing in an oligopoly market
- C) there are numerous producers of two goods competing in a competitive market
- D) the one producer of two goods sells the goods in a monopoly market
- E) a competitive market produces two goods

Answer: A

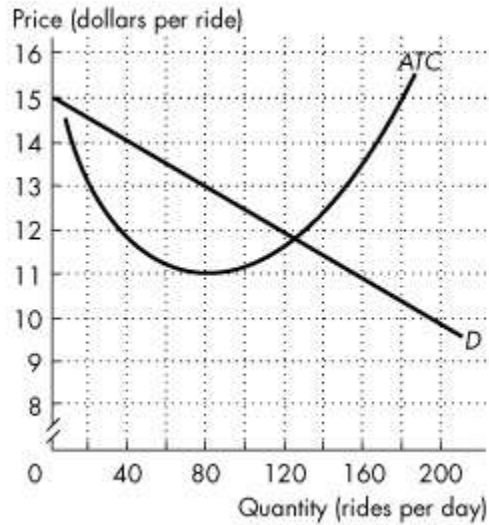
Type: MC

Topic: What Is Oligopoly?

Skill: Recognition

AACSB: Reflective Thinking

Use the figure below to answer the following question.



**Figure 15.1.1**

In the figure, *D* is the demand curve for taxi rides in a town, and *ATC* is the average total cost curve of a taxi company.

15) Refer to Figure 15.1.1. In the scenario above, the market is:

- A) A natural duopoly
- B) A natural oligopoly with three firms
- C) A natural monopoly
- D) Monopolistically competitive
- E) perfectly competitive

Answer: A

Diff: 2 Type: MC

Topic: What Is Oligopoly?

Skill: Analytical

AACSB: Analytical Skills

16) A monopolistically competitive firm is like an oligopolistic firm insofar as

- A) both face perfectly elastic demand.
- B) both can earn an economic profit in the long run.
- C) both have *MR* curves that lie beneath their demand curves.
- D) neither is protected by high barriers to entry.
- E) both are price takers.

Answer: C

Type: MC

Topic: What Is Oligopoly?

Skill: Conceptual

AACSB: Reflective Thinking

17) An oligopoly is a market structure in which there

- A) are a few buyers but many sellers.
- B) are no barriers to entry.
- C) are many independent sellers.
- D) are a few goods sold by many sellers.
- E) is a temptation to collude.

Answer: E

Type: MC

18) The distinguishing features of oligopoly are \_\_\_\_\_ and \_\_\_\_\_ in the industry.

- A) no barriers to entry; a small number of firms
- B) barriers to entry; a large number of firms
- C) no barriers to entry; a large number of firms
- D) barriers to entry; one firm
- E) barriers to entry; a small number of firms

Answer: E

Type: MC

19) Oligopoly is similar to

- A) perfect competition because both market types produce identical goods.
- B) perfect competition because both firms in both market types make zero economic profit in the long run.
- C) monopoly because both market types have barriers to entry.
- D) monopoly because both market types have a single firm.
- E) monopolistic competition because firms in both markets face a perfectly elastic demand.

Answer: C

Type: MC

20) In an oligopoly market, the Herfindahl-Hirschman Index is usually

- A) below 1,800.
- B) zero.
- C) above 1,800.
- D) equal to 10,000.
- E) between 100 and 1,000.

Answer: C

Type: MC

## 15.2 Oligopoly Games

1) All games share four common features. They are

- A) costs, prices, profit, and strategies.
- B) revenues, elasticity, profit, and payoffs.
- C) rules, strategies, profit, and outcome.
- D) patents, copyrights, barriers to entry, and rules.
- E) rules, strategies, payoffs, and outcome.

Answer: E

Diff: 2 Type: MC

Topic: Oligopoly Games

2) Prisoners' dilemma describes a case where

- A) collusion of the participants leads to the best solution from their point of view.
- B) rivalry among a large number of rivals leads to lower overall profit.
- C) one prisoner has no chance to be acquitted since there is no other prisoner to support his testimony.
- D) a prisoner has no incentive to confess to his crime, and stands a greater chance of not going to prison.
- E) rivalry of the participants leads to the worst solution from their point of view.

Answer: E

Diff: 2 Type: MC

Topic: Oligopoly Games

Use the table below to answer the following questions.

**Table 15.2.1**

		Bob	
		Confess	Don't
Joe	Confess	B: 10 years J: 10 years	B: 20 years J: 1 year
	Don't	B: 1 year J: 20 years	B: Go free J: Go free

3) Refer to Table 15.2.1. This table includes the sentences that Bob and Joe will receive if convicted. They have been apprehended by the police under the suspicion of committing armed robbery. The two are immediately separated and questioned about the case. Which one of the following observations is correct?

- A) Bob would be smart to confess no matter what Joe does.
- B) Joe would be smart not to confess no matter what Bob does.
- C) Both Bob and Joe would be better off not confessing if they both do not confess.
- D) Both Bob and Joe would be better off "coming clean" and confessing to their crime.
- E) Both Bob and Joe have a dominant strategy of not confessing.

Answer: C

Diff: 2 Type: MC

Topic: Oligopoly Games

4) Refer to Table 15.2.1. This table includes the sentences that Bob and Joe will receive if convicted. They have been apprehended by the police under the suspicion of committing armed robbery. The two are immediately separated and questioned about the case. Which one of the following observations is correct?

- A) If Joe confesses, Bob would be better off not confessing.
- B) If Bob confesses, Joe would be better off confessing.
- C) The outcome of the game, assuming Joe and Bob cannot collude, is they will both go free.
- D) If Joe does not confess, Bob would be better off confessing.
- E) The outcome of the game, assuming Joe and Bob cannot collude, is they will both confess.

Answer: B

Diff: 2 Type: MC

Topic: Oligopoly Games

5) Which one of the following is *not* a feature common to all games?

- A) rules
- B) collusion
- C) strategies
- D) payoffs
- E) an outcome

Answer: B

Diff: 2 Type: MC

Topic: Oligopoly Games

Source: Study Guide

6) In the prisoners' dilemma with players Art and Bob, each prisoner would be best off if

- A) both prisoners confess.
- B) both prisoners deny.
- C) Art denies and Bob confesses.
- D) Bob denies and Art confesses.
- E) none of the above is done.

Answer: B

Diff: 2 Type: MC

Topic: Oligopoly Games

Source: Study Guide

7) In the prisoners' dilemma, with players Art and Bob, the dominant strategy equilibrium is that

- A) both prisoners confess.
- B) neither prisoner confesses.
- C) Art denies and Bob confesses.
- D) indeterminate.
- E) Bob denies and Art confesses.

Answer: A

Diff: 2 Type: MC

Topic: Oligopoly Games

8) A dominant strategy equilibrium occurs when

- A) there is a clear strategy for each player independent of the other player's actions.
- B) each player takes the best possible action given the other player's action.
- C) each player complies with the collusive agreement.
- D) you cooperate until the other player cheats, and then you cheat forever.
- E) none of the above.

Answer: A

Diff: 3 Type: MC

Topic: Oligopoly Games

- 9) A Nash equilibrium occurs when
- A) there is a clear strategy for each player independent of the other player's actions.
  - B) each player takes the best possible action given the other player's action.
  - C) each player complies with the collusive agreement.
  - D) you cooperate until the other player cheats, and then you cheat forever.
  - E) none of the above.

Answer: B

Diff: 3 Type: MC

Topic: Oligopoly Games

- 10) For a cartel to succeed,
- A) it does not need the cooperation of a majority of firms in the industry.
  - B) there must be free entry of rival firms.
  - C) consumers must have alternative products available to satisfy the same need.
  - D) no major producer can remain outside the agreement of the cartel.
  - E) the industry must have an elastic demand.

Answer: D

Diff: 2 Type: MC

Topic: Oligopoly Games

- 11) Once a cartel determines the profit-maximizing price,
- A) all members of the cartel have a strong incentive to abide by the agreed-upon price.
  - B) each member will face the temptation to cheat on the cartel price to increase its sales and profit.
  - C) changes in the output of any member firms will have no impact on the market price.
  - D) entry into the industry of rival firms will have no impact on the profit of the cartel.
  - E) entry into the industry of rival firms will raise cartel profit as long as the new firms join the cartel.

Answer: B

Diff: 2 Type: MC

Topic: Oligopoly Games

- 12) In a cartel, the incentive to cheat is significant because
- A) each individual member has the incentive to restrict its own output to maximize profit.
  - B) the marginal cost is equal to the cartel price at the profit-maximizing output level.
  - C) each firm has the incentive to lower its price to sell more than the allotted amount.
  - D) each firm has the incentive to cheat by raising its price to maximize profit.
  - E) price is less than marginal cost for each member of the cartel.

Answer: C

Diff: 2 Type: MC

Topic: Oligopoly Games

- 13) If there is a successful collusive agreement in a duopoly to maximize profit,
- A) the market price will equal the marginal cost of production.
  - B) the market price will equal the average total cost of production.
  - C) the price will be the same as the price in a perfectly competitive market.
  - D) the price will be the monopoly price.
  - E) the market marginal revenue will be the same as the demand curve.

Answer: D

Diff: 2 Type: MC

Topic: Oligopoly Games

- 14) If a duopoly collusive agreement is made that maximizes joint profit,
- A) each of the duopolists has no incentive to cheat on the agreement.
  - B) each duopolist has the incentive to cheat on the duopoly agreement by lowering the price.
  - C) each duopolist has the incentive to cheat on the agreement by increasing the price to make monopoly profit.
  - D) there is no concern over the entrance of potential rivals, since they cannot decrease the duopolists' profit.
  - E) the dominant strategy is to collude.

Answer: B

Diff: 3 Type: MC

Topic: Oligopoly Games

- 15) Consider a duopoly with collusion. If the duopoly maximizes profit,
- A) each firm will produce the same amount.
  - B) each firm will produce its maximum output possible.
  - C) industry marginal revenue will equal industry marginal cost at the level of total output.
  - D) industry demand will equal industry marginal cost at the level of total output.
  - E) none of the above.

Answer: C

Diff: 2 Type: MC

Topic: Oligopoly Games

Source: Study Guide

- 16) The firms Trick and Gear form a cartel to collude to maximize profit. If this game is nonrepeated, the Nash equilibrium is
- A) both firms cheat on the agreement.
  - B) both firms comply with the agreement.
  - C) Trick cheats, while Gear complies with the agreement.
  - D) Gear cheats, while Trick complies with the agreement.
  - E) unknown.

Answer: A

Diff: 3 Type: MC

Topic: Oligopoly Games

Source: Study Guide

Use the table below to answer the following questions.

**Table 15.2.2**

		Firm B	
		Lower Prices	Higher Prices
Firm A	Lower Prices	A: \$2 B: \$5	A: \$20 B: -\$10
	Higher Prices	A: -\$10 B: \$25	A: \$10 B: \$20

17) Table 15.2.2 gives the payoff matrix in terms of economic profit for firms *A* and *B* when there are two strategies facing each firm: (1) charge a low price, or (2) charge a high price. The equilibrium in this game (played once) will be a dominant strategy equilibrium because

A) firm *B* will reduce profit by more than *A* if both charge a lower price.  
 B) firm *B* is the dominant firm.  
 C) the best strategy for each firm does not depend on the strategy chosen by the other firm.  
 D) there is no credible threat by either firm to "punish" the other if it breaks the agreement.  
 E) all of the above.

Answer: C

Diff: 3 Type: MC

Topic: Oligopoly Games

Source: Study Guide

18) Table 15.2.2 gives the payoff matrix in terms of economic profit for firms *A* and *B* when there are two strategies facing each firm: (1) charge a low price, or (2) charge a high price. Refer to the nonrepeated game in the table. In Nash equilibrium, firm *A* will make an economic profit of

- A) -\$10.  
 B) \$2.  
 C) \$10.  
 D) \$20.  
 E) \$5.

Answer: B

Diff: 3 Type: MC

Topic: Oligopoly Games

Source: Study Guide

19) Table 15.2.2 gives the payoff matrix in terms of economic profit for firms *A* and *B* when there are two strategies facing each firm: (1) charge a low price, or (2) charge a high price. Refer to the nonrepeated game in the table. If both firms could successfully collude, what would be firm *A*'s economic profit?

- A) -\$10
- B) \$2
- C) \$10
- D) \$20
- E) \$5

Answer: C

Diff: 3 Type: MC

Topic: Oligopoly Games

Source: Study Guide

20) Consider a cartel consisting of several firms that is maximizing total profit. If one firm cheats on the cartel agreement by cutting its price and increasing its output, the best response of the other firms is to

- A) cancel the cheating firm's membership in the cartel.
- B) continue to sell at the agreed-upon price.
- C) raise their price to recapture lost profit.
- D) cut their prices as well.
- E) cut output to keep total cartel output at its original level.

Answer: D

Diff: 2 Type: MC

Topic: Oligopoly Games

21) It is difficult to maintain a cartel for a long period of time. Which one of the following is the most important reason?

- A) Each firm has an incentive to collude.
- B) Other firms will enter the industry.
- C) Firms in the cartel will want to raise the price.
- D) Consumers will eventually decide not to buy the cartel's output.
- E) Each firm has an incentive to cheat.

Answer: E

Diff: 2 Type: MC

Topic: Oligopoly Games

22) There exists an incentive to cheat on a collusive agreement as long as

- A) price equals marginal cost.
- B) price equals marginal revenue.
- C) price exceeds marginal cost.
- D) price is above minimum average total cost.
- E) none of the above.

Answer: C

Diff: 3 Type: MC

Topic: Oligopoly Games

Use the table below to answer the following question.

**Table 15.2.3**

		Store X	
		Lower Prices	Don't Lower Prices
Store Y	Lower Prices	X: \$5 Y: \$5	X: \$1 Y: \$10
	Don't Lower Prices	X: \$10 Y: \$1	X: \$20 Y: \$20

23) Refer to Table 15.2.3. Store X and Store Y must decide whether or not to lower their prices. The table gives the economic profit made by Store X and Store Y. Which one of the following observations is correct?

- A) Both Store X and Store Y have a dominant strategy of raising their prices.
- B) If Store X lowers its prices and Store Y does not, Store X will earn a \$20 profit.
- C) If Store Y lowers its prices, Store X will be better off not lowering its prices.
- D) Both Store X and Store Y would be better off if they could collude and agree to not lower prices.
- E) Both Store X and Store Y have a dominant strategy of lowering their prices.

Answer: D

Diff: 3 Type: MC

Topic: Oligopoly Games

24) In the research and development game of chicken

- A) the best strategy for each player is to undertake research and development.
- B) the best strategy is for neither player to undertake research and development.
- C) the equilibrium is for only one firm to undertake research and development.
- D) the equilibrium is unique.
- E) no solution can be found.

Answer: C

Diff: 3 Type: MC

Topic: Oligopoly Games

Use the table below to answer the following questions.

**Table 15.2.4**

		Bud Light	
		Offer New Ads	Don't Offer New Ads
Miller Lite	Offer New Ads	B: \$100 M: \$100	B: \$50 M: \$200
	Don't Offer New Ads	B: \$200 M: \$50	B: \$120 M: \$120

25) Refer to Table 15.2.4 The marketers of Budweiser Light beer and Miller Lite beer must decide whether or not to offer new advertising campaigns promoting their products. The payoffs in the table are the economic profit made by Bud and Miller. Which one of the following observations is correct?

- A) This is not a game described as a prisoners' dilemma.
- B) If Bud offers a new advertising campaign and Miller does not, Bud will make a \$200 profit.
- C) Miller has a dominant strategy but Bud does not.
- D) Both Bud and Miller would be better off if they could collude and both offer new ads.
- E) If Miller offers a new advertising campaign and Bud does not, Bud will make a \$100 profit.

Answer: B

Diff: 3 Type: MC

Topic: Oligopoly Games

26) Refer to Table 15.2.4. The marketers of Budweiser Light beer and Miller Lite beer must decide whether or not to offer new advertising campaigns promoting their products. The payoffs in the table are the economic profit made by Bud and Miller. Which one of the following observations is correct?

- A) This game has no dominant strategies.
- B) This game has no Nash equilibrium.
- C) Miller has a dominant strategy but Bud does not.
- D) Bud has a dominant strategy but Miller does not.
- E) Bud and Miller each have a dominant strategy.

Answer: E

Diff: 3 Type: MC

Topic: Oligopoly Games

27) Refer to Table 15.2.4. The marketers of Budweiser Light beer and Miller Lite beer must decide whether or not to offer new advertising campaigns promoting their products. The payoffs in the table are the economic profit made by Bud and Miller. Which one of the following observations is correct?

- A) The equilibrium of the game is that both firms will conduct new advertising campaigns.
- B) The equilibrium of the game is that neither firm will conduct a new advertising campaign.
- C) The equilibrium solution has Bud conducting a new advertising campaign, but not Miller.
- D) The equilibrium solution has Miller conducting a new advertising campaign, but not Bud.
- E) There is no equilibrium to this game—the industry will have alternating cycles of advertising and no advertising.

Answer: A

Diff: 3 Type: MC

Topic: Oligopoly Games

28) Refer to Table 15.2.4. The marketers of Budweiser Light beer and Miller Lite beer must decide whether or not to offer new advertising campaigns promoting their products. The payoffs in the table are the economic profit made by Bud and Miller. Which one of the following observations is correct?

- A) This is a game described as a prisoners' dilemma.
- B) If Bud offers a new advertising campaign and Miller does not, Bud will earn a \$100 profit.
- C) If Bud offers a new advertising campaign, then Miller will be better off by not offering a new advertising campaign.
- D) Both Bud and Miller would be better off if they could collude and agree to coordinate their new advertising campaigns.
- E) If Miller does not offer a new advertising campaign, then Bud is better off if it doesn't offer a new advertising campaign.

Answer: A

Diff: 3 Type: MC

Topic: Oligopoly Games

Use the table below to answer the following questions.

**Table 15.2.5**

		Firm 1	
		Sell	Give away
Firm 2	Sell	1: \$3 2: \$3	1: \$4 2: -\$1
	Give away	1: -\$1 2: \$4	1: \$2 2: \$2

29) Refer to Table 15.2.5. Two software firms have developed an identical new software application. They are debating whether to give the new application away free and then sell add-ons or sell the application at \$30 a copy. The payoff matrix is above and the payoffs are profits in millions of dollars. What is Firm 1's best strategy?

- A) Give away the application regardless of what Firm 2 does.
- B) Sell the application at \$30 a copy regardless of what Firm 2 does.
- C) Give away the application only if Firm 2 sells the application.
- D) Give away the application only if Firm 2 gives away the application.
- E) Sell the application only if Firm 2 sells the application.

Answer: A

Type: MC

Topic: Oligopoly Games

Skill: Analytical

AACSB: Analytical Skills

30) Refer to Table 15.2.5. Two software firms have developed an identical new software application. They are debating whether to give the new application away free and then sell add-ons or sell the application at \$30 a copy. The payoff matrix is above and the payoffs are profits in millions of dollars. What is the Nash equilibrium of the game?

- A) Both Firm 1 and 2 will sell the software application at \$30 a copy.
- B) Both Firm 1 and 2 will give the software application away free.
- C) Firm 1 will give the application away free and Firm 2 will sell it at \$30.
- D) There is no Nash equilibrium to this game.
- E) Firm 1 will sell the application for \$30 and Firm 2 will give it away.

Answer: B

Type: MC

Topic: Oligopoly Games

Skill: Analytical

AACSB: Analytical Skills

Refer to the table below to answer the following question.

**Table 15.2.6**

		Firm A	
		R&D	No R&D
Firm B	R&D	A: \$25 B: \$15	A: -\$3 B: \$60
	No R&D	A: \$60 B: -\$3	A: \$50 B: \$35

31) Refer to Table 15.2.6. Firms A and B can conduct research and development (R&D) or not conduct it. R&D is costly but can increase the quality of the product and increase sales. The payoff matrix is the economic profits of the two firms and is given above, where the numbers are millions of dollars. A's best strategy is to

- A) conduct R&D regardless of what B does.
- B) not conduct R&D regardless of what B does.
- C) conduct R&D only if B conducts R&D.
- D) conduct R&D only if B does not conduct R&D.
- E) not conduct R&D only if B does not conduct R&D.

Answer: A

Type: MC

Topic: Oligopoly Games

Skill: Analytical

AACSB: Analytical Skills

32) Refer to Table 15.2.6. Firms A and B can conduct research and development (R&D) or not conduct it. R&D is costly but can increase the quality of the product and increase sales. The payoff matrix is the economic profits of the two firms and is given above, where the numbers are millions of dollars. The Nash equilibrium occurs when

- A) both A and B conduct R&D.
- B) only A conducts R&D.
- C) only B conducts R&D.
- D) neither A nor B conduct R&D.
- E) there is no Nash equilibrium.

Answer: A

Type: MC

Topic: Oligopoly Games

Skill: Analytical

AACSB: Analytical Skills

Refer to the table below to answer the following questions.

**Table 15.2.7**

		Disney	
		Thanksgiving Release	Christmas Release
Fox	Thanksgiving Release	D: \$100 F: \$80	D: \$105 F: \$95
	Christmas Release	D: \$110 F: \$100	D: \$95 F: \$85

33) Refer to Table 15.2.7. Disney and Fox must decide when to release their next films. The revenues received by each studio depends in part on when the other studio releases its film. Each studio can release its film at Thanksgiving or at Christmas. The revenues received by each studio, in millions of dollars, are given in the payoff matrix above. Which of the following statements correctly describes Fox's strategy given what Disney's release choice may be?

- A) If Disney chooses a Thanksgiving release, Fox should choose a Christmas release.
- B) If Disney chooses a Christmas release, Fox should choose a Thanksgiving release.
- C) Fox should release on Christmas regardless of what Disney does.
- D) Fox should release on Thanksgiving regardless of what Disney does.
- E) Both answers A and B are correct.

Answer: E

Type: MC

Topic: Oligopoly Games

Skill: Analytical

AACSB: Analytical Skills

34) Refer to Table 15.2.7. Disney and Fox must decide when to release their next films. The revenues received by each studio depends in part on when the other studio releases its film. Each studio can release its film at Thanksgiving or at Christmas. The revenues received by each studio, in millions of dollars, are given in the payoff matrix above. Which of the following statements correctly describes Disney's strategy given what Fox's release choice may be?

- A) If Fox chooses a Thanksgiving release, Disney should choose a Christmas release.
- B) If Fox chooses a Christmas release, Disney should choose a Thanksgiving release.
- C) Disney should release on Thanksgiving regardless of what Fox does.
- D) Disney should release on Christmas regardless of what Fox does.
- E) Both answers A and B are correct.

Answer: E

Type: MC

Topic: Oligopoly Games

Skill: Analytical

AACSB: Analytical Skills

Refer to the table below to answer the following questions.

**Table 15.2.8**

		Dr. Smith	
		Advertise	Don't Advertise
Dr. Jones	Advertise	S: \$80 J: \$70	S: \$60 J: \$110
	Don't Advertise	S: \$120 J: \$60	S: \$100 J: \$90

35) Refer to Table 15.2.8. Libertyville has two optometrists, Dr. Smith and Dr. Jones. Each optometrist can choose to advertise his service or not. The incomes of each optometrist, in thousands of dollars, are given in the payoff matrix above. Which of the following statements correctly describes Dr. Smith's strategy given what Dr. Jones may do?

- A) Dr. Smith advertises no matter what Dr. Jones does.
- B) Dr. Smith does not advertise no matter what Dr. Jones does.
- C) Dr. Smith advertises only if Dr. Jones doesn't advertise.
- D) Dr. Smith advertises only if Dr. Jones advertises.
- E) Dr. Smith does not advertise if Dr. Jones advertises.

Answer: A

Type: MC

Topic: Oligopoly Games

Skill: Analytical

AACSB: Analytical Skills

36) Refer to Table 15.2.8. Libertyville has two optometrists, Dr. Smith and Dr. Jones. Each optometrist can choose to advertise his service or not. The incomes of each optometrist, in thousands of dollars, are given in the payoff matrix above. Which of the following statements correctly describes Dr. Jones' strategy given what Dr. Smith may do?

- A) Dr. Jones advertises no matter what Dr. Smith does.
- B) Dr. Jones does not advertise no matter what Dr. Smith does.
- C) Dr. Jones advertises only if Dr. Smith doesn't advertise.
- D) Dr. Jones advertises only if Dr. Smith advertises.
- E) Dr. Jones does not advertise if Dr. Smith advertises.

Answer: A

Type: MC

Topic: Oligopoly Games

Skill: Analytical

AACSB: Analytical Skills

37) Refer to Table 15.2.8. Libertyville has two optometrists, Dr. Smith and Dr. Jones. Each optometrist can choose to advertise his service or not. The incomes of each optometrist, in thousands of dollars, are given in the payoff matrix above. Which of the following statements correctly categorizes the Nash equilibrium for the game?

- A) The game has a Nash equilibrium in which both optometrists advertise.
- B) The game has a Nash equilibrium in which both optometrists do not advertise.
- C) The game has a Nash equilibrium in which Dr. Smith advertises and Dr. Jones does not advertise.
- D) The game has a Nash equilibrium in which Dr. Smith does not advertise and Dr. Jones does advertise.
- E) The game has no Nash equilibrium.

Answer: A

Type: MC

Topic: Oligopoly Games

Skill: Analytical

AACSB: Analytical Skills

*Refer to the table below to answer the following question.*

**Table 15.2.9**

		Student 1	
		Work	Don't work
Student 2	Work	1: +10 2: +10	1: +5 2: +5
	Don't	1: +5 2: +50	1: 0 2: 0

38) Refer to Table 15.2.9. Two students are assigned a group project. Each has the option to work or not work to achieve a high grade. The payoffs are shown in the above table. Student 1

- A) works only if student 2 works.
- B) works regardless of the decision made by student 2.
- C) does not work if student 2 works.
- D) does not work regardless of what student 2 decides.
- E) works only if student 2 does not work.

Answer: B

Type: MC

Topic: Oligopoly Games

Skill: Analytical

AACSB: Analytical Skills

Refer to the table below to answer the following questions.

**Table 15.2.10**

		Firm A	
		Comply	Cheat
Firm B	Comply	A: \$1m B: \$1m	A: \$1.5m B: -\$0.5m
	Cheat	A: -\$0.5m B: \$1.5m	A: 0 B: 0

39) Refer to Table 15.2.10. Firm A and Firm B are the only producers of soap powder. They collude and agree to share the market equally. The payoff matrix shows the game they play. The equilibrium of the game is that Firm A \_\_\_\_\_ and Firm B \_\_\_\_\_.

- A) complies; cheats
- B) cheats; complies
- C) complies; complies
- D) cheats; cheats
- E) makes an economic profit; incurs an economic loss

Answer: D

Diff: 3 Type: MC

Topic: Oligopoly Games

Source: MyEconLab

40) Refer to Table 15.2.10. Firm A and Firm B are the only producers of soap powder. They collude and agree to share the market equally. The equilibrium \_\_\_\_\_ a dominant strategy equilibrium because the strategy in this game is for a firm \_\_\_\_\_.

- A) is; to comply regardless of the other firm's choice
- B) is not; to comply when the other firm cheats and to cheat when the other firm complies
- C) is; to cheat regardless of the other firm's choice
- D) is not; to comply when the other firm complies and to cheat when the other firm cheats
- E) is; to comply when the other firm cheats and to cheat when the other firm complies

Answer: C

Diff: 3 Type: MC

Topic: Oligopoly Games

Source: MyEconLab

41) The equilibrium strategy for each firm in a duopolist's dilemma is to \_\_\_\_\_. Firms \_\_\_\_\_ succeed in raising price and profits because each firm \_\_\_\_\_.

- A) comply; do not; makes a smaller economic profit if it complies with the agreement, but complying with the agreement is in the social interest, and most firms support the social interest
- B) comply; do; makes greater economic profit if it complies with the agreement, regardless of how the other firm acts
- C) cheat; do not; makes greater economic profit if it cheats on the agreement, regardless of how the other firm acts
- D) cheats; do; makes greater economic profit if it cheats on the agreement, regardless of how the other firm acts
- E) cheat; do; refuses to sell at any price below the monopoly price

Answer: C

Diff: 3 Type: MC

Topic: Oligopoly Games

Source: MyEconLab

42) In a prisoners' dilemma game, which of the following strategies gives the best outcome for *both* prisoners?

- A) Both prisoners deny.
- B) Both prisoners confess.
- C) One player confesses and the other player denies.
- D) Both prisoners hire good lawyers.
- E) none of the above

Answer: A

Type: MC

43) Caven and John have been arrested by the police, who have evidence that will convict them of robbing a bank. If convicted, each will receive a sentence of 6 years for the robbery. During questioning, the police suspect that Caven and John are responsible for a series of bank robberies. If both confess to the series, each will receive 12 years in jail. If only one confesses, he will receive 4 years and the one who does not confess will receive 14 years. What is the equilibrium for this game?

- A) Both deny.
- B) Caven confesses and John denies.
- C) John confesses and Caven denies.
- D) Both confess.
- E) None of the above

Answer: D

Type: MC

44) Two firms, Alpha and Beta, produce identical computer hard drives. They have identical costs, and the hard drives they produce are identical. The industry is a natural duopoly. Alpha and Beta enter into a collusive agreement, according to which they split the market equally. If both firms comply with the agreement,

A) together they will produce the monopoly quantity and make the monopoly economic profit.

B) the price of a hard drive will equal marginal cost.

C) each firm will make zero economic profit.

D) the oligopoly will produce more hard drives than a profit-maximizing monopoly would produce.

E) the oligopoly will produce fewer hard drives than a profit-maximizing monopoly would produce.

Answer: A

Type: MC

45) Two firms, Alpha and Beta, produce identical computer hard drives. They have identical costs, and the hard drives they produce are identical. The industry is a natural duopoly. Alpha and Beta enter into a collusive agreement, according to which they split the market equally. If both firms cheat on the agreement so the market is the same as a competitive market,

A) each firm makes zero economic profit in the long run.

B) each firm makes the monopoly profit.

C) the oligopoly will produce fewer hard drives than a profit-maximizing monopoly would produce.

D) the oligopoly will produce the same number of hard drives as a profit-maximizing monopoly would produce.

E) each firm incurs an economic loss and exits the market in the long run.

Answer: A

Type: MC

46) The maximum *total* economic profit that can be made by colluding duopolists

A) equals the economic profit made by a monopoly.

B) exceeds the economic profit made by a monopoly.

C) is less than the economic profit made by a monopoly.

D) is zero.

E) cannot be determined.

Answer: A

Type: MC

### 15.3 Repeated Games and Sequential Games

1) Consider a "prisoners' dilemma" game consisting of two firms in collusion to maximize profit. However, the game is repeated indefinitely and each player employs a tit-for-tat strategy. The equilibrium described here is called a

- A) credible strategy equilibrium.
- B) dominant player equilibrium.
- C) duopoly equilibrium.
- D) trigger strategy equilibrium.
- E) cooperative equilibrium.

Answer: E

Diff: 3 Type: MC

Topic: Repeated Games and Sequential Games

Use the table below to answer the following question.

**Table 15.3.1**

		Hare Gas Bar's Choices	
		\$1.15/litre	\$0.95/litre
Turtle Gas Bar's Choices	\$1.15/litre	H: \$500 T: \$500	H: \$1,000 T: \$50
	\$0.95/litre	H: \$50 T: \$1,000	H: \$200 T: \$200

2) Consider the game shown in Table 15.3.1 based on potential gas prices between two competitors. The game is played repeatedly and the result is a cooperative equilibrium. The payoffs in the table show the economic profit of the firms. The most likely outcome is

- A) a cycle of first \$0.95/litre, then \$1.15/litre, etc.
- B) Hare sets her prices at \$1.15/litre, and Turtle sets his at \$0.95/litre.
- C) Hare sets her prices at \$0.95/litre, and Turtle sets his at \$1.15/litre.
- D) both set their prices at \$1.15/litre.
- E) both set their prices at \$0.95/litre.

Answer: D

Diff: 3 Type: MC

Topic: Repeated Games and Sequential Games

- 3) Limit pricing is the practice of
- A) limiting the amount that can be purchased to drive up prices.
  - B) threatening to go to the limit in a price war if someone enters your market.
  - C) charging a monopoly price, but producing a quantity greater than the quantity at which  $MC = MR$ .
  - D) setting the price at the highest level that inflicts a loss on the entrant.
  - E) charging a price higher than the monopoly price, but producing a quantity greater than the quantity at which  $MC = MR$ .

Answer: D

Diff: 3 Type: MC

Topic: Repeated Games and Sequential Games

- 4) Consider the cartel of Trick and Gear. The game is repeated indefinitely and each firm employs a tit-for-tat strategy. The equilibrium is
- A) both firms cheat on the agreement.
  - B) both firms comply with the agreement.
  - C) Trick cheats and Gear complies with the agreement.
  - D) Gear cheats and Trick complies with the agreement.
  - E) unknown.

Answer: B

Diff: 3 Type: MC

Topic: Repeated Games and Sequential Games

Source: Study Guide

- 5) Consider the cartel of Trick and Gear. The game is repeated indefinitely and each firm employs a tit-for-tat strategy. The equilibrium is called
- A) a credible strategy equilibrium.
  - B) a dominant player equilibrium.
  - C) a duopoly equilibrium.
  - D) a trigger strategy equilibrium.
  - E) a cooperative equilibrium.

Answer: E

Diff: 3 Type: MC

Topic: Repeated Games and Sequential Games

Source: Study Guide

- 6) Which of the following quotes shows limit pricing in the widget industry?
- A) "I am producing extra widgets, even though it costs me short-run profit, to stop Wally's Widgets from expanding into my market."
  - B) "I am producing more widgets than Wally and I agreed to in our talk last week."
  - C) "If only Wally and I could agree on a higher price, we could make more profit."
  - D) "I have been spending extra on research and development of my new two-way widget."
  - E) none of the above

Answer: A

Diff: 2 Type: MC

Topic: Repeated Games and Sequential Games

- 7) Which of the following quotes shows a contestable market in the widget industry?
- A) "I am producing extra widgets, even though it costs me short-run profits, to stop Wally's Widgets from expanding into my market."
  - B) "I am producing more widgets than Wally and I agreed to in our talk last week."
  - C) "If only Wally and I could agree on a higher price, we could make more profits."
  - D) "I have been spending extra on research and development of my new two-way widget."
  - E) none of the above

Answer: A

Diff: 2 Type: MC

Topic: Repeated Games and Sequential Games

- 8) Which of the following quotes shows cheating on a cartel in the widget industry?
- A) "I am producing extra widgets, even though it costs me short-run profit, to stop Wally's Widgets from expanding into my market."
  - B) "I am producing more widgets than Wally and I agreed to in our talk last week."
  - C) "If only Wally and I could agree on a higher price, we could make more profit."
  - D) "I have been spending extra on research and development of my new two-way widget."
  - E) none of the above

Answer: B

Diff: 1 Type: MC

Topic: Repeated Games and Sequential Games

- 9) Limit pricing refers to
- A) the highest price a monopolist can set.
  - B) the highest price that just inflicts a loss on a potential entrant.
  - C) a strategy used by entering firms in contestable markets.
  - D) the lowest price a duopoly can set.
  - E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: Repeated Games and Sequential Games

Source: Study Guide

- 10) A contestable market exists whenever
- A) two or more firms are competing.
  - B) the Herfindahl-Hirschman Index exceeds 1,800.
  - C) the four-firm concentration ratio exceeds 50 percent.
  - D) a monopoly contests entry into its markets.
  - E) potential entry holds down prices.

Answer: E

Diff: 2 Type: MC

Topic: Repeated Games and Sequential Games

11) When a firm cooperates if the other cooperates, but plays the Nash equilibrium strategy forever if the other cheats, the strategy is a

- A) dominant strategy.
- B) trigger strategy.
- C) tit-for-tat strategy.
- D) wimp's strategy.
- E) cooperative strategy.

Answer: B

Diff: 2 Type: MC

Topic: Repeated Games and Sequential Games

Source: Study Guide

12) A tit-for-tat strategy can be used

- A) in a single-play game or a repeated game.
- B) in a single-play game but not a repeated game.
- C) in a repeated game but not a single-play game.
- D) in neither a repeated game nor a single-play game.
- E) only when there is no Nash equilibrium.

Answer: C

Type: MC

Topic: Repeated Games and Sequential Games

Skill: Analytical

AACSB: Reflective Thinking

13) A trigger strategy can be used

- A) in a single-play game or a repeated game.
- B) in a single-play game but not a repeated game.
- C) in a repeated game but not a single-play game.
- D) in neither a single-play game nor a repeated game.
- E) only when there is no Nash equilibrium.

Answer: C

Type: MC

Topic: Repeated Games and Sequential Games

Skill: Recognition

AACSB: Reflective Thinking

14) A strategy in which a player cooperates in the current period if the other player cooperated in the previous period, but the player cheats in the current period if the other player cheated in the previous period is called a

- A) tit-for-tat strategy.
- B) trigger strategy.
- C) duopoly strategy.
- D) dominant firm strategy.
- E) Nash strategy.

Answer: A

Type: MC

Topic: Repeated Games and Sequential Games

Skill: Recognition

AACSB: Reflective Thinking

15) A trigger strategy is one in which a player

- A) cooperates in the current period if the other player cooperated in the previous period, but cheats in the current period *only* if the other player cheated in the previous period.
- B) cheats in the current period if the other player cooperated in the previous period, but cooperates in the current period if the other player cheated in the previous period.
- C) cooperates in the current period if the other player has always cooperated, but cheats forever if the other player ever cheats.
- D) cheats in the current period if the other player has always cheated, but cooperates forever if the other player has ever cooperated.
- E) None of the above.

Answer: C

Type: MC

Topic: Repeated Games and Sequential Games

Skill: Recognition

AACSB: Reflective Thinking

16) Sarah's Soothing Diapers, Inc. and Orville's Odorless Diapers, Inc. are duopolists, who have agreed to collude. Orville has decided that he will comply with the collusive agreement as long as Sarah cooperated in the previous period. But if Sarah cheated in the previous period, Orville will punish Sarah by cheating in the current period. Orville's strategy is referred to as a

- A) Nash strategy.
- B) tit-for-tat strategy.
- C) trigger strategy.
- D) monkey-see, monkey-do strategy.
- E) dominant firm strategy.

Answer: B

Type: MC

Topic: Repeated Games and Sequential Games

Skill: Recognition

AACSB: Reflective Thinking

17) A market with a single firm but no barriers to entry is known as

- A) a natural monopoly.
- B) a contestable market.
- C) a perfectly competitive market.
- D) monopolistic competition.
- E) an oligopoly

Answer: B

Type: MC

Topic: Repeated Games and Sequential Games

Skill: Recognition

AACSB: Reflective Thinking

18) A market in which firms can enter and leave so easily that firms in the market face competition from potential entrants is called a

- A) contestable market.
- B) cartel.
- C) limit pricing market.
- D) monopolistic competition market.
- E) natural oligopoly

Answer: A

Type: MC

Topic: Repeated Games and Sequential Games

Skill: Recognition

AACSB: Reflective Thinking

19) Which of the following statements is *TRUE* about contestable markets?

- A) There are significant barriers to entry.
- B) Firms earn large economic profits.
- C) Each firm faces a perfectly elastic demand.
- D) There are few firms in the industry.
- E) None of the above.

Answer: D

Type: MC

Topic: Repeated Games and Sequential Games

Skill: Recognition

AACSB: Reflective Thinking

- 20) A contestable market is similar to a perfectly competitive market in that there
- A) are barriers to entry.
  - B) are no barriers to entry.
  - C) can be only one firm in the market.
  - D) will be no entry if the existing firm makes an economic profit.
  - E) is a perfectly elastic demand.

Answer: B

Type: MC

Topic: Repeated Games and Sequential Games

Skill: Recognition

AACSB: Reflective Thinking

- 21) In a contestable market the Herfindahl-Hirschman Index is \_\_\_\_\_ and the market behaves as if it is \_\_\_\_\_.

- A) low; perfectly competitive
- B) low; a monopoly
- C) high; perfectly competitive
- D) high; a monopoly
- E) zero; perfectly competitive

Answer: C

Type: MC

Topic: Repeated Games and Sequential Games

Skill: Conceptual

AACSB: Reflective Thinking

- 22) In a repeated game, punishments that result in heavy damages are an incentive for players to adopt the strategies that result in a \_\_\_\_\_ equilibrium.

- A) contestable
- B) strategic
- C) complementary
- D) cooperative
- E) satisfying

Answer: D

Type: MC

## 15.4 Anti-Combine Law

- 1) Anti-combine law attempts to
- A) support prices.
  - B) establish Crown corporations.
  - C) prevent monopoly behaviour.
  - D) establish fair trade laws.
  - E) deregulate monopolies.

Answer: C

Diff: 1 Type: MC

Topic: Anti-Combine Law

Source: Study Guide

- 2) Canada's anti-combine law dates back to the
- A) 1880s.
  - B) 1910s.
  - C) 1930s.
  - D) 1960s.
  - E) 1980s.

Answer: A

Diff: 2 Type: MC

Topic: Anti-Combine Law

Source: Study Guide

- 3) Canada's anti-combine law is enforced by
- A) a Competition Tribunal.
  - B) the courts.
  - C) Parliament.
  - D) A and B.
  - E) A and C.

Answer: D

Diff: 2 Type: MC

Topic: Anti-Combine Law

- 4) The Competition Act distinguishes between business practices that are criminal and noncriminal. Which of the following are criminal practices?

- A) conspiracy to fix prices
- B) bid-rigging
- C) resale price maintenance
- D) false advertising
- E) all of the above

Answer: E

Diff: 2 Type: MC

Topic: Anti-Combine Law

Source: Study Guide

5) Choose the statement below that is *incorrect*.

- A) The Competition Act distinguishes between practices that are criminal and practices that are noncriminal.
- B) The Director of the Competition Bureau sends alleged violations of a noncriminal nature to Parliament for examination.
- C) The Competition Act of 1986 established a Competition Bureau.
- D) The Competition Act of 1986 established a Competition Tribunal.
- E) Canada's anti-combine law dates from 1889.

Answer: B

Diff: 2 Type: MC

Topic: Anti-Combine Law

Source: MyEconLab

6) Anti-combine law \_\_\_\_\_.

- A) can work in the public interest to maximize total surplus or in the self-interest of producers to maximize producer surpluses
- B) always works in the self-interest of producers to maximize producer surpluses
- C) always works in the public interest to maximize total surplus
- D) encourages oligopolies to exhibit more monopolistic behaviours
- E) is always prosecuted in Canada's criminal courts

Answer: A

Diff: 2 Type: MC

Topic: Anti-Combine Law

Source: MyEconLab

7) All of the following except \_\_\_\_\_ are noncriminal offences under the Competition Act.

- A) refusal to deal
- B) mergers
- C) false advertising
- D) abuse of a dominant market position
- E) exclusive dealing

Answer: C

Diff: 2 Type: MC

Topic: Anti-Combine Law

Source: MyEconLab

8) A merger is unlikely to be approved if \_\_\_\_\_.

- A) there are fewer than 6 firms in a market
- B) it prevents or substantially lessens competition
- C) the good produced in the market has been deemed a necessity
- D) the industry is government regulated
- E) All of the above.

Answer: B

Diff: 2 Type: MC

Topic: Anti-Combine Law

Source: MyEconLab

9) The act of parliament that provides our anti-combine law is \_\_\_\_\_.

- A) the Anti-Combine Act of 1986
- B) the Anti-Combine Act of 1889
- C) the Competition Act of 1986
- D) the Competition Act of 1889
- E) the Competition Act of 1967

Answer: C

Diff: 2 Type: MC

Topic: Anti-Combine Law

Source: MyEconLab

## Chapter 16 Externalities

### 16.1 Externalities in Our Lives

1) An externality is defined as

- A) an additional cost imposed by the government on producers.
- B) an additional gain received by consumers from decisions made by the government.
- C) a cost or benefit that arises from production and falls on someone other than the producer, or a cost or benefit that arises from consumption and falls on someone other than the consumer.
- D) a marginal social cost.
- E) the additional amount consumers have to pay to consume an additional amount of a good or service.

Answer: C

Diff: 1 Type: MC

Topic: Externalities in Our Lives

2) An externality is a cost or benefit arising from an economic activity that falls on

- A) consumers but not producers.
- B) producers but not consumers.
- C) consumers or producers.
- D) someone other than consumers or producers.
- E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: Externalities in Our Lives

Source: Study Guide

3) Which of the following illustrates the concept of external cost?

- A) Bad weather reduces the size of the wheat crop.
- B) A reduction in the size of the wheat crop causes income of wheat farmers to fall.
- C) Smoking harms the health of the smoker.
- D) Smoking harms the health of nearby nonsmokers.
- E) Public health services reduce the transmission of disease.

Answer: D

Diff: 2 Type: MC

Topic: Externalities in Our Lives

Source: Study Guide

4) Air pollution generated by a paper mill factory is an example of a

- A) positive production externality.
- B) positive consumption externality.
- C) negative consumption externality.
- D) marginal external benefit.
- E) negative production externality.

Answer: E

Diff: 1 Type: MC

Topic: Externalities in Our Lives

5) Sixty percent of our air pollution comes from

- A) solid waste disposal.
- B) electric utilities.
- C) a growing world population.
- D) road transportation and industrial processes.
- E) none of the above.

Answer: D

Diff: 1 Type: MC

Topic: Externalities in Our Lives

6) A well-maintained water-front property that is enjoyed by other property owners is an example of

- A) an inefficient allocation of resources.
- B) a negative consumption externality.
- C) a positive consumption externality.
- D) a negative production externality.
- E) a positive production externality.

Answer: C

Diff: 2 Type: MC

Topic: Externalities in Our Lives

7) An example of an activity that creates a negative consumption externality is

- A) logging, which pollutes rivers.
- B) locating beehives next to an orange orchard.
- C) smoking, which harms the health of a bystander.
- D) a flu vaccination.
- E) none of the above.

Answer: C

Type: MC

Topic: Externalities in Our Lives

Skill: Conceptual

AACSB: Reflective Thinking

8) Smoking tobacco creates a \_\_\_\_\_ externality.

- A) negative consumption
- B) negative production
- C) positive consumption
- D) positive production
- E) none of the above

Answer: A

Diff: 1 Type: MC

Topic: Externalities in Our Lives

Skill: Conceptual

AACSB: Reflective Thinking

9) An example of an activity that creates a positive consumption externality is

- A) logging, which pollutes rivers.
- B) locating beehives next to an orange orchard.
- C) smoking, which harms the health of a bystander.
- D) a flu vaccination.
- E) a noisy party.

Answer: D

Type: MC

Topic: Externalities in Our Lives

Skill: Conceptual

AACSB: Reflective Thinking

10) A homeowner planting an attractive garden in front of his house creates \_\_\_\_\_.

A bakery baking bread creates \_\_\_\_\_.

- A) no externality; a positive production externality
- B) a positive consumption externality; no externality
- C) no externality; no externality
- D) a positive consumption externality; a positive production externality
- E) a positive production externality; no externality

Answer: D

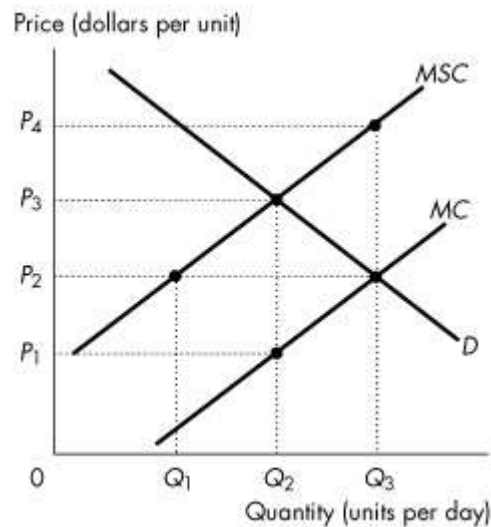
Type: MC

Topic: Externalities in Our Lives

Source: MyEconLab

## 16.2 Negative Externality: Pollution

Use the figure below to answer the following questions.



**Figure 16.2.1**

1) Refer to Figure 16.2.1. The figure shows the private marginal cost curve, the social marginal cost curve and the market demand curve. If the market is unregulated, then the quantity produced is

- A) zero.
- B)  $Q_1$ .
- C)  $Q_2$ .
- D)  $Q_3$ .
- E) too low.

Answer: D

Diff: 1 Type: MC

Topic: Negative Externality: Pollution

2) Refer to Figure 16.2.1. The figure shows the private marginal cost curve, the social marginal cost curve and the market demand curve. If the market is unregulated, then the price is

- A)  $P_1$ .
- B)  $P_4$ .
- C) below  $P_1$ .
- D)  $P_2$ .
- E)  $P_3$ .

Answer: D

Diff: 1 Type: MC

Topic: Negative Externality: Pollution

3) Refer to Figure 16.2.1. The figure shows the private marginal cost curve, the social marginal cost curve and the market demand curve. If the market is unregulated, then at the equilibrium output the marginal social cost of production is

- A) less than the marginal benefit to consumers.
- B) greater than the marginal benefit to consumers.
- C) equal to the marginal benefit to consumers.
- D) equal to the marginal private cost of production.
- E) less than the marginal private cost of production.

Answer: B

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

4) Refer to Figure 16.2.1. The figure shows the private marginal cost curve, the social marginal cost curve and the market demand curve. If the market is unregulated, then

- A) the quantity produced is efficient but price is too low.
- B) the quantity produced is less than the efficient quantity.
- C) the quantity produced is greater than the efficient quantity.
- D) the quantity produced is efficient but the price is too high.
- E) the externality is eliminated.

Answer: C

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

5) Refer to Figure 16.2.1. The figure shows the private marginal cost curve, the social marginal cost curve and the market demand curve. To promote an efficient allocation of resources, the government could impose a constant per unit tax equal to

- A) zero.
- B)  $P_1$ .
- C)  $P_3 - P_1$ .
- D)  $P_4 - P_1$ .
- E)  $P_3 - P_2$ .

Answer: C

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

6) Refer to Figure 16.2.1. The figure shows the private marginal cost curve, the social marginal cost curve and the market demand curve. If a constant per unit tax is imposed that generates an efficient allocation of resources, then the quantity produced is

- A) zero.
- B)  $Q_1$ .
- C)  $Q_2$ .
- D)  $Q_3$ .
- E) greater than  $Q_3$ .

Answer: C

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

7) Refer to Figure 16.2.1. The figure shows the private marginal cost curve, the social marginal cost curve and the market demand curve. If a constant per unit tax is imposed that generates an efficient allocation of resources, then consumers pay a per unit price of

- A) zero.
- B)  $P_1$ .
- C)  $P_2$ .
- D)  $P_3$ .
- E)  $P_4$ .

Answer: D

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

8) Refer to Figure 16.2.1. The figure shows the private marginal cost curve, the social marginal cost curve and the market demand curve. If a constant per unit tax is imposed that generates an efficient allocation of resources, then producers receive a per unit price of

- A) zero.
- B)  $P_4$ .
- C)  $P_3$ .
- D)  $P_2$ .
- E)  $P_1$ .

Answer: E

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

9) Effective strategies for addressing the problem of negative externalities include

- A) taxing the profit of polluting companies at twice the rate of non-polluting companies.
- B) imposing taxes on the activity that generates the pollution.
- C) stressing the use of renewable resources.
- D) imposing recycling laws.
- E) closing down a polluting industry.

Answer: B

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

Use the table below to answer the following questions.

**Table 16.2.1**

Output (units)	Marginal Social Benefit (dollars)	Marginal Private Cost (dollars)	Marginal Social Cost (dollars)
0	80	0	20
1	70	10	30
2	60	20	40
3	50	30	50
4	40	40	60
5	30	50	70
6	20	60	80

10) Refer to Table 16.2.1. Given in the table are the marginal private cost and the marginal social cost of the production of chemical fertilizer and the marginal social benefit from the consumption of fertilizer. Under these circumstances,

- A) there are positive externalities in this market.
- B) there are negative externalities in this market, equal to \$10 per unit.
- C) there are no externalities in this market.
- D) not enough information is provided to determine whether or not there are externalities.
- E) there are negative externalities in this market, equal to \$20 per unit.

Answer: E

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

11) Refer to Table 16.2.1. Given in the table are the marginal private cost and the marginal social cost of the production of chemical fertilizer and the marginal social benefit from the consumption of fertilizer. If the market is unregulated, the quantity produced is

- A) 1 unit.
- B) 2 units.
- C) 3 units.
- D) 4 units.
- E) 5 units.

Answer: D

Diff: 1 Type: MC

Topic: Negative Externality: Pollution

12) Refer to Table 16.2.1. Given in the table are the marginal private cost and the marginal social cost of the production of chemical fertilizer and the marginal social benefit from the consumption of fertilizer. If the market is unregulated, the market price is

- A) \$10 a unit.
- B) \$20 a unit.
- C) \$30 a unit.
- D) \$40 a unit.
- E) \$50 a unit.

Answer: D

Diff: 1 Type: MC

Topic: Negative Externality: Pollution

13) Refer to Table 16.2.1. Given in the table are the marginal private cost and the marginal social cost of the production of chemical fertilizer and the marginal social benefit from the consumption of fertilizer. Assume the market is perfectly competitive. If the market is unregulated, the marginal

- A) social cost equals the marginal private benefit.
- B) private cost is less than the marginal social benefit.
- C) private cost equals the marginal social benefit.
- D) social cost equals the marginal private cost.
- E) private cost is greater than the marginal social benefit.

Answer: C

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

14) Refer to Table 16.2.1. Given in the table are the marginal private cost and the marginal social cost of the production of chemical fertilizer and the marginal social benefit from the consumption of fertilizer. If the market is unregulated

- A) the quantity produced is the efficient quantity.
- B) the quantity produced is greater than the efficient quantity.
- C) the quantity produced is less than the efficient quantity.
- D) marginal external cost is maximized.
- E) production is technologically inefficient.

Answer: B

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

15) Refer to Table 16.2.1. Given in the table are the marginal private cost and the marginal social cost of the production of chemical fertilizer and the marginal social benefit from the consumption of fertilizer. If the government decides to correct the externality problem, it could

- A) subsidize production by \$20 per unit.
- B) subsidize production by \$10 per unit.
- C) provide the good itself.
- D) tax production by \$10 per unit.
- E) tax production by \$20 per unit.

Answer: E

Diff: 3 Type: MC

Topic: Negative Externality: Pollution

Use the figure below to answer the following questions.

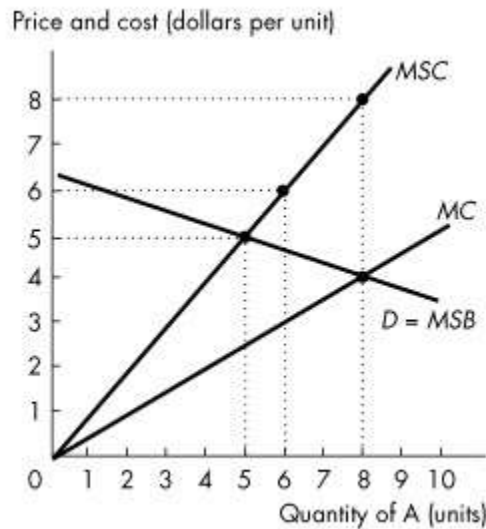


Figure 16.2.2

16) Refer to Figure 16.2.2. This figure shows the demand curve, the marginal private cost curve and the marginal social cost curve of good A. Production of the 6th unit of output generates a marginal *external*

- A) cost of \$1.50.
- B) cost of \$3.
- C) cost of \$6.
- D) benefit of \$3.
- E) benefit of \$6.

Answer: B

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

Source: Study Guide

17) Refer to Figure 16.2.2. This figure shows the demand curve, the marginal private cost curve and the marginal social cost curve of good A. How many units of good A are produced in an unregulated market?

- A) 0 units
- B) 5 units
- C) 6 units
- D) 8 units
- E) 9 units

Answer: D

Diff: 1 Type: MC

Topic: Negative Externality: Pollution

Source: Study Guide

18) Refer to Figure 16.2.2. This figure shows the demand curve, the marginal private cost curve and the marginal social cost curve of good A. What is the efficient quantity of good A?

- A) 0 units
- B) 5 units
- C) 6 units
- D) 8 units
- E) impossible to determine without additional information

Answer: B

Diff: 1 Type: MC

Topic: Negative Externality: Pollution

Source: Study Guide

19) Refer to Figure 16.2.2. This figure shows the demand curve, the marginal private cost curve and the marginal social cost curve of good A. If the government wanted to achieve the efficient quantity of good A, it could issue marketable permits. If the marketable permits result in the efficient quantity of good A, then the quantity of good A produced is

- A) 0 units.
- B) 5 units.
- C) 6 units.
- D) 8 units.
- E) a level impossible to determine without more information.

Answer: B

Diff: 3 Type: MC

Topic: Negative Externality: Pollution

20) In the absence of government intervention, a profit-maximizing firm producing a good with an external cost will produce a quantity at which

- A) price is greater than marginal private cost.
- B) price is less than marginal revenue.
- C) price is less than marginal private cost.
- D) price equals marginal private cost.
- E) marginal revenue equals marginal social cost.

Answer: D

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

21) When an additional unit of output is produced, the extra cost to society is the

- A) average total cost.
- B) marginal social cost.
- C) marginal private cost.
- D) marginal external cost.
- E) marginal damage.

Answer: B

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

22) Means of coping with negative externalities include all of the following *except*

- A) emission charges.
- B) patents.
- C) property rights.
- D) Pigovian taxes.
- E) marketable permits.

Answer: B

Diff: 1 Type: MC

Topic: Negative Externality: Pollution

23) Which one of the following is a means of coping with a negative externality?

- A) emission subsidies
- B) patents
- C) vouchers
- D) Pigovian taxes
- E) copyrights

Answer: D

Diff: 1 Type: MC

Topic: Negative Externality: Pollution

24) A battery acid producer pollutes the water upstream from the Polar Bear Club, a swimming club. If transactions costs are low, the quantity of pollution will be efficient

- A) only if Ronald Coase is a member of the Polar Bear Club.
- B) only if Ronald Coase is not a member of the Polar Bear Club.
- C) only if water property rights are assigned to the producer.
- D) only if water property rights are assigned to the Polar Bear Club.
- E) if water property rights are assigned either to the producer or to the Polar Bear Club.

Answer: E

Diff: 3 Type: MC

Topic: Negative Externality: Pollution

Source: Study Guide

25) The Coase theorem states that

- A) patents and copyrights will solve the problem of external costs.
- B) taxes will solve the problem of external costs.
- C) global warming is hard to solve due to the prisoners' dilemma aspect of the problem.
- D) property rights are social arrangements governing ownership, use and disposal of factors of production and goods and services.
- E) if property rights are established, and if only a small number of parties are involved, and if transactions costs are low, then private transactions are efficient.

Answer: E

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

Use the table below to answer the following questions.

**Table 16.2.2**  
Chemical Fertilizer Market

Output (tonnes)	Marginal Social Benefit (dollars)	Marginal Private Cost (dollars)	Marginal Social Cost (dollars)
1	140	50	80
2	120	60	90
3	100	70	100
4	80	80	110
5	60	90	120

26) Refer to Table 16.2.2. If the fertilizer market is perfectly competitive and unregulated, output (in tonnes) is

- A) 1.
- B) 2.
- C) 3.
- D) 4.
- E) 5.

Answer: D

Diff: 1 Type: MC

Topic: Negative Externality: Pollution

Source: Study Guide

27) Refer to Table 16.2.2. Fertilizer has a marginal

- A) external cost of \$100 a tonne.
- B) social cost of \$100 a tonne.
- C) external cost of \$30 a tonne.
- D) private cost of \$30 a tonne.
- E) external cost of \$0.

Answer: C

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

28) Refer to Table 16.2.2. The efficient output of fertilizer is

- A) 1 tonne.
- B) 2 tonnes.
- C) 3 tonnes.
- D) 4 tonnes.
- E) 5 tonnes.

Answer: C

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

Source: Study Guide

- 29) Refer to Table 16.2.2. The Pigovian tax that achieves the efficient quantity of output is
- A) \$0.
  - B) \$10 a tonne.
  - C) \$20 a tonne.
  - D) \$30 a tonne.
  - E) \$40 a tonne.

Answer: D

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

Use the figure below to answer the following questions.

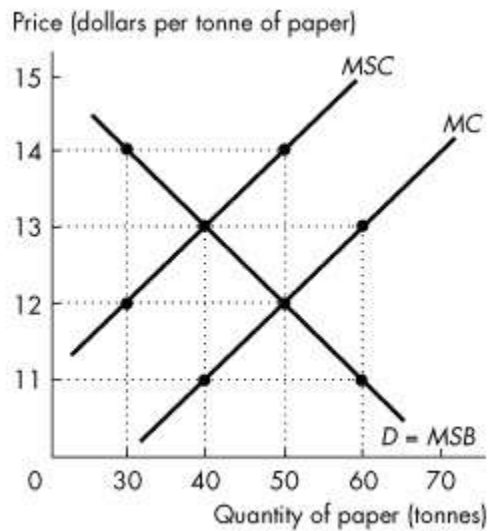


Figure 16.2.3

- 30) Refer to Figure 16.2.3. The unregulated outcome in the paper market is
- A) a quantity of 40 tonnes and a price of \$11 a tonne.
  - B) a quantity of 40 tonnes and a price of \$13 a tonne.
  - C) a quantity of 50 tonnes and a price of \$12 a tonne.
  - D) a quantity of 50 tonnes and a price of \$14 a tonne.
  - E) a quantity of 60 tonnes and a price of \$13 a tonne.

Answer: C

Diff: 1 Type: MC

Topic: Negative Externality: Pollution

31) Refer to Figure 16.2.3. In this market there is a marginal external

- A) cost of \$14 a tonne.
- B) cost of \$12 a tonne.
- C) cost of \$2 a tonne.
- D) benefit of \$2 a tonne.
- E) benefit of \$12 a tonne.

Answer: C

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

32) Refer to Figure 16.2.3. A tax of \_\_\_\_\_ per tonne is necessary to achieve the efficient output of \_\_\_\_\_ tonnes of paper.

- A) \$14; 50
- B) \$14; 30
- C) \$13; 40
- D) \$2; 50
- E) \$2; 40

Answer: E

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

33) If negative externalities exist, then in a market with no property rights,

- A)  $MSC = MSB$ .
- B)  $MSC < MSB$ .
- C)  $MSC > MSB$ .
- D)  $MSC =$  marginal external cost.
- E) none of the above.

Answer: C

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

34) CoolU has solved its smoking problem by allocating each student 5 smoking permits a day, and allowing trading. This is an example of

- A) marketable permits.
- B) emission charges.
- C) the Coase theorem.
- D) a pollution tax.
- E) a voucher.

Answer: A

Diff: 1 Type: MC

Topic: Negative Externality: Pollution

35) Consider the problem of carbon dioxide pollution due to the use of coal in electric power production. The discovery of very cheap solar power would lead to

- A) less carbon dioxide pollution.
- B) more carbon dioxide pollution.
- C) no change in the amount of carbon dioxide pollution.
- D) either more or less carbon dioxide pollution, depending on the amount of solar power pollution.
- E) either no change or more carbon dioxide pollution.

Answer: A

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

36) A system of marketable permits is used to reduce acid rain caused by emissions from electric power utilities. Which of the following statements is true?

- A) Market forces determine both the demand for marketable permits and their supply.
- B) Public choice determines both the demand for marketable permits and their supply.
- C) Market forces determine the demand for marketable permits, and property rights determine their supply.
- D) Property rights determine the demand for marketable permits, and the government determines their supply.
- E) Market forces determine the demand for marketable permits, and the government determines their supply.

Answer: E

Diff: 3 Type: MC

Topic: Negative Externality: Pollution

37) The Coase theorem tells us that in the presence of external costs in production,

- A) the government must intervene in the market to assure that the efficient level of output is produced.
- B) private parties can negotiate to produce the good at a level where marginal willingness to pay for the good by consumers is zero.
- C) private parties can never arrive at the efficient solution.
- D) then under certain conditions, private parties can arrive at the efficient solution without government involvement.
- E) and if transactions costs are high, then only the private sector will be able to produce the efficient amount of the good.

Answer: D

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

- 38) According to the Coase theorem, if transactions costs are low and property rights exist,
- A) negative externalities cause deadweight losses.
  - B) positive externalities cause deadweight losses.
  - C) private transactions are efficient.
  - D) public transactions are efficient.
  - E) the efficient level of pollution will be zero.

Answer: C

Diff: 3 Type: MC

Topic: Negative Externality: Pollution

- 39) The Coase theorem will apply only if
- A) an individual who is not affected by the externality can negotiate a settlement between the parties imposing the externality and the parties that are harmed by the externality.
  - B) the small number of people are involved.
  - C) the market is perfectly competitive.
  - D) the courts can be used to determine the amount of compensation that must be made to the damaged party.
  - E) the amount of compensation that must be made to the damaged party is small.

Answer: B

Diff: 3 Type: MC

Topic: Negative Externality: Pollution

- 40) The Coase theorem applies when transactions costs are
- A) low and property rights exist.
  - B) low and property rights do not exist.
  - C) high and property rights exist.
  - D) high and property rights do not exist.
  - E) low and there are no externalities.

Answer: A

Diff: 3 Type: MC

Topic: Negative Externality: Pollution

- 41) An externality is
- A) the amount by which price exceeds marginal private cost.
  - B) the amount by which price exceeds marginal social cost.
  - C) the effect of government regulation on market price and output.
  - D) someone who consumes a good without paying for it.
  - E) a cost or benefit that arises from an activity but affects people not part of the original activity.

Answer: E

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

Source: Study Guide

42) The marginal private cost curve ( $MC$ ) is a positively-sloped straight line starting at the origin. If marginal external cost increases as output increases, then the marginal social cost curve is a positively-sloped straight line

- A) parallel to and above the  $MC$  curve.
- B) parallel to and below the  $MC$  curve.
- C) starting at the origin, above the  $MC$  curve, and with a slope greater than the  $MC$  curve.
- D) starting at the origin, below the  $MC$  curve, and with a slope less than the  $MC$  curve.
- E) none of the above.

Answer: C

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

Source: Study Guide

43) One way to solve negative externality problems is

- A) to organize a limited boycott of the products.
- B) subsidize the externalities.
- C) eliminate transactions costs when property rights are not legally established.
- D) issue marketable permits to polluting firms.
- E) establish and enforce patents and copyrights.

Answer: D

Diff: 2 Type: MC

Topic: Negative Externality: Pollution

44) Pollution occurs when lumber is produced. If the lumber market is unregulated, there would be

- A) overproduction of lumber compared to the efficient amount.
- B) underproduction of lumber compared to the efficient amount.
- C) sometimes overproduction and sometimes underproduction of lumber compared to the efficient amount.
- D) an external benefit from producing lumber.
- E) no deadweight loss from production.

Answer: A

Type: MC

Topic: Negative Externality: Pollution

Skill: Conceptual

AACSB: Reflective Thinking

- 45) When the marginal social cost of the production of Good A is greater than the marginal private cost of the production of Good A, then
- A) a competitive, unregulated market produces less than the efficient quantity of Good A.
  - B) a competitive, unregulated market produces the efficient quantity of Good A.
  - C) a competitive, unregulated market produces more than the efficient quantity of Good A.
  - D) the government should levy a tax on the production of Good A that is equal to the horizontal distance between the two marginal cost curves.
  - E) a competitive, unregulated market does not create a deadweight loss.

Answer: C

Type: MC

Topic: Negative Externality: Pollution

Skill: Recognition

AACSB: Reflective Thinking

- 46) When the production of a good has an external cost, the
- A) marginal social cost curve lies below the marginal private cost curve.
  - B) marginal social benefit curve lies above the marginal private benefit curve.
  - C) equilibrium quantity in an unregulated, competitive market has a marginal social cost greater than the marginal social benefit.
  - D) equilibrium quantity in an unregulated, competitive market has a marginal social cost less than the marginal social benefit.
  - E) none of the above.

Answer: C

Type: MC

Topic: Negative Externality: Pollution

Skill: Recognition

AACSB: Reflective Thinking

- 47) Consider some type of industrial pollution that generates air pollution. This industry, if left unregulated, will produce
- A) too much output because they will ignore the marginal external costs.
  - B) the efficient level of output.
  - C) too little output because they will ignore the marginal external costs.
  - D) too little output because they will ignore the marginal external benefits.
  - E) too much output because they will ignore the marginal external benefits.

Answer: A

Type: MC

Topic: Negative Externality: Pollution

Skill: Conceptual

AACSB: Reflective Thinking

Use the table below to answer the following question.

**Table 16.2.3**

<b>Price</b> (cents per kilowatt)	<b>Quantity</b> (kilowatts per day)	<b>Marginal cost</b> (cents per kilowatt)
4	500	10
8	400	8
12	300	6
16	200	4
20	100	2

48) Refer to Table 16.2.3. The first two columns of the table show the demand schedule for electricity from a coal burning utility; the second and third columns show the utility's cost of producing electricity.

The marginal external cost of the pollution created is equal to the marginal cost.

Suppose the government levies a pollution tax such that the utility generates the efficient quantity of electricity. The pollution tax is \_\_\_\_\_ cents a kilowatt hour.

- A) 2
- B) 4
- C) 6
- D) 8
- E) 10

Answer: C

Type: MC

Topic: Negative Externality: Pollution

Source: MyEconLab

49) Betty and Anna work at the same office in Calgary. They both must attend a meeting in Edmonton, and they have decided to drive to the meeting together.

Betty is a cigarette smoker and her marginal benefit from smoking one package of cigarettes a day is \$40. Cigarettes are \$6 a pack.

Anna dislikes cigarette smoke and her marginal benefit from a smoke-free environment is \$50 a day.

If Betty drives her car with Anna as a passenger, \_\_\_\_\_. If Anna drives her car with Betty as a passenger, \_\_\_\_\_.

A) Anna will offer Betty an amount between \$34 and \$50 and Betty will not smoke; Betty does not smoke because Betty will not offer Anna a high enough price to be allowed to smoke

B) Betty will smoke because she owns the property rights in the car; Betty does not smoke because Betty will not offer Anna a high enough price to be allowed to smoke

C) Betty will smoke because she owns the property rights in the car; Betty will offer Anna \$51 and Betty will smoke

D) Anna will offer Betty an amount between \$34 and \$50 and Betty will not smoke; Betty will offer Anna \$51 and Betty will smoke

E) Betty will smoke because she is the car owner; Betty will offer Anna an amount between \$34 and \$50 and Betty will smoke

Answer: A

Type: MC

Topic: Negative Externality: Pollution

Source: MyEconLab

50) When the government issues marketable permits

A) each firm buys or sells permits until its marginal benefit from polluting equals the market price of a permit.

B) firms that have a low marginal cost of reducing pollution sell their permits, and firms that have a high marginal cost of reducing pollution buy permits.

C) the incentive to pollute is greater than when the government sets emission charges.

D) the price at which firms buy and sell permits is set by the government.

E) firms that have a high marginal cost of reducing pollution sell their permits, and firms that have a low marginal cost of reducing pollution buy permits.

Answer: B

Type: MC

Topic: Negative Externality: Pollution

Source: MyEconLab

51) All of the following statements about emission charges are correct *except*

- A) the more pollution a firm creates, the more it pays in emission charges.
- B) emission charges are frequently used in North America.
- C) the government sets a price per unit of pollution.
- D) to work out the emission charge that achieves efficiency, the government needs a lot of information about the polluting industry that is rarely available.
- E) emission charges are frequently used in Europe.

Answer: B

Type: MC

Topic: Negative Externality: Pollution

Source: MyEconLab

52) A private cost of production is a cost that is borne by the \_\_\_\_\_ of a good or service. A social cost of production is a cost that is \_\_\_\_\_.

- A) consumer; borne by the producer and by everyone else on whom the cost falls
- B) consumer; not borne by the producer but borne by other people
- C) producer; not borne by the producer but borne by other people
- D) producer; borne by the producer and by everyone else on whom the cost falls
- E) producer; borne by the consumer

Answer: D

Type: MC

Topic: Negative Externality: Pollution

Source: MyEconLab

53) Consider the production of pesticide that pollutes a lake used by a trout farmer. A marketable permit

- A) creates an efficient outcome when the price of the permit is set equal to the external cost.
- B) cannot result in the same outcome as when property rights are assigned to the pesticide producer.
- C) cannot result in the same outcome as when property rights are assigned to the trout farm.
- D) cannot result in the same outcome as when the government imposes a Pigovian tax.
- E) creates an efficient outcome when the price of the permits is set equal to the external benefit.

Answer: A

Type: MC

Topic: Negative Externality: Pollution

Source: MyEconLab

54) If the marginal private cost of producing one kilowatt of power in British Columbia equals five cents and the marginal social cost of each kilowatt equals nine cents, then the marginal external cost equals \_\_\_\_\_ per kilowatt.

- A) five cents
- B) nine cents
- C) four cents
- D) fourteen cents
- E) forty-five cents

Answer: C

Type: MC

- 55) If the production of a good creates pollution, then the
- A) marginal social benefit curve lies above the marginal private benefit curve.
  - B) marginal social cost curve lies above the marginal private cost curve.
  - C) marginal social benefit curve lies below the marginal private benefit curve.
  - D) marginal social cost curve lies below the marginal private cost curve.
  - E) marginal social benefit curve intersects the marginal private cost curve at the efficient quantity.

Answer: B

Type: MC

- 56) When Good A is produced, pollution is also produced. When the marginal social cost of production of Good A equals marginal social benefit from Good A, then

- I. there is no pollution
  - II. resources are used efficiently
- A) I only
  - B) II only
  - C) neither I nor II
  - D) both I and II
  - E) sometimes I and sometimes II, but never both simultaneously

Answer: B

Type: MC

- 57) Producing paper creates pollution. There is no externality in the consumption of paper. The efficient quantity of paper produced occurs when the

- A) marginal social benefit from paper is equal to zero.
- B) marginal social cost of the pollution from making paper is equal to zero.
- C) marginal private cost of the pollution from making paper is equal to zero.
- D) marginal private cost of paper equals the marginal private benefit from paper.
- E) marginal social benefit from paper is equal to the marginal social cost of paper.

Answer: E

Type: MC

- 58) A chemical factory and a fishing club share a lake. Producing chemicals creates water pollution that harms the fish. Initially the lake is owned by no one. Keeping in mind the Coase theorem, suppose transactions costs are low and the chemical factory is given ownership of the lake. Compared to the situation with no property rights, the quantity of chemicals produced

- A) decreases.
- B) stays the same.
- C) increases.
- D) changes but the direction of the change is unknown.
- E) decreases only if the marginal external benefit decreases.

Answer: A

Type: MC

### 16.3 Positive Externality: Knowledge

1) The marginal private benefit curve ( $MB$ ) is a negatively-sloped straight line. If marginal external benefit decreases as output increases, the marginal social benefit curve is a negatively-sloped straight line

- A) parallel to and above the  $MB$  curve.
- B) parallel to and below the  $MB$  curve.
- C) above the  $MB$  curve and steeper than the  $MB$  curve.
- D) above the  $MB$  curve and flatter than the  $MB$  curve.
- E) below the  $MB$  curve and flatter than the  $MB$  curve.

Answer: C

Diff: 1 Type: MC

Topic: Positive Externality: Knowledge

Use the figure below to answer the following questions.

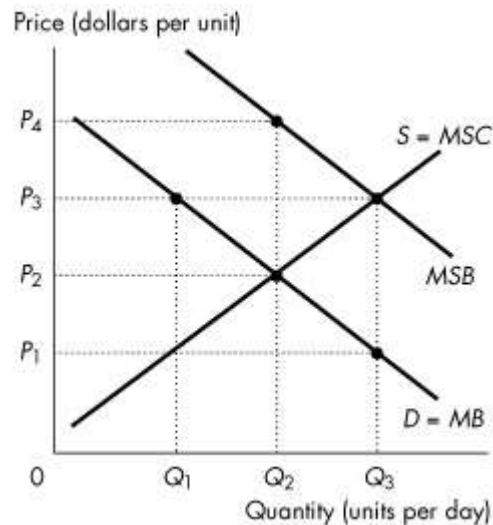


Figure 16.3.1

2) Refer to Figure 16.3.1. The figure shows the marginal private benefit curve, the marginal social benefit curve, and the market supply curve. If production is left to the private market, then the quantity produced is

- A) zero.
- B)  $Q_1$ .
- C)  $Q_2$ .
- D)  $Q_3$ .
- E) between 0 and  $Q_1$ .

Answer: C

Diff: 1 Type: MC

Topic: Positive Externality: Knowledge

3) Refer to Figure 16.3.1. The figure shows the marginal private benefit curve, the marginal social benefit curve, and the market supply curve. If production is left to the private market, then the price is

- A)  $P_1$ .
- B)  $P_3$ .
- C)  $P_2$ .
- D) greater than  $P_4$ .
- E)  $P_4$ .

Answer: C

Diff: 1 Type: MC

Topic: Positive Externality: Knowledge

4) Refer to Figure 16.3.1. The figure shows the marginal private benefit curve, the marginal social benefit curve, and the market supply curve. If production is left to the private market, then at the equilibrium quantity the marginal social benefit from consumption is

- A) less than the marginal cost to producers.
- B) less than the marginal social cost of production.
- C) equal to the marginal cost to producers.
- D) equal to the marginal private benefit from consumption.
- E) greater than the marginal cost to producers.

Answer: E

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

5) Refer to Figure 16.3.1. The figure shows the marginal private benefit curve, the marginal social benefit curve, and the market supply curve. If production is left to the private market, then

- A) the quantity produced is less than the efficient quantity.
- B) the quantity produced is greater than the efficient quantity.
- C) price is greater than marginal social benefit quantity.
- D) the marginal cost curve is horizontal.
- E) none of the above.

Answer: A

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

6) Refer to Figure 16.3.1. The figure shows the marginal private benefit curve, the marginal social benefit curve, and the market supply curve. To promote an efficient quantity the government could grant a subsidy equal to

- A) zero.
- B)  $P_1$ .
- C)  $P_3 - P_1$ .
- D)  $P_4 - P_1$ .
- E)  $P_2 - P_1$ .

Answer: C

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

7) Refer to Figure 16.3.1. The figure shows the marginal private benefit curve, the marginal social benefit curve, and the market supply curve. If a subsidy is granted that generates an efficient quantity, then quantity produced is

- A) zero.
- B)  $Q_1$ .
- C)  $Q_2$ .
- D)  $Q_3$ .
- E) greater than  $Q_3$ .

Answer: D

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

8) Refer to Figure 16.3.1. The figure shows the marginal private benefit curve, the marginal social benefit curve, and the market supply curve. If a voucher is given to consumers that generates an efficient outcome, then consumers pay

- A) zero.
- B)  $P_1$  per unit.
- C)  $P_2$  per unit.
- D)  $P_3$  per unit.
- E)  $P_4$  per unit.

Answer: B

Diff: 3 Type: MC

Topic: Positive Externality: Knowledge

9) Refer to Figure 16.3.1. The figure shows the marginal private benefit curve, the marginal social benefit curve, and the market supply curve. If a voucher is given to consumers that generates an efficient outcome, then producers receive a price of

- A) zero.
- B)  $P_1$  per unit.
- C)  $P_2$  per unit.
- D)  $P_3$  per unit.
- E)  $P_4$  per unit.

Answer: D

Diff: 3 Type: MC

Topic: Positive Externality: Knowledge

Use the table below to answer the following questions.

**Table 16.3.1**

Output (units)	Marginal Private Benefit (dollars)	Marginal Social Cost (dollars)	Marginal Social Benefit (dollars)
0	80	20	100
1	70	30	90
2	60	40	80
3	50	50	70
4	40	60	60
5	30	70	50
6	20	80	40

10) Refer to Table 16.3.1. The table shows marginal private benefit and the marginal social benefit from the consumption of chemical fertilizer and the marginal social cost of the production of fertilizer. Choose the correct statement.

- A) The marginal external benefit is \$20 per unit.
- B) The marginal external cost is \$10 per unit.
- C) There are no externalities associated with this market.
- D) The marginal external benefit is \$10 per unit.
- E) There is not enough information provided to determine whether or not there are externalities.

Answer: A

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

11) Refer to Table 16.3.1. The table shows marginal private benefit and the marginal social benefit from the consumption of chemical fertilizer and the marginal social cost of the production of fertilizer. If production is left to the private market, the quantity produced is

- A) 1 unit.
- B) 2 units.
- C) 3 units.
- D) 4 units.
- E) 5 units.

Answer: C

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

12) Refer to Table 16.3.1. The table shows marginal private benefit and the marginal social benefit from the consumption of chemical fertilizer and the marginal social cost of the production of fertilizer. If production is left to the private market, the market price is

- A) \$70 a unit.
- B) \$60 a unit.
- C) \$50 a unit.
- D) \$40 a unit.
- E) \$30 a unit.

Answer: C

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

13) Refer to Table 16.3.1. The table shows marginal private benefit and the marginal social benefit from the consumption of chemical fertilizer and the marginal social cost of the production of fertilizer. If production is left to the private market, then at the profit-maximizing output level marginal

- A) social cost equals marginal private benefit.
- B) private cost is less than marginal private benefit.
- C) social cost is less than marginal private benefit.
- D) social cost is greater than marginal private benefit.
- E) social benefit is less than marginal private benefit.

Answer: A

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

14) Refer to Table 16.3.1. The table shows marginal private benefit and the marginal social benefit from the consumption of chemical fertilizer and the marginal social cost of the production of fertilizer. If production is left to the private market, then

- A) an efficient quantity is produced.
- B) imposing a tax leads to production of the efficient quantity.
- C) too much fertilizer is produced.
- D) a system of marketable permits leads to production of the efficient quantity.
- E) an inefficient quantity is produced.

Answer: E

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

15) Refer to Table 16.3.1. The table shows marginal private benefit and the marginal social benefit from the consumption of chemical fertilizer and the marginal social cost of the production of fertilizer. An efficient quantity is produced if the government

- A) subsidizes production by \$20 per unit.
- B) subsidizes production by \$10 per unit.
- C) provides vouchers for consumption of \$20 per unit.
- D) taxes production by \$10 per unit.
- E) either A or C.

Answer: E

Diff: 3 Type: MC

Topic: Positive Externality: Knowledge

Use the figure below to answer the following questions.

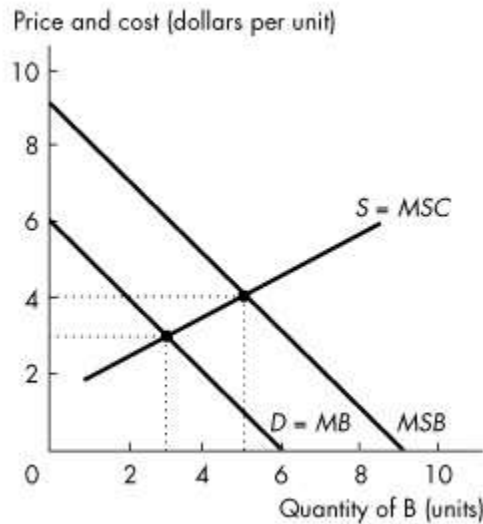


Figure 16.3.2

16) Refer to Figure 16.3.2. The figure shows the market for good *B*. How many units of good *B* are produced and consumed in an unregulated market?

- A) 0 units
- B) 3 units
- C) 5 units
- D) 6 units
- E) 9 units

Answer: B

Diff: 1 Type: MC

Topic: Positive Externality: Knowledge

Source: Study Guide

17) Refer to Figure 16.3.2. The figure shows the market for good *B*. What is the efficient quantity of good *B*?

- A) 0 units
- B) 3 units
- C) 5 units
- D) 6 units
- E) 9 units

Answer: C

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

Source: Study Guide

18) In Figure 16.3.2. The figure shows the market for good *B*. Which of the following government policies creates an efficient outcome?

- A) Tax the production of *B* by \$3 per unit.
- B) Tax the production of *B* by \$4 per unit.
- C) Provide vouchers for consumption of *B* of \$1 per unit.
- D) Provide vouchers for consumption of *B* of \$3 per unit.
- E) Provide vouchers for consumption of *B* of \$4 per unit.

Answer: D

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

Source: Study Guide

19) Refer to Figure 16.3.2. The figure shows the market for good *B*. Under public production, consumers pay \_\_\_\_\_ for each unit of *B*.

- A) zero
- B) \$1
- C) \$2
- D) \$3
- E) \$4

Answer: B

Diff: 3 Type: MC

Topic: Positive Externality: Knowledge

20) The devices the government can use to achieve a more efficient allocation of resources in the presence of external benefits include all of the following *except*

- A) subsidies.
- B) patents.
- C) copyrights.
- D) taxes.
- E) vouchers.

Answer: D

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

21) The devices the government can use to achieve a more efficient allocation of resources in the presence of external benefits include all of the following *except*

- A) intellectual property rights.
- B) subsidies.
- C) public production.
- D) marketable permits.
- E) patents.

Answer: D

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

Source: Study Guide

22) Complete the following sentence. Knowledge

- A) generates external benefits.
- B) generates external costs.
- C) displays diminishing marginal benefit.
- D) is encouraged by intellectual property rights.
- E) A and D are correct.

Answer: E

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

23) Which of the following is least likely to display diminishing marginal benefit?

- A) land
- B) labour
- C) capital
- D) entrepreneurship
- E) knowledge

Answer: E

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

24) If positive externalities exist and production is left to the private market, then at the quantity produced

- A)  $MSC = MSB$ .
- B)  $MSC < MSB$ .
- C)  $MSC > MSB$ .
- D)  $MSB =$  marginal external benefit.
- E)  $MSB = 1/MSC$ .

Answer: B

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

- 25) Choose the incorrect statement.
- A) A patent encourages invention.
  - B) A patent encourages innovation.
  - C) A patent has an economic cost.
  - D) A patent creates a negative externality.
  - E) A patent produces a monopoly.

Answer: D

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

- 26) Three ways governments can encourage production of goods with external benefits are
- A) private subsidies, marketable permits, and intellectual property rights.
  - B) private subsidies, marketable permits, and vouchers.
  - C) intellectual property rights, marketable permits, and vouchers.
  - D) taxes, emission charges, and marketable permits.
  - E) private subsidies, vouchers, and intellectual property rights.

Answer: E

Diff: 3 Type: MC

Topic: Positive Externality: Knowledge

- 27) The economic benefit of a patent or copyright must be balanced against
- A) the external benefit from the good.
  - B) the external cost of the good.
  - C) the marginal private cost of the good.
  - D) the cost of temporary monopoly.
  - E) the marginal social cost of the good.

Answer: D

Diff: 3 Type: MC

Topic: Positive Externality: Knowledge

- 28) In recent years, as provincial governments attempt to balance their budgets, they have increased tuition fees considerably. This increase will likely result in
- A) more students.
  - B) fewer students.
  - C) under-provision of education compared to the efficient level.
  - D) over-provision of education compared to the efficient level.
  - E) B and C.

Answer: E

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

- 29) A patent is an example of
- A) a subsidy.
  - B) a marketable permit.
  - C) a voucher.
  - D) a tax.
  - E) a legal device for creating property rights.

Answer: E

Diff: 1 Type: MC

Topic: Positive Externality: Knowledge

- 30) To increase efficiency,
- A) taxes are used to overcome both external benefits and external costs.
  - B) subsidies are used to overcome both external benefits and external costs.
  - C) subsidies are used to overcome external benefits, and taxes to overcome external costs.
  - D) taxes are used to overcome external benefits, and subsidies to overcome external costs.
  - E) emissions charges are used to overcome external benefits, and vouchers to overcome external costs.

Answer: C

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

- 31) A market economy tends to \_\_\_\_\_ goods with negative externalities and \_\_\_\_\_ goods with positive externalities.

- A) overproduce; overproduce
- B) overproduce; underproduce
- C) underproduce; overproduce
- D) underproduce; underproduce
- E) produce; consume

Answer: B

Diff: 2 Type: MC

Topic: Positive Externality: Knowledge

Source: Study Guide

- 32) The outcome from a voucher scheme is efficient when the government makes the value of the voucher equal to

- A) marginal external cost.
- B) marginal external benefit.
- C) private external cost.
- D) private external benefit.
- E) marginal social cost.

Answer: B

Type: MC

Topic: Positive Externality: Knowledge

Skill: Conceptual

AACSB: Reflective Thinking

33) A voucher can eliminate the deadweight loss and lead to an efficient outcome if the value of the voucher equals the \_\_\_\_\_ of the good.

- A) marginal external benefit
- B) marginal social benefit
- C) marginal private benefit
- D) marginal social cost
- E) marginal external cost

Answer: A

Type: MC

Topic: Positive Externality: Knowledge

Skill: Conceptual

AACSB: Reflective Thinking

Use the figure below to answer the following questions.

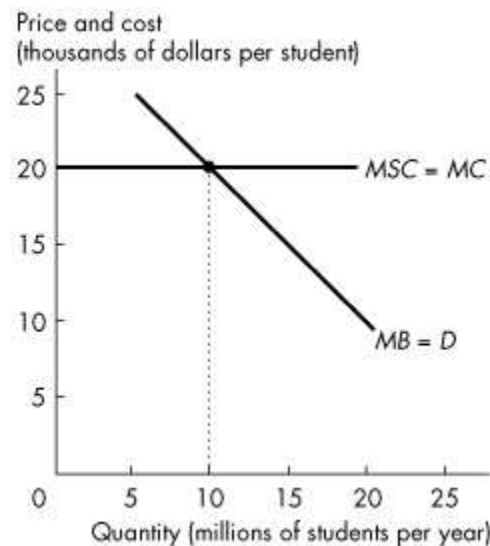


Figure 16.3.3

34) Refer to Figure 16.3.3. The figure shows the marginal private benefit and marginal social cost of a university education. If society's external benefit from university graduates is \$10,000 each, then the

- A) marginal social cost curve lies \$10,000 to the left of the private marginal benefit curve.
- B) marginal social cost curve lies \$10,000 to the right of the private marginal benefit curve.
- C) marginal social benefit curve lies \$10,000 below the private marginal benefit curve.
- D) marginal social benefit curve lies \$10,000 above the private marginal benefit curve.
- E) marginal social benefit curve is horizontal.

Answer: D

Type: MC

Topic: Positive Externality: Knowledge

Skill: Analytical

AACSB: Analytical Skills

35) Refer to Figure 16.3.3. The figure shows the marginal private benefit and marginal social cost of a university education. Society's external benefit from university graduates is \$10,000 each. With no subsidy

- A) no students go to university.
- B) less than 10 million students go to university.
- C) 10 million students go to university.
- D) more than 10 million students go to university.
- E) none of the above.

Answer: C

Type: MC

Topic: Positive Externality: Knowledge

Skill: Analytical

AACSB: Analytical Skills

36) Refer to Figure 16.3.3. The figure shows the marginal private benefit and marginal social cost of a university education. If society's external benefit from university graduates is \$10,000 each, then

- A) a subsidy of \$10,000 per student paid to the universities achieves efficiency.
- B) a tax of \$10,000 per student imposed on the universities achieves efficiency.
- C) 10 million students per year is the efficient number students.
- D) a subsidy of \$20,000 per student paid to the universities achieves efficiency.
- E) none of the above answers are correct.

Answer: A

Type: MC

Topic: Positive Externality: Knowledge

Skill: Analytical

AACSB: Analytical Skills

37) All of the following statements are correct *except*

- A) knowledge about one process spills over into other segments of the economy.
- B) additional knowledge makes people more productive, and there seems to be no tendency for the additional productivity from additional knowledge to diminish.
- C) knowledge has no external benefit.
- D) knowledge might be an exception to the principle of diminishing marginal benefit.
- E) it is necessary to use public policies to ensure that those who develop new ideas have incentives to encourage an efficient level of effort.

Answer: C

Type: MC

Topic: Positive Externality: Knowledge

Source: MyEconLab

38) Research and development \_\_\_\_\_ create an external benefit. With no intervention, we produce too \_\_\_\_\_ research and development.

A) does; little

B) does not; much

C) does not; little

D) does; much

E) none of the above. Research and development create an external cost.

Answer: A

Type: MC

Topic: Positive Externality: Knowledge

Source: MyEconLab

39) Researchers produce the efficient quantity of research and development if they receive a voucher equal to the marginal \_\_\_\_\_ benefit, or a subsidy equal to the marginal \_\_\_\_\_ benefit.

Patents and copyrights \_\_\_\_\_ result in an efficient amount of research and development.

A) social; social; cannot

B) social; social; can

C) external; external; cannot

D) external; external; can

E) external; social; can

Answer: D

Type: MC

Topic: Positive Externality: Knowledge

Source: MyEconLab

40) Most governments subsidize basic education because

A) there are external costs associated with well educated citizens.

B) the marginal social benefit from education is greater than the marginal private benefit.

C) of the existence of private schools.

D) the marginal social cost of education is greater than the marginal private cost.

E) otherwise too many students will receive educations.

Answer: B

Type: MC

41) Governments use subsidies \_\_\_\_\_.

A) as a means of increasing government spending

B) when they want to increase taxes

C) to achieve an efficient outcome in a market with external costs

D) to achieve an efficient outcome in a market with external benefits

E) and emission permits to achieve an efficient outcome in markets with external benefits

Answer: D

Type: MC

42) A private subsidy on a good

A) is similar to a tax because it decreases the production of the good being subsidized.

B) increases demand for the good.

C) punishes those who consume or produce the subsidized good.

D) has no effect on the quantity of the good produced.

E) increases production of that good.

Answer: E

Type: MC

43) A voucher can eliminate the deadweight loss and lead to an efficient outcome if the value of the voucher equals the \_\_\_\_\_ of the good.

A) marginal external cost

B) marginal social benefit

C) marginal private benefit

D) marginal social cost

E) marginal external benefit

Answer: E

Type: MC

44) Suppose that recycling rubber for running shoes creates an external benefit of \$2.00 per tonne of rubber. There are no external costs. The efficient amount of rubber will be recycled when the government creates a

A) subsidy of more than \$2.00 per tonne of rubber.

B) subsidy of \$2.00 per tonne of rubber.

C) tax of more than \$2.00 per tonne of rubber.

D) tax of \$2.00 per tonne of rubber.

E) voucher valued at \$2.10 a tonne of rubber.

Answer: B

Type: MC

## Chapter 17 Public Goods and Common Resources

### 17.1 Classifying Goods and Resources

1) A public good is

A) nonrival and nonexcludable.

B) produced by monopolies.

C) rival and excludable.

D) rival and nonexcludable.

E) nonrival and excludable.

Answer: A

Diff: 1 Type: MC

Topic: Classifying Goods and Resources

2) Private goods are

A) nonrival and excludable.

B) nonrival and nonexcludable.

- C) always produced in a non-regulated market.
- D) rival and excludable.
- E) rival and nonexcludable.

Answer: D

Diff: 2 Type: MC

Topic: Classifying Goods and Resources

3) When a good is nonrival and nonexcludable, it is a

- A) natural monopoly.
- B) private good.
- C) regulated good.
- D) public good.
- E) common resource.

Answer: D

Diff: 2 Type: MC

Topic: Classifying Goods and Resources

4) When a good is rival and excludable, it is a

- A) natural monopoly.
- B) public good.
- C) regulated good.
- D) private good.
- E) common resource.

Answer: D

Diff: 2 Type: MC

Topic: Classifying Goods and Resources

5) A natural monopoly is

- A) nonrival.
- B) excludable.
- C) rival.
- D) nonexcludable.
- E) both A and B.

Answer: E

Diff: 2 Type: MC

Topic: Classifying Goods and Resources

6) If a good is a public good,

- A) anyone can be excluded from enjoying its benefits.
- B) no one can be excluded from enjoying its benefits.
- C) consumers must pay a high price to enjoy its benefits.
- D) consumers pay a low price.
- E) economies of scale exist over the entire range of output for which there is a demand.

Answer: B

Diff: 2 Type: MC

Topic: Classifying Goods and Resources

7) An example of a public good is

- A) national defence.
- B) a Ford truck.
- C) a loaf of bread.
- D) a home computer.
- E) a television.

Answer: A

Diff: 2 Type: MC

Topic: Classifying Goods and Resources

8) A good that is nonrival and excludable is a

- A) private good.
- B) public good.
- C) government good.
- D) natural monopoly.
- E) common resource.

Answer: D

Diff: 2 Type: MC

Topic: Classifying Goods and Resources

9) A good that is rival and nonexcludable is a

- A) private good.
- B) public good.
- C) government good.
- D) regulated good.
- E) common resource.

Answer: E

Diff: 2 Type: MC

Topic: Classifying Goods and Resources

10) A common resource is

- A) regulated and excludable.
- B) rival and nonexcludable.
- C) nonrival and excludable.
- D) rival and excludable.
- E) nonrival and nonexcludable.

Answer: B

Diff: 2 Type: MC

Topic: Classifying Goods and Resources

11) Which one of the following goods is nonexcludable?

- A) a taxi
- B) a toll bridge
- C) the atmosphere
- D) an art museum
- E) all of the above

Answer: C

Diff: 2 Type: MC

Topic: Classifying Goods and Resources

12) Which one of the following goods is excludable?

- A) a city bus
- B) a bridge that does not charge a toll
- C) the atmosphere
- D) protection from the police force
- E) all of the above

Answer: A

Diff: 2 Type: MC

Topic: Classifying Goods and Resources

13) Which one of the following goods exhibits nonexcludability?

- A) a cheeseburger
- B) the Internet
- C) rides on the U.S. Space Shuttle
- D) cable TV
- E) air-traffic control

Answer: E

Diff: 2 Type: MC

Topic: Classifying Goods and Resources

14) When a city street is *not* congested, it is

- A) a common resource
- B) rival and excludable.
- C) rival and nonexcludable.
- D) a private good.
- E) a public good.

Answer: E

Diff: 2 Type: MC

Topic: Classifying Goods and Resources

Source: Study Guide

15) When a city street is congested, it is

- A) a common resource.
- B) nonrival and nonexcludable.
- C) nonrival and excludable.
- D) a private good.
- E) a public good.

Answer: A

Diff: 2 Type: MC

Topic: Classifying Goods and Resources

16) Suppose Bryan Adams wants to perform a concert in the City Park in Corner Brook Newfoundland. The city officials argue that the only way the concert can be given permission to be performed in the City Park is if it is free of charge. If Bryan Adams agrees to performing free of charge, then the concert is

- A) excludable.
- B) a private good.
- C) nonexcludable.
- D) rival.
- E) rival and nonexcludable.

Answer: C

Diff: 2 Type: MC

Topic: Classifying Goods and Resources

17) Which of the following quotations describes a rival good?

A) "Mom, Ashley is looking at me."

B) "Mom, Morgan won't let me watch the Backyardigans because she is watching Dora the Explorer."

C) "Mom, Harrison won't let me in his room."

D) "Mom, Taylor told me on the phone that he is also watching the Backyardigans on TV at his house."

E) "Mom said everyone in this house gets to enjoy the flowers in the garden."

Answer: B

Diff: 2 Type: MC

Topic: Classifying Goods and Resources

18) Which of the following quotations describes a nonexcludable and nonrival good?

A) "Mom, Ashley is looking at me."

B) "Mom, Morgan won't let me watch the Backyardigans because she is watching Dora the Explorer."

C) "Mom, Harrison won't let me in his room."

D) "Mom, Taylor told me on the phone that he is also watching the Backyardigans on TV at his house, but I'm not allowed to go over there."

E) "Mom said everyone in this house gets to enjoy the flowers in the garden."

Answer: E

Diff: 3 Type: MC

Topic: Classifying Goods and Resources

19) A common resource is

A) rival and either excludable or nonexcludable.

B) excludable and either rival or nonrival.

C) rival and excludable.

D) rival and nonexcludable.

E) nonexcludable and either rival or nonrival.

Answer: D

Diff: 1 Type: MC

Topic: Classifying Goods and Resources

20) An example of common resource is

A) fish in the ocean.

B) air-traffic control.

C) the Ambassador Bridge which goes between Windsor Ontario and Detroit.

D) the Internet.

E) national defence.

Answer: A

Diff: 1 Type: MC

Topic: Classifying Goods and Resources

21) The air in the atmosphere is

- A) nonrival and nonexcludable.
- B) rival and nonexcludable.
- C) nonrival and excludable.
- D) rival and excludable.
- E) a private good.

Answer: B

Diff: 1 Type: MC

Topic: Classifying Goods and Resources

22) Cable television and air-traffic control are similar to each other because both of them are

- A) excludable.
- B) nonexcludable.
- C) nonrival.
- D) rival.
- E) private services.

Answer: C

Diff: 1 Type: MC

Topic: Classifying Goods and Resources

23) Although both cable television and air-traffic control are nonrival, they differ from each other because

- A) cable television is a private good and air-traffic control is a public good.
- B) cable television is a public good and air-traffic control is a private good.
- C) cable television is nonexcludable and air-traffic control is a public good.
- D) cable television is nonexcludable and air-traffic control is excludable.
- E) cable television is excludable and air-traffic control is nonexcludable.

Answer: E

Diff: 1 Type: MC

Topic: Classifying Goods and Resources

## 17.2 Public Goods

1) An economy's marginal social benefit curve for a private good is obtained by summing the individual marginal

- A) cost curves horizontally.
- B) cost curves vertically.
- C) benefit curves horizontally.
- D) benefit curves vertically.
- E) benefit curves diagonally.

Answer: C

Diff: 2 Type: MC

Topic: Public Goods

Source: Study Guide

2) The marginal social benefit curve for a public good is derived by

- A) adding the marginal benefits of all individuals at each quantity.
- B) adding the quantities demanded by all individuals at each price.
- C) surveying consumers and asking how much they use a certain good or service.
- D) adding the total benefits for all consumers for a given quantity of the good.
- E) finding the maximum amount someone is willing to pay for one more unit of the good.

Answer: A

Diff: 2 Type: MC

Topic: Public Goods

3) The economy's demand curve for a public good is obtained by summing the individual

- A) marginal cost curves horizontally.
- B) marginal cost curves vertically.
- C) marginal benefit curves horizontally.
- D) marginal benefit curves vertically.
- E) benefit curves diagonally.

Answer: D

Diff: 2 Type: MC

Topic: Public Goods

Source: Study Guide

Use the figure below to answer the following questions.



**Figure 17.2.1**

4) Refer to Figure 17.2.1. Curve  $MB_A$  is Andrew's marginal benefit curve for a private good and curve  $MB_B$  is Betty's marginal benefit curve for the same private good. If Andrew and Betty are the only two consumers in the economy, which point would be on the economy's marginal social benefit curve?

- A) price of \$20, quantity of 3 units
- B) price of \$20, quantity of 4 units
- C) price of \$10, quantity of 4 units
- D) price of \$30, quantity of 0 units
- E) price of \$60, quantity of 1 units

Answer: B

Diff: 2 Type: MC

Topic: Public Goods

5) Refer to Figure 17.2.1. Curve  $MB_A$  is Andrew's marginal benefit curve for a public good and curve  $MB_B$  is Betty's marginal benefit curve for the same public good. If Andrew and Betty are the only two consumers in the economy, which point would be on the economy's marginal social benefit curve?

- A) price of \$20, quantity of 3
- B) price of \$20, quantity of 4
- C) price of \$10, quantity of 4
- D) price of \$30, quantity of 0
- E) price of \$60, quantity of 1

Answer: E

Diff: 2 Type: MC

Topic: Public Goods

6) For a private good, the economy's marginal social benefit curve is the \_\_\_\_\_ sum of the individual marginal benefit curves and for a public good, the economy's marginal social benefit curve is the \_\_\_\_\_ sum of the individual marginal benefit curves.

- A) vertical; vertical
- B) vertical; horizontal
- C) horizontal; vertical
- D) horizontal; horizontal
- E) horizontal and vertical; vertical and horizontal

Answer: C

Diff: 2 Type: MC

Topic: Public Goods

7) Suppose in a country there are only two persons. Person *A* is willing to pay \$50 to have one unit of a public good produced; person *B* is willing to pay \$60 to have one unit of a public good produced and \$50 to have two units produced. A point on the country's marginal social benefit curve for this public good is a price of \_\_\_\_\_ and quantity demanded of \_\_\_\_\_.

- A) \$50; 1 unit
- B) \$60; 1 unit
- C) \$110; 2 units
- D) \$110; 1 unit
- E) \$55; 1 unit

Answer: D

Diff: 3 Type: MC

Topic: Public Goods

8) If the marginal social cost of producing a public good is greater than the marginal social benefit, then

- A) more than the efficient quantity of the public good is being produced.
- B) less than the efficient quantity of the public good is being produced.
- C) the efficient quantity of the public good is being produced.
- D) the public good is being produced by a private firm.
- E) the public good must be a common resource.

Answer: A

Diff: 2 Type: MC

Topic: Public Goods

9) Free riding can occur if a good is

- A) excludable and rival.
- B) excludable and nonrival.
- C) a private good.
- D) nonexcludable and rival.
- E) nonexcludable and nonrival.

Answer: E

Diff: 2 Type: MC

Topic: Public Goods

10) Private provision of public goods

- A) fails because the private firm will always go broke.
- B) succeeds because public provision is often more costly.
- C) succeeds if consumers expect to obtain a benefit from the consumption of the public good.
- D) fails because of the free-rider problem.
- E) fails because private firms generally charge higher prices than public firms, and therefore lose customers.

Answer: D

Diff: 2 Type: MC

Topic: Public Goods

11) Public goods are provided by government because

- A) governments are more efficient than private firms at producing public goods.
- B) free-rider problems result in underproduction by private markets.
- C) people value national defence very highly.
- D) private firms will make an economic profit.
- E) private firms do not take into account the impact of external costs.

Answer: B

Diff: 2 Type: MC

Topic: Public Goods

12) The quantity of a public good produced by private provision

- A) is less than the efficient quantity.
- B) is equal to the efficient quantity.
- C) is greater than the efficient quantity.
- D) maximizes total public benefit.
- E) maximizes net public benefit.

Answer: A

Diff: 2 Type: MC

Topic: Public Goods

Source: Study Guide

13) Governments provide public goods such as national defence because

- A) governments are more efficient than private firms at producing public goods.
- B) of the free-rider problem which results in underproduction by private firms.
- C) people do not value national defence very highly.
- D) of the potential that private firms will make excess profit.
- E) of external costs.

Answer: B

Diff: 2 Type: MC

Topic: Public Goods

Source: Study Guide

- 14) The efficient scale of provision of a public good occurs where
- A) total benefit is at a maximum.
  - B) total benefit is at a minimum.
  - C) marginal social benefit is at a maximum.
  - D) marginal social benefit minus marginal social cost equals zero.
  - E) marginal social cost is at a minimum.

Answer: D

Diff: 2 Type: MC

Topic: Public Goods

Source: Study Guide

- 15) Public choice theory predicts that government
- A) acts to promote the redistribution of wealth and income.
  - B) acts to maximize the amount of campaign contributions.
  - C) acts to eliminate waste and promote an efficient allocation of resources.
  - D) makes choices that result in efficient provision of public goods.
  - E) makes choices that result in inefficient overprovision of public goods.

Answer: E

Diff: 2 Type: MC

Topic: Public Goods

- 16) Public choice theory predicts that
- A) voters are fully informed about the effects of policies.
  - B) voters are rationally ignorant.
  - C) governments make choices that achieve an efficient provision of public goods.
  - D) votes are based on reality, not perceptions.
  - E) votes are based on lobbyists' viewpoints.

Answer: B

Diff: 2 Type: MC

Topic: Public Goods

- 17) According to public choice theory government failure occurs because
- A) government officials do not listen to the pleading of special interest groups.
  - B) lobbyists write legislation.
  - C) government officials act in their own self-interest.
  - D) voters are fully informed about the effects of policies.
  - E) government cannot calculate the levels of externalities because there is no market for them.

Answer: C

Diff: 2 Type: MC

Topic: Public Goods

- 18) To attract a majority of voters, a political party will
- A) aim its message at the most enthusiastic groups.
  - B) aim its message at a small but loyal following.
  - C) present a political package aimed at making the wealthier voters better off.
  - D) present a political package aimed at making a majority of voters better off.
  - E) respond strongest to the most vigorous lobbyists.

Answer: D

Diff: 2 Type: MC

Topic: Public Goods

- 19) The idea that the platforms of the political parties will tend to become similar over time is
- A) not a reflection of reality.
  - B) true in theory but not true in actuality.
  - C) called the principle of minimum differentiation.
  - D) called the principle of minimal political confrontation.
  - E) the result of intense lobbying pressure.

Answer: C

Diff: 1 Type: MC

Topic: Public Goods

- 20) Minimum differentiation among the political parties suggests that
- A) the parties will have few ideas in common on their platforms.
  - B) the parties will offer few ideas on minimizing the size and scope of government.
  - C) the platforms of the parties will tend to become similar as they try to appeal to a majority of voters.
  - D) the platforms of the parties will tend to become dissimilar as they try to appeal to a loyal majority of voters.
  - E) the platforms of the parties will tend to have few, if any, new ideas.

Answer: C

Diff: 2 Type: MC

Topic: Public Goods

- 21) Rational ignorance suggests that
- A) all voters are ignorant.
  - B) all voters will be ignorant on issues that are not of special interest to them.
  - C) all voters will pursue information about each issue before voting.
  - D) low voter turnout is due to a lack of understanding of the importance of the political platforms.
  - E) it is easier to aim at the median voter because it is a less costly strategy for the politicians.

Answer: B

Diff: 2 Type: MC

Topic: Public Goods

22) Rational ignorance suggests that a voter should stop acquiring more information about an issue when

- A) the marginal benefit from acquiring the information equals zero.
- B) the total cost of acquiring the information is minimized.
- C) the total benefit from acquiring the information is maximized.
- D) the marginal cost of acquiring the information is equal to the marginal benefit derived from the information.
- E) the marginal cost of acquiring the information is greater than zero.

Answer: D

Diff: 2 Type: MC

Topic: Public Goods

23) Rational ignorance suggests that voters will

- A) understand defence technology before voting for defence policy.
- B) understand the auditing procedures of the Canada Revenue Agency before voting for tax reform.
- C) understand the chemistry of the atmosphere before voting for a clean-air act.
- D) vote without complete information on many issues.
- E) vote based on their complete trust in politicians and bureaucrats.

Answer: D

Diff: 2 Type: MC

Topic: Public Goods

24) Public choice theory assumes those involved in the political process are motivated by

- A) self-interest.
- B) the desire to achieve efficiency.
- C) dishonesty.
- D) public spirit.
- E) the desire for maximum profit.

Answer: A

Diff: 1 Type: MC

Topic: Public Goods

25) If all voters are well informed about national defence, the quantity of national defence provided by the government will be

- A) greater than the efficient quantity.
- B) less than the efficient quantity.
- C) the least costly quantity.
- D) the efficient quantity.
- E) the quantity that maximizes the budget of the Department of National Defence.

Answer: D

Diff: 2 Type: MC

Topic: Public Goods

Source: Study Guide

26) If voters are rationally ignorant, the quantity of national defence provided by the government will be

- A) greater than the efficient quantity.
- B) less than the efficient quantity.
- C) the least costly quantity.
- D) the quantity that maximizes the budget of the Department of National Defence.
- E) both A and D are correct.

Answer: E

Diff: 2 Type: MC

Topic: Public Goods

27) Competition between two political parties will cause those parties to propose policies

- A) that are quite different.
- B) that are quite similar.
- C) of rational ignorance.
- D) that reduce the well-being of middle-income families and increasing the well-being of the rich and the poor.
- E) that equate total costs and total benefits.

Answer: B

Diff: 2 Type: MC

Topic: Public Goods

Source: Study Guide

28) The budget of a government department is likely to increase beyond the efficient quantity if

- A) voters are well informed.
- B) there is rational voter ignorance combined with special interest lobbying.
- C) the political equilibrium can be described in terms of social interest theory.
- D) bureaucrats are rationally ignorant.
- E) there are negative externalities.

Answer: B

Diff: 2 Type: MC

Topic: Public Goods

29) The budget of a government department is likely to be efficient if

- A) voters are well informed.
- B) there is rational voter ignorance combined with special interest lobbying.
- C) the political equilibrium can be described in terms of public choice theory.
- D) bureaucrats are rationally ignorant.
- E) there are negative externalities.

Answer: A

Diff: 3 Type: MC

Topic: Public Goods

30) According to public choice theory, a voter will tend to be well informed if the issue in question

- A) is complicated and difficult to understand.
- B) affects everyone a little.
- C) is of special interest to a small group to which the voter does not belong.
- D) has a large direct effect on the voter.
- E) is important even if it does not directly affect the voter.

Answer: D

Diff: 2 Type: MC

Topic: Public Goods

31) Competitors who make themselves identical to appeal to the maximum number of voters illustrate the

- A) principle of maximum differentiation.
- B) principle of minimum differentiation.
- C) principle of rational ignorance.
- D) principle of nonrivalry.
- E) principle of excludability.

Answer: B

Diff: 2 Type: MC

Topic: Public Goods

Source: Study Guide

32) All of the following statements regarding rational ignorance are true *except*

- A) it results when the cost of information exceeds the expected benefit of acquiring the information.
- B) it allows special interest groups to exert political influence.
- C) combined with special interest groups, it yields inefficiency in the provision of public goods.
- D) it leads to an efficient outcome.
- E) none of the above.

Answer: D

Diff: 3 Type: MC

Topic: Public Goods

Use the table below to answer the following questions.

**Table 17.2.1**

Number of Voters	Current Income	Income after Proposal A	Income after Proposal B	Income after Proposal C
25	\$10,000	\$15,000	\$20,000	\$5,000
25	\$20,000	\$25,000	\$20,000	\$18,000
25	\$40,000	\$45,000	\$40,000	\$38,000
25	\$90,000	\$75,000	\$80,000	\$99,000

33) In Table 17.2.1, which one of the proposals will have the greatest support?

- A) Current income distribution
- B) Proposal A
- C) Proposal B
- D) Proposal C
- E) Proposal A or C

Answer: B

Diff: 3 Type: MC

Topic: Public Goods

34) In Table 17.2.1, which one of the proposals will have the least support?

- A) Current income distribution
- B) Proposal A
- C) Proposal B
- D) Proposal C
- E) Proposal A or C

Answer: D

Diff: 3 Type: MC

Topic: Public Goods

35) In Table 17.2.1, which of the proposals would be supported by political parties according to the principle of minimum differentiation?

- A) Current income distribution
- B) Proposal A
- C) Proposal B
- D) Proposal C
- E) Proposal A or C

Answer: B

Diff: 3 Type: MC

Topic: Public Goods

36) Growing voter income can lead to the growth of the government sector because

- A) public goods are income elastic.
- B) public goods are income inelastic.
- C) richer voters are more likely to be rationally ignorant.
- D) richer voters do not care about overprovision of government goods.
- E) none of the above.

Answer: A

Diff: 2 Type: MC

Topic: Public Goods

37) According to public choice theory, a voter will favour a candidate whose political program is

- A) perceived by the voter to be in his self-interest.
- B) best for the majority of the people.
- C) closest to efficiency.
- D) favoured by the median voter.
- E) all of the above.

Answer: A

Diff: 2 Type: MC

Topic: Public Goods

Source: Study Guide

38) Rational ignorance

- A) results when the cost of acquiring information exceeds the benefit of acquiring the information.
- B) allows special interest groups to exert political influence.
- C) combined with special-interest groups can yield inefficient provision of public goods.
- D) results in all of the above.
- E) results in none of the above.

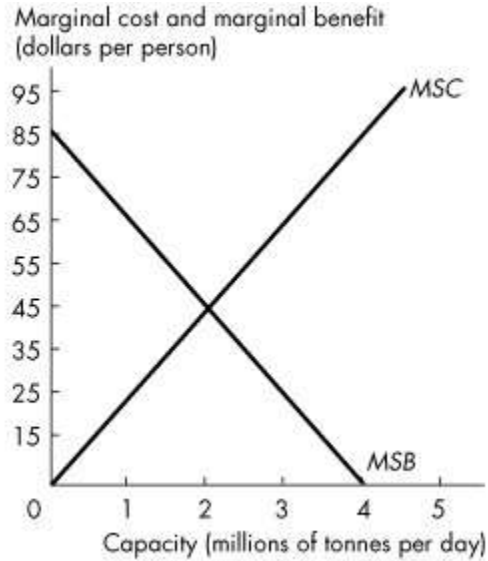
Answer: D

Diff: 3 Type: MC

Topic: Public Goods

Source: Study Guide

Use the figure below to answer the following question.



**Figure 17.2.2**

39) Refer to Figure 17.2.2. The graph shows the marginal social benefit and marginal social cost of a garbage disposal system in a city of 1 million people. If voters are well informed about the costs and benefits of the garbage disposal system, the political equilibrium of garbage is

- A) 2.0 million tonnes a day.
- B) 1.5 million tonnes a day.
- C) 2.5 million tonnes a day.
- D) 4.0 million tonnes a day.
- E) 0 million tonnes a day.

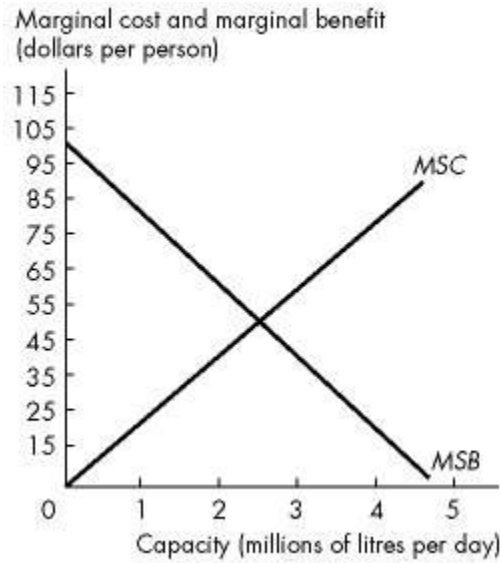
Answer: A

Diff: 3 Type: MC

Topic: Public Goods

Source: MyEconLab

Use the figure below to answer the following question.



**Figure 17.2.3**

40) Refer to Figure 17.2.3. The graph provides information about a waste disposal system in a city of 1 million people. If the city installs the efficient capacity, then each person pays \_\_\_\_\_ in taxes.

- A) \$125
- B) \$62.50
- C) \$250
- D) zero
- E) \$31.25

Answer: B

Diff: 3 Type: MC

Topic: Public Goods

Source: MyEconLab

41) Your city council is contemplating upgrading its traffic control system and the council believes that the bigger the computer it installs, the better job it can do. Elected officials want to install the scale of the system that will win the most votes. The city bureaucrats want to maximize the budget. Suppose that you are an economist and your job is to calculate the scale of the system that uses resources efficiently. Public choice theory predicts that the quantity chosen will result in \_\_\_\_\_. As an informed voter, you can attempt to influence the choice of the correct system by encouraging other voters to \_\_\_\_\_.

A) overprovision that maximizes the budget of the bureaucrats; vote only for officials that will provide the smaller efficient quantity

B) overprovision that maximizes the budget of the bureaucrats; increase their income elasticity of demand for the new traffic control system

C) the efficient quantity; decrease their income elasticity of demand for the new traffic control system

D) the efficient quantity; increase their income elasticity of demand for the new traffic control system

E) overprovision that minimizes the income elasticity of demand of bureaucrats; decrease their elasticity of demand for the new traffic control system

Answer: A

Diff: 3 Type: MC

Topic: Public Goods

Source: MyEconLab

42) According to \_\_\_\_\_ theory, governments make choices that result in an \_\_\_\_\_ provision of public goods. This outcome occurs in \_\_\_\_\_.

A) public choice; efficient; political markets in which voters are rationally ignorant

B) social interest; efficient; a perfect political system in which voters are fully informed about the effects of policies

C) social interest; efficient; political markets in which voters are rationally ignorant

D) public choice; inefficient; a perfect political system in which voters are full informed about the effects of policies

E) social interest; inefficient; political markets in which voters are rationally ignorant

Answer: B

Diff: 3 Type: MC

Topic: Public Goods

Source: MyEconLab

### 17.3 Common Resources

1) Which of the following achieves the efficient use of a common resource?

- A) property rights, production quotas, and individual transferable quotas
- B) property rights, individual transferable quotas, and subsidies
- C) property rights, production quotas, and subsidies
- D) individual transferable quotas and copyrights
- E) production quotas, individual transferable quotas, and copyrights

Answer: A

Diff: 2 Type: MC

Topic: Common Resources

2) One way to alleviate the tragedy of the commons is to

- A) eliminate production quotas for using the common resource.
- B) make the resource private property.
- C) allow all individuals to use the common resource free of charge.
- D) distribute common resources among those individuals who really need the resource free of charge.
- E) set a price of \$1 per unit of the common resource because it is an affordable price.

Answer: B

Diff: 2 Type: MC

Topic: Common Resources

3) An individual transferable quota is a production limit that

- A) has a price equal to marginal cost.
- B) is assigned to every producer in the industry at a predetermined price.
- C) is assigned to an individual who must transfer the quota to anyone the government assigns.
- D) is assigned to an individual who is free to transfer the quota to someone else.
- E) has a price equal to marginal benefit.

Answer: D

Diff: 2 Type: MC

Topic: Common Resources

4) The "tragedy of the commons" refers to

- A) the inability of lower income groups to achieve a higher level of education.
- B) the absence of incentives to prevent the overuse of a common resource that arises when its users have no incentive to conserve it and use it sustainably.
- C) the acceptance of deplorable working conditions by those who lack the human capital to obtain a better job.
- D) the tendency for bureaucrats to maximize their budget.
- E) farmers who allow their livestock to overgraze their fields.

Answer: B

Diff: 2 Type: MC

Topic: Common Resources

5) The absence of incentives to prevent the overuse of a common resource that arises when its users have no incentive to conserve it and use it sustainably is referred to as

- A) unsustainable production.
- B) sustainable production.
- C) the tragedy of the commons.
- D) rational ignorance.
- E) irrational production.

Answer: C

Diff: 2 Type: MC

Topic: Common Resources

6) Sustainable production is

- A) the rate of production that can be maintained indefinitely.
- B) the production output with the lowest average total cost.
- C) the production output where  $MC=ATC$ .
- D) the rate of production that maximizes marginal private benefit.
- E) the rate of production where  $MB=MC$ .

Answer: A

Diff: 2 Type: MC

Topic: Common Resources

7) Common resources are overused because

- A) the marginal private benefit of operating a boat is the quantity of fish a boat can catch.
- B) the social benefits outweigh the private benefits.
- C) the marginal private benefit will always exceed the marginal social cost.
- D) external costs are not considered.
- E) social costs are controlled by production quotas.

Answer: D

Diff: 2 Type: MC

Topic: Common Resources

8) In the equilibrium for a common resource with no government regulation,

- A) marginal social benefit is greater than marginal social cost.
- B) marginal social benefit equals marginal social cost.
- C) marginal social benefit is less than marginal cost.
- D) marginal social benefit is greater than marginal cost.
- E) marginal social benefit equals marginal cost.

Answer: E

Diff: 2 Type: MC

Topic: Common Resources

Source: Study Guide

- 9) The tragedy of the commons is the absence of incentives to
- A) reduce marginal cost of common resources.
  - B) prevent underuse of common resources.
  - C) prevent overuse of common resources.
  - D) discover new common resources.
  - E) export wool in sixteenth-century England.

Answer: C

Diff: 2 Type: MC

Topic: Common Resources

Source: Study Guide

- 10) When a production quota is used to remedy the problem of the commons, then
- A) the production quota is set so that use of the resource is where marginal private benefit equals marginal cost.
  - B) the production quota is set so that use of the resource is where marginal private benefit equals marginal social benefit.
  - C) the market equilibrium, but not the efficient outcome, is achieved.
  - D) all users of the resource have an incentive to cheat on the production quota.
  - E) the production quota is set so that marginal social benefit is maximized.

Answer: D

Type: MC

Topic: Common Resources

Skill: Conceptual

AACSB: Reflective Thinking

- 11) Setting a production quota does not always achieve the efficient use of a common resource because \_\_\_\_\_.

- A) marginal cost differs for each producer and it is in everyone's self-interest to cheat and produce more than the assigned quota
- B) the marginal private benefit from a production quota is zero
- C) marginal cost differs for each producer and the marginal social benefit from a production quota is zero
- D) a production quota does not totally eliminate the problem of free-ridership of a common resource
- E) none of the above

Answer: A

Type: MC

Topic: Common Resources

Skill: Analytical

Source: MyEconLab

AACSB: Analytical Skills

- 12) All of the following statements are true *except* \_\_\_\_\_.
- A) the market price of an ITQ equals the marginal social benefit minus the marginal cost
  - B) when an ITQ system is used in a fishing market, boat owners with a low marginal cost are willing and able to pay more for a quota than are boat owners with a higher marginal cost
  - C) individual differences in marginal cost do not prevent an ITQ system from delivering the efficient outcome
  - D) an ITQ is a production limit that is assigned to an individual who is free to transfer the quota to someone else
  - E) Canada does not use ITQs

Answer: A

Type: MC

Topic: Common Resources

Skill: Analytical

Source: MyEconLab

AACSB: Analytical Skills

13) Which of the following applies to the tragedy of the commons?

- I. In the absence of government action, there is an absence of incentives to prevent the overuse of the common resource.
- II. When consumers take account of the marginal social benefit and marginal social cost, overuse of the resource occurs.
- III. Even with government action, it is impossible for an efficient level of output to be achieved.

- A) I only
- B) I and II
- C) II and III
- D) I, II and III
- E) none of the above

Answer: A

Type: MC

14) In which of the following cases can the tragedy of the commons occur?

- I. Cattle grazing on private ranches.
- II. Catching lobsters off the coast of Florida.
- III. Raising salmon on salmon farms.
- IV) Using legal services provided by the courts.

- A) I only
- B) II only
- C) II and III only
- D) I and IV only
- E) I and II only

Answer: B

Type: MC

15) For a common resource, the marginal private cost curve slopes \_\_\_\_\_ and the marginal social cost curve slopes \_\_\_\_\_.

- A) upward; upward
- B) upward; downward
- C) downward; upward
- D) downward; downward
- E) upward or downward; in the same direction as the marginal private cost curve

Answer: A

Type: MC

16) The efficient use of a common resource requires that the \_\_\_\_\_ equals the \_\_\_\_\_.

- A) marginal private benefit; marginal social cost
- B) marginal social benefit; marginal social cost
- C) marginal private benefit; marginal social benefit
- D) marginal social cost; marginal private cost
- E) total benefit; total cost

Answer: B

Type: MC

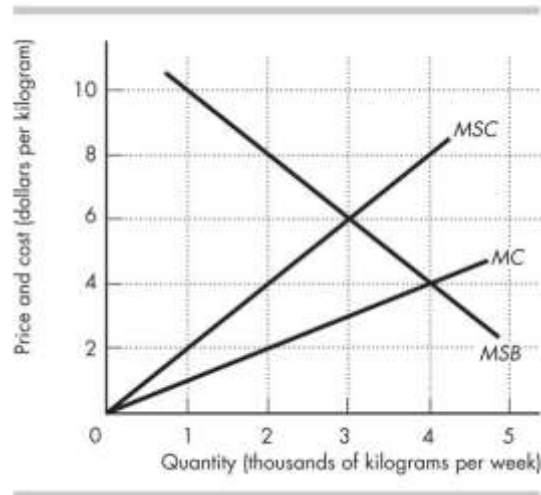
17) If property rights are assigned to a common resource, then the

- A) government needs to set an ITQ to achieve efficiency.
- B) government needs to set a production quota to achieve efficiency.
- C) more than the efficient quantity is produced.
- D) marginal social benefit increases.
- E) marginal private cost becomes equal to the marginal social cost.

Answer: E

Type: MC

Use the figure below to answer the following questions.



**Figure 17.3.1**

18) Figure 17.3.1 shows the marginal private cost curve, marginal social cost curve, and marginal social benefit curve for cod, a common resource. The equilibrium quantity in an unregulated market is

- A) 0 kilograms a week.
- B) 4,000 kilograms a week.
- C) 3,000 kilograms a week.
- D) 5,000 kilograms a week.
- E) 1,000 kilograms a week.

Answer: B

Type: MC

19) Figure 17.3.1 shows the marginal private cost curve, marginal social cost curve, and marginal social benefit curve for cod, a common resource. The efficient quantity is

- A) 0 kilograms a week.
- B) 4,000 kilograms a week.
- C) 3,000 kilograms a week.
- D) 5,000 kilograms a week.
- E) 1,000 kilograms a week.

Answer: C

Type: MC

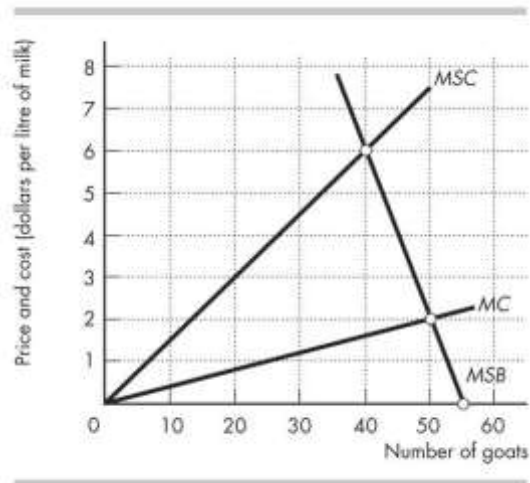
20) Figure 17.3.1 shows the marginal private cost curve, marginal social cost curve, and marginal social benefit curve for cod, a common resource. A quota that results in the common resource being used efficiently is set at

- A) 0 kilograms a week.
- B) 4,000 kilograms a week.
- C) 3,000 kilograms a week.
- D) 5,000 kilograms a week.
- E) 1,000 kilograms a week.

Answer: C

Type: MC

Use the figure below to answer the following questions.



**Figure 17.3.2**

21) Figure 17.3.2 shows the marginal private cost curve, marginal social cost curve, and marginal social benefit curve for raising goats on a common pasture. The equilibrium in an unregulated market is

- A) 0 goats.
- B) 40 goats.
- C) 50 goats.
- D) 55 goats.
- E) 35 goats.

Answer: C

Type: MC

22) Figure 17.3.2 shows the marginal private cost curve, marginal social cost curve, and marginal social benefit curve for raising goats on a common pasture. The efficient quantity is

- A) 0 goats.
- B) 40 goats.
- C) 50 goats.
- D) 55 goats.
- E) 35 goats.

Answer: B

Type: MC

23) Figure 17.3.2 shows the marginal private cost curve, marginal social cost curve, and marginal social benefit curve for raising goats on a common pasture. A quota that results in the common resource being used efficiently is set at

- A) 0 goats.
- B) 35 goats.
- C) 50 goats.
- D) 55 goats.
- E) 40 goats.

Answer: E

Type: MC

24) Figure 17.3.2 shows the marginal private cost curve, marginal social cost curve, and marginal social benefit curve for raising goats on a common pasture. If property rights to the pasture are granted to a farmer so that the farmer owns the pasture, the farmer raises

- A) 0 goats.
- B) 35 goats.
- C) 50 goats.
- D) 55 goats.
- E) 40 goats.

Answer: E

Type: MC

## Chapter 18 Markets for Factors of Production

### 18.1 The Anatomy of Factor Markets

1) The four factors of production are

- A) productive factors, neutral factors, entrepreneurial factors, and nonproductive factors.
- B) men, women, animals, and children.
- C) labour, capital, entrepreneurship, and land.
- D) machines, factories, buildings, and farms.
- E) labour, money, profits, and land.

Answer: C

Diff: 1 Type: MC

Topic: The Anatomy of Factor Markets

2) Profit is the factor price for

- A) capital.
- B) land.
- C) entrepreneurship.
- D) labour.
- E) capital services.

Answer: C

Type: MC

Topic: The Anatomy of Factor Markets

Skill: Recognition

AACSB: Reflective Thinking

- 3) Coal is an example of
- A) a nonrenewable natural resource.
  - B) a renewable natural resource.
  - C) capital.
  - D) a common resource.
  - E) capital.

Answer: A

Type: MC

Topic: The Anatomy of Factor Markets

Skill: Conceptual

AACSB: Reflective Thinking

4) Water from the Mackenzie River is an example of

- A) a nonrenewable natural resource.
- B) a natural resource that can be used repeatedly.
- C) capital.
- D) a static resource.
- E) a capital service.

Answer: B

Type: MC

Topic: The Anatomy of Factor Markets

Skill: Conceptual

AACSB: Reflective Thinking

5) Natural resources that are depleted as they are used

- A) should not be used.
- B) are called nonrenewable natural resources.
- C) should be used for only highly valued purposes.
- D) should be conserved for future generations.
- E) are called renewable natural resources.

Answer: B

Diff: 1 Type: MC

Topic: The Anatomy of Factor Markets

6) An example of a nonrenewable natural resource is

- A) oil.
- B) Lake Erie.
- C) rain.
- D) sunshine.
- E) the St. Lawrence River.

Answer: A

Diff: 1 Type: MC

Topic: The Anatomy of Factor Markets

7) Choose the statement that is *incorrect*.

- A) Capital consists of the tools, instruments, machines, buildings, and other constructions that have been produced in the past and that businesses now use to produce goods and services.
- B) A market for capital services is a rental market.
- C) The services of the capital that a firm owns and operates have an implicit price that arises from depreciation and interest costs.
- D) Capital is a factor of production.
- E) Most capital services are traded in a market.

Answer: E

Type: MC

8) Choose the statement that is *incorrect*.

- A) Entrepreneurship is a factor of production.
- B) Entrepreneurs receive the profit or bear the loss that results from their business decisions.
- C) Entrepreneurship consists of all the gifts of nature.
- D) Entrepreneurial services are traded in markets.
- E) Both C and D are incorrect.

Answer: E

Type: MC

9) Choose the statement that is correct.

- A) Labour services are the physical and mental work effort that people supply to produce goods and services.
- B) A labour market is a collection of people and firms who trade labour services.
- C) The price of labour services is the wage rate.
- D) Most labour services are traded on a contract, called a job.
- E) all of the above.

Answer: E

Type: MC

## 18.2 The Demand for a Factor of Production

1) Firms hire labour

- A) to minimize the average cost of the employment of labour.
- B) to exploit workers.
- C) to maximize profit.
- D) because capital is more expensive.
- E) to minimize costs.

Answer: C

Diff: 1 Type: MC

Topic: The Demand for a Factor of Production

2) To maximize profit, a firm hires labour until

- A) there is no more labour available at the market wage rate.
- B) they can sell that labour for no more than what they paid for it.
- C) the wage rate paid to the labour equals the marginal cost of production.
- D) the additional benefit of hiring the labour is equal to the additional revenue the labour generates.
- E) the value of marginal product equals the wage rate.

Answer: E

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

3) To maximize profit, the firm must equate the

- A) wage rate to the price of the good.
- B) wage rate to the marginal product of labour.
- C) value of marginal product to the factor price.
- D) marginal factor cost to the price of the output.
- E) marginal cost of the factor to the marginal product of the factor.

Answer: C

Diff: 1 Type: MC

Topic: The Demand for a Factor of Production

4) The value of marginal product of labour is the revenue

- A) generated by selling an additional unit of output.
- B) needed to hire an additional unit of labour.
- C) generated by the employment of an additional unit of labour.
- D) needed to cover the cost of producing an additional unit of output.
- E) generated to cover the cost of hiring an extra unit of labour.

Answer: C

Diff: 1 Type: MC

Topic: The Demand for a Factor of Production

5) If marginal product of a restaurant employee is 10 customers per hour, and the price of a meal is \$15, the restaurant employee's value of marginal product is

- A) \$15.
- B) \$7.5.
- C) \$12.5.
- D) \$10.
- E) \$150.

Answer: E

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

6) Suppose a gift shop in Corner Brook Newfoundland hires workers to personalize ornaments for Christmas. The store sells the personalized ornaments for \$6 each. The value of marginal product of this store's fourth worker is \$60. The marginal product of the fourth worker is

- A) 6 ornaments.
- B) 10 ornaments.
- C) 60 ornaments.
- D) 360 ornaments.
- E) 90 ornaments.

Answer: B

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

7) If the marginal product of a baker is 10 loaves of bread, and the price of a loaf of bread is \$2, the baker's value of marginal product is

- A) \$2.00.
- B) \$20.00.
- C) \$0.20.
- D) \$5.00.
- E) \$12.00.

Answer: B

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

8) The Brown's Egg store in Lethbridge Alberta hires workers to paint eggs. The price of an egg is \$2.50. The value of marginal product of this store's fifth worker is \$25. The marginal product of the fifth worker is

- A) 62.5 eggs.
- B) 25 eggs.
- C) 2 eggs.
- D) 10 eggs.
- E) 0.1 eggs.

Answer: D

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

Use the table below to answer the following questions.

**Table 18.2.1**

Labour (workers)	Output (units)
0	0
1	5
2	11
3	18
4	26
5	32
6	37
7	41
8	44
9	46
10	47

9) Refer to Table 18.2.1. If the firm can sell all the output it wants for the price of \$5 a unit, what is the value of marginal product of the 6th worker?

- A) \$20
- B) \$0
- C) \$25
- D) \$40
- E) \$185

Answer: C

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

10) Refer to Table 18.2.1. If the firm can sell all the output it wants for the price of \$4 a unit, what is the profit-maximizing number of workers if the wage rate is \$12?

- A) zero
- B) 10
- C) 4
- D) 8
- E) 6

Answer: D

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

11) Refer to Table 18.2.1. If the firm can sell all the output it wants for the price of \$5 a unit, what is the profit-maximizing number of workers if the wage rate is \$30?

- A) 1
- B) 3
- C) 5
- D) 6
- E) 7

Answer: C

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

12) Refer to Table 18.2.1. If the firm can sell all the output it wants for the price of \$10 a unit, what is the profit-maximizing number of workers if the wage rate is \$30?

- A) 1
- B) 5
- C) 6
- D) 8
- E) 9

Answer: D

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

13) If the price of the firm's output decreases, the value of marginal product curve

- A) remains unchanged.
- B) becomes more elastic.
- C) becomes more inelastic.
- D) shifts to the left.
- E) shifts to the right.

Answer: D

Diff: 1 Type: MC

Topic: The Demand for a Factor of Production

14) Mr. Shaw has a small factory in Estevan Saskatchewan. He will continue hiring labour as long as the value of marginal product of labour \_\_\_\_\_ the wage rate.

- A) is greater than
- B) is less than
- C) is less than or equal to
- D) determines
- E) maximizes

Answer: A

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

- 15) A profit-maximizing firm will continue to hire labour until the
- A) wage rate equals the last worker's marginal product.
  - B) last worker's value of marginal product is maximized.
  - C) last worker's value of marginal product is negative.
  - D) wage rate equals the last worker's value of marginal product.
  - E) last worker's value of marginal product equals zero.

Answer: D

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

Source: Study Guide

- 16) A shift in a firm's demand curve for labour occurs when there is a change in the
- A) wage rate.
  - B) opportunity cost of labour.
  - C) price of the output.
  - D) working-age population.
  - E) marginal cost of labour.

Answer: C

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

- 17) A shift in a firm's demand curve for labour occurs for all of the following reasons *except* a change in
- A) the prices of other factors of production.
  - B) technology.
  - C) the price of the firm's output.
  - D) wage rate.
  - E) marginal product of labour.

Answer: D

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

- 18) Suppose a profit-maximizing firm hires labour in a competitive labour market. If the value of marginal product of labour is greater than the wage rate, the firm should
- A) increase the wage rate.
  - B) decrease the wage rate.
  - C) increase the quantity of labour it hires.
  - D) decrease the quantity of labour it hires.
  - E) shift to a more labour-intensive production process.

Answer: C

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

- 19) When the price of a firm's output increases
- A) the supply of labour increases.
  - B) the firm hires less labour.
  - C) the marginal product of labour increases.
  - D) the firm's demand for labour curve shifts leftward.
  - E) the value of marginal product of labour increases.

Answer: E

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

- 20) A technological change that increases the value of marginal product of labour shifts the labour

- A) demand curve leftward.
- B) demand curve rightward.
- C) supply curve leftward.
- D) supply curve rightward.
- E) B and D.

Answer: B

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

Source: Study Guide

- 21) A decrease in the price of factors of production that are substitutes for labour shifts the labour

- A) demand curve leftward.
- B) demand curve rightward.
- C) supply curve leftward.
- D) supply curve rightward.
- E) B and D.

Answer: A

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

- 22) Mr. Smith's firm is currently hiring 30 workers. The value of marginal product of the last worker is \$7.00 per hour. The wage rate is \$8.00 per hour. To increase profit, Mr. Smith should

- A) continue hiring 30 workers because the firm earns a surplus of \$1.00 on each worker hired.
- B) increase the price of the firm's product so that the value of marginal product increases to \$8.00 per hour.
- C) decrease the price of the firm's product so that the value of marginal product increases to \$8.00 per hour.
- D) decrease the number of workers until the value of marginal product of labour equals \$8.00.
- E) increase the number of workers until the value of marginal product of labour equals \$8.00.

Answer: D

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

23) Suppose a profit-maximizing firm hires labour in a competitive labour market. If the value of marginal product of labour is less than the wage rate, the firm should

- A) increase the wage rate.
- B) decrease the wage rate.
- C) increase the quantity of labour it hires.
- D) decrease the quantity of labour it hires.
- E) shut down.

Answer: D

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

24) A decrease in the price of a firm's output

- A) decreases the supply of labour.
- B) increases the supply of labour.
- C) increases the value of marginal product of labour.
- D) decreases the quantity of labour demanded.
- E) decreases the value of marginal product of labour.

Answer: E

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

*Use the table below to answer the following questions.*

**Table 18.2.2**

Wendy owns an apple orchard and she employs students to pick the apples. In an hour they can pick the following amounts:

Number of Students	Quantity of Apples (kilograms per hour)
1	20
2	50
3	90
4	120
5	145
6	165
7	180
8	190

25) Refer to Table 18.2.2. If the price of apples is \$0.50 per kilogram, the value of marginal product of the 5th student is

- A) \$0.50 an hour.
- B) \$72.50 an hour.
- C) \$14.50 an hour.
- D) \$12.50 an hour.
- E) \$10 an hour.

Answer: D

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

26) Consider Table 18.2.2. If the price of apples is \$0.50 per kilogram, and the wage rate for apple pickers is \$7.50 per hour, then the number of pickers that Wendy will hire is

- A) 1.
- B) 3.
- C) 5.
- D) 7.
- E) 8.

Answer: D

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

27) A firm's value of marginal product of labour curve is also its

- A) marginal cost curve of labour.
- B) demand curve for labour.
- C) supply curve of labour.
- D) supply curve of output.
- E) marginal product curve.

Answer: B

Diff: 1 Type: MC

Topic: The Demand for a Factor of Production

Source: Study Guide

28) The demand curve for labour will shift rightward as a result of

- A) a decrease in the price of the firm's output.
- B) an increase in the wage rate.
- C) a decrease in the price of a substitute factor of production.
- D) an increase in the price of a substitute factor of production.
- E) a decrease in the wage rate.

Answer: D

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

29) The demand curve for labour will shift leftward as a result of

- A) a decrease in the wage rate.
- B) an increase in the wage rate.
- C) a decrease in the price of a substitute factor of production.
- D) an increase in the price of a substitute factor of production.
- E) an increase in the price of the firm's output.

Answer: C

Diff: 2 Type: MC

Topic: The Demand for a Factor of Production

30) The demand for a factor of production is

- A) a determined demand.
- B) a derived demand.
- C) a kinked demand.
- D) an insatiable demand.
- E) a desperate demand.

Answer: B

Diff: 1 Type: MC

Topic: The Demand for a Factor of Production

31) The idea that the demand for tire workers stems from the demand for automobiles is

- A) the value of the marginal product of labour.
- B) the value of the marginal product of tire workers.
- C) the value of the marginal product of auto workers.
- D) an output demand.
- E) a derived demand.

Answer: E

Diff: 1 Type: MC

Topic: The Demand for a Factor of Production

32) The demand for labour is a derived demand because it is derived from

- A) the demand for the output the labour produces.
- B) the supply of labour.
- C) union pressure.
- D) natural law.
- E) years of accumulated capital and technological advances.

Answer: A

Type: MC

33) The demand for the services of labour \_\_\_\_\_ a derived demand and the demand for the services of land \_\_\_\_\_ a derived demand.

- A) is not; is not
- B) is not; is
- C) is; is not
- D) is; is
- E) sometimes is and sometimes is not; sometimes is and sometimes is not

Answer: D

Type: MC

34) The value of marginal product is

- A) the value to the firm of hiring one more unit of a factor of production.
- B) the price of a unit of output multiplied by the marginal product of the factor of production.
- C) calculated as total revenue divided by the total quantity employed.
- D) Both A and B are correct.
- E) All of the above are correct.

Answer: B

Type: MC



35) A firm can sell its output for \$40 per unit. When it increases its labour force from 4 workers to 5 workers its output increases from 15 to 17 units. The value of marginal product of the 5th worker is

A) \$80.

B) \$40.

C) \$600.

D) \$680.

E) \$136.

Answer: A

Type: MC

### 18.3 Labour Markets

1) If the supply of labour decreases, which of the following events will occur?

- A) The wage rate will decrease and firms will increase the number of workers to the point at which the value of marginal product equals the new wage rate.
- B) The wage rate will decrease and firms will decrease the number of workers to the point at which the value of marginal product equals the new wage rate.
- C) The wage rate will increase and firms will decrease the number of workers to the point at which the value of marginal product equals the new wage rate.
- D) The wage rate will increase and firms will decrease the number of workers to the point at which the value of marginal product is greater than the new wage rate.
- E) The wage rate will increase and firms will decrease the number of workers to the point at which the value of marginal product is less than the new wage rate.

Answer: C

Diff: 2 Type: MC

Topic: Labour Markets

2) The reservation wage of labour is

- A) the wage below which the labourer will be willing to work.
- B) the wage above which the worker would be willing to retire.
- C) the wage rate at which the firm would find it profitable to hire labour.
- D) the wage rate that makes it necessary for the firm to shut down rather than pay this wage to labour.
- E) the wage rate above which the worker would be willing to supply labour to the market.

Answer: E

Diff: 1 Type: MC

Topic: Labour Markets

3) The substitution effect on labour supply refers to the degree to which

- A) the firm can substitute other factors of production for labour.
- B) buyers can substitute other products for the products that are made by organized labour.
- C) labour is willing to substitute nonlabour income for wages.
- D) labour prefers to substitute nonmonetary payments for money wages.
- E) labour is willing to substitute work for leisure.

Answer: E

Diff: 3 Type: MC

Topic: Labour Markets

- 4) The income effect on labour supply refers to
- A) the fact that at higher wages the worker earns more income.
  - B) the fact that as the wage rate increases and income increases, labourers demand more of all normal goods, including leisure activities.
  - C) the increase in the income of firms that is necessary to pay higher wages.
  - D) the fact that as workers become more productive, they earn more income.
  - E) the fact that as the wage rate increases and income increases, labourers demand more of all normal goods, including labour.

Answer: B

Diff: 3 Type: MC

Topic: Labour Markets

- 5) The labour supply curve may eventually become "backward bending" at high wages because
- A) the income effect of the higher wage is dominated by the substitution effect.
  - B) the income effect of the higher wage dominates the substitution effect of the higher wage.
  - C) firms will demand added productivity from the workers as the wage reaches very high levels.
  - D) firms will demand longer hours in trade for the higher wages.
  - E) people get tired of working so many hours and refuse to increase their labour supply.

Answer: B

Diff: 3 Type: MC

Topic: Labour Markets

- 6) If the wage rate increases, the *substitution* effect gives a household the incentive to
- A) raise its reservation wage.
  - B) increase leisure and decrease work.
  - C) increase work and decrease leisure.
  - D) increase both work and leisure.
  - E) decrease both work and leisure.

Answer: C

Diff: 3 Type: MC

Topic: Labour Markets

Source: Study Guide

- 7) If the wage rate decreases, the substitution effect gives a household the incentive to
- A) raise its reservation wage.
  - B) increase leisure and decrease work
  - C) increase work and decrease work.
  - D) increase both work and leisure.
  - E) decrease both work and leisure.

Answer: B

Diff: 3 Type: MC

Topic: Labour Markets

8) If the wage rate increases, the *income* effect gives a household the incentive to

- A) raise its reservation wage.
- B) increase leisure and decrease work.
- C) increase work and decrease leisure.
- D) increase both work and leisure.
- E) decrease both work and leisure.

Answer: B

Diff: 3 Type: MC

Topic: Labour Markets

Source: Study Guide

9) If the wage rate decreases, the income effect gives a household the incentive to

- A) raise its reservation wage.
- B) increase leisure and decrease work
- C) increase work and decrease leisure
- D) increase both work and leisure.
- E) decrease both work and leisure.

Answer: C

Diff: 3 Type: MC

Topic: Labour Markets

10) As the wage rate rises, a household will have a backward-bending supply of labour curve if

- A) the income effect reinforces the substitution effect.
- B) the wage rate rises above the reservation wage.
- C) the substitution effect dominates the income effect.
- D) the income effect dominates the substitution effect.
- E) leisure is an inferior good.

Answer: D

Diff: 3 Type: MC

Topic: Labour Markets

Source: Study Guide

11) If the desire for leisure increased, the wage rate would

- A) rise and employment would fall.
- B) rise and employment would rise.
- C) fall and employment would fall.
- D) fall and employment would rise.
- E) fall and employment would rise or fall.

Answer: A

Diff: 2 Type: MC

Topic: Labour Markets

Source: Study Guide

12) The income effect of a higher wage is defined as

- A) the increased income workers must be paid to be willing to work more.
- B) the increased prices of consumer goods that result from increased worker incomes.
- C) the increased demand for leisure that results from increased worker incomes.
- D) the increased workers' purchasing power that results from increased worker incomes.
- E) all of the above.

Answer: C

Diff: 3 Type: MC

Topic: Labour Markets

13) Complete the following sentence. A labour union is

- A) an illegal conspiracy of workers formed to strike against employers.
- B) a legal organization of workers with a goal to overthrow the capitalist class.
- C) an organized group of workers that attempts to increase wages and influence other job conditions.
- D) an organized group of crime syndicates.
- E) a union with members working in the same industry, but in different jobs.

Answer: C

Diff: 1 Type: MC

Topic: Labour Markets

14) A union is formed to restrict labour supply in a previously perfectly competitive labour market. If the union succeeds in raising the wage,

- A) employment will fall.
- B) employment will rise.
- C) employment will not change.
- D) the total wage bill will rise.
- E) the total wage bill will fall.

Answer: A

Diff: 2 Type: MC

Topic: Labour Markets

Source: Study Guide

15) For a monopsonist facing an upward-sloping supply curve of labour, the marginal cost of labour curve

- A) intersects the value of marginal product curve of labour at the equilibrium wage rate.
- B) is below and parallel to the supply of labour curve.
- C) is identical to the supply of labour curve.
- D) is above and parallel to the supply of labour curve.
- E) is above the supply curve of labour.

Answer: E

Diff: 3 Type: MC

Topic: Labour Markets

16) Unions try to raise the demand for their labour by

- A) raising wages.
- B) encouraging imports.
- C) supporting less restrictive immigration laws.
- D) sponsoring training for union members.
- E) lobbying against minimum wage laws.

Answer: D

Diff: 2 Type: MC

Topic: Labour Markets

17) A constraint on union effectiveness is

- A) the downward-sloping labour demand curve.
- B) the minimum wage law.
- C) the Fair Labour Standards Practices Act.
- D) increasing export competitiveness.
- E) the competition of other unions.

Answer: A

Diff: 2 Type: MC

Topic: Labour Markets

18) To increase the demand for union labour, unions do all of the following *except* support

- A) increases in the minimum wage.
- B) increases in import restrictions.
- C) immigration restrictions.
- D) an increase in the supply of foreign workers.
- E) training schemes and apprenticeship programs.

Answer: D

Diff: 2 Type: MC

Topic: Labour Markets

19) Which of the following would unions be *least* likely to support?

- A) an increase in the minimum wage
- B) immigration restrictions
- C) increasing the value of marginal product of their workers
- D) increasing demand for the goods their workers produce
- E) reducing barriers to imports

Answer: E

Diff: 2 Type: MC

Topic: Labour Markets

Source: Study Guide

- 20) Unions try to raise minimum wages because
- A) they wish to encourage employment among the poor.
  - B) they wish to help those on minimum wages.
  - C) this will decrease the supply of labour in their industry.
  - D) this will increase the demand for labour in their industry.
  - E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: Labour Markets

- 21) When compared to a monopsony labour market with the same value of marginal product curve and labour supply curve, a perfectly competitive labour market will pay a
- A) lower wage and employ fewer workers.
  - B) lower wage and employ more workers.
  - C) higher wage and employ fewer workers.
  - D) higher wage and employ more workers.
  - E) higher wage and employ the same amount of workers.

Answer: D

Diff: 3 Type: MC

Topic: Labour Markets

- 22) A monopsony exists when there is
- A) a single buyer in a market.
  - B) a single seller in a market.
  - C) a small number of large buyers in a market.
  - D) a small number of large sellers in a market.
  - E) an agreement amongst sellers in a market to set prices.

Answer: A

Diff: 1 Type: MC

Topic: Labour Markets

- 23) If a strike or lockout occurs in a bilateral monopoly situation, it is usually because
- A) the demand for labour is relatively inelastic.
  - B) the demand for labour is relatively elastic.
  - C) the supply of labour is relatively inelastic.
  - D) the supply of labour is relatively elastic.
  - E) one party has misjudged the costs each party can inflict on the other.

Answer: E

Diff: 2 Type: MC

Topic: Labour Markets

Source: Study Guide

24) Which one of the following would unions be most likely to support?

- A) increased barriers to imports
- B) eased immigration restrictions
- C) a decrease in the minimum wage
- D) decreasing demand for the goods their workers produce
- E) decreasing the marginal product of its workers

Answer: A

Diff: 2 Type: MC

Topic: Labour Markets

Use the figure below to answer the following questions.

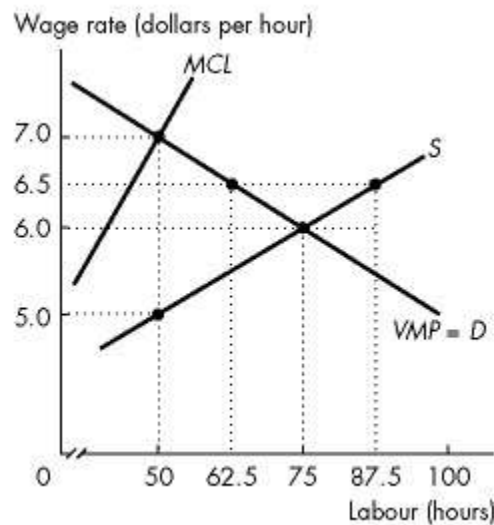


Figure 18.3.1

25) Refer to Figure 18.3.1. This figure shows the value of marginal product of labour curve, the labour supply curve, and the marginal cost of labour curve. If this labour market is competitive, the wage rate is

- A) \$3 an hour.
- B) \$5 an hour.
- C) \$6 an hour.
- D) \$7 an hour.
- E) greater than \$7 an hour.

Answer: C

Diff: 2 Type: MC

Topic: Labour Markets

26) Refer to Figure 18.3.1. This figure shows the value of marginal product of labour curve, the labour supply curve, and the marginal cost of labour curve. If this labour market is competitive, the quantity of labour employed is

- A) zero hours.
- B) 50 hours.
- C) 75 hours.
- D) 100 hours.
- E) greater than 100 hours.

Answer: C

Diff: 2 Type: MC

Topic: Labour Markets

27) Refer to Figure 18.3.1. This figure shows the value of marginal product of labour curve, the labour supply curve, and the marginal cost of labour curve. If this labour market is controlled by a monopsony, the wage rate is

- A) \$7 an hour.
- B) \$6 an hour.
- C) \$3 an hour.
- D) \$5 an hour.
- E) zero, because the market would shut down.

Answer: D

Diff: 3 Type: MC

Topic: Labour Markets

28) Refer to Figure 18.3.1. This figure shows the value of marginal product of labour curve, the labour supply curve, and the marginal cost of labour curve. If this labour market is controlled by a monopsony, then the monopsonist hires

- A) zero hours.
- B) 50 hours.
- C) 75 hours.
- D) 100 hours.
- E) greater than 100 hours.

Answer: B

Diff: 3 Type: MC

Topic: Labour Markets

29) Refer to Figure 18.3.1. This figure shows the value of marginal product of labour curve, the labour supply curve, and the marginal cost of labour curve. If a union and the monopsonist in Figure 18.3.1 are equally strong, the outcome will be an hourly wage

- A) of \$7.
- B) between \$5 and \$6.
- C) between \$5 and \$7.
- D) between \$6 and \$7.
- E) of \$6

Answer: C

Diff: 3 Type: MC

Topic: Labour Markets



30) Refer to Figure 18.3.1. This figure shows the value of marginal product of labour curve, the labour supply curve, and the marginal cost of labour curve. Suppose the government passes a minimum wage law that prohibits anyone from hiring labour at less than \$6.50 per hour. The new marginal cost of labour (*MCL*) for the monopsonist

- A) is not affected.
- B) equals \$6.50 only from zero to 50 hours of labour.
- C) equals \$6.50 only from zero to 75 hours of labour.
- D) equals \$6.50 only from zero to 100 hours of labour.
- E) none of the above.

Answer: E

Diff: 3 Type: MC

Topic: Labour Markets

31) Refer to Figure 18.3.1. This figure shows the value of marginal product of labour curve, the labour supply curve, and the marginal cost of labour curve. Suppose the government passes a minimum wage law that prohibits anyone from hiring labour at less than \$6.50 per hour. The monopsonist will hire

- A) 50 hours of labour.
- B) 75 hours of labour.
- C) 62.5 hours of labour.
- D) 100 hours of labour.
- E) 125 hours of labour.

Answer: C

Diff: 3 Type: MC

Topic: Labour Markets

32) Refer to Figure 18.3.1. This figure shows the value of marginal product of labour curve, the labour supply curve, and the marginal cost of labour curve. If this labour market is controlled by a monopsony, then the monopsonist

- A) pays a wage rate that is greater than the value of marginal product of labour.
- B) pays a wage rate exactly equal to the value of marginal product of labour.
- C) pays a wage rate that is less than the value of marginal product of labour.
- D) employs more labour hours per week than in a competitive labour market.
- E) pays a wage equal to the marginal cost of labour.

Answer: C

Diff: 3 Type: MC

Topic: Labour Markets

Use the figure below to answer the following questions.

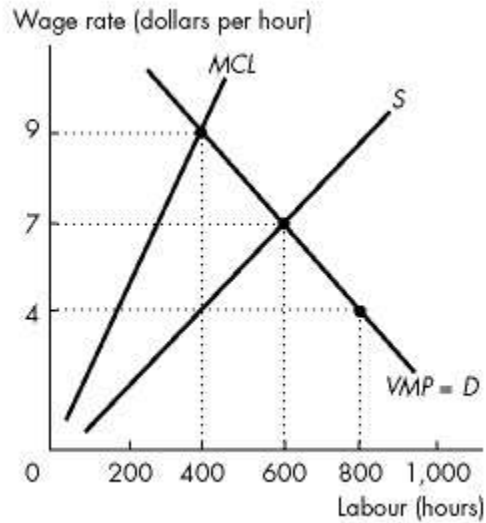


Figure 18.3.2

33) Refer to Figure 18.3.2. This figure illustrates a monopsonist in the labour market. The profit-maximizing wage rate is \_\_\_\_\_ and the quantity of labour hired is \_\_\_\_\_.

- A) \$4 per hour; 800 hours
- B) \$4 per hour; 400 hours
- C) \$7 per hour; 600 hours
- D) \$9 per hour; 400 hours
- E) none of the above.

Answer: B

Diff: 3 Type: MC

Topic: Labour Markets

Source: Study Guide

34) Refer to Figure 18.3.2. If the labour market illustrated in this figure becomes competitive, the equilibrium wage rate is \_\_\_\_\_ and the quantity of labour hired is \_\_\_\_\_.

- A) \$4 per hour; 800 hours
- B) \$4 per hour; 400 hours
- C) \$7 per hour; 600 hours
- D) \$9 per hour; 400 hours
- E) none of the above.

Answer: C

Diff: 2 Type: MC

Topic: Labour Markets

Source: Study Guide

35) Refer to Figure 18.3.2. Suppose this industry is initially in a monopsony situation and then the government introduces a minimum wage of \$8 per hour. Choose the correct statement.

- A) The wage rate rises, but employment decreases.
- B) The wage rate rises, but employment stays the same.
- C) The wage rate rises to \$8 per hour, and employment increases to 800 hours.
- D) The wage rate rises to \$8 per hour, and employment increases to 600 hours.
- E) The wage rate rises to \$8 per hour, and employment increases to 500 hours.

Answer: E

Diff: 3 Type: MC

Topic: Labour Markets

36) If a union forms to face the monopsonist in Figure 18.3.2, the situation is one of

- A) binding arbitration.
- B) derived demand.
- C) duopoly.
- D) collusive oligopoly.
- E) bilateral monopoly.

Answer: E

Diff: 2 Type: MC

Topic: Labour Markets

Source: Study Guide

37) If a union and the monopsonist in Figure 18.3.2 agree to bargaining, the outcome is an hourly wage rate

- A) of \$7.
- B) between \$4 and \$7.
- C) between \$4 and \$9.
- D) between \$7 and \$9.
- E) of \$9.

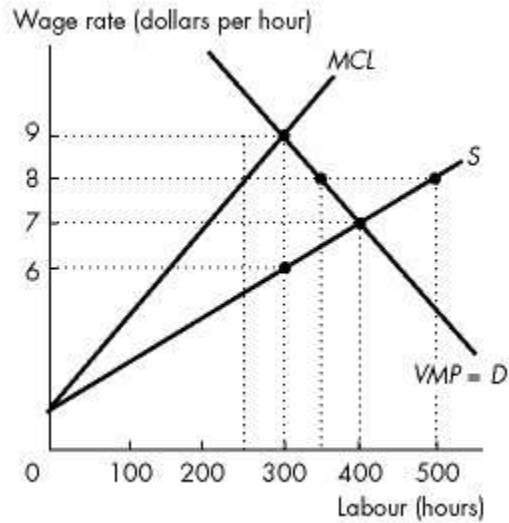
Answer: C

Diff: 3 Type: MC

Topic: Labour Markets

Source: Study Guide

Use the figure below to answer the following questions.



**Figure 18.3.3**

38) Refer to Figure 18.3.3. For the monopsonist employer illustrated in this figure, the profit-maximizing wage rate is \_\_\_\_\_ and the quantity of labour hired is \_\_\_\_\_.

- A) \$9 per hour; 300 hours
- B) \$8 per hour; 350 hours
- C) \$8 per hour; 500 hours
- D) \$7 per hour; 400 hours
- E) \$6 per hour; 300 hours

Answer: E

Diff: 3 Type: MC

Topic: Labour Markets

Source: Study Guide

39) Refer to Figure 18.3.3. Suppose the government passes a minimum wage law that prohibits anyone from hiring labour at less than \$8 per hour. The monopsonist will hire

- A) 250 hours of labour.
- B) 300 hours of labour.
- C) 350 hours of labour.
- D) 400 hours of labour.
- E) 450 hours of labour.

Answer: C

Diff: 3 Type: MC

Topic: Labour Markets

40) During the past year, Teddy had a part-time job at which he is willing to work 30 hours each week. During Teddy's annual review, his boss grants him an 8 percent increase in his wage. As a result of the wage increase, Teddy is now willing to work 25 hours each week. Teddy's opportunity cost of \_\_\_\_\_ has risen and for Teddy the substitution effect of the wage hike is \_\_\_\_\_ the income effect.

- A) leisure; less than
- B) leisure; more than
- C) labour; less than
- D) labour; more than
- E) leisure; equal to

Answer: A

Type: MC

Use the table below to answer the following questions.

Wage rate (dollars per hour)	Quantity of labour supplied (hours per day)	Quantity of labour demanded (hours per day)
5	200	600
10	300	500
15	400	400
20	500	300
25	600	200

Table 18.3.1

41) Refer to Table 18.3.1. Table 18.3.1 gives information about the labour market in Lantis, a community in which the labour market is perfectly competitive. The equilibrium wage rate is \_\_\_\_\_ an hour and the quantity of labour employed is \_\_\_\_\_ hours per day.

- A) \$25; 600
- B) \$25; 200
- C) \$15; 400
- D) \$5; 200
- E) \$5; 600

Answer: C

Type: MC

42) Refer to Table 18.3.1. Table 18.3.1 gives information about the labour market in Lantis, a community in which the labour market is perfectly competitive. If the price of the good that Lantis produces increases and the value of marginal product of labour changes by \$10 an hour, the equilibrium wage rate \_\_\_\_\_ an hour and the quantity of labour employed \_\_\_\_\_.

- A) rises to \$17.50; increases to 450 hours
- B) rises to \$10; increases to 600
- C) rises to \$20; increases to 500 hours
- D) remains at \$15; decreases to 300 hours
- E) rises to \$20; decreases to 300 hours

Answer: C

Type: MC

## 18.4 Capital and Natural Resource Markets

- 1) If the value of marginal product of capital decreases as more capital is employed, then the
- A) supply curve of capital is upward sloping.
  - B) supply curve of capital is downward sloping.
  - C) demand curve for capital is horizontal.
  - D) demand curve for capital is downward sloping.
  - E) demand curve for capital is upward sloping.

Answer: D

Diff: 2 Type: MC

Topic: Capital and Natural Resource Markets

- 2) If the market for a nonrenewable natural resource is currently in equilibrium, the price of the resource

- A) is equal to the value of marginal product of the resource.
- B) is expected to rise at a rate equal to the interest rate.
- C) is expected to fall at a rate equal to the interest rate.
- D) will actually rise at a rate equal to the interest rate.
- E) will actually fall at a rate equal to the interest rate.

Answer: B

Diff: 2 Type: MC

Topic: Capital and Natural Resource Markets

Source: Study Guide

- 3) Equilibrium occurs in the market for oil when the

- A) price of the oil equals the interest rate.
- B) increase in the price of oil equals the expected increase in the interest rate.
- C) expected increase in the price of oil over time is equal to the interest rate.
- D) stock of oil is eventually depleted.
- E) price of oil today equals the expected future price.

Answer: C

Diff: 3 Type: MC

Topic: Capital and Natural Resource Markets

- 4) The Hotelling Principle states that

- A) hotels will tend to be built next to major highways.
- B) equilibrium in natural resource markets occurs when the expected increase in the price of the resource over time is equal to the interest rate.
- C) the resource will be depleted at a rate equal to the rate of interest.
- D) natural resources should be depleted only for the production of goods that would help maintain environmental quality.
- E) we should conserve nonrenewable natural resources.

Answer: B

Diff: 3 Type: MC

Topic: Capital and Natural Resource Markets

5) Which of the following is a nonrenewable natural resource?

- A) coal
- B) land
- C) water
- D) trees
- E) rain

Answer: A

Diff: 1 Type: MC

Topic: Capital and Natural Resource Markets

Source: Study Guide

6) In the short run, the market supply of land is

- A) relatively elastic.
- B) relatively inelastic.
- C) perfectly elastic.
- D) perfectly inelastic.
- E) either elastic or inelastic depending on the productivity of the land.

Answer: D

Diff: 2 Type: MC

Topic: Capital and Natural Resource Markets

7) The demand for capital is determined by \_\_\_\_\_. The demand for land is determined by \_\_\_\_\_. The supply of \_\_\_\_\_ is perfectly \_\_\_\_\_.

- A) how much capital is renewable and how much is nonrenewable; how much land is renewable and how much is nonrenewable; land; elastic
- B) the value of marginal product of capital; the value of marginal product of land; land; inelastic
- C) how much capital is renewable and how much is nonrenewable; how much land is renewable and how much is nonrenewable; capital; elastic
- D) the value of marginal product of capital; the value of marginal product of land; capital; inelastic
- E) the value of marginal product of capital; the value of marginal product of land; land; elastic

Answer: B

Type: MC

Topic: Capital and Natural Resource Markets

Source: MyEconLab

8) The supply of a nonrenewable natural resource is determined by all of the following factors *except*

- A) the value of marginal product.
- B) the known reserves of the natural resource.
- C) the scale of current production facilities.
- D) the expected future price.
- E) all of the above determine supply of a nonrenewable resource.

Answer: A

Type: MC

Topic: Capital and Natural Resource Markets

Source: MyEconLab

9) The Hotelling Principle is the idea that the price of a \_\_\_\_\_ is expected to rise at a rate equal to the \_\_\_\_\_.

- A) nonrenewable natural resource; inflation rate
- B) unit of capital; interest rate
- C) nonrenewable natural resource; interest rate
- D) unit of capital; inflation rate
- E) nonrenewable natural resource; percentage increase in demand

Answer: C

Type: MC

Topic: Capital and Natural Resource Markets

Source: MyEconLab

10) If the price of a natural resource is expected to rise at a rate that exceeds the interest rate, demand \_\_\_\_\_, supply \_\_\_\_\_, and the price \_\_\_\_\_.

- A) decreases; increases; falls
- B) increases; decreases; rises
- C) increases; increases; rises, falls, or remains unchanged
- D) decreases; decreases; rises, falls, or remains unchanged
- E) increases; does not change; rises

Answer: B

Type: MC

Topic: Capital and Natural Resource Markets

Source: MyEconLab

11) The Internet is \_\_\_\_\_ natural resource. Power generated by wind turbines is \_\_\_\_\_ natural resource.

- A) not a; a nonrenewable
- B) a renewable; a renewable
- C) a renewable; a nonrenewable
- D) not a; a renewable
- E) not a; not a

Answer: D

Type: MC

Topic: Capital and Natural Resource Markets

Source: MyEconLab

12) Coal in an Alberta coal mine is \_\_\_\_\_ natural resource. Algonquin Park is \_\_\_\_\_ natural resource.

- A) a nonrenewable; a nonrenewable
- B) a renewable; a renewable
- C) a nonrenewable; a renewable
- D) a renewable; a nonrenewable
- E) a nonrenewable; not a

Answer: C

Type: MC

Topic: Capital and Natural Resource Markets  
Source: MyEconLab

13) All of the following statements are correct *except*

- A) the supply of capital is derived from the value of marginal product of capital.
- B) the lower the rental rate of capital, other things remaining the same, the greater is the quantity of capital demanded.
- C) the higher the rental rate, other things remaining the same, the greater is the quantity of capital supplied.
- D) profit-maximizing firms hire the quantity of capital services that makes the value of marginal product of capital equal to the rental rate of capital.
- E) if the present value of the future rental payments of an item of capital equipment is less than the cost of buying the capital, the firm will rent or lease the equipment.

Answer: A

Type: MC

Topic: Capital and Natural Resource Markets  
Source: MyEconLab

14) Choose the correct statement.

- A) The quantity of land demanded cannot be changed by people's decisions.
- B) The supply of each particular block of land is perfectly inelastic.
- C) The lower the rental rate, other things remaining the same, the smaller is the quantity of land demanded.
- D) Profit-maximizing firms rent the quantity of land at which the value of marginal product of land is equal to the quantity of land demanded.
- E) None of the above statements are correct.

Answer: B

Type: MC

Topic: Capital and Natural Resource Markets  
Source: MyEconLab

15) The value of marginal product of oil is the \_\_\_\_\_ influence on demand. The greater the quantity of oil used, the \_\_\_\_\_ is the value of marginal product of oil.

- A) speculative; greater
- B) fundamental; greater
- C) fundamental; smaller
- D) speculative; smaller
- E) none of the above

Answer: C

Type: MC

Topic: Capital and Natural Resource Markets  
Source: MyEconLab

16) All of the following statements are correct *except*

A) if the price of oil is expected to rise at a rate equal to the interest rate, demand increases and supply increases.

B) the interest rate is the opportunity cost of holding an oil inventory.

C) if the price of oil is expected to rise at a rate that exceeds the interest rate, demand increases and supply decreases.

D) according to the Hotelling Principle, the price of a nonrenewable natural resource is expected to rise at a rate equal to the interest rate.

E) the marginal cost of extraction of oil is the fundamental determinant of supply.

Answer: A

Type: MC

Topic: Capital and Natural Resource Markets

Source: MyEconLab

## 18.5 Mathematical Note: Present Value and Discounting

1) Suppose the interest rate is 5 percent per year. What is the present value of the \$210 that will be received two years from today?

- A) \$210
- B) \$190.48
- C) \$231.53
- D) \$200
- E) \$42

Answer: B

Diff: 2 Type: MC

Topic: Mathematical Note: Present Value and Discounting

2) The present value of the \$50 that will be received next year is \$40. What is the interest rate?

- A) 10 percent
- B) 8 percent
- C) 20 percent
- D) 50 percent
- E) 25 percent

Answer: E

Diff: 2 Type: MC

Topic: Mathematical Note: Present Value and Discounting

3) What will be the value in one year of \$25 invested today at an annual interest rate of 5 percent?

- A) \$25
- B) \$26.25
- C) \$27.50
- D) \$30
- E) \$23.81

Answer: B

Diff: 2 Type: MC

Topic: Mathematical Note: Present Value and Discounting

4) The \_\_\_\_\_ of a future amount of money is the amount that, if invested today, will grow to be as large as that future amount when the interest it earns is taken into account.

- A) current value
- B) future value
- C) present value
- D) market value
- E) profit value

Answer: C

Diff: 1 Type: MC

Topic: Mathematical Note: Present Value and Discounting

5) What is the most an investor would be willing to pay for a stock that will pay \$210 next year and nothing before or after?

- A) \$200 regardless of the interest rate.
- B) \$200 if the interest rate is 5 percent per year.
- C) \$190.91 if the interest rate is 10 percent per year.
- D) B and C.
- E) None of the above.

Answer: D

Diff: 2 Type: MC

Topic: Mathematical Note: Present Value and Discounting

6) The present value of a future payment of money will be higher the

- A) higher the interest rate or the further in the future the payment.
- B) lower the interest rate or the further in the future the payment.
- C) higher the interest rate or the nearer the date of the future payment.
- D) lower the interest rate or the nearer the date of the future payment.
- E) lower the interest rate, independent of the date of the future payment.

Answer: D

Diff: 2 Type: MC

Topic: Mathematical Note: Present Value and Discounting

7) The present value of a future payment of money will be lower the

- A) higher the interest rate or the further in the future the payment.
- B) lower the interest rate or the further in the future the payment.
- C) higher the interest rate or the nearer the date of the future payment.
- D) lower the interest rate or the nearer the date of the future payment.
- E) lower the interest rate, independent of the date of the future payment.

Answer: A

Diff: 2 Type: MC

Topic: Mathematical Note: Present Value and Discounting

8) If the annual rate of interest is 10 percent per year, what is the present value of \$100 received one year from now?

- A) \$90.00
- B) \$90.91
- C) \$95.45
- D) \$100.00
- E) \$110.00

Answer: B

Diff: 2 Type: MC

Topic: Mathematical Note: Present Value and Discounting

9) If the interest rate is 10 percent per year, the present value of \$100 in *two* years is

- A) \$80.00.
- B) \$82.64.
- C) \$90.91.
- D) \$120.00.
- E) \$121.00.

Answer: B

Diff: 2 Type: MC

Topic: Mathematical Note: Present Value and Discounting

10) If the present value of \$500 to be received in one year is \$463, the interest rate is

- A) 5 percent per year.
- B) 8 percent per year.
- C) 10 percent per year.
- D) 20.8 percent per year.
- E) 37 percent per year.

Answer: B

Diff: 2 Type: MC

Topic: Mathematical Note: Present Value and Discounting

11) If the rate of interest is 15 percent per year, the present value of the \$200 to be received in two years is

- A) \$170.00.
- B) \$185.00.
- C) \$173.91.
- D) \$264.50.
- E) \$151.23.

Answer: E

Diff: 2 Type: MC

Topic: Mathematical Note: Present Value and Discounting

12) If the present value of the \$1,000 to be received in one year is \$800, the interest rate is

- A) 25 percent per year.
- B) 8 percent per year.
- C) 10 percent per year.
- D) 12 percent per year.
- E) 125 percent per year.

Answer: A

Diff: 2 Type: MC

Topic: Mathematical Note: Present Value and Discounting

13) If the present value of \$100 received one year from now is \$80, what is the annual interest rate?

- A) 8 percent
- B) 10 percent
- C) 20 percent
- D) 25 percent
- E) 50 percent

Answer: D

Diff: 2 Type: MC

Topic: Mathematical Note: Present Value and Discounting

14) The present value of a future sum of money is the amount that, if invested today, will grow

- A) as large as that future sum, given the interest rate.
- B) as large as that future sum.
- C) as large as that future sum, less taxes payable.
- D) as large as that future sum, if the rate of interest is zero.
- E) at a constant rate forever.

Answer: A

Diff: 2 Type: MC

Topic: Mathematical Note: Present Value and Discounting

15) Assuming  $r$  is the rate of interest, to compute the present value of a dollar to be received a year from today, you

- A) multiply the dollar by  $r$ .
- B) divide the dollar by  $(1 - r)$ .
- C) multiply the dollar by  $(1 + r)$ .
- D) divide the dollar by  $r$ .
- E) divide the dollar by  $(1 + r)$ .

Answer: E

Diff: 2 Type: MC

Topic: Mathematical Note: Present Value and Discounting

Use the information below to answer the following questions.

### Fact 18.5.1

The Burning Belly Taco Stand is considering buying some new special ovens. Each oven will cost \$1,000, and will last for 2 years before it wears out. The ovens will be used to make the Taco Stands famous "Burning Ring of Fire" tacos, and will generate a value of marginal product of \$600 for the first oven, \$570 for the second oven, and \$530 for the third oven. (Assume all revenues are earned at the end of the year.)

16) Refer to Fact 18.5.1. If the rate of interest is 5 percent, how many ovens will the Burning Belly Taco Stand buy?

- A) zero
- B) 1
- C) 2
- D) 3
- E) insufficient information to answer

Answer: C

Diff: 3 Type: MC

Topic: Mathematical Note: Present Value and Discounting

17) Consider Fact 18.5.1. If the rate of interest is 10 percent, how many ovens will the Burning Belly Taco Stand buy?

- A) zero
- B) 1
- C) 2
- D) 3
- E) insufficient information to answer

Answer: B

Diff: 3 Type: MC

Topic: Mathematical Note: Present Value and Discounting

## Chapter 19 Economic Inequality

### 19.1 Measuring Economic Inequality

1) Which of the following does Statistics Canada use to provide measures of economic inequality?

- A) market income only
- B) market income and after-tax income only
- C) after-tax income only
- D) total market and after-tax income only
- E) market income, total income, and after-tax income

Answer: E

Diff: 1 Type: MC

Topic: Measuring Economic Inequality

2) Market income equals

- A) the wages, interest, rent, and profit earned in factor markets after paying income taxes.
- B) the wages, interest, and profit earned in factor markets before paying income taxes.
- C) the wages, interest, and rent earned in factor markets before paying income taxes.
- D) the wages, interest, rent, and profit earned in factor markets before paying income taxes.
- E) the wages, rent, and profit earned in factor markets before paying income taxes.

Answer: D

Diff: 1 Type: MC

Topic: Measuring Economic Inequality

3) Total income equals

- A) market income minus payments to firms by governments.
- B) market income plus cash payments to households by governments.
- C) the wages, interest, rent, and profit earned in factor markets before paying income taxes.
- D) the wages, interest, rent, and profit earned in factor markets after paying income taxes.
- E) market income minus cash payments to households by governments.

Answer: B

Diff: 1 Type: MC

Topic: Measuring Economic Inequality

4) After-tax income equals

- A) total income minus tax payments by households to governments.
- B) total income minus tax payments by households to firms.
- C) total income plus tax payments by households to governments.
- D) market income plus cash payments to households by governments.
- E) market income minus tax payments by households to governments.

Answer: A

Diff: 1 Type: MC

Topic: Measuring Economic Inequality

5) In 2009, the poorest 20 percent of households received what percentage of the nation's after-tax income?

- A) 10.6 percent
- B) 4.9 percent
- C) 24.0 percent
- D) 16.3 percent
- E) 17.4 percent

Answer: B

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

6) In 2009, the median household income in Canada was

- A) \$5,000.
- B) \$25,000.
- C) \$48,300.
- D) \$59,700.
- E) \$65,000.

Answer: C

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

7) In 2009, the mean household income in Canada was

- A) \$59,700.
- B) \$39,700.
- C) \$25,000.
- D) \$48,300.
- E) \$65,000.

Answer: A

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

8) In 2009, what percentage of households received the mode income in Canada?

- A) 5 percent
- B) 10 percent
- C) 7 percent
- D) 17.4 percent
- E) 20 percent

Answer: C

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

9) In 2009, the mode income received by 7.0 percent of households in Canada was between

- A) \$18,500 and \$21,999.
- B) \$15,000 and \$19,999.
- C) \$30,000 and \$34,999.
- D) \$16,000 and \$22,500.
- E) \$18,000 and \$24,999.

Answer: B

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

10) In 2009, the 20 percent of households with the highest incomes received what percentage of the total after-tax income?

- A) 14 percent
- B) 2 percent
- C) 71 percent
- D) 44.2 percent
- E) 55.8 percent

Answer: D

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

11) An income Lorenz curve

- A) graphs the cumulative percentage of income against the cumulative percentage of households.
- B) measures the income among households ranked from the poorest to the richest.
- C) measures the income among households ranked from the richest to the poorest.
- D) measures the factor prices earned by the rich compared with the poor.
- E) is a downward-sloping curve.

Answer: A

Diff: 1 Type: MC

Topic: Measuring Economic Inequality

12) If each household made the same amount of income, then the Lorenz curve would be

- A) not defined, because it measures income inequality not income equality.
- B) the line of poverty.
- C) the line of equality.
- D) a right angle.
- E) horizontal.

Answer: C

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

13) In 2009, the middle 20 percent of households received what percentage of total Canadian after-tax income?

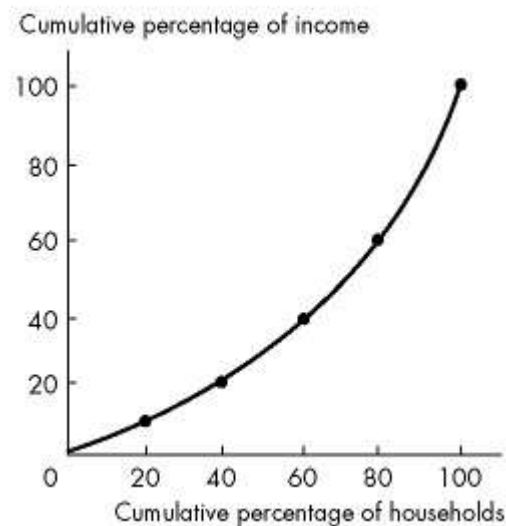
- A) 10.6 percent
- B) 16.3 percent
- C) 25 percent
- D) 43 percent
- E) 52 percent

Answer: B

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

Use the figure below to answer the following questions.



**Figure 19.1.1**

14) Refer to Figure 19.11. The poorest 20 percent of households receive what share of total income?

- A) 40 percent
- B) 60 percent
- C) 20 percent
- D) 5 percent
- E) 10 percent

Answer: E

Diff: 1 Type: MC

Topic: Measuring Economic Inequality

15) Refer to Figure 19.11. The richest 20 percent of households receive what share of total income?

- A) 10 percent
- B) 30 percent
- C) 40 percent
- D) 60 percent
- E) 100 percent

Answer: C

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

16) Refer to Figure 19.11. The middle 20 percent of households receive what share of total income?

- A) 20 percent
- B) 25 percent
- C) 35 percent
- D) 15 percent
- E) 60 percent

Answer: A

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

17) A Lorenz curve illustrates the distribution of income by graphing the

- A) cumulative percentage of income received and the cumulative percentage of households.
- B) chance of a family earning a specific income.
- C) wealth earned by a cumulative percentage of households.
- D) cumulative frequency of specific incomes.
- E) percentage change in income for a percentage change in population.

Answer: A

Diff: 1 Type: MC

Topic: Measuring Economic Inequality

18) The larger the gap between the Lorenz curve and the line of equality,

- A) the greater is the equality in the income distribution.
- B) the less is the inequality in the income distribution.
- C) the poorer are the top 50 percent of households.
- D) the richer are the lowest 50 percent of households.
- E) the greater is the inequality in the income distribution.

Answer: E

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

- 19) The closer the Lorenz curve is to the line of equality,  
A) the more equal is the distribution.  
B) the less equal is the distribution.  
C) the more unfair is the income distribution.  
D) the richer are the highest 5 percent of households.  
E) the poorer are the highest 5 percent of households.

Answer: A

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

- 20) Household characteristics that stand out when determining the incidence of poverty include all of the following except  
A) household type.  
B) education.  
C) age of householder.  
D) ethnic background.  
E) number of children.

Answer: D

Diff: 1 Type: MC

Topic: Measuring Economic Inequality

- 21) Poverty is  
A) an income below the national average income level.  
B) an income below the national median income level.  
C) a state in which a family's income is too low to be able to buy the quantities of food, shelter, and clothing that are deemed necessary.  
D) the income earned by the poorest 20 percent of households.  
E) a state in which a family spends more than 50 percent of its income on food, shelter, and clothing.

Answer: C

Diff: 1 Type: MC

Topic: Measuring Economic Inequality

- 22) The low-income cutoff level is  
A) a level of housing and food provided by the government.  
B) a fixed real income used to determine whether or not a household may qualify for welfare.  
C) the income level below which a family normally spends 73.6 percent or more of its income on food, shelter, and clothing.  
D) the income level below which a family normally spends 63.6 percent or more of its income on food, shelter, and clothing.  
E) a level of income below which starvation occurs.

Answer: D

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

23) From an examination of data on income and wealth, it can be concluded that

- A) wealth distribution is more equal than income distribution.
- B) income distribution is more equal than wealth distribution.
- C) wealth distribution is equal to income distribution.
- D) income and wealth are the same.
- E) income and wealth are unrelated.

Answer: B

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

24) The inequality in the distribution of wealth is

- A) less than the inequality in the distribution of income.
- B) decreased by the existence of assortative mating.
- C) a better measure of the inequality in the distribution of economic resources than is the inequality in the distribution of income.
- D) shown by a Lorenz curve that is farther away from the line of equality than the Lorenz curve for income.
- E) all of the above.

Answer: D

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

25) The wealthiest 10 percent of Canadian families own approximately

- A) 10 percent of the wealth.
- B) 17 percent of the wealth.
- C) 56 percent of the wealth.
- D) 67 percent of the wealth.
- E) 80 percent of the wealth.

Answer: C

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

26) Which diagram is used by economists to illustrate the distribution of income or wealth?

- A) Lorenz curve
- B) normal bell-shaped distribution
- C) wage differential curve
- D) low-income cut-off curve
- E) marginal revenue product diagram

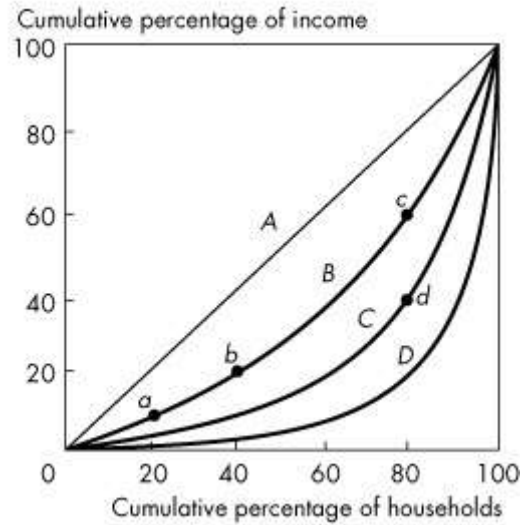
Answer: A

Diff: 1 Type: MC

Topic: Measuring Economic Inequality

Source: Study Guide

Use the figure below to answer the following questions.



**Figure 19.1.2**

27) Consider the Lorenz curves in Figure 19.1.2. Which Lorenz curve corresponds to the greatest income inequality?

- A) A
- B) B
- C) C
- D) D
- E) impossible to tell without additional information

Answer: D

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

Source: Study Guide

28) Refer to Figure 19.1.2. What is curve A called?

- A) market distribution line
- B) line of equality
- C) fairness line
- D) low-income cut-off line
- E) none of the above

Answer: B

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

Source: Study Guide

29) Consider the Lorenz curves in Figure 19.1.2. Which point indicates that the richest 20 percent of families earn 60 percent of the income?

- A) *a*
- B) *b*
- C) *c*
- D) *d*
- E) none of the above

Answer: D

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

30) Consider the Lorenz curves in Figure 19.1.2. Which point indicates that the richest 20 percent of families earn 80 percent of the income?

- A) *a*
- B) *b*
- C) *c*
- D) *d*
- E) none of the above

Answer: E

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

31) Consider the Lorenz curves in Figure 19.1.2. Which point indicates that the poorest 20 percent of families earn 9 percent of the income?

- A) *a*
- B) *b*
- C) *c*
- D) *d*
- E) none of the above

Answer: A

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

32) Which point in Figure 19.1.2 indicates that the richest 20 percent of families earn 40 percent of the income?

- A) *a*
- B) *b*
- C) *c*
- D) *d*
- E) none of the above

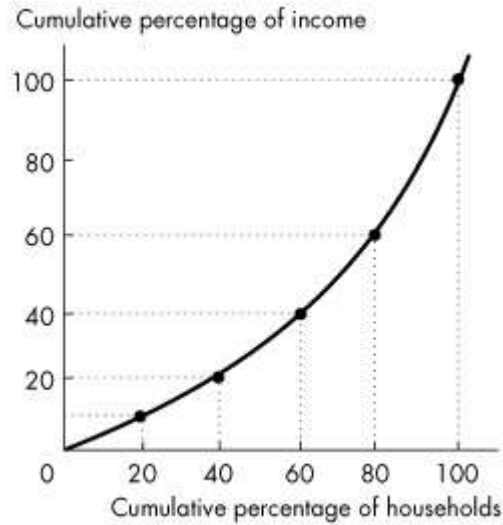
Answer: C

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

Source: Study Guide

Use the figure below to answer the following questions.



**Figure 19.1.3**

33) In Figure 19.1.3, the richest 20 percent of all families receive what share of all income?

- A) 10 percent
- B) 20 percent
- C) 30 percent
- D) 40 percent
- E) none of the above

Answer: D

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

Source: Study Guide

34) In Figure 19.1.3, the poorest 20 percent of all families receive what share of income?

- A) 10 percent
- B) 20 percent
- C) 30 percent
- D) 40 percent
- E) none of the above

Answer: A

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

Source: Study Guide

35) In Figure 19.1.3, the middle 20 percent of all families receive what share of income?

- A) 10 percent
- B) 20 percent
- C) 30 percent
- D) 40 percent
- E) none of the above

Answer: B

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

Source: Study Guide

36) The curve in Figure 19.1.3 is the

- A) line of fairness.
- B) line of equality.
- C) learning curve.
- D) wage differential curve.
- E) Lorenz curve.

Answer: E

Diff: 1 Type: MC

Topic: Measuring Economic Inequality

Source: Study Guide

37) In Figure 19.1.3, the second poorest 20 percent of all families receive what share of income?

- A) 10 percent
- B) 20 percent
- C) 30 percent
- D) 40 percent
- E) none of the above

Answer: A

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

38) In Figure 19.1.3, the second richest 20 percent of all families receive what share of income?

- A) 10 percent
- B) 20 percent
- C) 30 percent
- D) 40 percent
- E) none of the above

Answer: B

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

39) In Canada, the low-income cut-off level for a family is when \_\_\_\_\_ or more of income is spent on food, shelter, and clothing.

- A) 33.6 percent
- B) 43.6 percent
- C) 53.6 percent
- D) 63.6 percent
- E) 73.6 percent

Answer: D

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

40) The Gini coefficient for a perfectly equal distribution of income is

- A) equal to zero.
- B) equal to 1.
- C) equal to 100.
- D) equal to infinity.
- E) negative.

Answer: A

Diff: 1 Type: MC

Topic: Measuring Economic Inequality

Source: Study Guide

41) The distribution of annual income

- A) understates the degree of inequality because it does not take into account the family's stage in its life cycle.
- B) understates the degree of inequality because it does not take into account the distribution of human capital.
- C) overstates the degree of inequality because it does not take into account the family's stage in its life cycle.
- D) overstates the degree of inequality because it does not take into account the distribution of human capital.
- E) is an accurate measure of the degree of inequality.

Answer: C

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

Source: Study Guide

- 42) Wealth differs from income because
- A) income is a stock and wealth is a flow.
  - B) wealth is derived from income.
  - C) income is what you earn and wealth is what you own.
  - D) income is what you own and wealth is what you earn.
  - E) wealth is preferable to income.

Answer: C

Diff: 1 Type: MC

Topic: Measuring Economic Inequality

Source: Study Guide

- 43) The distribution of *wealth*
- A) understates the degree of inequality because it does not take into account the family's stage in its life cycle.
  - B) understates the degree of inequality because it does not take into account the distribution of human capital.
  - C) overstates the degree of inequality because it does not take into account the family's stage in its life cycle.
  - D) overstates the degree of inequality because it does not take into account the distribution of human capital.
  - E) is an accurate measure of the degree of inequality.

Answer: D

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

Source: Study Guide

- 44) Measured wealth distributions that do not consider the distribution of human capital
- A) overstate the equality of the income distribution.
  - B) understate the inequality of the income distribution.
  - C) are correct since human capital is difficult to accurately measure.
  - D) overstate the inequality of the wealth distribution.
  - E) are correct because the distribution of human capital is about the same as the distribution of non-human wealth.

Answer: D

Diff: 2 Type: MC

Topic: Measuring Economic Inequality

## 19.2 Inequality in the World Economy

1) Incomes in China and India are a small fraction of incomes in Canada. But incomes in China and India are growing at more than twice the rate of those in Canada. As a result, the inequality in income between the people in China and India and people in Canada is \_\_\_\_\_ and the world Gini ratio is \_\_\_\_\_.

- A) staying relatively constant; remaining constant
- B) increasing in some years and decreasing in other years; remaining constant
- C) decreasing; decreasing
- D) increasing; increasing
- E) decreasing; increasing

Answer: C

Diff: 2 Type: MC

Topic: Inequality in the World Economy

Source: MyEconLab

2) Among Canada, Finland, and South Africa, income is distributed most equally in \_\_\_\_\_ and least equally in \_\_\_\_\_.

- A) South Africa; Finland
- B) Canada; South Africa
- C) South Africa; Canada
- D) Finland; Canada
- E) Finland; South Africa

Answer: E

Type: MC

3) The distribution of world income is \_\_\_\_\_ the distribution of Canadian income.

- A) more equal than
- B) equal to
- C) not comparable to
- D) equal to the distribution of Canadian wealth and more equal than
- E) less equal than

Answer: E

Type: MC

4) Between 1980 and 2000, the world Gini ratio \_\_\_\_\_ indicating \_\_\_\_\_ in the world distribution of income.

- A) fell; greater equality
- B) fell; greater inequality
- C) did not change; no change
- D) rose; greater equality
- E) rose; greater inequality

Answer: A

Type: MC

- 5) The world distribution of income has become more equal since 1970 because
- A) average incomes in poorer countries are rising much faster than average incomes in rich countries.
  - B) the distribution of income within most countries has become more equal.
  - C) foreign aid programs from rich nations have increased in size and especially in effectiveness.
  - D) technology is used similarly in all countries.
  - E) all of the above

Answer: A

Type: MC

### 19.3 The Sources of Economic Inequality

- 1) The demand for high-skilled labour is derived from the
- A) exploitation of the low-skilled workers.
  - B) marginal cost of production.
  - C) lower wage of the labour.
  - D) supply of the high-skilled labourers.
  - E) value of marginal product of high-skilled labour.

Answer: E

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

- 2) The demand for low-skilled labour is derived from the
- A) work left undone by the high-skilled workers.
  - B) marginal cost of production.
  - C) lower wage rate of the labour.
  - D) supply of the high-skilled labourers.
  - E) value of marginal product of low-skilled labour.

Answer: E

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

- 3) The greater the value of marginal product of labour,
- A) the greater is the supply of labour.
  - B) the greater is the demand for labour.
  - C) the greater is the marginal cost of production.
  - D) the greater is unemployment.
  - E) the lower is the wage rate.

Answer: B

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

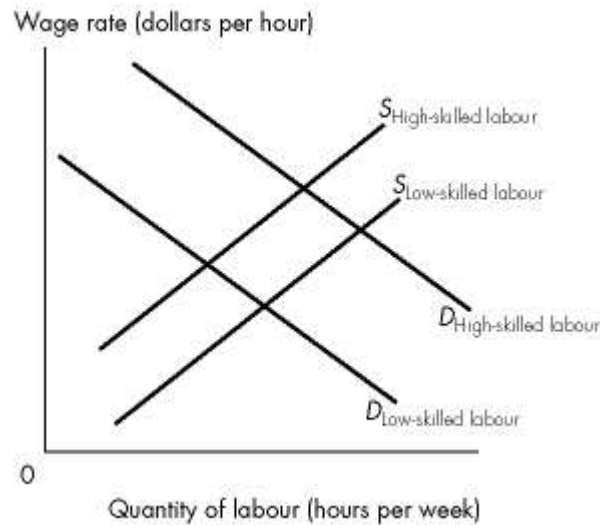
- 4) If the supply of labour curve is upward sloping but not vertical, and if the value of marginal product of labour increases,
- A) the supply of labour increases.
  - B) the wage rate rises.
  - C) the marginal cost of production increases.
  - D) the exploitation of workers decreases.
  - E) employment is unchanged.

Answer: B

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

Use the figure below to answer the following questions.



**Figure 19.3.1**

- 5) Refer to Figure 19.2.1. For any given quantity of labour employed,
- A) the elasticity of demand for high-skilled labourers is less than the elasticity of demand for low-skilled labourers.
  - B) high-skilled labourers will receive a lower wage than low-skilled labourers.
  - C) high-skilled labourers will receive a greater wage than low-skilled labourers.
  - D) the vertical distance between the two demand curves is the compensation for the cost of acquiring the skill.
  - E) the vertical distance between the two curves is the present value of human capital.

Answer: C

Diff: 1 Type: MC

Topic: The Sources of Economic Inequality

Source: Study Guide

- 6) Refer to Figure 19.3.1. At any given employment level, the vertical distance between the demand curves of the high-skilled and low-skilled workers
- A) is equal to the difference in the value of marginal product of the workers.
  - B) is equal to the difference in the work ethic of the workers.
  - C) is caused by discrimination against minorities.
  - D) is caused by discrimination against women.
  - E) equals the cost of acquiring the skills.

Answer: A

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

- 7) The vertical distance between the two supply curves in Figure 19.3.1
- A) is the compensation for the cost of acquiring human capital.
  - B) is the *VMP* of skill.
  - C) is the result of discrimination against low-skilled workers.
  - D) is the result of subsidies for high-skilled workers.
  - E) will disappear if there is free entry in the high-skilled market.

Answer: A

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

Source: Study Guide

- 8) Refer to Figure 19.3.1. At the equilibrium wage rates,
- A) more high-skilled workers will be hired than low-skilled workers.
  - B) more low-skilled workers will be hired than high-skilled workers.
  - C) the horizontal distance between the two demand curves is the compensation for the cost of acquiring human capital.
  - D) the horizontal distance between the two supply curves is the value of marginal product of skill.
  - E) none of the above.

Answer: A

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

- 9) Refer only to the information in Figure 19.3.1. At any given wage rate,
- A) more hours of low-skilled labour will be demanded than high-skilled labour.
  - B) more hours of high-skilled labour will be demanded than low-skilled labour.
  - C) more hours of low-skilled labour will be supplied than high-skilled labour.
  - D) more hours of high-skilled labour will be supplied than low-skilled labour.
  - E) both B and C are correct.

Answer: E

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

Use the figure below to answer the following questions.



**Figure 19.3.2**

10) Refer to Figure 19.3.2. At an employment level of 40 hours per week, the difference in the value of marginal product of high-skilled workers and low-skilled workers is

- A) \$0.
- B) \$2 an hour.
- C) \$6 an hour.
- D) \$4 an hour.
- E) \$3 an hour.

Answer: B

Diff: 1 Type: MC

Topic: The Sources of Economic Inequality

11) Refer to Figure 19.3.2. At an employment level of 20 hours per week, firms are willing to pay

- A) a wage rate of \$7 an hour to low-skilled workers.
- B) a maximum of \$5 an hour to high-skilled workers.
- C) up to \$7 an hour for high-skilled workers.
- D) the same for high-skilled workers as for low-skilled workers.
- E) \$3 an hour more for high-skilled workers.

Answer: C

Diff: 1 Type: MC

Topic: The Sources of Economic Inequality

- 12) Refer to Figure 19.3.2. At a wage rate of \$5, an employer would hire
- A) the same amount of high-skilled workers and low-skilled workers.
  - B) 20 hours of low-skilled labour and 40 hours of high-skilled labour.
  - C) 60 hours of low-skilled labour and 20 hours of high-skilled labour.
  - D) 20 hours of low-skilled labour and 60 hours of high-skilled labour.
  - E) 40 hours of low-skilled labour and 60 hours of high-skilled labour.

Answer: D

Diff: 1 Type: MC

Topic: The Sources of Economic Inequality

- 13) Refer to Figure 19.3.2. For the employer to hire 40 hours per week of both high-skilled and low-skilled labour,

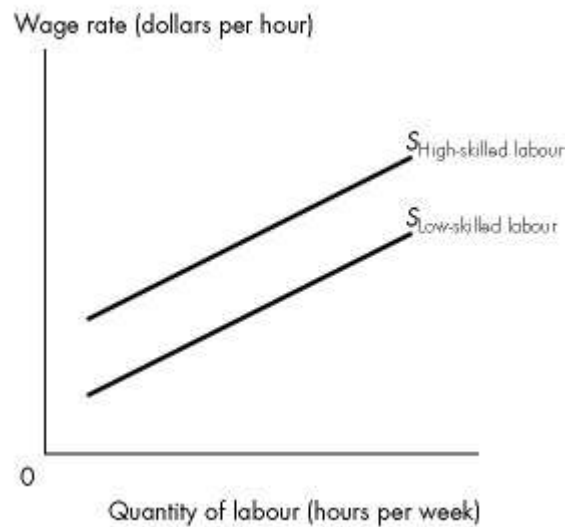
- A) high-skilled workers would have to earn a wage rate that is twice that of the low-skilled workers.
- B) high-skilled workers would have to earn a wage rate that is less than that of the low-skilled workers.
- C) high-skilled workers would have to earn a wage that is \$2 more than the wage paid to low-skilled workers.
- D) low-skilled workers would have to earn a wage that is \$2 more than the wage paid to high-skilled workers.
- E) high-skilled workers need to earn a wage that is between zero and \$2 more than low-skilled workers.

Answer: C

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

Use the figure below to answer the following question.



**Figure 19.3.3**

14) Refer to Figure 19.3.3. At any given level of employment for high-skilled and low-skilled workers, the vertical distance between the two supply curves

- A) disappears if there is free entry into the skill market.
- B) disappears if there is equal pay for work of equal value.
- C) is created by discrimination against low-skilled workers.
- D) is the compensation required for the cost of acquiring human capital.
- E) equals the value of marginal product of skill.

Answer: D

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

Use the figure below to answer the following question.



**Figure 19.3.4**

15) Refer to Figure 19.3.4. At an employment level of 30 hours per week, the compensation required for the cost of acquiring human capital is

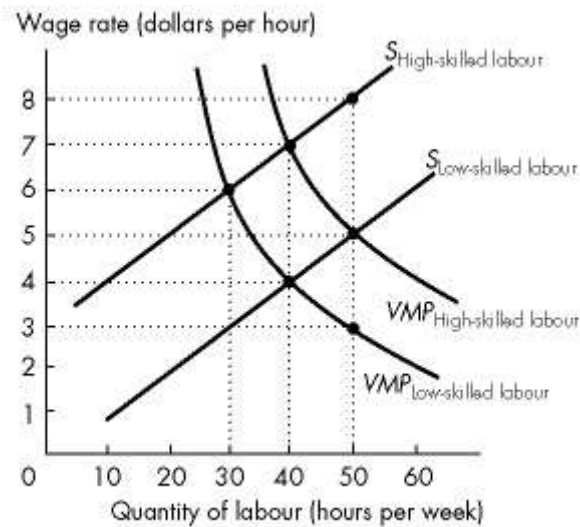
- A) \$0.
- B) \$2 an hour.
- C) \$4 an hour.
- D) \$6 an hour.
- E) cannot be determined without knowing the demand for labour.

Answer: B

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

Use the figure below to answer the following questions.



**Figure 19.3.5**

16) Refer to Figure 19.3.5. This figure shows the labour supply curves and the value of marginal product curves for high-skilled and low-skilled workers. The equilibrium wage rate for low-skilled workers is

- A) \$3 an hour.
- B) \$7 an hour.
- C) \$6 an hour.
- D) \$5 an hour.
- E) \$4 an hour.

Answer: E

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

17) Refer to Figure 19.3.5. This figure shows the labour supply curves and the value of marginal product curves for high-skilled and low-skilled workers. The equilibrium wage rate for high-skilled workers is

- A) \$5 an hour.
- B) \$4 an hour.
- C) \$6 an hour.
- D) \$8 an hour.
- E) \$7 an hour.

Answer: E

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

18) Refer to Figure 19.3.5. This figure shows the labour supply curves and the value of marginal product curves for high-skilled and low-skilled workers. If the labour markets are competitive, then for a 40-hour work week, high-skilled workers must be paid

A) an extra \$3 to compensate for the cost of acquiring their human capital and for their increased productivity.

B) an extra \$20 to compensate for the cost of acquiring their human capital and for their increased productivity.

C) an extra \$120 to compensate for the cost of acquiring their human capital and for their increased productivity.

D) an extra \$300 to compensate for the cost of acquiring their human capital and for their enhanced productivity.

E) an extra \$180 to compensate for the cost of acquiring their human capital and for their increased productivity.

Answer: C

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

19) Refer to Figure 19.3.5. This figure shows the labour supply curves and the value of marginal product curves for high-skilled and low-skilled workers. If there is an increase in the supply of high-skilled workers and the supply of high-skilled workers is now equal to the supply of low-skilled workers, then

A) wages paid to high-skilled workers would fall to \$4 an hour.

B) wages paid to high-skilled workers would fall to \$5 an hour.

C) wages paid to high-skilled workers would fall to \$6 an hour.

D) there would be no change in the wages of high-skilled workers, because high-skilled workers always earn more than low-skilled workers.

E) there would be no change in the wages of high-skilled workers, because their value of marginal product is unchanged.

Answer: B

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

20) Refer to Figure 19.3.5. This figure shows the labour supply curves and the value of marginal product curves for high-skilled and low-skilled workers. If there is an increase in the supply of high-skilled workers and the supply of high-skilled workers is now equal to the supply of low-skilled workers, then employment of high-skilled labour would

A) remain the same.

B) decrease.

C) increase to 40 hours per week.

D) increase to 50 hours per week.

E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

- 21) One important source of earnings differentials is the
- A) style of dress of the employee.
  - B) hair colour of the employee.
  - C) type of car driven by the employee.
  - D) number of years it takes the employee to graduate from college.
  - E) education level of the employee.

Answer: E

Diff: 1 Type: MC

Topic: The Sources of Economic Inequality

- 22) Which one of the following is *not* a reason why the wages of high-skilled workers exceed the wages of low-skilled workers?
- A) The market for high-skilled workers is more competitive than the market for low-skilled labour.
  - B) The value of marginal product of high-skilled workers is greater than that of low-skilled workers.
  - C) The cost of obtaining the human capital required for high-skilled workers is greater than the cost of obtaining the human capital required for low-skilled workers.
  - D) High-skilled workers have acquired more human capital than low-skilled workers.
  - E) The demand curve for high-skilled workers lies to the right of the demand curve for low-skilled workers.

Answer: A

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

Source: Study Guide

- 23) Other things remaining the same, if education costs rise substantially, we would expect to see
- A) a decrease in the value of marginal product of high-skilled workers.
  - B) a decrease in the demand for high-skilled workers.
  - C) an increase in the supply of high-skilled workers.
  - D) an increase in the number of high-skilled workers employed.
  - E) an increase in the wages received by high-skilled workers.

Answer: E

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

- 24) Which of the following statements is *false*? Human capital
- A) is the accumulated skill and knowledge of human beings.
  - B) is costly to acquire.
  - C) increases from on-the-job training.
  - D) increases from higher wages.
  - E) increases from education.

Answer: D

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

25) Which of the following three statements is *true*? Human capital

- A) decreases your value of marginal product.
- B) lowers your wages.
- C) may reduce your income while you are accumulating it.
- D) All of the above statements are true.
- E) None of the above three statements are true.

Answer: C

Diff: 1 Type: MC

Topic: The Sources of Economic Inequality

26) A generation that is wealthy and leaves assets to another generation that is not wealthy

- A) increases the inequality of the income distribution.
- B) decreases the inequality of the income distribution.
- C) does not change the distribution of income.
- D) proves that inheritance taxes are needed.
- E) is improving efficiency.

Answer: B

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

27) Complete the following sentence. Passing on wealth from one generation to another

- A) can decrease the inequality of wealth.
- B) will decrease the inequality of income.
- C) is limited since the government taxes this at a very high marginal tax rate.
- D) is one of the main causes of social unrest.
- E) will make the distribution of wealth more closely match the distribution of human capital.

Answer: A

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

28) Complete the following sentence. Assortative mating

- A) tends to breakdown barriers between the social classes.
- B) tends to increase the equality of the income distribution.
- C) tends to increase the equality of the distribution of wealth.
- D) tends to keep the income and wealth distributions from becoming more equal.
- E) occurs rarely these days due to changes in social values.

Answer: D

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

29) Assortative mating means that

- A) poor men tend to marry rich women.
- B) people tend to marry within their own socioeconomic class.
- C) people tend to marry above their own socioeconomic class.
- D) same sex marriages occur because "like attracts like."
- E) people with different values will marry.

Answer: B

Diff: 1 Type: MC

Topic: The Sources of Economic Inequality

Source: Study Guide

30) If discrimination takes the form of consumers discriminating against a group of workers, the effect on this group of workers will be to shift their

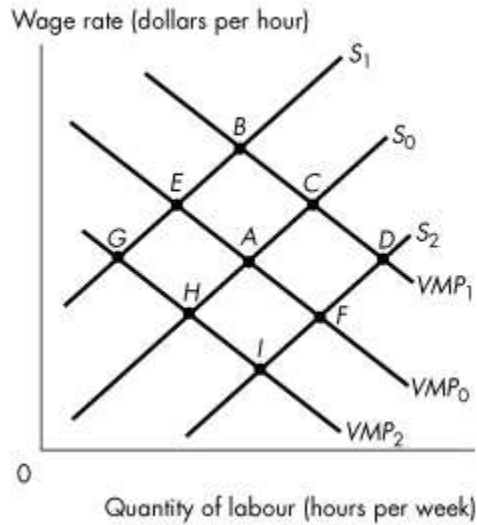
- A) value of marginal product curve rightward and increase their wage rate.
- B) value of marginal product curve leftward and decrease their wage rate.
- C) value of marginal product curve rightward and decrease their wage rate.
- D) supply of labour curve leftward and increase their wage rate.
- E) supply of labour curve rightward and decrease their wage rate.

Answer: B

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

Use the figure below to answer the following questions.



**Figure 19.3.6**

31) Refer to Figure 19.3.6. If this is the market for a group of workers who are discriminated against by customers and point A represents the equilibrium without discrimination, which point represents the equilibrium for the workers who are discriminated against?

- A) *D*
- B) *B*
- C) *I*
- D) *C*
- E) *H*

Answer: E

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

32) Refer to Figure 19.3.6. If this is the market for a group of workers who are discriminated in favour of by consumers and point A represents the equilibrium without discrimination, which point represents the equilibrium for the workers who receive favourable discrimination?

- A) *D*
- B) *B*
- C) *I*
- D) *C*
- E) *H*

Answer: D

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

33) Refer to Figure 19.3.6. This is the market for a group of workers. If point *A* represents the equilibrium for workers with higher human capital, which point represents the equilibrium for the workers with less human capital?

- A) *D*
- B) *B*
- C) *I*
- D) *C*
- E) *H*

Answer: C

Diff: 3 Type: MC

Topic: The Sources of Economic Inequality

34) In an economy in 2011, 3 million people had full-time managerial and professional jobs that paid an average of \$800 a week. At the same time, 1 million people had full-time sales positions that paid an average of \$530 a week. Managers and professionals are paid more than salespeople because \_\_\_\_\_.

- A) the supply curve of managers and professionals lies above that of salespeople
- B) the demand curve for managers and professionals lies above that of salespeople
- C) managers and professionals have a higher value of marginal product
- D) the typical manager or professional has incurred a higher cost of education
- E) all of the above

Answer: E

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

Source: MyEconLab

35) The main reason that wealth inequality persists across generations is that \_\_\_\_\_.

- A) people tend to marry within their own socioeconomic class
- B) intergenerational transfers can only increase wealth inequality
- C) there are differences between households in their degree of specialization
- D) rich families have equal wealth over the life cycle
- E) all of the above

Answer: A

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

Source: MyEconLab

36) Choose the correct sentence.

- A) Inherited wealth does not change income inequality because debts can't be forced onto the next generation.
- B) Inherited wealth can increase income inequality because debts can't be forced onto the next generation, but it can also decrease income inequality.
- C) Inherited wealth decreases income inequality because debts are forced onto the next generation.
- D) Inherited wealth decreases income inequality because on average most people inherit the same amount of money.
- E) Inherited wealth always increases income inequality because of assortative mating.

Answer: B

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

Source: MyEconLab

37) Technological change \_\_\_\_\_ the demand for high-skilled workers and \_\_\_\_\_ the demand for low-skilled workers. As a result, income inequality \_\_\_\_\_.

- A) increases; decreases; decreases
- B) increases; decreases; increases
- C) increases; increases; decreases
- D) decreases; decreases; increases
- E) increases; does not change; increases

Answer: B

Diff: 2 Type: MC

Topic: The Sources of Economic Inequality

Source: MyEconLab

38) Discrimination results in \_\_\_\_\_ compared to a situation with no discrimination.

- A) a lower wage rate but no change in the number employed
- B) a higher number employed and a lower wage rate
- C) a smaller number employed but no change in the wage rate
- D) a smaller number employed and a lower wage rate
- E) none of the above

Answer: D

Type: MC

39) Discrimination \_\_\_\_\_ workers in the group being discriminated against and \_\_\_\_\_ workers in the group being favoured.

- A) decreases the supply of; increases the supply of
- B) decreases the demand for and the supply of; increases the demand for and the supply of
- C) does not change the demand for; increases the demand for
- D) decreases the demand for; increases the demand for
- E) decreases the demand for; does not change the demand for

Answer: D

Type: MC

- 40) A firm that discriminates has \_\_\_\_\_ a firm that does not discriminate and \_\_\_\_\_.
- A) the same costs as; competes most often with firms from other countries
  - B) the same costs as; can successfully maximize profit in a competitive industry
  - C) lower costs than; drives other firms out of a competitive industry
  - D) higher costs than; competes most often with firms from other countries
  - E) higher costs than; cannot survive in a competitive industry

Answer: E

Type: MC

- 41) Customer discrimination against female realtors \_\_\_\_\_ the number of female realtors and \_\_\_\_\_ their perceived value of marginal product.

- A) decreases; decreases
- B) decreases; increases
- C) increases; increases
- D) increases; decreases
- E) decreases; does not change

Answer: A

Type: MC

## 19.4 Income Redistribution

- 1) Government transfer payments, such as welfare payments, redistribute income and
- A) increase the incentive to work.
  - B) improve economic efficiency.
  - C) increase tax receipts.
  - D) decrease the incentive to work.
  - E) push the Lorenz curve further away from the line of equality.

Answer: D

Diff: 1 Type: MC

Topic: Income Redistribution

- 2) The three main avenues through which the government redistributes income are
- A) subsidized services, sales taxes, and user fees.
  - B) sales taxes, income maintenance programs, and income taxes.
  - C) income maintenance programs, user fees, and welfare programs.
  - D) subsidized services, income taxes, and income maintenance programs.
  - E) welfare programs, income taxes, and income maintenance programs.

Answer: D

Diff: 2 Type: MC

Topic: Income Redistribution

- 3) A progressive income tax
- A) taxes lower income people a larger percentage than higher income people.
  - B) taxes income at an average rate that increases with income.
  - C) receives more tax from rich people, but taxes them at the same rate as poor people.
  - D) taxes everyone at the same rate.
  - E) is rarely used in advanced economies.

Answer: B

Diff: 1 Type: MC

Topic: Income Redistribution

- 4) A proportional income tax
- A) taxes lower income people a larger percentage than higher income people.
  - B) taxes lower income people a smaller percentage than higher income people.
  - C) receives less tax from higher income people, but taxes them at the same rate as lower income people.
  - D) taxes everyone at the same rate.
  - E) taxes everyone the same amount.

Answer: D

Diff: 1 Type: MC

Topic: Income Redistribution

5) A regressive income tax

- A) taxes income at an average rate that decreases with income.
- B) taxes lower income people a smaller percentage than higher income people.
- C) receives more from rich people, but taxes them at the same rate as poor people.
- D) taxes everyone at the same rate.
- E) taxes income at a marginal rate that increases with rises in income.

Answer: A

Diff: 1 Type: MC

Topic: Income Redistribution

6) In Canada, the highest income tax rates are in

- A) Quebec.
- B) Manitoba.
- C) Alberta.
- D) Ontario.
- E) British Columbia.

Answer: A

Diff: 2 Type: MC

Topic: Income Redistribution

7) In Canada, the lowest income tax rates are in

- A) British Columbia.
- B) Quebec.
- C) Manitoba.
- D) Alberta.
- E) Ontario.

Answer: D

Diff: 2 Type: MC

Topic: Income Redistribution

8) The tax system at both the federal and provincial levels is

- A) progressive.
- B) regressive.
- C) proportional.
- D) a combination of proportional and regressive.
- E) a combination of progressive and regressive.

Answer: A

Diff: 2 Type: MC

Topic: Income Redistribution

- 9) Comparing the distribution of income after taxes and benefits to the distribution of market income, it is true that the distribution of income after taxes and benefits is \_\_\_\_\_ the distribution of market income.
- A) more equally distributed than
  - B) less equally distributed than
  - C) more equally distributed only for the middle quintile than
  - D) as equally distributed as the
  - E) more equally distributed for the bottom two quintiles and less equally distributed for the top three quintiles than

Answer: A

Diff: 2 Type: MC

Topic: Income Redistribution

- 10) Income maintenance programs include all of the following programs *except*

- A) social security programs.
- B) workers' compensation.
- C) Canada Pension Plan.
- D) employment insurance.
- E) the minimum wage.

Answer: E

Diff: 1 Type: MC

Topic: Income Redistribution

- 11) One criticism of social security programs such as the Guaranteed Income Supplement is that

- A) it promotes efficiency rather than equity.
- B) it helps equity but hurts efficiency.
- C) it gives too much money to the elderly.
- D) it gives too much money to the poor.
- E) it gives too much money to the rich.

Answer: B

Diff: 2 Type: MC

Topic: Income Redistribution

- 12) Policies that result in a redistribution of income toward the poor include all of the following *except*

- A) public provision of elementary education.
- B) public provision of high school education.
- C) public provision of health-care services.
- D) public excise taxes.
- E) public provision of subsidized university education.

Answer: D

Diff: 1 Type: MC

Topic: Income Redistribution

13) In the absence of government policies to redistribute income, the income distribution will be the

- A) market distribution.
- B) unfair distribution.
- C) capitalist distribution.
- D) efficient distribution.
- E) line of equality.

Answer: A

Diff: 1 Type: MC

Topic: Income Redistribution

14) If the average tax rate increases as income increases, the income tax is

- A) progressive.
- B) proportional.
- C) negative.
- D) regressive.
- E) excessive.

Answer: A

Diff: 2 Type: MC

Topic: Income Redistribution

Source: Study Guide

15) Which one of the following reduces the inequality of income or wealth relative to the market distribution?

- A) government payments to the poor
- B) a regressive income tax
- C) large inheritances
- D) assortative mating
- E) all of the above

Answer: A

Diff: 2 Type: MC

Topic: Income Redistribution

Source: Study Guide

16) If the average tax rate decreases as income increases, the income tax is

- A) progressive.
- B) proportional.
- C) negative.
- D) regressive.
- E) redistributive.

Answer: D

Diff: 2 Type: MC

Topic: Income Redistribution

Use the table below to answer the following questions.

**Table 19.4.1**

Current Gross Income	Tax Payment Plan A	Tax Payment Plan B	Tax Payment Plan C	Tax Payment Plan D
0	0	0	0	200
1,000	100	100	200	200
2,000	200	400	200	200
4,000	400	1,600	200	200

17) In Table 19.4.1, which tax plan is proportional?

- A) Plan A
- B) Plan B
- C) Plan C
- D) Plan D
- E) impossible to calculate without additional information

Answer: A

Diff: 2 Type: MC

Topic: Income Redistribution

Source: Study Guide

18) In Table 19.4.1, which tax plan is progressive?

- A) Plan A
- B) Plan B
- C) Plan C
- D) Plan D
- E) impossible to calculate without additional information

Answer: B

Diff: 2 Type: MC

Topic: Income Redistribution

Source: Study Guide

19) A welfare trap occurs when the marginal tax rate is

- A) negative.
- B) zero.
- C) 100% or more.
- D) positive.
- E) less than the average tax rate.

Answer: C

Diff: 2 Type: MC

Topic: Income Redistribution

20) Economic efficiency and economic equity have what relation?

- A) Redistribution of income reduces economic equality while it increases economic efficiency.
- B) Income is equitably distributed in free market systems without intervention by government.
- C) There is a no tradeoff between the two.
- D) There is a tradeoff between equality and efficiency.
- E) More equality is generally more efficient.

Answer: D

Diff: 1 Type: MC

Topic: Income Redistribution

21) Redistribution of income from the rich to the poor will lead to a reduction in total output.

This is known as the

- A) market distribution.
- B) Robin Hood principle.
- C) inheritance principle.
- D) big tradeoff.
- E) capitalist dilemma.

Answer: D

Diff: 1 Type: MC

Topic: Income Redistribution

Source: Study Guide

22) The group that faces the weakest incentive to work are

- A) those who pay the highest income tax rate
- B) those who pay the lowest income tax rate.
- C) the middle class.
- D) households that benefit from welfare.
- E) all of the above.

Answer: D

Diff: 1 Type: MC

Topic: Income Redistribution

Refer to the table below to answer the following questions.

**Table 19.4.2**

<b>Before -tax income</b> (dollars)	<b>Plan A tax</b> (dollars)	<b>Plan B tax</b> (dollars)	<b>Plan C tax</b> (dollars)
<b>10,000</b>	1,000	1,000	2,000
<b>20,000</b>	2,000	4,000	2,000
<b>30,000</b>	3,000	9,000	2,000

23) Refer to Table 19.4.2. The table shows three tax payment schemes. Which tax payment plan *reduces* inequality?

- A) Plan A
- B) Plan A and Plan C
- C) Plan C
- D) Plan B
- E) Plan A, Plan B, and Plan C

Answer: D

Diff: 1 Type: MC

Topic: Income Redistribution

Source: MyEconLab

24) Refer to Table 19.4.2. The table shows three tax payment schemes. Which tax payment plan has no effect on inequality?

- A) Plan B
- B) Plan C
- C) Plan A
- D) Plan A and Plan C
- E) Plan B and Plan C

Answer: C

Diff: 1 Type: MC

Topic: Income Redistribution

Source: MyEconLab

25) The redistribution of income creates the big tradeoff between \_\_\_\_\_.

- A) receiving workers' compensation and not receiving workers' compensation
- B) equity and efficiency
- C) qualifying to receive employment insurance and not qualifying to receive employment insurance
- D) earning an income and losing welfare benefits
- E) being rich and being poor

Answer: B

Diff: 1 Type: MC

Topic: Income Redistribution

Source: MyEconLab

26) Last year you earned \$45,000 and paid \$9,000 in income taxes. This year you earned \$60,000 and paid \$15,000 in income taxes. What type of income tax do you face?

- A) regressive
- B) proportional
- C) progressive
- D) flat
- E) Both B and D are correct.

Answer: C

Type: MC

27) Joe earns \$100,000 per year. He pays a tax rate of 28 percent on the first \$60,000 of income and a tax rate of 15 percent on income above \$60,000. This tax system is an example of a \_\_\_\_\_ income tax.

- A) progressive
- B) proportional
- C) regressive
- D) flat
- E) Both B and D are correct.

Answer: C

Type: MC

## Chapter 20 Measuring GDP and Economic Growth

### 20.1 Gross Domestic Product

1) Gross domestic product is

- A) the final value of all goods produced in a country in a given time period.
- B) the market value of all goods and services produced in a country during a given time period.
- C) the market value of all the final goods and services produced in a country during a given time period.
- D) the average value of output produced in a country in a given time period.
- E) the market value of all the intermediate goods and services produced in a country during a given time period.

Answer: C

Diff: 3 Type: MC

Topic: Gross Domestic Product

2) In calculating GDP, economists use the value of final goods and services because

- A) by using final goods and services, they avoid double counting.
- B) final goods can be exported to other countries.
- C) intermediate goods are imported from other countries.
- D) GDP is underestimated if intermediate goods are used instead.
- E) none of the above.

Answer: A

Diff: 3 Type: MC

Topic: Gross Domestic Product

3) Which of the following statements is true?

- A) Final goods and services produced abroad by Canadians are part of Canadian GDP.
- B) Final goods and services produced in Canada by foreigners are part of the foreign country's GDP.
- C) Final goods and services produced in Canada by foreigners are part of Canada's GDP.
- D) Final goods and services produced in Canada by foreigners are imports.
- E) Final goods and services produced in Canada by foreigners are exports.

Answer: C

Diff: 3 Type: MC

Topic: Gross Domestic Product

4) The circular flow diagram illustrates the expenditures made by

- A) households only.
- B) households and firms only.
- C) households and investors only.
- D) firms, households, and governments only.
- E) households, firms, governments, and the rest of the world.

Answer: E

Diff: 1 Type: MC

Topic: Gross Domestic Product

- 5) In the circular flow model,
- A) households are sellers of factor services in goods markets.
  - B) households are buyers of goods and services in the factor markets.
  - C) firms are sellers of the factors in factor markets.
  - D) firms are sellers of goods and services in goods markets.
  - E) firms are buyers of goods and services in final markets.

Answer: D

Diff: 1 Type: MC

Topic: Gross Domestic Product

- 6) The purchasers in the goods markets are
- A) households and government only.
  - B) households and firms only.
  - C) households and net exporters only.
  - D) households, firms, and government only.
  - E) households, firms, government, and those who import our goods.

Answer: E

Diff: 1 Type: MC

Topic: Gross Domestic Product

- 7) Of the following items, which one would be considered as investment in the *National Income and Expenditure Accounts*?

- A) The purchase of a new van by a potter who packs it with his wares and travels to art shows on weekends.
- B) The purchase of 100 shares of Bell Canada stock on the Toronto Stock Exchange.
- C) The purchase of a 100-year-old house that was put on the protected historic sites list.
- D) The purchase of a Canadian government bond.
- E) All of the above.

Answer: A

Diff: 1 Type: MC

Topic: Gross Domestic Product

- 8) Complete the following sentence. Net exports equals

- A) exports divided by imports.
- B) exports plus imports.
- C) exports minus imports.
- D) imports minus exports.
- E) foreign borrowing by residents of Canada minus domestic borrowing by nonresidents of Canada.

Answer: C

Diff: 1 Type: MC

Topic: Gross Domestic Product

9) Which one of the following is an expenditure flow from households to firms?

- A) goods and services
- B) factor services
- C) payments for goods and services
- D) payments for factor services
- E) loans

Answer: C

Diff: 1 Type: MC

Topic: Gross Domestic Product

10) Which one of the following is an income flow from firms to households?

- A) goods and services
- B) factor services
- C) payments for goods and services
- D) payments for factor services
- E) loans

Answer: D

Diff: 1 Type: MC

Topic: Gross Domestic Product

11) Which one of the following flows from firms to households?

- A) goods and services
- B) factor services
- C) payments for goods and services
- D) payments for loans
- E) loans

Answer: A

Diff: 1 Type: MC

Topic: Gross Domestic Product

12) For the aggregate economy, income equals

- A) expenditure, but these are not generally equal to GDP.
- B) GDP, but expenditure is generally less than these.
- C) expenditure equals GDP.
- D) expenditure equals GDP only if there is no government or foreign sectors.
- E) expenditure equals GDP only if there is no depreciation.

Answer: C

Diff: 2 Type: MC

Topic: Gross Domestic Product

Source: Study Guide

13) Which one of the following is *false*?

- A)  $Y = C + I + G + M - X$
- B)  $Y - C - I - G - X + M = 0$
- C)  $X - M = Y - C - I - G$
- D)  $Y + M = C + I + G + X$
- E)  $Y = C + I + G + X - M$

Answer: A

Diff: 3 Type: MC

Topic: Gross Domestic Product

14) Which one of the following is *true*?

- A)  $Y = C + I + G + M - X$
- B)  $I + G + X = Y + I + M$
- C)  $Y = C + S + I$
- D)  $Y + M = C + I + G$
- E)  $Y = C + I + G + X - M$

Answer: E

Diff: 3 Type: MC

Topic: Gross Domestic Product

15) Which of the following is *not* correct?

- A) Investment is the purchase of new plant, equipment, and buildings and the additions to inventories.
- B) Net investment equals gross investment minus depreciation.
- C) Depreciation decreases the value of a firm's capital.
- D) Gross investment is the amount by which the value of capital increases.
- E) Gross investment is the total amount spent buying new capital and replacing depreciated capital.

Answer: D

Diff: 2 Type: MC

Topic: Gross Domestic Product

16) Suppose the economy's capital increases over the year. It must be true that

- A) net investment was greater than gross investment.
- B) net investment was positive.
- C) depreciation was greater than net investment.
- D) depreciation was greater than gross investment.
- E) depreciation is less than zero.

Answer: B

Diff: 2 Type: MC

Topic: Gross Domestic Product

17) SaskWidget produces plastic parts. At the beginning of the year, they held \$24 million worth of capital. At the end of the year, they held \$20 million worth of capital. One can conclude that

- A) net investment increased by \$4 million.
- B) gross investment decreased by \$4 million.
- C) gross investment increased by \$4 million.
- D) depreciation exceeded gross investment by \$4 million.
- E) depreciation equals \$4 million.

Answer: D

Diff: 2 Type: MC

Topic: Gross Domestic Product

18) One of the reasons why real GDP grows is that

- A) prices increase.
- B) governments collect more taxes.
- C) capital grows as a result of investment.
- D) imports increase.
- E) people have more income.

Answer: C

Diff: 2 Type: MC

Topic: Gross Domestic Product

19) Which of the following would be an example of a consumption expenditure?

- A) More spending by the government on children's programs.
- B) An increase in welfare payments to single mothers.
- C) The purchase of a new car by the IPSCO steel company.
- D) The purchase of a new car by the Singh household.
- E) All of the above.

Answer: D

Diff: 2 Type: MC

Topic: Gross Domestic Product

Source: Study Guide

20) The change in capital from year to year is equal to

- A) gross investment.
- B) gross investment minus net investment.
- C) savings.
- D) net investment minus depreciation
- E) gross investment minus depreciation.

Answer: E

Diff: 2 Type: MC

Topic: Gross Domestic Product

21) Capital in year 2012 equals capital in year 2011

- A) minus depreciation.
- B) plus net investment plus depreciation.
- C) plus gross investment.
- D) plus net investment.
- E) plus net investment minus depreciation.

Answer: D

Diff: 2 Type: MC

Topic: Gross Domestic Product

Source: Study Guide

Use the figure below to answer the following questions.

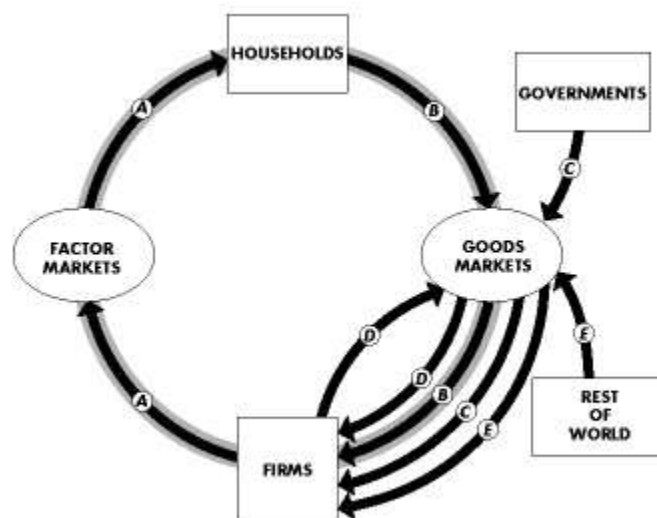


Figure 20.1.1

22) Refer to Figure 20.1.1, which shows the circular flow of expenditure and income for Venus.

During 2012, A was \$100, B was \$50, C was \$30 and D was \$10. How much is GDP?

- A) \$75
- B) \$50
- C) \$90
- D) \$100
- E) None of the above

Answer: D

Diff: 2 Type: MC

Topic: Gross Domestic Product

23) Refer to Figure 20.1.1, which shows the circular flow of expenditure and income for Venus. During 2012, *A* was \$100, *B* was \$50, *C* was \$30 and *D* was \$10. How much is net exports?

- A) \$10
- B) \$25
- C) \$30
- D) \$50
- E) None of the above

Answer: A

Diff: 2 Type: MC

Topic: Gross Domestic Product

24) Refer to Figure 20.1.1, which shows the circular flow of expenditure and income for Venus. During 2012, *A* was \$100, *B* was \$50, *C* was \$30 and *D* was \$10. How much is aggregate expenditure?

- A) \$50
- B) \$75
- C) \$90
- D) \$100
- E) None of the above

Answer: D

Diff: 3 Type: MC

Topic: Gross Domestic Product

25) Refer to Figure 20.1.1, which shows the circular flow of expenditure and income for Venus. During 2012, *A* was \$100, *B* was \$50, *C* was \$30 and *D* was \$10. What is aggregate income?

- A) \$25
- B) \$50
- C) \$75
- D) \$90
- E) \$100

Answer: E

Diff: 2 Type: MC

Topic: Gross Domestic Product

Use the information below to answer the following questions.

**Fact 20.1.1**

At the beginning of 2012, Peter's Perfectly Prickly Piercing Parlour had \$5,000 worth of bellybutton and eyebrow rings on hand, 2 computers (each worth \$1,000), 1 cash register worth \$100, electrical equipment worth \$500, and one piercing needle worth \$500. At the end of 2012, they had \$5,000 worth of bellybutton and eyebrow rings, a new high speed computer worth \$3,000 (they had to throw out the old ones), the same cash register, which was now worthless, electrical equipment worth \$600, and they had upgraded the needle at a cost of \$700 which was valued at \$1,000.

26) Refer to Fact 20.1.1. Peter's capital at the beginning of 2012 is

- A) \$8,100.
- B) \$7,000.
- C) \$3,100.
- D) \$7,600.
- E) \$5,000.

Answer: A

Diff: 2 Type: MC

Topic: Gross Domestic Product

27) Refer to Fact 20.1.1. Peter's capital at the end of 2012 is

- A) \$7,000.
- B) \$9,600.
- C) \$4,400.
- D) \$7,600.
- E) \$4,000.

Answer: B

Diff: 2 Type: MC

Topic: Gross Domestic Product

28) Refer to Fact 20.1.1. Peter's gross investment in 2012 is

- A) \$2,800.
- B) \$3,800.
- C) \$1,800.
- D) \$7,800.
- E) \$5,800.

Answer: B

Diff: 3 Type: MC

Topic: Gross Domestic Product

29) Refer to Fact 20.1.1. Peter's depreciation in 2012 is

- A) \$2,300.
- B) \$800.
- C) zero.
- D) \$1,000.
- E) \$3,000.

Answer: A

Diff: 2 Type: MC

Topic: Gross Domestic Product

30) Refer to Fact 20.1.1. Peter's net investment in 2012 is

- A) \$2,000.
- B) \$3,800.
- C) \$1,800.
- D) \$7,800.
- E) \$1,500.

Answer: E

Diff: 2 Type: MC

Topic: Gross Domestic Product

31) The value of intermediate goods is not counted in GDP

- A) to keep from including goods that reduce society's welfare.
- B) because of the tremendous difficulty in keeping track of all the intermediate goods produced in an economy as large as that of Canada.
- C) because they are only sold in factor markets.
- D) to avoid counting their value twice and overstating the value of GDP.
- E) because they are not consumed in the current year.

Answer: D

Diff: 2 Type: MC

Topic: Gross Domestic Product

32) Intermediate goods are

- A) sold to their ultimate user.
- B) produced by one firm, bought by another firm, and used as a component of a final good or service.
- C) included directly in the measure of GDP.
- D) capital.
- E) purchased this year but consumed in future years.

Answer: B

Diff: 1 Type: MC

Topic: Gross Domestic Product

33) An art collector recently sold a piece of pottery for \$300. He had purchased it for \$200 two years earlier. How will the most recent sale affect GDP?

- A) GDP will increase by \$100.
- B) GDP will not change.
- C) GDP will increase by \$300.
- D) GDP will increase by \$200.
- E) GDP 2 years ago must be adjusted downwards by \$200, and current GDP will rise by \$300.

Answer: B

Diff: 2 Type: MC

Topic: Gross Domestic Product

34) Which of the following would *not* be included in GDP for 2011?

- A) A car produced in 2011 and held in inventory until 2012.
- B) A car produced in 2011 and sold in 2012.
- C) The value of all cars produced in 2011.
- D) A car produced in January of 2011 and sold in November of 2011.
- E) A car produced in 2010 and sold in 2011.

Answer: E

Diff: 2 Type: MC

Topic: Gross Domestic Product

35) Stock and bond sales are not included in GDP because they

- A) do not occur in the year in which the production represented by them takes place.
- B) represent corporate production.
- C) represent indebtedness.
- D) are not goods and services.
- E) are not sold in the country in which they are produced.

Answer: D

Diff: 2 Type: MC

Topic: Gross Domestic Product

36) In calculating GDP, all of the following are excluded *except*

- A) the value of intermediate goods.
- B) the value of all homes built in the year in question.
- C) the value of used goods.
- D) purchases of stocks and bonds.
- E) subsidies from the government.

Answer: B

Diff: 2 Type: MC

Topic: Gross Domestic Product

37) From the following list, choose the item that would be included in a current measure of GDP.

- A) the purchase of a previously owned house that was built last year
- B) a social security cheque for \$500
- C) the purchase of 10 litres of gasoline for your car
- D) a \$2,000 cheque from your Aunt Grace
- E) income from the sale of your Canadian Snowfun stocks

Answer: C

Diff: 1 Type: MC

Topic: Gross Domestic Product

38) Which one of the following would *not* be counted as part of this year's GDP?

- A) The lumber you purchase when building bookshelves for your room.
- B) The government bond you buy for your newborn niece.
- C) The purchase of a new personal computer that was produced in the current year.
- D) The purchase of wheat that was produced in the current year by a Saskatchewan farmer.
- E) The purchase of a house that was produced in the current year.

Answer: B

Diff: 1 Type: MC

Topic: Gross Domestic Product

39) How much would the production of a kayak add to GDP if the shell costs \$250, the paint costs \$20, the finisher costs \$35, the manufacturer sold it to the dealer for \$500, and the dealer sold it to his customer for \$800?

- A) \$1,605
- B) \$1,300
- C) \$500
- D) \$305
- E) \$800

Answer: E

Diff: 2 Type: MC

Topic: Gross Domestic Product

40) Which of the following adds to Canadian GDP?

- A) I shovel my own driveway.
- B) I sell my used Honda.
- C) The production and sale of flour to a bakery.
- D) The purchase of a CD made in China.
- E) The ice cream I buy from my grocery store.

Answer: E

Type: MC

Topic: Gross Domestic Product

Source: Study Guide

41) A bakery uses flour to produce bread.

When calculating GDP, we include \_\_\_\_\_, because when we add the value of the flour to the value of the loaf of bread to calculate GDP, the result is \_\_\_\_\_.

- A) only the value of the bread sold in a store; double counting
- B) only the value of the flour used to produce the bread; double counting
- C) both the value of the bread sold in a store and the value of the flour used to produce the bread; double counting
- D) both the value of the bread sold in a store and the value of the flour used to produce the bread; the true value of the economy's output
- E) none of the above

Answer: A

Type: MC

Topic: Gross Domestic Product

Source: MyEconLab

42) The firm that printed your textbook bought the paper from XYZ Paper Mills.

This purchase of paper \_\_\_\_\_ part of GDP because the paper is \_\_\_\_\_ good.

- A) is not; a final
- B) is not; an intermediate
- C) is; an intermediate
- D) is; a final
- E) is; a nonrenewable

Answer: B

Type: MC

Topic: Gross Domestic Product

Source: MyEconLab

43) In the circular flow diagram, aggregate expenditure includes \_\_\_\_\_.

- A) consumption expenditure, saving, investment and government expenditure
- B) saving, investment, and taxes
- C) consumption expenditure, investment, government expenditure, and exports
- D) consumption expenditure, investment, government expenditure and net exports
- E) government expenditure, transfer payments, and taxes

Answer: D

Type: MC

44) Which of the following are equal to one another?

- I. aggregate production
  - II. aggregate expenditure
  - III. aggregate income
- A) I equals II, but I does not equal III.
  - B) I equals III, but I does not equal II.
  - C) II equals III, but II does not equal I.
  - D) III equals II, but III does not equal I
  - E) I equals II equals III.

Answer: E

Type: MC

45) Suppose Mail Boxes Etc. buys a new copier for its store for \$1,000. A year later, when the firm wants to upgrade to a new copier, it finds that the old copier is only worth \$750. Over the year the copier was used, \_\_\_\_\_ has occurred.

- A) depreciation
- B) demarcation
- C) devaluation
- D) denouement
- E) disparity

Answer: A

Type: MC

46) Which of the following relationships is correct?

- A)  $\text{Gross Investment} = \text{Net Investment} + \text{Depreciation}$
- B)  $\text{Consumption expenditure} = \text{Net Investment} - \text{Depreciation}$
- C)  $\text{Net Investment} = \text{Gross Investment} + \text{Depreciation}$
- D)  $\text{Depreciation} = \text{Gross Investment} - \text{Consumption expenditure}$
- E)  $\text{Saving} = \text{Gross Investment} - \text{Taxes}$

Answer: A

Type: MC

## 20.2 Measuring Canada's GDP

1) To measure GDP, Statistics Canada uses

- A) the expenditure approach.
- B) the income approach.
- C) the value-added approach.
- D) only A and B.
- E) A, B and C.

Answer: D

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

2) A hypothetical economy produced four final goods during the year: plates, TVs, bicycles, and computers. Forty plates were produced and sold for \$10 each. Five TVs were produced and sold for \$300 each. Fifty bicycles were produced and sold for \$100 each. Three computers were produced and sold for \$750 each. With this information, one could determine

- A) gross investment for this economy.
- B) net investment for this economy.
- C) indirect taxes less subsidies for this economy.
- D) whether factors had been fully employed in this economy.
- E) total income for this economy.

Answer: E

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

3) Suppose the economy of Econoworld produces only two goods, kayaks and birdseed. In one year 20 kayaks are produced and sold for \$1,000 each and 10 bags of birdseed are produced and sold for \$30 each. The value of nominal GDP for this year is

- A) \$20,000.
- B) \$300.
- C) \$20,300.
- D) \$23,000.
- E) 20 kayaks plus 10 bags of birdseed.

Answer: C

Diff: 1 Type: MC

Topic: Measuring Canada's GDP

- 4) The expenditure approach measures GDP by adding together
- A) wages, salaries and supplementary labour income, and other factor incomes.
  - B) wages, salaries and supplementary labour income, other factor income, subsidies paid by the government, indirect taxes paid, and income of nonfarm unincorporated businesses.
  - C) compensation of employees, rental income, corporate profits, net interest, proprietors' income, indirect taxes paid, and capital consumption expenditures, and by subtracting subsidies paid by the government.
  - D) the total expenditures of consumers, firms, net exporters, and by governments at all levels.
  - E) the total expenditures of consumers and firms.

Answer: D

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

*Use the table below to answer the following questions.*

**Table 20.2.1**  
Data From Eastland

Wages, salaries, and supplementary labour income	800
Other factor incomes	260
Government expenditures on goods and services	240
Depreciation	240
Investment	400
Personal income taxes net of transfer payments	140
Indirect taxes	120
Net exports	80
Consumption expenditure	640

- 5) Refer to Table 20.2.1. From the information given in the table, the value of gross domestic product is
- A) \$1,280.
  - B) \$1,290.
  - C) \$1,360.
  - D) \$1,120.
  - E) \$1,100.

Answer: C

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

6) Refer to Table 20.2.1. From the information given in the table, the value of net domestic income at factor cost is

- A) \$1,280.
- B) \$1,290.
- C) \$1,360.
- D) \$1,060.
- E) \$1,100.

Answer: D

Diff: 3 Type: MC

Topic: Measuring Canada's GDP

7) Refer to Table 20.2.1. From the data in the table, what additional data are needed to compute net domestic income at market prices?

- A) statistical discrepancy
- B) transfer payments
- C) subsidies
- D) depreciation
- E) net taxes

Answer: C

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

8) Refer to Table 20.2.1. From the data in the table, what is total income in Eastland?

- A) \$1,120
- B) \$1,180
- C) \$1,360
- D) \$1,420
- E) \$1,280

Answer: C

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

9) The largest component of GDP using the expenditure approach is

- A) investment
- B) consumption expenditure
- C) exports
- D) government expenditure
- E) imports

Answer: B

Diff: 1 Type: MC

Topic: Measuring Canada's GDP

10) Which one of the following would be included in the calculation of GDP by the expenditure approach?

- A) the purchase of 20 shares of a new issue of IBM stock
- B) the purchase of an original eighteenth century work of art
- C) the value of your brother's services when he mows the lawn for the family
- D) the cost of adding a new kitchen to your house
- E) the income you pay to your gardener

Answer: D

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

*Use the table below to answer the following questions.*

**Table 20.2.2**

Government expenditures on goods and services	\$ 500
Wages, salaries, and supplementary labour income	2,000
Depreciation	400
Investment	400
Consumption expenditure	2,200
Net exports	-50
Indirect taxes	150
<u>Statistical discrepancy</u>	<u>0</u>

11) Refer to Table 20.2.2. Gross domestic product equals

- A) \$3,050.
- B) \$3,150.
- C) \$3,400.
- D) \$5,600.
- E) \$5,050.

Answer: A

Diff: 1 Type: MC

Topic: Measuring Canada's GDP

12) Refer to Table 20.2.2. Net domestic income at market prices equals

- A) \$3,050.
- B) \$3,150.
- C) \$3,400.
- D) \$4,650.
- E) \$2,650.

Answer: E

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

13) Which one of the following is *not* an example of investment in the expenditure approach to measuring GDP? General Motors

- A) buys a new auto stamping machine.
- B) adds 500 new cars to inventories.
- C) buys shares in another company.
- D) builds another assembly plant.
- E) replaces some worn-out stamping machines.

Answer: C

Diff: 1 Type: MC

Topic: Measuring Canada's GDP

*Use the table below to answer the following questions.*

**Table 20.2.3**

Item	Millions of dollars
Wages paid to labour	800,000
Consumption expenditure	650,000
Taxes paid on wages	200,000
Government payments to support unemployed, sick, & aged	50,000
Firms' profits	200,000
Investment	250,000
Taxes paid on profits	50,000
Government expenditure on goods and service	200,000
Exports	250,000
Saving	200,000
Imports	300,000

14) Refer to Table 20.2.3. Consider the economy represented in the table. GDP in this economy, in millions of dollars, is

- A) \$1,150,000
- B) \$850,000.
- C) \$1,350,000.
- D) \$1,050,000.
- E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

15) Refer to Table 20.2.3. Consider the economy represented in the table. Total income, in millions of dollars, is

- A) \$800,000.
- B) \$850,000.
- C) \$1,350,000.
- D) \$1,050,000.
- E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

16) Net domestic income at market prices can be derived by which one of the following? GDP (income approach) minus

- A) taxes.
- B) corporate profits.
- C) subsidies.
- D) consumption expenditure.
- E) depreciation.

Answer: E

Diff: 1 Type: MC

Topic: Measuring Canada's GDP

17) The sum of wages, salaries and supplementary labour income, and other factor incomes is

- A) gross domestic product.
- B) gross domestic income.
- C) net domestic income at factor cost.
- D) net domestic product.
- E) total output of the economy.

Answer: C

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

18) In the Canadian economy, market prices and factor costs would be the same except for

- A) depreciation.
- B) exports.
- C) personal taxes.
- D) indirect taxes and subsidies.
- E) capital consumption.

Answer: D

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

19) Net domestic income at market prices equals

- A) consumption expenditure plus government expenditure plus net exports plus investment.
- B) consumption expenditure plus government expenditure plus exports plus personal taxes.
- C) indirect business taxes plus personal income plus net exports.
- D) all incomes plus indirect taxes minus subsidies.
- E) all incomes minus depreciation.

Answer: D

Diff: 1 Type: MC

Topic: Measuring Canada's GDP

Use the table below to answer the following questions.

**Table 20.2.4**

Other factor incomes	\$570
Indirect taxes	230
Depreciation	250
Wages, salaries and supplementary labour income	1,350
Consumption expenditure	1,400
Government expenditure on goods and services	500
Government transfer payments	50
Net exports	40
Subsidies	0

20) Refer to Table 20.2.4. Gross domestic product is equal to

- A) \$2,400.
- B) \$1,920.
- C) \$2,150.
- D) \$1,940.
- E) \$2,350.

Answer: A

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

21) Refer to Table 20.2.4. Net domestic income at market prices is equal to

- A) \$2,150.
- B) \$1,920.
- C) \$2,400.
- D) \$1,940.
- E) \$2,350.

Answer: A

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

22) Refer to Table 20.2.4. Gross investment is equal to

- A) \$460.
- B) \$260.
- C) \$400.
- D) \$560.
- E) \$250.

Answer: A

Diff: 3 Type: MC

Topic: Measuring Canada's GDP

23) Refer to Table 20.2.4. Net investment is equal to

- A) \$250.
- B) \$210.
- C) \$510.
- D) \$560.
- E) \$150.

Answer: B

Diff: 3 Type: MC

Topic: Measuring Canada's GDP

24) Which approach to measuring GDP is being used when Statistics Canada sums wages, salaries and supplementary labour income, and other factor incomes?

- A) opportunity cost approach
- B) expenditure approach
- C) value-added approach
- D) factor cost approach
- E) income approach

Answer: E

Diff: 1 Type: MC

Topic: Measuring Canada's GDP

25) Which approach to measuring GDP is being used when Statistics Canada sums spending on goods and services for consumer goods, government, business investments and exports, net of imports?

- A) value added
- B) income
- C) factor cost
- D) expenditure
- E) opportunity cost

Answer: D

Diff: 1 Type: MC

Topic: Measuring Canada's GDP

26) To derive net domestic income at market prices from gross domestic product, we

- A) subtract gross investment from GDP.
- B) subtract the statistical discrepancy from GDP.
- C) add the statistical discrepancy to GDP.
- D) subtract depreciation from GDP.
- E) add depreciation to GDP.

Answer: D

Diff: 1 Type: MC

Topic: Measuring Canada's GDP

27) To obtain the factor cost of a good from its market price

- A) add indirect taxes and subtract subsidies.
- B) subtract indirect taxes and add subsidies.
- C) subtract both indirect taxes and subsidies.
- D) add both indirect taxes and subsidies.
- E) subtract depreciation.

Answer: B

Diff: 1 Type: MC

Topic: Measuring Canada's GDP

Source: Study Guide

28) Wages, salaries, and supplementary labour income are components of which approach to measuring GDP?

- A) income approach
- B) expenditure approach
- C) injections approach
- D) output approach
- E) value-added approach

Answer: A

Diff: 1 Type: MC

Topic: Measuring Canada's GDP

29) Real GDP equals

- A) nominal GDP minus the value of intermediate goods.
- B) nominal GDP adjusted for the depreciation of capital.
- C) the value of final goods and services produced in a given year when valued at the prices of a reference base year.
- D) nominal GDP minus the value of goods exported to foreign countries.
- E) nominal GDP minus the rate of inflation.

Answer: C

Diff: 1 Type: MC

Topic: Measuring Canada's GDP

30) Suppose in current dollar terms, GDP increased by approximately 7 percent between one period and the next, but real GDP fell by 2 percent. Which one of the following explanations is most likely?

- A) Prices fell by 9 percent.
- B) Prices fell by 2 percent.
- C) Output rose by 2 percent.
- D) Prices increased by 7 percent.
- E) Prices increased by 9 percent.

Answer: E

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

- 31) Real GDP will increase only if the
- A) average level of prices rises.
  - B) quantity of goods and services produced increases.
  - C) unemployment rate rises.
  - D) employment rate rises.
  - E) employment rate falls.

Answer: B

Diff: 1 Type: MC

Topic: Measuring Canada's GDP

- 32) In recent history, real GDP has risen less rapidly than nominal GDP. This is because
- A) the general price level fell.
  - B) capital increased.
  - C) the goal of zero population growth has been reached.
  - D) the general price level rose.
  - E) the level of population rose.

Answer: D

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

- 33) If nominal GDP increased by 11 percent during a year while real GDP increased by only 5 percent, then the
- A) price level decreased by 6 percent.
  - B) price level increased by 16 percent.
  - C) price level remained steady but real output fell by 6 percent.
  - D) unemployment rate fell during the year.
  - E) price level increased by 6 percent.

Answer: E

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

- 34) If you want to investigate the claim that more goods and services were produced in the economy during 2011 than 2012, what should you look at?

- A) real GDP
- B) nominal GDP
- C) intermediate GDP
- D) GDP calculated using the expenditure approach
- E) either B or D

Answer: A

Diff: 1 Type: MC

Topic: Measuring Canada's GDP

35) Nominal GDP will increase

- A) only if the average level of prices rises.
- B) only if the quantity of goods and services produced increases.
- C) only if the unemployment rate rises.
- D) only if both the average level of prices rises and the quantity of goods and services produced increases.
- E) if either the average level of prices rises or the quantity of goods and services produced increases.

Answer: E

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

Use the table below to answer the following questions.

**Table 20.2.5**  
Data From Southton

Item	Price (dollars)		Quantity (number of items)	
	Base Year	Current Year	Base Year	Current Year
Rubber Ducks	1.00	1.25	100	100
Beach Towels	9.00	6.00	12	14

36) Refer to Table 20.2.5. From the data in the table, compute Southton's nominal GDP in the current year.

- A) \$197
- B) \$208
- C) \$209
- D) \$226
- E) It cannot be calculated given the data.

Answer: C

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

Source: Study Guide

37) Refer to Table 20.2.5. From the data in the table, compute Southton's nominal GDP in the base year.

- A) \$208
- B) \$197
- C) \$209
- D) \$226
- E) It cannot be calculated given the data.

Answer: A

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

Source: Study Guide

38) Refer to Table 20.2.5. From the data in the table, compute Southton's real GDP in the base year.

- A) \$208
- B) \$197
- C) \$209
- D) \$226
- E) It cannot be calculated given the data.

Answer: A

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

Source: Study Guide

*Use the table below to answer the following questions.*

**Table 20.2.6**

There are only two goods in this economy.

	Price		Quantity	
	Base Year (dollars)	Current Year (dollars)	Base Year	Current Year
Bread	1.00	2.10	70,000	75,000
Computer Disks	1.00	1.80	25,000	18,000

39) Refer to Table 20.2.6. Consider the data in this table. What is current nominal GDP?

- A) \$189,900
- B) \$192,000
- C) \$95,000
- D) \$93,000
- E) None of the above

Answer: A

Diff: 2 Type: MC

Topic: Measuring Canada's GDP

40) Refer to Table 20.2.6. Consider the data in this table. What is current real GDP in terms of base-year prices?

- A) \$189,900
- B) \$192,000
- C) \$95,000
- D) \$93,000
- E) None of the above

Answer: D

Diff: 3 Type: MC

Topic: Measuring Canada's GDP

41) Choose the correct statement.

- A) When nominal GDP increases, real GDP decreases.
- B) Nominal GDP is just a more precise name for real GDP.
- C) We measure the change in production by comparing nominal GDP in one year with real GDP in the previous year.
- D) Nominal GDP is just a more precise name for GDP.
- E) Nominal GDP and real GDP both increase when the average level of prices increase.

Answer: D

Type: MC

Topic: Measuring Canada's GDP

Source: MyEconLab

42) A south sea island produces only coconuts.

In 2005, the price of a coconut is \$2.00 and the quantity produced is 400.

In 2012, the price of a coconut is \$1.50 and the quantity produced is 350.

2005 is the reference base year.

Real GDP in 2012 in terms of base-year prices is

- A) \$600.
- B) \$525.
- C) \$800.
- D) \$700.
- E) \$750.

Answer: D

Type: MC

Topic: Measuring Canada's GDP

Source: MyEconLab

43) In the *National Income and Expenditure Accounts*, government expenditure refers to spending on goods and services by

- A) federal and provincial governments only.
- B) the federal government only. Provincial and local government expenditures are included in provincial GDP calculations.
- C) provincial and local governments only.
- D) federal, provincial, and local governments.
- E) the federal government and local governments only. Provincial government expenditures are included in provincial GDP calculations.

Answer: D

Diff: 1 Type: MC

Topic: Gross Domestic Product

44) Consumption expenditure includes only \_\_\_\_\_.

- A) expenditure by Canadian households on goods and services produced in Canada
- B) expenditure by Canadian households and firms on goods and services produced in Canada
- C) expenditure by Canadian households, firms, and governments on goods and services produced in Canada
- D) expenditure by Canadian households on goods and services produced in Canada and in the rest of the world
- E) expenditure by Canadian households and foreigners on goods and services produced in Canada

Answer: D

Type: MC

45) The purchase of a new home is categorized as \_\_\_\_\_.

- A) consumption expenditure
- B) consumption expenditure and investment
- C) investment only if the home owners take out a mortgage
- D) investment
- E) consumption expenditure only if the home owners do not take out a mortgage

Answer: D

Type: MC

46) Government expenditure on goods and services \_\_\_\_\_.

- A) includes transfer payments
- B) includes expenditure by all levels of government on goods and services
- C) is always greater than consumption expenditure
- D) plus consumption expenditure equals aggregate expenditure
- E) plus consumption expenditure plus investment equals aggregate expenditure

Answer: B

Type: MC

### 20.3 The Uses and Limitations of Real GDP

1) Which of the following items would be included in a current measure of GDP?

- A) Your labour in fixing a leaky pipe under your sink.
- B) The value of safety on the streets of your community.
- C) A professional gardener who regularly cuts your lawn.
- D) The illegal sale of a bag of marijuana.
- E) All of the above.

Answer: C

Diff: 1 Type: MC

Topic: The Uses and Limitations of Real GDP

2) Suppose Angela falls in love with and subsequently marries her regularly employed housekeeper, Tony. What effect would this action have on GDP?

- A) It would stay the same.
- B) It would fall.
- C) It would rise.
- D) It would fall but then increase after the honeymoon was over.
- E) It depends on whether he starts to work in the house free of charge or whether she still pays him.

Answer: E

Diff: 2 Type: MC

Topic: The Uses and Limitations of Real GDP

3) Since non-market exchanges are excluded from measures of GDP, the GDP measure tends to

- A) underestimate the total production of an economy.
- B) overestimate the total production of an economy.
- C) be of little significance in determining the total production of an economy.
- D) be of little use to anyone but market economists.
- E) place too much value on market transactions.

Answer: A

Diff: 2 Type: MC

Topic: The Uses and Limitations of Real GDP

4) Which of the following is *not* a reason for GDP incorrectly measuring the value of total output?

- A) leisure time
- B) household production
- C) underground economic activity
- D) depreciation
- E) environmental quality

Answer: D

Diff: 2 Type: MC

Topic: The Uses and Limitations of Real GDP

Source: Study Guide

5) The existence of which one of the following is *not* a reason for the fact that GDP gives an incorrect estimate of the value of total output in the economy?

- A) social justice
- B) political freedom
- C) health and life expectancy
- D) taxes
- E) leisure time

Answer: D

Diff: 2 Type: MC

Topic: The Uses and Limitations of Real GDP

6) The existence of which one of the following is a reason for the fact that GDP gives an underestimated value of total output in the economy?

- A) pollution
- B) market activities
- C) underground economy
- D) depreciation
- E) environmental problems

Answer: C

Diff: 2 Type: MC

Topic: The Uses and Limitations of Real GDP

7) The maximum level of real GDP that can be produced while avoiding shortages of labour, capital, land, and entrepreneurial ability that would bring rising inflation is

- A) real GDP.
- B) nominal GDP.
- C) actual GDP.
- D) potential GDP.
- E) productive GDP.

Answer: D

Type: MC

Topic: The Uses and Limitations of Real GDP

Skill: Recognition

AACSB: Reflective Thinking

8) In any year, real GDP

- A) must always be less than potential GDP.
- B) might be greater than, less than, or equal to potential GDP.
- C) will always be greater than potential GDP because of the tendency of nations to incur inflation.
- D) always equals potential GDP.
- E) increases if potential GDP increases, and decreases if potential GDP decreases.

Answer: B

Type: MC

Topic: The Uses and Limitations of Real GDP

Skill: Conceptual

AACSB: Reflective Thinking

- 9) The business cycle is defined as the
- A) regular growth rate of the real GDP.
  - B) regular fluctuations of real GDP below potential GDP.
  - C) irregular fluctuations of prices around real GDP.
  - D) periodic but irregular up-and-down movement of total production and other measures of economic activity.
  - E) periodic and regular up-and-down movement of total production.

Answer: D

Type: MC

Topic: The Uses and Limitations of Real GDP

Skill: Recognition

AACSB: Reflective Thinking

- 10) Business cycles are
- A) irregular, with some having two recessions and no expansion.
  - B) predictable, with a recession following a trough.
  - C) unpredictable, but always have two phases and two turning points.
  - D) unpredictable, and don't always have two phases and two turning points.
  - E) predictable with an expansion following a trough.

Answer: C

Type: MC

Topic: The Uses and Limitations of Real GDP

Skill: Recognition

AACSB: Reflective Thinking

- 11) The four parts of the business cycle occur in the following order:
- A) recession, trough, peak, expansion.
  - B) expansion, trough, peak, recession.
  - C) recession, trough, expansion, peak.
  - D) expansion, trough, recession, peak.
  - E) trough, peak, expansion, recession.

Answer: C

Type: MC

Topic: The Uses and Limitations of Real GDP

Skill: Recognition

AACSB: Reflective Thinking

- 12) A recession is a period with
- A) negative growth rate in real GDP that lasts at least one quarter.
  - B) positive growth rate in real GDP that lasts at least one quarter.
  - C) positive growth rate in real GDP that lasts at least two quarters.
  - D) negative growth rate in real GDP that lasts at least two quarters.
  - E) a slowdown in real GDP growth but not necessarily negative real GDP growth.

Answer: D

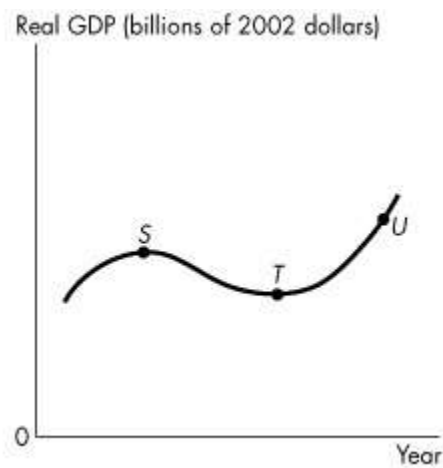
Type: MC

Topic: The Uses and Limitations of Real GDP

Skill: Recognition

AACSB: Reflective Thinking

Use the figure below to answer the following questions.



**Figure 20.3.1**

- 13) Refer to Figure 20.3.1. In the figure, the distance between points *S* and *T* represents
- A) an expansion.
  - B) a trough.
  - C) a peak.
  - D) a recession.
  - E) a business cycle.

Answer: D

Type: MC

Topic: The Uses and Limitations of Real GDP

Skill: Analytical

AACSB: Analytical Skills

- 14) Refer to Figure 20.3.1. In the figure, the distance between points *T* and *U* represents
- A) an expansion.
  - B) a trough.
  - C) a peak.
  - D) a recession.
  - E) a business cycle.

Answer: A

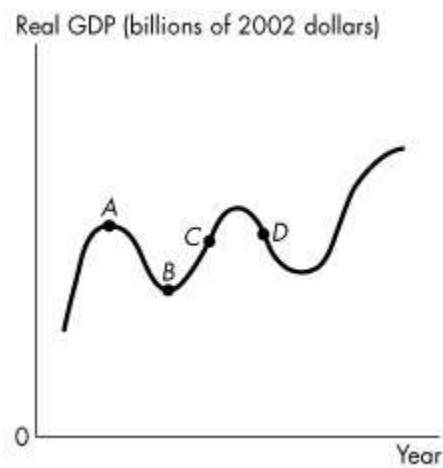
Type: MC

Topic: The Uses and Limitations of Real GDP

Skill: Analytical

AACSB: Analytical Skills

*Use the figure below to answer the following questions.*



**Figure 20.3.2**

- 15) Refer to Figure 20.3.2. In the figure, a recession begins at point \_\_\_\_\_ and an expansion begins at point \_\_\_\_\_.

- A) A; B
- B) B; C
- C) B; A
- D) D; C
- E) C; D

Answer: A

Type: MC

Topic: The Uses and Limitations of Real GDP

Skill: Analytical

AACSB: Analytical Skills

16) Refer to Figure 20.3.2. In the figure, a trough is at point \_\_\_\_\_ and a peak is at point \_\_\_\_\_.

- A) *A; B*
- B) *B; C*
- C) *B; A*
- D) *D; C*
- E) *C; D*

Answer: C

Type: MC

Topic: The Uses and Limitations of Real GDP

Skill: Analytical

AACSB: Analytical Skills

17) In comparing Canada and China we find that

- A) real GDP per person is about the same in the two countries.
- B) Canada's real GDP per person is less than China's real GDP per person once we adjust for currency differences.
- C) China's real GDP per person is less than real GDP per person in Canada.
- D) Canada's real GDP per person is much larger than China's real GDP per person when purchasing power parity prices are used but is less than China's real GDP per person when exchange rate prices are used.
- E) none of the above.

Answer: C

Type: MC

Topic: The Uses and Limitations of Real GDP

Skill: Recognition

AACSB: Reflective Thinking

18) The underground economy is any economic activity that

- A) produces intermediate goods or services.
- B) is not taxed.
- C) is unreported or illegal.
- D) has negative social value.
- E) is conducted underground.

Answer: C

Diff: 1 Type: MC

Topic: The Uses and Limitations of Real GDP

Source: Study Guide

- 19) Given that pollution is a by-product of some production processes,
- A) GDP accountants adjust GDP downward.
  - B) GDP accountants adjust GDP upward.
  - C) GDP accountants do not adjust GDP unless pollution is a serious problem.
  - D) GDP tends to overstate economic well-being.
  - E) GDP tends to understate economic well-being.

Answer: D

Diff: 2 Type: MC

Topic: The Uses and Limitations of Real GDP

Source: Study Guide

- 20) Which of the following statements by politicians is talking about the business cycle?
- A) "Canadian unemployment is falling due to the upturn in the economy."
  - B) "Crime rates increase every spring as the school year ends."
  - C) "An average of 220,000 new jobs are created each year in Canada."
  - D) "More capital investment will create more jobs."
  - E) "Business always rises just before Christmas."

Answer: A

Type: MC

Topic: The Uses and Limitations of Real GDP

Source: Study Guide

- 21) Why is the Human Development Index thought to be a better measure of economic well-being than real GDP per person?
- A) It includes a measure of resource depletion.
  - B) It ignores health, which is hard to measure.
  - C) It includes leisure time and household production.
  - D) It includes health and education measures, as well as real GDP per person.
  - E) It includes only health and education measures, ignoring real GDP per person.

Answer: D

Type: MC

Topic: The Uses and Limitations of Real GDP

Source: Study Guide

- 22) When we use PPP we can make valid international comparisons of real GDP because we
- A) calculate the value of goods and services produced in two countries using the same quantities.
  - B) use data provided by the IMF.
  - C) use the price data provided by the two countries but not the quantities.
  - D) calculate the value of goods and services produced in two countries using the same prices.
  - E) use official government data.

Answer: D

Type: MC

Topic: The Uses and Limitations of Real GDP

Source: MyEconLab

23) All of the following statements are true *except*

A) the Lucas wedge is the dollar value of the accumulated gap between what real GDP per person would have been if the 1960s growth rate had persisted and what real GDP per person turned out to be.

B) the Lucas wedge accumulated to \$400,000 per person by 2010.

C) the Lucas wedge equals real GDP minus potential GDP.

D) the Lucas wedge arises from the slowdown of productivity growth that began during the 1970s.

E) real GDP per person was \$30,700 per year lower in 2010 than it would have been with no growth slowdown.

Answer: C

Type: MC

Topic: The Uses and Limitations of Real GDP

Source: MyEconLab

24) Potential GDP is \_\_\_\_\_.

A) the maximum amount of GDP that can be produced while avoiding shortages of labour, capital, land, and entrepreneurship that would bring rising inflation

B) the same as real GDP

C) the same as nominal GDP

D) equal to real GDP multiplied by the price level

E) equal to nominal GDP multiplied by the price level

Answer: A

Type: MC

25) Real GDP \_\_\_\_\_.

A) fluctuates from year to year but is always below potential GDP

B) grows at a constant 3 percent per year

C) fluctuates around potential GDP

D) equals potential GDP when the price level is constant

E) equals potential GDP in the base year

Answer: C

Type: MC

26) What we produce during our working time is \_\_\_\_\_ as part of GDP and the enjoyment we gain from our leisure time is \_\_\_\_\_ as part of GDP.

A) included; included

B) not included; not included

C) included; not included

D) not included; included

E) included; sometimes but not always included

Answer: C

Type: MC

## 20.4 Mathematical Note: Chained-Dollar Real GDP

Use the table below to answer the following questions.

**Table 20.4.1**

<b>Item</b>	<b>2011 Quantity</b>	<b>2011 Price</b>	<b>2012 Quantity</b>	<b>2012 Price</b>
CD players	10	\$100	15	\$110
bananas	50 bunches	\$2	100 bunches	\$3

1) Refer to Table 20.4.1. In this table, at 2011 prices, the value of production from 2011 to 2012 has increased by

- A) 77.3 percent.
- B) 54.5 percent.
- C) 10.8 percent.
- D) 91.7 percent.
- E) 56 percent.

Answer: B

Diff: 3 Type: MC

Topic: Mathematical Note: Chained-Dollar Real GDP

2) Refer to Table 20.4.1. In this table, at 2012 prices, the value of production from 2011 to 2012 has increased by

- A) 56 percent.
- B) 91.7 percent.
- C) 10.8 percent.
- D) 54.5 percent.
- E) 77.3 percent.

Answer: A

Diff: 3 Type: MC

Topic: Mathematical Note: Chained-Dollar Real GDP

3) Refer to Table 20.4.1. Calculating chained-dollar real GDP, real GDP in 2012 increased by

- A) 56 percent.
- B) 55.25 percent.
- C) 54.5 percent.
- D) 30 percent.
- E) 75 percent.

Answer: B

Diff: 3 Type: MC

Topic: Mathematical Note: Chained-Dollar Real GDP

4) Refer to Table 20.4.1. Chained-dollar real GDP in 2012 is

- A) \$1665.
- B) \$1950.5.
- C) \$1707.75.
- D) \$1250.
- E) \$1100.

Answer: C

Diff: 3 Type: MC

Topic: Mathematical Note: Chained-Dollar Real GDP

5) The reference base year is 2011.

To calculate the chained-dollar real GDP in 2012 we calculate

- A) the value of the final goods and services produced in 2012 valued at the prices that prevailed in 2012.
- B) the value of the final goods and services produced in 2012 valued at the prices that prevailed in the base year.
- C) nominal GDP in 2012 multiplied by price level.
- D) the value of final goods and services produced in the base year valued at the 2012 prices.
- E) the base-year GDP and add the average of the increases in real GDP calculated using 2011 prices and 2012 prices.

Answer: E

Diff: 2 Type: MC

Topic: Mathematical Note: Chained-Dollar Real GDP

Source: Study Guide

6) At 2010 prices, the value of production in 2011 was 2 percentage points higher than in 2010.

At 2011 prices, the value of production in 2011 was 4 percentage points higher than in 2010.

The chained-dollar real GDP is \_\_\_\_\_ in 2011 than in 2010.

- A) 4 percent greater
- B) 3 percent greater
- C) 3 percent smaller
- D) 2 percent smaller
- E) 2 percent greater

Answer: B

Type: MC

Topic: Mathematical Note: Chained-Dollar Real GDP

Source: MyEconLab

Use the table below to answer the following question.

**Table 20.4.2**

<b><i>In 2010</i></b>		
<b><i>Item</i></b>	<b><i>Quantity</i></b>	<b><i>Price</i></b>
Digital cameras	7	\$2 each
Chocolate bars	2	\$1 each
Watches	3	\$3 each

<b><i>In 2011</i></b>		
<b><i>Item</i></b>	<b><i>Quantity</i></b>	<b><i>Price</i></b>
Digital cameras	1	\$9 each
Chocolate bars	6	\$8 each
Watches	9	\$10 each

7) Refer to Table 20.4.2. An economy produces only digital cameras, chocolate bars, and watches.

The table gives the quantities produced and prices in 2010 and 2011.

The base year is 2010.

The chained-dollar real GDP in 2011 is

A) \$34.

B) \$25.

C) \$147.

D) \$109.

E) \$36.

Answer: A

Type: MC

Topic: Mathematical Note: Chained-Dollar Real GDP

Source: MyEconLab

Use the table below to answer the following question.

**Table 20.4.3**

<b><i>In 2010</i></b>		
<b><i>Item</i></b>	<b><i>Quantity</i></b>	<b><i>Price</i></b>
Cell phones	2	\$1 each
Pens	9	\$1 each
Pizza	4	\$1 each

<b><i>In 2011</i></b>		
<b><i>Item</i></b>	<b><i>Quantity</i></b>	<b><i>Price</i></b>
Cell phones	8	\$7 each
Pens	4	\$6 each
Pizza	9	\$5 each

8) Refer to Table 20.4.3. An economy produces only cell phones, pens, and pizza. The table gives the quantities produced and prices in 2010 and 2011. The base year is 2010.

The chained-dollar real GDP in 2011 is

- A) \$13.
- B) \$21.
- C) \$125.
- D) \$88.
- E) \$19.

Answer: B

Type: MC

Topic: Mathematical Note: Chained-Dollar Real GDP

Source: MyEconLab

Use the table below to answer the following question.

**Table 20.4.4**

<i>Quantities</i>	<i>2011</i>	<i>2012</i>
Bananas	1,000 bunches	1,100 bunches
Coconuts	500 bunches	525 bunches

<i>Prices</i>	<i>2011</i>	<i>2012</i>
Bananas	\$2 a bunch	\$3 a bunch
Coconuts	\$10 a bunch	\$8 a bunch

9) Refer to Table 20.4.4. The table provides data on the economy of Tropical Republic that produces only bananas and coconuts.

Nominal GDP in 2011 is \_\_\_\_\_. Nominal GDP in 2012 is \_\_\_\_\_. The chained-dollar real GDP in 2012 expressed in 2011 dollars is \_\_\_\_\_.

- A) \$7,500; \$7,000; \$7,472.50
- B) \$7,472.50; \$7,000; \$7,500
- C) \$7,000; \$7,500; \$7,472.50
- D) \$7,472.50; \$7,500; \$7,000
- E) \$1,500; \$1,625; \$1,575

Answer: C

Type: MC

Topic: Mathematical Note: Chained-Dollar Real GDP

Source: MyEconLab

## **Chapter 21 Monitoring Jobs and Inflation**

### 21.1 Employment and Unemployment

1) The working-age population is the total number of people

- A) in the labour force.
- B) in the labour force who are employed.
- C) aged 15 years and over.
- D) in the labour force, aged 15 years and over.
- E) in the labour force, aged 15 years and over, and employed.

Answer: C

Diff: 1 Type: MC

Topic: Employment and Unemployment

2) Which one of the following people would be counted as unemployed in Canada?

- A) Veena is not working, but she is looking for a full-time job.
- B) Kathy has stopped looking for work since she was unable to find a suitable job during a one-month search.
- C) Sharon is a college student with a job.
- D) Christos has been laid off from his job a month ago, and has not been looking for a new job as he is waiting for a severance package from his former employer.

E) Benoit who was laid off when his firm closed down 2 months ago and has not been looking for work as he is going back to school.

Answer: A

Diff: 2 Type: MC

Topic: Employment and Unemployment

3) Which one of the following people would be counted as unemployed in Canada?

A) Doris works only 5 hours a week but is looking for a full-time job.

B) Kanhaya has stopped looking for work since he was unable to find a suitable job during a two-month search.

C) Sharon recently began looking for work after staying at home for 10 years to look after her children.

D) Maurice is on a 2 month vacation out of the country but is still looking for a job using the internet.

E) Taylor is a homemaker.

Answer: C

Diff: 2 Type: MC

Topic: Employment and Unemployment

- 4) Which one of the following people would be counted as unemployed in Canada?
- A) Simone is currently working but expects to be laid off by the end of the month, before next month's survey can be completed.
  - B) Ruth is a 14-year-old student and has been looking for an after-school job every day for the past month.
  - C) Sarah has been looking for a job but is taking a month-long break from the job-seeking effort due to her lack of skills.
  - D) Rebekah is a recent graduate looking for work.
  - E) Ron has quit looking because he believes that there is no work available for him.

Answer: D

Diff: 2 Type: MC

Topic: Employment and Unemployment

- 5) Which one of the following people would be counted as unemployed in Canada?
- A) a part-time worker who repeatedly expresses a desire to become a full-time worker
  - B) a person who has been seeking a job for the last six months, but recently gave up looking because he was discouraged by his job prospects
  - C) a person who will be starting a new job in 6 months
  - D) a person who expects to be laid off by the end of the month before next month's survey can be completed
  - E) a person who has been laid off for 10 weeks and is not looking for a job because he is waiting to be called back to his old job

Answer: E

Diff: 2 Type: MC

Topic: Employment and Unemployment

- 6) The labour force is
- A) the total number of people employed.
  - B) the total number of people aged 15 years and over.
  - C) the total number of people in the working-age population who are employed.
  - D) the total number of people in the working-age population who are either employed or unemployed.
  - E) none of the above.

Answer: D

Diff: 1 Type: MC

Topic: Employment and Unemployment

- 7) The unemployment rate is defined as the number of
- A) unemployed people divided by the number of employed people.
  - B) employed people divided by the number of people in the country.
  - C) unemployed people divided by the number of people in the country.
  - D) unemployed people divided by the sum of the people employed and the people unemployed.
  - E) unemployed people divided by the number of people in the country who are employed.

Answer: D

Diff: 1 Type: MC

Topic: Employment and Unemployment

8) Counting involuntary part-time workers as unemployed would

- A) not change the actual unemployment rate.
- B) lower the measured unemployment rate.
- C) raise the natural unemployment rate.
- D) raise the full employment rate.
- E) raise the measured unemployment rate.

Answer: E

Diff: 2 Type: MC

Topic: Employment and Unemployment

9) Who of the following would be counted as unemployed in Canada?

- A) Doris only works five hours a week but is looking for a full-time job.
- B) Kanhaya has stopped looking for work since he was unable to find a suitable job during a two-month search.
- C) Sharon is a college student with no job.
- D) Maurice has been laid off from his job for 20 weeks but expects to be called back soon.
- E) Bogdan has been laid off from his job but does not expect to be called back, and is not looking.

Answer: D

Diff: 2 Type: MC

Topic: Employment and Unemployment

Source: Study Guide

10) Who of the following would be counted as unemployed in Canada?

- A) Caitlin, who is 14 years old, and looking for a babysitting job.
- B) James, who is a full-time student looking for a part-time job.
- C) Youngmin, who is a part-time hamburger flipper looking for a full-time job.
- D) Emmanuel, who lost his job at the steel plant when an automated assembly line was introduced six months ago, and has been job searching every day.
- E) Vik, who has been staying at home watching "The Old and the Boring" soap opera, and not searching since he was laid off at the flour mill.

Answer: D

Diff: 2 Type: MC

Topic: Employment and Unemployment

11) If the working-age population increases, then

- A) the size of the labour force will increase.
- B) the number of people employed will increase.
- C) the unemployment rate will increase.
- D) the labour force participation rate will increase.
- E) the total number of people aged 15 years and above will increase.

Answer: E

Diff: 2 Type: MC

Topic: Employment and Unemployment

12) In a country with a working-age population of 20 million, 13 million are employed, 1.5 million are unemployed, and 1 million of the employed are working part-time, half of whom wish to work full-time. The size of the labour force is

- A) 20 million.
- B) 15.5 million.
- C) 14.5 million.
- D) 13 million.
- E) 11.5 million.

Answer: C

Diff: 2 Type: MC

Topic: Employment and Unemployment

Source: Study Guide

13) In a country with a working-age population of 20 million, 13 million are employed, 1.5 million are unemployed, and 1 million of the employed are working part-time, half of whom wish to work full-time. The labour force participation rate is

- A) 75.5 percent.
- B) 72.5 percent.
- C) 65 percent.
- D) 57.5 percent.
- E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: Employment and Unemployment

Source: Study Guide

14) In a country with a working-age population of 22 million, 16 million are employed, 2 million are unemployed, and 1 million of the employed are working part-time, half of whom wish to work full-time. The unemployment rate is

- A) 10 percent.
- B) 10.3 percent.
- C) 11.1 percent.
- D) 15.4 percent.
- E) none of the above.

Answer: C

Diff: 2 Type: MC

Topic: Employment and Unemployment

15) In a country with a working-age population of 22 million, 16 million are employed, 2 million are unemployed, and 1 million of the employed are working part-time, half of whom wish to work full-time. The employment-to-population ratio is

- A) 72.7 percent.
- B) 65 percent.
- C) 75.5 percent.
- D) 57.5 percent.
- E) none of the above.

Answer: A

Diff: 2 Type: MC

Topic: Employment and Unemployment

16) In a country with a working-age population of 22 million, 16 million are employed, 2 million are unemployed, and 1 million of the employed are working part-time, half of whom wish to work full-time. The involuntary part-time rate is

- A) 6.3 percent.
- B) 12.5 percent.
- C) 2.8 percent.
- D) 5 percent.
- E) none of the above.

Answer: C

Diff: 3 Type: MC

Topic: Employment and Unemployment

17) In a country with a working-age population of 30 million, 18 million are employed, 2 million are unemployed, and 2 million of the employed are working part-time, half of whom wish to work full-time. The labour force is

- A) 30 million.
- B) 18 million.
- C) 20 million.
- D) 22 million.
- E) 16 million.

Answer: C

Diff: 1 Type: MC

Topic: Employment and Unemployment

18) In a country with a working-age population of 30 million, 18 million are employed, 2 million are unemployed, and 2 million of the employed are working part-time, half of whom wish to work full-time. The labour force participation rate is

- A) 73.3 percent.
- B) 66.7 percent.
- C) 60 percent.
- D) 53.3 percent.
- E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: Employment and Unemployment

19) In a country with a working-age population of 30 million, 18 million are employed, 2 million are unemployed, and 2 million of the employed are working part-time, half of whom wish to work full-time. The unemployment rate is

- A) 10 percent.
- B) 9.1 percent.
- C) 14.3 percent.
- D) 11.1 percent.
- E) none of the above.

Answer: A

Diff: 2 Type: MC

Topic: Employment and Unemployment

20) In a country with a working-age population of 30 million, 18 million are employed, 2 million are unemployed, and 2 million of the employed are working part-time, half of whom wish to work full-time. The employment-to-population ratio is

- A) 73.3 percent.
- B) 66.7 percent.
- C) 60 percent.
- D) 53.3 percent.
- E) none of the above.

Answer: C

Diff: 2 Type: MC

Topic: Employment and Unemployment

21) In a country with a working-age population of 30 million, 18 million are employed, 2 million are unemployed, and 2 million of the employed are working part-time, half of whom wish to work full-time. The involuntary part-time rate is

- A) 10 percent.
- B) 5 percent.
- C) 4.8 percent.
- D) 4.5 percent.
- E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: Employment and Unemployment

22) Which of the following reflects an increase in unemployment?

- A) an increase in the employment-to-population ratio
- B) a decrease in the unemployment rate
- C) an increase in the labour force participation rate
- D) an increase in the involuntary part-time rate
- E) none of the above

Answer: E

Diff: 2 Type: MC

Topic: Employment and Unemployment

23) The labour force participation rate is

- A) the percentage of the working-age population who are employed.
- B) the percentage of the labour force who are unemployed or employed.
- C) the percentage of the working-age population who are either unemployed or employed.
- D) the percentage of the labour force who are employed.
- E) none of the above.

Answer: C

Diff: 2 Type: MC

Topic: Employment and Unemployment

24) The employment-to-population ratio is

- A) the percentage of the working-age population who are employed.
- B) the percentage of the labour force who are unemployed or employed.
- C) the percentage of the working-age population who are unemployed or employed.
- D) the percentage of the labour force who are employed.
- E) none of the above.

Answer: A

Diff: 1 Type: MC

Topic: Employment and Unemployment

25) In a recession, typically

- A) unemployment rises.
- B) the employment-to-population ratio decreases.
- C) the employment-to-population rate rises.
- D) the labour force participation rate rises.
- E) both A and B are correct.

Answer: E

Diff: 2 Type: MC

Topic: Employment and Unemployment

26) In a recession, typically

- A) unemployment decreases.
- B) the labour force participation rate increases.
- C) the employment-to-population ratio decreases.
- D) the employment-to-population ratio increases.
- E) none of the above.

Answer: C

Diff: 1 Type: MC

Topic: Employment and Unemployment

27) Complete the following sentence. In an expansion, typically

- A) unemployment increases.
- B) the labour force participation rate increases.
- C) the employment-to-population ratio decreases.
- D) employment decreases.
- E) both B and D are correct.

Answer: B

Diff: 1 Type: MC

Topic: Employment and Unemployment

28) Which of the following pieces of information do you need to calculate the labour force participation rate?

- I. the number of employed persons
- II. the number of unemployed persons
- III. the population
- IV. the working age population

- A) I and II
- B) I and III
- C) I, II and III
- D) I, II and IV
- E) all of the above

Answer: D

Type: MC

Topic: Employment and Unemployment

Skill: Recognition

AACSB: Reflective Thinking

29) Since 1960, Canadian labour force participation rate has \_\_\_\_\_ and the unemployment rate has \_\_\_\_\_.

- A) trended higher; trended higher
- B) trended lower; varied over the business cycle
- C) varied over the business cycle; trended higher
- D) trended higher; varied over the business cycle
- E) trended higher; trended lower

Answer: D

Type: MC

Topic: Employment and Unemployment

Skill: Recognition

AACSB: Reflective Thinking

- 30) If the people who take early retirement are not counted in the working-age population, then
- A) the unemployment rate would be lower.
  - B) the labour force participation rate would be less.
  - C) the unemployment rate would be higher.
  - D) the labour force participation rate would be higher.
  - E) none of the above.

Answer: D

Type: MC

Topic: Employment and Unemployment

Skill: Conceptual

AACSB: Reflective Thinking

- 31) If the labour force participation rate is rising and the working-age population is not changing, then the

- A) size of the labour force is rising.
- B) number of unemployed people is rising and the size of the labour force is falling.
- C) size of the labour force is falling.
- D) number of unemployed people is falling and the size of the labour force is rising.
- E) number of employed people must be increasing.

Answer: A

Type: MC

Topic: Employment and Unemployment

Skill: Analytical

AACSB: Reflective Thinking

- 32) The working-age population can be divided into two groups:

- A) those who are employed and those who are unemployed.
- B) those in the labour force and discouraged workers.
- C) those who work full time and those who work part time.
- D) those in the labour force and those not in the labour force.
- E) those who are over the age of 15 and those who are under the age of 15.

Answer: D

Type: MC

- 33) Which of the following statements is incorrect?

- A) The labour force is equal to the number of people employed plus the number of people unemployed.
- B) The unemployment rate is the number of persons who are unemployed divided by the labour force, all multiplied by 100.
- C) The labour-force participation rate is the labour force divided by the working-age population, all multiplied by 100.
- D) The employment-to-population ratio is the number of people employed divided by the working-age population, all multiplied by 100.
- E) The involuntary part-time rate is the number of involuntary part-time workers divided by the number employed, all multiplied by 100.

Answer: E

Type: MC

34) Which of the following is *NOT* included in the working-age population?

- A) discouraged workers
- B) involuntary part-time workers
- C) retired workers
- D) students over the age of 15
- E) All of the above are included in the working-age population.

Answer: E

Type: MC

35) Suppose the working-age population in Tiny Town is 100 people. If 25 of these people are not in the labour force, the \_\_\_\_\_ equals \_\_\_\_\_.

- A) labour force; 75 people
- B) unemployment rate; 25 percent
- C) unemployment rate; 33 percent
- D) employment-to-population ratio; 25 percent
- E) employment-to-population ratio; 75 percent

Answer: A

Type: MC

## 21.2 Unemployment and Full Employment

1) In a country with a working-age population of 22 million, 16 million are employed, 2 million are unemployed, and 1 million of the employed are working part-time, half of whom wish to work full-time. If 500,000 of those unemployed are cyclically unemployed, what is the natural unemployment rate?

- A) 11.1 percent
- B) 5.6 percent
- C) 8.3 percent
- D) 9.4 percent
- E) none of the above

Answer: C

Diff: 3 Type: MC

Topic: Unemployment and Full Employment

2) In a country with a working-age population of 30 million, 18 million are employed, 2 million are unemployed, and 2 million of the employed are working part-time, half of whom wish to work full-time. If 1 million of those unemployed are cyclically unemployed, what is the natural unemployment rate?

- A) 5.6 percent
- B) 5 percent
- C) 6.7 percent
- D) 11.1 percent
- E) none of the above

Answer: B

Diff: 3 Type: MC

Topic: Unemployment and Full Employment

3) Which one of the following people is structurally unemployed?

- A) a Saskatchewan welder who lost her job when her company relocated to B. C. and is currently looking for a job
- B) a Nova Scotia fishery worker who is searching for a better job closer to home
- C) a steel worker who is laid off but who expects to be called back soon
- D) an office worker who has lost her job because of a general slowdown in economic activity
- E) none of the above

Answer: A

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

Source: Study Guide

4) Unemployment caused by permanently decreased demand for horse-drawn carriages is an example of

- A) cyclical unemployment.
- B) seasonal unemployment.
- C) frictional unemployment.
- D) structural unemployment.
- E) discouraged unemployment.

Answer: D

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

Source: Study Guide

5) Which one of the following people is cyclically unemployed?

- A) a Saskatchewan welder who lost her job when her company relocated to B. C. and is currently looking for a job
- B) a Nova Scotia fishery worker who is searching for a better job closer to home
- C) a steel worker who is laid off but who expects to be called back soon
- D) an office worker who has lost her job because of a general slowdown in economic activity
- E) none of the above

Answer: D

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

Source: Study Guide

6) Which one of the following people is frictionally unemployed? A steel worker who

- A) loses her job because of technological change.
- B) is laid off but expects to be called back soon.
- C) gives up her job because she retires.
- D) decides to leave the labour force and become a full-time ballet student.
- E) becomes discouraged and stops looking for a job.

Answer: B

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

Source: Study Guide

7) If the economy is at full employment, then

- A) the entire population is employed.
- B) the entire labour force is employed.
- C) the only unemployment is frictional unemployment plus discouraged workers.
- D) the unemployment rate is less than 3 percent.
- E) all unemployment arises from normal frictions and structural change.

Answer: E

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

- 8) The natural unemployment rate is
- A) equal to 0 percent.
  - B) the same as the cyclical unemployment rate.
  - C) the rate at which cyclical unemployment is equal to 6 percent.
  - D) the rate at which cyclical unemployment is equal to 0 percent.
  - E) none of the above.

Answer: D

Diff: 1 Type: MC

Topic: Unemployment and Full Employment

Source: Study Guide

- 9) At full employment, there is no
- A) natural unemployment.
  - B) unemployment.
  - C) cyclical unemployment.
  - D) structural unemployment.
  - E) frictional unemployment.

Answer: C

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

Source: Study Guide

- 10) A zero percent unemployment rate
- A) is one of the economic goals of the Canadian government.
  - B) would alleviate scarcity.
  - C) is not consistent with the notion of full employment.
  - D) was last achieved during World War II when everyone was willing to work at the going wage rate to end the war.
  - E) is the only efficient unemployment rate.

Answer: C

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

- 11) Complete the following sentence. Full employment
- A) occurs when all unemployment is cyclical and structural.
  - B) occurs when all unemployment is frictional and discouraged.
  - C) occurs when there is zero unemployment.
  - D) occurs when there is zero frictional unemployment.
  - E) occurs when there is zero cyclical unemployment.

Answer: E

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

Use the table below to answer the following questions.

**Table 21.2.1**

This table shows the answers given by interviewees to the Labour Force Survey

---

Person A	Now that kids are in school full-time, this person is looking for work and has been interviewed for three jobs over the past 2 weeks.
Person B	This person has been laid off but expects to be called back in a few weeks, just as soon as the economy improves.
Person C	This person has just graduated from university and will start a new job in 8 weeks. In the meantime, this person is surveying local drinking establishments.
Person D	This person was laid off last year when new equipment at the plant reduced the number of jobs. Since his layoff, this person has been constantly job searching.
Person E	This economics graduate is working two nights a week at the 7-11, but wants full-time work as an economist.

---

12) In Table 21.2.1, which person is frictionally unemployed?

- A) A
- B) B
- C) C
- D) E
- E) none of them

Answer: A

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

13) In Table 21.2.1, which person is structurally unemployed?

- A) A
- B) B
- C) C
- D) D
- E) none of them

Answer: D

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

14) In Table 21.2.1, which person is cyclically unemployed?

- A) A
- B) B
- C) C
- D) D and B
- E) A and C

Answer: B

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

15) In Table 21.2.1, which person is a discouraged worker?

- A) A
- B) B
- C) C
- D) D
- E) none of them

Answer: E

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

16) Structural unemployment arises in part because

- A) there are not enough jobs available.
- B) of technological change.
- C) people become discouraged when they cannot find jobs.
- D) people will not quit their present jobs until they can find suitable employment elsewhere.
- E) of unrealistic wage expectations.

Answer: B

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

17) Full employment does not mean that there is zero unemployment because

- A) some cyclical unemployment is always present.
- B) some frictional and structural unemployment is always present.
- C) business fluctuations are inevitable.
- D) of the existence of discouraged workers.
- E) of unrealistic wage expectations.

Answer: B

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

- 18) In a dynamic economy under ideal conditions, the unemployment rate
- A) should be zero.
  - B) is greater than zero percent due to natural unemployment.
  - C) increases as the price level rises.
  - D) decreases as the price level falls.
  - E) averages 6 percent.

Answer: B

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

- 19) If the economy is operating at full employment, then
- A) everyone who wants a job has one.
  - B) the entire labour force is employed.
  - C) the unemployment rate is approximately 3 percent.
  - D) the unemployment rate is zero.
  - E) none of the above.

Answer: E

Diff: 1 Type: MC

Topic: Unemployment and Full Employment

- 20) Jesse just graduated from university, and is looking for her first job. Jesse is
- A) frictionally unemployed.
  - B) structurally unemployed.
  - C) not unemployed.
  - D) cyclically unemployed.
  - E) not in the labour force.

Answer: A

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

- 21) Caitlin is working part-time at the Mr. G store, but wants to work full-time. She is
- A) frictionally unemployed.
  - B) structurally unemployed.
  - C) not in the labour force.
  - D) cyclically unemployed.
  - E) none of the above.

Answer: E

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

22) Michael lost his job as a night security guard because he kept falling asleep at the job. Now he is looking for a new job. Michael is

- A) frictionally unemployed.
- B) structurally unemployed.
- C) not unemployed.
- D) cyclically unemployed.
- E) none of the above.

Answer: A

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

23) Rochelle lost her job as a salesperson when sales fell off during the recession. Now she is looking for a new job. Rochelle is

- A) frictionally unemployed.
- B) structurally unemployed.
- C) not unemployed.
- D) cyclically unemployed.
- E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

24) Henelyn lost her job as a factory worker when she was replaced by a robotic machine. Now she is looking for a new job. Henelyn is

- A) frictionally unemployed.
- B) structurally unemployed.
- C) not unemployed.
- D) cyclically unemployed.
- E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

25) People become unemployed when they

- A) retire.
- B) are on maternity leave.
- C) quit working to go to university.
- D) leave university and start seeking work.
- E) all of the above.

Answer: D

Diff: 1 Type: MC

Topic: Unemployment and Full Employment

26) People end unemployment when they

- A) retire from a job.
- B) quit work to go to school.
- C) quit work to raise a family.
- D) are recalled from a layoff.
- E) are laid off.

Answer: D

Diff: 1 Type: MC

Topic: Unemployment and Full Employment

27) Counting discouraged workers as unemployed would

- A) not change the measured unemployment rate.
- B) lower the measured unemployment rate.
- C) raise the natural unemployment rate.
- D) raise the full employment rate.
- E) raise the measured unemployment rate.

Answer: E

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

Source: Study Guide

28) If the number of discouraged workers increases, everything else remaining the same, then the

- A) unemployment rate will increase.
- B) employment-to-population ratio will decrease.
- C) labour force participation rate will increase.
- D) labour force participation rate will decrease.
- E) employment-to-population ratio will increase.

Answer: D

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

Source: Study Guide

29) If the number of discouraged workers decreases because many of them start to look for work, everything else remaining the same, then the

- A) unemployment rate will increase.
- B) employment-to-population ratio will decrease.
- C) labour force participation rate will increase.
- D) labour force participation rate will decrease.
- E) both A and C.

Answer: E

Diff: 2 Type: MC

Topic: Unemployment and Full Employment

30) Suppose the economy is experiencing frictional unemployment of 1 percent, structural unemployment of 3 percent and cyclical unemployment of 4 percent. What is the natural unemployment rate?

- A) 3 percent
- B) 4 percent
- C) 5 percent
- D) 7 percent
- E) 8 percent

Answer: B

Type: MC

Topic: Unemployment and Full Employment

Skill: Analytical

AACSB: Reflective Thinking

31) Suppose that the natural unemployment rate is 4.5 percent and the actual unemployment rate is 3.5 percent. Then cyclical unemployment is

- A) 1 percent.
- B) -1 percent.
- C) 8 percent.
- D) 0 percent.
- E) 3.5 percent.

Answer: B

Type: MC

Topic: Unemployment and Full Employment

Skill: Analytical

AACSB: Reflective Thinking

32) Suppose that the unemployment rate equals 4.5 percent and that the natural unemployment rate is 5.5 percent. We can conclude that

- A) potential GDP is greater than real GDP.
- B) potential GDP equals real GDP.
- C) potential GDP is less than real GDP.
- D) we have mismeasured the natural unemployment rate.
- E) real GDP is greater than nominal GDP.

Answer: C

Type: MC

Topic: Unemployment and Full Employment

Skill: Conceptual

AACSB: Reflective Thinking

- 33) If the economy is at full employment,
- A) the entire population is employed.
  - B) the entire labour force is employed.
  - C) the only unemployment is frictional unemployment plus discouraged workers.
  - D) real GDP equals potential GDP.
  - E) all unemployment is cyclical and structural.

Answer: D

Type: MC

Topic: Unemployment and Full Employment

Skill: Recognition

AACSB: Reflective Thinking

- 34) When the unemployment rate is less than the natural unemployment rate, real GDP is \_\_\_\_\_ than potential GDP and the output gap is \_\_\_\_\_.

- A) greater; positive
- B) smaller; positive
- C) greater; negative
- D) smaller; negative
- E) greater; equal to zero

Answer: A

Type: MC

Topic: Unemployment and Full Employment

Skill: Recognition

Source: MyEconLab

AACSB: Reflective Thinking

- 35) When the unemployment rate \_\_\_\_\_ the natural unemployment rate, real GDP \_\_\_\_\_ potential GDP.

- A) equal; is less than
- B) is greater than; is less than
- C) is less than; is less than
- D) equals; is greater than
- E) is greater than; equals

Answer: B

Type: MC

Topic: Unemployment and Full Employment

Skill: Recognition

Source: MyEconLab

AACSB: Reflective Thinking

36) Some unemployment is unavoidable because \_\_\_\_\_.

- A) people are making transitions through the stages of life and businesses are making transitions
- B) many part-time workers would like to have full-time work
- C) often people become discouraged workers
- D) many people in the working-age population attend school and are unemployed
- E) there is always some cyclical unemployment

Answer: A

Type: MC

Topic: Unemployment and Full Employment

Skill: Recognition

Source: MyEconLab

AACSB: Reflective Thinking

37) The official unemployment rate might underestimate the underutilization of labour resources for all of the following reasons *except* \_\_\_\_\_.

- A) it excludes part-time workers who want full-time jobs
- B) it excludes discouraged workers
- C) it excludes marginally attached workers
- D) it excludes people who are waiting to be called back to jobs from which they have been laid off
- E) the official unemployment rate excludes all of the above

Answer: D

Type: MC

Topic: Unemployment and Full Employment

Skill: Recognition

Source: MyEconLab

AACSB: Reflective Thinking

38) The unemployment rate is supposed to measure \_\_\_\_\_. It is an imperfect measure because \_\_\_\_\_.

- A) the number of unemployed plus the number of marginally attached workers expressed as a percentage of the labour force; it excludes the marginally attached workers because Statistics Canada considers them as employed
- B) the percentage of the working-age population who are unemployed; it is impossible to count everyone in the working-age population
- C) the percentage of the labour force who are unemployed; it is impossible to count everyone in the labour force
- D) the underutilization of labour resources; it excludes some underutilized labour and some unemployment is unavoidable
- E) the underutilization of labour resources; it includes part-time workers and excludes discouraged workers

Answer: D

Type: MC

Topic: Unemployment and Full Employment

Skill: Recognition

Source: MyEconLab

AACSB: Reflective Thinking

39) The three types of unemployment are

- A) frictional, structural, and involuntary.
- B) voluntary, involuntary, and natural.
- C) voluntary, involuntary, and cyclical.
- D) frictional, structural, and cyclical.
- E) cyclical, maternity leave, and paternity leave.

Answer: D

Type: MC

40) Frictional unemployment \_\_\_\_\_.

- A) includes discouraged workers
- B) is voluntary part-time unemployment
- C) includes workers who have lost their jobs due to an economic downturn
- D) is unemployment associated with normal labour turnover
- E) occurs when changes in technology change the skills needed to perform jobs

Answer: D

Type: MC

41) Suppose the country of Tiny Town experiences frictional unemployment. This frictional unemployment would

- A) signal that the country is in a recession.
- B) be considered a natural occurrence in a growing economy.
- C) signal the number of discouraged workers is growing.
- D) increase structural unemployment.
- E) decrease the output gap.

Answer: B

Type: MC

### 21.3 The Price Level, Inflation, and Deflation

- 1) The reference base period is 2002. A consumer price index of 122 in 2012 means that
- A) prices of consumer goods have gone up by a factor of 12.2.
  - B) if the price of a good was \$100 in 2002, its price in 2012 is \$122.
  - C) prices of consumer goods have more than doubled.
  - D) the market basket of consumer goods that cost \$122 in 2002 can be purchased for \$100 in 2012.
  - E) the average of the prices paid by urban consumers for a fixed market basket of consumer goods and services was 22 percent higher in 2012 than it was on average during 2002.

Answer: E

Diff: 1 Type: MC

Topic: The Price Level and Inflation

- 2) If the CPI was 128 at the end of 2011 and 136 at the end of 2012, what was the inflation rate in 2012?

- A) 4.2 percent
- B) 5.9 percent
- C) 6.25 percent
- D) 8 percent
- E) 9.4 percent

Answer: C

Diff: 2 Type: MC

Topic: The Price Level and Inflation

- 3) If the CPI was 95 at the end of 2011 and 105 at the end of 2012, what was the inflation rate in 2012?

- A) 10 percent
- B) 105 percent
- C) 9.5 percent
- D) 5 percent
- E) 10.5 percent

Answer: E

Diff: 2 Type: MC

Topic: The Price Level and Inflation

- 4) If the CPI was 228 at the end of 2011 and 236 at the end of 2012, what was the inflation rate in 2012?

- A) 8 percent
- B) 236 percent
- C) 3.5 percent
- D) 3.4 percent
- E) 4 percent

Answer: C

Diff: 2 Type: MC

Topic: The Price Level and Inflation

5) If the CPI was 140 at the end of 2011 and 150 at the end of 2012, what was the inflation rate in 2012?

- A) 7.14 percent
- B) 10 percent
- C) 6.25 percent
- D) 8 percent
- E) 6.67 percent

Answer: A

Diff: 2 Type: MC

Topic: The Price Level and Inflation

6) If the CPI was 180 at the end of 2011, and 216 at the end of 2012, the inflation rate in 2012 was

- A) 216 percent.
- B) 36 percent.
- C) 16.67 percent.
- D) 20 percent.
- E) 18 percent.

Answer: D

Diff: 2 Type: MC

Topic: The Price Level and Inflation

7) The cost of the CPI basket in base-period prices is \$200 and the cost of the CPI basket in current-period prices is \$450. The CPI in the current year is

- A) 450.
- B) 225.
- C) 300.
- D) 250.
- E) 44.44.

Answer: B

Diff: 2 Type: MC

Topic: The Price Level and Inflation

8) The consumer price index is a measure of

- A) the average of the prices paid by urban consumers for a fixed basket of consumer goods and services.
- B) the commodity prices paid by urban consumers for a fixed basket of consumer goods and services.
- C) the consumer prices paid by average households for a fixed basket of goods and services.
- D) the average of the prices paid by rural consumers for a fixed basket of consumer goods and services.
- E) the lowest prices paid by urban consumers for a fixed basket of consumer goods and services.

Answer: A

Diff: 2 Type: MC

Topic: The Price Level and Inflation

- 9) The inflation rate measures
- A) the annual change in the price level.
  - B) the annual percentage change in the price level.
  - C) the average price level.
  - D) the annual percentage change in the wage rate.
  - E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: The Price Level and Inflation

*Use the table below to answer the following questions.*

**Table 21.3.1**

Suppose a simple economy produces three goods only.  
The price and output data for some selected years are shown below.

	Price (dollars)	Price (dollars)	Quantity (number)	Quantity (number)
	2002	2012	2002	2012
Pop	0.75	1.10	100	120
Crackers	1.25	2.10	300	280
Cucumbers	2.00	3.00	200	190

- 10) Refer to Table 21.3.1. The reference base period is 2002. The CPI in 2012 is
- A) 1,340.
  - B) 158.
  - C) 100.
  - D) 96.
  - E) 63.

Answer: B

Diff: 3 Type: MC

Topic: The Price Level and Inflation

- 11) Refer to Table 21.3.1. The reference base period is 2002. Which one of the following statements is true?
- A) From 2002 to 2012, the cost of the market basket rose by 58 percent.
  - B) It costs 158 times more in 2012 than it does in 2002 to buy the same market basket.
  - C) All prices have risen by the same amount.
  - D) The inflation rate in 2012 is greater than the inflation rate in 2002.
  - E) The inflation rate in 2002 is greater than the inflation rate in 2012.

Answer: A

Diff: 3 Type: MC

Topic: The Price Level and Inflation

- 12) Refer to Table 21.3.1. The reference base period is 2002. the CPI in 2002 is
- A) 1,340.
  - B) 158.
  - C) 100.
  - D) 96.
  - E) 63.

Answer: C

Diff: 2 Type: MC

Topic: The Price Level and Inflation

- 13) Refer to Table 21.3.1. The reference base period is 2008. The CPI in 2002 is
- A) 100.
  - B) 157.
  - C) 129.
  - D) 63.
  - E) 152.

Answer: D

Diff: 3 Type: MC

Topic: The Price Level and Inflation

- 14) Refer to Table 21.3.1. The reference base period is 2012. The CPI in 2012 is
- A) 100.
  - B) 157.
  - C) 129.
  - D) 64.
  - E) 153.

Answer: A

Diff: 2 Type: MC

Topic: The Price Level and Inflation

- 15) If the CPI in 2008 was 100 and the CPI in 2006 was 115, then the inflation rate in 2006 is
- A) 1.5 percent.
  - B) 100 percent.
  - C) 11.5 percent.
  - D) 115 percent.
  - E) none of the above.

Answer: E

Diff: 2 Type: MC

Topic: The Price Level and Inflation

16) The fixed basket of Econoland consists of 10 units of *A*, 20 units of *B*, and 30 units of *C*. Current prices are \$1 per unit of *A*, \$2 per unit of *B*, and \$3 per unit of *C*. Base year prices are \$1 for each unit of *A*, *B*, and *C*. What is the CPI in the current year?

- A) 43
- B) 100
- C) 233
- D) 430
- E) 140

Answer: C

Diff: 3 Type: MC

Topic: The Price Level and Inflation

17) The Consumer Price Index measures inflation by using

- A) all goods and services that are produced using a current-year basket.
- B) all goods and services that are produced using a base-year basket.
- C) only consumption goods and services purchased using a current-year basket.
- D) only consumption goods and services purchased using a base-year basket.
- E) A and D.

Answer: D

Diff: 2 Type: MC

Topic: The Price Level and Inflation

18) The technique used to calculate the CPI implicitly assumes that consumers buy

- A) relatively more of goods with relative prices that are increasing.
- B) relatively less of goods with relative prices that are decreasing.
- C) the same relative quantities of goods as in a base year.
- D) goods and services whose quality improves at the rate of growth of real GDP.
- E) more computers and CD players and fewer black-and-white TVs.

Answer: C

Diff: 2 Type: MC

Topic: The Price Level and Inflation

Source: Study Guide

19) If there is a 5 percent increase in the CPI, then there will most likely be

- A) a 5 percent rise in the cost of living.
- B) a less than 5 percent rise in the cost of living because of consumers substituting away from goods whose relative prices rise towards other goods.
- C) a more than 5 percent rise in the cost of living because of consumers substituting away from goods whose relative prices rise towards other goods.
- D) a less than 5 percent rise in the cost of living because of falling quality of goods over time.
- E) a more than 5 percent rise in the cost of living because of the introduction of new goods.

Answer: B

Diff: 2 Type: MC

Topic: The Price Level and Inflation

20) All of the following are possible sources of bias in using the Consumer Price Index to measure inflation *except*

- A) the introduction of new goods.
- B) an improvement in the quality of goods.
- C) commodity substitution.
- D) an increase in the cost of living
- E) Both C and D are exceptions.

Answer: D

Diff: 2 Type: MC

Topic: The Price Level and Inflation

21) If prices at Wendy's rise, more consumers buy their meals at McDonald's and fewer consumers buy their meals at Wendy's. This is an example of

- A) consumers' action to boycott Wendy's.
- B) outlet substitution.
- C) commodity substitution.
- D) both A and B.
- E) both B and C.

Answer: B

Diff: 2 Type: MC

Topic: The Price Level and Inflation

22) Suppose a trade union and a firm agree to increase the wage rate by the same percentage as the increase in the Consumer Price Index. If the CPI increases by 5 percent, then the real income of workers will

- A) increase by 5 percent as well.
- B) remain unchanged, accounting for bias in the calculation of the CPI.
- C) decrease by 5 percent, accounting for bias in the calculation of the CPI.
- D) increase by more than 5 percent, accounting for bias in the calculation of the CPI.
- E) increase by less than 5 percent, accounting for bias in the calculation of the CPI.

Answer: D

Diff: 3 Type: MC

Topic: The Price Level and Inflation

Use the table below to answer the following question.

**Table 21.3.2**  
Data From Southton

Item	Price	Price	Quantity	Quantity
	(dollars)	(dollars)	(number)	(number)
	Base	Current	Base	Current
Rubber Ducks	1.00	1.25	100	100
Beach Towels	9.00	6.00	12	14

23) Refer to Table 21.3.2. From the data in Table 21.3.2, what is Southton's consumer price index for the current year?

- A) 112
- B) 105.6
- C) 100.5
- D) 100
- E) 94.7

Answer: E

Diff: 2 Type: MC

Topic: The Price Level and Inflation

Source: Study Guide

24) Comparing the core inflation rate to the Consumer Price Index, the core inflation rate

- A) controls for the biases of the CPI.
- B) measures all goods produced, not just consumer goods.
- C) uses current period quantities, not base period quantities.
- D) excludes the volatile elements of the CPI.
- E) includes volatile elements not in the CPI.

Answer: D

Diff: 2 Type: MC

Topic: The Price Level and Inflation

Source: Study Guide

25) If the inflation rate is positive, the price level in an economy is

- A) falling rapidly.
- B) rising.
- C) constant.
- D) falling slowly.
- E) zero.

Answer: B

Diff: 2 Type: MC

Topic: The Price Level and Inflation

Source: Study Guide

- 26) Commodity substitution bias in the CPI refers to the fact that the CPI
- A) takes into account the substitution of goods by consumers when relative prices change.
  - B) takes no account of the substitution of goods by consumers when relative prices change.
  - C) substitutes quality changes whenever they occur without taking account of the cost of the quality changes.
  - D) substitutes relative prices for absolute prices of goods.
  - E) accounts for improved quality in price rises.

Answer: B

Type: MC

Topic: The Price Level and Inflation

Skill: Recognition

AACSB: Reflective Thinking

- 27) Of the following sequences of price levels, which correctly represents a 5 percent inflation rate?

- A) 100, 100, 100, 100
- B) 100, 105, 105, 105
- C) 100, 105, 110, 115
- D) 100, 105, 110.25, 115.76
- E) 95, 100, 105, 110

Answer: D

Type: MC

Topic: The Price Level and Inflation

Skill: Analytical

AACSB: Analytical Skills

- 28) The commodity substitution bias is that
- A) consumers substitute high-quality goods for low-quality goods.
  - B) government spending is a good substitute for investment expenditures.
  - C) national saving and foreign borrowing are interchangeable.
  - D) consumers decrease the quantity they buy of goods whose relative prices rise and increase the quantity of goods whose relative price falls.
  - E) consumers substitute more expensive goods for less expensive goods when technology advances.

Answer: D

Type: MC

Topic: The Price Level and Inflation

Skill: Recognition

AACSB: Reflective Thinking

29) Hyperinflation is defined as

- A) declining inflation rates.
- B) rising but low inflation rates.
- C) very high inflation rates.
- D) very low inflation rates.
- E) an increase in the price level.

Answer: C

Type: MC

Topic: The Price Level and Inflation

Skill: Recognition

AACSB: Reflective Thinking

30) Choose the *incorrect* statement.

- A) The outlet substitution bias injects an upward bias into the CPI.
- B) When the quality of a good improves over time and as a result the price rises, the CPI counts the entire price rise as inflation and so overstates inflation.
- C) When relative prices change and people substitute to the lower priced good, the CPI ignores the substitution and the CPI overstates inflation.
- D) The CPI basket is constantly updated to allow for the introduction of new goods.
- E) All of the above statements are incorrect.

Answer: D

Type: MC

Topic: The Price Level and Inflation

Skill: Recognition

Source: MyEconLab

AACSB: Reflective Thinking

31) The price indexes that are alternatives to the CPI are \_\_\_\_\_.

- A) the GDP deflator and the chained price index for consumption
- B) the chained price index for consumption and the CPI deflator
- C) the core GDP deflator and the CPI deflator
- D) the GDP deflator and the CPI deflator
- E) the unbiased CPI and the unbiased GDP deflator

Answer: A

Type: MC

Topic: The Price Level and Inflation

Skill: Recognition

Source: MyEconLab

AACSB: Reflective Thinking

32) The CPIC \_\_\_\_\_.

A) does not overcome the source of bias in the CPI

B) overcomes the sources of bias in the CPI by eliminating measures of the goods and services with the most volatile prices

C) overcomes the sources of bias in the CPI by incorporating substitutions and using current and previous period quantities

D) overcomes the sources of bias in the CPI by giving extra weight to the measures of the goods and services with the most volatile prices

E) overcomes the sources of bias in the CPI by always using discount store prices

Answer: C

Type: MC

Topic: The Price Level and Inflation

Skill: Recognition

Source: MyEconLab

AACSB: Reflective Thinking

Refer to the table below to answer the following question.

**Table 21.3.3**

Region	2006	2007	2008
United State	117.1	120.4	124.0
Euro area	113.6	117.1	119.6
Japan	98.1	98.1	98.8

33) Refer to Table 21.3.3. The IMF *World Economic Outlook* reports the price level data given in the table. The region with the highest inflation rate in 2007 is \_\_\_\_\_. The region with the highest inflation rate in 2008 is \_\_\_\_\_.

A) the Euro area; the United States

B) Japan; the United States

C) the Euro area; Japan

D) the United States; Japan

E) the United States; the Euro area

Answer: A

Type: MC

Topic: The Price Level and Inflation

Skill: Recognition

Source: MyEconLab

AACSB: Reflective Thinking

34) Between 1972 and 2012, Canada's inflation rate as measured by the CPI \_\_\_\_\_.

- A) rises in some years and falls in some years
- B) consistently rises every year
- C) consistently falls every year
- D) was always between 1 and 3 percent a year
- E) was always positive

Answer: A

Type: MC

35) In China, suppose that the price level was 100 in 2007, 110 in 2008, 120 in 2009, and 130 in 2011. Over this time period,

- A) zero inflation occurred.
- B) the inflation rate increased.
- C) the inflation rate was positive.
- D) the inflation rate decreased.
- E) Both C and D are correct.

Answer: E

Type: MC

36) If the inflation rate is negative, the price level in an economy is \_\_\_\_\_.

- A) rising rapidly
- B) rising slowly
- C) falling
- D) constant
- E) none of the above

Answer: C

Type: MC

## Chapter 22 Economic Growth

### 22.1 The Basics of Economic Growth

1) Economic growth is

- A) a sustained expansion of production possibilities measured as the increase in nominal GDP over a given period.
- B) a sustained expansion of consumption expenditure over a given period.
- C) always accompanied by a rising price level.
- D) equal to real GDP per capita multiplied by 70.
- E) a sustained expansion of production possibilities measured as the increase in real GDP over a given period.

Answer: E

Diff: 2 Type: MC

Topic: The Basics of Economic Growth

Skill: Recognition

AACSB: Reflective Thinking

2) In 2010, Northland had real GDP of \$4.21 billion and a population of 2.98 million. In 2011,

real GDP was \$4.59 billion and population was 2.97 million. What was Northland's economic growth rate in 2011?

- A) 0.38 percent
- B) 3.8 percent
- C) 8.3 percent
- D) 9.0 percent
- E) 11.1 percent

Answer: D

Type: MC

Topic: The Basics of Economic Growth

Skill: Analytical

AACSB: Analytical Skills

3) In 2010, Northland had real GDP of \$4.21 billion and a population of 2.98 million. In 2011, real GDP was \$4.59 billion and population was 2.97 million. Between 2010 and 2011, Northland's standard of living \_\_\_\_\_.

- A) increased
- B) decreased
- C) did not change
- D) might have increased, decreased, or remained unchanged
- E) doubled.

Answer: A

Type: MC

Topic: The Basics of Economic Growth

Skill: Conceptual

AACSB: Analytical Skills

4) In 2010, Northland had real GDP of \$4.21 billion and a population of 2.98 million. In 2011, real GDP was \$4.59 billion and population was 2.97 million. Northland's real GDP per person in 2011 was

- A) \$1,545.
- B) \$380.
- C) \$1,413.
- D) \$132.
- E) \$1.41.

Answer: A

Type: MC

Topic: The Basics of Economic Growth

Skill: Analytical

AACSB: Analytical Skills

5) During 2011, the country of Economia had real GDP of \$115 billion and the population was 0.9 billion. In 2010, real GDP was \$105 billion and the population was 0.85 billion. In 2011, real GDP per person was

- A) \$124.
- B) \$135.
- C) \$117.
- D) \$12,778.
- E) \$128.

Answer: E

Diff: 2 Type: MC

Topic: The Basics of Economic Growth

Skill: Analytical

AACSB: Analytical Skills

6) During 2011, the country of Economia had real GDP of \$115 billion and the population was 0.9 billion. In 2010, real GDP was \$105 billion and the population was 0.85 billion. In 2010, real GDP per person was

- A) \$128.
- B) \$124.
- C) \$135.
- D) \$117.
- E) \$1,235.

Answer: B

Diff: 2 Type: MC

Topic: The Basics of Economic Growth

Skill: Analytical

AACSB: Analytical Skills

7) Suppose a country's population grows by 2 percent a year and, at the same time, its real GDP grows by 5 percent a year. Real GDP per person is increasing by \_\_\_\_\_ a year.

- A) 2 percent
- B) 5 percent
- C) 10 percent
- D) 16 percent
- E) 3 percent

Answer: E

Type: MC

Topic: The Basics of Economic Growth

Skill: Analytical

AACSB: Analytical Skills

8) The Rule of 70 is used to

- A) estimate how much of an economy's growth rate is attributable to increases in capital per hour of labour.
- B) calculate the standard of living.
- C) calculate the economy's growth rate.
- D) estimate how long it will take the level of any variable to double.
- E) estimate how much of an economy's growth rate is attributable to technological advance.

Answer: D

Type: MC

Topic: The Basics of Economic Growth

Skill: Recognition

AACSB: Reflective Thinking

9) Using the Rule of 70, if the country of Flowerdom's current growth rate of real GDP per person is 7 percent a year, how long will it take the country's real GDP per person to double?

- A) 1 year
- B) 2 years
- C) 10 years
- D) 49 years
- E) 7 years

Answer: C

Diff: 2 Type: MC

Topic: The Basics of Economic Growth

Skill: Analytical

AACSB: Analytical Skills

10) Using the Rule of 70, if the country of Flowerdom's current growth rate of real GDP per person is 10 percent a year, how long will it take the country's real GDP per person to double?

- A) 0.7 years
- B) 1 year
- C) 10 years
- D) 49 years
- E) 7 years

Answer: E

Diff: 2 Type: MC

Topic: The Basics of Economic Growth

Skill: Analytical

AACSB: Analytical Skills

11) Slowdonia's current growth rate of real GDP per person is 2 percent a year. How long will it take to double real GDP per person?

- A) half a year
- B) approximately 10 years
- C) 28.6 years
- D) 35 years
- E) 2 years

Answer: D

Diff: 3 Type: MC

Topic: The Basics of Economic Growth

Skill: Analytical

AACSB: Analytical Skills

12) Slowdonia's current growth rate of real GDP per person is 1 percent a year. How long will it take to double real GDP per person?

- A) 10 years
- B) 35 years
- C) 70 years
- D) 100 years
- E) Real GDP per person will never double

Answer: C

Diff: 3 Type: MC

Topic: The Basics of Economic Growth

Skill: Analytical

AACSB: Analytical Skills

13) If real GDP per person is growing at 4 percent per year, it will double in

- A) 17.5 years.
- B) 25 years.
- C) 4 years.
- D) 8 years.
- E) 56 years.

Answer: A

Type: MC

Topic: The Basics of Economic Growth

Skill: Analytical

AACSB: Analytical Skills

14) Suppose a country is producing \$20 million of real GDP. If the economy grows at 10 percent per year, approximately how many years will it take for real GDP to grow to \$80 million?

- A) 14
- B) 7
- C) 4
- D) 30
- E) 3.5 years

Answer: A

Type: MC

Topic: The Basics of Economic Growth

Skill: Analytical

AACSB: Analytical Skills

15) Real GDP per person in the country of Flip is \$10,000, and the growth rate is 10 percent a year. Real GDP per person in the country of Flap is \$20,000 and the growth rate is 5 percent a year. When will real GDP per person be greater in Flip than in Flap?

- A) in 2 years
- B) in 15 years
- C) never
- D) in 10 years
- E) in 7 years

Answer: B

Type: MC

Topic: The Basics of Economic Growth

Skill: Analytical

AACSB: Analytical Skills

16) Growthland's real GDP per person was \$112,000 in 2009 and \$117,000 in 2010. What is the growth rate of Growthland's real GDP per person in 2010?

A) 4.3%

B) 4.5%

C) 5%

D) 12%

E) 17%

Answer: B

Type: MC

Topic: The Basics of Economic Growth

Source: Study Guide

## 22.2 Economic Growth Trends

1) In which of the following decades did Canada experience the slowest economic growth?

- A) 1960s
- B) 1970s
- C) 1980s
- D) 1940s
- E) 1990s

Answer: C

Diff: 2 Type: MC

Topic: Economic Growth Trends

2) Canada's economic growth rate was highest in which of the following decades?

- A) the 1930s
- B) the 1960s
- C) the 1970s
- D) the 1980s
- E) the 1990s

Answer: B

Diff: 2 Type: MC

Topic: Economic Growth Trends

Source: Study Guide

3) Which of the following statements about Canada's long-term growth trends is *false*?

- A) Economic growth rates have been steady, except for the business cycle.
- B) Economic growth rates show periods of slow and high growth.
- C) Economic growth rates were faster in the 1990s than in the 1980s.
- D) Economic growth rates have slightly faster in the United States than in Canada.
- E) African countries have fallen further behind Canada in recent years.

Answer: A

Type: MC

Topic: Economic Growth Trends

Source: Study Guide

4) Between 1926 and 2010 real GDP per person in Canada grew at an average rate of

- A) 2.8 percent a year.
- B) 1.7 percent a year.
- C) 2.0 percent a year.
- D) 3.6 percent a year.
- E) 4.3 percent a year.

Answer: C

Diff: 3 Type: MC

Topic: Economic Growth Trends

- 5) Compared to growth in other countries, between 1960 and 2010 Canada
- A) fell behind most other countries.
  - B) dramatically caught up to and passed other countries.
  - C) worsened dramatically versus the United States, but did better versus other countries.
  - D) did as well or better than most countries except certain Asian countries.
  - E) did none of the above.

Answer: D

Type: MC

Topic: Economic Growth Trends

Source: Study Guide

- 6) Between 1926 and 2010, the average growth rate of real GDP per person in Canada was \_\_\_\_\_ percent a year. During this period, \_\_\_\_\_ grew at a faster rate than \_\_\_\_\_.

- A) 2.0; GDP; the population
- B) 2.0; real GDP; the population
- C) 1.0; inflation; real GDP
- D) 3.0; the population; real GDP
- E) 3.0; inflation; real GDP

Answer: B

Type: MC

Topic: Economic Growth Trends

Source: MyEconLab

- 7) Convergence between real GDP per person in Canada and Japan was relatively \_\_\_\_\_ during the 1960s; convergence has recently been \_\_\_\_\_.

- A) slow; increasing
- B) rapid; decreasing
- C) rapid; increasing at an even faster rate
- D) slow; decreasing
- E) rapidly; continuing at the 1960s pace

Answer: B

Type: MC

Topic: Economic Growth Trends

Source: MyEconLab

- 8) The gap between real GDP per person in Canada and Hong Kong has \_\_\_\_\_ since 1960. During this period, the growth rate of real GDP per person in Canada has been \_\_\_\_\_ than in Hong Kong.

- A) reversed; faster
- B) increased; faster
- C) remained constant; equal
- D) reversed; slower
- E) decreased; faster

Answer: D

Type: MC

Topic: Economic Growth Trends

Source: MyEconLab

9) Between 1960 and 2010, growth rates in real GDP per person in Hong Kong, Korea, Singapore, Taiwan, and China \_\_\_\_\_ the growth rate of real GDP per person in Canada. China's real GDP per person in 2010 is approximately equal to real GDP per person in Hong Kong in \_\_\_\_\_.

- A) exceeded; 1998
- B) were less than; 1988
- C) were less than; 1976
- D) exceeded; 1976
- E) were approximately equal to; 1968

Answer: D

Type: MC

Topic: Economic Growth Trends

Source: MyEconLab

10) During the last 10 years, which of the following had the lowest level of real GDP per person?

- A) Eastern Europe
- B) Central and South America
- C) Africa
- D) Japan
- E) China

Answer: C

Type: MC

11) Of the following countries, which has the lowest level of real GDP per person?

- A) China
- B) Singapore
- C) Hong Kong
- D) Korea
- E) Canada

Answer: A

Type: MC

### 22.3 How Potential GDP Grows

- 1) An increase in labour hours will lead to
- A) an upward shift of the aggregate production function.
  - B) a movement along the aggregate production function.
  - C) both a movement along and an upward shift of the aggregate production function.
  - D) neither a movement along nor a shift of the aggregate production function.
  - E) a downward shift of the aggregate production function.

Answer: B

Type: MC

Topic: How Potential GDP Grows

Skill: Conceptual

AACSB: Reflective Thinking

- 2) The aggregate production function is graphed as
- A) a downward-sloping curve.
  - B) an upward-sloping straight line.
  - C) an upward-sloping line that becomes flatter as the quantity of labour increases.
  - D) an upward-sloping line that becomes steeper as the quantity of labour increases.
  - E) a production possibilities frontier.

Answer: C

Type: MC

Topic: How Potential GDP Grows

Skill: Recognition

AACSB: Reflective Thinking

- 3) The decreasing slope of the aggregate production function reflects
- A) diminishing returns.
  - B) rising unemployment.
  - C) decreasing costs.
  - D) increasing aggregate demand.
  - E) a decrease in potential GDP.

Answer: A

Type: MC

Topic: How Potential GDP Grows

Skill: Conceptual

AACSB: Reflective Thinking

4) According to the law of diminishing returns, along the aggregate production function an additional unit of

- A) capital produces more output than an additional unit of labour.
- B) labour decreases output.
- C) labour produces more output than the previous unit.
- D) labour produces less output than the previous unit.
- E) labour increases the real wage rate.

Answer: D

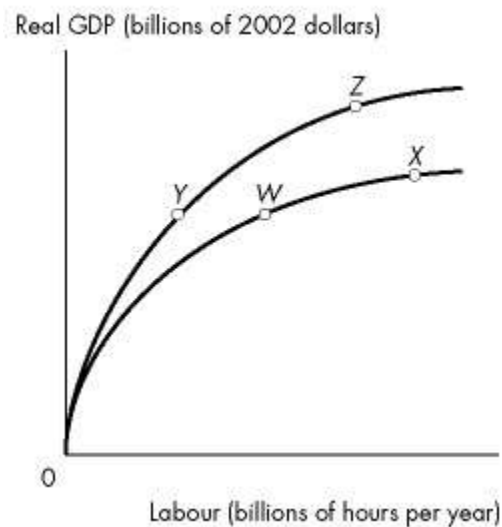
Type: MC

Topic: How Potential GDP Grows

Skill: Recognition

AACSB: Reflective Thinking

Use the figure below to answer the following question.



**Figure 22.3.1**

5) Refer to Figure 22.3.1. The country of Kemper is on its aggregate production function at point *W* in the above figure. If the population increases with no change in capital or technology, the economy will

- A) move to point such as *Y*.
- B) remain at point *W*.
- C) move to point such as *X*.
- D) move to point such as *Z*.
- E) either remain at point *W* or move to point *X*.

Answer: C

Type: MC

Topic: How Potential GDP Grows

Skill: Conceptual

AACSB: Analytical Skills

- 6) If the money wage rate is \$15.00 an hour and the price level is 120, the real wage rate is
- A) \$8.50 an hour.
  - B) \$10.75 an hour.
  - C) \$12.50 an hour.
  - D) \$15.00 an hour.
  - E) \$18 an hour.

Answer: C

Type: MC

Topic: How Potential GDP Grows

Skill: Analytical

AACSB: Analytical Skills

- 7) If the money wage rate is \$10.00 an hour and the price level is 60, the real wage rate is
- A) \$16.67 an hour.
  - B) \$18.75 an hour.
  - C) \$10.00 an hour.
  - D) \$12.50 an hour.
  - E) \$6.00 an hour.

Answer: A

Type: MC

Topic: How Potential GDP Grows

Skill: Analytical

AACSB: Analytical Skills

- 8) If the real wage rate is \$10.00 an hour and the price level is 60, the money wage rate is
- A) \$16.75 an hour.
  - B) \$18.50 an hour.
  - C) \$10.00 an hour.
  - D) \$6.00 an hour.
  - E) \$16.67 an hour.

Answer: D

Type: MC

Topic: How Potential GDP Grows

Skill: Analytical

AACSB: Analytical Skills

9) When the quantity of labour demanded exceeds the quantity of labour supplied, the real wage rate

- A) rises to eliminate the labour market shortage.
- B) falls to eliminate the labour market surplus.
- C) rises to eliminate the labour market surplus.
- D) falls to eliminate the labour market shortage.
- E) does not change but the money wage rate rises to eliminate the labour market shortage.

Answer: A

Type: MC

Topic: How Potential GDP Grows

Skill: Conceptual

AACSB: Reflective Thinking

10) In the labour market, an increase in labour productivity \_\_\_\_\_ the real wage rate and \_\_\_\_\_ the level of employment.

- A) raises; increases
- B) raises; decreases
- C) lowers; increases
- D) lowers; decreases
- E) raises; does not change

Answer: A

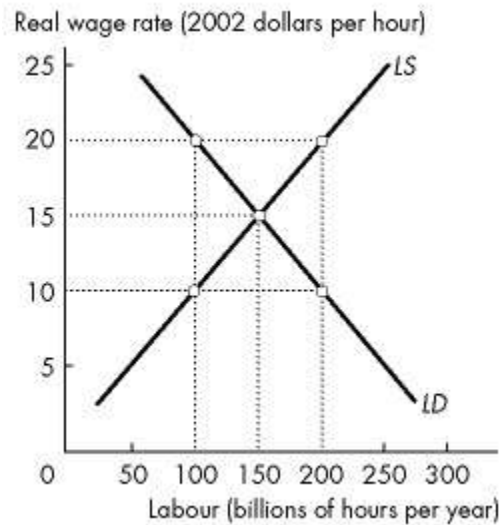
Type: MC

Topic: How Potential GDP Grows

Skill: Analytical

AACSB: Analytical Skills

Use the figure below to answer the following questions.



**Figure 22.3.2**

11) Refer to Figure 22.3.2. The equilibrium real wage rate is

- A) \$10 an hour.
- B) \$15 an hour.
- C) \$20 an hour.
- D) any wage rate above \$15 an hour.
- E) any wage rate below \$15 an hour.

Answer: B

Type: MC

Topic: How Potential GDP Grows

Skill: Analytical

AACSB: Analytical Skills

12) Refer to Figure 22.3.2. The equilibrium quantity of labour is

- A) 100 billion hours.
- B) 150 billion hours.
- C) 200 billion hours.
- D) 50 billion hours.
- E) 250 billion hours.

Answer: B

Type: MC

Topic: How Potential GDP Grows

Skill: Analytical

AACSB: Analytical Skills

- 13) Refer to Figure 22.3.2. If the real wage is \$20 an hour, a labour
- A) shortage will occur and the real wage will rise.
  - B) shortage will occur and the real wage will fall.
  - C) surplus will occur and the real wage will rise.
  - D) surplus will occur and the real wage will fall.
  - E) surplus will occur and the demand for labour will increase.

Answer: D

Type: MC

Topic: How Potential GDP Grows

- 14) When the population increases with no change in labour productivity, employment \_\_\_\_\_ and potential GDP \_\_\_\_\_.
- A) decreases; decreases
  - B) increases; increases
  - C) decreases; increases
  - D) increases; decreases
  - E) increases; does not change

Answer: B

Type: MC

Topic: How Potential GDP Grows

Skill: Analytical

AACSB: Reflective Thinking

Use the table below to answer the following questions.

**Table 22.3.1**

Real wage rate (2002 dollars per hour)	Quantity of labour demanded (billions of hours per year)	Quantity of labour supplied (billions of hours per year)
15	70	10
20	60	20
25	50	30
30	40	40
35	30	50

Real GDP (trillions of 2002 dollars per year)	Quantity of labour (billions of hours per year)
3	20
9	30
14	40
18	50
21	60

15) Refer to Table 22.3.1. The tables show the labour market and the aggregate production function schedule for the country of Pickett. Potential GDP is \_\_\_\_\_.

- A) \$40 trillion
- B) \$6 trillion
- C) \$14 trillion
- D) \$25 trillion
- E) \$9 trillion

Answer: C

Type: MC

Topic: How Potential GDP Grows

Skill: Analytical

AACSB: Analytical Skills

16) Refer to Table 22.3.1. The tables show the labour market and the production function schedule for the country of Pickett. An increase in population changes the quantity of labour supplied by 20 billion hours at each real wage rate. Potential GDP \_\_\_\_\_.

- A) does not change.
- B) decreases to \$3 trillion.
- C) increases to \$50 trillion.
- D) increases to \$18 trillion.
- E) increases to \$20 trillion.

Answer: D

Type: MC

Topic: How Potential GDP Grows

Skill: Analytical

AACSB: Analytical Skills

17) Labour productivity is

- A) real GDP per hour of labour times the hours of work.
- B) real GDP per hour of labour times the population.
- C) the quantity of real GDP produced by an hour of labour.
- D) the rate of change in real GDP per hour of labour.
- E) none of the above.

Answer: C

Type: MC

Topic: How Potential GDP Grows

Skill: Recognition

AACSB: Reflective Thinking

18) If real GDP is \$800 million and aggregate labour hours are 20 million, labour productivity is \_\_\_\_\_.

- A) \$40 an hour
- B) \$16,000 million
- C) \$40 million
- D) \$160 an hour
- E) \$16 an hour

Answer: A

Type: MC

Topic: How Potential GDP Grows

Skill: Analytical

AACSB: Analytical Skills

19) If real GDP is \$12,150 billion and aggregate labour hours are 270 billion, labour productivity equals

- A) \$6.50 an hour.
- B) \$45 an hour.
- C) \$48 an hour.
- D) \$650 an hour.
- E) \$32.81 an hour.

Answer: B

Diff: 3 Type: MC

Topic: How Potential GDP Grows

Skill: Analytical

AACSB: Analytical Skills

20) When labour productivity increases, the demand for labour curve \_\_\_\_\_ and the supply of labour curve \_\_\_\_\_.

- A) shifts rightward; shifts rightward
- B) shifts rightward; does not shift
- C) shifts leftward; shifts rightward
- D) shifts leftward; does not shift
- E) shifts rightward; shifts leftward

Answer: B

Type: MC

Topic: How Potential GDP Grows

Skill: Analytical

AACSB: Analytical Skills

21) An increase in labour productivity \_\_\_\_\_ the real wage rate and an increase in population \_\_\_\_\_ the real wage rate.

- A) raises; lowers
- B) raises; raises
- C) lowers; lowers
- D) lowers; raises
- E) raises; does not change

Answer: A

Type: MC

Topic: How Potential GDP Grows

Skill: Analytical

AACSB: Analytical Skills

- 22) An increase in population results in
- A) an upward shift in the production function.
  - B) a movement along the production function.
  - C) a leftward shift of the labour supply curve.
  - D) a rightward shift of the labour demand curve.
  - E) both B and D are correct.

Answer: B

Diff: 3 Type: MC

Topic: How Potential GDP Grows

Skill: Conceptual

AACSB: Analytical Skills

- 23) If the population increases, then potential GDP \_\_\_\_\_, employment \_\_\_\_\_, and \_\_\_\_\_ potential GDP per hour of labour.

- A) increases; increases; decreases
- B) increases; decreases; decreases
- C) decreases; increases; increases
- D) decreases; decreases; decreases
- E) increases; increases; increases

Answer: A

Type: MC

Topic: How Potential GDP Grows

Skill: Analytical

AACSB: Analytical Skills

- 24) If new capital increases labour productivity, the supply of labour \_\_\_\_\_ and the demand for labour \_\_\_\_\_.

- A) stays the same; increases
- B) increases; increases
- C) increases; decreases
- D) decreases; stays the same
- E) increases; stays the same

Answer: A

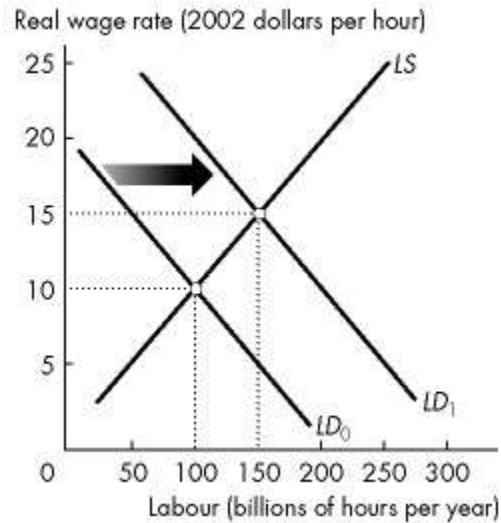
Type: MC

Topic: How Potential GDP Grows

Skill: Analytical

AACSB: Reflective Thinking

Use the figure below to answer the following question.



**Figure 22.3.3**

25) Refer to Figure 22.3.3. As a result of the rightward shift in the demand curve for labour from  $LD_0$  to  $LD_1$ , the equilibrium level of employment \_\_\_\_\_, potential GDP \_\_\_\_\_, and potential GDP per hour of labour \_\_\_\_\_.

- A) increases; increases; increases
- B) increases; decreases; increases
- C) decreases; increases; decreases
- D) decreases; decreases; decreases
- E) increases; increases; decreases

Answer: A

Type: MC

Topic: How Potential GDP Grows

Skill: Analytical

AACSB: Analytical Skills

- 26) *Ceteris paribus*, an increase in labour productivity results in a
- A) higher real wage rate and higher potential GDP per hour of labour.
  - B) lower real wage rate and higher potential GDP per hour of labour.
  - C) higher real wage rate and lower potential GDP per hour of labour.
  - D) lower real wage rate and lower potential GDP per hour of labour.
  - E) constant real wage rate in the long run.

Answer: A

Type: MC

Topic: How Potential GDP Grows

Source: Study Guide

- 27) *Ceteris paribus*, an increase in population results in a
- A) higher level of labour employed and higher potential GDP per hour of labour.
  - B) lower level of labour employed and higher potential GDP per hour of labour.
  - C) higher level of labour employed and lower potential GDP per hour of labour.
  - D) lower level of labour employed and lower potential GDP per hour of labour.
  - E) constant level of labour employed and constant potential GDP per hour of labour.

Answer: C

Type: MC

Topic: How Potential GDP Grows

Source: Study Guide

- 28) The aggregate production function shows how \_\_\_\_\_ varies with \_\_\_\_\_.

- A) real GDP; labour
- B) labour; leisure
- C) real GDP; leisure
- D) labour; capital
- E) real GDP; capital

Answer: A

Type: MC

- 29) A movement along the aggregate production function is the result of a change in \_\_\_\_\_.

- A) capital
- B) technology
- C) the quantity of labour
- D) the interest rate
- E) the inflation rate

Answer: C

Type: MC

## 22.4 Why Labour Productivity Grows

- 1) Labour productivity grows as
- A) consumption expenditure increases.
  - B) depreciation increases.
  - C) physical capital grows.
  - D) human capital grows.
  - E) both C and D are correct.

Answer: E

Type: MC

Topic: Why Labour Productivity Grows

Skill: Conceptual

AACSB: Reflective Thinking

- 2) If capital per worker increases, labour productivity
- A) decreases for a given level of technology.
  - B) increases because the level of technology increases.
  - C) increases for a given level of technology.
  - D) decreases because the level of technology decreases.
  - E) does not change unless technology advances at the same time.

Answer: C

Type: MC

Topic: Why Labour Productivity Grows

Skill: Analytical

AACSB: Reflective Thinking

- 3) If capital per worker decreases, real GDP per hour of labour
- A) decreases because the level of technology decreases.
  - B) increases because the level of technology increases.
  - C) increases for a given level of technology.
  - D) decreases for a given level of technology.
  - E) none of the above.

Answer: D

Type: MC

Topic: Why Labour Productivity Grows

Skill: Analytical

AACSB: Reflective Thinking

- 4) An increase in education and training  
A) increases labour productivity.  
B) increases aggregate hours.  
C) decreases real GDP growth.  
D) increases the employment-to-population ratio.  
E) is an increase in physical capital.

Answer: A

Type: MC

Topic: Why Labour Productivity Grows

Skill: Conceptual

AACSB: Reflective Thinking

- 5) \_\_\_\_\_ is the accumulated skill and knowledge of human beings.

- A) Labour productivity  
B) Human capital  
C) Capital  
D) Technology  
E) Human investment

Answer: B

Type: MC

Topic: Why Labour Productivity Grows

Skill: Recognition

AACSB: Reflective Thinking

- 6) Human capital is the  
A) machinery used by humans to produce GDP.  
B) technology used by humans to produce GDP.  
C) skill and knowledge accumulated by humans.  
D) plant and equipment produced by humans and not by machines.  
E) none of the above.

Answer: C

Type: MC

Topic: Why Labour Productivity Grows

Skill: Recognition

AACSB: Reflective Thinking

- 7) Which of the following statements regarding human capital is *INCORRECT*?
- A) Human capital is the accumulated skill and knowledge of human beings.
  - B) Education is the only vehicle for the creation of human capital because training simply reinforces what has already been learned.
  - C) The accumulation of human capital is the source of both increased labour productivity and technological advance.
  - D) Writing and mathematics, the most basic of human skills, are crucial elements in economic progress.
  - E) All of the above statements are correct.

Answer: B

Type: MC

Topic: Why Labour Productivity Grows

Skill: Conceptual

AACSB: Reflective Thinking

- 8) Which of the following is *not* a source of economic growth?
- A) increasing stock market prices
  - B) better educated workers
  - C) growing physical capital
  - D) appropriate incentive system
  - E) advances in technology

Answer: A

Type: MC

Topic: Why Labour Productivity Grows

Source: Study Guide

- 9) The Industrial Revolution in England was largely the result of
- A) growth in human capital.
  - B) population growth.
  - C) technological innovations that were financed mainly by government spending.
  - D) technological innovations encouraged by the patent system.
  - E) the elimination of the patent system.

Answer: D

Type: MC

- 10) Factors that influence labour productivity include \_\_\_\_\_.
- A) the inflation rate, the real wage rate, and the exchange rate
  - B) the labour demand curve
  - C) physical capital, the real wage rate, and technology
  - D) the demand for labour, the real wage rate, and technology
  - E) physical capital, human capital, and technology

Answer: E

Type: MC

- 11) Labour productivity rises when
- A) technological progress is stagnant.
  - B) firms invest more in hiring workers than in replacing worn-out capital.
  - C) the amount of capital per worker decreases.
  - D) the real wage rate falls.
  - E) the amount of capital per worker increases.

Answer: E

Type: MC

- 12) In developing nations, microloans \_\_\_\_\_.
- A) have enabled small businesses with limited access to credit to purchase capital and expand, allowing greater economic growth
  - B) have increased the indebtedness of impoverished people, slowing economic growth
  - C) are primarily used to finance consumption expenditure, leading to economic growth
  - D) are far too small to have any discernible effect
  - E) discourage saving and investment

Answer: A

Type: MC

## 22.5 Growth Theories, Evidence, and Policies

- 1) Which one of the following quotations could be attributed to a supporter of the classical growth theory?
- A) "Growth will last as long as technology keeps advancing."
  - B) "Prosperity will last as long as technology keeps advancing."
  - C) "Growth will last only until the increase in population brings productivity down to the subsistence level."
  - D) "Prosperity will last as long as there is knowledge accumulation."
  - E) "Growth will last as long as knowledge accumulation continues."

Answer: C

Diff: 2 Type: MC

Topic: Growth Theories and Policies

- 2) The new growth theory holds that growth can persist indefinitely based on the major assumption that
- A) discoveries result from regulations.
  - B) knowledge capital does not experience diminishing returns.
  - C) knowledge is a public capital good.
  - D) discoveries bring profit.
  - E) knowledge destroys profit.

Answer: B

Diff: 2 Type: MC

Topic: Growth Theories and Policies

3) Which theory of economic growth argues that growth does *not* automatically slow down?

- A) classical growth theory
- B) neoclassical growth theory
- C) new growth theory
- D) all of the theories
- E) none of the theories

Answer: C

Diff: 2 Type: MC

Topic: Growth Theories and Policies

4) Which theory of economic growth argues that, in the long run, people do not benefit from growth?

- A) classical growth theory
- B) neoclassical growth theory
- C) new growth theory
- D) all of the theories
- E) none of the theories

Answer: A

Diff: 2 Type: MC

Topic: Growth Theories and Policies

5) Which theory of economic growth argues that population growth lowers the real wage rate and stops economic growth?

- A) classical growth theory
- B) neoclassical growth theory
- C) new growth theory
- D) all of the theories
- E) none of the theories

Answer: A

Diff: 2 Type: MC

Topic: Growth Theories and Policies

6) The key difference between the neoclassical growth theory and the classical growth theory is that

- A) capital is not subject to diminishing returns under classical growth theory.
- B) capital is subject to diminishing returns under classical growth theory.
- C) increases in population drive workers' incomes back down to the subsistence level in classical growth theory.
- D) growth in the neoclassical growth theory ends with a population explosion.
- E) in classical growth theory, the pace of technological change influences the economic growth rate but economic growth does not influence the pace of technological change.

Answer: C

Diff: 3 Type: MC

Topic: Growth Theories and Policies

- 7) The key difference between the neoclassical growth theory and the new growth theory is that
- A) capital is not subject to diminishing returns under new growth theory.
  - B) capital is subject to diminishing returns under new growth theory.
  - C) increases in population drive workers' incomes back down to the subsistence level in neoclassical growth theory.
  - D) the pace of technological advances are caused by chance in new growth theory.
  - E) labour productivity grows indefinitely in neoclassical growth theory.

Answer: A

Diff: 3 Type: MC

Topic: Growth Theories and Policies

- 8) In the classical growth theory, economic growth eventually stops due to
- A) diminishing returns.
  - B) knowledge capital being easily replicated.
  - C) the real rate of interest falling back down to its target rate.
  - D) real GDP per person becoming too high.
  - E) high population growth resulting from the increase in real GDP per person.

Answer: E

Diff: 2 Type: MC

Topic: Growth Theories and Policies

Source: Study Guide

- 9) In the neoclassical growth theory, economic growth eventually stops after a technological advance when
- A) the return on capital falls and the incentive to invest weakens.
  - B) knowledge capital is replicated.
  - C) the subsistence real wage rate falls.
  - D) the real wage rate increases.
  - E) high population growth occurs.

Answer: A

Diff: 3 Type: MC

Topic: Growth Theories and Policies

- 10) Knowledge capital is different from physical capital because knowledge capital
- A) does not experience diminishing returns.
  - B) experiences diminishing returns.
  - C) is free.
  - D) increases with investment.
  - E) none of the above.

Answer: A

Diff: 2 Type: MC

Topic: Growth Theories and Policies

11) Growth eventually stops in neoclassical growth theory when

- A) technology stops advancing.
- B) saving increases.
- C) discoveries are replicated.
- D) the return on capital increases.
- E) population growth lowers the real wage rate.

Answer: A

Diff: 2 Type: MC

Topic: Growth Theories and Policies

12) An assumption of the neoclassical growth theory is that

- A) people earn a subsistence real wage in the long run.
- B) technological advances are the result of chance.
- C) the marginal product of all types of capital increases as more capital is accumulated.
- D) discoveries are a public capital good.
- E) encouraging international trade increases economic growth.

Answer: B

Diff: 2 Type: MC

Topic: Growth Theories and Policies

13) An assumption of the new growth theory is that

- A) people earn a subsistence real wage in the long run.
- B) all technological advances are the result of chance.
- C) the marginal product of all types of capital increases as more capital is accumulated.
- D) the growth rate of labour productivity depends on people's ability to innovate.
- E) technological advances encourage international trade.

Answer: D

Diff: 2 Type: MC

Topic: Growth Theories and Policies

14) Which theory of economic growth concludes that technological advances are influenced by the profit motive?

- A) classical growth theory
- B) neoclassical growth theory
- C) new growth theory
- D) neo growth theory
- E) none of the theories

Answer: C

Diff: 2 Type: MC

Topic: Growth Theories and Policies

- 15) Compared to physical capital, knowledge capital
- A) can be replicated without diminishing returns.
  - B) can be held in your hand.
  - C) leads to an automatic slowdown in growth.
  - D) cannot be replicated without diminishing returns.
  - E) none of the above.

Answer: A

Diff: 2 Type: MC

Topic: Growth Theories and Policies

Source: Study Guide

- 16) Which of the following is a suggestion for increasing Canadian economic growth rates?
- A) Stimulate saving by taxing consumption.
  - B) Reduce the time period for patent protection to increase replication.
  - C) Put less public research funds into universities.
  - D) Protect our industries from foreign competition.
  - E) Tax education.

Answer: A

Type: MC

Topic: Growth Theories and Policies

Source: Study Guide

- 17) In neoclassical growth theory, if the rate of return on capital increases due to a technological advance, then
- A) the rate of return on capital will eventually decline.
  - B) capital per hour of labour will decrease.
  - C) real GDP per hour of labour will decrease.
  - D) the rate of return on capital will never decline.
  - E) population growth will explode.

Answer: A

Type: MC

Topic: Growth Theories and Policies

Source: Study Guide

18) According to \_\_\_\_\_ growth theory, growth of real GDP per person comes to a stop because a population explosion returns real GDP per person to the subsistence level. According to \_\_\_\_\_ growth theory, growth of real GDP per person comes to a stop when technology stops advancing.

According to \_\_\_\_\_ growth theory, growth of real GDP per person is unending.

- A) classical; new; neoclassical
- B) neoclassical; classical; new
- C) new; neoclassical; classical
- D) classical; neoclassical; new
- E) new; classical; neoclassical

Answer: D

Type: MC

Topic: Growth Theories and Policies

Source: MyEconLab

19) Choose the statements concerning neoclassical growth theory which are true.

1. Neoclassical growth theory was developed in the late 19th century.
2. The rate of technological change influences the economic growth rate but economic growth does not influence the pace of technological change.
3. Economic growth will stop if technology stops advancing.
4. Technological change results from the choices people make in the pursuit of profit.

- A) Statements 1 and 4 are correct.
- B) Statements 3 and 4 are correct.
- C) Statements 2 and 3 are correct.
- D) Statements 1 and 3 are correct.
- E) Statements 2 and 4 are correct.

Answer: C

Type: MC

Topic: Growth Theories and Policies

Source: MyEconLab

20) All of the following statements are included in new growth theory *except* \_\_\_\_\_.

- A) discoveries are a public capital good
- B) discoveries result from choices
- C) the forces of competition destroy incentives to make new discoveries
- D) discoveries bring profit, and competition destroys profit
- E) knowledge is capital that is not subject to the law of diminishing returns

Answer: C

Type: MC

Topic: Growth Theories and Policies

Source: MyEconLab

- 21) According to Thomas Robert Malthus, \_\_\_\_\_.
- A) labour productivity increases continuously
  - B) the population growth rate is fixed
  - C) technological advances lead to permanent increases in real GDP per person
  - D) increases in real GDP per person are only temporary
  - E) knowledge capital does not experience diminishing returns

Answer: D

Type: MC

- 22) Which of the following ideas apply to the neoclassical growth theory?
- I. The rate of technological change influences the rate of economic growth.
  - II. Technological change promotes saving and investment.
  - III. Convergence of economic growth rates across countries.

- A) I only
- B) II only
- C) III only
- D) I and II only
- E) I, II, and III

Answer: E

Type: MC

## Chapter 23 Finance, Saving, and Investment

### 23.1 Financial Institutions and Financial Markets

1) Capital is

- A) the tools, instruments, machines, buildings, and other items that have been produced in the past and that are used today to produce goods and services.
- B) financial wealth.
- C) the sum of investment and government expenditure on goods.
- D) net investment.
- E) gross investment.

Answer: A

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Recognition

AACSB: Reflective Thinking

2) Gross investment

- A) is the total amount spent on new capital.
- B) includes only replacement investment.
- C) equals wealth minus saving.
- D) equals saving minus wealth.
- E) is the change in the value of capital

Answer: A

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Recognition

AACSB: Reflective Thinking

3) The total amount spent on new capital is

A) wealth.

B) gross investment.

C) depreciation.

D) net investment.

E) saving.

Answer: B

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Recognition

AACSB: Reflective Thinking

4) In January 2011, Tim's Gyms, Inc. owned machines valued at \$1 million. During the year, the market value of the machines fell by 30 percent. During 2011, Tim spent \$200,000 on new machines. During 2011, Tim's gross investment was

- A) \$1 million.
- B) \$300,000.
- C) \$200,000
- D) \$900,000.
- E) \$100,000.

Answer: C

Diff: 1 Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Analytical

AACSB: Analytical Skills

5) Net investment equals

- A) capital minus depreciation.
- B) gross investment minus depreciation.
- C) the total quantity of plant, equipment, and buildings.
- D) gross investment/depreciation.
- E) wealth minus saving.

Answer: B

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Recognition

AACSB: Reflective Thinking

6) The increase in the value of capital is

- A) gross investment.
- B) depreciation.
- C) net investment.
- D) private sector spending.
- E) wealth.

Answer: C

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Recognition

AACSB: Reflective Thinking

- 7) Capital stock increases when
- A) gross investment exceeds net investment.
  - B) net investment exceeds gross investment.
  - C) gross investment is negative.
  - D) net investment is positive.
  - E) net investment is zero.

Answer: D

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Conceptual

AACSB: Reflective Thinking

- 8) If the economy's capital increases over time,
- A) net investment is positive.
  - B) depreciation is less than zero.
  - C) depreciation exceeds gross investment.
  - D) gross investment equals depreciation.
  - E) gross investment is zero.

Answer: A

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Conceptual

AACSB: Reflective Thinking

- 9) If the economy's capital decreases over time,
- A) net investment is positive.
  - B) depreciation is less than zero.
  - C) depreciation exceeds gross investment.
  - D) gross investment equals net investment.
  - E) gross investment is zero.

Answer: C

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Conceptual

AACSB: Reflective Thinking

10) In January 2011, Tim's Gyms, Inc. owned machines valued at \$1 million. During the year, the market value of the machines fell by 10 percent. During 2011, Tim spent \$200,000 on new machines. During 2011, Tim's net investment was

- A) \$1 million.
- B) \$300,000.
- C) \$200,000.
- D) \$100,000.
- E) \$1.1 million.

Answer: D

Diff: 1 Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Analytical

AACSB: Analytical Skills

11) The Acme Stereo Company had a capital stock of \$24 million at the beginning of the year. At the end of the year, the firm had a capital stock of \$20 million. Thus its

- A) net investment was some amount but we need more information to determine the amount.
- B) net investment was \$4 million for the year.
- C) gross investment was zero.
- D) net investment was -\$4 million for the year.
- E) depreciation was \$4 million.

Answer: D

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Analytical

AACSB: Analytical Skills

12) At the beginning of the year, Tom's Tubes had a capital stock of 5 tube-inflating machines. During the year, Tom scrapped 2 old machines and purchased 3 new machines. Tom's net investment for the year totaled

- A) 1 machine.
- B) 2 machines.
- C) 3 machines.
- D) 6 machines.
- E) 5 machines

Answer: A

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Analytical

AACSB: Analytical Skills

13) At the beginning of the year, Tom's Tubes had a capital stock of 5 tube-inflating machines. During the year, Tom scrapped 2 old machines and purchased 3 new machines. Tom's gross investment for the year totaled

- A) 1 machine.
- B) 2 machines.
- C) 3 machines.
- D) 6 machines.
- E) 8 machines.

Answer: C

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Analytical

AACSB: Analytical Skills

14) At the beginning of the year, Tom's Tubes had capital of 5 tube-inflating machines. During the year, Tom scrapped 2 old machines and purchased 3 new machines. Tom's capital at the end of year was

- A) 1 machine.
- B) 2 machines.
- C) 3 machines.
- D) 6 machines.
- E) 8 machines.

Answer: D

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Analytical

AACSB: Analytical Skills

15) Which of the following is *FALSE* about saving?

- A) Saving adds to wealth.
- B) Income left after paying taxes can either be consumed or saved.
- C) Saving equals wealth minus consumption expenditure.
- D) Saving is the source of funds used to finance investment.
- E) Saving supplies funds in loan markets, bond markets, and stock markets.

Answer: C

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Recognition

AACSB: Reflective Thinking

16) At the beginning of the year, your wealth is \$10,000. During the year, you have an income of \$90,000 and you spend \$80,000 on consumption goods and services. You pay no taxes. Your wealth at the end of the year is

- A) \$20,000.
- B) \$0.
- C) \$90,000.
- D) \$100,000.
- E) \$10,000.

Answer: A

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Analytical

AACSB: Analytical Skills

17) At the beginning of the year, your wealth is \$10,000. During the year, you have an income of \$80,000 and you spend \$90,000 on consumption goods and services. You pay no taxes. Your wealth at the end of the year is

- A) \$20,000.
- B) \$0.
- C) \$90,000.
- D) \$100,000.
- E) \$10,000.

Answer: B

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Analytical

AACSB: Analytical Skills

18) In 2011, Tim's Gyms needs to finance the building of a new gym. Suppose Tim secures this financing from a bank, and the bank receives ownership if Tim fails to make payments. This type of funding is

- A) a mortgage obtained in the loan market.
- B) a stock issued in the bond market.
- C) a bond issued in the bond market.
- D) a mortgage obtained in the stock market.
- E) a stock issued in the loan market.

Answer: A

Diff: 1 Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Conceptual

AACSB: Reflective Thinking

19) The funds used to buy physical capital are

- A) net investment.
- B) financial capital.
- C) saving.
- D) wealth.
- E) investment.

Answer: B

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Recognition

AACSB: Reflective Thinking

20) This year Pizza Hut spent \$1.3 billion on new capital in its stores. Depreciation during the year was \$300 million. Pizza Hut's gross investment was \_\_\_\_\_ and its net investment was \_\_\_\_\_.

- A) \$1.3 billion; \$1.6 billion
- B) \$1.0 billion; \$1.3 billion
- C) \$1.3 billion; \$1.0 billion
- D) \$1.0 billion; \$0.7 billion
- E) \$1.3 billion; \$0.3 billion

Answer: C

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Analytical

AACSB: Analytical Skills

21) If a bank's net worth is negative, then the bank is

- A) liquid.
- B) insolvent.
- C) illiquid.
- D) solvent.
- E) none of the above.

Answer: B

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Recognition

AACSB: Reflective Thinking

22) In which market would you find mortgage-backed securities?

- A) stock market
- B) bond market
- C) housing market
- D) capital market
- E) loan market

Answer: B

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Recognition

Source: Study Guide

AACSB: Reflective Thinking

23) Elena owns a Canada Savings Bond with a price of \$5,000, which pays \$500 per year. The price of the bond rises in the bond market to \$7,500. What is the new interest rate on the bond?

- A) 5%
- B) 6.67%
- C) 10%
- D) 20%
- E) 500%

Answer: B

Type: MC

Topic: Financial Institutions and Financial Markets

Skill: Recognition

Source: Study Guide

AACSB: Reflective Thinking

24) Suppose that a bond promises to pay its holder \$100 a year forever. If the price of the bond increases from \$1,000 to \$1,250, then the interest rate on the bond \_\_\_\_\_.

- A) rises from 8 percent a year to 10 percent a year
- B) falls from 10 percent a year to 6 percent a year
- C) falls from 10 percent a year to 8 percent a year
- D) rises because the bond becomes a better investment
- E) does not change because the purchaser buys the bond knowing that interest rates will be adjusted

Answer: C

Type: MC

25) Suppose a bond promises to pay its holder \$100 a year forever. The interest rate on the bond rises from 4 percent to 5 percent. The price of the bond \_\_\_\_\_.

- A) falls from \$2,500 to \$2,000
- B) falls from \$25,000 to \$20,000
- C) rises from \$2,000 to \$2,500
- D) rises from \$20,000 to \$25,000
- E) does not change. Bond prices are constant.

Answer: A

Type: MC

26) The key Canadian financial institutions include all of the following *except* \_\_\_\_\_.

- A) commercial banks
- B) trust and loan companies
- C) credit unions and caisses populaires
- D) pension funds
- E) ATMs

Answer: E

Type: MC

27) Choose the statement that is *incorrect* about trust and loan companies.

- A) Trust and loan companies hold more than 70 percent of the total assets of the Canadian financial services sector.
- B) The largest trust and loan companies are owned by banks.
- C) Trust and loan companies accept deposits and make personal loans and mortgage loans.
- D) Trust and loan companies administer estates.
- E) Trust and loan companies administer trusts and pension plans.

Answer: A

Type: MC

28) Choose the statement that is *incorrect*.

- A) A financial institution can be solvent but illiquid.
- B) A firm is illiquid if it has made long-term loans with borrowed funds and is faced with a sudden demand to repay more of what it has borrowed than its available cash.
- C) Insolvency and illiquidity were at the core of a global financial meltdown in 2007-2008.
- D) A financial institution's net worth is the market value of what it has lent minus the market value of what it has borrowed.
- E) All of the above are true.

Answer: E

Type: MC

## 23.2 The Loanable Funds Market

1) Investment is financed by which of the following?

- I. Government spending.
  - II. Household saving.
  - III. Borrowing from the rest of the world.
- A) I, II, and III
  - B) I and II only
  - C) I and III only
  - D) II and III only
  - E) None of the above

Answer: D

Type: MC

Topic: The Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

2) National saving equals

- A) private saving + private wealth.
- B) private saving + government saving.
- C) private saving - net taxes.
- D) government saving.
- E) investment.

Answer: B

Type: MC

Topic: The Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

3) If national saving equals \$100,000, net taxes equal \$100,000 and government expenditure equals \$25,000, what is private saving?

- A) \$25,000
- B) \$225,000
- C) -\$25,000
- D) zero
- E) \$175,000

Answer: A

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

4) Suppose Canada spends more on foreign goods and services than foreigners spend on our goods and services. Then

- A) Canada must borrow an amount equal to national saving.
- B) Canada must borrow an amount equal to imports minus exports.
- C) the rest of the world may or may not finance Canada's trade deficit.
- D) Canada must borrow an amount equal to consumption expenditure plus investment.
- E) none of the above.

Answer: B

Type: MC

Topic: The Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

5) In 2011, Country A has net taxes of \$30 million and government expenditures of \$35 million. Private saving in Country A is \$5 million and consumption expenditure is \$80 million. The government of Country A is running a budget \_\_\_\_\_ and national saving is \_\_\_\_\_.

- A) surplus; \$5 million
- B) deficit; -\$5 million
- C) deficit; \$5 million
- D) surplus; \$25 million
- E) deficit; zero

Answer: E

Diff: 2 Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

Refer to the table below to answer the following questions.

**Table 23.2.1**

Item	Millions of dollars
Consumption expenditure	80
Government expenditure on goods and services	30
Net taxes	35
Investment	20
Imports	10
Exports	20

6) Refer to Table 23.2.1. Private saving is

- A) -\$15 million.
- B) \$40 million.
- C) \$25 million.
- D) \$20 million.
- E) \$80 million.

Answer: C

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

7) Refer to Table 23.2.1. Government saving is

- A) \$15 million.
- B) -\$5 million.
- C) \$5 million.
- D) \$45 million.
- E) \$20 million.

Answer: C

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

8) Approximately, the real interest rate \_\_\_\_\_ the inflation rate \_\_\_\_\_ the nominal interest rate.

- A) plus; equals
- B) equals; plus
- C) equals; minus
- D) minus; equals
- E) times; divided by 100 equals

Answer: A

Type: MC

Topic: The Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

9) The real interest rate

- A) can never be negative.
- B) is approximately equal to the nominal interest rate plus the inflation rate.
- C) is approximately equal to the nominal interest rate minus the inflation rate.
- D) increases when the inflation rate increases.
- E) none of the above.

Answer: C

Type: MC

Topic: The Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

10) Suppose that you took out a \$1,000 loan in January and had to pay \$75 in annual interest. During the year, inflation was 6 percent. Which of the following statements is correct?

- A) The nominal interest rate is 7.5 percent and the real interest rate is 1.5 percent.
- B) The nominal interest rate is 7.5 percent and the real interest rate is 13.5 percent.
- C) The real interest rate is 7.5 percent and the nominal interest rate is 1.5 percent.
- D) The real interest rate is 6 percent and the nominal interest rate is 7.5 percent.
- E) The real interest rate is 6 percent and the nominal interest rate is -1.5 percent.

Answer: A

Diff: 2 Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

11) If the nominal interest rate is 11 percent and the inflation rate is 9 percent, then the real interest rate is approximately

- A) 2 percent.
- B) 20 percent.
- C) 4 percent.
- D) 18 percent.
- E) -2 percent.

Answer: A

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

12) A firm's decision to invest in a project is based on the

- A) real interest rate and expected total revenue.
- B) nominal interest rate and expected total revenue.
- C) nominal interest rate and the expected profit.
- D) real interest rate and the expected profit.
- E) expected future income, wealth, and default risk.

Answer: D

Type: MC

Topic: The Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

13) Suppose a firm has an investment project which will cost \$200,000 and result in \$30,000 profit. The firm will not undertake the project if the interest rate is \_\_\_\_\_.

- A) greater than 15 percent
- B) greater than 10 percent
- C) greater than 5 percent
- D) positive
- E) greater than 7.5 percent

Answer: A

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

14) As the \_\_\_\_\_ interest rate increases, the quantity of loanable funds demanded \_\_\_\_\_.

A) real; increases

B) real; decreases

C) nominal; increases

D) nominal; decreases

E) None of the above. There is no relationship between interest rates and loanable funds.

Answer: B

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

15) The demand for loanable funds is the relationship between the quantity of loanable funds demanded and the \_\_\_\_\_ other things remaining the same.

A) real interest rate

B) nominal interest rate

C) inflation rate

D) price level

E) quantity of loanable funds supplied

Answer: A

Type: MC

Topic: The Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

16) The demand for loanable funds curve

A) is horizontal.

B) has a negative slope.

C) is vertical.

D) has a positive slope.

E) slopes downward at high real interest rates and slopes upward at low real interest rates.

Answer: B

Type: MC

Topic: The Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

17) As the \_\_\_\_\_ interest rate rises \_\_\_\_\_.

- A) nominal; the demand for loanable funds curve shifts rightward
- B) real; the demand for loanable funds curve shifts rightward
- C) nominal; the demand for loanable funds curve shifts leftward
- D) real; a movement occurs up along the demand for loanable funds curve
- E) real; a movement occurs down along the demand for loanable funds curve

Answer: D

Diff: 2 Type: MC

Topic: The Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

18) If the real interest rate rises from 3 percent to 5 percent,

- A) the nominal interest rate falls.
- B) the demand for loanable funds curve shifts rightward.
- C) there is a movement up along the demand for loanable funds curve.
- D) the supply of loanable funds curve shifts rightward.
- E) there is a movement down along the supply of loanable funds curve.

Answer: C

Diff: 2 Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

19) A rise in the real interest rate

- A) shifts the demand for loanable funds curve rightward.
- B) shifts the demand for loanable funds curve leftward.
- C) creates a movement up along the demand for loanable funds curve.
- D) creates a movement down along the demand for loanable funds curve.
- E) none of the above.

Answer: C

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

20) A fall in the real interest rate

- A) shifts the demand for loanable funds curve rightward.
- B) shifts the demand for loanable funds curve leftward.
- C) creates a movement up along the demand for loanable funds curve.
- D) creates a movement down along the demand for loanable funds curve.
- E) none of the above.

Answer: D

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

21) The quantity of loanable funds demanded increases when

- A) expected profit decreases.
- B) the real interest rate rises.
- C) the real interest rate falls.
- D) the supply of loanable funds decreases.
- E) wealth increases.

Answer: C

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

22) A decrease in the real interest rate leads to a \_\_\_\_\_ the demand for loanable funds curve, and a decrease in expected profit leads to a \_\_\_\_\_ the demand for loanable funds curve.

- A) rightward shift of; leftward shift of
- B) movement down along; movement up along
- C) rightward shift of; movement up along
- D) movement down along; leftward shift of
- E) movement down along; rightward shift of

Answer: D

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

23) A decrease in the demand for loanable funds occurs when

- A) the real interest rate rises.
- B) the government raises taxes.
- C) the government cuts taxes.
- D) expected profit decreases.
- E) expected profit increases.

Answer: D

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

24) During a recession, firms decrease their profit expectations. As a result, there is a \_\_\_\_\_ shift of the \_\_\_\_\_ loanable funds curve.

- A) rightward; supply of
- B) leftward; demand for
- C) rightward; demand for
- D) rightward, supply of
- E) leftward; demand for loanable funds curve and supply of

Answer: B

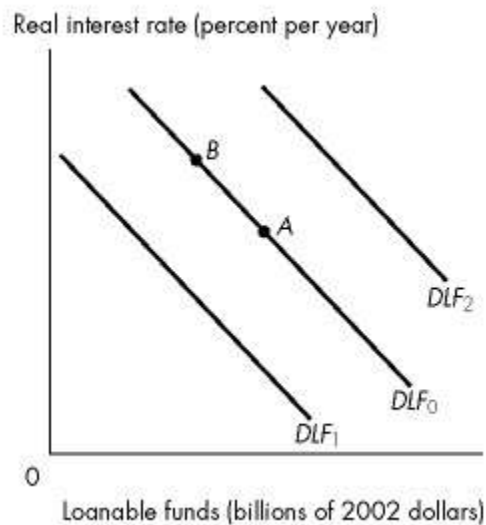
Diff: 2 Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

Refer to the figure below to answer the following question.



**Figure 23.2.1**

25) Refer to Figure 23.2.1. In Figure 23.2.1, the economy is at point A on the initial demand for loanable funds curve  $DLF_0$ . What happens if the real interest rate rises?

- A) There is a movement to a point such as B on the demand for loanable funds curve  $DLF_0$ .
- B) The demand for loanable funds curve shifts rightward to curve  $DLF_2$ .
- C) The demand for loanable funds curve shifts leftward to curve  $DLF_1$ .
- D) Either A or B can occur.
- E) Either A or C can occur.

Answer: A

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

Refer to the figure below to answer the following questions.

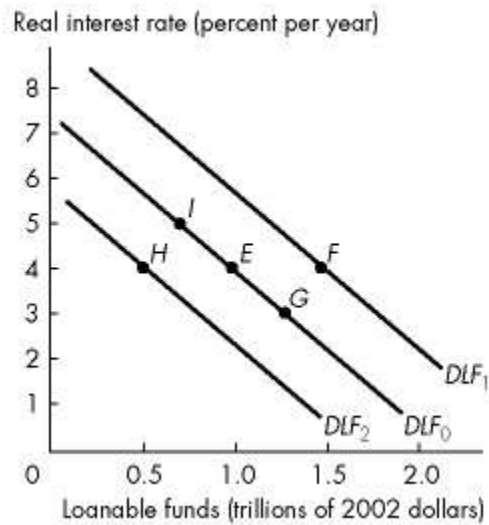


Figure 23.2.2

26) Refer to Figure 23.2.2. In Figure 23.2.2, a decrease in the real interest rate will result in a movement from point *E* to

- A) point *F*.
- B) point *G*.
- C) point *H*.
- D) point *I*.
- E) either point *G* or point *F*.

Answer: B

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

27) Refer to Figure 23.2.2. In Figure 23.2.2, an increase in expected profit will result in a movement from point *E* to

- A) point *F*.
- B) point *G*.
- C) point *H*.
- D) point *I*.
- E) either point *I* or point *F*.

Answer: A

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

28) Refer to Figure 23.2.2. In Figure 23.2.2, a decrease in expected profit will result in a movement from point *E* to

- A) point *F*.
- B) point *G*.
- C) point *H*.
- D) point *I*.
- E) either point *G* or point *H*.

Answer: C

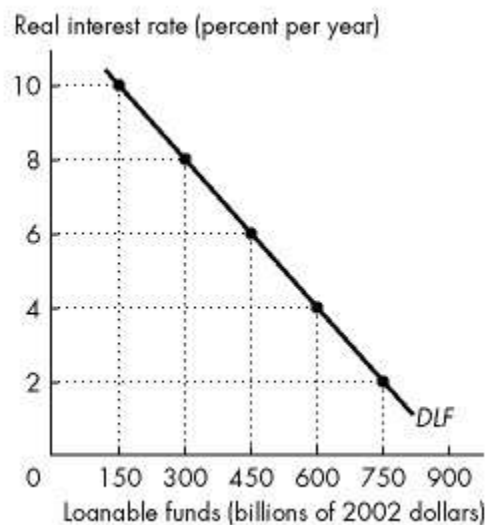
Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

*Refer to the figure below to answer the following questions.*



**Figure 23.2.3**

29) Refer to Figure 23.2.3. In Figure 23.2.3, if the real interest rate is 6 percent, the quantity of loanable funds demanded is

- A) \$150 billion.
- B) \$300 billion.
- C) \$450 billion.
- D) \$600 billion.
- E) only amount less than \$450 billion.

Answer: C

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

30) In Figure 23.2.3, if the real interest rate is constant at 6 percent and expected profit falls, the quantity of loanable funds demanded will be

- A) less than \$450 billion.
- B) \$450 billion.
- C) between \$450 billion and \$600 billion.
- D) greater than \$600 billion.
- E) zero.

Answer: A

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

31) In Figure 23.2.3, if the real interest rate is constant at 6 percent and expected profit rises, the amount of loanable funds demanded will be

- A) less than \$450 billion.
- B) \$450 billion.
- C) between \$300 billion and \$450 billion.
- D) greater than \$450 billion.
- E) zero.

Answer: D

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

32) All of the following are sources of loanable funds *EXCEPT*

- A) business investment.
- B) private saving.
- C) government budget surplus.
- D) international borrowing.
- E) none of the above.

Answer: A

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

33) Which of the following influences household saving?

- I. The real interest rate.
  - II. Disposable income.
  - III. Expected future income.
- A) I only
  - B) I and II
  - C) I and III
  - D) I, II, and III
  - E) None of the above

Answer: D

Type: MC

Topic: The Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

34) If households' disposable income decreases, then

- A) households' saving will decrease.
- B) households' saving will increase.
- C) the supply of loanable funds decreases.
- D) a movement occurs down along the supply of loanable funds curve.
- E) both A and C are correct.

Answer: E

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

35) Households will choose to save more if

- A) expected future income decreases.
- B) current disposable income increases.
- C) current disposable income decreases.
- D) both A and B are correct.
- E) both A and C are correct.

Answer: D

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

36) Which of the following is correct?

- A) As disposable income increases, the real interest rate rises.
- B) As disposable income decreases, saving decreases.
- C) The higher a household's wealth the greater is its saving.
- D) Both B and C are correct.
- E) Both A and C are correct.

Answer: B

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

37) \_\_\_\_\_ increases households' saving.

- A) A decrease in the real interest rate
- B) A tax cut that increases disposable income
- C) Higher expected future income
- D) An increase in wealth
- E) An increase in default risk

Answer: B

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

38) The greater a household's \_\_\_\_\_ the less is its saving.

- A) return from saving
- B) wealth
- C) disposable income
- D) expected future profit
- E) all of the above

Answer: B

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

39) As the \_\_\_\_\_ rises, the quantity of loanable funds supplied \_\_\_\_\_ other things remaining the same.

- A) nominal interest rate; increases
- B) real interest rate; increases
- C) inflation rate; increases
- D) real interest rate; decreases
- E) inflation rate; decreases

Answer: B

Type: MC

Topic: The Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

40) The supply of loanable funds is the relationship between the quantity loanable funds supplied and \_\_\_\_\_ other things remaining the same.

- A) real GDP
- B) the price level
- C) the real interest rate
- D) the inflation rate
- E) the nominal interest rate

Answer: C

Type: MC

Topic: The Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

41) The supply of loanable funds curve

- A) has a positive slope.
- B) is vertical.
- C) is horizontal.
- D) has a negative slope.
- E) is upward sloping at low real interest rates and downward sloping at high real interest rates.

Answer: A

Type: MC

Topic: The Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

42) Changes in all of the following *shift* the supply curve of loanable funds *EXCEPT*

- A) the real interest rate.
- B) wealth.
- C) disposable income.
- D) expected future income.
- E) default risk.

Answer: A

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

43) Which of the following will shift the supply of loanable funds curve leftward?

- A) a decrease in the real interest rate
- B) a decrease in real wealth
- C) a decrease in disposable income
- D) a decrease in expected future income
- E) a decrease in default risk

Answer: C

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Analytical Skills

44) An increase in \_\_\_\_\_ will shift the supply of loanable funds curve \_\_\_\_\_.

- A) expected future income; rightward
- B) wealth; leftward
- C) disposable income; leftward
- D) default risk; rightward
- E) the real interest rate; rightward

Answer: B

Diff: 2 Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Analytical Skills

45) As a result of a recession, the default risk increases. How does this change affect the loanable funds market?

- A) There is a movement up along the supply of loanable funds curve.
- B) There is a leftward shift of the supply of loanable funds curve.
- C) There is a movement down along the demand for loanable funds curve.
- D) There is a rightward shift of the supply of loanable funds curve.
- E) There is a movement up along the demand for loanable funds curve.

Answer: B

Diff: 2 Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Analytical Skills

46) When the real interest rate increases,

- A) the supply of loanable funds curve shifts rightward.
- B) the supply of loanable funds curve shifts leftward.
- C) there is a movement up along the supply of loanable funds curve.
- D) there is a movement down along the supply of loanable funds curve.
- E) the demand for loanable funds curve shifts leftward.

Answer: C

Type: MC

Topic: The Market for Loanable Funds

Skill: Recognition

AACSB: Analytical Skills

47) Which of the following is true?

- I. As the real interest rate increases, people increase the quantity they save.
- II. The supply of loanable funds curve is downward sloping.
- III. As disposable income increases, the supply of loanable funds curve becomes steeper.

- A) I and III only
- B) II and III only
- C) I only
- D) III only
- E) I, II, and III

Answer: C

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

- 48) A decrease in disposable income \_\_\_\_\_.
- A) has no effect on the supply of loanable funds curve
  - B) shifts the supply of loanable funds curve rightward
  - C) shifts the supply of loanable funds curve leftward
  - D) creates a movement up along the supply of loanable funds curve
  - E) creates a movement down along the supply of loanable funds curve

Answer: C

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

- 49) If households believe they will experience higher income in the near future, there is a
- A) rightward shift of the supply of loanable funds curve.
  - B) leftward shift of the supply of loanable funds curve.
  - C) movement up along the supply of loanable funds curve.
  - D) movement up along the demand for loanable funds curve.
  - E) rightward shift of the demand for loanable funds curve.

Answer: B

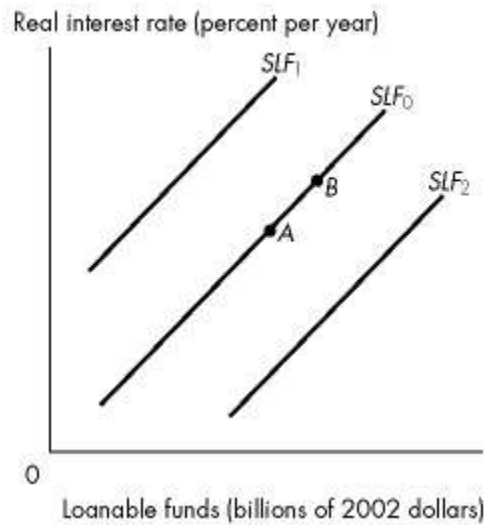
Diff: 2 Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

Refer to the figure below to answer the following questions.



**Figure 23.2.4**

50) Refer to Figure 23.2.4. In Figure 23.2.4, the economy is at point A on the supply of loanable funds curve  $SLF_0$ . What happens if disposable income decreases?

- A) Nothing; the economy would remain at point A.
- B) There is a movement to a point such as B on the supply of loanable funds curve  $SLF_0$ .
- C) The supply of loanable funds curve shifts rightward to a curve such as  $SLF_2$ .
- D) The supply of loanable funds curve shifts leftward to a curve such as  $SLF_1$ .
- E) None of the above.

Answer: D

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

51) Refer to Figure 23.2.4. In Figure 23.2.4, the economy is at point A on the supply of loanable funds curve  $SLF_0$ . What happens if the real interest rate rises?

- A) Nothing; the economy would remain at point A.
- B) There is a movement to a point such as B on the supply of loanable funds curve  $SLF_0$ .
- C) The supply of loanable funds curve shifts rightward to a curve such as  $SLF_2$ .
- D) The supply of loanable funds curve shifts leftward to a curve such as  $SLF_1$ .
- E) None of the above.

Answer: B

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

52) In the market for loanable funds, as the real interest rate rises the \_\_\_\_\_ and the \_\_\_\_\_.

- A) quantity of loanable funds supplied increases; quantity of loanable funds demanded decreases
- B) quantity of loanable funds supplied decreases; quantity of loanable funds demanded increases
- C) supply of loanable funds increases; demand for loanable funds decreases
- D) supply of loanable funds decreases; demand for loanable funds increases
- E) quantity of loanable funds supplied increases; supply of loanable funds increases

Answer: A

Type: MC

Topic: The Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

53) The equilibrium real interest rate is determined by the

- A) demand for loanable funds curve and the supply of loanable funds curve.
- B) demand for loanable funds curve and real GDP.
- C) supply of loanable funds curve and financial institutions.
- D) government expenditure curve and the taxation curve.
- E) banks and insurance companies.

Answer: A

Type: MC

Topic: The Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

54) Suppose the current real interest rate is 4 percent and the equilibrium real interest rate is 3 percent. Choose the correct statement.

- A) The supply of loanable funds increases.
- B) There is a surplus of loanable funds.
- C) There is a shortage of loanable funds.
- D) There is neither a shortage nor surplus of loanable funds.
- E) The demand for loanable funds decreases.

Answer: B

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Analytical Skills

55) If the quantity of loanable funds supplied exceeds the quantity of loanable funds demanded, then \_\_\_\_\_.

- A) the real interest rate will rise
- B) the supply of loanable funds increases
- C) people will save more
- D) the real interest rate will fall
- E) the demand for loanable funds increases

Answer: D

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

56) If the real interest rate is above the equilibrium real interest rate,

- A) lenders are unable to find borrowers willing to borrow all of the available funds and the real interest rate falls.
- B) borrowers are unable to borrow all of the funds they want to borrow and the real interest rate rises.
- C) lenders are unable to find borrowers willing to borrow all of the available funds and the real interest rate rises.
- D) borrowers are unable to borrow all of the funds they want to borrow and the real interest rate falls.
- E) a shortage of loanable funds exists.

Answer: A

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

57) If the real interest rate is below the equilibrium real interest rate,

- A) lenders are unable to find borrowers willing to borrow all of the available funds and the real interest rate falls.
- B) borrowers are unable to borrow all of the funds they want to borrow and the real interest rate rises.
- C) lenders are unable to find borrowers willing to borrow all of the available funds and the real interest rate rises.
- D) borrowers are unable to borrow all of the funds they want to borrow and the real interest rate falls.
- E) a surplus of loanable funds exists.

Answer: B

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

- 58) If the real interest rate is below the equilibrium real interest rate,
- A) lenders will be unable to find borrowers willing to borrow all of the available funds and the supply of loanable funds curve shifts leftward.
  - B) borrowers will be unable to borrow all of the funds they want to borrow and the demand for loanable funds curve shifts rightward.
  - C) a shortage of loanable funds exists, and the real interest rate rises.
  - D) borrowers will be unable to borrow all of the funds they want to borrow and the demand for loanable funds curve shifts leftward.
  - E) lenders will be unable to find borrowers willing to borrow all of the available funds and the supply of loanable funds curve shifts rightward.

Answer: C

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

- 59) In the market for loanable funds, if the interest rate is above the equilibrium level
- A) a shortage of loanable funds exists.
  - B) a surplus of loanable funds exists.
  - C) expected profit falls.
  - D) government expenditure decreases.
  - E) wealth increases.

Answer: B

Type: MC

Topic: The Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

- 60) An increase in disposable income shifts the supply of loanable funds curve
- A) leftward and decreases the real interest rate.
  - B) leftward and increases the real interest rate.
  - C) rightward and decreases the real interest rate.
  - D) rightward and increases the real interest rate.
  - E) rightward and the demand for loanable funds curve leftward.

Answer: C

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

61) Technological progress that increases expected profit shifts the demand for loanable funds curve

- A) leftward and decreases the real interest rate.
- B) rightward and increases the real interest rate.
- C) rightward and decreases the real interest rate.
- D) leftward and increases the real interest rate.
- E) rightward and the supply of loanable funds curve leftward.

Answer: B

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

62) What is the effect of a decrease in expected profit?

- A) The demand curve for loanable funds shifts leftward and the real interest rate falls.
- B) The supply curve of loanable funds shifts rightward and the nominal interest rate rises.
- C) A movement down along the demand curve for loanable funds occurs.
- D) The real interest rate rises as saving increases.
- E) The demand curve for loanable funds shifts rightward and the real interest rate rises.

Answer: A

Diff: 2 Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

63) If disposable income increases, people \_\_\_\_\_ saving, the supply of loanable funds will \_\_\_\_\_ and the real interest rate will \_\_\_\_\_.

- A) increase; decrease; rise
- B) decrease; decrease; rise
- C) increase; increase; fall
- D) decrease; increase; fall
- E) increase; increase; rise or fall depending on the shift of the demand curve for loanable funds

Answer: C

Diff: 2 Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

64) Suppose the market for loanable funds is in equilibrium. If expected profit falls, the equilibrium real interest rate \_\_\_\_\_ and the quantity of loanable funds \_\_\_\_\_.

A) falls; decreases

B) falls; increases

C) rises; increases

D) rises; decreases

E) falls; increases or decreases but we don't know for sure

Answer: A

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

Refer to the figure below to answer the following questions.

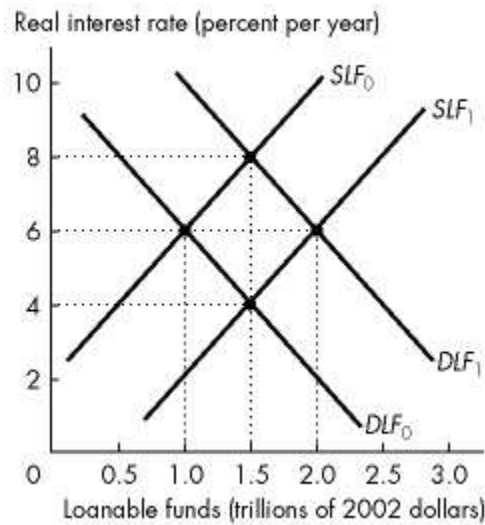


Figure 23.2.5

65) Refer to Figure 23.2.5. In Figure 23.2.5, the supply of loanable funds curve is  $SLF_0$  and the demand for loanable funds curve is  $DLF_0$ . An expansion that increases disposable income and expected profit

- A) shifts the supply of loanable funds curve rightward to curve  $SLF_1$  and does not shift the demand for loanable funds curve.
- B) shifts the supply of loanable funds curve rightward to curve  $SLF_1$ , and shifts the demand for loanable funds curve rightward to curve  $DLF_1$ .
- C) shifts the demand for loanable funds curve rightward to curve  $DLF_1$  and does not shift the supply of loanable funds curve.
- D) has no effect on either the demand for loanable funds curve or the supply of loanable funds curve.
- E) none of the above.

Answer: B

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

- 66) Refer to Figure 23.2.5. In Figure 23.2.5, the initial supply of loanable funds curve is  $SLF_0$  and the initial demand for loanable funds curve is  $DLF_0$ . An increase in the expected profit
- A) shifts the supply of loanable funds curve rightward to curve  $SLF_1$  and does not shift the demand for loanable funds curve.
  - B) shifts the supply of loanable funds curve rightward to curve  $SLF_1$ , and shifts the demand for loanable funds curve rightward to curve  $DLF_1$ .
  - C) shifts the demand for loanable funds curve rightward to curve  $DLF_1$  and does not shift the supply of loanable funds curve.
  - D) has no effect on either the demand for loanable funds curve or the supply of loanable funds curve.
  - E) none of the above.

Answer: C

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

67) Which of the following is *false*?

- A)  $Y = C + I + G + M - X$
- B)  $I = S + (T - G) + (M - X)$
- C)  $Y = C + S + T$
- D)  $Y + M = C + I + G + X$
- E)  $Y = C + I + G + X - M$

Answer: A

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

Source: Study Guide

AACSB: Analytical Skills

68) In Canada's economy, investment is financed by

- A)  $C + I + G + X - M$ .
- B)  $C + S + T$ .
- C)  $S + T + M$ .
- D)  $S + (T - G) + (X - M)$ .
- E)  $S + (T - G) + (M - X)$ .

Answer: E

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

Source: Study Guide

AACSB: Analytical Skills

- 69) Investment will be higher if
- A) the government deficit is higher.
  - B) national saving is higher.
  - C) net exports are higher.
  - D) the real interest rate is higher.
  - E) government spending is higher.

Answer: B

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

Source: Study Guide

AACSB: Analytical Skills

70) Southton has investment of \$100, private saving of \$90, net taxes of \$25, government expenditure of \$30, exports of \$25 and imports of \$10. What is national saving?

- A) \$85
- B) \$90
- C) \$95
- D) \$100
- E) \$105

Answer: A

Type: MC

Topic: The Market for Loanable Funds

Skill: Analytical

Source: Study Guide

AACSB: Analytical Skills

71) When the inflation rate is zero, the \_\_\_\_\_.

- A) real interest rate equals the nominal interest rate
- B) demand for loanable funds increases
- C) supply of loanable funds decreases
- D) nominal interest rate is zero
- E) Both B and C occur.

Answer: A

Type: MC

72) Which of the following explains why the demand for loanable funds is negatively related to the real interest rate?

- A) Consumers are willing to spend less so they save more at higher real interest rates.
- B) Interest rate flexibility in financial markets assures an equilibrium in which saving equals investment.
- C) A lower real interest rate makes more investment projects profitable.
- D) All of the above are reasons why the demand for loanable funds is negatively related to the real interest rate.
- E) None of the above are reasons why the demand for loanable funds is negatively related to the real interest rate.

Answer: C

Type: MC

### 23.3 Government in the Loanable Funds Market

1) If net taxes exceed government expenditures, the government sector has a budget \_\_\_\_\_ and government saving is \_\_\_\_\_.

- A) surplus; positive
- B) surplus; negative
- C) deficit; positive
- D) deficit; negative
- E) balance that is zero; zero

Answer: A

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

2) When a government has a budget surplus, the surplus

- A) helps finance investment.
- B) crowds-out private saving.
- C) must be subtracted from private saving.
- D) increases the world real interest rate.
- E) decreases the demand for loanable funds.

Answer: A

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

3) When government saving is negative,

- A) the real interest rate rises.
- B) the real interest rate falls.
- C) investment increases.
- D) the real interest rate falls if crowding-out occurs.
- E) the supply of loanable funds increases.

Answer: A

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

- 4) The tendency for a government budget deficit to decrease investment is called the
- A) government dissaving effect.
  - B) crowding-out effect.
  - C) Ricardo-Barro effect.
  - D) capital investment effect.
  - E) deficit effect.

Answer: B

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

- 5) The crowding-out effect refers to
- A) government spending crowding out private spending.
  - B) private saving crowding out government saving.
  - C) a government deficit crowding out investment.
  - D) private investment crowding out government saving.
  - E) private saving crowding out net taxes.

Answer: C

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

- 6) Crowding out leads to all of the following *EXCEPT*
- A) a higher real interest rate.
  - B) a decrease in investment.
  - C) a smaller quantity of capital in the future.
  - D) a decrease in private saving.
  - E) crowding out leads to all of the above.

Answer: D

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Conceptual

AACSB: Reflective Thinking

- 7) If the government begins to run a larger budget deficit, the demand for loanable funds \_\_\_\_\_ and the real interest rate \_\_\_\_\_.
- A) decreases; falls
  - B) decreases; rises
  - C) increases; rises
  - D) increases; falls
  - E) increases; rises or falls depending on the change in the supply of loanable funds

Answer: C

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Analytical

AACSB: Reflective Thinking

8) A government budget deficit \_\_\_\_\_ the demand for loanable funds and \_\_\_\_\_ investment.

- A) increases; increases
- B) increases; decreases
- C) decreases; increases
- D) decreases; decreases
- E) increases; rises or falls depending on the change in the supply of loanable funds

Answer: B

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Analytical

AACSB: Reflective Thinking

9) A government budget deficit \_\_\_\_\_ the demand for loanable funds, \_\_\_\_\_ the real interest rate, and \_\_\_\_\_ investment.

- A) increases; decreases; crowds out
- B) increases; decreases; increases
- C) decreases; increases; increases
- D) decreases; increases; crowds out
- E) increases; increases; crowds out

Answer: E

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Analytical

AACSB: Reflective Thinking

10) If China's government increases its budget surplus, there is \_\_\_\_\_ in the supply of loanable funds, private saving \_\_\_\_\_ and investment \_\_\_\_\_.

- A) an increase; decreases; increases
- B) a decrease; increases; increases
- C) an increase; increases; increases
- D) a decrease; decreases; increases
- E) an increase; decreases; is crowded out

Answer: A

Diff: 3 Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

11) The tendency for private saving to increase in response to growing government deficits is known as the

- A) crowding out effect.
- B) money illusion effect.
- C) Keynes effect.
- D) Ricardo-Barro effect.
- E) Mulroney-Harper effect.

Answer: D

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

12) According to the Ricardo-Barro effect,

- A) government deficits raise the real interest rate.
- B) taxpayers fail to foresee that government deficits imply higher future taxes.
- C) households increase personal saving when governments run budget deficits.
- D) government budget deficits increase households' expected future disposable income.
- E) a government deficit decreases the supply of loanable funds.

Answer: C

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

13) The Ricardo-Barro effect of a government budget deficit is

- A) an increase in private saving.
- B) a large crowding-out effect that decreases investment.
- C) a large crowding-out effect that decreases national saving.
- D) a decrease in net exports.
- E) a decrease in private saving.

Answer: A

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

14) The Ricardo-Barro effect holds that

- A) equal increases in taxes and government expenditures have no effect on equilibrium real GDP.
- B) a government budget deficit has no effect on the real interest rate.
- C) a government budget deficit crowds out private investment.
- D) a government budget deficit induces a decrease in saving that magnifies the crowding out effect.
- E) none of the above.

Answer: B

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

15) According to the Ricardo-Barro effect, government deficits

- A) lead to a rise in the equilibrium real interest rate, crowding out investment.
- B) lead to simultaneous increases in private saving and have no effect on the equilibrium real interest rate and investment.
- C) lead to simultaneous decreases in private saving and decreases in the equilibrium real interest rate and investment.
- D) lead to a fall in the equilibrium real interest rate and an increase in investment.
- E) raise the real interest rate but have no effect on the nominal interest rate.

Answer: B

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

16) According to the Ricardo-Barro effect,

- A) the government budget has no effect on the real interest rate.
- B) a government budget deficit crowds out private investment.
- C) financing government spending with taxes has a less severe effect on private investment than financing through government borrowing.
- D) All of the above.
- E) None of the above.

Answer: A

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Recognition

AACSB: Reflective Thinking

17) If the Ricardo-Barro effect occurs, \_\_\_\_\_ in private saving finances the government budget deficit and the real interest rate \_\_\_\_\_.

- A) an increase; remains the same
- B) a decrease; increases
- C) an increase; falls
- D) a decrease; remains the same
- E) an increase; rises

Answer: A

Diff: 2 Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

18) If the Ricardo-Barro effect occurs, a government budget deficit raises the equilibrium real interest rate by \_\_\_\_\_ and decreases the equilibrium quantity of investment by \_\_\_\_\_ if the Ricardo-Barro effect is absent.

- A) more; more than
- B) more; less than
- C) less; more than
- D) less; less than
- E) the same amount; the same amount as

Answer: D

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Analytical

AACSB: Analytical Skills

19) A decrease in the government budget deficit decreases the \_\_\_\_\_ loanable funds and an increase in the government budget surplus increases the \_\_\_\_\_ loanable funds.

- A) demand for; demand for
- B) demand for; supply of
- C) supply of; demand for
- D) supply of; supply of
- E) demand for loanable funds and the supply of; supply of loanable funds and the demand for

Answer: B

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Conceptual

AACSB: Analytical Skills

Use the table below to answer the following question.

**Table 23.3.1**  
Data from Northland

Real interest rate (percent per year)	Demand for Loanable Funds (billions of dollars)	Supply of Loanable Funds (billions of dollars)
3	160	40
4	140	60
5	120	80
6	100	100
7	80	120
8	60	140

20) Refer to Table 23.3.1. Table 23.3.1 shows the market for loanable funds in Northland. The government budget is balanced. If the government moves from a balanced budget to a surplus of \$20 billion, the new equilibrium has a real interest rate of \_\_\_\_\_ percent and quantity of loanable funds traded equal to \_\_\_\_\_.

- A) 6.5; \$110 billion
- B) 6.5; \$90 billion
- C) 5.5; \$90 billion
- D) 5.5; \$110 billion
- E) 6; \$120 billion

Answer: D

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

21) In the market for loanable funds, a larger government surplus leads to

- A) a higher real interest rate, and increased investment.
- B) a higher real interest rate, and decreased investment.
- C) a lower real interest rate, and increased investment.
- D) a lower real interest rate, and decreased investment.
- E) no effect on the real interest rate or investment.

Answer: C

Type: MC

Topic: Government in the Market for Loanable Funds

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

22) Choose the statement that is *incorrect*.

- A) According to the Ricardo-Barro effect, taxpayers are rational people who know that a budget deficit today means that future taxes will be higher and future disposable incomes will be smaller.
- B) According to the Ricardo-Barro effect, a budget deficit has no effect on either the real interest rate or investment.
- C) Most economists believe that the Ricardo-Barro effect holds in the market for loanable funds.
- D) According to the Ricardo-Barro effect, the quantity of loanable funds demanded increases when a government budget deficit occurs, and private saving and the private supply of loanable funds increase to match the quantity of loanable funds demanded.
- E) All of the above statements are correct.

Answer: C

Diff: 2 Type: MC

Topic: Government in the Market for Loanable Funds

Source: MyEconLab

23) A government budget surplus occurs, which \_\_\_\_\_ loanable funds. The real interest rate \_\_\_\_\_, household saving \_\_\_\_\_, and investment \_\_\_\_\_.

- A) increases the demand for; rises; increases; decreases
- B) increases the supply of; falls; increases; decreases
- C) increases the supply of; falls; decreases; increases
- D) decreases the demand for; falls; decreases; increases
- E) decreases the supply of; decreases; decreases; increases

Answer: C

Diff: 2 Type: MC

Topic: Government in the Market for Loanable Funds

Source: MyEconLab

Refer to the table below to answer the following question.

**Table 23.3.2**

Real interest rate (percent per year)	Loanable funds demanded (trillions of 2002 dollars)	Loanable funds supplied (trillions of 2002 dollars)
4	8.5	5.5
5	8.0	6.0
6	7.5	6.5
7	7.0	7.0
8	6.5	7.5
9	6.0	8.0
10	5.5	8.5

24) Refer to Table 23.3.2. The table shows an economy's demand for loanable funds and supply of loanable funds schedules when the government's budget is balanced. The quantity of loanable funds demanded increases by \$1 trillion at each real interest rate and the quantity of loanable funds supplied increases by \$2 trillion at each real interest rate. If the government wants investment to be \$9 trillion, it must \_\_\_\_\_ its budget balance by \_\_\_\_\_ trillion.

- A) increase; \$1
- B) decrease; \$1
- C) increase; \$1.5
- D) decrease; \$1.5
- E) increase; \$2

Answer: A

Diff: 2 Type: MC

Topic: Government in the Market for Loanable Funds

Source: MyEconLab

Refer to the table below to answer the following question.

**Table 23.3.3**

Real interest rate (percent per year)	Loanable funds demanded (trillions of 2002 dollars)	Loanable funds supplied (trillions of 2002 dollars)
4	7.5	4.5
5	7.0	5.0
6	6.5	5.5
7	6.0	6.0
8	5.5	6.5
9	5.0	7.0
10	4.5	7.5

25) Refer to Table 23.3.3. The table shows the demand for loanable funds schedule and the private supply of loanable funds schedule when the government's budget is balanced. If the Ricardo-Barro effect occurs, and if the government budget deficit is \$2.0 trillion, the real interest rate is \_\_\_\_\_ percent a year and the quantity of investment is \_\_\_\_\_ trillion.

- A) 5.0; \$5.0
- B) 9.0; \$7.0
- C) 3.0; \$7.5
- D) 5.0; \$7.0
- E) 7.0; \$6.0

Answer: E

Diff: 2 Type: MC

Topic: Government in the Market for Loanable Funds

Source: MyEconLab

Refer to the table below to answer the following question.

**Table 23.3.4**

Real interest rate (percent per year)	Loanable funds demanded (trillions of 2002 dollars)	Loanable funds supplied (trillions of 2002 dollars)
4	7.0	7.0
5	6.5	7.5
6	6.0	8.0
7	5.5	8.5
8	5.0	9.0
9	4.5	9.5
10	4.0	10.0

26) Refer to Table 23.3.4. The table shows an economy's demand for loanable funds schedule and the private supply of loanable funds schedule when the government's budget is balanced. If the government budget deficit is \$1.0 trillion, the real interest rate is \_\_\_\_\_ percent a year, the quantity of investment is \_\_\_\_\_ trillion, and the quantity of private saving is \_\_\_\_\_ trillion.

- A) 7; \$5.5; \$8.5
- B) 7; \$8.5; \$5.5
- C) 5; \$6.5; \$7.5
- D) 3; \$6.5; \$7.0
- E) 5; \$7.5; \$6.5

Answer: C

Diff: 2 Type: MC

Topic: Government in the Market for Loanable Funds

Source: MyEconLab

Refer to the table below to answer the following question.

**Table 23.3.5**

Real interest rate (percent per year)	Loanable funds demanded (trillions of 2002 dollars)	Loanable funds supplied (trillions of 2002 dollars)
4	8.5	4.5
5	8.0	5.0
6	7.5	5.5
7	7.0	6.0
8	6.5	6.5
9	6.0	7.0
10	5.5	7.5

27) Refer to Table 23.3.5. The table shows an economy's demand for loanable funds schedule and supply of loanable funds schedule when the government's budget is balanced. If the government budget surplus is \$2.0 trillion, the real interest rate is \_\_\_\_\_ percent a year, the quantity of investment is \_\_\_\_\_ trillion, and the quantity of private saving is \_\_\_\_\_ trillion.

- A) 10; \$5.5; \$7.5
- B) 10; \$7.5; \$5.5
- C) 8; \$6.5; \$6.5
- D) 6; \$7.5; \$7.5
- E) 6; \$7.5; \$5.5

Answer: E

Diff: 2 Type: MC

Topic: Government in the Market for Loanable Funds

Source: MyEconLab

28) The government of Greece is running a large budget deficit. With no Ricardo-Barro effect, which of the following events will occur?

- I. The supply curve of loanable funds will shift leftward.
  - II. A higher real interest rate crowds out investment.
  - III. Saving increases.
- A) I only
  - B) II only
  - C) III only
  - D) I and II only
  - E) I, II, and III

Answer: D

Type: MC

### 23.4 The Global Loanable Funds Market

- 1) If we import more than we export from the rest of the world we
- A) are a net borrower of funds from the rest of the world.
  - B) are a net lender of funds to the rest of the world.
  - C) are running a trade surplus.
  - D) are helping to finance investment in the rest of the world.
  - E) have a surplus of funds at the world equilibrium interest rate.

Answer: A

Type: MC

Topic: The Global Loanable Funds Market

Skill: Recognition

AACSB: Reflective Thinking

- 2) Real interest rates around the world tend to
- A) be quite different because no two countries are exactly the same.
  - B) be equal after adjusting for differences in risk because financial capital seeks the highest possible return.
  - C) differ because inflation rates differ across countries.
  - D) be equal because trading partners would not do business otherwise.
  - E) none of the above.

Answer: B

Diff: 3 Type: MC

Topic: The Global Loanable Funds Market

Skill: Conceptual

AACSB: Reflective Thinking

- 3) The real interest rate is \_\_\_\_\_ in Canada compared to Zimbabwe because \_\_\_\_\_.
- A) lower; there is a lower risk premium in Canada
  - B) higher; more firms want to borrow financial capital in Canada than in Zimbabwe
  - C) lower; Canada is a net borrower
  - D) higher; Zimbabwe is a net borrower
  - E) higher; the supply of loanable funds is greater in Canada

Answer: A

Diff: 2 Type: MC

Topic: The Global Loanable Funds Market

Skill: Conceptual

AACSB: Reflective Thinking

4) A small country is a net foreign borrower. Its real interest rate without foreign borrowing is \_\_\_\_\_ the world real interest rate.

- A) higher than
- B) equal to
- C) lower than
- D) not comparable to
- E) either higher than or equal to

Answer: A

Type: MC

Topic: The Global Loanable Funds Market

Skill: Conceptual

AACSB: Reflective Thinking

5) A very small country is a net foreign borrower. Its supply of loanable funds increases but it still remains a net foreign borrower. As a result, the equilibrium quantity of loanable funds used in the country \_\_\_\_\_ and the country's foreign borrowing \_\_\_\_\_.

- A) does not change; decreases
- B) does not change; does not change
- C) does not change; increases
- D) increases; does not change
- E) increases; decreases

Answer: A

Type: MC

Topic: The Global Loanable Funds Market

Skill: Analytical

AACSB: Analytical Skills

6) A very small country is a net foreign borrower and its demand for loanable funds increases. As a result, the equilibrium quantity of loanable funds used in the country \_\_\_\_\_ and the country's foreign borrowing \_\_\_\_\_.

- A) does not change; increases
- B) does not change; does not change
- C) increases; increases
- D) increases; does not change
- E) increases; decreases

Answer: C

Type: MC

Topic: The Global Loanable Funds Market

Skill: Analytical

AACSB: Analytical Skills

7) A very small country is a net foreign lender and its supply of loanable funds increases. As a result, the equilibrium quantity of loanable funds used in the country \_\_\_\_\_ and the country's foreign lending \_\_\_\_\_.

- A) increases; decreases
- B) does not change; does not change
- C) does not change; increases
- D) increases; does not change
- E) does not change; decreases

Answer: C

Type: MC

Topic: The Global Loanable Funds Market

Skill: Analytical

AACSB: Analytical Skills

8) If the world real interest rate falls, then a country that is a net foreign lender

- A) increases the amount of its lending.
- B) does not change the amount of its lending.
- C) decreases the amount of its lending.
- D) changes from being a net foreign lender to a net foreign borrower.
- E) none of the above.

Answer: C

Type: MC

Topic: The Global Loanable Funds Market

Skill: Analytical

AACSB: Analytical Skills

9) Loanable funds flow among countries because \_\_\_\_\_.

- A) including differences in risk, the real interest rate is always higher in some countries than in others and this real interest rate differential will not change
- B) funds flow into the country with the highest nominal interest rate and out of the country in which the nominal interest rate is lowest
- C) it creates more stability for domestic businesses to have foreign investors
- D) funds flow into the country with the highest real interest rate and out of the country in which the real interest rate is lowest
- E) rational investors want diversified portfolios

Answer: D

Type: MC

Topic: The Global Loanable Funds Market

Skill: Analytical

Source: MyEconLab

AACSB: Analytical Skills

10) In an individual economy that is integrated into the global market, the demand for loanable funds is determined by the \_\_\_\_\_ demand and the supply of loanable funds is determined by the \_\_\_\_\_ supply.

- A) country's; world's
- B) country's; country's
- C) world's; country's
- D) world's; world's
- E) world's; World Bank's

Answer: A

Type: MC

Topic: The Global Loanable Funds Market

Skill: Analytical

Source: MyEconLab

AACSB: Analytical Skills

11) If a country has a shortage of loanable funds at the world real interest rate \_\_\_\_\_.

- A) the country increases its net exports
- B) the country decreases its net exports
- C) the demand for loanable funds in this country decreases
- D) world suppliers of loanable funds move funds to this country
- E) the world interest rate falls

Answer: D

Type: MC

Topic: The Global Loanable Funds Market

Skill: Analytical

Source: MyEconLab

AACSB: Analytical Skills

12) An increase in the government budget deficit \_\_\_\_\_. If the country is an international borrower, the government budget deficit \_\_\_\_\_. If the country is an international lender, the government budget deficit \_\_\_\_\_.

- A) increases the country's supply of loanable funds; decreases foreign lending; increases foreign borrowing
- B) decreases the country's demand for loanable funds; decreases foreign lending; increases foreign borrowing
- C) increases the country's demand for loanable funds; increases foreign borrowing; decreases foreign lending
- D) decreases the country's supply of loanable funds; increases foreign borrowing; decreases foreign lending
- E) increases the country's demand for loanable funds; decreases foreign borrowing; increases foreign lending

Answer: C

Type: MC

Topic: The Global Loanable Funds Market

Skill: Analytical

Source: MyEconLab

AACSB: Analytical Skills

13) A country's exports are \$490 billion and its imports are \$529 billion. Choose the correct statement.

- I. The country is a net foreign borrower.
  - II. The Ricardo-Barro effect holds in this country.
  - III. This country does not have an equilibrium in its loanable funds market.
- A) I only
  - B) II only
  - C) III only
  - D) I and II only
  - E) I, II, and III

Answer: A

Type: MC

14) A country's imports are \$490 billion and its exports are \$529 billion. Choose the correct statement.

- I. The country is a net foreign borrower.
- II. The Ricardo-Barro effect holds in this country.
- III. This country does not have an equilibrium in its loanable funds market.

- A) I only
- B) II only
- C) III only
- D) I and II only
- E) None of the statements are true.

Answer: E

Type: MC

## Chapter 24 Money, the Price Level, and Inflation

### 24.1 What Is Money?

1) Money is

- A) equivalent to barter.
- B) currency plus credit cards plus debit cards.
- C) the same as gold.
- D) a means of payment.
- E) currency plus coins.

Answer: D

Diff: 1 Type: MC

Topic: What Is Money?

2) Which of the following best fits the definition of money?

- A) gold
- B) any commodity or token that is generally acceptable as a means of payment
- C) an obligation between the parties to a transaction
- D) any unit of account
- E) any medium of exchange

Answer: B

Diff: 1 Type: MC

Topic: What Is Money?

3) If you can find someone to swap what you have for what you want, then

- A) money is necessary for the exchange to work.
- B) specialization is impossible in the society in which you live.
- C) there exists a double coincidence of wants.
- D) there exists a double system of money.
- E) there exists a monetary exchange system.

Answer: C

Diff: 1 Type: MC

Topic: What Is Money?

4) Without money to act as a medium of exchange,

- A) the standard of living in the economy would increase.
- B) barter exchange would allow for a much simpler yet increased standard of living.
- C) the increased transactions costs associated with trading would prohibit some trades from taking place.
- D) independence in production would lead to a proliferation of new products.
- E) all exchanges that take place under a monetary system would still take place.

Answer: C

Diff: 1 Type: MC

Topic: What Is Money?

- 5) Money's function as a unit of account can best be described as
- A) an agreed measure for stating the prices of goods and services.
  - B) an entry in an accounting ledger.
  - C) a method of recording transactions.
  - D) a commodity that can be exchanged for another commodity.
  - E) a generally accepted medium of exchange.

Answer: A

Diff: 1 Type: MC

Topic: What Is Money?

- 6) Which one of the following is *not* a function of money?

- A) medium of exchange
- B) means of payment
- C) store of value
- D) measure of liquidity
- E) unit of account

Answer: D

Diff: 2 Type: MC

Topic: What Is Money?

- 7) Which of the following is a function of money?

- A) A medium of exchange.
- B) A measure of liquidity.
- C) A means of pooling risk.
- D) A store of exchange.
- E) A means of reducing transactions costs.

Answer: A

Diff: 1 Type: MC

Topic: What Is Money?

Source: Study Guide

- 8) Money's function as a store of value can best be described as

- A) an agreed measure for stating the prices of goods and services.
- B) a guarantee of a double coincidence of wants.
- C) an efficient means of writing contracts over a long time period.
- D) something that can be held and exchanged later for goods and services.
- E) a generally acceptable exchange system.

Answer: D

Diff: 2 Type: MC

Topic: What Is Money?

- 9) The higher and more unpredictable the changes in a monetary unit, the
- A) more likely it will be used as a store of value.
  - B) less likely it will be used as a store of value.
  - C) more confidence people will have in holding it for the future.
  - D) less likely contracts will be written to counterbalance the uncertainty of its value in the future.
  - E) more likely it will be used as a standard of deferred payment.

Answer: B

Diff: 2 Type: MC

Topic: What Is Money?

- 10) The higher and more unpredictable the changes in the monetary unit, the
- A) lower the opportunity cost of using it as a medium of exchange.
  - B) lower the opportunity cost of using it as a store of value.
  - C) higher the opportunity cost of using it as a store of value.
  - D) less likely barter exchange will replace it.
  - E) lower the opportunity cost of using it as a standard of deferred payment.

Answer: C

Diff: 2 Type: MC

Topic: What Is Money?

- 11) Money can take the form of any one of the following *except*

- A) a credit card.
- B) a chequing deposit.
- C) a savings deposit.
- D) Bank of Canada notes.
- E) coins.

Answer: A

Diff: 2 Type: MC

Topic: What Is Money?

- 12) The official definitions of money can include all of the following *except*

- A) currency outside banks.
- B) personal chequable deposits.
- C) non-chequable deposits.
- D) deposits at trust and mortgage loan companies.
- E) cheques.

Answer: E

Diff: 2 Type: MC

Topic: What Is Money?

13) Which of the following is *not* considered money in Canada today?

- A) deposits at credit unions
- B) bank of Canada notes
- C) deposits at banks
- D) coins
- E) debit cards

Answer: E

Diff: 2 Type: MC

Topic: What Is Money?

14) Which one of the following items is *not* included in the M1 definition of money?

- A) currency outside banks.
- B) personal chequable deposits
- C) non-personal chequable deposits
- D) fixed term deposits
- E) Neither B nor D are part of M1.

Answer: D

Diff: 2 Type: MC

Topic: What Is Money?

15) The largest component of M1 is

- A) currency outside banks.
- B) personal chequable deposits.
- C) non-personal chequable deposits.
- D) fixed term deposits.
- E) non-personal non-chequable deposits.

Answer: C

Diff: 1 Type: MC

Topic: What Is Money?

16) Using a credit card can best be likened to

- A) taking out a loan.
- B) a barter exchange.
- C) using any other form of money, because you can immediately take the goods you purchase home.
- D) writing a cheque on your chequable deposit.
- E) withdrawing money from a savings account.

Answer: A

Diff: 2 Type: MC

Topic: What Is Money?

17) Which of the following assets is the *most* liquid?

- A) a Canada Savings Bond
- B) a credit card
- C) a house
- D) cash
- E) a line of credit

Answer: D

Diff: 2 Type: MC

Topic: What Is Money?

18) If the prices of goods and services are stated in terms of kilograms of salt, then salt is

- A) a unit of account.
- B) a standard of deferred payment.
- C) a store of value.
- D) quasi-money.
- E) a medium of exchange.

Answer: A

Diff: 2 Type: MC

Topic: What Is Money?

19) Which one of the following is a component of M2 but not of M1?

- A) currency outside banks
- B) personal chequable deposits
- C) personal non-chequable deposits
- D) currency in a bank vault
- E) Canada Savings Bonds

Answer: C

Diff: 1 Type: MC

Topic: What Is Money?

Source: Study Guide

20) Which one of the following is *not* a store of value?

- A) credit cards
- B) personal chequable deposits
- C) fixed term deposits
- D) non-personal chequable deposits
- E) non-chequable deposits

Answer: A

Diff: 2 Type: MC

Topic: What Is Money?

Source: Study Guide

21) Which of the following is a store of value?

- A) a credit card
- B) a cheque
- C) a debit card
- D) a fixed term deposit
- E) all of the above

Answer: D

Diff: 2 Type: MC

Topic: What Is Money?

22) Which one of the following is considered to be money?

- A) a chequable deposit
- B) a blank cheque
- C) a credit card
- D) a debit card
- E) a Canada Savings Bond

Answer: A

Diff: 2 Type: MC

Topic: What Is Money?

23) Which one of the following is considered to be money?

- A) a cheque
- B) a debit card
- C) a credit card
- D) currency
- E) all of the above

Answer: D

Diff: 2 Type: MC

Topic: What Is Money?

24) Which one of the following is *not* money?

- A) a chequable deposit
- B) Canadian currency
- C) a credit card
- D) a non-chequable deposit
- E) a fixed term deposit

Answer: C

Diff: 2 Type: MC

Topic: What Is Money?

- 25) Anything can be money as long as it
- A) has low transactions costs.
  - B) is not too bulky.
  - C) has intrinsic worth.
  - D) meets the double coincidence of wants.
  - E) is acceptable as a medium of exchange.

Answer: E

Diff: 2 Type: MC

Topic: What Is Money?

26) Consider the following data from the economy of Adanac:

- Currency outside banks: \$15 billion
- Personal and non-personal chequable deposits: \$40 billion
- Personal non-chequable deposits: \$50 billion
- Non-personal non-chequable deposits: \$125 billion
- Fixed term deposits: \$200 billion

The value of M1 is \$\_\_\_\_\_ billion and the value of M2 is \$\_\_\_\_\_ billion.

- A) 105; 230
- B) 110; 235
- C) 55; 430
- D) 55; 230
- E) 60; 430

Answer: C

Diff: 2 Type: MC

Topic: What Is Money?

27) Barter can only take place if there is

- A) money.
- B) a double coincidence of wants.
- C) a double coincidence of money.
- D) no inflation.
- E) none of the above.

Answer: B

Diff: 1 Type: MC

Topic: What Is Money?

28) If Wolfgang transfers \$1,000 out of his chequable deposit account and places it in his non-chequable deposit account,

- A) M1 and M2 fall.
- B) M1 falls and M2 rises.
- C) M1 falls and M3 rises.
- D) M1 falls and M2 remains the same.
- E) M1 rises and M2 remains the same.

Answer: D

Diff: 2 Type: MC

Topic: What Is Money?

29) If Wolfgang transfers \$1,000 out of his non-chequable deposit account and places it in his chequable deposit account,

- A) M1 and M2 fall.
- B) M1 falls and M2 rises.
- C) M1 falls and M3 rises.
- D) M1 falls and M2 remains the same.
- E) M1 rises and M2 remains the same.

Answer: E

Diff: 2 Type: MC

Topic: What Is Money?

30) Which one of the following is most liquid?

- A) chequable deposits
- B) real estate
- C) government bonds
- D) debit cards
- E) cheques

Answer: A

Diff: 1 Type: MC

Topic: What Is Money?

31) Liquidity is

- A) the ease with which an asset can be converted into a means of payment.
- B) the degree of certainty of the price of an asset.
- C) a high-risk asset.
- D) the net flow of gold into the Bank of Canada.
- E) the same as currency.

Answer: A

Diff: 1 Type: MC

Topic: What Is Money?

Use the information below to answer the following question.

**Fact 24.1.1**

The information describes a hypothetical banking system. Assume that all banks are holding their desired reserves.

Actual reserves in banking system	\$1,000
Total chequable deposits	\$5,500
Securities held by chartered banks	\$1,000
Currency outside banks	\$500

32) Refer to Fact 24.1.1. The quantity of money as measured by M1 is equal to

- A) \$2,500.
- B) \$1,500.
- C) \$6,500.
- D) \$7,000.
- E) \$6,000.

Answer: E

Diff: 2 Type: MC

Topic: What Is Money?

33) In a world with no money, costs are expressed in terms of other goods. If one video game costs two hamburgers, and a hamburger costs three pops, how many pops would it take to buy a video game?

- A) 5
- B) 3
- C) 6
- D)  $3/2$
- E)  $1/6$

Answer: C

Type: MC

34) During a period of severe inflation, which function of money is most seriously affected?

- A) store of value
- B) unit of account
- C) medium of exchange
- D) means of payment
- E) none of the above

Answer: A

Type: MC

## 24.2 The Banking System

1) Which one of the following would *not* be considered a depository institution?

- A) The Bank of Canada.
- B) a credit union
- C) a *caisse populaire*
- D) a trust and mortgage loan company
- E) The Bank of Montreal

Answer: A

Diff: 1 Type: MC

Topic: The Banking System

2) A private firm that takes deposits from households and firms and makes loans to other households and firms is

- A) a usurer.
- B) a depository institution.
- C) a credit company.
- D) a stockbroker.
- E) an insurance company.

Answer: B

Diff: 1 Type: MC

Topic: The Banking System

3) Which one of the following is *not* a depository institution?

- A) a trust and mortgage loan company
- B) a foreign-owned chartered bank
- C) a credit union
- D) a *caisse populaire*
- E) a car insurance company

Answer: E

Diff: 1 Type: MC

Topic: The Banking System

4) In 2008, chartered banks held reserves equal to approximately \_\_\_\_\_ percent of deposits.

- A) 0.4
- B) 0.04
- C) 4.0
- D) 0.14
- E) 14.0

Answer: A

Diff: 1 Type: MC

Topic: The Banking System

5) The reserves of a bank include

- A) the cash in its vault plus the value of its chequable deposits.
- B) the cash in its vault plus any deposits held on account at the Bank of Canada.
- C) the cash in its vault plus any gold held for the bank at the Bank of Canada.
- D) all of its common stock holdings, the cash in its vault, and all deposits held on account with the Bank of Canada.
- E) the cash in its vault plus any deposits held on account with the Bank of Canada plus the value of any government bonds that it holds.

Answer: B

Diff: 2 Type: MC

Topic: The Banking System

6) Which one of the following is *not* a service of depository institutions?

- A) Lowering the cost of borrowing.
- B) Providing a place for reserve account deposits.
- C) Pooling risk.
- D) Creating liquidity.
- E) Lowering the cost of monitoring borrowers.

Answer: B

Diff: 2 Type: MC

Topic: The Banking System

7) Pooling risk

- A) refers to a default contract made by a bank to other banks.
- B) refers to spreading the risk of loan default among all the depositors within the depository institution.
- C) is now illegal under the Nuisance Act of 2007.
- D) occurs when one person lends to an entire group or pool of borrowers.
- E) refers to the lower cost of obtaining funds from a depository institution.

Answer: B

Diff: 2 Type: MC

Topic: The Banking System

8) The Bank of Canada does *not* do which of the following?

- A) Supervise chartered banks.
- B) Lend money to the public.
- C) Act as a lender of last resort to banks.
- D) Issue bank notes.
- E) Hold government of Canada securities.

Answer: B

Diff: 1 Type: MC

Topic: The Banking System

9) The Bank of Canada is the lender of last resort. This means banks may borrow money from the Bank of Canada

- A) whenever they are short of reserves.
- B) overnight.
- C) if they have sufficient securities to support the loan.
- D) if the banking system as a whole is short of reserves.
- E) to finance a sudden and dramatic increase in overseas reserves.

Answer: D

Diff: 1 Type: MC

Topic: The Banking System

10) Which of the following statements about depository institutions is *false*?

- A) They create liquidity by borrowing long and lending short.
- B) They keep reserves to meet cash withdrawals.
- C) A credit union is an example of a depository institution.
- D) They pool, and therefore reduce, risk.
- E) They borrow at lower interest rates and lend at higher rates.

Answer: A

Diff: 2 Type: MC

Topic: The Banking System

Source: Study Guide

11) Which of the following is an economic function of a chartered bank?

- A) Issuing bank notes.
- B) Pooling risk.
- C) Supervising financial markets.
- D) Conducting monetary policy.
- E) None of the above.

Answer: B

Diff: 2 Type: MC

Topic: The Banking System

12) Which of the following does *not* affect the size of the monetary base?

- A) the amount of notes issued by the Bank of Canada
- B) the amount of loans issued by chartered banks
- C) the amount of coins issued by the Canadian Mint
- D) the amount of chartered bank deposits at the Bank of Canada
- E) none of the above

Answer: B

Diff: 2 Type: MC

Topic: The Banking System

13) The Monetary Base consists of the sum of

A) Bank of Canada notes held within the Bank of Canada, bank deposits at the Bank of Canada, and coins held by banks.

B) Bank of Canada notes held outside the Bank of Canada, the desired reserves of chartered banks, and coins held by banks.

C) Bank of Canada notes held outside the Bank of Canada, bank deposits at the Bank of Canada, and coins held by banks and the public.

D) Bank of Canada notes held within the Bank of Canada, bank deposits at the Bank of Canada, and coins held by banks and the public.

E) Bank of Canada notes held outside the Bank of Canada, bank deposits at the Bank of Canada, and notes and coins held by banks.

Answer: C

Diff: 1 Type: MC

Topic: The Banking System

14) Choose the statement that is *incorrect*.

A) A chartered bank is a private firm, chartered under the Bank Act of 1992 to receive deposits and make loans.

B) A credit union is a cooperative organization that operates under the Co-operative Credit Association Act of 1992.

C) A caisse populaire is similar to a credit union.

D) Trust and mortgage loan companies receive deposits, make loans, and act as trustee for pension funds and for estates.

E) Trust and mortgage loan companies have the bulk of the deposits in M1 and M2.

Answer: E

Type: MC

15) Which of the following is an asset of the Bank of Canada?

A) loans to depository institutions

B) Bank of Canada notes

C) depository institution deposits

D) deposits of private Canadian citizens

E) loans to private Canadian citizens

Answer: A

Type: MC

16) When the Bank of Canada sells government securities to a bank, how are the Bank of Canada's *assets* affected?

A) The bank's reserves held at the Bank of Canada increase.

B) The bank's reserves held at the Bank of Canada decrease.

C) Bank of Canada notes increase.

D) The amount of the Bank of Canada's government securities increases.

E) The amount of the Bank of Canada's government securities decreases.

Answer: E

Type: MC

### 24.3 How Banks Create Money

- 1) A bank can create money by
- A) selling some of its securities.
  - B) increasing its reserves.
  - C) lending its excess reserves.
  - D) printing more cheques.
  - E) converting reserves into securities.

Answer: C

Diff: 2 Type: MC

Topic: How Banks Create Money

- 2) Excess reserves are
- A) desired reserves minus actual reserves.
  - B) required reserves minus actual reserves.
  - C) liquidity funds minus actual reserves.
  - D) actual reserves minus desired reserves.
  - E) required reserves minus desired reserves.

Answer: D

Diff: 1 Type: MC

Topic: How Banks Create Money

- 3) Whenever desired reserves exceed actual reserves, the bank
- A) can make new loans.
  - B) will call in loans.
  - C) will go out of business.
  - D) is in a profit-making position.
  - E) has excess reserves.

Answer: B

Diff: 2 Type: MC

Topic: How Banks Create Money

- 4) Whenever actual reserves exceed desired reserves, the bank
- A) can make new loans.
  - B) will go out of business.
  - C) needs to call in loans.
  - D) will borrow funds from another bank.
  - E) will raise the interest rate on its loans.

Answer: A

Diff: 2 Type: MC

Topic: How Banks Create Money

5) The ratio of currency to deposits is the

- A) currency drain ratio.
- B) excess reserve ratio.
- C) monetary reserve ratio.
- D) reserve ratio.
- E) currency ratio.

Answer: A

Diff: 1 Type: MC

Topic: How Banks Create Money

6) The money creation process begins when

- A) desired reserves increase because of an increase in deposits.
- B) the quantity of money increases.
- C) banks have excess reserves.
- D) bank deposits increase.
- E) banks lend reserves.

Answer: C

Diff: 1 Type: MC

Topic: How Banks Create Money

7) If people decide to transfer their currency into their bank deposits then, all else constant, their decisions will

- A) cause the quantity of money to decrease.
- B) cause lower inflation.
- C) cause higher real interest rates.
- D) cause the quantity of money to increase immediately.
- E) increase the actual reserves of banks.

Answer: E

Diff: 2 Type: MC

Topic: How Banks Create Money

8) Suppose that a country has \$50 billion in bank reserves, \$100 billion in currency held by the public, and \$500 billion in bank deposits. The currency drain ratio is

- A) 18%.
- B) 50%.
- C) 30%.
- D) 10%.
- E) 20%.

Answer: E

Diff: 2 Type: MC

Topic: How Banks Create Money

Use the information below to answer the following questions.

**Fact 24.3.1**

The Bank of Speedy Creek has chosen the following initial balance sheet:

Assets		Liabilities	
Reserves	\$40	Deposits	\$500
Loans	<u>\$460</u>		
	\$500		

9) Refer to Fact 24.3.1. Based on the Bank of Speedy Creek's initial balance sheet, what is its desired reserve ratio?

- A) 4 percent
- B) 8 percent
- C) 12.5 percent
- D) 25 percent
- E) 40 percent

Answer: B

Diff: 2 Type: MC

Topic: How Banks Create Money

Source: Study Guide

10) Refer to Fact 24.3.1. Huck Finn comes along and deposits \$10. After Huck's deposit, but before any other actions occur, the total amount of money in the economy

- A) has stayed the same, with its components unchanged.
- B) has stayed the same, with currency decreasing and deposits increasing.
- C) has fallen, with currency decreasing and deposits staying the same.
- D) has risen, with currency unchanged and deposits increasing.
- E) has fallen, with currency decreasing and deposits unchanged.

Answer: B

Diff: 2 Type: MC

Topic: How Banks Create Money

Source: Study Guide

Use the information below to answer the following questions.

**Fact 24.3.2**

The Bank of Hobbiton has chosen the following initial balance sheet:

Assets		Liabilities	
Reserves	\$100	Deposits	\$2,000
Loans	<u>\$1,900</u>		
	\$2,000		

11) Refer to Fact 24.3.2. Based on the Bank of Hobbiton's initial balance sheet, what is its desired reserve ratio?

- A) 10 percent
- B) 100 percent
- C) 20 percent
- D) 5 percent
- E) not calculable with the available information

Answer: D

Diff: 2 Type: MC

Topic: How Banks Create Money

12) Refer to Fact 24.3.2. Bilbo Baggins comes to the bank and deposits a \$100 bill. After Bilbo's deposit, but before any other actions occur, the total quantity of money in the economy

- A) has stayed the same, with its components unchanged.
- B) has stayed the same, with currency decreasing and deposits increasing.
- C) has fallen, with currency decreasing and deposits staying the same.
- D) has risen, with currency unchanged and deposits increasing.
- E) has fallen, with currency decreasing and deposits unchanged.

Answer: B

Diff: 2 Type: MC

Topic: How Banks Create Money

13) The Canadian money multiplier is calculated as the

- A) change in monetary base divided by the change in deposits.
- B) change in quantity of bank notes divided by the change in monetary base.
- C) change in monetary base divided by the change in monetary holdings of households.
- D) change in the quantity of money divided by the change in the monetary base.
- E) change in monetary base divided by the change in quantity of money.

Answer: D

Diff: 2 Type: MC

Topic: How Banks Create Money

- 14) The quantity of money that the banking system can create is limited by
- A) bank managers' decisions.
  - B) the monetary base, desired reserves, and desired currency holdings.
  - C) the number of consumers who apply for loans.
  - D) the credit ratings of the consumers who are applying for loans.
  - E) the quantity of bank notes released by the Bank of Canada.

Answer: B

Type: MC

Topic: How Banks Create Money

Source: MyEconLab

- 15) If the desired reserve ratio is 3 percent and deposits totaled \$5.75 billion, banks hold
- A) \$172.5 million in reserves.
  - B) \$0.1725 million in reserves.
  - C) \$172.5 million in excess reserves.
  - D) \$0.1725 million in excess reserves.
  - E) \$192 million in reserves.

Answer: A

Type: MC

- 16) The banks on Sunny Island have deposits of \$4 million, reserves of \$600,000, and loans of \$2.4 million. The desired reserve ratio is 10 percent. The banks have \_\_\_\_\_ of desired reserves and \_\_\_\_\_ of excess reserves.

- A) \$400,000; \$600,000
- B) \$200,000; \$400,000
- C) \$400,000; \$200,000
- D) \$600,000; \$200,000
- E) \$200,000; \$600,000

Answer: C

Type: MC

- 17) When the nominal interest rate rises, the opportunity cost of holding money \_\_\_\_\_.

- A) rises and people hold more money
- B) falls and people hold more money
- C) falls and people hold less money
- D) rises and people hold less money
- E) does not change

Answer: D

Type: MC

18) When the interest rate falls in the money market, the quantity of money demanded \_\_\_\_\_ and the quantity of money supplied \_\_\_\_\_.

- A) increases; remains unchanged
- B) increases; decreases
- C) remains unchanged; decreases
- D) remains unchanged; remains unchanged
- E) decreases; increases

Answer: A

Type: MC

19) Suppose that the interest rate is greater than the equilibrium interest rate. Which of the following statements is true?

- I. There is an excess quantity of money.
- II. The quantity of money automatically increases.
- III. The interest rate falls.

- A) I only
- B) II only
- C) III only
- D) I and III only
- E) None of the above statements are true.

Answer: D

Type: MC

## 24.4 The Money Market

1) The opportunity cost of holding money increases when the

- A) purchasing power of money increases.
- B) nominal interest rate rises.
- C) price of goods and services decrease.
- D) income of consumers increases.
- E) income of consumers decreases.

Answer: B

Diff: 2 Type: MC

Topic: The Money Market

2) Choose the correct statement.

- A) The quantity of money measured in constant dollars is nominal money.
- B) The quantity of money measured in dollars is nominal money.
- C) The quantity of nominal money demanded is inversely related to the price level.
- D) As real GDP increase the quantity of nominal money demanded decreases.
- E) As the interest rate rises, the quantity of real money demanded increases.

Answer: B

Diff: 1 Type: MC

Topic: The Money Market

3) If the price level doubles, all else constant, the quantity of

- A) real money demanded will double.
- B) nominal money demanded will double.
- C) real money demanded will half.
- D) nominal money demanded will half.
- E) nominal money demanded will remain constant.

Answer: B

Diff: 2 Type: MC

Topic: The Money Market

4) Real money is equal to

- A) nominal income divided by the velocity of circulation.
- B) nominal income divided by the price level.
- C) nominal money divided by the price level.
- D) the price level divided by nominal money.
- E) nominal money divided by nominal income.

Answer: C

Diff: 1 Type: MC

Topic: The Money Market

- 5) Nominal money is equal to real
- A) money times the price level.
  - B) GDP times the price level.
  - C) GDP times the GDP deflator.
  - D) money divided by the price level.
  - E) GDP times real money.

Answer: A

Diff: 1 Type: MC

Topic: The Money Market

- 6) Everything else remaining the same, an increase in real GDP
- A) increases the demand for real money.
  - B) decreases the demand for real money.
  - C) does not change the demand for real money.
  - D) increases the demand for real money up to a point, and then demand will automatically fall.
  - E) decreases the demand for real money up to a point, and then demand will automatically rise.

Answer: A

Diff: 2 Type: MC

Topic: The Money Market

Use the figure below to answer the following questions.

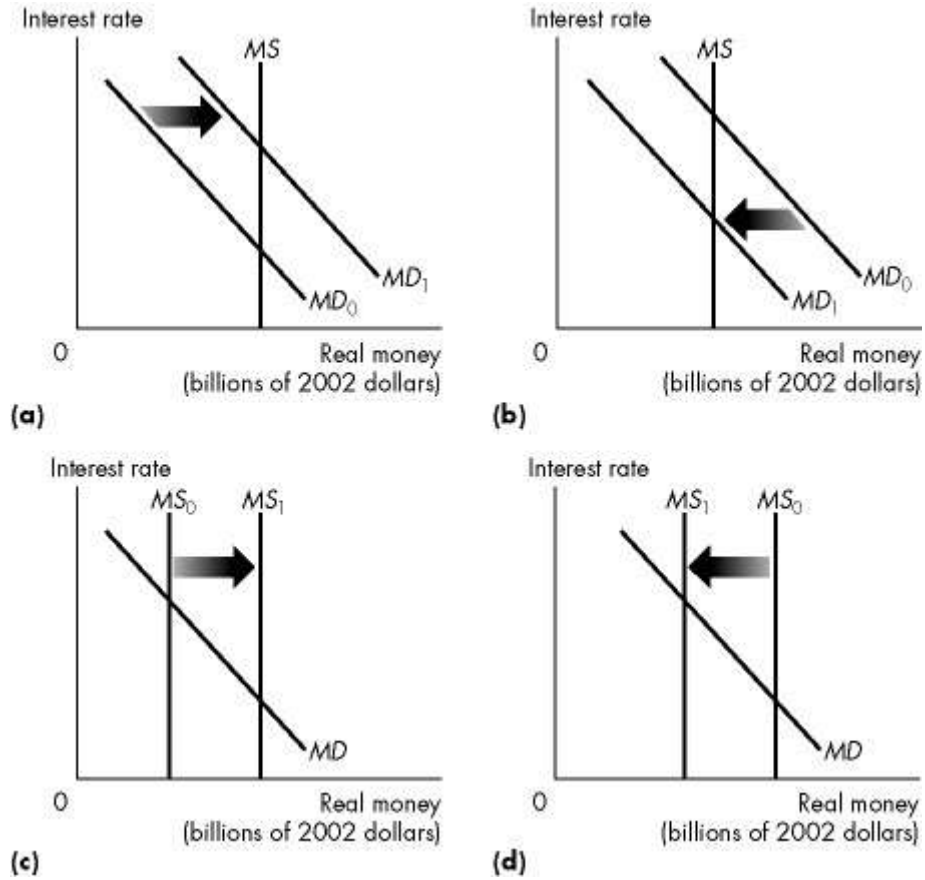


Figure 24.4.1

7) Refer to Figure 24.4.1. Everything else remaining the same, which graph best shows an increase in real GDP?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (a) and (c)

Answer: A

Diff: 2 Type: MC

Topic: The Money Market

8) Refer to Figure 24.4.1. Everything else remaining the same, which graph best shows a decrease in real GDP?

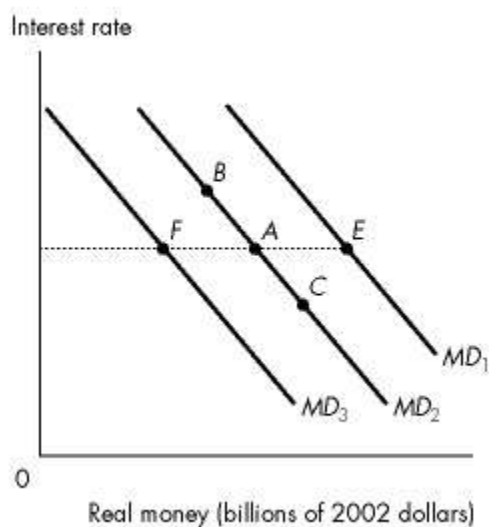
- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (a) and (c)

Answer: B

Diff: 2 Type: MC

Topic: The Money Market

Use the figure below to answer the following questions.



**Figure 24.4.2**

9) Refer to Figure 24.4.2. Which one of the following best describes the response to an increase in real GDP?

- A) Movement from A to F
- B) Movement from A to C
- C) Movement from E to A
- D) Movement from B to A
- E) Movement from A to E

Answer: E

Diff: 2 Type: MC

Topic: The Money Market

10) Refer to Figure 24.4.2. Which one of the following best describes the response to a decrease in real GDP?

- A) A movement from *A* to *C*
- B) A movement from *A* to *B*
- C) A movement from *A* to *E*
- D) A movement from *B* to *C*
- E) A movement from *E* to *A*

Answer: E

Diff: 2 Type: MC

Topic: The Money Market

11) Refer to Figure 24.4.2. Which one of the following best describes the response to a decrease in the market price of bonds?

- A) A movement from *A* to *B*
- B) A movement from *A* to *C*
- C) A movement from *A* to *F*
- D) A movement from *A* to *E*
- E) A movement from *E* to *A*

Answer: A

Diff: 2 Type: MC

Topic: The Money Market

12) Refer to Figure 24.4.2. Which one of the following best describes the response to a rise in the market price of bonds?

- A) A movement from *A* to *B*
- B) A movement from *A* to *C*
- C) A movement from *A* to *F*
- D) A movement from *A* to *E*
- E) A movement from *C* to *A*

Answer: B

Diff: 2 Type: MC

Topic: The Money Market

13) Refer to Figure 24.4.2. Which one of the following best describes the response to a rise in the price level?

- A) A movement from *A* to *B*
- B) A movement from *A* to *C*
- C) A movement from *A* to *F*
- D) A movement from *A* to *E*
- E) none of the above

Answer: E

Diff: 2 Type: MC

Topic: The Money Market

14) The amount of real money people want to hold will increase if either the amount they are spending increases or the

- A) price level increases.
- B) price level decreases.
- C) interest rate increases.
- D) interest rate decreases.
- E) price of bond falls.

Answer: D

Diff: 2 Type: MC

Topic: The Money Market

15) The amount of real money people want to hold will decrease if either \_\_\_\_\_ or the interest rate \_\_\_\_\_.

- A) the price level increases; rises
- B) the price level decreases; falls
- C) real GDP increases; falls
- D) real GDP decreases; rises
- E) the price of bonds increase; rises

Answer: D

Diff: 2 Type: MC

Topic: The Money Market

16) Which one of the following will shift the demand for money curve rightward?

- A) an increase in real GDP
- B) an increase in the price level
- C) a decrease in the price level
- D) an increase in the interest rate
- E) a decrease in the interest rate

Answer: A

Diff: 2 Type: MC

Topic: The Money Market

17) If households and firms find they are holding less money than desired, they will

- A) sell bonds, and the interest rate will rise.
- B) sell bonds, and the interest rate will fall.
- C) buy bonds, and the interest rate will rise.
- D) buy bonds, and the interest rate will fall.
- E) buy goods, and the price level will rise.

Answer: A

Diff: 3 Type: MC

Topic: The Money Market

Source: Study Guide

18) If households and firms find they are holding more money than desired, they will

- A) sell bonds, and the interest rate will rise.
- B) sell bonds, and the interest rate will fall.
- C) buy bonds, and the interest rate will rise.
- D) buy bonds, and the interest rate will fall.
- E) buy goods, and the price level will rise.

Answer: D

Diff: 3 Type: MC

Topic: The Money Market

19) The opportunity cost of holding currency is

- A) the price level.
- B) consumption given up.
- C) the real interest rate.
- D) the nominal interest rate.
- E) the inflation rate.

Answer: D

Diff: 1 Type: MC

Topic: The Money Market

20) Money market equilibrium occurs

- A) when interest rates are constant.
- B) when the level of real GDP is constant.
- C) when the quantity of real money supplied equals the quantity of real money demanded.
- D) only under a fixed exchange rate.
- E) when bond prices are constant.

Answer: C

Diff: 1 Type: MC

Topic: The Money Market

Source: Study Guide

21) If the interest rate is above the equilibrium rate, how is equilibrium achieved in the money market?

- A) People buy goods to get rid of their excess money, lowering the price of goods and lowering the interest rate.
- B) People sell goods to get rid of their excess money, lowering the price of goods and lowering the interest rate.
- C) People sell bonds to get rid of their excess money, lowering the price of bonds and lowering the interest rate.
- D) People sell bonds to get rid of their excess money, raising the price of bonds and lowering the interest rate.
- E) People buy bonds to get rid of their excess money, raising the price of bonds and lowering the interest rate.

Answer: E

Diff: 3 Type: MC

Topic: The Money Market

Source: Study Guide

- 22) If the interest rate is below the equilibrium, how is equilibrium achieved in the money market?
- A) People buy goods to get rid of their excess money, lowering the price of goods and raising the interest rate.
  - B) People sell goods to get rid of their excess money, lowering the price of goods and raising the interest rate.
  - C) People sell bonds to get rid of their excess money, lowering the price of bonds and raising the interest rate.
  - D) People sell bonds to try and raise more money, lowering the price of bonds and raising the interest rate.
  - E) People buy bonds to get rid of their excess money, raising the price of bonds and raising the interest rate.

Answer: D

Diff: 3 Type: MC

Topic: The Money Market

*Use the table below to answer the following questions.*

**Table 24.4.1**

	<b>A</b>	<b>B</b>	<b>C</b>
<b>1</b>	$r$	$Y_0$	$Y_1$
<b>2</b>	7	1.0	1.5
<b>3</b>	6	1.5	2.0
<b>4</b>	5	2.0	2.5
<b>5</b>	4	2.5	3.0
<b>6</b>	3	3.0	3.5
<b>7</b>	2	3.5	4.0
<b>8</b>	1	4.0	4.5

23) Refer to Table 24.4.1. The spreadsheet provides information about the demand for money in Minland.

Column A is the nominal interest rate,  $r$ . Columns B and C show the quantity of money demanded at two different levels of real GDP:  $Y_0$  is \$10 billion and  $Y_1$  is \$20 billion.

The quantity of money is \$3 billion. Real GDP is \$20 billion.

If the interest rate is less than 4 percent a year

- A) people sell bonds, the price of a bond falls, and the interest rate rises.
- B) people buy bonds, the price of a bond rises, and the interest rate rises.
- C) people sell bonds, the price of a bond falls, and the interest rate falls.
- D) people buy bonds, the price of a bond rises, and the interest rate falls.
- E) the demand for money increases.

Answer: A

Type: MC

Topic: The Money Market

Source: MyEconLab



24) Refer to Table 24.4.1. The spreadsheet provides information about the demand for money in Minland.

Column A is the nominal interest rate,  $r$ . Columns B and C show the quantity of money demanded at two different levels of real GDP:  $Y_0$  is \$10 billion and  $Y_1$  is \$20 billion.

The quantity of money is \$3 billion. Real GDP is \$20 billion.

If the interest rate is greater than 4 percent a year

- A) people buy bonds, the price of a bond rises, and the interest rate rises.
- B) people buy bonds, the price of a bond rises, and the interest rate falls.
- C) people sell bonds, the price of a bond falls, and the interest rate rises.
- D) people sell bonds, the price of a bond falls, and the interest rate falls.
- E) the demand for money decreases.

Answer: B

Type: MC

Topic: The Money Market

Source: MyEconLab

25) When the nominal interest rate rises, the opportunity cost of holding money \_\_\_\_\_.

- A) rises and people hold more money
- B) falls and people hold more money
- C) falls and people hold less money
- D) rises and people hold less money
- E) does not change

Answer: D

Type: MC

## 24.5 The Quantity Theory of Money

1) The quantity theory of money begins with the equation of exchange,  $MV = PY$ , and then adds the assumptions that

- A) velocity varies inversely with the interest rate, and the price level is independent of the quantity of money.
- B) velocity and the price level are independent of the quantity of money.
- C) potential GDP and the quantity of money are independent of the price level.
- D) potential GDP and the price level are independent of the quantity of money.
- E) velocity and potential GDP are independent of the quantity of money.

Answer: E

Diff: 2 Type: MC

Topic: The Quantity Theory of Money

Source: Study Guide

2) According to the quantity theory of money, an increase in the quantity of money will increase the price level

- A) but have no effect on real GDP or the velocity of circulation.
- B) and increase real GDP and the velocity of circulation.
- C) and increase real GDP but decrease the velocity of circulation.
- D) and decrease real GDP and increase the velocity of circulation.
- E) but have no effect on real GDP and will decrease the velocity of circulation.

Answer: A

Diff: 2 Type: MC

Topic: The Quantity Theory of Money

Source: Study Guide

3) GDP is \$2,000 billion, the price level is 100, and the velocity of circulation is 5. The quantity of money is

- A) \$10,000 billion.
- B) \$2,000 billion.
- C) \$400 billion.
- D) \$20 billion.
- E) \$500 billion.

Answer: C

Diff: 2 Type: MC

Topic: The Quantity Theory of Money

4) Real GDP is \$2,000 billion, the price level is 120, and the velocity of circulation is 5.

Nominal GDP is

- A) \$24 billion.
- B) \$600 billion.
- C) \$2,000 billion.
- D) \$2,400 billion.
- E) \$166.67 billion.

Answer: D

Diff: 2 Type: MC

Topic: The Quantity Theory of Money

5) Real GDP is \$2,560 billion, the price level is 125, and the velocity of circulation is 5. The quantity of money is

- A) \$2,048 billion.
- B) \$625 billion.
- C) \$20.48 billion.
- D) \$400 billion.
- E) \$640 billion.

Answer: E

Diff: 2 Type: MC

Topic: The Quantity Theory of Money

6) Real GDP is \$2,560 billion, the quantity of money \$800 billion, and the velocity of circulation is 4. The price level is

- A) 125.
- B) 6.4.
- C) 1,000.
- D) 3,200.
- E) 3.2.

Answer: A

Diff: 2 Type: MC

Topic: The Quantity Theory of Money

7) According to the quantity theory of money, in the long run

- A)  $V/M$  is constant.
- B)  $Y/M$  is constant.
- C)  $Y/P$  is constant.
- D)  $M/P$  is constant.
- E)  $M/V$  is constant.

Answer: D

Type: MC

Topic: The Quantity Theory of Money

Source: Study Guide

8) International evidence shows us that

A) there is a general tendency for money growth and inflation to be correlated but the quantity theory does not predict inflation precisely.

B) in the long run a 1 percent increase in the growth rate of money causes a 1 percent increase in inflation.

C) there is a general tendency for money growth and inflation to be inversely related, and the quantity theory is a poor predictor of inflation.

D) money growth and inflation are always rising, and the quantity theory predicts inflation accurately.

E) there is a general tendency for money growth and inflation to be correlated and the quantity theory predicts inflation precisely.

Answer: A

Type: MC

Topic: The Quantity Theory of Money

Source: MyEconLab

9) On the average in Canada, the inflation rate and the money growth rate minus real GDP growth rate

A) move in opposite directions.

B) are not related.

C) rise and fall together.

D) are always rising.

E) are always equal.

Answer: C

Type: MC

Topic: The Quantity Theory of Money

Source: MyEconLab

10) Quantecon is a country in which the quantity theory of money operates. The country has a constant population, capital stock, and technology. In year 1, real GDP was \$400 million, the price level was 200, and the velocity of circulation was 20.

In year 2 the quantity of money was 20 percent higher than in year 1.

The quantity of money in year 1 was \_\_\_\_\_.

The quantity of money in year 2 was \_\_\_\_\_.

The price level in year 2 is \_\_\_\_\_.

A) \$20 million; 24 million; 240

B) \$20 million; \$24 million; 220

C) \$40 million; \$48 million; 240

D) \$40 million; \$48 million; 220

E) \$80 million; \$88 million; 200

Answer: C

Type: MC

Topic: The Quantity Theory of Money

Source: MyEconLab

## 24.6 Mathematical Note: The Money Multiplier

1) Suppose that people decide to hold more money as cash. Which statement best illustrates the impact of this action on the money multiplier? The money multiplier

- A) decreases because of the decrease in the currency drain ratio.
- B) increases because of the decrease in the currency drain ratio.
- C) increases because of a decrease in deposits.
- D) increases because of the increase in the currency drain ratio.
- E) decreases because of the increase in the currency drain ratio.

Answer: E

Diff: 2 Type: MC

Topic: Mathematical Note: The Money Multiplier

2) Which of the following will increase the size of the money multiplier?

- A) a decrease in the desired reserve ratio
- B) an increase in the desired reserve ratio
- C) a decrease in the currency drain ratio
- D) an increase in the currency drain ratio
- E) either A or C above

Answer: E

Diff: 2 Type: MC

Topic: Mathematical Note: The Money Multiplier

3) The money multiplier will decrease if the currency drain ratio

- A) increases or the desired reserve ratio increases.
- B) decreases or the desired reserve ratio decreases.
- C) decreases or the desired reserve ratio increases.
- D) increases or the desired reserve ratio decreases.
- E) decreases and the monetary base increases.

Answer: A

Diff: 2 Type: MC

Topic: Mathematical Note: The Money Multiplier

4) Suppose that the desired reserve ratio is 0.25 and the currency drain ratio is 0.25. The money multiplier is

- A) 1.71.
- B) 2.50.
- C) 2.40.
- D) 1.40.
- E) 2.08.

Answer: B

Diff: 2 Type: MC

Topic: Mathematical Note: The Money Multiplier

5) Suppose that the banking system has excess reserves of \$10 million, the desired reserve ratio is 10 percent and the currency drain ratio is 40 percent. By how much will the quantity of money increase?

- A) \$12.5 million
- B) \$28 million
- C) \$50 million
- D) \$40 million
- E) \$22 million

Answer: B

Diff: 2 Type: MC

Topic: Mathematical Note: The Money Multiplier

*Use the information below to answer the following questions.*

**Fact 24.6.1**

The Bank of Speedy Creek has chosen the following initial balance sheet:

Assets		Liabilities	
Reserves	\$40	Deposits	\$500
Loans	\$460		
	\$500		

6) Refer to Fact 24.6.1. Suppose all the banks in the banking system have the same desired reserve ratio as the Bank of Speedy Creek. If the currency drain ratio is 32 percent, what is the size of the money multiplier?

- A) 3.3
- B) 1.25
- C) 5.0
- D) 4.0
- E) 2.7

Answer: A

Diff: 2 Type: MC

Topic: Mathematical Note: The Money Multiplier

7) The Canadian currency drain ratio for M1 is approximately \_\_\_\_\_ percent in 2010.

- A) 15
- B) 24
- C) 11
- D) 34
- E) 75

Answer: C

Diff: 1 Type: MC

Topic: Mathematical Note: The Money Multiplier

8) Canada's M1 multiplier is \_\_\_\_\_ than Canada's M2 multiplier because the currency drain for M1 is \_\_\_\_\_ than for M2, and the desired reserve ratio for M1 is \_\_\_\_\_ than for M2.

- A) smaller; larger; larger
- B) larger; smaller; larger
- C) larger; smaller; smaller
- D) smaller; larger; smaller
- E) smaller; smaller; smaller

Answer: A

Type: MC

Topic: Mathematical Note: The Money Multiplier

Source: MyEconLab

9) The money multiplier can also be calculated as \_\_\_\_\_, where  $a$  is the currency drain ratio and  $b$  is the desired reserve ratio.

- A)  $(a + b) \div (1 + b)$
- B)  $a \div (a + b)$
- C)  $(1 + a) \div (a + b)$
- D)  $(a + b) \div (1 + a)$
- E)  $(1 + b) \div (a + b)$

Answer: C

Type: MC

Topic: Mathematical Note: The Money Multiplier

Source: MyEconLab

10) In the United Kingdom, the currency drain ratio is 0.38 and the desired reserve ratio is 0.002. The U.K. money multiplier is

- A) 2.62.
- B) 0.38.
- C) 0.28.
- D) 2.77.
- E) 3.61.

Answer: E

Type: MC

Topic: Mathematical Note: The Money Multiplier

Source: MyEconLab

11) You are given the following information about the economy of Nocoins:

The banks have deposits of \$300 billion. Their reserves are \$15 billion, two thirds of which is in deposits with the central bank. Households and firms hold \$30 billion in bank notes. There are no coins!

The banks have no excess reserves.

The Bank of Nocoins, the central bank, increases bank reserves by \$0.5 billion.

The quantity of money \_\_\_\_\_.

The change in the quantity of money is not equal to the change in the monetary base because \_\_\_\_\_.

The money multiplier is \_\_\_\_\_.

A) increases; when bank reserves increase, banks loan out their excess reserves and a multiplier process ensues; 7.33

B) decreases; money includes currency but the monetary base does not include currency; 7.0

C) decreases; an increase in monetary base brings about a decrease in the quantity of money; 7.33

D) increases; the components of the monetary base are not the components of the quantity of money; 7.0

E) increases; the monetary base includes bank deposits; 7.0

Answer: A

Type: MC

Topic: Mathematical Note: The Money Multiplier

Source: MyEconLab

## Chapter 25 The Exchange Rate and the Balance of Payments

### 25.1 The Foreign Exchange Market

1) Foreign currency is

A) the market for foreign exchange.

B) the price at which one currency exchanges for another currency.

C) foreign notes, coins and bank deposits.

D) foreign notes and coins only.

E) the purchasing power of foreign money.

Answer: C

Diff: 1 Type: MC

Topic: The Foreign Exchange Market

2) The foreign exchange market is

A) made up of importers, exporters, banks, international travellers, and specialist traders.

B) the place where people exchange the currencies of different countries.

C) the market in which more than \$600 trillion in foreign exchange is traded each year.

D) both A and C are correct.

E) both A and B are correct.

Answer: D

Diff: 1 Type: MC

Topic: The Foreign Exchange Market

- 3) The exchange rate is the
- A) volume of currency exchanged between importers and exporters.
  - B) price at which one currency exchanges for another currency.
  - C) rate of currency appreciation or depreciation.
  - D) percentage change in the volume of currency exchanges.
  - E) average rate at which foreign currencies are exchanged.

Answer: B

Diff: 2 Type: MC

Topic: The Foreign Exchange Market

- 4) If the Canadian dollar depreciates, it means that
- A) one Canadian dollar buys less foreign currency.
  - B) inflation has eroded the purchasing power of Canadian money.
  - C) Canada's exchange rate falls.
  - D) both A and C are correct.
  - E) all of the above are true.

Answer: D

Diff: 1 Type: MC

Topic: The Foreign Exchange Market

5) Suppose that the Canadian dollar exchanges for 1.05 U.S. dollars and also for 0.65 Euros. A U.S. dollar exchanges for

- A) 1.00 Euro.
- B) 1.70 Euros.
- C) 0.40 Euros.
- D) 0.68 Euros.
- E) 0.62 Euros.

Answer: E

Diff: 2 Type: MC

Topic: The Foreign Exchange Market

6) If the exchange rate is 97 U.S. cents per Canadian dollar, then

- A) the Canadian dollar is cheaper than the U.S. dollar.
- B) the U.S. dollar is more expensive than the Canadian dollar.
- C) the Canadian dollar will appreciate.
- D) one U.S. dollar will buy 1.03 Canadian dollars.
- E) one U.S. dollar will buy 0.97 Canadian dollars.

Answer: D

Diff: 2 Type: MC

Topic: The Foreign Exchange Market

7) Currency depreciation is a reduction in the

- A) precious metal content in coins, such as the replacement of silver with copper in quarters.
- B) goods and services a currency can purchase within its own country, usually the result of a period of inflation.
- C) amount of foreign currency that can be obtained in trade for each unit of domestic currency.
- D) amount of domestic currency that must be exchanged for a unit of foreign exchange.
- E) amount of domestic goods foreign currency can purchase.

Answer: C

Diff: 1 Type: MC

Topic: The Foreign Exchange Market

8) Appreciation of a currency means

- A) an increase in the amount of goods and services that currency can purchase within its own country.
- B) an increase in the precious metal content in coins.
- C) a shortage of currency.
- D) that currency can buy more foreign currency.
- E) that currency can buy less foreign currency.

Answer: D

Diff: 1 Type: MC

Topic: The Foreign Exchange Market

- 9) Between 2002 and 2007, the Canadian dollar
- A) depreciated against the U.S. dollar.
  - B) appreciated against the U.S. dollar.
  - C) remained constant against the U.S. dollar.
  - D) was not able to vary against the U.S. dollar, because the exchange rate was fixed against the Japanese yen.
  - E) bought the same number of U.S. dollars as the Euro.

Answer: B

Diff: 1 Type: MC

Topic: The Foreign Exchange Market

- 10) The market in which the currency of one country is exchanged for the currency of another country is the
- A) money market.
  - B) capital market.
  - C) foreign exchange market.
  - D) forward exchange market.
  - E) international trading market.

Answer: C

Diff: 1 Type: MC

Topic: The Foreign Exchange Market

*Refer to the table below to answer the following questions.*

**Table 25.1.1**

Currency	2009 Exchange Rate	2010 Exchange Rate
EU euro	2 euros/dollar	3 euros/dollar
Japanese yen	120 yen/dollar	90 yen/dollar

- 11) Refer to Table 25.1.1. Between 2009 and 2010, the Canadian dollar \_\_\_\_\_ versus the euro and \_\_\_\_\_ versus the yen.
- A) appreciated; depreciated
  - B) appreciated; appreciated
  - C) depreciated; depreciated
  - D) depreciated; appreciated
  - E) not changed; not changed

Answer: A

Diff: 2 Type: MC

Topic: The Foreign Exchange Market

Source: Study Guide

- 12) Refer to Table 25.1.1. Between 2009 and 2010, the yen
- A) must have depreciated in value versus the euro.
  - B) must have appreciated in value versus the euro.
  - C) may or may not have appreciated in value versus the euro.
  - D) will have appreciated in value versus the euro if the euro has a high weight in CERI.
  - E) will have appreciated in value versus the euro if the euro has a lower weight in CERI.

Answer: B

Diff: 2 Type: MC

Topic: The Foreign Exchange Market

Source: Study Guide

- 13) Suppose the dollar-yen foreign exchange rate changes from 140 yen per dollar to 130 yen per dollar. Then the yen has

- A) depreciated against the dollar, and the dollar has appreciated against the yen.
- B) depreciated against the dollar, and the dollar has depreciated against the yen.
- C) appreciated against the dollar, and the dollar has appreciated against the yen.
- D) appreciated against the dollar, and the dollar has depreciated against the yen.
- E) neither appreciated nor depreciated, but the dollar has depreciated against the yen.

Answer: D

Diff: 2 Type: MC

Topic: The Foreign Exchange Market

- 14) Suppose that the following situation exists in the foreign exchange market: 1 Canadian dollar buys \$1.05 U.S., and 1 Canadian dollar buys 8.6 Chinese yuan. How many yuan will \$1 U.S. buy?

- A) 8.6 yuan
- B) 1.0 yuan
- C) 8.2 yuan
- D) 0.12 yuan
- E) 0.14 yuan

Answer: C

Diff: 2 Type: MC

Topic: The Foreign Exchange Market

- 15) Suppose that the following situation exists in the foreign exchange market: 1 Canadian dollar buys \$1.01 U.S., and 1 Canadian dollar buys 6.63 South African rand. How many U.S. dollars will one rand buy?

- A) \$6.56
- B) \$1.01
- C) \$0.17
- D) \$0.15
- E) \$6.63

Answer: D

Diff: 2 Type: MC

Topic: The Foreign Exchange Market

16) Suppose that the following situation exists in the foreign exchange market: 1 Canadian dollar buys 7.2 Chinese yuan and 1 Canadian dollar buys 5.77 South African rand. How many yuan will one rand buy?

- A) 0.80 yuan
- B) 1.25 yuan
- C) 7.20 yuan
- D) 5.77 yuan
- E) 1.43 yuan

Answer: B

Diff: 2 Type: MC

Topic: The Foreign Exchange Market

17) If the exchange rate is too high in the foreign exchange market,

- A) there is a surplus and the exchange rate will rise.
- B) there is a surplus and the exchange rate will fall.
- C) exports are cheap, and the demand curve for Canadian dollars will shift rightward.
- D) there is a shortage and the exchange rate will fall.
- E) there is a shortage and the exchange rate will rise.

Answer: B

Diff: 1 Type: MC

Topic: The Foreign Exchange Market

Source: Study Guide

18) The lower the exchange rate, the

- A) larger is the quantity of Canadian dollars supplied in the foreign exchange market.
- B) larger is the quantity of Canadian dollars demanded in the foreign exchange market.
- C) smaller is the quantity of Canadian dollars supplied in the foreign exchange market.
- D) smaller is the quantity of Canadian dollars demanded in the foreign exchange market.
- E) B and C.

Answer: E

Diff: 2 Type: MC

Topic: The Foreign Exchange Market

19) Which of the following factors influence the demand for Canadian dollars?

- A) The exchange rate and the world demand for Canadian exports.
- B) Interest rates in Canada and other countries, and the expected future exchange rate.
- C) The world demand for Canadian exports and Canadian demand for imports.
- D) Both A and B.
- E) Both B and C.

Answer: D

Diff: 2 Type: MC

Topic: The Foreign Exchange Market

- 20) The law of demand for foreign exchange tells us that other things remaining the same,
- A) the higher the exchange rate, the greater is the quantity of Canadian dollars demanded.
  - B) the higher the exchange rate, the greater is the demand for Canadian dollars.
  - C) the higher the exchange rate, the greater is the supply of Canadian dollars.
  - D) the higher the exchange rate, the smaller is the quantity of Canadian dollars demanded.
  - E) the lower the exchange rate, the greater is the supply of Canadian dollars.

Answer: D

Diff: 1 Type: MC

Topic: The Foreign Exchange Market

- 21) The law of supply of foreign exchange tells us that other things remaining the same,
- A) the lower the exchange rate, the greater is the quantity of Canadian dollars supplied.
  - B) the higher the exchange rate, the greater is the quantity of Canadian dollars supplied.
  - C) the higher the exchange rate, the greater is the supply of Canadian dollars
  - D) the lower the exchange rate, the greater is the supply of Canadian dollars.
  - E) the lower the exchange rate, the smaller is the supply of Canadian dollars.

Answer: B

Diff: 1 Type: MC

Topic: The Foreign Exchange Market

- 22) The higher the exchange rate, all other things remaining the same, the
- A) smaller is the supply of Canadian imports.
  - B) smaller is the volume of Canadian imports.
  - C) greater is the volume of Canadian imports.
  - D) greater is the supply of Canadian imports.
  - E) greater is the demand for Canadian exports.

Answer: C

Diff: 2 Type: MC

Topic: The Foreign Exchange Market

- 23) At the equilibrium exchange rate \_\_\_\_\_.
- A) the demand for dollars equals the supply of dollars
  - B) a shortage may exist but a surplus may not exist
  - C) a surplus may exist but a shortage may not exist
  - D) the quantity of dollars demanded equals the quantity of dollars supplied
  - E) the Canadian dollar is trading for 100 U.S. cents per Canadian dollar

Answer: D

Diff: 2 Type: MC

Topic: The Foreign Exchange Market

Source: MyEconLab

24) In the foreign exchange market, a change in which of the following will result in a movement along the demand curve for Canadian dollars?

- A) the U.S. interest rate
- B) the Canadian interest rate
- C) the exchange rate
- D) the expected future exchange rate
- E) both A and B

Answer: C

Type: MC

25) Consider the market for Canadian dollars. If the exchange rate rises from 2 Mexican pesos per dollar to 4 Mexican pesos per dollar, \_\_\_\_\_.

- A) a movement up along the demand curve for Canadian dollars occurs
- B) a movement down along the demand curve for Canadian dollars occurs
- C) the demand for Canadian dollars increases
- D) the demand for Canadian dollars decreases
- E) none of the above

Answer: A

Type: MC

26) If the equilibrium exchange rate is 110 yen per dollar and the current exchange rate is 120 yen per dollar, then the \_\_\_\_\_.

- A) supply curve of Canadian dollars shifts rightward
- B) demand curve for Canadian dollars shifts rightward
- C) supply curve of Canadian dollars shifts leftward
- D) demand curve for Canadian dollars shifts leftward
- E) dollar will depreciate

Answer: E

Type: MC

## 25.2 Exchange Rate Fluctuations

1) Which one of the following shifts the demand curve for dollars rightward?

- A) An increase in the demand for foreign goods by Canadians.
- B) A decrease in the demand for Canadian goods by foreigners.
- C) The dollar is expected to appreciate.
- D) The dollar is expected to depreciate.
- E) U.S. interest rates rise.

Answer: C

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

Source: Study Guide

2) Which of the following shifts the supply curve of Canadian dollars rightward?

- A) An increase in the demand for foreign goods by Canadians.
- B) A decrease in the demand for Canadian goods by foreigners.
- C) The dollar is expected to appreciate.
- D) U.S. interest rates fall.
- E) None of the above.

Answer: A

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

Source: Study Guide

3) Which one of the following would result in the dollar depreciating against the Japanese yen?

- A) a fall in the Canadian interest rate
- B) a rise in the Canadian interest rate
- C) a fall in the Japanese interest rate
- D) an increase in the expected future Canadian exchange rate
- E) an increase in the Canadian interest rate differential

Answer: A

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

4) Which one of the following would result in the dollar appreciating against the Japanese yen?

- A) a rise in the Canadian interest rate
- B) a fall in the Canadian interest rate
- C) a fall in the Japanese interest rate
- D) a decrease in the expected future Canadian exchange rate
- E) both A and C

Answer: E

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

5) The Canadian exchange rate appreciates if

- A) prices increase in the United States and other countries but remain constant in Canada.
- B) the Canadian interest rate falls.
- C) the U.S. interest rate rises.
- D) all of the above.
- E) none of the above.

Answer: A

Diff: 3 Type: MC

Topic: Exchange Rate Fluctuations

6) The Canadian exchange rate depreciates if

- A) prices increase in the United States and other countries but remain constant in Canada.
- B) the Canadian interest rate rises.
- C) the U.S. interest rate rises.
- D) all of the above.
- E) none of the above.

Answer: C

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

7) Which of the following quotations best describes purchasing power parity?

- A) "The recent high Canadian interest rate has increased demand for the Canadian dollar."
- B) "The market feeling is that the Canadian dollar is overvalued and will likely depreciate."
- C) "The price of bananas is the same in Canada and the United States, adjusting for the exchange rate."
- D) "The expected depreciation of the Canadian dollar is currently lowering demand for it."
- E) None of the above.

Answer: C

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

Source: Study Guide

8) Suppose that people expect that the Canadian exchange rate will decrease in the near future. How will this situation affect the Canadian exchange rate?

- A) The supply of Canadian dollars decreases, the demand for Canadian dollars increases and the exchange rate rises.
- B) The supply of Canadian dollars increases, the demand for Canadian dollars decreases and the exchange rate falls.
- C) The supply of Canadian dollars decreases, the demand for Canadian dollars decreases and the exchange rate falls.
- D) The supply of Canadian dollars increases, the demand for Canadian dollars decreases and the exchange rate rises.
- E) Neither the supply of Canadian dollars nor the demand for Canadian dollars changes.

Answer: B

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

- 9) Suppose that a U.S. dollar can earn interest of 5 percent a year in Chicago and a Canadian dollar can earn interest of 7 percent a year in Winnipeg. Will money flow from Chicago to Winnipeg?
- A) Yes, because the returns on money are higher in Winnipeg.
  - B) No, because the outflow of U.S. funds would create a decrease in the U.S. dollar value, penalizing investors when they attempted to recover their funds.
  - C) No, if investors expect that the Canadian dollar will appreciate by at least 2 percent per year.
  - D) No, if investors expect the U.S. dollar to appreciate by at least 2 percent per year.
  - E) No, as long as the U.S. dollar maintains higher purchasing power than the Canadian dollar.

Answer: D

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

- 10) If the price of a burger is \$2.90 Canadian in Toronto and \$3 U.S. in New York, and if purchasing power parity holds, then the exchange rate is

- A) \$1 U.S. per Canadian dollar.
- B) \$3 U.S. per Canadian dollar.
- C) 97 cents U.S. per Canadian dollar.
- D) 103 cents U.S. per Canadian dollar.
- E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

- 11) Suppose the price of a burger is \$4.50 Canadian in Toronto, and the exchange rate is 103 U.S. cents per Canadian dollar. Then

- A) the price of a burger is \$4.50 U.S. in New York if purchasing power parity holds.
- B) the price of a burger is \$4.64 U.S. in New York if interest rate parity holds.
- C) the price of a burger is \$4.64 U.S. in New York if purchasing power parity holds.
- D) the Canadian dollar is expected to appreciate according to purchasing power parity.
- E) the Canadian dollar is expected to depreciate according to purchasing power parity.

Answer: C

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

- 12) Suppose the interest rate in Canada rises and the interest rate in Japan remains the same. Interest rate parity implies that given equal risk

- A) the inflation rate is higher in Japan.
- B) Japanese financial investments are less profitable.
- C) the yen is expected to depreciate against the dollar.
- D) the yen is expected to appreciate against the dollar.
- E) Canadian financial investments are less profitable.

Answer: D

Diff: 3 Type: MC

Topic: Exchange Rate Fluctuations

Source: Study Guide

13) Suppose the interest rate in Canada falls and the interest rate in Japan remains the same. Interest rate parity implies that given equal risk

- A) the inflation rate is higher in Japan.
- B) Japanese financial investments are more profitable.
- C) the yen is expected to depreciate against the dollar.
- D) the yen is expected to appreciate against the dollar.
- E) Canadian financial investments are less profitable.

Answer: C

Diff: 3 Type: MC

Topic: Exchange Rate Fluctuations

14) Suppose interest rates are 3 percent in Japan and 6 percent in Canada. The current value of the exchange rate is 110 Japanese yen per dollar, and it is generally expected that in one year the exchange rate will be 106.7 yen per dollar. Under these circumstances,

- A) interest rate parity is violated.
- B) an international investor could make money by borrowing in Japan and lending in Canada, assuming no transaction costs.
- C) an international investor could make money by borrowing in Canada and lending in Japan, assuming no transaction costs.
- D) interest rate parity is not violated.
- E) A and C are true.

Answer: D

Diff: 3 Type: MC

Topic: Exchange Rate Fluctuations

15) Suppose interest rates are 3 percent in Japan and 6 percent in Canada. The current value of the exchange rate is 110 Japanese yen per dollar, and it is generally expected that in one year the exchange rate will be 106.7 yen per dollar. However, new information is released that changes everyone's expectations, and they think the exchange rate in one year will still be 110 yen per dollar. As a result of this change,

- A) the demand for Canadian dollars increases.
- B) the supply of Canadian dollars decreases.
- C) people will borrow in Canada and lend in Japan.
- D) the demand for Canadian dollars decreases.
- E) A and B.

Answer: E

Diff: 3 Type: MC

Topic: Exchange Rate Fluctuations

- 16) Which of the following quotations best describes interest rate parity in action?
- A) "The demand for the Canadian dollar has increased due to the recent increase in the Canadian interest rate."
  - B) "The market feeling is that the Canadian dollar is overvalued and will likely appreciate."
  - C) "The price of bananas is the same in Canada and the United States, adjusting for the exchange rate."
  - D) "The expected appreciation of the Canadian dollar is currently lowering demand for it."
  - E) none of the above

Answer: A

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

- 17) Suppose you think that the Canadian dollar exchange rate will depreciate against the U.S. dollar over the next month. What should you do now in anticipation of profit?

- A) Buy Canadian dollars.
- B) Buy U.S. dollars.
- C) Sell Canadian dollars.
- D) Sell U.S. dollars.
- E) Do both B and C.

Answer: E

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

- 18) Suppose you think that the Canadian dollar exchange rate will appreciate against the U.S. dollar over the next month. What should you do now in anticipation of profit?

- A) Buy Canadian dollars.
- B) Buy U.S. dollars.
- C) Sell Canadian dollars.
- D) Sell U.S. dollars.
- E) Do both A and D.

Answer: E

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

- 19) When would the exchange rate fall the most?

- A) The supply of and demand for dollars both increase.
- B) The supply of dollars increases, and the demand for dollars decreases.
- C) The supply of dollars decreases, and the demand for dollars increases.
- D) The supply of and demand for dollars both decrease.
- E) The Bank of Canada intervenes.

Answer: B

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

Source: Study Guide

20) When would the exchange rate rise the most?

- A) The supply of and demand for dollars both increase.
- B) The supply of dollars increases, and the demand for dollars decreases.
- C) The supply of dollars decreases, and the demand for dollars increases.
- D) The supply of and demand for dollars both decrease.
- E) The Bank of Canada intervenes.

Answer: C

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

21) Which of the following factors move the demand curve for Canadian dollars and the supply curve of Canadian dollars in opposite directions?

- A) The interest rate differential increases or decreases.
- B) The world demand for Canadian exports increases or decreases.
- C) Canadian imports increase or decrease.
- D) The expected future exchange rate rises or falls.
- E) Both A and D above.

Answer: E

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

22) Suppose that Canada's demand for imports decreases. All other things equal,

- A) the demand for Canadian dollars decreases and the supply of Canadian dollars increases.
- B) the demand for Canadian dollars increases.
- C) both the supply of and demand for Canadian dollars decreases.
- D) the supply of Canadian dollars decreases.
- E) the supply of Canadian dollars decreases and demand for Canadian dollars increases.

Answer: D

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

23) Suppose new information leads people to expect future appreciation of the Canadian dollar.

Then all of the following occurs *except*

- A) the demand for dollars increases
- B) the supply of dollars decreases
- C) the current exchange rate rises
- D) the interest rate must rise
- E) none of the above

Answer: D

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

24) Suppose the exchange rate between the Canadian dollar and the British pound is 0.5 pounds per dollar. If a radio sells for 38 pounds in Britain and purchasing power parity holds, what is the dollar price of the radio?

- A) \$19
- B) \$26
- C) \$38
- D) \$57
- E) \$76

Answer: E

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

Source: Study Guide

25) A change in the exchange rate, other things remaining the same, brings a

- A) change in the quantity of Canadian dollars demanded and a movement along the demand curve.
- B) change in the quantity of Canadian dollars demanded with *no* movement along the demand curve.
- C) shift of the demand curve for Canadian dollars with a movement along the demand curve.
- D) change in the quantity of Canadian dollars demanded and a shift of the demand curve.
- E) shift of the demand curve for Canadian dollars with *no* movement along the demand curve.

Answer: A

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

26) A change in the exchange rate, other things remaining the same, brings a

- A) shift of the supply curve for Canadian dollars with *no* movement along the supply curve.
- B) change in the quantity of Canadian dollars supplied and a shift of the supply curve.
- C) shift of the supply curve for Canadian with a movement along the demand curve.
- D) change in the quantity of Canadian dollars supplied with *no* movement along the supply curve.
- E) change in the quantity of Canadian dollars supplied and a movement along the supply curve.

Answer: E

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

27) Suppose that the following situation exists in the foreign exchange market. 1 Canadian dollar buys 5.77 South African rand. If the price of a bottle of South African wine is 32 rand, what is the price in Canadian dollars if purchase power parity exists?

- A) \$184.64
- B) \$32.00
- C) \$5.55
- D) \$18.46
- E) \$18.02

Answer: C

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

28) The exchange rate is volatile because

- A) government policy promotes interest rate fluctuation.
- B) the demand curve for foreign exchange is very flat.
- C) the demand curve for foreign exchange is very steep.
- D) the supply curve of dollars is vertical.
- E) the supply of dollars and demand for dollars are influenced by similar events.

Answer: E

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

29) The demand curve for dollars shifts rightward if

- A) the Canadian exchange rate falls.
- B) the price of Canadian goods and services increases.
- C) Canadian interest rates rise.
- D) foreign interest rates rise.
- E) the expected future value of the dollar falls.

Answer: C

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

30) The supply curve of dollars shifts rightward if

- A) the Canadian exchange rate rises.
- B) the price of Canadian goods and services decreases.
- C) Canadian interest rates rise.
- D) foreign interest rates rise.
- E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

31) Choose the correct statements.

1. The exchange rate is the value of the Canadian dollar expressed in units of foreign currency per Canadian dollar.
  2. The real exchange rate is the relative price of Canadian-produced goods and services to foreign-produced goods and services.
  3. The exchange rate is a measure of the quantity of the real GDP of other countries that a unit of Canadian real GDP buys.
  4. The exchange rate is the relative price of Canadian-produced goods and services to foreign-produced goods and services.
- A) Statements 1 and 2 are correct.  
B) Statements 3 and 4 are correct.  
C) Statements 1 and 3 are correct.  
D) Statements 2 and 4 are correct.  
E) Statements 2 and 3 are correct.

Answer: A

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

Source: MyEconLab

32) Choose the correct statements about the real exchange rate.

1. The real exchange rate is a measure of how much of one money exchanges for a unit of another money.
  2. The real exchange rate is the value of the Canadian dollar expressed in units of foreign currency per Canadian dollar.
  3. The real exchange rate is the relative price of Canadian-produced goods and services to foreign-produced goods and services.
  4. The real exchange rate is a measure of the quantity of the real GDP of other countries that we get for a unit of Canadian real GDP.
- A) Statements 1 and 2 are correct.  
B) Statements 2 and 4 are correct.  
C) Statements 1 and 3 are correct.  
D) Statements 3 and 4 are correct.  
E) Statements 2 and 3 are correct.

Answer: D

Diff: 2 Type: MC

Topic: Exchange Rate Fluctuations

Source: MyEconLab

33) Airbus is a European producer of airliners. Indian Airlines wants to buy 23 Airbus planes from Airbus because of an increased demand for world travel. The currency of India is the rupee. The currency of the European Union is the euro. As a result, \_\_\_\_\_.

- A) the supply curve of euros shifts rightward
- B) the supply curve of euros shifts leftward
- C) the demand curve for rupees shifts rightward
- D) the demand curve for euros shifts leftward
- E) demand curve for euros shifts rightward

Answer: E

Type: MC

34) Other things remaining the same, the Canadian interest rate differential increases for sure if the Canadian interest rate \_\_\_\_\_.

- A) rises and the U.S. interest rate falls
- B) rises and the U.S. interest rate rises
- C) falls and the U.S. interest rate falls
- D) falls and the U.S. interest rate rises
- E) doesn't change and the U.S. interest rate rises

Answer: A

Type: MC

35) Given the Canadian price level  $P$ , the foreign country price level  $P^*$ , and the nominal exchange rate  $E$  in foreign currency per Canadian dollar, the real exchange rate  $RER$  equals \_\_\_\_\_.

- A)  $E \times (P^*/P)$
- B)  $(P/P^*) / E$
- C)  $P \times (E/P^*)$
- D)  $P \times E \times P^*$
- E)  $E \times (P/P^*)$

Answer: E

Type: MC

36) Initially the exchange rate between the South Korean won and the Canadian dollar is 950 won per dollar. If the exchange rate rises to 1,000 won per dollar and the Canadian and South Korean price levels do not change, then in the short run the real exchange rate \_\_\_\_\_.

- A) rises
- B) falls
- C) does not change
- D) either rises, falls, or remains the same but we don't know for sure
- E) is 1,000 won per dollar

Answer: A

Type: MC

37) If the price level in Canada is 120, the price level in South Africa is 140, and the exchange rate is 7 South African rands per dollar, then the real exchange rate is \_\_\_\_\_.

A) 8.2

B) 7

C) 6

D) 8.4

E) 9.8

Answer: C

Type: MC

### 25.3 Exchange Rate Policy

1) Which of the following exchange rate policies uses a target exchange rate, but allows the target to change?

- A) crawling peg
- B) flexible exchange rate
- C) fixed exchange rate
- D) moving target
- E) none of the above

Answer: A

Type: MC

Topic: Exchange Rate Policy

Skill: Conceptual

AACSB: Reflective Thinking

2) Suppose the Bank of Canada follows a fixed exchange rate of \$1 U.S. per Canadian dollar. If the demand for Canadian dollars temporarily increases, to maintain the target exchange rate, the Bank can

- A) sell Canadian dollars.
- B) buy Canadian dollars.
- C) violate interest rate parity.
- D) violate purchasing power parity.
- E) enforce interest rate parity.

Answer: A

Type: MC

Topic: Exchange Rate Policy

Skill: Conceptual

AACSB: Reflective Thinking

3) Suppose the Bank of Canada follows a fixed-exchange rate of 0.50 U.K. pounds per Canadian dollar. If the demand for dollars temporarily decreases, to maintain the target exchange rate, the Bank can

- A) sell dollars.
- B) buy dollars.
- C) increase Canadian exports.
- D) increase Canadian imports.
- E) violate purchasing power parity.

Answer: B

Type: MC

Topic: Exchange Rate Policy

Skill: Conceptual

AACSB: Reflective Thinking

4) If the Bank of Canada sets a target exchange rate that is higher than the current exchange rate, then

- A) the Bank must sell dollars.
- B) the Bank must buy dollars.
- C) the Bank can do nothing in the short run.
- D) will print more dollars for foreign distribution.
- E) None of the above.

Answer: B

Type: MC

Topic: Exchange Rate Policy

Skill: Conceptual

AACSB: Reflective Thinking

5) If the exchange rate is higher than the Bank of Canada's target exchange rate, the Bank

- A) implements purchasing power parity.
- B) implements interest rate parity.
- C) buys dollars.
- D) sells dollars.
- E) none of the above.

Answer: D

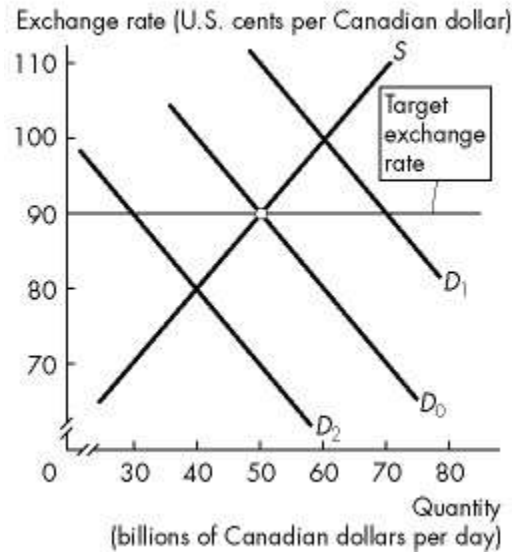
Type: MC

Topic: Exchange Rate Policy

Skill: Conceptual

AACSB: Reflective Thinking

Refer to the figure below to answer the following questions.



**Figure 25.3.1**

6) In Figure 25.3.1, suppose the demand for dollars *temporarily* increases so that the demand curve shifts to  $D_1$ . To maintain the target exchange rate, the Bank of Canada

- A) sells dollars.
- B) buys dollars.
- C) must violate interest rate parity but not purchasing power parity.
- D) must raise the target exchange rate.
- E) must lower the target exchange rate.

Answer: A

Type: MC

Topic: Exchange Rate Policy

Skill: Analytical

AACSB: Analytical Skills

7) In Figure 25.3.1, suppose the demand for dollars *temporarily* decreases so that the demand curve shifts to  $D_2$ . To maintain the target exchange rate, the Bank of Canada

- A) sells dollars.
- B) buys dollars.
- C) must violate both interest rate parity *and* purchasing power parity.
- D) must raise the target exchange rate.
- E) must lower the target exchange rate.

Answer: B

Type: MC

Topic: Exchange Rate Policy

Skill: Analytical

AACSB: Analytical Skills

- 8) In Figure 25.3.1, suppose the demand for dollars *permanently* decreases to  $D_2$ . To maintain the target, the Bank of Canada
- A) buys dollars.
  - B) sells dollars.
  - C) must decrease the nation's net exports.
  - D) cannot permanently maintain the exchange rate target of 90 U.S. cents per Canadian dollar.
  - E) none of the above.

Answer: D

Type: MC

Topic: Exchange Rate Policy

Skill: Analytical

AACSB: Analytical Skills

- 9) If a nation's central bank increased domestic interest rates, the nation's exchange rate would change if the country's exchange rate was
- A) a flexible exchange rate.
  - B) a fixed exchange rate.
  - C) a crawling peg.
  - D) a nominally fixed exchange rate.
  - E) none of the above.

Answer: A

Diff: 2 Type: MC

Topic: Exchange Rate Policy

Skill: Conceptual

AACSB: Reflective Thinking

- 10) China has used a fixed yuan exchange rate and a crawling peg exchange rate. In both cases, China pegs its currency to the
- A) U.S. dollar.
  - B) Japanese yen.
  - C) euro.
  - D) Mexican peso.
  - E) Russian ruble.

Answer: A

Diff: 2 Type: MC

Topic: Exchange Rate Policy

Skill: Conceptual

AACSB: Reflective Thinking

- 11) If a country's central bank does not intervene in the foreign exchange market, the country has
- A) a crawling peg exchange rate policy.
  - B) a fixed exchange rate policy.
  - C) a flexible exchange rate policy.
  - D) no exchange rate policy.
  - E) a responsible exchange rate policy.

Answer: C

Type: MC

Topic: Exchange Rate Policy

Skill: Conceptual

AACSB: Reflective Thinking

- 12) If a country's currency appreciates and its official holdings of foreign currency increase. The central bank is \_\_\_\_\_ foreign currency to limit the appreciation, and the official settlements account balance is \_\_\_\_\_.

- A) buying; negative
- B) selling negative
- C) buying; positive
- D) selling; positive
- E) buying; zero

Answer: A

Type: MC

Topic: Exchange Rate Policy

Skill: Conceptual

Source: MyEconLab

AACSB: Reflective Thinking

- 13) One consequence of China operating a crawling peg is that China \_\_\_\_\_.

- A) is accumulating U.S. dollar reserves
- B) will eventually run out of foreign reserves, and the yuan will depreciate
- C) will eventually run out of foreign reserves, and the yuan will appreciate
- D) will become more competitive in the long run
- E) none of the above

Answer: A

Type: MC

Topic: Exchange Rate Policy

Skill: Conceptual

Source: MyEconLab

AACSB: Reflective Thinking

14) The Bank of Canada \_\_\_\_\_.

A) has no influence on the exchange rate

B) sells Canadian dollars to the United States in an attempt to depreciate the Canadian dollar and increase Canadian exports to the United States

C) alternates between a flexible, fixed, and crawling peg exchange rate policy depending on economic conditions

D) follows a flexible exchange rate policy, although the Bank's actions can impact the exchange rate

E) buys Canadian dollars from the United States in an attempt to depreciate the Canadian dollar and increase Canadian exports to the United States

Answer: D

Type: MC

15) All of the following statements are true *except* \_\_\_\_\_.

A) China's exchange rate policy increases exports in the long run

B) China's exchange rate policy is mainly an attempt to control inflation

C) China's exchange rate policy results in a yuan that has a lower foreign exchange rate against the U.S. dollar than it would otherwise have

D) China's exchange rate policy does not impact the real exchange rate in the long run

E) All of the above are true.

Answer: A

Type: MC

## 25.4 Financing International Trade

1) If the current account is in surplus and the capital and financial account is also in surplus, then the official settlements account balance is

- A) negative.
- B) positive.
- C) probably close to zero, but could be either negative or positive.
- D) zero.
- E) equal to the sum of the current account and the capital account.

Answer: A

Diff: 2 Type: MC

Topic: Financing International Trade

2) If the current account is in deficit and the capital and financial account is also in deficit, then the official settlements account balance is

- A) negative.
- B) positive.
- C) probably close to zero, but could be either negative or positive.
- D) zero.
- E) equal to the sum of the current account and the capital account.

Answer: B

Diff: 2 Type: MC

Topic: Financing International Trade

3)  $NX =$

- A)  $C + I + G$ .
- B)  $(S + I) - (T + G)$ .
- C)  $(G - T) + (I - S)$ .
- D)  $(S - I) + (G - T)$ .
- E)  $(T - G) + (S - I)$ .

Answer: E

Diff: 2 Type: MC

Topic: Financing International Trade

4) Which one of the following transactions would be recorded as a positive entry in the Canadian balance of payment accounts?

- A) A Canadian tourist spends \$3,000 while visiting France.
- B) A Canadian tourist spends \$3,000 while visiting Banff.
- C) A Canadian citizen purchases a U.K. government bond.
- D) A Canadian corporation sends interest payments on outstanding bonds to U.S. citizens.
- E) A French tourist spends \$3,000 while visiting Banff.

Answer: E

Diff: 2 Type: MC

Topic: Financing International Trade

5) Complete the following sentence. Foreign borrowing

- A) always leads to a lower level of consumption in the future for the debtor nation because part of its future GDP is used to pay off the foreign debt.
- B) always leads to a higher level of consumption in the future for the debtor nation because foreign borrowing enables a greater than otherwise possible increase in the nation's capital stock.
- C) could lead to higher consumption levels in the future, if the borrowing is used to finance investment that generates economic growth.
- D) could lead to lower consumption levels in the future, if the borrowing is used for current consumption.
- E) C and D

Answer: E

Diff: 2 Type: MC

Topic: Financing International Trade

*Use the information below to answer the following questions.*

### **Fact 25.4.1**

You are given the following information about the country of Ecoland, whose currency is the turkey, and whose official settlements balance is zero.

Variable	Billions of turkies
Real GDP	50
Consumption expenditure	30
Government expenditure on goods and services	12
Investment	11
Exports	10
Government budget deficit	2

6) Refer to Fact 25.4.1. What is the value of the private sector deficit or surplus?

- A) zero
- B) -3 billion turkies
- C) -1 billion turkies
- D) -2 billion turkies
- E) +1 billion turkies

Answer: C

Diff: 3 Type: MC

Topic: Financing International Trade

7) Refer to Fact 25.4.1. What is the value of the capital account and financial balance for Ecoland, given the value of net interest income plus net transfers is +3 billion turkies?

- A) +3 billion turkies
- B) +6 billion turkies
- C) -3 billion turkies
- D) -1 billion turkies
- E) zero

Answer: E

Diff: 3 Type: MC

Topic: Financing International Trade

8) Refer to Fact 25.4.1. What is the current account balance for Ecoland, given the value of net interest income plus net transfers is +3 billion turkies?

- A) -3 billion turkies
- B) -6 billion turkies
- C) +3 billion turkies
- D) +1 billion turkies
- E) zero

Answer: E

Diff: 3 Type: MC

Topic: Financing International Trade

9) Refer to Fact 25.4.1. What is the net exports?

- A) -2 billion turkies
- B) -1 billion turkies
- C) 3 billion turkies
- D) -3 billion turkies
- E) 1 billion turkies

Answer: D

Diff: 3 Type: MC

Topic: Financing International Trade

10) Refer to Fact 25.4.1. What is the imports?

- A) 13 billion turkies
- B) 7 billion turkies
- C) 11 billion turkies
- D) 9 billion turkies
- E) 12 billion turkies

Answer: A

Diff: 3 Type: MC

Topic: Financing International Trade

11) Refer to Fact 25.4.1. What is the amount of saving by the people of Ecoland?

- A) 8 billion turkies
- B) 10 billion turkies
- C) 20 billion turkies
- D) 6 billion turkies
- E) 12 billion turkies

Answer: B

Diff: 3 Type: MC

Topic: Financing International Trade

12) Refer to Fact 25.4.1. What is the amount of net taxes?

- A) 10 billion turkies
- B) 12 billion turkies
- C) 2 billion turkies
- D) 8 billion turkies
- E) 14 billion turkies

Answer: A

Diff: 2 Type: MC

Topic: Financing International Trade

13) A debtor nation is one that during its entire history has

- A) lent more to the rest of the world than it has borrowed from it.
- B) borrowed more from the rest of the world than it has lent to it.
- C) invested more in the rest of the world than has been invested in it.
- D) a public sector deficit that is larger than its net exports.
- E) had a government debt.

Answer: B

Diff: 2 Type: MC

Topic: Financing International Trade

14) If Northland is currently a net lender and a debtor nation,

- A) it has loaned more than it borrowed from the rest of the world this year, but borrowed more than it loaned during its history.
- B) it has borrowed more from the rest of the world than it loaned this year and also borrowed more than it loaned during its history.
- C) it has loaned more than it borrowed from the rest of the world this year and has loaned more than it borrowed during its history.
- D) its accounting system must be in error if it shows the nation to be a net lender and a debtor nation at the same time.
- E) its debts must be currently growing.

Answer: A

Diff: 2 Type: MC

Topic: Financing International Trade

15) Suppose that a country's government expenditures are \$500 billion, net taxes are \$400 billion, saving is \$200 billion, and investment is \$250 billion. The country has a government budget

- A) surplus and a private sector surplus.
- B) surplus and a private sector deficit.
- C) deficit and a private sector surplus.
- D) deficit and a private sector deficit.
- E) surplus and a private sector balance.

Answer: D

Diff: 2 Type: MC

Topic: Financing International Trade

16) Suppose that a country's government expenditures are \$500 billion, net taxes are \$400 billion, saving is \$200 billion, and investment is \$250 billion. Net exports are a

- A) surplus of \$150 billion.
- B) surplus of \$50 billion.
- C) deficit of \$150 billion.
- D) deficit of \$50 billion.
- E) deficit of \$250 billion.

Answer: C

Diff: 2 Type: MC

Topic: Financing International Trade

17) Suppose that a country's government expenditures are \$400 billion, net taxes are \$300 billion, saving is \$300 billion, and investment is \$250 billion. There is a private sector

- A) surplus of \$150 billion.
- B) surplus of \$50 billion.
- C) deficit of \$150 billion.
- D) deficit of \$50 billion.
- E) deficit of \$250 billion.

Answer: B

Diff: 2 Type: MC

Topic: Financing International Trade

18) Suppose that a country's government expenditures are \$400 billion, net taxes are \$300 billion, saving is \$300 billion, and investment is \$250 billion. This country has a government budget

- A) surplus and a private sector surplus.
- B) surplus and a private sector deficit.
- C) deficit and a private sector surplus.
- D) deficit and a private sector deficit.
- E) surplus and a private sector balance.

Answer: C

Diff: 2 Type: MC

Topic: Financing International Trade

Source: Study Guide

19) Suppose that a country's government expenditures are \$400 billion, net taxes are \$300 billion, saving is \$300 billion, and investment is \$250 billion. Net exports are a

- A) surplus of \$150 billion.
- B) surplus of \$50 billion.
- C) deficit of \$150 billion.
- D) deficit of \$50 billion.
- E) deficit of \$250 billion.

Answer: D

Diff: 2 Type: MC

Topic: Financing International Trade

Use the table below to answer the following questions.

**Table 25.4.1**

Year	Borrowed from Rest of World (billions of dollars)	Loaned to Rest of World (billions of dollars)
1	60	20
2	60	40
3	60	60
4	60	80

20) Refer to Table 25.4.1. If Mengia's official settlement balance was in balance every year, for which year or years can you say for sure there was a current account surplus?

- A) year 4 only
- B) year 2 only
- C) years 2 and 3
- D) years 1 and 2
- E) years 3 and 4

Answer: A

Diff: 3 Type: MC

Topic: Financing International Trade

Source: Study Guide

21) Refer to Table 25.4.1. If Mengia's official settlement balance was in surplus every year, for which year or years can you say for sure there was a current account deficit?

- A) year 1 only
- B) year 2 only
- C) years 2 and 3
- D) years 1 and 2
- E) years 3 and 4

Answer: D

Diff: 3 Type: MC

Topic: Financing International Trade

22) Refer to Table 25.4.1. If Mengia's official settlement balance was in deficit every year, for which year or years can you say *for sure* there was a current account surplus?

- A) year 1 only
- B) year 2 only
- C) years 2 and 3
- D) years 1 and 2
- E) years 3 and 4

Answer: E

Diff: 3 Type: MC

Topic: Financing International Trade

Source: Study Guide

23) Refer to Table 25.4.1. The country Mengia came into existence at the beginning of year 1. Given the information, in year 4 Mengia is a

- A) net lender and a creditor nation.
- B) net lender and a debtor nation.
- C) net borrower and a creditor nation.
- D) net borrower and a debtor nation.
- E) net lender and neither a creditor nor a debtor nation.

Answer: B

Diff: 2 Type: MC

Topic: Financing International Trade

Source: Study Guide

24) Suppose initially Canada has all its international payments accounts in balance (no surplus or deficit). Then Canadian firms increase the amount they export to Japan, and the Japanese finance the increase by borrowing from Canada. In Canada everything else remaining the same there will now be a

- A) current and financial account surplus and capital account surplus.
- B) current and financial account surplus and capital account deficit.
- C) current and financial account deficit and capital account surplus.
- D) current and financial account deficit and capital account deficit.
- E) current and financial account deficit and capital account balance.

Answer: B

Diff: 2 Type: MC

Topic: Financing International Trade

25) Suppose initially Canada has all its international payments accounts in balance (no surplus or deficit). Then Canadian firms increase the amount they import from Japan, financing that increase by borrowing from Japan. Everything else remaining the same there will now be a current and financial account

- A) surplus and a capital account surplus.
- B) surplus and a capital account deficit.
- C) deficit and a capital account surplus.
- D) deficit and a capital account deficit.
- E) surplus and a capital account balance.

Answer: C

Diff: 2 Type: MC

Topic: Financing International Trade

Source: Study Guide

26) Which one of the following is a balance of payments account?

- A) capital and financial account
- B) foreign exchange account
- C) saving account
- D) trade account
- E) all of the above

Answer: A

Diff: 1 Type: MC

Topic: Financing International Trade

27) Which one of the following is a balance of payments account?

- A) current account
- B) borrowing account
- C) official lending account
- D) net interest account
- E) public account

Answer: A

Diff: 1 Type: MC

Topic: Financing International Trade

28) Between 1999 and 2008, Canada was a

- A) a net borrower from the rest of the world.
- B) a net lender to the rest of the world.
- C) neither a borrower nor a lender to the rest of the world.
- D) borrowing and lending in equal amounts with the rest of the world.
- E) none of the above

Answer: B

Diff: 2 Type: MC

Topic: Financing International Trade

29) A creditor nation is a country

- A) that has contributed money for the advancement of health care in less developed countries.
- B) that does not borrow money from foreign nations.
- C) that during its entire history has invested more in the rest of the world than other countries have invested in it.
- D) that has active monetary policy to ensure adequate loans for housing of the poor.
- E) whose official settlements account is rising in value.

Answer: C

Diff: 1 Type: MC

Topic: Financing International Trade

- 30) The change in Canadian official reserves is recorded in the
- A) current account.
  - B) capital and financial account.
  - C) consumption expenditure account.
  - D) international investment account.
  - E) official settlements account.

Answer: E

Diff: 2 Type: MC

Topic: Financing International Trade

- 31) The current account records
- A) net exports, net interest income and net transfers.
  - B) net value of Canadian investments and foreign investments.
  - C) current government expenditure.
  - D) current consumption expenditure.
  - E) current investment.

Answer: A

Diff: 2 Type: MC

Topic: Financing International Trade

- 32) The official settlements account measures the
- A) value of Canadian merchandise purchased by foreigners.
  - B) net value of foreign goods officially purchased by Canada.
  - C) net value of Canadian official exports of services.
  - D) change in the government's holdings of foreign currency.
  - E) change in Canada's net exports.

Answer: D

Diff: 1 Type: MC

Topic: Financing International Trade

- 33) In 2010, the largest item in the current account is
- A) exports.
  - B) imports.
  - C) net interest income.
  - D) net transfers.
  - E) foreign investment in Canada.

Answer: B

Diff: 1 Type: MC

Topic: Financing International Trade

- 34) Canada's balance of payments accounts are the
- A) current account, capital and financial account, and net interest account.
  - B) capital and financial account, official settlements account, and merchandise trade account.
  - C) current account, capital and financial account, and official settlements account.
  - D) official settlements account, current account, and net interest account.
  - E) capital and financial account, current account, and merchandise trade account.

Answer: C

Diff: 1 Type: MC

Topic: Financing International Trade

- 35) The world's largest net borrower and debtor nation, \_\_\_\_\_, borrows internationally to finance \_\_\_\_\_.

- A) the United States; consumption
- B) the United States; private and public investment
- C) China; consumption
- D) China; private and public investment
- E) Japan; consumption

Answer: B

Diff: 1 Type: MC

Topic: Financing International Trade

Source: MyEconLab

- 36) The private sector balance and the government sector balance tend to move in \_\_\_\_\_. Net exports respond \_\_\_\_\_.

- A) opposite directions; closely to the government sector balance
- B) the same direction; to the sum of the government sector and private sector balances
- C) the same direction; closely to the government sector balance
- D) opposite directions; to the sum of the government sector and private sector balances
- E) the same direction; to changes in the exchange rate

Answer: D

Diff: 1 Type: MC

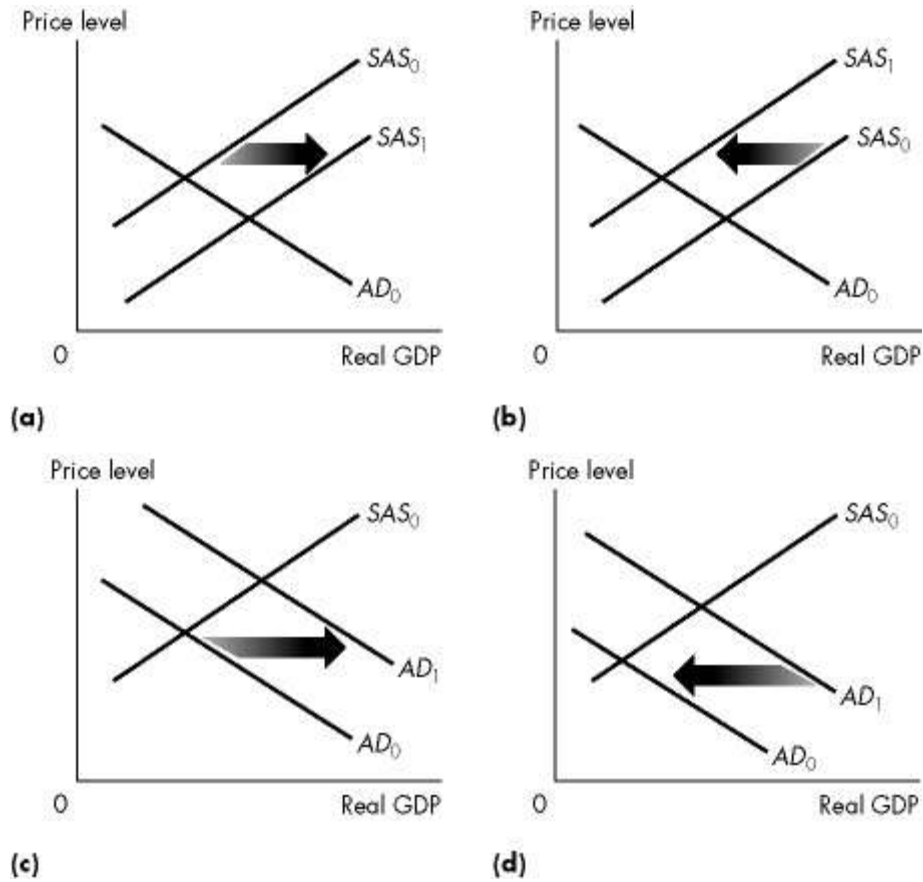
Topic: Financing International Trade

Source: MyEconLab

## **Chapter 26 Aggregate Supply and Aggregate Demand**

### 26.1 Aggregate Supply

*Use the figure below to answer the following questions.*



**Figure 26.1.1**

1) Refer to Figure 26.1.1. Which graph illustrates what happens when factor prices decrease?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (a) and (b)

Answer: A

Diff: 2 Type: MC

Topic: Aggregate Supply

Source: Study Guide

2) Refer to Figure 26.1.1. Which graph illustrates what happens when factor prices rise?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (a) and (b)

Answer: B

Diff: 2 Type: MC

Topic: Aggregate Supply

3) Which one of the following newspaper quotations describes a movement along an *LAS* curve?

- A) "The decrease in consumer spending may lead to a recession."
- B) "The increase in consumer spending is expected to lead to inflation, without any increase in real GDP."
- C) "Recent higher wage settlements are expected to cause higher inflation this year."
- D) "Growth has been unusually high the last few years due to more women entering the labour force."
- E) "The recent tornadoes destroyed many factories in Calgary and Edmonton."

Answer: B

Diff: 3 Type: MC

Topic: Aggregate Supply

4) Which one of the following newspaper quotations describes a shift of only the *SAS* curve?

- A) "The decrease in consumer spending may lead to a recession."
- B) "The increase in consumer spending is expected to lead to inflation, without any increase in real GDP."
- C) "Recent higher wage settlements are expected to cause higher inflation this year."
- D) "Growth has been unusually high the last few years due to more women entering the work force."
- E) "The recent tornadoes destroyed many factories in Calgary and Edmonton."

Answer: C

Diff: 2 Type: MC

Topic: Aggregate Supply

5) Which one of the following newspaper quotations describes a rightward shift of the *LAS* curve?

- A) "The decrease in consumer spending may lead to a recession."
- B) "The increase in consumer spending is expected to lead to inflation, without any increase in real GDP."
- C) "Recent higher wage settlements are expected to cause higher inflation this year."
- D) "Growth has been unusually high the last few years due to more women entering the work force."
- E) "The recent tornadoes destroyed many factories in Calgary and Edmonton."

Answer: D

Diff: 2 Type: MC

Topic: Aggregate Supply

6) Which one of the following newspaper quotations describes a leftward shift of the *LAS* curve?

- A) "The decrease in consumer spending may lead to a recession."
- B) "The increase in consumer spending is expected to lead to inflation, without any increase in real GDP."
- C) "Recent higher wage settlements are expected to cause higher inflation this year."
- D) "Growth has been unusually high the last few years due to more women entering the work force."
- E) "The recent tornadoes destroyed many factories in Calgary and Edmonton."

Answer: E

Diff: 2 Type: MC

Topic: Aggregate Supply

7) Which of the following does not change short-run aggregate supply?

- A) a change in the money wage rate
- B) technological change
- C) a change in the full-employment quantity of labour
- D) an increase in the quantity of capital
- E) a change in expected future profits

Answer: E

Diff: 2 Type: MC

Topic: Aggregate Supply

8) Complete the following sentence. Potential GDP

- A) increases as the price level rises.
- B) is the level of real GDP when unemployment is zero.
- C) increases as the quantity of money in the economy increases.
- D) does not vary with the price level.
- E) never changes.

Answer: D

Diff: 2 Type: MC

Topic: Aggregate Supply

9) A vertical long-run aggregate supply curve indicates that

- A) an increase in the price level will not expand an economy's output in the long run.
- B) output rates greater than the long-run output rate are unattainable.
- C) an increase in the price level will permit the economy to achieve a higher level of output.
- D) an increase in the price level will increase technological change and economic growth.
- E) the long-run aggregate supply curve never shifts.

Answer: A

Diff: 2 Type: MC

Topic: Aggregate Supply

- 10) The long-run aggregate supply curve is vertical because
- A) potential GDP is independent of the price level.
  - B) actual output can never exceed, even temporarily, the output rate implied by the economy's long-run aggregate supply curve.
  - C) a vertical long-run aggregate supply curve indicates the maximum output rate that an economy can ever reach.
  - D) a vertical long-run supply curve indicates that an increase in aggregate demand will lead to a larger real GDP, but not a larger nominal GDP.
  - E) potential GDP never changes.

Answer: A

Diff: 2 Type: MC

Topic: Aggregate Supply

- 11) The short-run aggregate supply curve indicates
- A) the relationship between the price level and real GDP demanded by consumers, investors, governments, and net exporters.
  - B) the relationship between the price level and the natural unemployment rate.
  - C) the relationship between the purchasing power of wages and the quantity of labour supplied by households.
  - D) the relationship between the quantity of real GDP supplied and the price level when the money wage rate, the prices of other resources, and potential GDP remain constant.
  - E) the various quantities of real GDP producers supply at different income levels.

Answer: D

Diff: 1 Type: MC

Topic: Aggregate Supply

- 12) The long-run aggregate supply curve is
- A) vertical.
  - B) negatively sloped.
  - C) positively sloped but extremely steep.
  - D) almost flat.
  - E) positively sloped at low levels of real GDP and vertical at high levels of real GDP.

Answer: A

Diff: 1 Type: MC

Topic: Aggregate Supply

- 13) The short-run aggregate supply curve is the relationship between the quantity of real GDP supplied and
- A) the quantity of real GDP demanded.
  - B) real income.
  - C) the inflation rate.
  - D) the real interest rate.
  - E) the price level.

Answer: E

Diff: 1 Type: MC

Topic: Aggregate Supply

- 14) Everything else remaining the same, the short-run aggregate supply curve shifts rightward if
- A) the money wage rate increases.
  - B) aggregate demand increases.
  - C) the full-employment quantity of labour increases.
  - D) factor prices increase.
  - E) the quantity of capital decreases.

Answer: C

Diff: 2 Type: MC

Topic: Aggregate Supply

- 15) Which one, if any, of the following events shift the short-run aggregate supply curve but not the long-run aggregate supply curve?
- A) A change in factor prices.
  - B) A change in the quantity of capital.
  - C) An advance in technology.
  - D) An increase in the full-employment quantity of labour.
  - E) None of the above.

Answer: A

Diff: 2 Type: MC

Topic: Aggregate Supply

- 16) Suppose there is an increase in the quantity of capital. As a result, the *SAS*
- A) and the *LAS* curves both shift leftward.
  - B) and the *LAS* curves both shift rightward.
  - C) curve does not shift but the *LAS* curve shifts rightward.
  - D) curve does not shift but the *LAS* curve shifts leftward.
  - E) shifts rightward, but the *LAS* curve does not shift.

Answer: B

Diff: 2 Type: MC

Topic: Aggregate Supply

- 17) Potential GDP is the level of real GDP at which
- A) aggregate demand equals short-run aggregate supply.
  - B) there is full employment.
  - C) there is a recessionary gap.
  - D) there is over-full employment.
  - E) prices are sure to rise.

Answer: B

Diff: 1 Type: MC

Topic: Aggregate Supply

Source: Study Guide

- 18) A technological advance shifts
- A) both *SAS* and *AD* rightward.
  - B) both *SAS* and *LAS* leftward.
  - C) *SAS* rightward but leaves *LAS* unchanged.
  - D) *LAS* rightward but leaves *SAS* unchanged.
  - E) both *SAS* and *LAS* rightward.

Answer: E

Diff: 2 Type: MC

Topic: Aggregate Supply

Source: Study Guide

- 19) An increase in oil prices to a country that is a net importer of oil shifts
- A) both the short-run aggregate supply and long-run aggregate supply curves rightward.
  - B) both the short-run aggregate supply and long-run aggregate supply curves leftward.
  - C) the short-run aggregate supply curve leftward, but leaves the long-run aggregate supply curve unchanged.
  - D) the long-run aggregate supply curve rightward, but leaves the short-run aggregate supply curve unchanged.
  - E) the short-run aggregate supply curve leftward, but shifts the long-run aggregate supply curve rightward.

Answer: C

Diff: 2 Type: MC

Topic: Aggregate Supply

- 20) If the money wage rate falls, then
- A) the *AD* curve shifts rightward.
  - B) firms hire less labour.
  - C) the *LAS* curve shifts rightward.
  - D) the *SAS* curve shifts rightward.
  - E) C and D.

Answer: D

Diff: 2 Type: MC

Topic: Aggregate Supply

- 21) Long-run aggregate supply will increase for all of the following reasons *except*
- A) a fall in the money wage rate.
  - B) an increase in human capital.
  - C) the introduction of new technology.
  - D) an increase in the full-employment quantity of labour.
  - E) an increase in the quantity of capital.

Answer: A

Diff: 2 Type: MC

Topic: Aggregate Supply

Source: Study Guide

22) An increase in the money wage rate shifts

A) both *SAS* and *LAS* rightward.

B) both *SAS* and *LAS* leftward.

C) *SAS* leftward, but leaves *LAS* unchanged.

D) *LAS* rightward, but leaves *SAS* unchanged.

E) *SAS* rightward, but leaves *LAS* unchanged.

Answer: C

Diff: 2 Type: MC

Topic: Aggregate Supply

Source: Study Guide

## 26.2 Aggregate Demand

1) Aggregate demand

A) measures the amount of a nation's goods and services that people are willing to buy.

B) measures the amount of a nation's labour, capital, and technology that people are willing to buy.

C) is the relationship between the quantity of real GDP demanded and the price level.

D) increases when the price level falls.

E) both C and D are correct.

Answer: C

Diff: 1 Type: MC

Topic: Aggregate Demand

2) Which of the following situations illustrates how fiscal policy can influence aggregate demand?

A) The Bank of Canada raises interest rates so people plan to buy less consumer durables. As a result, the aggregate demand curve shifts leftward.

B) Investors, anticipating an erosion of financial wealth due to inflation, decide to save more. As a result, aggregate demand decreases.

C) The government reduces the goods and services tax. As a result, consumption expenditure increases and aggregate demand increases.

D) The exchange rate value of the Canadian dollar rises. As a result, people living near the U.S.-Canada border increase their imports of goods and net exports decrease.

E) Both A and C are examples of fiscal policy.

Answer: C

Diff: 2 Type: MC

Topic: Aggregate Demand

3) Which of the following situations illustrates how monetary policy can influence aggregate demand?

A) The Bank of Canada raises interest rates so people plan to buy less consumer durables. As a result, the aggregate demand curve shifts leftward.

B) Investors, anticipating an erosion of financial wealth due to inflation, decide to save more. As a result, aggregate demand decreases.

C) The government reduces the goods and services tax. As a result, consumption expenditure increases and aggregate demand increases.

D) The exchange rate value of the Canadian dollar rises. As a result, people living near the U.S.-Canada border increase their imports of goods and net exports decrease.

E) Both A and D are examples of monetary policy.

Answer: A

Diff: 2 Type: MC

Topic: Aggregate Demand

- 4) Disposable income is aggregate income
- A) minus taxes and benefits.
  - B) minus taxes plus transfer payments.
  - C) minus fixed expenses such as rent and utilities.
  - D) plus transfer payments.
  - E) minus taxes.

Answer: B

Diff: 1 Type: MC

Topic: Aggregate Demand

- 5) The quantity of real GDP demanded is composed of the purchases of
- A) households and net exporters only.
  - B) firms, bondholders, and net exporters only.
  - C) firms and governments only.
  - D) consumers, firms, governments, and net exporters.
  - E) consumers, firms, and governments only.

Answer: D

Diff: 2 Type: MC

Topic: Aggregate Demand

- 6) The quantity of real GDP demanded does *not* depend on decisions made by
- A) foreigners.
  - B) households.
  - C) suppliers.
  - D) governments.
  - E) firms.

Answer: C

Diff: 1 Type: MC

Topic: Aggregate Demand

- 7) The quantity of real GDP demanded is the sum of real consumption expenditure ( $C$ ), investment ( $I$ ),
- A) government expenditure ( $G$ ), exports ( $X$ ), and imports ( $M$ ).
  - B) government expenditure ( $G$ ), and exports ( $X$ ) minus imports ( $M$ ).
  - C) exports ( $X$ ), and imports ( $M$ ).
  - D) and exports ( $X$ ) minus imports ( $M$ ).
  - E) and government expenditure ( $G$ ).

Answer: B

Diff: 2 Type: MC

Topic: Aggregate Demand

- 8) The aggregate demand curve is a relationship between
- A) real aggregate expenditure and real GDP.
  - B) real income and real GDP.
  - C) real prices and real GDP.
  - D) the price level and the quantity of real GDP demanded.
  - E) the price level and nominal GDP.

Answer: D

Diff: 1 Type: MC

Topic: Aggregate Demand

- 9) Which one of the following variables is *not* held constant along a given aggregate demand curve?

- A) fiscal policy
- B) real income
- C) tax rates
- D) expectations about inflation
- E) the price level

Answer: E

Diff: 2 Type: MC

Topic: Aggregate Demand

- 10) Which one of the following variables can change without creating a shift of the aggregate demand curve?

- A) the interest rate
- B) price level
- C) the tax rate
- D) expectations about inflation
- E) monetary policy

Answer: B

Diff: 2 Type: MC

Topic: Aggregate Demand

- 11) Your total wealth is \$1,000, which you are holding in your savings account. If the price level rises by 10 percent, your wealth

- A) increases by an unknown amount.
- B) is unchanged.
- C) decreases to \$990.
- D) is worth 10 percent less than before the price level change.
- E) increases to \$1,100.

Answer: D

Diff: 2 Type: MC

Topic: Aggregate Demand

12) If the price level rises, then the wealth effect leads to

- A) an increase in real wealth, an increase in current consumption expenditure, and an increase in saving.
- B) an increase in real wealth, an increase in current consumption expenditure, and a decrease in saving.
- C) a decrease in real wealth, an increase in current consumption expenditure, and an increase in saving.
- D) a decrease in real wealth, an increase in current consumption expenditure, and a decrease in saving.
- E) a decrease in real wealth, a decrease in current consumption expenditure, and an increase in saving.

Answer: E

Diff: 3 Type: MC

Topic: Aggregate Demand

13) Which one of the following factors will *not* shift the aggregate demand curve?

- A) an increase in the interest rate
- B) an increase in the expected inflation rate
- C) an increase in the price level
- D) an increase in expected future profits
- E) an increase in the quantity of money

Answer: C

Diff: 2 Type: MC

Topic: Aggregate Demand

14) If a change in wealth is induced by a change in the price level, then this would be shown as a

- A) movement along the aggregate demand curve.
- B) shift of the aggregate demand curve due to the substitution effects.
- C) movement along the aggregate demand curve due to the substitution effects.
- D) movement along the aggregate supply curve.
- E) shift of the aggregate demand curve due to the wealth effect.

Answer: A

Diff: 2 Type: MC

Topic: Aggregate Demand

15) Everything else remaining the same, an increase in the quantity of money

- A) shifts the aggregate demand curve rightward.
- B) shifts the aggregate demand curve leftward.
- C) shifts the aggregate supply curve leftward.
- D) shifts the aggregate supply curve rightward.
- E) creates a movement down along the aggregate demand curve.

Answer: A

Diff: 2 Type: MC

Topic: Aggregate Demand

16) Everything else remaining the same, which one of the following increases aggregate demand?

- A) an increase in taxes
- B) an increase in transfer payments
- C) a decrease in government spending
- D) a decrease in the price level
- E) a decrease in the quantity of money

Answer: B

Diff: 2 Type: MC

Topic: Aggregate Demand

17) Everything else remaining the same, an increase in the interest rate increases saving and

- A) increases aggregate demand through the international substitution effect.
- B) decreases aggregate demand through the international substitution effect.
- C) increases aggregate demand through the intertemporal substitution effect.
- D) decreases aggregate demand through the intertemporal substitution effect.
- E) increases aggregate demand through the wealth effect.

Answer: D

Diff: 3 Type: MC

Topic: Aggregate Demand

18) Everything else remaining the same, an increase in foreign income

- A) increases Canada's aggregate supply.
- B) increases Canada's aggregate demand.
- C) decreases Canada's aggregate demand.
- D) creates a movement downward along Canada's aggregate demand curve.
- E) decreases Canada's aggregate supply.

Answer: B

Diff: 2 Type: MC

Topic: Aggregate Demand

19) Which one of the following is a reason for the negative slope of the aggregate demand curve?

- A) the real wage effect
- B) the substitution effects
- C) the expected inflation effect
- D) the nominal balance effect
- E) the income effect

Answer: B

Diff: 2 Type: MC

Topic: Aggregate Demand

20) Which one of the following shifts the aggregate demand curve leftward?

- A) a decrease in the interest rate
- B) an increase in expected inflation
- C) an increase in taxes
- D) an increase in the price level
- E) an increase in the money wage rate

Answer: C

Diff: 2 Type: MC

Topic: Aggregate Demand

Use the figure below to answer the following questions.

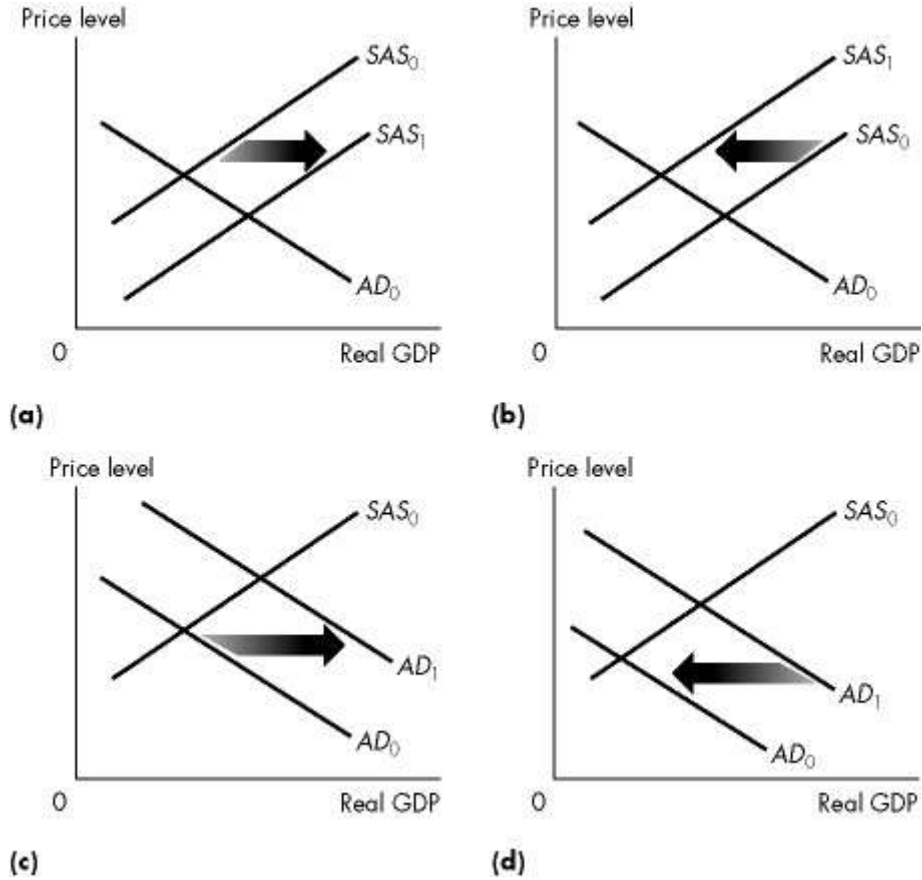


Figure 26.2.1

21) Refer to Figure 26.2.1. Which graph illustrates what happens when government expenditure increases?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) None of the above

Answer: C

Diff: 2 Type: MC

Topic: Aggregate Demand

Source: Study Guide

22) Refer to Figure 26.2.1. Which graph illustrates what happens when the quantity of money decreases?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) None of the above

Answer: D

Diff: 2 Type: MC

Topic: Aggregate Demand

Source: Study Guide

23) Refer to Figure 26.2.1. Which graph illustrates what happens when expected future income increases?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) None of the above.

Answer: C

Diff: 2 Type: MC

Topic: Aggregate Demand

Source: Study Guide

24) Refer to Figure 26.2.1. Which graph illustrates what happens when government expenditure decreases?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (a) and (b)

Answer: D

Diff: 2 Type: MC

Topic: Aggregate Demand

25) Refer to Figure 26.2.1. Which graph illustrates what happens when the quantity of money increases?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) (a) and (b)

Answer: C

Diff: 2 Type: MC

Topic: Aggregate Demand

26) Which of the following does *not* change aggregate demand?

- A) an increase in expected future income
- B) a change in fiscal policy
- C) a change in monetary policy
- D) an advance in technology
- E) a rise in the exchange rate

Answer: D

Diff: 2 Type: MC

Topic: Aggregate Demand

27) Everything else remaining the same, an increase in the expected inflation rate

- A) shifts the aggregate demand curve rightward.
- B) shifts the aggregate demand curve leftward.
- C) shifts the short-run aggregate supply curve leftward.
- D) shifts the long-run aggregate supply curve rightward.
- E) creates a movement up along the aggregate demand curve.

Answer: A

Diff: 2 Type: MC

Topic: Aggregate Demand

## 26.3 Explaining Macroeconomic Trends and Fluctuations

1) Which one of the following newspaper quotations describes a movement along an *SAS* curve?

- A) "The decrease in consumer spending may lead to a recession."
- B) "The increase in consumer spending is expected to lead to inflation, without any increase in real GDP."
- C) "Recent higher wage settlements are expected to cause higher inflation this year."
- D) "Growth has been unusually high the last few years due to more women entering the labour force."
- E) "The recent tornadoes destroyed many factories in Calgary and Edmonton."

Answer: A

Diff: 3 Type: MC

Topic: Explaining Macroeconomic Fluctuations

Source: Study Guide

2) Full-employment equilibrium occurs when

- A) aggregate demand equals short-run aggregate supply.
- B) all who are willing and able to work, are working.
- C) real GDP equals potential GDP.
- D) real GDP equals potential GDP and the wage level is set so that the GDP deflator equals 100.
- E) all who are willing and able to work, are working and the wage level is set so that the GDP deflator equals 100.

Answer: C

Diff: 1 Type: MC

Topic: Explaining Macroeconomic Fluctuations

3) A recessionary gap is the amount by which

- A) potential GDP exceeds real GDP.
- B) demand will increase to achieve full employment at a given price level.
- C) the supply curve must increase to achieve full employment at a given price level.
- D) the price level must adjust to achieve full employment.
- E) real GDP exceeds potential GDP.

Answer: A

Diff: 1 Type: MC

Topic: Explaining Macroeconomic Fluctuations

4) An inflationary gap is the amount by which

- A) potential GDP exceeds real GDP.
- B) demand must increase to achieve full employment at a given price level.
- C) supply must increase to achieve full employment at a given price level.
- D) the price level must adjust to achieve full employment.
- E) real GDP exceeds potential GDP.

Answer: E

Diff: 1 Type: MC

Topic: Explaining Macroeconomic Fluctuations

- 5) When the actual unemployment rate is equal to the natural unemployment rate, then the
- A) inflation rate must be zero.
  - B) long-run aggregate supply curve is upward sloping.
  - C) short-run aggregate supply curve is vertical.
  - D) economy is operating at potential GDP.
  - E) the money wage rate will rise.

Answer: D

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

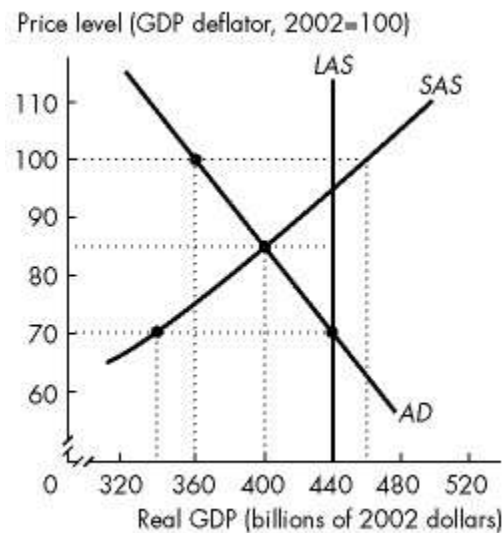
- 6) When an economy is operating on its long-run aggregate supply curve,
- A) the actual inflation rate is greater than the anticipated inflation rate.
  - B) the actual unemployment rate equals the natural unemployment rate.
  - C) unemployment will fall to an unusually low rate that is not likely to last into the future.
  - D) real GDP demanded exceeds real GDP supplied.
  - E) inflation must be positive.

Answer: B

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

*Use the figure below to answer the following questions.*



**Figure 26.3.1**

- 7) Refer to Figure 26.3.1. Short-run macroeconomic equilibrium real GDP in Econoworld is
- A) \$360 billion.
  - B) \$400 billion.
  - C) \$440 billion.
  - D) \$480 billion.
  - E) \$520 billion.

Answer: B

Diff: 1 Type: MC

Topic: Explaining Macroeconomic Fluctuations

8) Refer to Figure 26.3.1. When the economy of Econoworld is in short-run macroeconomic equilibrium, the price level is

- A) 100.
- B) 90.
- C) 75.
- D) 70.
- E) 85.

Answer: E

Diff: 1 Type: MC

Topic: Explaining Macroeconomic Fluctuations

9) Refer to Figure 26.3.1. Econoworld is at its short-run macroeconomic equilibrium. There is a difference between \_\_\_\_\_ real GDP and potential GDP of \$\_\_\_\_\_ billion.

- A) above full-employment equilibrium; 40
- B) above full-employment equilibrium; 20
- C) below full-employment equilibrium; 40
- D) below full-employment equilibrium; 20
- E) full-employment equilibrium; 0

Answer: C

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

10) Refer to Figure 26.3.1. As Econoworld automatically adjusts to long-run equilibrium, the

- A) *SAS* curve shifts rightward.
- B) *AD* curve shifts rightward.
- C) *SAS* curve shifts leftward.
- D) *AD* curve shifts leftward.
- E) *LAS* curve shifts leftward.

Answer: A

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

11) Refer to Figure 26.3.1. If Econoworld automatically adjusts to a long-run equilibrium, then in the long-run macroeconomic equilibrium

- A) the price level is 70.
- B) real GDP is \$440 billion.
- C) actual unemployment exceeds the natural unemployment rate.
- D) potential GDP is greater than in the short run.
- E) both A and B.

Answer: E

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

- 12) Refer to Figure 26.3.1. Consider statements (1) and (2) and select the correct answer.
- (1) The economy of Econoworld is experiencing an above full-employment equilibrium.
  - (2) SAS will automatically shift rightward as the economy adjusts to long-run equilibrium.
- A) (1) is true; (2) is false.
  - B) (2) is true; (1) is false.
  - C) (1) and (2) are false.
  - D) (1) and (2) are true.
  - E) (1) is true; (2) is true if unemployment is below the natural rate.

Answer: B

Diff: 3 Type: MC

Topic: Explaining Macroeconomic Fluctuations

- 13) Refer to Figure 26.3.1. Consider statements (1) and (2) and select the correct answer.
- (1) The actual unemployment rate exceeds the natural unemployment rate.
  - (2) Short-run aggregate supply will automatically shift leftward as the economy adjusts to long-run equilibrium.
- A) (1) is true; (2) is false.
  - B) (2) is true; (1) is false.
  - C) (1) and (2) are false.
  - D) (1) and (2) are true.
  - E) (1) is true; (2) is true if the money wage rate falls.

Answer: A

Diff: 3 Type: MC

Topic: Explaining Macroeconomic Fluctuations

- 14) Refer to Figure 26.3.1. Consider statements (1) and (2) and select the correct answer.
- (1) The economy of Econoworld is experiencing a below full-employment equilibrium.
  - (2) The actual unemployment rate equals the natural unemployment rate.
- A) (1) is true; (2) is false.
  - B) (2) is true; (1) is false.
  - C) (1) and (2) are false.
  - D) (1) and (2) are true.
  - E) (1) is true; (2) is true if the natural unemployment rate is too high.

Answer: A

Diff: 3 Type: MC

Topic: Explaining Macroeconomic Fluctuations

Use the figure below to answer the following questions.

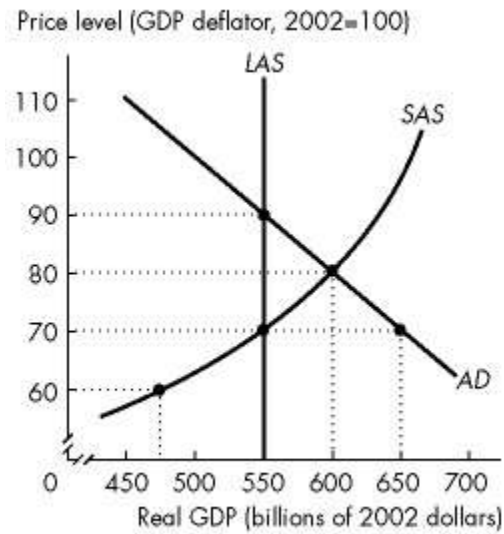


Figure 26.3.2

15) Refer to Figure 26.3.2. Short-run macroeconomic equilibrium real GDP in Mythlo is \_\_\_\_\_ billion.

- A) \$500
- B) \$650
- C) \$550
- D) \$600
- E) \$475

Answer: D

Diff: 1 Type: MC

Topic: Explaining Macroeconomic Fluctuations

16) Refer to Figure 26.3.2. When the economy of Mythlo is in short-run macroeconomic equilibrium, the price level is

- A) 65.
- B) 95.
- C) 70.
- D) 75.
- E) 80.

Answer: E

Diff: 1 Type: MC

Topic: Explaining Macroeconomic Fluctuations

17) Refer to Figure 26.3.2. In Mythlo there is a difference between the \_\_\_\_\_ equilibrium real GDP and potential GDP of \_\_\_\_\_ billion.

- A) above full-employment; \$50
- B) above full-employment; \$25
- C) below full-employment; \$50
- D) below full-employment; \$25
- E) full employment; 0

Answer: A

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

18) Refer to Figure 26.3.2. As the economy of Mythlo automatically adjusts to long-run equilibrium, the

- A) *SAS* curve shifts rightward.
- B) *AD* curve shifts rightward.
- C) *SAS* curve shifts leftward.
- D) *AD* curve shifts leftward.
- E) *LAS* curve shifts rightward.

Answer: C

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

19) Refer to Figure 26.3.2. Currently in Mythlo

- A) there is a below full-employment equilibrium.
- B) the actual unemployment rate is less than the natural unemployment rate.
- C) potential GDP is greater than equilibrium GDP.
- D) the actual unemployment rate is equal to the natural unemployment rate.
- E) there is a recessionary gap.

Answer: B

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

20) Refer to Figure 26.3.2. If the economy of Mythlo automatically adjusts to long-run equilibrium, then

- A) the price level rises to 90.
- B) real GDP is \$600 billion.
- C) the actual unemployment rate exceeds the natural unemployment rate.
- D) potential GDP decreases.
- E) the *SAS* curve shifts rightward.

Answer: A

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

- 21) Refer to Figure 26.3.2. Consider statements (1) and (2) and select the correct answer.
- (1) The economy of Mythlo is experiencing an above full-employment equilibrium.
  - (2) SAS will automatically shift rightward as the economy adjusts to long-run equilibrium.
- A) (1) is true; (2) is false.
  - B) (2) is true; (1) is false.
  - C) (1) and (2) are false.
  - D) (1) and (2) are true.
  - E) (1) is true; (2) is true only if the *LAS* curve shifts rightward at the same time.

Answer: A

Diff: 3 Type: MC

Topic: Explaining Macroeconomic Fluctuations

- 22) Refer to Figure 26.3.2. Consider statements (1) and (2) and select the correct answer.
- (1) The actual unemployment rate exceeds the natural unemployment rate in the short run.
  - (2) SAS automatically shifts rightward as the economy adjusts to long-run equilibrium.
- A) (1) is true; (2) is false.
  - B) (2) is true; (1) is false.
  - C) (1) and (2) are false.
  - D) (1) and (2) are true.
  - E) (1) is false; (2) is true if the *LAS* curve shifts rightward at the same time.

Answer: C

Diff: 3 Type: MC

Topic: Explaining Macroeconomic Fluctuations

- 23) Short-run macroeconomic equilibrium *always* occurs when the
- A) economy is at full employment.
  - B) economy is below full employment.
  - C) economy is above full employment.
  - D) quantity of real GDP demanded equals the quantity of real GDP supplied.
  - E) *AD* curve intersects the *LAS* curve.

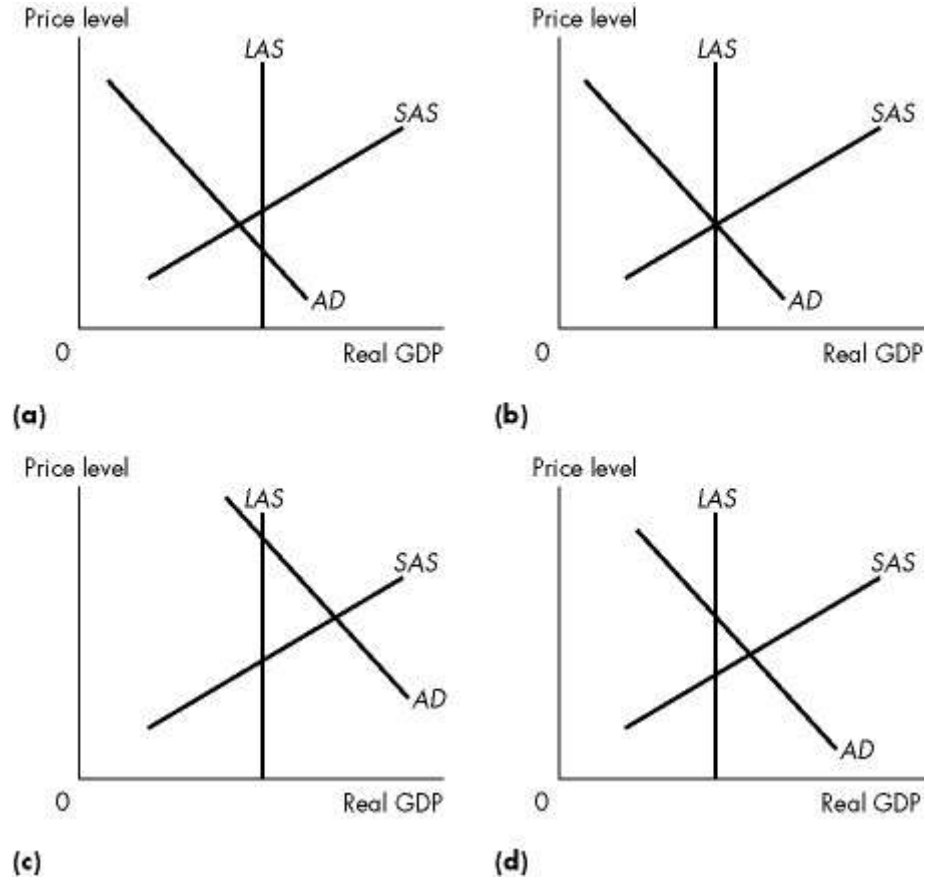
Answer: D

Diff: 1 Type: MC

Topic: Explaining Macroeconomic Fluctuations

Source: Study Guide

Use the figure below to answer the following questions.



**Figure 26.3.3**

24) Refer to Figure 26.3.3. Which one of the graphs illustrates a below full-employment equilibrium?

- A) (a) only
- B) (b) only
- C) (c) only
- D) (d) only
- E) both (c) and (d)

Answer: A

Diff: 1 Type: MC

Topic: Explaining Macroeconomic Fluctuations

Source: Study Guide

25) Refer to Figure 26.3.3. Which of the graphs illustrates an above full-employment equilibrium?

- A) (a) only
- B) (b) only
- C) (c) only
- D) (d) only
- E) both (c) and (d)

Answer: E

Diff: 1 Type: MC

Topic: Explaining Macroeconomic Fluctuations

Source: Study Guide

26) Refer to Figure 26.3.3. In which of the graphs would we predict that eventually the price level will rise and real GDP will fall, all else remaining the same?

- A) (a) only
- B) (d) only
- C) (b) only
- D) (c) and (d)
- E) (c) only

Answer: D

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

27) Refer to Figure 26.3.3. In which of the graphs would we predict that eventually the price level will fall and real GDP will decrease, all else remaining the same?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) none of the graphs

Answer: E

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

28) Refer to Figure 26.3.3. Which one of the graphs illustrates a full-employment equilibrium?

- A) (a) only
- B) (b) only
- C) (c) only
- D) (d) only
- E) (c) and (d)

Answer: B

Diff: 1 Type: MC

Topic: Explaining Macroeconomic Fluctuations

29) Refer to Figure 26.3.3. In which of the graphs would we predict that eventually the price level will fall and real GDP will increase, all else remaining the same?

- A) (a) only
- B) (b) only
- C) (c) only
- D) (d) only
- E) (c) and (d)

Answer: A

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

30) Refer to Figure 26.3.3(a). You might expect the government to

- A) do nothing except maintain the current equilibrium.
- B) cut government expenditure.
- C) increase government expenditure.
- D) pursue trade policies that reduce exports.
- E) raise taxes.

Answer: C

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

31) Refer to Figure 26.3.3(b). You might expect the government to

- A) do nothing except maintain the current equilibrium.
- B) cut government expenditure.
- C) increase government expenditure.
- D) pursue trade policies that reduce exports.
- E) raise taxes.

Answer: A

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

32) If real GDP is greater than potential GDP, the economy is

- A) not in short-run equilibrium.
- B) in a recessionary equilibrium.
- C) in an above full-employment equilibrium.
- D) in a below full-employment equilibrium.
- E) in long-run equilibrium.

Answer: C

Diff: 1 Type: MC

Topic: Explaining Macroeconomic Fluctuations

Source: Study Guide

33) If factor prices remain constant, an increase in aggregate demand

- A) increases the price level and increases real GDP.
- B) increases the price level and decreases real GDP.
- C) decreases the price level and increases real GDP.
- D) decreases the price level and decreases real GDP.
- E) increases the price level, and leaves real GDP unchanged.

Answer: A

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

Source: Study Guide

34) Beginning at a long-run equilibrium, an increase in aggregate demand

- A) increases the price level and in the long run increases real GDP.
- B) increases the price level and in the long run decreases real GDP.
- C) decreases the price level and in the long run increases real GDP.
- D) decreases the price level and in the long run decreases real GDP.
- E) increases the price level, but in the long run there is no change in real GDP.

Answer: E

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

35) We observe an increase in the price level and a decrease in real GDP. Which of the following is a possible explanation?

- A) an increase in expected future profits
- B) an increase in expected future income
- C) an increase in factor prices
- D) an increase in the quantity of capital
- E) an increase in the quantity of money

Answer: C

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

Source: Study Guide

36) We observe an increase in the price level and an increase in real GDP. Which of the following is a possible explanation?

- A) a decrease in the quantity of money
- B) a decrease in expected future income
- C) an increase in factor prices
- D) an increase in the quantity of capital
- E) an increase in expected future profits

Answer: E

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

37) We observe a decrease in the price level and a decrease in real GDP. Which of the following is a possible explanation?

- A) a decrease in the quantity of money
- B) an increase in expected future income
- C) an increase in factor prices
- D) an increase in the quantity of capital
- E) an increase in expected future profits

Answer: A

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

38) We observe a decrease in the price level and an increase in real GDP. Which of the following is a possible explanation?

- A) a decrease in the quantity of money
- B) a decrease in expected future income
- C) an increase in factor prices
- D) an increase in the quantity of capital
- E) an increase in expected future profits

Answer: D

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

39) The economy cannot remain indefinitely with real GDP greater than potential GDP because the money wage rate will

- A) decrease, shifting the LAS curve rightward.
- B) decrease, shifting the SAS curve rightward.
- C) increase, shifting the LAS curve leftward.
- D) increase, shifting the SAS curve leftward.
- E) increase, shifting the SAS curve rightward.

Answer: D

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

40) If real GDP is less than potential GDP, then the economy is

- A) not in short-run equilibrium.
- B) in a full-employment equilibrium.
- C) in an above full-employment equilibrium.
- D) in a below full-employment equilibrium.
- E) in long-run equilibrium.

Answer: D

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

Use the table below to answer the following questions.

**Table 26.3.1**

Price Level (2002=100)	Aggregate Demand (billions of 2002 dollars)	Short-Run Aggregate Supply (billions of 2002 dollars)	Long-Run Aggregate Supply (billions of 2002 dollars)
100	800	300	600
110	700	400	600
120	600	500	600
130	500	600	600
140	400	700	600

41) Refer to Table 26.3.1. Consider the economy represented in the table. In short-run macroeconomic equilibrium, the price level is \_\_\_\_\_ and the level of real GDP is \_\_\_\_\_ billion.

- A) 120; \$600
- B) 120; \$500
- C) 125; \$550
- D) 130; \$600
- E) 130; \$500

Answer: C

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

Source: Study Guide

42) Refer to Table 26.3.1. Consider the economy represented in the table. The economy is in

- A) a long-run equilibrium, and resource prices will not change.
- B) an above full-employment equilibrium, and factor prices will increase.
- C) an above full-employment equilibrium, and factor prices will decrease.
- D) a below full-employment equilibrium, and factor prices will decrease.
- E) a below full-employment equilibrium, and factor prices will increase.

Answer: D

Diff: 3 Type: MC

Topic: Explaining Macroeconomic Fluctuations

Source: Study Guide

43) Refer to Table 26.3.1. Consider the economy represented in the table. There is

- A) an inflationary gap equal to \$100 billion.
- B) an inflationary gap equal to \$50 billion.
- C) a recessionary gap equal to \$50 billion.
- D) a recessionary gap equal to \$100 billion.
- E) neither an inflationary nor a recessionary gap because the economy is at full employment.

Answer: C

Diff: 3 Type: MC

Topic: Explaining Macroeconomic Fluctuations

Source: Study Guide

44) Refer to Table 26.3.1. Consider the economy represented in the table. The economy eventually moves to its long-run equilibrium. In long-run equilibrium, the price level is \_\_\_\_\_ and real GDP is \_\_\_\_\_ billion.

- A) 125; \$550
- B) 120; \$600
- C) 120; \$500
- D) 130; \$600
- E) 130; \$500

Answer: B

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

45) Refer to Table 26.3.1. As this economy moves to long-run equilibrium, the

- A) *SAS* curve shifts leftward.
- B) *SAS* curve shifts rightward.
- C) *AD* curve shifts rightward.
- D) *AD* curve shifts leftward.
- E) *LAS* curve shifts leftward.

Answer: B

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

46) Consider an economy starting from a position of full employment. Which one of the following changes does *not* occur as a result of a decrease in aggregate demand?

- A) The price level decreases.
- B) The level of real GDP decreases in the short run.
- C) A recessionary gap arises.
- D) Factor prices decrease in the long run, shifting the short-run aggregate supply curve rightward.
- E) The long-run aggregate supply curve shifts leftward to create the new long-run equilibrium.

Answer: E

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

Source: Study Guide

47) Consider an economy starting from a position of full employment. Which one of the following occurs as a result of an advance in technology?

- A) The price level falls.
- B) Real GDP decreases in the short run.
- C) An inflationary gap arises.
- D) Factor prices rise in the long run, shifting the short-run aggregate supply curve leftward.
- E) The long-run aggregate supply curve shifts leftward to create the new long-run equilibrium.

Answer: A

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

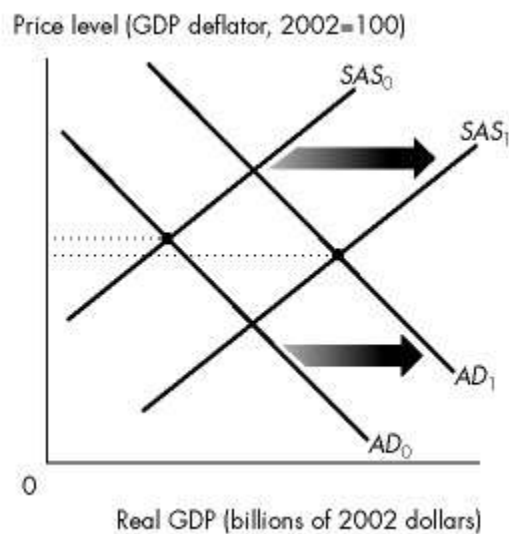
- 48) Consider an economy starting from a position of full employment. Which one of the following changes does *not* occur as a result of an increase in aggregate demand?
- A) The price level rises.
  - B) Real GDP increases in the short run.
  - C) An inflationary gap arises.
  - D) Factor prices rise in the long run, shifting the short-run aggregate supply curve to the left.
  - E) The long-run aggregate supply curve shifts rightward to create the new long-run equilibrium.

Answer: E

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

Use the figure below to answer the following question.



**Figure 26.3.4**

- 49) Refer to Figure 26.3.4. The changes represented
- A) cannot occur because aggregate demand and short-run aggregate supply cannot change at the same time.
  - B) lead to an inflationary gap.
  - C) lead to a recessionary gap.
  - D) cause a proportionate increase in long run aggregate supply.
  - E) increase real GDP.

Answer: E

Diff: 3 Type: MC

Topic: Explaining Macroeconomic Fluctuations

- 50) All of the following will raise the price level *except*
- A) aggregate demand increases and short-run aggregate supply decreases.
  - B) aggregate demand increases.
  - C) short-run aggregate supply decreases.
  - D) an increase in the quantity of capital.
  - E) an increase in the quantity of money.

Answer: D

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

- 51) Which of the following will lower the price level for sure?
- A) The *AD* curve shifts rightward and the *SAS* curve shifts leftward.
  - B) The *AD* curve shifts rightward and the *SAS* curve remains unchanged.
  - C) The *SAS* curve shifts leftward.
  - D) The *LAS* curve shifts leftward.
  - E) None of the above.

Answer: E

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

- 52) If real GDP is greater than potential GDP, we would expect
- A) the money wage rate to fall.
  - B) the money wage rate to rise.
  - C) potential GDP to increase.
  - D) potential GDP to decrease.
  - E) A and C.

Answer: B

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

- 53) If real GDP is less than potential GDP, we would expect
- A) the money wage rate to fall.
  - B) the money wage rate to rise.
  - C) potential GDP to increase.
  - D) potential GDP to decrease.
  - E) A and C.

Answer: A

Diff: 2 Type: MC

Topic: Explaining Macroeconomic Fluctuations

Use the table below to answer the following question.

**Table 26.3.2**

	<b>2004</b>	<b>2005</b>	<b>2006</b>
Real GDP growth rate	8.1	8.3	7.3
Inflation	4.2	4.7	4.6

54) Refer to Table 26.3.2. The International Monetary Fund's World Economic Outlook database provides the data given in the table for India in 2004, 2005 and 2006.

The numbers in the table are consistent with

A) increases in long-run and short-run aggregate supply and even greater increases in aggregate demand.

B) increases in short-run aggregate supply and increases in aggregate demand, but the increases in aggregate demand are smaller than the increases in short-run aggregate supply.

C) increases in long-run and short-run aggregate supply and even larger decreases in aggregate demand.

D) decreases in long-run and short-run aggregate supply and even greater decreases in aggregate demand.

E) increases in short-run aggregate supply and no change in aggregate demand.

Answer: A

Type: MC

Topic: Explaining Macroeconomic Fluctuations

Source: MyEconLab

55) Economic growth results when there are increases in

A) aggregate demand.

B) the real wage rate.

C) long-run aggregate supply.

D) the inflationary gap.

E) short-run aggregate supply resulting from falling money wage rates and falling factor prices.

Answer: C

Type: MC

Topic: Explaining Macroeconomic Fluctuations

Source: MyEconLab

Use the table below to answer the following questions.

**Table 26.3.3**

Price level	Aggregate demand	Short-run aggregate supply	Long-run aggregate supply
(2002 = 100)	(trillions of 2002 dollars)		
140	4	8	7
130	5	7	7
120	6	6	7
110	7	5	7
100	8	4	7

56) Refer to Table 26.3.3. When the economy is at its short-run macroeconomic equilibrium, the price level is

- A) 90.
- B) 110.
- C) 100.
- D) 120.
- E) 130.

Answer: D

Type: MC

57) Refer to Table 26.3.3. When the economy is at its short-run macroeconomic equilibrium,

- A) the unemployment rate is below its natural rate.
- B) the unemployment rate is above its natural rate.
- C) the money wage rate will rise.
- D) the long-run aggregate supply curve will shift eventually shift leftward to return to full employment.
- E) potential GDP will eventually increase.

Answer: B

Type: MC

58) Refer to Table 26.3.3. When the economy is at its short-run macroeconomic equilibrium, the economy

- A) is also in a long-run macroeconomic equilibrium.
- B) has an inflationary gap.
- C) has a recessionary gap.
- D) has neither an inflationary nor a recessionary gap.
- E) Both A and D are correct.

Answer: C

Type: MC

- 59) Refer to Table 26.3.3. With no interference from the central bank or the government, the
- A) money wage rate will eventually rise.
  - B) money wage rate will eventually fall.
  - C) short-run aggregate supply curve will shift leftward.
  - D) long-run aggregate supply curve will shift leftward.
  - E) aggregate demand curve will shift rightward.

Answer: B

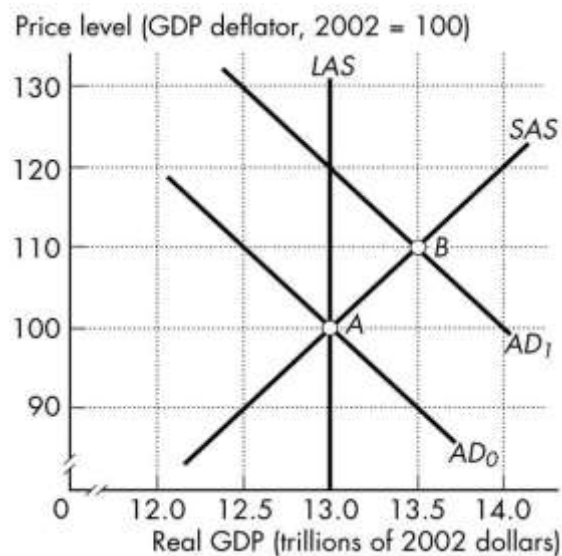
Type: MC

- 60) Refer to Table 26.3.3. With no interference from the central bank or the government, the
- A) short-run aggregate supply curve will shift rightward.
  - B) short-run aggregate supply curve will shift leftward.
  - C) long-run aggregate supply curve will shift rightward.
  - D) long-run aggregate supply curve will shift leftward.
  - E) Both A and C will occur.

Answer: A

Type: MC

Use the figure below to answer the following questions.



**Figure 26.3.5**

- 61) Refer to Figure 26.3.5. At point *B* the economy has
- A) an inflationary gap with real GDP in excess of potential GDP.
  - B) an inflationary gap with real GDP less than potential GDP.
  - C) a recessionary gap with real GDP in excess of potential GDP.
  - D) a recessionary gap with real GDP less than potential GDP.
  - E) neither an inflationary gap nor a recessionary gap.

Answer: A

Type: MC



62) Refer to Figure 26.3.5. When the economy is at full employment, real GDP is

- A) \$13 trillion.
- B) \$13.5 trillion.
- C) more than \$13 trillion and less than \$13.5 trillion.
- D) less than \$13 trillion.
- E) 100.

Answer: A

Type: MC

63) Refer to Figure 26.3.5. If the aggregate demand curve is  $AD_2$ , real GDP is

- A) \$13 trillion.
- B) \$13.5 trillion.
- C) more than \$13 trillion and less than \$13.5 trillion.
- D) less than \$13 trillion.
- E) 100

Answer: B

Type: MC

64) Refer to Figure 26.3.5. Potential GDP is

- A) \$13 trillion.
- B) \$13.5 trillion.
- C) more than \$13 trillion and less than \$13.5 trillion.
- D) less than \$13 trillion.
- E) 100

Answer: A

Type: MC

65) Refer to Figure 26.3.5. The shift of the aggregate demand curve from  $AD_0$  to  $AD_1$  might have been the result of

- A) an increase in government expenditure.
- B) a decrease in taxes.
- C) an increase in the quantity of money.
- D) a fall in the foreign exchange rate
- E) all of the above.

Answer: D

Type: MC

## 26.4 Macroeconomic Schools of Thought

- 1) Which of the following news quotes *best* describes a *Keynesian* view of a recession?
- A) "Rapid computerization is creating obsolete workers and higher unemployment."
  - B) "The unexpectedly tight fiscal policy is raising spending and lowering unemployment."
  - C) "The anti-inflationary policy of the Bank of Canada is increasing spending."
  - D) "The cuts in government spending have helped lower consumer spending and created unemployment."
  - E) "Businesses are very worried about future sales and have lowered their purchases of capital equipment."

Answer: E

Type: MC

Topic: Macroeconomic Schools of Thought

Source: Study Guide

- 2) Which of the following news quotes *best* describes a *new classical* view of a recession?
- A) "Rapid computerization is creating obsolete workers and higher unemployment."
  - B) "The unexpectedly tight fiscal policy is raising spending and lowering unemployment."
  - C) "The anti-inflationary policy of the Bank of Canada is increasing spending."
  - D) "The cuts in government spending have helped lower consumer spending and created unemployment."
  - E) "Businesses are very worried about future sales and have lowered their purchases of capital equipment."

Answer: A

Type: MC

Topic: Macroeconomic Schools of Thought

Source: Study Guide

- 3) A \_\_\_\_\_ macroeconomist believes that the economy is self-regulating and always at full employment.

A \_\_\_\_\_ macroeconomist believes the economy requires active help from fiscal policy and monetary policy to maintain full employment.

- A) Keynesian; new Keynesian
- B) classical; monetarist
- C) classical; Keynesian
- D) new classical; monetarist
- E) monetarist; classical

Answer: C

Type: MC

Topic: Macroeconomic Schools of Thought

Source: MyEconLab

4) A \_\_\_\_\_ macroeconomist believes that business cycle fluctuations are the efficient responses of a well-functioning market economy that is bombarded by shocks that arise from the uneven pace of technological change.

A \_\_\_\_\_ macroeconomist believes that the short-run aggregate supply curve is horizontal at a fixed price level.

- A) new classical; monetarist
- B) classical; monetarist
- C) Keynesian; new Keynesian
- D) new classical; new Keynesian
- E) monetarist; new classical

Answer: D

Type: MC

Topic: Macroeconomic Schools of Thought

Source: MyEconLab

5) Which of the following statements about the monetarist view of the macroeconomy is *incorrect*?

- A) The money wage rate is sticky.
- B) Taxes should be kept low to avoid disincentive effects that decrease potential GDP.
- C) All recessions result from inappropriate monetary policy.
- D) Left alone, the economy rarely operates at full employment.
- E) Provided that the quantity of money is kept on a steady growth path, no active stabilization is needed to offset changes in aggregate demand.

Answer: D

Type: MC

Topic: Macroeconomic Schools of Thought

Source: MyEconLab

6) Which of the following statements about the Keynesian view of the macroeconomy is *incorrect*?

- A) Technological change is the most significant influence on both aggregate demand and aggregate supply.
- B) To achieve and maintain full employment, active help from fiscal policy and monetary policy is required.
- C) Expectations are based on "animal spirits."
- D) The money wage rate is extremely sticky in the downward direction so there is no automatic mechanism for eliminating a recessionary gap.
- E) Expectations are the most significant influence on aggregate demand.

Answer: A

Type: MC

Topic: Macroeconomic Schools of Thought

Source: MyEconLab

- 7) The defining feature of the classical view of macroeconomics is that the economy is
- A) rarely at full employment.
  - B) driven by expectations called "animal spirits."
  - C) self-regulating and always at full employment.
  - D) constantly bombarded by shocks that arise from the uneven pace of technological change.
  - E) the most significant influence on aggregate demand is expectations.

Answer: C

Type: MC

Topic: Macroeconomic Schools of Thought

Source: MyEconLab

- 8) Classical macroeconomists recommend
- A) policies that actively offset changes in long-run aggregate supply that result in negative economic growth.
  - B) an increase in the quantity of money to offset decreases in aggregate demand and a decrease in the quantity of money to offset increases in aggregate demand.
  - C) policies that actively offset changes in aggregate demand that bring recession.
  - D) policies that minimize the disincentive effects of taxes on employment, investment, and technological change.
  - E) all of the above.

Answer: D

Type: MC

Topic: Macroeconomic Schools of Thought

Source: MyEconLab

- 9) The defining feature of the Keynesian view of macroeconomics is that the economy is
- A) rarely at full employment.
  - B) self-regulating and always at full employment.
  - C) that the quantity of money is the most significant influence on aggregate demand.
  - D) constantly bombarded by shocks that arise from the uneven pace of technological change.
  - E) no active stabilization is needed to offset changes in aggregate demand.

Answer: A

Type: MC

Topic: Macroeconomic Schools of Thought

Source: MyEconLab

10) Keynesian macroeconomists recommend

A) an increase in the quantity of money to offset decreases in aggregate demand and a decrease in the quantity of money to offset increases in aggregate demand.

B) policies that actively offset changes in long-run aggregate supply that result in negative economic growth.

C) policies that minimize the disincentive effects of taxes on employment, investment, and technological change.

D) policies that actively offset changes in aggregate demand that bring recession.

E) none of the above.

Answer: D

Type: MC

Topic: Macroeconomic Schools of Thought

Source: MyEconLab

## Chapter 27 Expenditure Multipliers: The Keynesian Model

### 27.1 Fixed Prices and Expenditure Plans

1) Disposable income is

A) used for consumption only.

B) aggregate income minus taxes plus transfer payments.

C) aggregate income plus transfer payments.

D) aggregate income minus taxes.

E) aggregate income minus transfer payments.

Answer: B

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

2) Dissaving occurs when a household

A) spends less than it receives in disposable income.

B) spends more than it saves.

C) saves more than it spends.

D) consumes more than it receives in disposable income.

E) borrows.

Answer: D

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

3) Complete the following sentence. A household

A) consumes or pays taxes out of disposable income.

B) consumes, saves, or pays taxes out of disposable income.

C) consumes or saves out of disposable income.

D) only consumes out of disposable income.

E) None of the above.

Answer: C

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 4) The marginal propensity to consume is the
- A) fraction of the first dollar of disposable income received that is saved.
  - B) fraction of the first dollar of disposable income received that is consumed.
  - C) fraction of the last dollar of disposable income received that is saved.
  - D) fraction of a change in disposable income that is spent on consumption.
  - E) total amount of consumption divided by the total amount of disposable income.

Answer: D

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 5) The marginal propensity to consume is calculated as
- A) consumption expenditure divided by the change in disposable income.
  - B) the change in consumption expenditure divided by disposable income.
  - C) consumption expenditure divided by total disposable income.
  - D) the change in consumption expenditure divided by saving.
  - E) the change in consumption expenditure divided by the change in disposable income.

Answer: E

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 6) The marginal propensity to save is calculated as
- A) saving divided by disposable income.
  - B) saving divided by the change in disposable income.
  - C) the change in saving divided by the change in consumption expenditure.
  - D) the change in saving divided by the change in disposable income.
  - E) the change in saving divided by disposable income.

Answer: D

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 7) The marginal propensity to consume
- A) is negative if dissaving is present.
  - B) is greater than 1 if dissaving is present.
  - C) is between 1/2 and 1.
  - D) is greater than 1 but less than 2.
  - E) is between zero and 1.

Answer: E

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 8) The marginal propensity to save
- A) equals  $1 - MPC$ .
  - B) is between zero and 1/2.
  - C) is greater than 1.
  - D) is greater than 1 but less than 2.
  - E) is negative.

Answer: A

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 9) The sum of the marginal propensity to save and the marginal propensity to consume
- A) always equals 1.
  - B) sometimes equals 1.
  - C) always equals 0.
  - D) never equals 1.
  - E) is greater than zero but less than 1.

Answer: A

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 10) If the marginal propensity to save is 0.2, then
- A) the marginal propensity to consume is larger than 0.8.
  - B) the marginal propensity to consume is 0.8.
  - C) the marginal propensity to consume is also 0.2.
  - D) the slope of the consumption function is 0.2.
  - E) the slope of the saving function is 0.8.

Answer: B

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 11) If a household's disposable income increases from \$12,000 to \$22,000 and at the same time its consumption expenditure increases from \$4,000 to \$9,000, then

- A) the household is dissaving.
- B) the slope of the consumption function is 0.6.
- C) the slope of the consumption function is 0.5.
- D) the marginal propensity to consume over this range is negative.
- E) the marginal propensity to save over this range is negative.

Answer: C

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 12) If consumption expenditure for a household increases from \$300 to \$500 when disposable income increases from \$200 to \$500, the marginal propensity to consume is

- A) equal to 1.
- B) equal to 0.75.
- C) equal to 1.33.
- D) negative.
- E) equal to 0.67.

Answer: E

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

13) If the marginal propensity to consume is 0.85, what change in consumption expenditure would you expect if disposable income increases by \$200 million?

- A) \$20 million
- B) \$170 million
- C) \$180 million
- D) \$1,800 million
- E) \$18 million

Answer: B

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

14) If consumption is \$8,000 when disposable income is \$10,000, the marginal propensity to consume

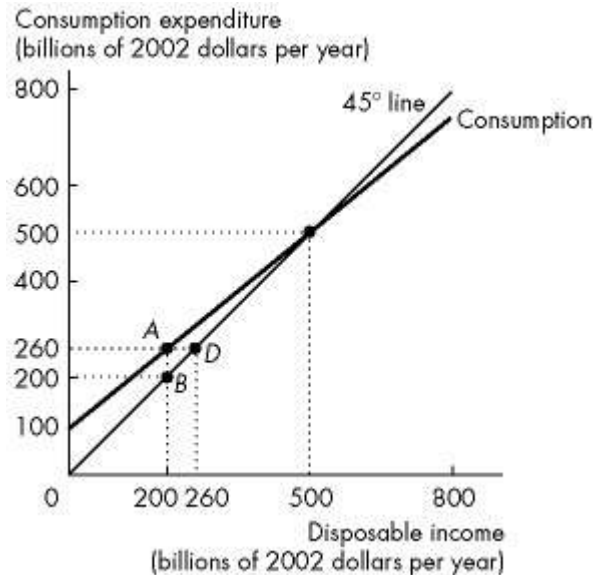
- A) is 0.50.
- B) is 0.75.
- C) is 0.80.
- D) is 1.25.
- E) cannot be determined from the information given.

Answer: E

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

Use the figure below to answer the following questions.



**Figure 27.1.1**

This figure describes the relationship between consumption expenditure and disposable income for a model economy.

- 15) Refer to Figure 27.1.1. Consumption and disposable income are equal
- A) at all points along the consumption function.
  - B) when saving equals \$40 billion and disposable income equals \$540 billion.
  - C) when disposable income is \$500 billion.
  - D) when disposable income is \$600 billion.
  - E) when disposable income is greater than or equal to \$500 billion.

Answer: C

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 16) Refer to Figure 27.1.1. When disposable income is \$500 billion, saving is equal to

- A) disposable income.
- B) zero.
- C) \$20 billion.
- D) consumption expenditure.
- E) \$40 billion.

Answer: B

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 17) Refer to Figure 27.1.1. When disposable income is \$200 billion,
- A) saving is equal to line segment *AD*.
  - B) households are consuming less than \$200 billion.
  - C) businesses are spending more than households because the consumption function lies above the 45° line.
  - D) households are dissaving an amount equal to line segment *AB*.
  - E) households are saving an amount equal to line segment *AB*.

Answer: D

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 18) Refer to Figure 27.1.1. When disposable income is equal to \$200 billion, saving is
- A) zero.
  - B) \$200 billion.
  - C) \$150 billion.
  - D) \$60 billion.
  - E) - \$60 billion.

Answer: E

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 19) Refer to Figure 27.1.1. The marginal propensity to consume for this economy is
- A) 0.5.
  - B) 1.
  - C) 0.2.
  - D) 0.8.
  - E) 0.6.

Answer: D

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 20) When the consumption function lies below the 45° line, households
- A) spend all of any increase in disposable income.
  - B) consume more than their disposable income.
  - C) are saving some portion of their disposable income.
  - D) save all of any increase in disposable income.
  - E) are dissaving.

Answer: C

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 21) The vertical distance between the consumption function and the  $45^\circ$  line measures
- A) disposable income.
  - B) consumption.
  - C) saving or dissaving.
  - D) the marginal propensity to consume.
  - E) the marginal propensity to save.

Answer: C

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

Use the table below to answer the following question.

**Table 27.1.1**

The following table shows the relationship between consumption expenditure ( $C$ ) and disposable income ( $YD$ ) for a hypothetical economy.

$YD$ (dollars)	$C$ (dollars)
100	225
200	300
300	375
400	450
500	525
600	600

- 22) Refer to Table 27.1.1. If  $YD$  is \$400, then saving is

- A) -\$50.
- B) \$50.
- C) zero.
- D) \$100.
- E) -\$125.

Answer: A

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 23) Refer to Table 27.1.1. The marginal propensity to consume is

- A) increasing as  $YD$  increases.
- B) equal to 1 when  $YD$  equals \$600.
- C) 0.75.
- D) 0.25.
- E) 1.33.

Answer: C

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

24) Refer to Table 27.1.1. The marginal propensity to save is

- A) decreasing as  $YD$  increases.
- B) equal to zero when  $YD$  equals \$600.
- C) 0.75.
- D) 0.25.
- E) 4.

Answer: D

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

25) Refer to Table 27.1.1. Based on the information in the table, if  $YD$  were zero, then

- A) consumption would be zero.
- B) consumption would be \$150.
- C) saving would be zero.
- D) consumption would be -\$150.
- E) consumption would be \$100.

Answer: B

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

26) Refer to Table 27.1.1. Based on the information in the table, saving would be \$125 if  $YD$  were

- A) \$1,000.
- B) \$1,100.
- C) \$1,200.
- D) \$1,300.
- E) \$900.

Answer: B

Diff: 3 Type: MC

Topic: Fixed Prices and Expenditure Plans

27) The consumption functions for the Canadian economy covering the period from 1970 to 2010 indicate a marginal propensity to consume approximately equal to

- A) 0.9.
- B) 0.65.
- C) 0.85.
- D) 0.7.
- E) 0.54.

Answer: C

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

Use the table below to answer the following questions.

**Table 27.1.2**

Disposable Income (dollars)	Consumption Expenditure (dollars)
325	325
400	375
475	425
550	475
625	525

28) Refer to Table 27.1.2. When saving is zero, what is the level of disposable income?

- A) \$325
- B) \$400
- C) \$475
- D) \$550
- E) \$625

Answer: A

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

29) Refer to Table 27.1.2. What is the value of the marginal propensity to consume?

- A) 0.75
- B) 0.25
- C) 1.33
- D) 0.34
- E) 0.67

Answer: E

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

30) Refer to Table 27.1.2. What is the value of the marginal propensity to save?

- A) 0.27
- B) 0.25
- C) 0.67
- D) 0.33
- E) 1.33

Answer: D

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

31) Refer to Table 27.1.2. Saving equals \$100 when disposable income is

- A) \$475.
- B) \$550.
- C) \$525.
- D) \$575.
- E) \$625.

Answer: E

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

32) The consumption function shows the relationship between consumption expenditure and

- A) the interest rate.
- B) the price level.
- C) disposable income.
- D) saving.
- E) nominal income.

Answer: C

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

33) The fraction of a change in disposable income that is saved is the

- A) marginal propensity to consume.
- B) marginal propensity to save.
- C) marginal propensity to dispose.
- D) marginal tax rate.
- E) saving function.

Answer: B

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

Source: Study Guide

34) The fraction of a change in disposable income spent on consumption is the

- A) marginal propensity to consume.
- B) marginal propensity to save.
- C) marginal propensity to dispose.
- D) marginal tax rate.
- E) consumption function.

Answer: A

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 35) The saving function shows the relationship between saving and
- A) the interest rate.
  - B) the price level.
  - C) disposable income.
  - D) consumption.
  - E) nominal income.

Answer: C

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

*Use the table below to answer the following questions.*

**Table 27.1.3**

Disposable Income (dollars)	Consumption Expenditure (dollars)
0	100
100	165
200	230
300	295
400	360

- 36) Refer to Table 27.1.3. Autonomous consumption is equal to
- A) \$0.
  - B) \$65.
  - C) \$100.
  - D) \$260.
  - E) \$400.

Answer: C

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

- 37) Refer to Table 27.1.3. The marginal propensity to consume is
- A) 0.35.
  - B) 0.65.
  - C) 1.15.
  - D) 1.65.
  - E) 1.54.

Answer: B

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

Source: Study Guide

38) In Table 27.1.3, at which of the following values of disposable income is there positive saving?

- A) 0
- B) 100
- C) 200
- D) 300
- E) both C and D are correct

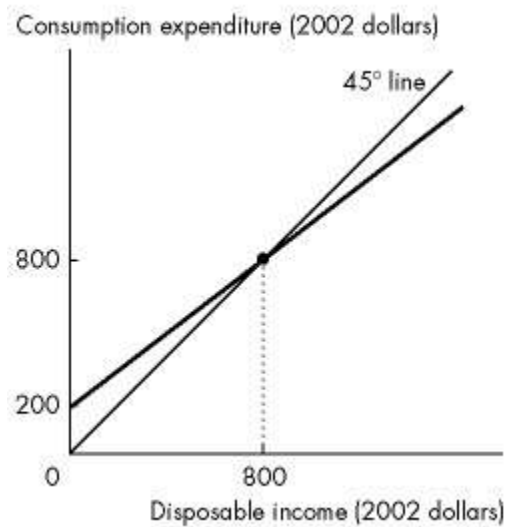
Answer: D

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

Source: Study Guide

*Use the figure below to answer the following questions.*



**Figure 27.1.2**

39) Refer to Figure 27.1.2. Autonomous consumption is

- A) -200.
- B) \$200.
- C) \$800.
- D) \$600.
- E) zero.

Answer: B

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

40) Refer to Figure 27.1.2. The marginal propensity to consume is

- A) 800.
- B) 0.8.
- C) 0.2.
- D) 0.25.
- E) 0.75.

Answer: E

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

41) The slope of the consumption function is

- A) less than the slope of the 45° line.
- B) greater than the slope of the 45° line.
- C) equal to the slope of the 45° line.
- D) one.
- E) zero.

Answer: A

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

42) Which of the following events would shift the consumption function upward?

- A) an increase in disposable income
- B) a decrease in disposable income
- C) a decrease in wealth
- D) a decrease in expected future disposable income
- E) an increase in wealth

Answer: E

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

Source: Study Guide

43) Everything else remaining the same, a decrease in expected future income \_\_\_\_\_ current consumption expenditure and \_\_\_\_\_ saving.

- A) increases; increases
- B) increases; decreases
- C) decreases; increases
- D) decreases; decreases
- E) does not change; does not change

Answer: C

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

44) Everything else remaining the same, if Canadians expect future disposable income to rise, then

- A) Canada's consumption function shifts downward.
- B) Canada's consumption function shifts upward.
- C) a movement occurs up along Canada's consumption function.
- D) a movement occurs down along Canada's consumption function.
- E) Canada's saving function shifts upward.

Answer: B

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

45) The marginal propensity to import is calculated as

- A) imports divided by the change in real GDP.
- B) the change in imports divided by real GDP.
- C) imports divided by real GDP.
- D) the change in imports divided by the change in real GDP.
- E) none of the above.

Answer: D

Diff: 1 Type: MC

Topic: Fixed Prices and Expenditure Plans

46) If an economy's real GDP increases from \$100 billion to \$150 billion, and at the same time its imports increase from \$40 billion to \$50 billion, then the marginal propensity to import

- A) decreases from 0.4 to 0.2.
- B) is greater than 0.2 and less than 0.4.
- C) is 0.2.
- D) is 0.36.
- E) is 0.4.

Answer: C

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

47) An increase in autonomous consumption

- A) shifts the consumption function upward.
- B) shifts the consumption function downward.
- C) creates a movement downward along the consumption function.
- D) creates a movement upward along the consumption function.
- E) changes the slope of the consumption function.

Answer: A

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

48) The marginal propensity to import is equal to \_\_\_\_\_.

- A) disposable income minus consumption expenditure minus saving divided by real GDP
- B) the change in imports divided by the change in real GDP that brought it about, other things remaining the same
- C) the change in net imports divided by the change in disposable income, other things remaining the same
- D) imports minus exports
- E)  $1 - MPC$

Answer: B

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

Source: MyEconLab

49) When disposable income increases

- A) the consumption function shifts upward.
- B) the saving function shifts downward.
- C) a movement occurs down along the consumption function.
- D) a movement occurs up along the consumption function.
- E) Both A and B are correct.

Answer: D

Type: MC

50) The marginal propensity to consume

- A) is equal to zero when disposable income equals consumption expenditure.
- B) is equal to 1 minus the slope of the saving function.
- C) is negative when saving is positive.
- D) increases as the economy moves upward along the consumption function.
- E) is greater than the slope of the 45-degree line.

Answer: B

Type: MC

## 27.2 Real GDP with a Fixed Price Level

1) The aggregate expenditure curve shows the relationship between aggregate planned expenditure and

- A) disposable income.
- B) real GDP.
- C) the interest rate.
- D) consumption expenditure.
- E) the price level.

Answer: B

Diff: 1 Type: MC

Topic: Real GDP with a Fixed Price Level

Source: Study Guide

2) If there is an unplanned increase in inventories, aggregate planned expenditure is

- A) greater than real GDP and firms increase production.
- B) greater than real GDP and firms decrease production.
- C) less than real GDP and firms increase production.
- D) less than real GDP and firms decrease production.
- E) less than real GDP and firms decrease investment.

Answer: D

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

Source: Study Guide

3) If aggregate planned expenditure exceeds real GDP, then inventories

- A) increase and real GDP increases.
- B) increase and real GDP falls.
- C) decrease and real GDP increases.
- D) decrease and real GDP decreases.
- E) remain constant and real GDP remains constant.

Answer: C

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

4) If aggregate planned expenditure is less than real GDP, then inventories

- A) increase and real GDP increases.
- B) increase and real GDP falls.
- C) decrease and real GDP increases.
- D) decrease and real GDP decreases.
- E) remain constant and real GDP remains constant.

Answer: B

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

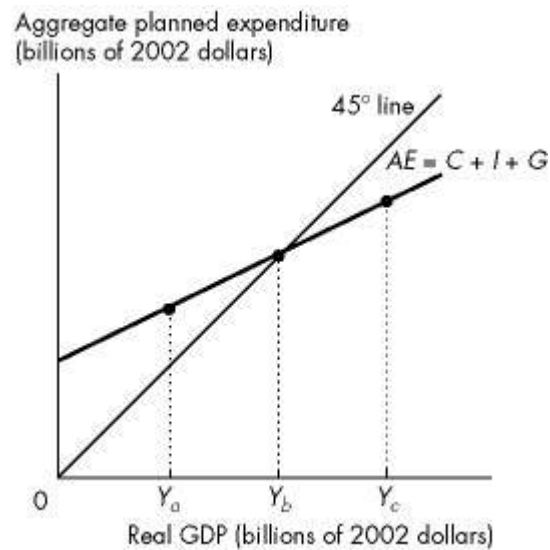
- 5) If real GDP is \$3 billion and aggregate planned expenditure is \$3.5 billion, then inventories
- A) increase and production increases.
  - B) increase and production decreases.
  - C) decrease and production increases.
  - D) decrease and production decreases.
  - E) remain the same and production decreases.

Answer: C

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

Use the figure below to answer the following questions.



**Figure 27.2.1**

There are no exports or imports in this economy.

- 6) Refer to Figure 27.2.1. When real GDP is equal to  $Y_a$ , then
- A) actual expenditure is less than planned expenditure.
  - B) actual expenditure is greater than planned expenditure.
  - C) planned expenditure is equal to actual expenditure.
  - D) the economy is in equilibrium.
  - E) real GDP decreases.

Answer: A

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

7) Refer to Figure 27.2.1. When real GDP is equal to  $Y_b$ , then

- A) actual expenditure is less than planned expenditure.
- B) actual expenditure is greater than planned expenditure.
- C) planned expenditure is equal to actual expenditure.
- D) real GDP increases.
- E) real GDP decreases.

Answer: C

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

8) Refer to Figure 27.2.1. When real GDP is equal to  $Y_c$ , then

- A) actual expenditure is less than planned expenditure.
- B) actual expenditure is greater than planned expenditure.
- C) planned expenditure is equal to actual expenditure.
- D) the economy is in equilibrium.
- E) real GDP increases.

Answer: B

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

9) Refer to Figure 27.2.1. Equilibrium real GDP

- A) is decreasing.
- B) is equal to  $Y_a$ .
- C) is equal to  $Y_b$ .
- D) is equal to  $Y_c$ .
- E) can be any of  $Y_a$ ,  $Y_b$ , or  $Y_c$  depending on what is happening to inventories.

Answer: C

Diff: 1 Type: MC

Topic: Real GDP with a Fixed Price Level

10) Refer to Figure 27.2.1. When real GDP is equal to  $Y_a$ , then aggregate planned expenditure

- A) exceeds real GDP and real GDP increases.
- B) is less than real GDP and real GDP decreases.
- C) exceeds real GDP and real GDP decreases.
- D) is equal to real GDP and real GDP neither increases nor decreases.
- E) is less than real GDP and real GDP increases.

Answer: A

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

11) Refer to Figure 27.2.1. When real GDP is equal to  $Y_b$ , then aggregate planned expenditure is

- A) less than real GDP and real GDP decreases.
- B) less than real GDP and real GDP increases.
- C) greater than real GDP and real GDP increases.
- D) greater than real GDP and real GDP decreases.
- E) equal to real GDP and real GDP neither increases nor decreases.

Answer: E

Diff: 1 Type: MC

Topic: Real GDP with a Fixed Price Level

12) Refer to Figure 27.2.1. When real GDP is equal to  $Y_c$ , then aggregate planned expenditure is

- A) less than real GDP and real GDP decreases.
- B) less than real GDP and real GDP increases.
- C) greater than real GDP and real GDP decreases.
- D) equal to real GDP and real GDP neither increases nor decreases.
- E) greater than real GDP and real GDP increases.

Answer: A

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

Use the figure below to answer the following questions.

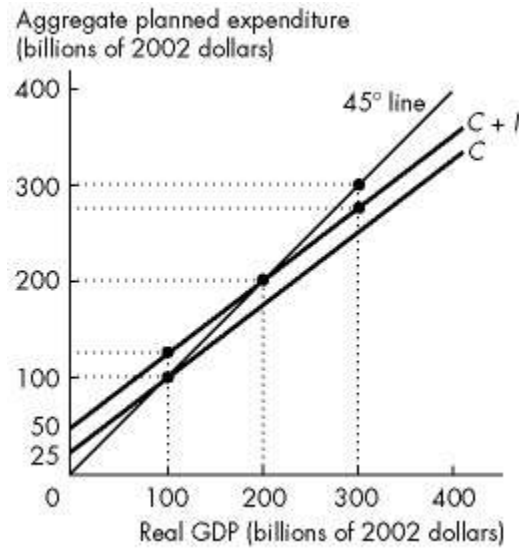


Figure 27.2.2

The economy depicted does *not* engage in international trade and has no government. Planned aggregate expenditure ( $AE$ ) is equal to the sum of consumption expenditure ( $C$ ) and investment ( $I$ ).

13) Refer to Figure 27.2.2. Investment is

- A) \$50 billion.
- B) \$25 billion.
- C) \$75 billion.
- D) \$100 billion.
- E) increasing as real GDP increases.

Answer: B

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

14) Refer to Figure 27.2.2. Equilibrium expenditure is

- A) \$100 billion.
- B) \$300 billion.
- C) \$250 billion.
- D) \$200 billion.
- E) \$400 billion.

Answer: D

Diff: 1 Type: MC

Topic: Real GDP with a Fixed Price Level

- 15) Refer to Figure 27.2.2. When real GDP is to \$300 billion, real GDP
- A) \$25 billion is less than aggregate planned expenditure, and firms decrease production.
  - B) exceeds aggregate planned expenditure by \$25 billion, and firms increase production.
  - C) is the same as aggregate planned expenditure, and firms do not change production.
  - D) exceeds aggregate planned expenditure by \$25 billion, and firms decrease production.
  - E) exceeds aggregate planned expenditure by \$50 billion, and firms increase production.

Answer: D

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

- 16) Refer to Figure 27.2.2. When real GDP is \$100 billion,
- A) real GDP is less than aggregate planned expenditure, and firms increase production.
  - B) aggregate planned expenditure is greater than real GDP, and firms decrease production.
  - C) real GDP is greater than aggregate planned expenditure, and firms decrease production.
  - D) aggregate planned expenditure equals real GDP, and the economy is in equilibrium.
  - E) aggregate planned expenditure is less than real GDP, and firms increase production.

Answer: A

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

- 17) If there is an unplanned decrease in inventories, aggregate planned expenditure is
- A) greater than real GDP, and firms increase production.
  - B) greater than real GDP, and firms decrease production.
  - C) less than real GDP, and firms increase production.
  - D) less than real GDP, and firms decrease production.
  - E) greater than real GDP, and firms increase investment.

Answer: A

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

- 18) If  $AE = 50 + 0.6Y$  and  $Y = 200$ , then unplanned inventories
- A) increase by 75.
  - B) increase by 30.
  - C) decrease by 75.
  - D) decrease by 30.
  - E) do not change and equilibrium exists.

Answer: B

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

Source: Study Guide

19) If  $AE = 100 + 0.7Y$  and  $Y = 300$ , then unplanned inventories

- A) increase by 10.
- B) increase by 200.
- C) decrease by 10.
- D) decrease by 200.
- E) do not change and equilibrium exists.

Answer: C

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

20) A change in consumption, in response to a change in income, is

- A) unplanned consumption.
- B) autonomous consumption.
- C) induced consumption.
- D) equilibrium consumption.
- E) planned consumption.

Answer: C

Diff: 1 Type: MC

Topic: Real GDP with a Fixed Price Level

21) Consumption expenditure minus imports, which varies with real GDP, is

- A) aggregate expenditure.
- B) autonomous expenditure.
- C) planned consumption.
- D) induced expenditure.
- E) unplanned consumption.

Answer: D

Diff: 1 Type: MC

Topic: Real GDP with a Fixed Price Level

22) Equilibrium expenditure occurs when

- A) consumption equals real GDP.
- B) aggregate planned expenditure equals real GDP.
- C) aggregate planned expenditure equals consumption.
- D) induced consumption equals aggregate planned expenditure.
- E) none of the above.

Answer: B

Diff: 1 Type: MC

Topic: Real GDP with a Fixed Price Level

23) Suppose real GDP increases by \$1 billion and, as a result, consumption increases by \$500 million. This change in consumption is

- A) unplanned.
- B) induced.
- C) autonomous.
- D) too little.
- E) planned.

Answer: B

Diff: 1 Type: MC

Topic: Real GDP with a Fixed Price Level

24) Everything else remaining the same, autonomous consumption

- A) increases as disposable income decreases.
- B) increases as disposable income increases.
- C) does not change as disposable income changes.
- D) is usually assumed to be zero.
- E) decreases as disposable income decreases.

Answer: C

Diff: 1 Type: MC

Topic: Real GDP with a Fixed Price Level

25) Which one of the following variables has an induced component?

- A) investment
- B) consumption
- C) exports
- D) government expenditure on goods and services
- E) all of the above

Answer: B

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

26) As real GDP increases

- A) autonomous consumption increases.
- B) planned investment increases.
- C) exports increase.
- D) imports increase.
- E) imports decrease.

Answer: D

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

- 27) As real GDP decreases
- A) induced consumption decreases.
  - B) planned investment increases.
  - C) exports increase.
  - D) imports increase.
  - E) induced consumption increases.

Answer: A

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

- 28) The fact that imports increase as real GDP increases implies that imports are part of
- A) marginal expenditure.
  - B) autonomous expenditure.
  - C) consumption expenditure.
  - D) equilibrium expenditure.
  - E) induced expenditure.

Answer: E

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

- 29) Which one of the following will lead to an increase in the slope of the *AE* function?
- A) an increase in the marginal propensity to import
  - B) an increase in the marginal tax rate
  - C) a decrease in the marginal propensity to consume
  - D) a decrease in the marginal propensity to save
  - E) an increase in the marginal propensity to save

Answer: D

Diff: 3 Type: MC

Topic: Real GDP with a Fixed Price Level

Use the figure below to answer the following questions.

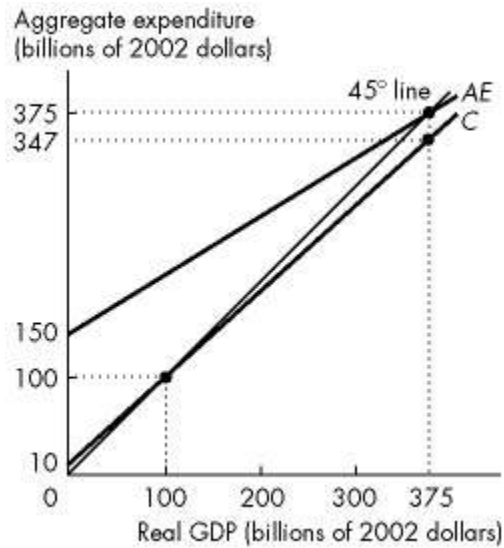


Figure 27.2.3

There are no taxes in this economy.

30) In Figure 27.2.3, the marginal propensity to consume, assuming no income taxes, is

- A) 0.3.
- B) 0.6.
- C) 0.9.
- D) 1.0.
- E) 0.93.

Answer: C

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

Source: Study Guide

31) In Figure 27.2.3, *autonomous* expenditure is

- A) \$10 billion.
- B) \$100 billion.
- C) \$150 billion.
- D) \$347 billion.
- E) \$375 billion.

Answer: C

Diff: 1 Type: MC

Topic: Real GDP with a Fixed Price Level

Source: Study Guide

32) In Figure 27.2.3, equilibrium expenditure is

- A) \$10 billion.
- B) \$100 billion.
- C) \$150 billion.
- D) \$347 billion.
- E) \$375 billion.

Answer: E

Diff: 1 Type: MC

Topic: Real GDP with a Fixed Price Level

Source: Study Guide

33) In Figure 27.2.3, the marginal propensity to import is

- A) 0.
- B) 0.1.
- C) 0.25.
- D) 0.3.
- E) 0.6.

Answer: D

Diff: 2 Type: MC

Topic: Real GDP with a Fixed Price Level

Source: Study Guide

34) In Figure 27.2.3, at the equilibrium level of real GDP, *induced* expenditure is

- A) \$28 billion.
- B) \$150 billion.
- C) \$225 billion.
- D) \$347 billion.
- E) \$375 billion.

Answer: C

Diff: 3 Type: MC

Topic: Real GDP with a Fixed Price Level

Source: Study Guide

Refer to the table below to answer the following question.

**Table 27.2.1**

<i>Y</i> (trillions of dollars)	<i>C</i> (trillions of dollars)	<i>I</i> (trillions of dollars)	<i>G</i> (trillions of dollars)	<i>X</i> (trillions of dollars)	<i>M</i> (trillions of dollars)
1.0	1.00	0.5	0.7	0.45	1.15
2.0	1.65	0.5	0.7	0.45	0.30
3.0	2.30	0.5	0.7	0.45	0.45
4.0	2.95	0.5	0.7	0.45	0.60
5.0	3.60	0.5	0.7	0.45	0.75
6.0	4.25	0.5	0.7	0.45	0.90

35) Table 27.2.1 gives the aggregate expenditure schedule. Equilibrium expenditure is equal to \_\_\_\_\_.

- A) \$4 trillion
- B) \$3 trillion
- C) \$5 trillion
- D) zero
- E) \$2 trillion

Answer: A

Diff: 3 Type: MC

Topic: Real GDP with a Fixed Price Level

Source: MyEconLab

36) If aggregate planned expenditure exceeds real GDP then \_\_\_\_\_.

- A) inventories decrease, and the *AE* curve shifts downward
- B) inventories increase, and the *AE* curve shifts upward
- C) inventories decrease, and as real GDP increases a movement up along the *AE* curve occurs
- D) inventories increase, and as real GDP increases a movement up along the *AE* curve occurs
- E) inventories increase, and the short-run aggregate supply curve shifts rightward

Answer: C

Diff: 3 Type: MC

Topic: Real GDP with a Fixed Price Level

Source: MyEconLab

37) The components of aggregate expenditure that are influenced by real GDP are \_\_\_\_\_.

- A) investment, exports, and imports
- B) consumption expenditure, government expenditure, investment, and imports
- C) consumption expenditure, investment, and imports
- D) consumption expenditure and imports
- E) wages, transfer payments, and government expenditure

Answer: D

Diff: 2 Type: MC

Topic: Fixed Prices and Expenditure Plans

Source: MyEconLab

38) Everything else remaining the same, an increase in the marginal propensity to import \_\_\_\_\_ the slope of the  $AE$  curve and \_\_\_\_\_ equilibrium expenditure.

- A) decreases; increases
- B) increases; increases
- C) decreases; decreases
- D) increases; decreases
- E) does not change; does not change

Answer: C

Type: MC

39) Everything else remaining the same, an increase in the marginal propensity to consume \_\_\_\_\_ the slope of the  $AE$  curve and \_\_\_\_\_ equilibrium expenditure.

- A) decreases; increases
- B) increases; increases
- C) decreases; decreases
- D) increases; decreases
- E) does not change; does not change

Answer: B

Type: MC

### 27.3 The Multiplier

1) If there is a decrease in autonomous expenditure, the new *AE* curve is

- A) flatter than the original *AE* curve.
- B) steeper than the original *AE* curve.
- C) parallel and above the original *AE* curve.
- D) parallel and below the original *AE* curve.
- E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: The Multiplier

2) All else constant, a decrease in the income tax rate will result in

- A) a movement down along the aggregate expenditure curve.
- B) an upward shift of the *AE* curve with no change in its slope.
- C) a downward shift of the *AE* curve with no change in its slope.
- D) a decrease in the consumption expenditure.
- E) an *AE* curve with a steeper slope.

Answer: E

Diff: 2 Type: MC

Topic: The Multiplier

3) Everything else remaining the same, which one of the following would increase equilibrium real GDP?

- A) an increase in saving
- B) an increase in exports
- C) a decrease in investment
- D) an increase in taxes
- E) a decrease in exports

Answer: B

Diff: 2 Type: MC

Topic: The Multiplier

4) The slope of the *AE* curve equals

- A) aggregate expenditure divided by real GDP.
- B) the change in aggregate expenditure divided by the change in real GDP.
- C) the change in consumption divided by the change in real GDP.
- D) the change in consumption plus government expenditure divided by the change in aggregate income.
- E) the change in income divided by the change in autonomous expenditure.

Answer: B

Diff: 2 Type: MC

Topic: The Multiplier

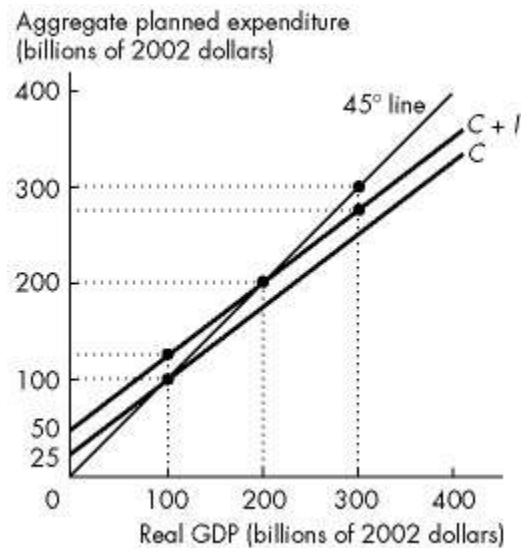
- 5) The aggregate expenditure curve will become steeper if
- A) people become thriftier.
  - B) people show an increased preference for foreign-made products.
  - C) firms expect an increase in future profit.
  - D) income tax rates are lowered.
  - E) income tax rates are raised.

Answer: D

Diff: 2 Type: MC

Topic: The Multiplier

Use the figure below to answer the following question(s).



**Figure 27.3.1**

The economy shown in the graph does not engage in international trade and has no government. Planned aggregate expenditure equals the sum of consumption expenditure ( $C$ ) and investment ( $I$ ).

- 6) Refer to Figure 27.3.1. Autonomous expenditure equals
- A) \$100 billion.
  - B) \$25 billion.
  - C) \$50 billion.
  - D) \$125 billion.
  - E) none of the above.

Answer: C

Diff: 1 Type: MC

Topic: The Multiplier

7) Refer to Figure 27.3.1. The slope of the *AE* curve is

- A) 0.75.
- B) 0.25.
- C) 0.50.
- D) 0.67.
- E) 1.33.

Answer: A

Diff: 2 Type: MC

Topic: The Multiplier

8) Refer to Figure 27.3.1. The multiplier for this economy is

- A) 2.
- B) 4.
- C) 2.5.
- D) 1.
- E) 3.

Answer: B

Diff: 2 Type: MC

Topic: The Multiplier

9) Refer to Figure 27.3.1. At equilibrium induced expenditure equals

- A) \$200 billion.
- B) \$50 billion.
- C) \$25 billion.
- D) \$100 billion.
- E) \$150 billion.

Answer: E

Diff: 2 Type: MC

Topic: The Multiplier

10) Refer to Figure 27.3.1. If investment increases by \$25 billion, then real GDP increases by

- A) \$25 billion.
- B) \$125 billion.
- C) \$50 billion.
- D) \$100 billion.
- E) \$75 billion.

Answer: D

Diff: 2 Type: MC

Topic: The Multiplier

- 11) As the aggregate expenditure curve becomes steeper, the value of the multiplier becomes
- A) equal to the marginal propensity to save.
  - B) larger.
  - C) smaller.
  - D) negative.
  - E) greater than 1.

Answer: B

Diff: 2 Type: MC

Topic: The Multiplier

- 12) The formula for the multiplier in an open economy is
- A)  $1/(1 + \text{slope of the } AE \text{ curve})$ .
  - B)  $1/(1 - \text{marginal propensity to import})$ .
  - C)  $1/(1 + \text{marginal propensity to import})$ .
  - D)  $1/(1 - \text{slope of the } AE \text{ curve})$ .
  - E)  $1/(1 - MPC)$ .

Answer: D

Diff: 2 Type: MC

Topic: The Multiplier

- 13) The multiplier can take on any value
- A) only between zero and 1.
  - B) only between -1 and 1.
  - C) only between 1 and 2.
  - D) only greater than 1.
  - E) greater than zero.

Answer: E

Diff: 3 Type: MC

Topic: The Multiplier

Use the table below to answer the following question(s).

**Table 27.3.1**

The following table shows the relationship between aggregate planned expenditure and real GDP in the hypothetical economy of Econoworld.

Real GDP (billions of 2002 dollars)	Aggregate planned expenditure (billions of 2002 dollars)
0	100
200	260
400	420
600	580
800	740

14) Refer to Table 27.3.1. What is the slope of the *AE* curve?

- A) 0.8
- B) 0.6
- C) 0.75
- D) 1
- E) 1.3

Answer: A

Diff: 2 Type: MC

Topic: The Multiplier

15) Refer to Table 27.3.1. The equilibrium level of real GDP is

- A) \$525 billion.
- B) \$550 billion.
- C) \$450 billion
- D) \$500 billion
- E) none of the above.

Answer: D

Diff: 2 Type: MC

Topic: The Multiplier

16) Refer to Table 27.3.1. Autonomous expenditure is

- A) \$100 billion.
- B) \$125 billion.
- C) \$50 billion.
- D) \$500 billion.
- E) zero.

Answer: A

Diff: 1 Type: MC

Topic: The Multiplier

17) Refer to Table 27.3.1. The multiplier

- A) is 5.
- B) is 2.5.
- C) is 4.
- D) is 1.8.
- E) cannot be determined without more information.

Answer: A

Diff: 2 Type: MC

Topic: The Multiplier

18) Refer to Table 27.3.1. If investment increases by \$25 billion, the real GDP becomes

- A) \$525 billion.
- B) \$625 billion.
- C) \$725 billion.
- D) \$600 billion.
- E) \$675 billion.

Answer: B

Diff: 2 Type: MC

Topic: The Multiplier

19) An increase in autonomous expenditure shifts the *AE* curve

- A) upward but leaves its slope unchanged.
- B) upward and the curve becomes steeper.
- C) downward but leaves its slope unchanged.
- D) downward and the curve becomes steeper.
- E) upward and the curve becomes less steep.

Answer: A

Diff: 2 Type: MC

Topic: The Multiplier

Use the figure below to answer the following question.

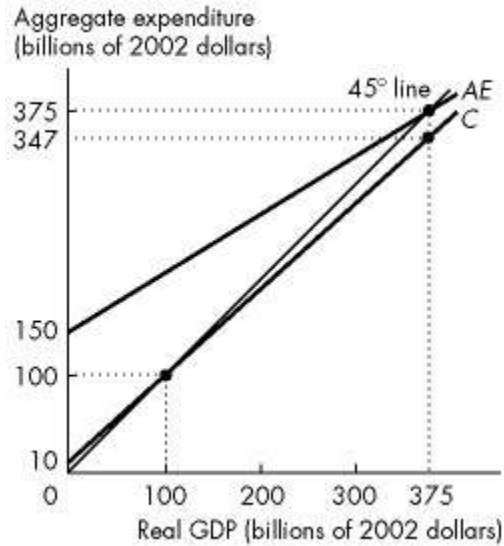


Figure 27.3.2

20) In Figure 27.3.2, the multiplier is

- A) 0.25.
- B) 1.00.
- C) 1.60.
- D) 2.50.
- E) 10.

Answer: D

Diff: 2 Type: MC

Topic: The Multiplier

Source: Study Guide

21) In a recent study, the University of Underfunded argued that it created four times as many jobs as people that it hired directly. This argument illustrates the idea

- A) of the marginal propensity to consume.
- B) of the multiplier.
- C) of government spending.
- D) of the tax multiplier.
- E) that universities are wasting taxpayers' dollars.

Answer: B

Diff: 2 Type: MC

Topic: The Multiplier

- 22) If investment increases by \$200, and as a result income increases by \$800, then the
- A) multiplier is  $1/4$ .
  - B) slope of the *AE* curve is 0.75.
  - C) slope of the *AE* curve is  $1/4$ .
  - D) multiplier is 3.
  - E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: The Multiplier

- 23) Which of the following quotations illustrates the idea of the multiplier?
- A) "The new stadium will generate \$200 million in spinoff spending."
  - B) "Higher expected profits are leading to higher investment spending by business, and will lead to higher consumer spending."
  - C) "The projected cuts in government jobs will hurt the local retail industry."
  - D) "Taking the grain elevator out of our small town will destroy 300 jobs."
  - E) all of the above

Answer: E

Diff: 2 Type: MC

Topic: The Multiplier

Source: Study Guide

- 24) Which of the following quotations illustrates an increase in aggregate expenditure?
- A) "The new stadium will generate \$200 million in spin off spending."
  - B) "Higher expected profits are leading to higher investment spending by business, and will lead to higher consumer spending."
  - C) "The projected cuts in government jobs will hurt the local retail industry."
  - D) "Taking the grain elevator out of our small town will destroy 300 jobs."
  - E) Both A and B.

Answer: E

Diff: 2 Type: MC

Topic: The Multiplier

- 25) Which of the following quotations illustrates a decrease in aggregate expenditure?
- A) "The new stadium will generate \$200 million in spin off spending."
  - B) "Higher expected profits are leading to higher investment spending by business, and will lead to higher consumer spending."
  - C) "The projected cuts in government jobs will hurt the local retail industry."
  - D) "Taking the grain elevator out of our small town will destroy 300 jobs."
  - E) Both C and D.

Answer: E

Diff: 2 Type: MC

Topic: The Multiplier

26) You observe that unplanned inventories are increasing. You predict that there will be \_\_\_\_\_.

- A) a trough
- B) a business cycle
- C) a recession
- D) an expansion
- E) a collapse of the stock market

Answer: C

Diff: 2 Type: MC

Topic: The Multiplier

Source: MyEconLab

27) A decrease in the marginal propensity to import \_\_\_\_\_, everything else remaining the same.

- A) makes the multiplier larger
- B) makes the multiplier smaller
- C) has no effect on the multiplier
- D) sometimes increases the multiplier and sometimes decreases the multiplier
- E) increases the marginal propensity to consume

Answer: A

Diff: 2 Type: MC

Topic: The Multiplier

Source: MyEconLab

28) The multiplier shows that as \_\_\_\_\_ expenditure changes, real GDP changes by \_\_\_\_\_ amount.

- A) autonomous; an even larger
- B) autonomous; the same
- C) induced; the same
- D) induced; an even larger
- E) induced; a smaller

Answer: A

Type: MC

29) The multiplier is greater than 1 because a change in autonomous expenditure leads to \_\_\_\_\_.

- A) more investment
- B) more induced expenditure
- C) move saving
- D) more exports
- E) even more autonomous expenditure

Answer: B

Type: MC

## 27.4 The Multiplier and the Price Level

1) An increase in the price level

- A) shifts the *AE* curve upward and increases equilibrium expenditure.
- B) shifts the *AE* curve upward and decreases equilibrium expenditure.
- C) shifts the *AE* curve downward and increases equilibrium expenditure.
- D) shifts the *AE* curve downward and decreases equilibrium expenditure.
- E) has no impact on the *AE* curve.

Answer: D

Diff: 2 Type: MC

Topic: The Multiplier and the Price Level

Source: Study Guide

2) A decrease in the price level

- A) increases aggregate expenditure and produces a movement along the aggregate demand curve.
- B) increases aggregate expenditure and produces a rightward shift of the aggregate demand curve.
- C) increases aggregate expenditure and produces a leftward shift of the aggregate demand curve.
- D) has no effect on aggregate expenditure.
- E) increases aggregate expenditure, but has no effect on the aggregate demand curve.

Answer: A

Diff: 2 Type: MC

Topic: The Multiplier and the Price Level

Source: Study Guide

3) A rise in the price level

- A) decreases aggregate expenditure and produces a movement along the aggregate demand curve.
- B) decreases aggregate expenditure and produces a rightward shift of the aggregate demand curve.
- C) decreases aggregate expenditure and produces a leftward shift of the aggregate demand curve.
- D) has no effect on aggregate expenditure.
- E) increases aggregate expenditure, but has no effect on the aggregate demand curve.

Answer: A

Diff: 2 Type: MC

Topic: The Multiplier and the Price Level

- 4) The aggregate expenditure curve and the aggregate demand curve are
- A) not related at all.
  - B) the same curve, just with different names.
  - C) linked because if the price level rises, the aggregate expenditure curve shifts downward, and the aggregate demand curve shifts leftward.
  - D) linked because if the price level rises, the aggregate expenditure curve shifts downward, and there is a movement up along the aggregate demand curve.
  - E) linked because if the price level rises, the aggregate expenditure curve shifts downward, and there is a movement down along the aggregate demand curve.

Answer: D

Diff: 2 Type: MC

Topic: The Multiplier and the Price Level

- 5) A shift in the aggregate expenditure curve as a result of a rise in the price level,
- A) shifts the aggregate demand curve leftward.
  - B) has no effect on the aggregate demand curve.
  - C) shifts the aggregate demand curve rightward.
  - D) creates a movement down along the aggregate demand curve.
  - E) creates a movement up along the aggregate demand curve.

Answer: E

Diff: 2 Type: MC

Topic: The Multiplier and the Price Level

- 6) Suppose that investment increases by \$10 billion. If the multiplier is 2, the *AD* curve
- A) shifts rightward by the horizontal distance \$20 billion.
  - B) shifts rightward by a horizontal distance greater than \$20 billion.
  - C) shifts rightward by a horizontal distance less than \$20 billion.
  - D) is not affected.
  - E) shifts upward by a vertical distance equal to \$20 billion.

Answer: A

Diff: 2 Type: MC

Topic: The Multiplier and the Price Level

Source: Study Guide

- 7) Suppose that investment decreases by \$15 billion. If the multiplier is 2.5, the aggregate demand curve
- A) shifts leftward by a horizontal distance of \$37.5 billion.
  - B) shifts leftward by a horizontal distance greater than \$37.5 billion.
  - C) shifts leftward by a horizontal distance less than \$37.5 billion.
  - D) shifts upward by a vertical distance of \$37.5 billion.
  - E) is not affected.

Answer: A

Diff: 2 Type: MC

Topic: The Multiplier and the Price Level

8) Suppose the multiplier is 2 and the short-run aggregate supply curve is positively sloped. Investment increases by \$10 billion. In the short run, equilibrium real GDP

- A) increases by \$20 billion.
- B) increases by more than \$20 billion.
- C) decreases by less than \$20 billion.
- D) does not change.
- E) increases by less than \$20 billion.

Answer: E

Diff: 2 Type: MC

Topic: The Multiplier and the Price Level

Source: Study Guide

9) Suppose the multiplier is 2.5 and investment increases by \$20 billion. Starting at potential GDP, in the long run, equilibrium real GDP

- A) increases by \$50 billion.
- B) increases by more than \$50 billion.
- C) decreases by less than \$50 billion.
- D) does not change.
- E) increases by less than \$50 billion.

Answer: D

Diff: 2 Type: MC

Topic: The Multiplier and the Price Level

Source: Study Guide

10) Suppose that investment decreases by \$15 billion. If the multiplier is 2, and the short-run aggregate supply curve is positively sloped. In the short run, equilibrium real GDP

- A) decreases by \$30 billion.
- B) decreases by more than \$30 billion.
- C) decreases by less than \$30 billion.
- D) increases by less than \$30 billion.
- E) does not change.

Answer: C

Diff: 2 Type: MC

Topic: The Multiplier and the Price Level

11) Suppose that investment increases by \$10 billion. Which one of the following would reduce the effect of this increase in autonomous expenditure on equilibrium real GDP in the short run?

- A) an increase in the marginal propensity to consume.
- B) a decrease in the marginal propensity to import
- C) a decrease in the marginal tax rate
- D) a steeper short-run aggregate supply curve
- E) a flatter short-run aggregate supply curve

Answer: D

Diff: 2 Type: MC

Topic: The Multiplier and the Price Level

12) Everything else remaining the same, if aggregate demand changes, the amount by which the AD curve shifts depends on

- A) the change in aggregate supply.
- B) the change in autonomous expenditure and the multiplier.
- C) changes in induced expenditure.
- D) the change in the price level.
- E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: The Multiplier and the Price Level

13) Suppose there is an increase in exports. Assuming the price level is held constant, which one of the following best describes the sequence of changes in the economy?

- A) Autonomous expenditure increases, induced expenditure increases, real GDP increases, and the price level rises.
- B) Induced expenditure increases, autonomous expenditure increases, real GDP increases, and consumption increases.
- C) Induced expenditure increases, real GDP increases, autonomous expenditure increases, and the price level increases, lowering autonomous expenditure and real GDP increases by a smaller amount.
- D) Induced expenditure increases, real GDP increases, autonomous expenditure increases, real GDP increases more, autonomous expenditure increases again, etc.
- E) Autonomous expenditure increases, real GDP increases, induced expenditure increases, real GDP increases more, induced expenditure increases again, and the process continues until equilibrium expenditure is reached.

Answer: E

Diff: 2 Type: MC

Topic: The Multiplier and the Price Level

14) In the long run, the multiplier

- A) has a larger effect on real GDP than it has in the short run, because the multiplier effect has a longer time period to exert its impact on the economy.
- B) has a larger effect on real GDP than it has in the short run, because there are more induced expenditures in the long run.
- C) has a larger effect on real GDP than it has in the short run because of changes in the price level.
- D) has a smaller effect on real GDP than it has in the short run because of changes in the price level.
- E) can have a smaller or larger effect on real GDP than it has in the short run.

Answer: D

Diff: 3 Type: MC

Topic: The Multiplier and the Price Level

- 15) The difference in the influence of a multiplier between the short run and the long run, is that
- A) the multiplier effect is larger in the long run.
  - B) the multiplier effect is zero in the long run.
  - C) the multiplier effect is zero in the short run.
  - D) there is no multiplier effect in the short run.
  - E) the multiplier effect depends on potential GDP in the long run.

Answer: B

Diff: 2 Type: MC

Topic: The Multiplier and the Price Level

- 16) A rise in the price level \_\_\_\_\_.

- A) shifts the *AD* curve rightward and brings a movement up along the *AE* curve
- B) shifts the *AE* curve upward and brings a movement down along the *AD* curve
- C) shifts the *AE* curve downward and brings a movement up along the *AD* curve
- D) shifts the *AD* curve leftward and brings a movement down along the *AE* curve
- E) shifts the *AE* curve downward and shifts the *AD* curve rightward

Answer: C

Diff: 2 Type: MC

Topic: The Multiplier and the Price Level

Source: MyEconLab

- 17) An increase in investment shifts the *AE* curve upward by an amount equal to the \_\_\_\_\_, and shifts the *AD* curve rightward by an amount equal to the \_\_\_\_\_.

- A) change in investment; change in investment times the multiplier
- B) change in investment times the multiplier; change in investment times the multiplier
- C) change in investment times the multiplier; change in investment
- D) change in investment; change in investment
- E) change in investment divided by the multiplier; change in investment

Answer: A

Diff: 2 Type: MC

Topic: The Multiplier and the Price Level

Source: MyEconLab

- 18) The larger the multiplier, the \_\_\_\_\_ the *AE* curve and the \_\_\_\_\_ the *AD* curve from a given increase in investment.

- A) steeper; greater the rightward shift of
- B) steeper; greater the movement upward along
- C) flatter; greater the rightward shift of
- D) flatter; greater the movement upward along
- E) steeper; greater the movement downward along

Answer: A

Type: MC

19) Which of the following events shifts the aggregate expenditure curve and also shifts the aggregate demand curve?

I. a decrease in investment

II. a change in the price level

III. an increase in exports

A) I and II

B) I and III

C) II and III

D) I, II, and III

E) all of the above

Answer: B

Type: MC

## 27.5 Mathematical Note: The Algebra of the Keynesian Model

Use the information below to answer the following question.

### Fact 27.5.1

The economy of Beverly Hills has a consumption function of  $C = 10 + 0.8Y$ , investment equal to 6, government expenditure equal to 10, exports equal to 10, and an import function of  $M = 0.1Y$ .

1) Refer to Fact 27.5.1. What is the equation for the aggregate expenditure curve for this economy?

- A)  $AE = 16 + 0.7Y$
- B)  $AE = 36 - 0.7Y$
- C)  $AE = 26 + 0.8Y$
- D)  $AE = 36 + 0.9Y$
- E)  $AE = 36 + 0.7Y$

Answer: E

Diff: 2 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

Source: Study Guide

2) Refer to Fact 27.5.1. What is equilibrium real GDP in this economy?

- A) 36
- B) 120
- C) 130
- D) 360
- E) none of the above

Answer: B

Diff: 3 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

Source: Study Guide

3) Refer to Fact 27.5.1. What is consumption expenditure in equilibrium in this economy?

- A) 298
- B) 106
- C) 38.8
- D) 114
- E) none of the above

Answer: B

Diff: 3 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

4) Refer to Fact 27.5.1. What is the multiplier for this economy?

- A) 1.43
- B) 3.33
- C) 0.3
- D) 10
- E) 5

Answer: B

Diff: 2 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

5) Refer to Fact 27.5.1. If autonomous consumption increases by 10, what is the new equation of the aggregate expenditure function for this economy?

- A)  $AE = 26 + 0.7Y$
- B)  $AE = 36 + 0.7Y$
- C)  $AE = 46 + 0.7Y$
- D)  $AE = 46 + 0.8Y$
- E)  $AE = 46 + 0.9Y$

Answer: C

Diff: 2 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

6) Refer to Fact 27.5.1. If autonomous consumption increases by 10, what is the new equilibrium real GDP for this economy?

- A) 153.33
- B) 120
- C) 86.67
- D) 460
- E) 230

Answer: A

Diff: 3 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

Use the information below to answer the following questions.

**Fact 27.5.2**

The economy of Tinseltown has a consumption function of  $C = 15 + 0.7Y$ , investment equal to 8, government expenditure equal to 12, exports equal to 20, and an import function of  $M = 0.2Y$ .

7) Refer to Fact 27.5.2. What is the equation for the aggregate expenditure curve for this economy?

- A)  $AE = 35 + 0.5Y$
- B)  $AE = 55 + 0.7Y$
- C)  $AE = 55 + 0.9Y$
- D)  $AE = 45 - 0.5Y$
- E)  $AE = 55 + 0.5Y$

Answer: E

Diff: 2 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

8) Refer to Fact 27.5.2. What is equilibrium real GDP for this economy?

- A) 110
- B) 55
- C) 27.5
- D) 70
- E) 550

Answer: A

Diff: 3 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

9) Refer to Fact 27.5.2. What is consumption expenditure in equilibrium in this economy?

- A) 35.25
- B) 62
- C) 53.5
- D) 77
- E) 92

Answer: E

Diff: 3 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

10) Refer to Fact 27.5.2. What is the multiplier for this economy?

- A) 0.5
- B) 3.33
- C) 10
- D) 2
- E) 1

Answer: D

Diff: 2 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

Use the figure below to answer the following question.

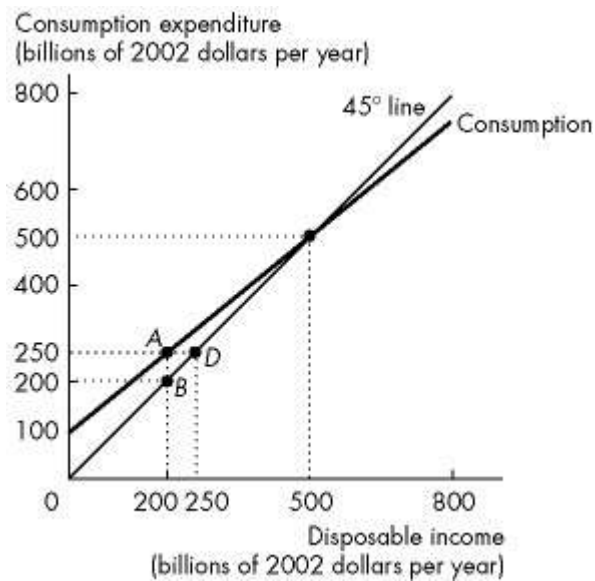


Figure 27.5.1

This figure describes the relationship between consumption expenditure and disposable income.

11) Refer to Figure 27.5.1. The equation of the consumption function is

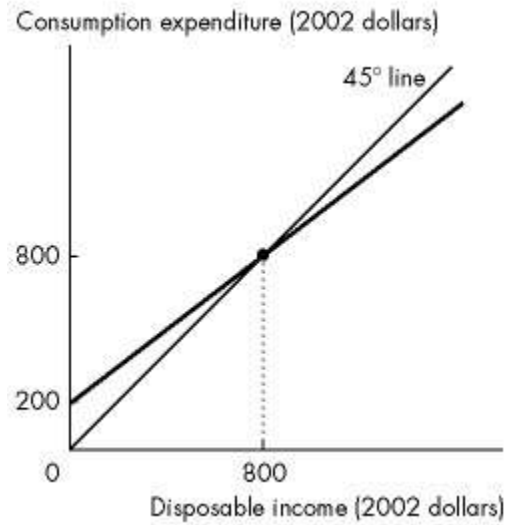
- A)  $C = 100 + 0.8Y$ .
- B)  $C = 100 + 0.8YD$ .
- C)  $C = 100 + 0.2YD$ .
- D)  $C = 100 + 0.6YD$ .
- E)  $C = 500 + 0.8YD$ .

Answer: B

Diff: 2 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

Use the figure below to answer the following questions.



**Figure 27.5.2**

12) Refer to Figure 27.5.2. The equation of the consumption function is

- A)  $C = 200 + 0.8YD$ .
- B)  $C = 200 + 800YD$ .
- C)  $C = 200 + 0.75YD$ .
- D)  $C = 200 + 0.25YD$ .
- E)  $C = 200 + 200YD$ .

Answer: C

Diff: 2 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

13) Refer to Figure 27.5.2. The equation of the saving function that corresponds to the consumption function in this figure is

- A)  $S = 200 + 0.8YD$ .
- B)  $S = -200 + 0.8YD$ .
- C)  $S = 200 + 0.75YD$ .
- D)  $S = -200 + 0.75YD$ .
- E)  $S = -200 + 0.25YD$ .

Answer: E

Diff: 2 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

14) If the saving function is  $S = -25 + 0.4YD$ , then the consumption function is

- A)  $C = 25 + 0.6Y$ .
- B)  $C = -25 + 0.4YD$ .
- C)  $C = 25 - 0.4YD$ .
- D)  $C = 25 + 0.6YD$ .
- E)  $C = 25 + 0.4YD$ .

Answer: D

Diff: 2 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

15) If the saving function is  $S = -25 + 0.4YD$ , then autonomous consumption is

- A) 25.
- B) -25.
- C) 15.
- D) 10.
- E) 0.6.

Answer: A

Diff: 2 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

16) Autonomous consumption is 50. With every increase of one dollar in disposable income, consumption increases 60 cents. The marginal tax rate is 10 percent. The equation of the consumption function is

- A)  $C = 50 + 0.6Y$ .
- B)  $C = 50 + 0.54YD$ .
- C)  $C = 50 + 0.5YD$ .
- D)  $C = 50 + 0.06Y$ .
- E)  $C = 50 + 0.54Y$ .

Answer: E

Diff: 3 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

17) The slope of the aggregate planned expenditure curve is equal to

- A)  $[b(1 - t) - m]$ .
- B) the marginal propensity to consume.
- C) the marginal propensity to import.
- D) 1 minus the marginal propensity to import.
- E) the autonomous expenditure multiplier.

Answer: A

Diff: 2 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

18) You are given the following information about the Canadian economy. Autonomous consumption expenditure is \$50 billion, investment is \$200 billion, and government expenditure is \$250 billion. The marginal propensity to consume is 0.7 and net taxes are \$250 billion. Net taxes are assumed to be constant and not vary with income. Exports are \$500 billion and imports are \$450 billion.

The consumption function in billions of dollars is \_\_\_\_\_.

- A)  $C = 50 + 0.7Y$
- B)  $C = 0.7(Y - 250)$
- C)  $C = 50 + 0.7(Y - 250)$
- D)  $C = 50 + 0.7(YD - 250)$
- E)  $C = 50 + 0.7Y - 250$

Answer: C

Diff: 2 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

Source: MyEconLab

19) You are given the following information about the Canadian economy. Autonomous consumption expenditure is \$50 billion, investment is \$200 billion, and government expenditure is \$250 billion. The marginal propensity to consume is 0.7 and net taxes are \$250 billion. Net taxes are assumed to be constant and not vary with income. Exports are \$500 billion and imports are \$450 billion.

The equation of the  $AE$  curve in billions of dollars is \_\_\_\_\_. Equilibrium expenditure is \_\_\_\_\_.

- A)  $AE = 0.7 + 375Y$ ; \$1,250 billion
- B)  $AE = 0.7Y + 300$ ; \$1,000 billion
- C)  $AE = 0.7Y + 1,275$ ; \$4,250 billion
- D)  $AE = 0.7Y + 375$ ; \$1,250 billion
- E)  $AE = 0.7Y + 375$ ; \$536 billion

Answer: D

Diff: 2 Type: MC

Topic: Mathematical Note: The Algebra of the Keynesian Model

Source: MyEconLab

20) In an economy, autonomous spending is \$20 trillion and the slope of the  $AE$  curve is 0.8. The equation of the  $AE$  curve is \_\_\_\_\_.

- A)  $AE = 0.2Y - 20$
- B)  $AE = 20 + 0.2 Y$
- C)  $AE = 20 + 0.8 Y$
- D)  $AE = 0.8 Y - 20$
- E)  $AE = 20 - 0.8 Y$

Answer: C

Type: MC

21) In an economy, autonomous spending is \$20 trillion and the slope of the *AE* curve is 0.8. Equilibrium expenditure is \_\_\_\_\_. With a fixed price level, the multiplier is \_\_\_\_\_.

- A) \$25 trillion; 1.25
- B) \$100 trillion; 1.25
- C) \$25 trillion; 5
- D) \$20 trillion; 4
- E) \$100 trillion; 5

Answer: E

Type: MC

## Chapter 28 Canadian Inflation, Unemployment, and Business Cycle

### 28.1 Inflation Cycles

1) Which of the following would cause the aggregate demand curve to keep shifting rightward year after year?

- A) a one-time tax cut
- B) a one-time increase in government expenditures on goods and services
- C) inflation
- D) excess wage demands
- E) a persistent increase in the quantity of money

Answer: E

Diff: 2 Type: MC

Topic: Inflation Cycles

Source: Study Guide

2) At full employment an increase in the quantity of money (*ceteris paribus*) can create a

- A) demand-pull inflation, as can an increase in government expenditure.
- B) demand-pull inflation, but an increase in government expenditure cannot.
- C) cost-push inflation, as can an increase in government expenditure.
- D) cost-push inflation, but an increase in government expenditure cannot.
- E) demand-pull and a cost-push inflation, as can an increase in government expenditure.

Answer: A

Diff: 2 Type: MC

Topic: Inflation Cycles

3) Demand-pull inflation occurs when

- A) aggregate demand increases.
- B) aggregate supply decreases.
- C) input costs rise.
- D) people incorrectly forecast inflation.
- E) unemployment is above the natural rate.

Answer: A

Diff: 1 Type: MC

Topic: Inflation Cycles

Source: Study Guide

4) Inflation resulting from an increase in aggregate demand is called

- A) cost-push inflation.
- B) demand-pull inflation.
- C) anticipated inflation.
- D) unanticipated inflation.
- E) political inflation.

Answer: B

Diff: 1 Type: MC

Topic: Inflation Cycles

- 5) Which one of the following can create a demand-pull inflation?
- A) a sharp increase in the price of oil
  - B) higher wages negotiated by unions
  - C) a cut in the interest rate
  - D) a decrease in investment as a result of a decrease in expected future profits
  - E) a decrease in government expenditure on goods and services

Answer: C

Diff: 2 Type: MC

Topic: Inflation Cycles

- 6) Stagflation occurs when the economy experiences both
- A) rising inflation and increasing real GDP.
  - B) falling inflation and decreasing real GDP.
  - C) rising inflation and decreasing real GDP.
  - D) falling inflation and increasing real GDP.
  - E) low exports and low imports.

Answer: C

Diff: 1 Type: MC

Topic: Inflation Cycles

- 7) Suppose the economy is in long-run equilibrium when the price of oil rises. Which one of the following is not a short-run effect of this situation?

- A) an increase in real GDP above long-run real GDP
- B) an increase in the price level
- C) a decrease in real GDP
- D) an increase in unemployment
- E) a decrease in consumer spending

Answer: A

Diff: 2 Type: MC

Topic: Inflation Cycles

- 8) Suppose OPEC unexpectedly collapses, which leads to a fall in the price of oil. As a result, the price level

- A) rises, and real GDP increases.
- B) rises, and real GDP decreases.
- C) falls, and real GDP increases.
- D) falls, and real GDP decreases.
- E) rises, and real GDP remains the same.

Answer: C

Diff: 1 Type: MC

Topic: Inflation Cycles

- 9) An increase in the price level due to an increase in the price of oil
- A) creates stagflation in the short-run and *will* trigger a cost-push inflation.
  - B) creates stagflation in the short-run and *may* trigger off a cost-push inflation.
  - C) increases output above potential GDP.
  - D) leads to an increase in the money wage rate.
  - E) leads to a decrease in the money wage rate.

Answer: B

Diff: 2 Type: MC

Topic: Inflation Cycles

Source: Study Guide

- 10) Cost-push inflation can result from an initial
- A) decrease in personal income taxes.
  - B) increase in personal income taxes.
  - C) increase in government expenditure.
  - D) increase in the money wage rate.
  - E) increase in transfer payments.

Answer: D

Diff: 1 Type: MC

Topic: Inflation Cycles

- 11) Stagflation can result from
- A) a leftward shift of the demand curve.
  - B) a rightward shift of the demand curve.
  - C) a leftward shift of the short-run aggregate supply curve.
  - D) a rightward shift of the short-run aggregate supply curve.
  - E) a rightward shift of the long-run aggregate supply curve.

Answer: C

Diff: 1 Type: MC

Topic: Inflation Cycles

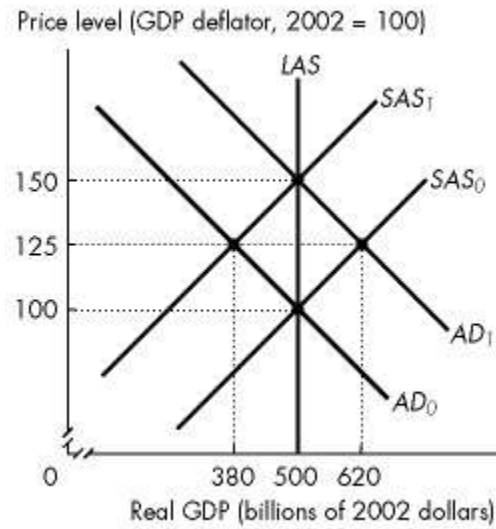
- 12) A cost-price inflation spiral results if the policy response to stagflation is to keep
- A) decreasing aggregate demand.
  - B) decreasing short-run aggregate supply.
  - C) increasing aggregate demand.
  - D) increasing short-run aggregate supply.
  - E) doing nothing.

Answer: C

Diff: 2 Type: MC

Topic: Inflation Cycles

Use the figure below to answer the following question.



**Figure 28.1.1**

13) Refer to Figure 28.1.1. The figure illustrates an economy initially in equilibrium at the intersection of the  $SAS_0$  curve and the  $AD_0$  curve. Which of the following shifts the short-run aggregate supply curve from  $SAS_0$  to  $SAS_1$ ?

- A) an increase in the price of oil
- B) an increase in the price level
- C) an increase in the marginal product of labour
- D) an increase in the demand for money
- E) a decrease in the money wage rate

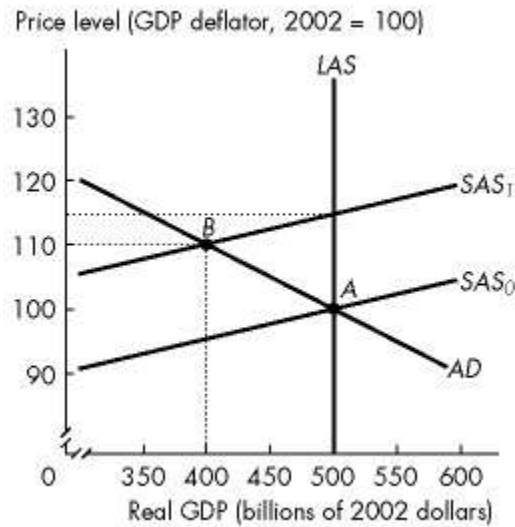
Answer: A

Diff: 2 Type: MC

Topic: Inflation Cycles

Source: Study Guide

Use the figure below to answer the following questions.



**Figure 28.1.2**

14) Refer to Figure 28.1.2. The economy is in long-run equilibrium. If the short-run aggregate supply curve shifts leftward from  $SAS_0$  to  $SAS_1$ , *ceteris paribus*, then people expected

- A) a 10 percent inflation.
- B) the price level to rise to 110.
- C) the real wage rate to fall by 10 percent.
- D) a real GDP decrease of \$50 billion.
- E) a 15 percent inflation.

Answer: E

Diff: 2 Type: MC

Topic: Inflation Cycles

15) Refer to Figure 28.1.2. The economy is in long-run equilibrium. If the short-run aggregate supply curve shifts leftward from  $SAS_0$  to  $SAS_1$ , *ceteris paribus*, then the actual inflation rate

- A) is greater than the expected inflation rate.
- B) is less than the expected inflation rate.
- C) is the same as the expected inflation rate.
- D) cannot be determined without more information.
- E) depends on what happens to wage settlements.

Answer: B

Diff: 3 Type: MC

Topic: Inflation Cycles

16) Refer to Figure 28.1.2. The vertical distance between  $SAS_0$  and  $SAS_1$  represents the

- A) actual inflation rate.
- B) expected increase in real GDP.
- C) actual decrease in real GDP.
- D) expected inflation rate.
- E) expected decrease in the real wage rate.

Answer: D

Diff: 2 Type: MC

Topic: Inflation Cycles

17) Refer to Figure 28.1.2. If the short-run aggregate supply curve does not shift, and remains at  $SAS_0$ , then the expected inflation rate is

- A) zero.
- B) 10 percent.
- C) 15 percent.
- D) 5 percent.
- E) -10 percent.

Answer: A

Diff: 2 Type: MC

Topic: Inflation Cycles

18) Refer to Figure 28.1.2. If  $SAS$  shifts from  $SAS_0$  to  $SAS_1$ , then

- A) inflation is expected to be 10 percent.
- B) inflation will be 10 percent.
- C) a recession will occur.
- D) unemployment will fall.
- E) B and C.

Answer: E

Diff: 2 Type: MC

Topic: Inflation Cycles

19) Refer to Figure 28.1.2. Consider the market for labour as the short-run aggregate supply curve shifts leftward from  $SAS_0$  to  $SAS_1$ . This shift could have been the result of an agreement between workers and employers for a

- A) 10 percent decrease in the money wage rate.
- B) 10 percent increase in the money wage rate.
- C) 15 percent decrease in the money wage rate.
- D) 15 percent increase in the money wage rate.
- E) 10 percent increase in the real wage rate.

Answer: D

Diff: 2 Type: MC

Topic: Inflation Cycles

20) Refer to Figure 28.1.2. Complete the following sentence. The figure illustrates

- A) cost-push inflation.
- B) demand-pull inflation.
- C) a cost-push inflation spiral.
- D) a one time rise in the price level.
- E) A and C are both correct.

Answer: D

Diff: 1 Type: MC

Topic: Inflation Cycles

21) A forecast based on all the relevant information is

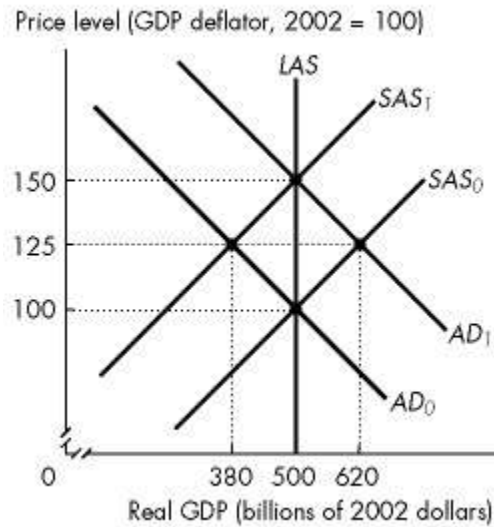
- A) an adaptive expectation.
- B) a future expectation.
- C) a rational expectation.
- D) always a correct expectation.
- E) a perfect forecast.

Answer: C

Diff: 2 Type: MC

Topic: Inflation Cycles

Use the figure below to answer the following questions.



**Figure 28.1.3**

22) Refer to Figure 28.1.3. Assume that the figure illustrates an economy initially in equilibrium at the intersection of the  $SAS_0$  curve and the  $AD_0$  curve. If the aggregate demand curve is correctly expected to shift to  $AD_1$ , new equilibrium real GDP is \_\_\_\_\_ and the new equilibrium price level is \_\_\_\_\_.

- A) \$380 billion; 125
- B) \$500 billion; 150
- C) \$500 billion; 100
- D) \$620 billion; 125
- E) \$500 billion; 125

Answer: B

Diff: 2 Type: MC

Topic: Inflation Cycles

Source: Study Guide

23) Refer to Figure 28.1.3. Assume that the figure illustrates an economy initially in equilibrium at the intersection of the  $SAS_0$  curve and the  $AD_0$  curve. If the aggregate demand curve is expected to shift to  $AD_1$  but remains at  $AD_0$ , the new equilibrium real GDP is \_\_\_\_\_ and the new equilibrium price level is \_\_\_\_\_.

- A) \$380 billion; 100
- B) \$500 billion; 150
- C) \$500 billion; 100
- D) \$620 billion; 125
- E) \$380 billion; 125

Answer: E

Diff: 3 Type: MC

Topic: Inflation Cycles

Source: Study Guide

24) Refer to Figure 28.1.3. Assume that the figure illustrates an economy initially in equilibrium at the intersection of the  $SAS_0$  curve and the  $AD_0$  curve. If the aggregate demand curve is expected to remain at  $AD_0$  but shifts to  $AD_1$ , the new equilibrium real GDP is \_\_\_\_\_ and the new equilibrium price level is \_\_\_\_\_.

- A) \$380 billion; 125
- B) \$500 billion; 150
- C) \$500 billion; 100
- D) \$620 billion; 125
- E) \$500 billion; 125

Answer: D

Diff: 3 Type: MC

Topic: Inflation Cycles

Source: Study Guide

Use the figure below to answer the following question.

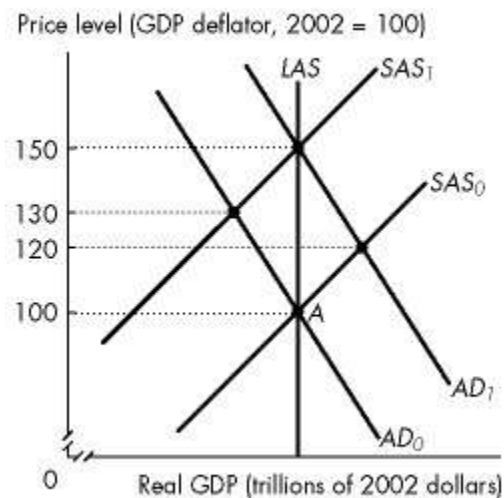


Figure 28.1.4

25) Refer to Figure 28.1.4. The figure illustrates an economy initially in equilibrium at point A. If the quantity of money is expected to increase by 50 percent, what is the rational expectation of the price level?

- A) 100
- B) 120
- C) 130
- D) 150
- E) We cannot tell without more information on wage negotiations.

Answer: D

Diff: 2 Type: MC

Topic: Inflation Cycles

26) A correctly anticipated increase in the quantity of money, in an economy with an unchanging long-run aggregate supply, will result in

- A) a rise in the price level and an increase in real GDP.
- B) a rise in the price level and a decrease in real GDP.
- C) a proportional rise in the price level and no change in real GDP.
- D) no change in the price level and an increase in real GDP.
- E) no change in the price level and no change in real GDP.

Answer: C

Diff: 3 Type: MC

Topic: Inflation Cycles

27) Suppose the quantity of money is expected to remain unchanged but it actually increases. The price level

- A) rises and real GDP increases.
- B) rises and real GDP decreases.
- C) falls and real GDP increases.
- D) falls and real GDP decreases.
- E) rises and real GDP stays the same.

Answer: A

Diff: 2 Type: MC

Topic: Inflation Cycles

28) An economy is in long-run equilibrium when aggregate supply unexpectedly decreases. Then real GDP (*ceteris paribus*) will be

- A) above potential GDP.
- B) below potential GDP.
- C) equal to potential GDP.
- D) either above, below, or equal to potential GDP depending on the position of the aggregate demand curve.
- E) either above or equal to potential GDP depending on the position of the aggregate demand curve.

Answer: B

Diff: 3 Type: MC

Topic: Inflation Cycles

29) A correctly anticipated increase in the quantity of money

- A) increases the price level with no change in real GDP.
- B) does not change the price level or real GDP.
- C) does not change the price level but increases real GDP.
- D) increases the price level and increases real GDP.
- E) does not change the price level but decreases real GDP.

Answer: A

Diff: 2 Type: MC

Topic: Inflation Cycles

30) A forecast that is based on all the relevant information available is

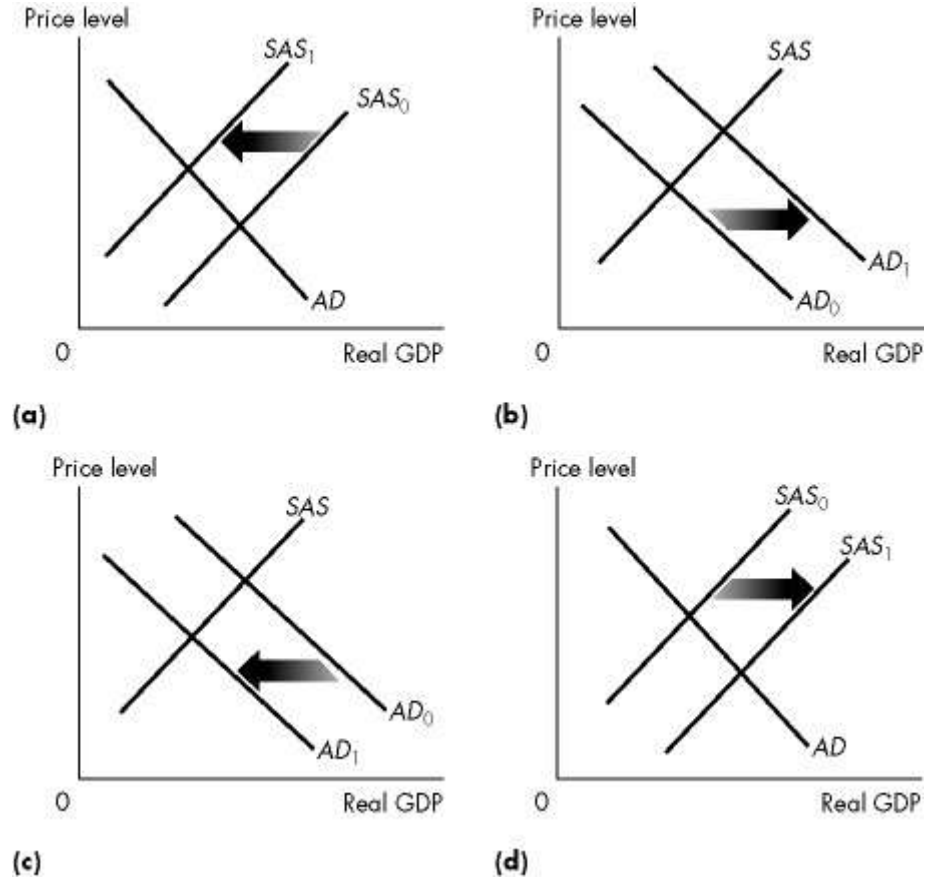
- A) usually no better than a random guess given that the future bears many uncertainties.
- B) usually accurate.
- C) called a rational expectation.
- D) useful only in the prediction of cost-push inflation.
- E) useful only in the prediction of demand-pull inflation.

Answer: C

Diff: 2 Type: MC

Topic: Inflation Cycles

Use the figure below to answer the following question.



**Figure 28.1.5**

31) Refer to Figure 28.1.5. Which one of the graphs in the figure represents an economy experiencing stagflation?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) none of the above

Answer: A

Diff: 2 Type: MC

Topic: Inflation Cycles

32) Refer to Figure 28.1.5. Which one of the graphs in the figure represents an economy with the price level expected to remain constant?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) none of the above

Answer: E

Diff: 3 Type: MC

Topic: Inflation Cycles

33) The economy starts out at a full-employment equilibrium. Some events then occur that generate a demand-pull inflation.

All of the following events *except* an increase in \_\_\_\_\_ might cause a demand-pull inflation.

- A) the money wage rate
- B) exports
- C) the quantity of money
- D) government expenditure
- E) transfer payments

Answer: A

Type: MC

Topic: Inflation Cycles

Source: MyEconLab

Use the figure below to answer the following question.



**Figure 28.1.6**

34) Refer to Figure 28.1.6. Starting at point A, the initial effect of a demand-pull inflation is a move to point \_\_\_\_\_. As a demand-pull inflation spiral proceeds, it follows the path \_\_\_\_\_.

- A) E; I
- B) C; E, H, I
- C) C; B, H, G, I
- D) B; E, G, I
- E) none of the above

Answer: B

Type: MC

Topic: Inflation Cycles

Source: MyEconLab

35) Refer to Figure 28.1.6. Starting at point A, the initial effect of a cost-push inflation is a move to point \_\_\_\_\_. As a cost-push inflation spiral proceeds, it follows the path \_\_\_\_\_.

- A) C; B, H, G, I
- B) C; E, H, I
- C) B; E, G, I
- D) E; I
- E) C; F

Answer: C

Type: MC

Topic: Inflation Cycles

Source: MyEconLab

36) The economy starts out at a full-employment equilibrium. Some events then occur that generate a cost-push inflation.

Which of the following events might cause a cost-push inflation?

- A) a decrease in exports
- B) an increase in the quantity of money
- C) a decrease in government expenditure
- D) an increase in the money wage rate or an increase in the money prices of raw materials
- E) an increase in taxes

Answer: D

Type: MC

Topic: Inflation Cycles

Source: MyEconLab

37) Suppose that the money prices of raw materials rise. With no action by the Bank of Canada,

- I. the aggregate demand curve shifts rightward and the price level rises.
- II. the aggregate demand curve shifts rightward and the aggregate supply curve shifts leftward.
- III. the initial outcome is lower employment and a rise in the price level.

- A) I only
- B) II only
- C) III only
- D) I and II only
- E) I, II, and III

Answer: C

Type: MC

38) Stagflation is the result of

- A) a decrease in aggregate demand.
- B) a decrease in short-run aggregate supply.
- C) an increase in aggregate demand.
- D) an increase in short-run aggregate supply.
- E) a decrease in short-run aggregate supply combined with a simultaneous increase in aggregate supply.

Answer: B

Type: MC

39) When the price level is rising and simultaneously real GDP is decreasing

- A) the natural unemployment rate is rising.
- B) the natural unemployment rate is falling.
- C) stagflation is occurring.
- D) the economy is experiencing an expansionary gap.
- E) Both A and C are correct.

Answer: C

Type: MC

40) Suppose aggregate demand increases by more than expected. Which of the following describes what occurs?

- A) Real GDP is greater than potential GDP.
- B) The price level rises.
- C) Unemployment falls.
- D) The natural unemployment rate does not change.
- E) All of the above.

Answer: E

Type: MC

## 28.2 Inflation and Unemployment: The Phillips Curve

- 1) Along the short-run Phillips curve, everything remaining the same, the higher the
- A) unemployment rate, the lower the inflation rate.
  - B) price level, the lower the inflation rate.
  - C) money wage rate, the lower is the unemployment rate.
  - D) quantity of money, the lower the unemployment rate.
  - E) growth rate of the quantity of money, the higher the inflation rate.

Answer: A

Diff: 1 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

- 2) The short-run Phillips curve shows the relationship between \_\_\_\_\_ holding constant the expected inflation rate and the natural unemployment rate.
- A) the inflation rate and the economic growth rate
  - B) unemployment and the economic growth rate
  - C) the inflation rate and the unemployment rate
  - D) growth and potential GDP.
  - E) the inflation rate and the growth of the money wage rate.

Answer: C

Diff: 1 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

- 3) If the unemployment rate rises and the inflation rate falls, while the natural unemployment rate and the expected inflation rate remain constant, then we are studying a movement along the
- A) aggregate demand curve.
  - B) long-run aggregate supply curve.
  - C) Friedman curve.
  - D) short-run Phillips curve.
  - E) Phelps-Friedman curve.

Answer: D

Diff: 2 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

- 4) For a given expected inflation rate, the higher the unemployment rate, the lower is the actual inflation rate. This relationship is the \_\_\_\_\_ Phillips curve. When the expected inflation rate changes, this is shown as a movement along the \_\_\_\_\_ Phillips curve.
- A) short-run; short-run
  - B) long-run; long-run
  - C) long-run; natural
  - D) natural; short-run
  - E) short-run; long-run

Answer: E

Diff: 3 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

5) If the natural unemployment rate rises

- A) the long-run Phillips curve shifts rightward and the short-run Phillips curve does not change.
- B) the long-run Phillips curve shifts leftward and the short-run Phillips curve does not change.
- C) the short-run Phillips curve shifts rightward and the long-run Phillips curve does not change.
- D) the short-run and long-run Phillips curves both shift leftward.
- E) the short-run and long-run Phillips curves both shift rightward.

Answer: E

Diff: 3 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

6) If the natural unemployment rate falls

- A) the long-run Phillips curve shifts rightward and the short-run Phillips curve does not change.
- B) the long-run Phillips curve shifts leftward and the short-run Phillips curve does not change.
- C) the short-run Phillips curve shifts rightward.
- D) the short-run and long-run Phillips curves both shift leftward.
- E) the short-run and long-run Phillips curves both shift rightward.

Answer: D

Diff: 3 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

7) The short-run Phillips curve shows the relationship between

- A) the price level and real GDP in the short run.
- B) the price level and unemployment in the short run.
- C) unemployment and real GDP in the short run.
- D) inflation and unemployment, when inflation expectations can change.
- E) inflation and unemployment, when the expected inflation rate and the natural unemployment rate remain constant.

Answer: E

Diff: 1 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

Source: Study Guide

8) Along the short-run Phillips curve, if the actual unemployment rate falls below the natural unemployment rate, the

- A) actual inflation rate will be equal to the expected inflation rate.
- B) actual inflation rate will be greater than the expected inflation rate.
- C) actual inflation rate will be less than the expected inflation rate.
- D) actual inflation rate may be greater than, equal to, or less than the expected inflation rate
- E) expected inflation rate will fall to zero.

Answer: B

Diff: 3 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

- 9) A movement down along the short-run Phillips curve results from an unanticipated
- A) decrease in aggregate demand.
  - B) increase in aggregate demand.
  - C) decrease in short-run aggregate supply.
  - D) increase in short-run aggregate supply.
  - E) increase in the natural unemployment rate.

Answer: A

Diff: 2 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

- 10) An increase in the expected rate of inflation shifts the
- A) short-run Phillips curve downward.
  - B) short-run Phillips curve upward.
  - C) long-run Phillips curve rightward.
  - D) long-run Phillips curve leftward.
  - E) B and C are correct.

Answer: B

Diff: 2 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

*Use the table below to answer the following questions.*

**Table 28.2.1**

Inflation (percent per year)	Unemployment (percent)
12	4
11	5
10	6
9	7
8	8
7	9

- 11) Refer to Table 28.2.1. The table gives points on the short-run Phillips curve for the country of Ruritania. If the expected inflation rate is 10 percent, what is the natural unemployment rate?

- A) 4 percent
- B) 5 percent
- C) 6 percent
- D) 7 percent
- E) 9 percent

Answer: C

Diff: 2 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

12) Refer to Table 28.2.1. The table gives points on the short-run Phillips curve for the country of Ruritania. If the expected inflation rate is 10 percent, and the inflation rate unexpectedly rises to 12 percent, what is the unemployment rate?

- A) 4 percent
- B) 5 percent
- C) 6 percent
- D) 7 percent
- E) 9 percent

Answer: A

Diff: 2 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

13) Refer to Table 28.2.1. The table gives points on the short-run Phillips curve for the country of Ruritania. If the expected inflation rate is 10 percent, and the inflation rate unexpectedly falls to 8 percent, what is the unemployment rate?

- A) 4 percent
- B) 5 percent
- C) 6 percent
- D) 7 percent
- E) 8 percent

Answer: E

Diff: 2 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

14) Refer to Table 28.2.1. The table gives points on the short-run Phillips curve for the country of Ruritania. If the expected inflation rate is 10 percent, and the inflation rate unexpectedly rises to 12 percent and stays there for some period of time, the expected inflation rate becomes \_\_\_\_\_ percent and the natural unemployment rate is \_\_\_\_\_ percent.

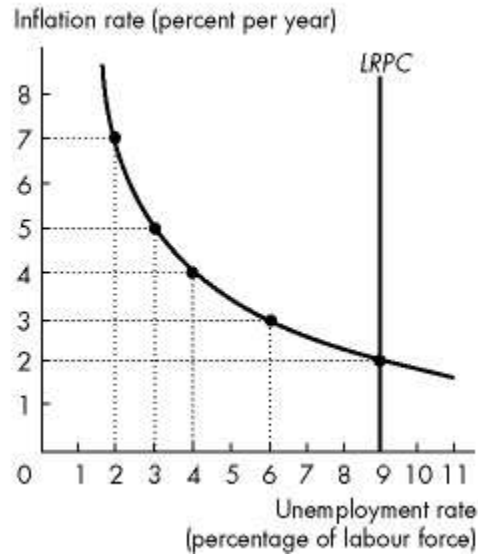
- A) 12; 4
- B) 10; 4
- C) 10; 6
- D) 12; 6
- E) 12; 5

Answer: D

Diff: 3 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

Use the figure below to answer the following questions.



**Figure 28.2.2**

15) Refer to Figure 28.2.2. The figure illustrates an economy's Phillips curves. What is the natural unemployment rate?

- A) 9 percent
- B) 6 percent
- C) 4 percent
- D) 7 percent
- E) cannot be determined without more information

Answer: A

Diff: 2 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

Source: Study Guide

16) Refer to Figure 28.2.2. The figure illustrates an economy's Phillips curves. What is the expected inflation rate?

- A) 9 percent
- B) 4 percent
- C) 2 percent
- D) 7 percent
- E) cannot be determined without more information

Answer: C

Diff: 2 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

Source: Study Guide

17) Refer to Figure 28.2.2. The figure illustrates an economy's Phillips curves. If the current inflation rate is 4 percent, what is the current unemployment rate?

- A) 9 percent
- B) 6 percent
- C) 4 percent
- D) 3 percent
- E) cannot be determined without more information

Answer: C

Diff: 1 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

Source: Study Guide

18) Refer to Figure 28.2.2. The figure illustrates an economy's Phillips curves. If the current inflation rate is 3 percent, what is the current unemployment rate?

- A) 9 percent
- B) 6 percent
- C) 4 percent
- D) 3 percent
- E) cannot be determined without more information

Answer: B

Diff: 1 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

19) Refer to Figure 28.2.2. The figure illustrates an economy's Phillips curves. If the current inflation rate is 4 percent, what is the natural unemployment rate?

- A) 9 percent
- B) 6 percent
- C) 4 percent
- D) 3 percent
- E) cannot be determined without more information

Answer: A

Diff: 2 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

20) Refer to Figure 28.2.2. The figure illustrates an economy's Phillips curves. If the expected inflation rate changes to 3 percent, the

- A) short run Phillips curve will shift upward and the long run Phillips curve will not change.
- B) short run Phillips curve will shift downward and the long run Phillips curve will not change.
- C) short run Phillips curve will shift upward and the long run Phillips curve will shift leftward.
- D) short run Phillips curve will shift upward and the long run Phillips curve will shift rightward.
- E) short run Phillips curve will shift downward and the long run Phillips curve will shift rightward.

Answer: A

Diff: 2 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

- 21) If the inflation rate is lower than the expected inflation rate,  
A) unemployment is above the natural rate.  
B) the natural unemployment rate will increase.  
C) the expected inflation rate will increase.  
D) unemployment is below the natural rate.  
E) the economy is not operating on the short-run Phillips curve.

Answer: A

Diff: 2 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

Source: Study Guide

- 22) If there is a fully anticipated increase in the inflation rate  
A) unemployment will be below the natural rate.  
B) unemployment will be above the natural rate.  
C) the natural unemployment rate will increase.  
D) the economy is not operating on the *LRPC* curve.  
E) the economy is operating on the *LRPC* curve.

Answer: E

Diff: 2 Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

Source: Study Guide

- 23) If the natural unemployment rate increases, the long-run Phillips curve \_\_\_\_\_, the short-run Phillips curve \_\_\_\_\_, and the expected inflation rate \_\_\_\_\_.  
A) does not shift; does not shift; does not change  
B) shifts rightward; shifts rightward; does not change  
C) does not shift; shifts rightward; rises  
D) shifts rightward; curve does not shift; falls  
E) shifts rightward; shifts rightward; falls

Answer: B

Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

Source: MyEconLab

- 24) The Canadian short-run Phillips curve \_\_\_\_\_ when the expected inflation rate rises and \_\_\_\_\_ when the expected inflation rate falls.

The Canadian short-run Phillips curve \_\_\_\_\_ when the natural unemployment rate increases and \_\_\_\_\_ when the natural unemployment rate decreases.

- A) shifts downward; shifts upward; shifts rightward; shifts leftward  
B) does not shift; does not shift; shifts rightward; shifts leftward  
C) shifts upward; shifts downward; does not shift; does not shift  
D) shifts upward; shifts downward; shifts rightward; shifts leftward  
E) shifts upward; does not shift; shifts rightward; does not shift

Answer: D

Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

Source: MyEconLab

25) The Canadian long-run Phillips curve \_\_\_\_\_ when the expected inflation rate rises and \_\_\_\_\_ when the expected inflation rate falls.

The Canadian long-run Phillips curve \_\_\_\_\_ when the natural unemployment rate increases and \_\_\_\_\_ when the natural unemployment rate decreases.

- A) does not shift; does not shift; does not shift; does not shift
- B) does not shift; does not shift; shifts rightward; shifts leftward
- C) shifts upward; shifts downward; shifts rightward; shifts leftward
- D) shifts rightward; shifts leftward; does not shift; does not shift
- E) shifts rightward; shifts leftward; shifts rightward; shifts leftward

Answer: B

Type: MC

Topic: Inflation and Unemployment: The Phillips Curve

Source: MyEconLab

**Table 28.2.2**

Inflation rate (percent per year)	Unemployment rate (percent)
8	3
6	4
4	5
2	6

26) Refer to Table 28.2.2. The economy's natural unemployment rate is 4 percent. Table 28.2.2 gives some points on the economy's short-run Phillips curve. When the unemployment rate is 4 percent \_\_\_\_\_.

- A) actual inflation is greater than expected inflation
- B) actual inflation is less than expected inflation
- C) and the inflation rate is 6 percent a year, the short-run and long-run Phillips curves intersect
- D) and the expected inflation rate is 8 percent a year, the short-run Phillips curve shifts downward
- E) aggregate demand increases

Answer: C

Type: MC

27) Refer to Table 28.2.2. The economy's natural unemployment rate is 4 percent. Table 28.2.2 gives some points on the economy's short-run Phillips curve. If the expected inflation rate rises to 8 percent a year, \_\_\_\_\_.

- A) the long-run Phillips curve shifts leftward
- B) the short-run Phillips curve shifts upward
- C) the short-run Phillips curve shifts downward
- D) Both A and B are correct.
- E) Both A and C are correct.

Answer: B

Type: MC

28) Consider the short-run Phillips curve in Canada since the 1960s. Choose the best statement.

- A) Canada's inflation/unemployment tradeoff is best shown as a series of shifting short-run Phillips curves that sometimes shift upward and sometimes shift downward.
- B) Canada's inflation/unemployment tradeoff is undefined.
- C) Canada's short-run Phillips curve is consistently shifting upward.
- D) Canada's short-run Phillips curve is consistently shifting downward.
- E) Canada's short-run Phillips curve is consistently shifting rightward.

Answer: A

Type: MC

### 28.3 The Business Cycle

1) According to \_\_\_\_\_, the business cycle is the result of aggregate demand growing at a fluctuating rate.

- A) the Keynesian cycle theory only
- B) only the Keynesian and monetarist cycle theories
- C) the Keynesian, monetarist, and real business cycle theories
- D) the Keynesian, monetarist, and new classical cycle theories
- E) real business cycle theory

Answer: D

Type: MC

Topic: The Business Cycle

Skill: Recognition

AACSB: Reflective Thinking

2) Which of the following are business cycle theories that regard fluctuations in aggregate demand as the factor that creates business cycles?

- I. Keynesian cycle theory
- II. real business cycle theory
- III. monetarist cycle theory

- A) I only
- B) I and II
- C) I and III
- D) I, II and III
- E) II and III

Answer: C

Type: MC

Topic: The Business Cycle

Skill: Recognition

AACSB: Reflective Thinking

3) Which of the following is *not* a mainstream theory of the business cycle?

- A) Keynesian cycle theory
- B) Monetarist cycle theory
- C) New Keynesian cycle theory
- D) Real business cycle theory
- E) New classical cycle theory

Answer: D

Type: MC

Topic: The Business Cycle

Skill: Recognition

AACSB: Reflective Thinking

- 4) In the Keynesian business cycle theory, business cycles begin with a change in
- A) inflation expectations.
  - B) government expenditure.
  - C) business confidence.
  - D) monetary policy.
  - E) the money wage rate.

Answer: C

Type: MC

Topic: The Business Cycle

Skill: Recognition

AACSB: Reflective Thinking

- 5) \_\_\_\_\_ states that the main source of economic fluctuations is fluctuations in business confidence.

- A) Real business cycle theory
- B) New classical cycle theory
- C) Keynesian cycle theory
- D) Monetarist cycle theory
- E) None of the above

Answer: C

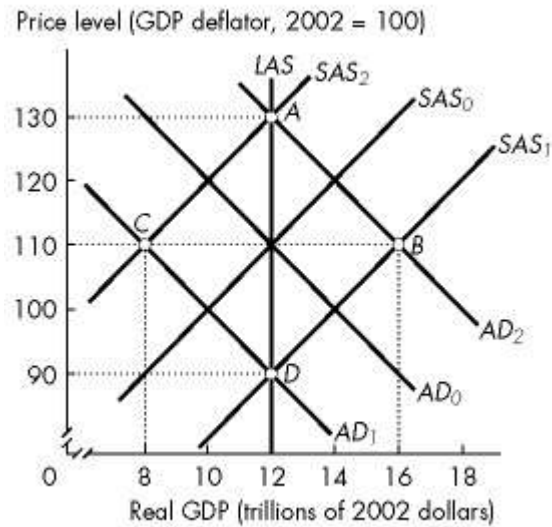
Type: MC

Topic: The Business Cycle

Skill: Recognition

AACSB: Reflective Thinking

Use the figure below to answer the following questions.



**Figure 28.3.1**

6) Refer to Figure 28.3.1. Suppose the economy moves from point *A* to point *C*. According to the monetarist theory of the business cycle, what could have caused this movement?

- A) an increase in the money wage rate
- B) an increase in the growth rate of the quantity of money
- C) a decrease in the growth rate of the quantity of money
- D) an increase in uncertainty
- E) animal spirits

Answer: C

Type: MC

Topic: The Business Cycle

Skill: Analytical

AACSB: Analytical Skills

7) Refer to Figure 28.3.1. Suppose the economy moves from point *D* to point *B*. According to the monetarist theory of the business cycle, what could have caused this movement?

- A) a decrease in the money wage rate
- B) an increase in uncertainty about future sales and profits
- C) an increase in the growth rate of the quantity of money
- D) an increase in the money wage rate
- E) a decrease in exports

Answer: C

Type: MC

Topic: The Business Cycle

Skill: Analytical

AACSB: Analytical Skills

- 8) Both new Keynesian and new classical cycle theories claim that
- A) animal spirits can trigger a business cycle.
  - B) shifts in the *SAS* curve are the main impulse for a business cycle.
  - C) unexpected changes in aggregate demand trigger a business cycle.
  - D) expected changes in the quantity of money can trigger a business cycle.
  - E) a change in the price of oil is the major cause of a business cycle.

Answer: C

Type: MC

Topic: The Business Cycle

9) The key difference between new classical cycle theory and new Keynesian cycle theory is that the new classical cycle theory believes that \_\_\_\_\_ while the new Keynesian cycle theory believes that \_\_\_\_\_.

- A) expected changes in aggregate demand change real GDP; expected changes in aggregate demand do not change real GDP
- B) only unexpected changes in aggregate demand change real GDP; only expected changes in aggregate demand change real GDP
- C) only unexpected changes in aggregate demand change real GDP; both expected and unexpected changes in aggregate demand change real GDP
- D) the short-run aggregate supply curve is horizontal; the short-run aggregate supply curve is vertical.
- E) expected and unexpected changes in aggregate demand change real GDP; only changes in labour productivity change aggregate demand

Answer: C

Type: MC

Topic: The Business Cycle

Skill: Conceptual

AACSB: Reflective Thinking

10) The \_\_\_\_\_ cycle theory states that only unexpected fluctuations in aggregate demand bring fluctuations in real GDP around potential GDP.

- A) new Keynesian
- B) new classical
- C) Keynesian
- D) monetarist
- E) real business

Answer: B

Type: MC

Topic: The Business Cycle

Skill: Recognition

AACSB: Reflective Thinking

11) In new classical cycle theory, \_\_\_\_\_ bring fluctuations in real GDP around potential GDP.

- A) unexpected changes in aggregate demand
- B) expected changes in aggregate demand
- C) fluctuations in money growth with rigid wages
- D) fluctuations in investment coupled with rigid wages
- E) expected changes in labour productivity

Answer: A

Type: MC

Topic: The Business Cycle

Skill: Recognition

AACSB: Reflective Thinking

12) The new classical theory argues that the primary factor leading to business cycles is

- A) expected fluctuations in aggregate demand.
- B) expected fluctuations in short-run aggregate supply.
- C) unexpected fluctuations in aggregate demand.
- D) unexpected fluctuations in short-run aggregate supply.
- E) unexpected fluctuations in long-run aggregate supply.

Answer: C

Type: MC

Topic: The Business Cycle

Skill: Recognition

AACSB: Reflective Thinking

13) New Keynesian economists believe that \_\_\_\_\_ is influenced by \_\_\_\_\_.

- A) yesterday's money wage rate; today's rational expectations of the money wage
- B) today's money wage rate; yesterday's rational expectations of the price level
- C) yesterday's rational expectations of the price level; today's money wage rate
- D) today's money wage rate; today's rational expectations of the price level
- E) today's money wage rate; animal spirits

Answer: B

Type: MC

Topic: The Business Cycle

Skill: Recognition

AACSB: Reflective Thinking

14) Which business cycle theory emphasizes that, because of previously negotiated wage agreements, both expected and unexpected fluctuations in aggregate demand can change real GDP?

- A) the new classical cycle theory
- B) the new Keynesian cycle theory
- C) Monetarist cycle theory
- D) Keynesian cycle theory
- E) Real business cycle theory

Answer: B

Type: MC

Topic: The Business Cycle

Skill: Recognition

AACSB: Reflective Thinking

15) The factor leading to business cycles in the \_\_\_\_\_ cycle theory is unexpected fluctuations in aggregate demand while in the \_\_\_\_\_ cycle theory both unexpected and expected fluctuations in aggregate demand are factors that lead to business cycles.

- A) new classical; monetarist
- B) new classical; new Keynesian
- C) new Keynesian; Keynesian
- D) monetarist; new Keynesian
- E) real business; monetarist

Answer: B

Type: MC

Topic: The Business Cycle

Skill: Conceptual

AACSB: Reflective Thinking

16) According to \_\_\_\_\_ theory, a decrease in productivity growth shifts the \_\_\_\_\_.

- A) real business cycle; *AD* curve rightward
- B) Keynesian cycle; *SAS* curve leftward
- C) real business cycle; demand for loanable funds curve leftward
- D) Keynesian cycle; *SAS* curve rightward
- E) real business cycle; *AD* curve leftward

Answer: C

Type: MC

Topic: The Business Cycle

Skill: Conceptual

AACSB: Reflective Thinking

17) The key ripple effect in real business cycle theory is the \_\_\_\_\_ decision and it depends on the \_\_\_\_\_.

- A) when-to-invest; real interest rate
- B) when-to-work; real interest rate
- C) what-to-save; nominal interest rate
- D) where-to-work; real wage rate
- E) when-to-work; rigidity of the money wage rate

Answer: B

Type: MC

Topic: The Business Cycle

Skill: Recognition

AACSB: Reflective Thinking

18) According to the real business cycle theory, what effects follow from a change in productivity?

- I. Investment demand changes.
- II. The demand for labour changes.
- III. Government expenditure changes.

- A) I
- B) I and II
- C) I and III
- D) II and III
- E) I, II and III

Answer: B

Type: MC

Topic: The Business Cycle

Skill: Conceptual

AACSB: Reflective Thinking

19) "Intertemporal substitution" in real business cycle theory refers to the change in the \_\_\_\_\_ as a result of the change in the real interest rate.

- A) personal tax rate
- B) demand for loanable funds
- C) supply of labour
- D) consumer demand for goods
- E) demand for labour

Answer: C

Type: MC

Topic: The Business Cycle

Skill: Recognition

AACSB: Reflective Thinking

20) In real business cycle theory, a decrease in productivity leads to all of the following events *EXCEPT*

- A) a decrease in the demand for labour.
- B) a decrease in the demand for loanable funds.
- C) a rise in the real wage rate.
- D) a fall in the real interest rate.
- E) a decrease in the supply of labour.

Answer: C

Type: MC

Topic: The Business Cycle

Skill: Conceptual

AACSB: Reflective Thinking

21) In real business cycle theory, the supply of labour

- A) increases if the nominal interest rate rises.
- B) is independent of the real interest rate.
- C) decreases if the real interest rate rises.
- D) decreases if the real interest rate falls.
- E) decreases if the real wage rate decreases.

Answer: D

Type: MC

Topic: The Business Cycle

Skill: Conceptual

AACSB: Reflective Thinking

22) Suppose that a severe shock that decreases the demand for loanable funds hits Canada. Which of the following can we expect to occur according to real business cycle theory?

- A) The real interest rate will fall.
- B) People will work fewer hours.
- C) The real wage rate will fall.
- D) The demand for loanable funds will decrease.
- E) All of the above are true.

Answer: E

Type: MC

Topic: The Business Cycle

Skill: Conceptual

AACSB: Reflective Thinking

23) According to real business cycle theory, an increase in productivity \_\_\_\_\_ the demand for loanable funds, \_\_\_\_\_ the demand for labour, and \_\_\_\_\_ the supply of labour. The real interest rate will \_\_\_\_\_.

- A) increase; increases; does not change; fall
- B) increase; increases; does not change; rise
- C) decrease; decreases; decreases; fall
- D) increases; increases; increases; rise
- E) increases; increases; increases; fall

Answer: D

Type: MC

Topic: The Business Cycle

Skill: Conceptual

AACSB: Reflective Thinking

24) According to the real business cycle theory, during a recession the demand for labour \_\_\_\_\_ and the supply of labour \_\_\_\_\_.

- A) increases; decreases
- B) decreases; does not change
- C) does not change; decreases
- D) decreases; decreases
- E) decreases; increases

Answer: D

Type: MC

Topic: The Business Cycle

Skill: Conceptual

AACSB: Reflective Thinking

25) According to real business cycle theory, workers' decisions to work now versus later depend on

- A) the real wage rate today but not the real wage rate in the future.
- B) the money wage rate.
- C) the real interest rate.
- D) labour productivity.
- E) none of the above.

Answer: C

Type: MC

Topic: The Business Cycle

Skill: Conceptual

AACSB: Reflective Thinking

26) Suppose that in response to a decrease in real interest rates, a person decides to reduce his supply of labour today and increase it in the future. This behaviour is most consistent with the

- A) new classical cycle theory.
- B) Keynesian cycle theory.
- C) new Keynesian cycle theory.
- D) real business cycle theory.
- E) monetarist cycle theory.

Answer: D

Type: MC

Topic: The Business Cycle

Skill: Conceptual

AACSB: Reflective Thinking

27) According to real business cycle theory, if the Bank of Canada increases the quantity of money when real GDP decreases, real GDP

- A) will increase but only temporarily.
- B) will increase permanently.
- C) and the price level will both be unaffected.
- D) will be unaffected, but the price level will rise.
- E) will decrease due to the inefficiencies introduced into production as a result.

Answer: D

Type: MC

Topic: The Business Cycle

Source: Study Guide

28) Suppose that the business cycle in Canada is best described by RBC theory.

An advance in technology increases productivity.

The when-to-work decision depends on the real interest rate. The \_\_\_\_\_ the real interest rate, other things remaining the same, the \_\_\_\_\_ is the supply of labour today.

RBC theorists believe the when-to-work effect is \_\_\_\_\_.

- A) lower; smaller; small
- B) higher; smaller; small
- C) higher; larger; large
- D) lower; larger; large
- E) higher; larger; small

Answer: C

Diff: 2 Type: MC

Topic: The Business Cycle

Source: MyEconLab

29) According to mainstream business cycle theory, \_\_\_\_\_ grows at a steady rate and \_\_\_\_\_ grows at a fluctuating rate.

- A) aggregate demand; long-run aggregate supply
- B) potential GDP; aggregate demand
- C) potential GDP; short-run aggregate supply
- D) short-run aggregate supply; long-run aggregate supply
- E) short-run aggregate supply; aggregate demand

Answer: B

Type: MC

Topic: The Business Cycle

Source: MyEconLab

30) In real business cycle theory, \_\_\_\_\_ are the main source of economic fluctuations.

- A) unexpected changes in government expenditure
- B) random fluctuations in investment
- C) random fluctuations in productivity
- D) unexpected changes in the full-employment quantity of labour
- E) changes in the quantity of money

Answer: C

Type: MC

Topic: The Business Cycle

Source: MyEconLab

31) In real business cycle theory, the supply of labour

- A) increases if the real interest rate falls.
- B) increases if the real interest rate rises.
- C) increases if the demand for labour decreases.
- D) is not influenced by changes in the real interest rate.
- E) increases if the demand for loanable funds decreases.

Answer: B

Type: MC

32) According to real business cycle theory, a fall in the real interest rate \_\_\_\_\_ the supply of labour and \_\_\_\_\_ employment.

- A) decreases; decreases
- B) increases; increases
- C) decreases; increases
- D) increases; decreases
- E) does not change; does not change

Answer: A

Type: MC

33) Real business cycle theorists believe that the intertemporal substitution effect \_\_\_\_\_. Many other economists believe that the intertemporal substitution effect \_\_\_\_\_.

- A) is large; is negligible
- B) is negligible; is large
- C) occurs in the money market; occurs in the labour market
- D) occurs in the labour market; occurs in the money market
- E) none of the above

Answer: A

Type: MC

## Chapter 29 Fiscal Policy

### 29.1 The Federal Budget

1) If revenues exceed outlays, the government's budget balance is \_\_\_\_\_, and the government has a budget \_\_\_\_\_.

- A) negative; deficit
- B) positive; surplus
- C) positive; deficit
- D) negative; surplus
- E) zero; deficit

Answer: B

Diff: 1 Type: MC

Topic: Government Budgets

2) If outlays exceed revenues, the government's budget balance is \_\_\_\_\_, and the government has a budget \_\_\_\_\_.

- A) negative; deficit
- B) positive; surplus
- C) positive; deficit
- D) negative; surplus
- E) zero; surplus

Answer: A

Diff: 1 Type: MC

Topic: Government Budgets

3) Government debt is

- A) equal to revenues minus outlays.
- B) always increasing.
- C) a phenomena that occurs only during times of war.
- D) the total amount of government borrowing.
- E) the result of a rising price level.

Answer: D

Diff: 1 Type: MC

Topic: Government Budgets

4) All of the following statements are true *except*

- A) total revenues have no strong trends.
- B) revenues include corporate income taxes, personal income taxes; indirect taxes and investment income.
- C) the main source of fluctuations in revenues is corporate income taxes.
- D) indirect taxes decreased during the 1990s due to the introduction of the GST.
- E) total revenues increased through the 1960s and 1980s.

Answer: C

Diff: 2 Type: MC

Topic: Government Budgets

5) All of the following statements are true *except*

- A) the three components of government outlays are transfer payments, expenditures on goods and services, and debt interest.
- B) debt interest has been steadily increasing since 1960.
- C) expenditures on goods and services have a downward trend.
- D) outlays increased steadily from 1971 through 1985.
- E) transfer payments decreased sharply during the 1990s.

Answer: B

Diff: 2 Type: MC

Topic: Government Budgets

6) Choose the correct statement

- A) The federal government debt was 5 percent of GDP in 1970.
- B) The debt-to-GDP ratio increased slightly during the 2008-2009 recession.
- C) The debt-to-GDP ratio increased from 1974 through 1997, and then began to decrease.
- D) The government debt increases when the government has a budget deficit.
- E) All of the above.

Answer: E

Diff: 2 Type: MC

Topic: Government Budgets

7) During the 1980s and 1990s in Canada,

- A) investment income as a percentage of GDP increased.
- B) indirect taxes as a percentage of GDP increased steadily.
- C) personal income taxes as a percentage of GDP decreased.
- D) total revenues as a percentage of GDP increased by over 5 percent.
- E) none of the above.

Answer: E

Diff: 2 Type: MC

Topic: Government Budgets

8) The main components of government revenues are

- A) transfer payments, investment income, and indirect taxes.
- B) personal income taxes, corporate income taxes, indirect taxes, and investment income.
- C) debt interest, expenditures on goods and services, and income taxes.
- D) corporate income taxes, indirect taxes, and transfer payments.
- E) debt interest, corporate income taxes, and income taxes.

Answer: B

Diff: 2 Type: MC

Topic: Government Budgets

9) The category of federal government revenues that fluctuates the most is

- A) investment income.
- B) transfer payments.
- C) personal income taxes.
- D) debt interest.
- E) indirect taxes.

Answer: C

Diff: 2 Type: MC

Topic: Government Budgets

10) Suppose the government starts with a debt of \$0. Then in year 1, there is a deficit of \$100 billion, in year 2 there is a deficit of \$60 billion, in year 3 there is a surplus of \$40 billion, and in year 4 there is a deficit of \$20 billion. What is government debt at the end of year 4?

- A) \$20 billion.
- B) \$140 billion.
- C) \$180 billion.
- D) Somewhat greater than \$220 billion, depending on the interest rate.
- E) Somewhat greater than \$140 billion, depending on the interest rate.

Answer: B

Diff: 1 Type: MC

Topic: Government Budgets

11) Which of the following would *not* increase an existing budget deficit?

- A) an increase in interest on the government debt
- B) an increase in government expenditures on goods and services
- C) an increase in government transfer payments
- D) an increase in indirect taxes
- E) a decrease in investment income

Answer: D

Diff: 1 Type: MC

Topic: Government Budgets

Source: Study Guide

12) Fiscal policy is

- A) the use of the federal budget to achieve macroeconomic objectives.
- B) any policy by the Bank of Canada.
- C) budgeting policy by aggregate households.
- D) any attempt by the federal government or Bank of Canada to control inflation.
- E) effective only when the federal government has a budget surplus.

Answer: A

Diff: 1 Type: MC

Topic: Government Budgets

13) Which of the following is *not* a source of government revenues?

- A) personal income taxes
- B) transfer payments
- C) corporate income taxes
- D) indirect taxes
- E) investment income

Answer: B

Diff: 1 Type: MC

Topic: Government Budgets

14) Which of the following is a government outlay?

- A) personal income taxes
- B) investment income
- C) debt interest
- D) indirect taxes
- E) corporate income taxes

Answer: C

Diff: 1 Type: MC

Topic: Government Budgets

Source: Study Guide

15) As a percentage of provincial GDP, provincial government outlays are highest in

- A) Alberta.
- B) Newfoundland and Labrador.
- C) the Yukon Territory.
- D) Nunavut.
- E) Quebec.

Answer: D

Diff: 2 Type: MC

Topic: Government Budgets

16) What are the main categories of the federal government outlays?

- A) transfer payments, expenditures on goods and services, and debt interest
- B) indirect taxes, farmers' subsidies, and debt interest
- C) personal income taxes, expenditures on goods and services, and debt interest
- D) investment income, debt interest and transfer payments
- E) none of the above

Answer: A

Diff: 2 Type: MC

Topic: Government Budgets

17) Outlays as a percentage of provincial GDP are the highest in \_\_\_\_\_, whereas the largest transfers from the federal government are made to \_\_\_\_\_.

- A) Ontario; Northern Canada and the Atlantic provinces
- B) British Columbia; Northern Canada and the Atlantic provinces
- C) Alberta; Northern Canada and the Atlantic provinces
- D) Northern Canada; Northern Canada and the Atlantic provinces
- E) Northern Canada and the Atlantic provinces; Quebec

Answer: D

Diff: 2 Type: MC

Topic: Government Budgets

18) The government of Ricardia's budget lists the following projected revenues and outlays: \$25 million in personal income taxes, \$15 million in corporate income taxes, \$5 million in indirect taxes, \$2 million in investment income, \$30 million in transfer payments, \$12 million in government expenditure, and \$8 million in debt interest. Ricardia has a government budget

- A) surplus of \$3 million.
- B) surplus of \$57 million.
- C) surplus of \$13 million.
- D) deficit of \$13 million.
- E) deficit of \$3 million.

Answer: E

Diff: 2 Type: MC

Topic: Government Budgets

Source: Study Guide

19) The largest source of revenues for the federal government is

- A) transfer payments.
- B) expenditures on goods and services.
- C) personal income taxes.
- D) corporate income taxes.
- E) indirect taxes such as the GST.

Answer: C

Diff: 2 Type: MC

Topic: Government Budgets

Source: Study Guide

20) Prior to World War II, the purpose of the federal budget was to \_\_\_\_\_.

- A) stabilize the economy
- B) achieve macroeconomic objectives such as full employment and price level stability
- C) finance the business of government
- D) provide incentives to encourage investment
- E) oversee revenue equalization among the provinces

Answer: C

Type: MC

21) Canada's government debt

A) is smaller than the value of the public capital stock so Canada's debt has not financed public consumption expenditure.

B) is larger than the value of the public capital stock so some of Canada's debt has financed public consumption expenditure.

C) equals the value of the public capital stock.

D) has risen every year since 1975.

E) is smaller than the value of the public capital stock so some of Canada's debt has financed public consumption expenditure.

Answer: B

Type: MC

22) The Federal Budget of 2011-12 projected \_\_\_\_\_.

A) a government budget surplus

B) a balanced budget

C) a government budget deficit

D) a decreasing government debt

E) Both A and D are correct.

Answer: C

Type: MC

## 29.2 Supply-Side Effects of Fiscal Policy

1) An increase in income taxes

- A) does not affect potential GDP because potential GDP depends on technology only.
- B) does not affect potential GDP as long as the economy's endowments of resources and the state of technology remain unchanged.
- C) increases potential GDP because workers have to work longer hours to maintain the same standard of living before the tax increase.
- D) decreases potential GDP because workers' incentives to work are weakened.
- E) decreases potential GDP because real GDP decreases when households have less disposable income to spend.

Answer: D

Diff: 3 Type: MC

Topic: Supply Side Effects of Fiscal Policy

2) A tax cut on capital income

- A) does not affect potential GDP because the interest rate affects aggregate expenditure only.
- B) does not affect potential GDP because it has no impact on the supply of labour.
- C) increases potential GDP because workers have greater incentives to work.
- D) increases potential GDP because the supply of loanable funds increases.
- E) increases potential GDP because households have more disposable income to spend.

Answer: D

Diff: 2 Type: MC

Topic: Supply Side Effects of Fiscal Policy

3) Consider all the effects of fiscal policy. A cut in the income tax

- A) shifts the *AD* curve rightward but does not shift either the *LAS* or *SAS* curve.
- B) shifts the *AD*, *SAS*, and *LAS* curves rightward.
- C) shifts the *SAS* curve rightward but does not shift either the *AD* or *LAS* curve.
- D) shifts both the *SAS* and *LAS* curves rightward but does not shift the *AD* curve.
- E) shifts the *LAS* curve rightward but does not shift either the *AD* or *SAS* curve.

Answer: B

Diff: 3 Type: MC

Topic: Supply Side Effects of Fiscal Policy

4) Consider all the effects on fiscal policy. A cut in the tax on capital income

- A) shifts the *AD* curve rightward.
- B) shifts the *SAS* curve rightward.
- C) shifts the *LAS* curve rightward.
- D) all of the above.
- E) only B and C.

Answer: D

Diff: 2 Type: MC

Topic: Supply Side Effects of Fiscal Policy

- 5) Consider all the effects of fiscal policy. An income tax cut
- A) increases both real GDP and the price level.
  - B) increases real GDP but decreases the price level.
  - C) increases real GDP but leaves the price level unchanged.
  - D) increases real GDP and the price level may rise or fall.
  - E) does not change real GDP or the price level.

Answer: D

Diff: 3 Type: MC

Topic: Supply Side Effects of Fiscal Policy

- 6) An income tax cut that provides a greater incentive to work than an alternative tax cut will result in comparatively
- A) higher long-run real GDP and a higher price level.
  - B) higher long-run real GDP and a lower price level.
  - C) the same level of long-run real GDP and price level.
  - D) the same level of long-run real GDP and a higher price level.
  - E) the same level of long-run real GDP and a lower price level.

Answer: B

Diff: 2 Type: MC

Topic: Supply Side Effects of Fiscal Policy

- 7) If the nominal interest rate is 11%, the inflation rate is 4% and the tax rate is 25%, what is the real after-tax interest rate?
- A) -1.25%
  - B) 4.25%
  - C) 5.25%
  - D) 8%
  - E) 10%

Answer: B

Diff: 2 Type: MC

Topic: Supply Side Effects of Fiscal Policy

Source: Study Guide

- 8) The Laffer Curve has been criticized by mainstream economists because
- A) there is no theoretical possibility of higher tax rates leading to lower tax revenues.
  - B) higher tax rates do not create negative incentive effects.
  - C) tax cuts are just spent, not saved as predicted by the theory.
  - D) savers look only at real interest rates, not nominal interest rates.
  - E) empirically, tax cuts have not led to higher tax revenues.

Answer: E

Diff: 2 Type: MC

Topic: Supply Side Effects of Fiscal Policy

Source: Study Guide

- 9) An income tax \_\_\_\_\_ potential GDP by shifting the labour \_\_\_\_\_ curve \_\_\_\_\_.
- A) increases; demand; rightward
  - B) decreases; demand; rightward
  - C) increases; supply; rightward
  - D) decreases; supply; leftward
  - E) increases; supply curve and labour demand curve; rightward

Answer: D

Type: MC

Topic: Supply Side Effects of Fiscal Policy

Skill: Conceptual

AACSB: Analytical Skills

- 10) If we compare Canada to France and the United Kingdom, Canada's tax wedge is \_\_\_\_\_ the French tax wedge and \_\_\_\_\_ the U.K. tax wedge.

- A) larger than; smaller than
- B) equal to; larger than
- C) smaller than; smaller than
- D) larger than; larger than
- E) smaller than; larger than

Answer: C

Type: MC

Topic: Supply Side Effects of Fiscal Policy

Skill: Recognition

AACSB: Reflective Thinking

- 11) The difference between the before-tax and after-tax rates is the

- A) tax plug.
- B) deadweight gain.
- C) tax wedge.
- D) taxation penalty.
- E) deadweight loss.

Answer: C

Type: MC

Topic: Supply Side Effects of Fiscal Policy

Skill: Recognition

AACSB: Reflective Thinking

12) If we compare the United States to France, we see that potential GDP per person in France is \_\_\_\_\_ than that in the United States because the French tax wedge is \_\_\_\_\_ than the U.S. tax wedge.

- A) greater; larger
- B) greater; smaller
- C) less; larger
- D) less; smaller
- E) none of the above

Answer: C

Type: MC

Topic: Supply Side Effects of Fiscal Policy

Skill: Conceptual

AACSB: Reflective Thinking

13) Suppose the tax rate on interest income is 50 percent, the real interest rate is 3 percent, and the inflation rate is 4 percent. The real after-tax interest rate is

- A) -0.5 percent.
- B) 3.5 percent.
- C) 3.0 percent.
- D) 4.0 percent.
- E) -3.5 percent.

Answer: A

Type: MC

Topic: Supply Side Effects of Fiscal Policy

Skill: Analytical

AACSB: Analytical Skills

14) Suppose the tax rate on interest income is 25 percent, the real interest rate is 4 percent, and the inflation rate is 4 percent. The real after-tax interest rate is

- A) 0.5 percent.
- B) 3.5 percent.
- C) 4.0 percent.
- D) 2.0 percent.
- E) -0.5 percent.

Answer: D

Type: MC

Topic: Supply Side Effects of Fiscal Policy

Skill: Analytical

AACSB: Analytical Skills

15) The Laffer curve is the relationship between

- A) government expenditure and potential GDP.
- B) the tax rate and potential GDP.
- C) tax revenue and potential GDP.
- D) the tax rate and the amount of tax revenue.
- E) government outlays and revenues.

Answer: D

Type: MC

Topic: Supply Side Effects of Fiscal Policy

Skill: Recognition

AACSB: Reflective Thinking

16) According to the Laffer curve, raising the tax rate

- A) always increases the amount of tax revenue.
- B) always decreases the amount of tax revenue.
- C) does not change the amount of tax revenue.
- D) might increase, decrease, or not change the amount of tax revenue.
- E) has no effect on the amount of tax revenue.

Answer: D

Type: MC

Topic: Supply Side Effects of Fiscal Policy

Skill: Conceptual

AACSB: Reflective Thinking

17) The Laffer curve shows that increasing \_\_\_\_\_ increases \_\_\_\_\_ when \_\_\_\_\_ low.

- A) tax revenue; potential GDP; tax revenue is
- B) the tax rate; tax revenue; the tax rate is
- C) potential GDP; tax revenue; tax revenue is
- D) government outlays; the budget deficit; government expenditure is
- E) investment; potential GDP; the interest rate is

Answer: B

Type: MC

Topic: Supply Side Effects of Fiscal Policy

Skill: Conceptual

AACSB: Reflective Thinking

18) An increase in the tax on capital income \_\_\_\_\_ the supply of loanable funds and \_\_\_\_\_ investment.

- A) increases; increases
- B) increases; decreases
- C) decreases; increases
- D) decreases; decreases
- E) decreases the demand for loanable funds; decreases or increases

Answer: D

Type: MC

Topic: Supply Side Effects of Fiscal Policy

Skill: Conceptual

Source: Study Guide

AACSB: Reflective Thinking

19) Suppose that in China, investment is \$400 billion, saving is \$400 billion, tax revenues are \$500 billion, exports are \$300 billion, and imports are \$200 billion. The government budget \_\_\_\_\_ the supply of loanable funds, which \_\_\_\_\_ the real interest rate and \_\_\_\_\_ investment.

- A) surplus increases; lowers; decreases
- B) surplus decreases; raises; increases
- C) surplus increases; lowers; increases
- D) deficit decreases; raises; decreases
- E) surplus increases; raises; decreases

Answer: C

Diff: 2 Type: MC

Topic: Supply Side Effects of Fiscal Policy

Source: MyEconLab

20) Suppose that in China, investment is \$400 billion, saving is \$400 billion, tax revenues are \$500 billion, exports are \$300 billion, and imports are \$200 billion. \_\_\_\_\_ in government expenditure or \_\_\_\_\_ in taxes will further increase China's budget \_\_\_\_\_, increase investment and speed economic growth.

- A) A decrease; an increase; surplus
- B) An increase; a decrease; deficit
- C) An increase; an increase; surplus
- D) A decrease; a decrease; deficit
- E) A decrease; an increase; deficit

Answer: A

Diff: 2 Type: MC

Topic: Supply Side Effects of Fiscal Policy

Source: MyEconLab

21) The government is proposing to increase the tax rate on labour income and asks you to report on the supply-side effects of such an action. According to the research of Edward C. Prescott, cross-country evidence for Canada, the United States, the United Kingdom, and France shows all of the following *except* \_\_\_\_\_.

A) the greater the tax wedge, the smaller the level of employment and the smaller the potential GDP

B) potential GDP per person in France is 14 percent below that of the United States (per person) and the entire difference can be attributed to the difference in the tax wedge in the two countries

C) potential GDP per person in the United Kingdom is 41 percent below that of the United States (per person) and about a third of the difference arises from the different tax wedges

D) between Canada, the United States, France, and the United Kingdom, the tax wedge is greatest in the United Kingdom, and the country with the smallest tax wedge has the smallest potential GDP

E) potential GDP per person in Canada is 16 percent below that of the United States but this difference is due to different productivities

Answer: D

Diff: 2 Type: MC

Topic: Supply Side Effects of Fiscal Policy

Source: MyEconLab

22) The government increases the tax rate on labour income and at the same time cuts the rate of sales tax to keep the amount of tax collected constant. As a result, the supply of labour \_\_\_\_\_, the demand for labour \_\_\_\_\_, and the equilibrium level of employment \_\_\_\_\_. The before-tax wage rate \_\_\_\_\_, and the after-tax wage rate \_\_\_\_\_. Potential GDP \_\_\_\_\_.

A) decreases; does not change; decreases; rises; falls; decreases

B) decreases; increases; does not change; rises; falls; does not change

C) does not change; does not change; does not change; does not change; does not change; does not change

D) decreases; decreases; decreases; rises; falls; decreases

E) does not change; increases; increases; does not change; decreases; increases

Answer: C

Diff: 2 Type: MC

Topic: Supply Side Effects of Fiscal Policy

Source: MyEconLab

23) The government increases the tax rate on labour income. As a result, the supply of labour \_\_\_\_\_ and the demand for labour \_\_\_\_\_. The equilibrium level of employment \_\_\_\_\_.

A) decreases; increases; does not change

B) does not change; decreases; decreases

C) increases; does not change; decreases

D) decreases; decreases; decreases

E) does not change; decreases; decreases

Answer: C

Diff: 2 Type: MC

Topic: Supply Side Effects of Fiscal Policy

Source: MyEconLab

24) The government increases the tax rate on labour income. At the equilibrium level of employment, the before-tax wage rate \_\_\_\_\_ and the after-tax wage rate \_\_\_\_\_. Potential GDP \_\_\_\_\_.

- A) rises; falls; decreases
- B) falls; rises; does not change
- C) rises; falls; does not change
- D) falls; rises; decreases
- E) rises; falls; increases

Answer: A

Diff: 2 Type: MC

Topic: Supply Side Effects of Fiscal Policy

Source: MyEconLab

25) A tax on interest income \_\_\_\_\_.

- A) decreases the demand for loanable funds but does not change the real interest rate
- B) increases the demand for loanable funds and raises the real interest rate
- C) increases the supply of loanable funds and lowers the real interest rate
- D) decreases the supply of loanable funds and has no influence on the real interest rate
- E) has no effect on the demand for loanable funds

Answer: E

Type: MC

26) A tax on labour income \_\_\_\_\_.

- A) decreases the demand for labour but does not change the real wage rate
- B) increases the demand for labour and raises the real wage rate
- C) increases the supply of labour and lowers the real wage rate
- D) decreases the supply of labour and has no influence on the real wage rate
- E) has no effect on the demand for labour

Answer: E

Type: MC

### 29.3 Fiscal Stimulus

1) Currently the government of Ricardia has outlays equal to \$100 billion, and a tax scheme that is related positively to real GDP by the following equation:  $\text{Taxes} = \$25 \text{ billion} + 0.1(\text{real GDP})$ .

What are autonomous taxes in Ricardia?

- A) It depends on the level of real GDP.
- B) 0.1
- C) \$2.5 billion
- D) \$250 billion
- E) \$25 billion

Answer: E

Diff: 2 Type: MC

Topic: Fiscal Stimulus

2) Currently the government of Ricardia has outlays equal to \$100 billion, and a tax scheme that is related positively to real GDP by the following equation:  $\text{Taxes} = \$25 \text{ billion} + 0.1(\text{real GDP})$ . What is the real GDP when the government has a balanced budget?

- A) \$100
- B) \$250
- C) \$1,250 billion
- D) \$750 billion
- E) \$1,000 billion

Answer: D

Diff: 2 Type: MC

Topic: Fiscal Stimulus

3) If the economy is in a recession, and the government has a budget deficit, then there

- A) must be a structural deficit.
- B) must be a structural surplus.
- C) may be a structural deficit, but not a structural surplus.
- D) may be a structural surplus, but not a structural deficit.
- E) may be either a structural surplus or deficit.

Answer: E

Diff: 3 Type: MC

Topic: Fiscal Stimulus

4) The structural deficit is the deficit

- A) in a recession.
- B) in an expansion.
- C) that would occur at potential GDP.
- D) caused by the business cycle.
- E) that would occur at the trough of the business cycle.

Answer: C

Diff: 1 Type: MC

Topic: Fiscal Stimulus

- 5) The cyclical deficit
- A) is a persistent economic phenomenon.
  - B) occurs when the economy is at full employment.
  - C) arises purely because real GDP does not equal potential GDP.
  - D) is an accumulation of the government debt.
  - E) none of the above.

Answer: C

Diff: 1 Type: MC

Topic: Fiscal Stimulus

- 6) Norland has the budget deficit of \$15 billion. According to the government economists, Norland has a structural deficit of \$3 billion. What is a cyclical deficit in Norland?

- A) \$18 billion
- B) \$15 billion
- C) \$10 billion
- D) \$12 billion
- E) zero

Answer: D

Diff: 1 Type: MC

Topic: Fiscal Stimulus

- 7) Everything else remaining the same, as the economy enters a recession,

- A) tax revenues rise and interest payments on the debt rise.
- B) tax revenues and transfer payments rise.
- C) government outlays rise and tax revenues fall.
- D) government outlays tend to fall and tax revenues fall.
- E) interest payments on the debt rise and tax revenues fall.

Answer: C

Diff: 1 Type: MC

Topic: Fiscal Stimulus

- 8) Everything else remaining the same, as the economy enters an expansion,

- A) tax revenues rise and transfer payments fall.
- B) tax revenues and transfer payments fall.
- C) tax revenues and transfer payments rise.
- D) tax revenues fall and transfer payments remain constant.
- E) transfer payments and interest on the debt rise.

Answer: A

Diff: 1 Type: MC

Topic: Fiscal Stimulus

9) If the economy is in an expansion, and the federal government is running a deficit, then a recession would automatically

- A) decrease the deficit.
- B) increase taxes.
- C) increase government outlays.
- D) increase the deficit.
- E) C and D.

Answer: E

Diff: 2 Type: MC

Topic: Fiscal Stimulus

10) If the economy is in a recession and the federal government is running a deficit, then an expansion would

- A) automatically balance the budget.
- B) automatically increase the deficit.
- C) automatically decrease the deficit.
- D) leave the deficit unchanged.
- E) increase the deficit only if the interest rate rises.

Answer: C

Diff: 2 Type: MC

Topic: Fiscal Stimulus

11) Consider the economy of NoTax, where the multiplier is 2.5. If the government desires to shift the *AD* curve rightward by \$5 billion, the correct increase in government expenditure is

- A) \$2 billion.
- B) \$2.5 billion.
- C) \$3 billion.
- D) \$7.5 billion.
- E) \$8.33 billion.

Answer: A

Diff: 3 Type: MC

Topic: Fiscal Stimulus

Source: Study Guide

12) A cyclical deficit occurs when

- A) government outlays are greater than revenues.
- B) government outlays are less than revenues.
- C) there is a deficit due to the fact real GDP is greater than potential GDP.
- D) there is a deficit due to the fact real GDP is less than potential GDP.
- E) there is a deficit even when real GDP equals potential GDP.

Answer: D

Diff: 2 Type: MC

Topic: Fiscal Stimulus

Source: Study Guide

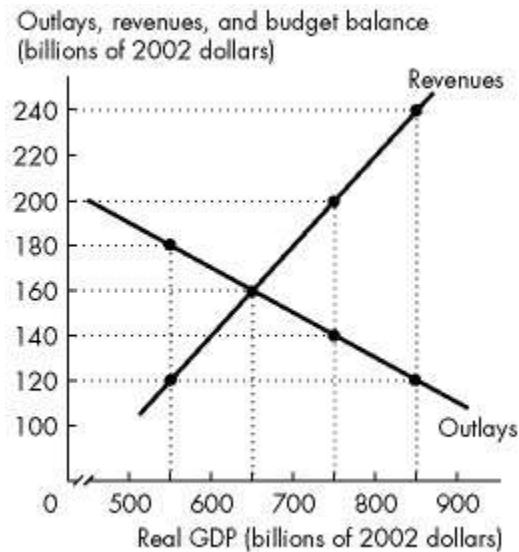
- 13) A structural deficit  
 A) is present only if real GDP is greater than potential.  
 B) exists even if real GDP equals potential.  
 C) equals the cyclical deficit plus the actual deficit.  
 D) is greater than a cyclical deficit.  
 E) none of the above.

Answer: B

Diff: 2 Type: MC

Topic: Fiscal Stimulus

Use the figure below to answer the following questions.



**Figure 29.3.1**

- 14) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. The budget is balanced when real GDP equals \_\_\_\_\_.

- A) \$550 billion  
 B) \$600 billion  
 C) \$650 billion  
 D) \$700 billion  
 E) \$750 billion

Answer: C

Diff: 2 Type: MC

Topic: Fiscal Stimulus

15) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. If real GDP equals \$550 billion, the budget is

- A) in balance.
- B) a surplus of \$60 billion.
- C) a surplus of \$40 billion.
- D) a deficit of \$60 billion.
- E) a deficit of \$40 billion.

Answer: D

Diff: 2 Type: MC

Topic: Fiscal Stimulus

16) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. If real GDP equals \$550 billion, the structural deficit is

- A) zero.
- B) \$60 billion.
- C) a surplus of \$60 billion.
- D) a surplus of \$40 billion.
- E) unknown given the available information.

Answer: E

Diff: 2 Type: MC

Topic: Fiscal Stimulus

17) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. If potential GDP is \$750 billion,

- A) neither a structural surplus nor a structural deficit exists.
- B) the structural deficit is \$60 billion.
- C) the structural deficit is \$40 billion.
- D) the structural surplus is \$60 billion.
- E) the structural surplus is \$40 billion.

Answer: D

Diff: 2 Type: MC

Topic: Fiscal Stimulus

18) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. If potential GDP is \$750 billion, and actual real GDP is \$650 billion, the cyclical deficit is

- A) zero.
- B) \$60 billion.
- C) \$40 billion.
- D) equal to the structural deficit.
- E) \$180 billion.

Answer: B

Diff: 3 Type: MC

Topic: Fiscal Stimulus

19) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. Automatic fiscal policy would be shown as a movement

- A) from right to left along the revenues curve.
- B) from left to right along the revenues curve.
- C) from right to left along the outlays curve.
- D) from left to right along the outlays curve.
- E) all of the above.

Answer: E

Diff: 3 Type: MC

Topic: Fiscal Stimulus

20) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. Discretionary fiscal policy would be shown as a movement

- A) from right to left along the revenues curve.
- B) from left to right along the revenues curve.
- C) from right to left along the outlays curve.
- D) from left to right along the outlays curve.
- E) none of the above.

Answer: E

Diff: 2 Type: MC

Topic: Fiscal Stimulus

21) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. A discretionary fiscal restraint policy would be shown as

- A) a movement from left to right along the revenues curve.
- B) a movement from left to right along the outlays curve.
- C) an upward shift of the revenues curve.
- D) an upward shift of the outlays curve.
- E) both A and C.

Answer: C

Diff: 3 Type: MC

Topic: Fiscal Stimulus

22) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. Discretionary expansionary fiscal policy would be shown as

- A) a movement from left to right along the revenues curve.
- B) a movement from left to right along the outlays curve.
- C) an upward shift of the revenues curve.
- D) an upward shift of the outlays curve.
- E) both A and C.

Answer: D

Diff: 3 Type: MC

Topic: Fiscal Stimulus

23) Refer to Figure 29.3.1, which shows the outlays and revenues for the government of Pianoland. An automatic increase in tax revenues would be shown as a

- A) movement from left to right along the revenues curve.
- B) movement from left to right along the outlays curve.
- C) shift upwards in the revenues curve.
- D) shift upwards in the the outlays curve.
- E) both A and C.

Answer: A

Diff: 2 Type: MC

Topic: Fiscal Stimulus

24) Automatic fiscal policy

- A) requires action by Parliament.
- B) is triggered by the state of the economy.
- C) involves only a change in government outlays and no change in revenues.
- D) involves only a change in personal income tax rates.
- E) occurs during recessions but not during expansions.

Answer: B

Diff: 1 Type: MC

Topic: Fiscal Stimulus

25) Discretionary fiscal policy

- A) requires action by Parliament.
- B) is triggered by the state of the economy.
- C) involves only a change in government outlays and no change in revenues.
- D) involves only a change in personal income tax rates.
- E) occurs during recessions but not during expansions.

Answer: A

Diff: 1 Type: MC

Topic: Fiscal Stimulus

26) Which one of the following happens automatically if the economy goes into a recession?

- A) Government outlays increase and revenues do not change.
- B) Revenues decrease and government outlays do not change.
- C) The government budget deficit increases or the government budget surplus decreases.
- D) The government budget deficit decreases.
- E) Both government outlays and revenues increase, and the deficit stays the same.

Answer: C

Diff: 1 Type: MC

Topic: Fiscal Stimulus

Source: Study Guide

- 27) During an expansion, revenues  
A) and government outlays decrease.  
B) decrease and government outlays increase.  
C) increase and government outlays decrease.  
D) and government outlays increase.  
E) remain constant and government outlays increase.

Answer: C

Diff: 1 Type: MC

Topic: Fiscal Stimulus

Source: Study Guide

- 28) During a recession, revenues  
A) and government outlays decrease.  
B) decrease and government outlays increase.  
C) increase and government outlays decrease.  
D) and government outlays increase.  
E) remain constant and government outlays increase.

Answer: B

Diff: 1 Type: MC

Topic: Fiscal Stimulus

- 29) Which of the following is an example of a fiscal policy designed to counter a recessionary gap?

- A) increasing debt interest payments  
B) increasing taxes  
C) decreasing transfer payments  
D) increasing transfer payments  
E) decreasing government expenditures on goods and services

Answer: D

Diff: 1 Type: MC

Topic: Fiscal Stimulus

Source: Study Guide

- 30) Which of the following is an example of a fiscal restraint policy?

- A) increasing government expenditure  
B) increasing taxes  
C) cutting transfer payments  
D) A and B  
E) B and C

Answer: E

Diff: 1 Type: MC

Topic: Fiscal Stimulus

- 31) Expansionary fiscal policy
- A) increases aggregate demand.
  - B) decreases aggregate demand.
  - C) increases short-run aggregate supply.
  - D) increases long-run aggregate supply.
  - E) A, C, and D are correct.

Answer: A

Diff: 2 Type: MC

Topic: Fiscal Stimulus

32) The effect of a change in taxes is less than the same sized change in government expenditure because

- A) the amount by which consumption initially changes is equal to  $MPC$  times the tax change.
- B) some people do not pay their taxes.
- C) changes in government expenditure do not directly affect consumption.
- D) tax rates are the same regardless of income levels.
- E) none of the above.

Answer: A

Type: MC

Topic: Fiscal Stimulus

Skill: Conceptual

AACSB: Reflective Thinking

33) An advantage of automatic stabilizers over discretionary fiscal policy is that

- A) automatic stabilizers are not subject to all the same time lags that discretionary fiscal policy is.
- B) automatic stabilizers can be easily fine-tuned to move the economy to full employment.
- C) only Parliament is involved in implementing automatic stabilizers instead of both Parliament and the Bank of Canada.
- D) automatic stabilizers require only a simple majority of Parliament to pass whereas discretionary fiscal policy requires a two-thirds majority to pass.
- E) automatic stabilizers work in recessions and expansions but discretionary fiscal policy works only in a recession.

Answer: A

Type: MC

Topic: Fiscal Stimulus

Skill: Conceptual

AACSB: Reflective Thinking

34) If the budget deficit is \$50 billion and the structural deficit is \$10 billion, the cyclical deficit is

- A) \$10 billion.
- B) \$40 billion.
- C) \$60 billion.
- D) \$50 billion
- E) \$20 billion.

Answer: B

Type: MC

Topic: Fiscal Stimulus

Skill: Analytical

AACSB: Analytical Skills

35) If the economy has a structural deficit of \$25 billion and a cyclical deficit of \$75, we can conclude that the current budget deficit is \_\_\_\_\_ billion.

- A) \$25
- B) \$50
- C) \$75
- D) \$100
- E) \$125

Answer: D

Type: MC

Topic: Fiscal Stimulus

Skill: Analytical

AACSB: Analytical Skills

36) When real GDP equals potential GDP of \$12 trillion, the budget deficit is \$1 trillion. Real GDP actually equals \$14 trillion and the budget surplus is \$3 trillion. The economy has a structural \_\_\_\_\_ and a cyclical \_\_\_\_\_.

- A) deficit of \$1 trillion; surplus of \$4 trillion
- B) deficit of \$1 trillion; surplus of \$2 trillion
- C) surplus of \$4 trillion; deficit of \$1 trillion
- D) surplus of \$3 trillion; surplus of \$2 trillion
- E) deficit of \$4 trillion; surplus of \$1 trillion

Answer: A

Type: MC

Topic: Fiscal Stimulus

Skill: Analytical

Source: MyEconLab

AACSB: Analytical Skills

37) Choose the correct statement.

- A) Contractionary fiscal policy can eliminate inflationary pressure.
- B) Eliminating an inflationary gap is very simple - calculate the size of the gap and the size of the multiplier, then change government expenditure for an immediate decrease in real GDP.
- C) When an economy is in an above full-employment equilibrium, an equal decrease in government expenditure and autonomous taxes cannot return the economy to full employment.
- D) When an economy is in an above full-employment equilibrium, an increase in taxes will decrease aggregate demand, but because the autonomous tax multiplier is smaller than the government expenditure multiplier, the economy will not return to potential GDP.
- E) All of the above.

Answer: A

Type: MC

Topic: Fiscal Stimulus

Skill: Analytical

Source: MyEconLab

AACSB: Analytical Skills

38) The economy is in a recession and the recessionary gap is large. Discretionary fiscal policy that might occur is \_\_\_\_\_. Automatic fiscal policy that might occur is \_\_\_\_\_. A discretionary fiscal stimulation package that would avoid a budget deficit is a simultaneous and equal \_\_\_\_\_.

- A) an increase in transfer payments and a fall in taxes; an increase in government expenditure and a cut in taxes; increase in transfer payments and taxes
- B) a decrease in transfer payments and an increase in taxes; a decrease in government expenditure and an increase in taxes; decrease in transfer payments and taxes
- C) an increase in government expenditure and a cut in taxes; an increase in transfer payments and a fall in taxes; increase in government expenditure and taxes
- D) a decrease in government expenditure and an increase in taxes; a decrease in transfer payments and an increase in taxes; decrease in government expenditure and taxes
- E) none of the above

Answer: C

Type: MC

Topic: Fiscal Stimulus

Skill: Analytical

Source: MyEconLab

AACSB: Analytical Skills

39) If real GDP is less than potential GDP, which of the following fiscal policies would increase real GDP?

- A) a decrease in taxes
- B) an increase in government expenditures
- C) a fall in the interest rate
- D) Both A and B are correct
- E) Both B and C are correct.

Answer: D

Type: MC

40) The use of fiscal policy is limited because

- A) of recognition lag.
- B) of law-making lag.
- C) of impact lag.
- D) all of the above
- E) none of the above

Answer: D

Type: MC

41) Choose the correct statement.

- A) Tax cuts increase aggregate supply and aggregate demand.
- B) Tax cuts strengthen the incentive to work and to invest.
- C) The tax multiplier becomes smaller as time passes.
- D) According to Barro and Uhlig, tax cuts are a less powerful way to stimulate real GDP than spending increases.
- E) Both A and B are correct.

Answer: E

Type: MC

42) In 2011, Canada had \_\_\_\_\_.

- A) a structural deficit and a cyclical deficit
- B) a structural deficit and a cyclical surplus
- C) a structural surplus and a cyclical deficit
- D) a structural surplus and a cyclical surplus
- E) a balanced structural budget and a cyclical deficit

Answer: A

Type: MC

43) Which of the following policies shifts the *AD* curve the farthest leftward?

- A) a decrease in government expenditure of \$10 billion
- B) an increase in taxes of \$10 billion
- C) a decrease in taxes of \$10 billion
- D) an increase in government expenditure of \$10 billion
- E) a simultaneous increase in government expenditure of \$10 billion and taxes of \$10 billion

Answer: A

Type: MC

## Chapter 30 Monetary Policy

### 30.1 Monetary Policy Objectives and Framework

1) Core inflation is the percentage change in

- A) the Consumer Price Index including the eight most volatile prices.
- B) an inflation rate that ranges between 1 percent and 3 percent annually.
- C) the Consumer Price Index excluding the eight most volatile prices.
- D) the average of the 8 most volatile prices in the Consumer Price Index.
- E) the target midpoint inflation rate of 2 percent per year.

Answer: C

Diff: 1 Type: MC

Topic: Monetary Policy Objective and Framework

2) How is responsibility for monetary policy set forth in Canada?

A) The Canadian Government administers monetary policy through the office of the Minister of Finance.

B) The Bank of Canada administers monetary policy as directed by the Minister of Finance.

C) The Bank of Canada Act places responsibility for the conduct of monetary policy on the Bank's Governing Council.

D) The Prime Minister bears ultimate responsibility for monetary policy.

E) Both B and D.

Answer: C

Diff: 1 Type: MC

Topic: Monetary Policy Objective and Framework

3) Which of the following benefits flow from the application of an inflation-control target?

A) If actual inflation exceeds the target range, the Bank of Canada can induce a recession to correct the matter.

B) The monetary authorities can change the target range whenever they feel it is appropriate.

C) People can make decisions with an understanding that inflation rates will remain relatively low.

D) Financial market traders have a clearer understanding of the Bank of Canada's intentions.

E) Both C and D.

Answer: E

Diff: 1 Type: MC

Topic: Monetary Policy Objective and Framework

4) Which of the following issues is a concern that critics express about the use of an inflation-control target?

A) The policy control rests in the hands of civil servants rather than in the hands of elected officials.

B) The policy control rests in the hands of elected officials rather than in the hands of civil servants.

C) It encourages a focus on real GDP growth at the expense of employment and of inflation.

D) It encourages a focus on inflation at the expense of employment and real GDP growth.

E) Monetary policy tends to be sensitive to the state of employment while focusing on inflation control targets.

Answer: D

Diff: 1 Type: MC

Topic: Monetary Policy Objective and Framework

5) Who are the members of the Bank of Canada's Governing Council?

A) The Ministers of Finance from each province as well as the Federal Minister of Finance.

B) The Prime Minister, the Minister of Finance, and the Bank's Governor.

C) The Minister of Finance, the Governor, and four Deputy Governors.

D) The Bank's Governor, Senior Deputy Governor, and four Deputy governors who are appointed by the Prime Minister to represent the public interest.

E) The Bank's Governor, Senior Deputy Governor, and four Deputy Governors.

Answer: E

Diff: 1 Type: MC

Topic: Monetary Policy Objective and Framework

6) How is consultation between the Bank of Canada and the Government of Canada on monetary policy arranged?

A) Consultations are arranged at the discretion of the Minister of Finance.

B) No consultation is required or needed.

C) The Bank of Canada Act requires regular consultations between the Governor and the Minister of Finance.

D) Consultations are arranged at the discretion of the Governor of the Bank of Canada.

E) Consultations are arranged through the Parliamentary Committee on Finance.

Answer: C

Diff: 1 Type: MC

Topic: Monetary Policy Objective and Framework

7) Why does the Bank of Canada pay close attention to the core inflation rate in addition to the overall CPI inflation rate?

- A) The core rate is more volatile and therefore a better predictor of trend inflation.
- B) The core rate includes taxes, while the overall CPI rate does not.
- C) The core rate has a lower average value and therefore makes the Bank look better.
- D) The core rate is less volatile and a better predictor of future CPI inflation.
- E) The core rate excludes eight volatile prices and is therefore more likely to stay within the target band.

Answer: D

Type: MC

Topic: Monetary Policy Objective and Framework

Source: Study Guide

8) One criticism of the Bank of Canada's focus on an inflation control target is that

- A) if inflation falls below the target range a recession will result.
- B) if inflation edges above the target range, the Bank decreases aggregate demand and could create a recession.
- C) the Bank pays too much attention to unemployment and real GDP growth and not enough to inflation control.
- D) it makes setting expectations of inflation difficult.
- E) the Bank rarely achieves its target.

Answer: B

Type: MC

Topic: Monetary Policy Objective and Framework

Source: Study Guide

9) The objective of the Bank of Canada's monetary policy is

- A) to keep the unemployment rate below 5 percent, the inflation rate between 1 and 3 percent a year, and long-term real GDP growth above 4 percent a year.
- B) to control the quantity of money and interest rates to avoid inflation and when possible prevent excessive swings in real GDP growth and unemployment.
- C) to keep the unemployment rate below 5 percent, the inflation rate between 1 and 3 percent a year, and long-term interest rates below 4 percent a year.
- D) to keep the labour force participation rate above 80 percent, the inflation rate below 2 percent a year, and the exchange rate fluctuating by less than 3 percent a year.
- E) to keep the overnight loans rate below 2 percent a year and the unemployment rate at its natural rate.

Answer: B

Type: MC

Topic: Monetary Policy Objective and Framework

Source: MyEconLab

10) The two parts of the inflation-control target are that the inflation-control target range will be \_\_\_\_\_ percent a year, and policy will aim at keeping the trend of inflation at \_\_\_\_\_ percent a year.

- A) 3 to 5; 4
- B) 1 to 3; 2
- C) 2 to 4; 3
- D) 0 to 2; 1
- E) -1 to 1; 0

Answer: B

Type: MC

Topic: Monetary Policy Objective and Framework

Source: MyEconLab

11) Choose the statement that is *incorrect*.

- A) The actual path of the CPI was on trend from 1995 through 1998.
- B) Between 1999 and 2001, the CPI moved below the 2 percent trend line.
- C) The actual path of the CPI was below trend from 2001 through 2007.
- D) The Bank of Canada and the Government of Canada agree that the inflation-control target range will be 1 percent to 3 percent.
- E) All of the above statements are incorrect.

Answer: C

Type: MC

12) The current Governor of the Bank of Canada is

- A) Stephen Harper.
- B) Mark Carney.
- C) David Dodge.
- D) Paul Martin.
- E) Ben Bernanke.

Answer: B

Type: MC

## 30.2 The Conduct of Monetary Policy

1) As the sole issuer of Canadian money, the Bank of Canada can set any one of three variables:

- A) the monetary base, the exchange rate, and the short-term interest rate.
- B) the money base, the interest rate, and the unemployment rate.
- C) the rate of inflation, the interest rate, and the unemployment rate.
- D) the exchange rate, the interest rate, and the inflation rate.
- E) the inflation rate, the unemployment rate, and the real economic growth rate.

Answer: A

Diff: 1 Type: MC

Topic: The Conduct of Monetary Policy

2) What is the overnight loans rate?

- A) The percentage change in the volume of loans that take place overnight.
- B) The interest rate that the Bank of Canada charges chartered banks.
- C) The interest rate on loans that the big banks make to each other.
- D) The volume of loans that take place during the night.
- E) The interest rate that the Bank of Canada pays when it buys securities from chartered banks.

Answer: C

Diff: 1 Type: MC

Topic: The Conduct of Monetary Policy

3) How can the Bank of Canada use the bank rate to regulate the overnight loans rate?

- A) The overnight loans rate is set at a quarter percentage point above the bank rate, which in turn is set by the Bank of Canada.
- B) The bank rate is set at the settlement balances rate plus 0.25 percentage points.
- C) The bank rate is set at 0.25 percentage points below the settlement balances rate, which is used to determine the overnight loans rate.
- D) The overnight loans rate is set at 25 basis points above the bank rate.
- E) The bank rate is set at the target overnight rate plus 0.25 percentage points.

Answer: E

Diff: 2 Type: MC

Topic: The Conduct of Monetary Policy

4) 25 basis points is

- A) a quarter of a percentage point.
- B) a quarter of the Bank of Canada's target inflation rate.
- C) the spread between the savings rate and the lending rate.
- D) the spread between the bank rate and the settlement balances rate.
- E) the gap by which real GDP exceeds potential GDP.

Answer: A

Diff: 1 Type: MC

Topic: The Conduct of Monetary Policy

- 5) The operating band is
- A) the interest rate that is established through an open market operation.
  - B) the target overnight interest rate plus or minus 25 basis points.
  - C) the target inflation rate plus or minus a quarter of a percentage point.
  - D) a half percentage point range in the target inflation rate.
  - E) the range between the lending rate and the borrowing rate.

Answer: B

Diff: 1 Type: MC

Topic: The Conduct of Monetary Policy

- 6) The settlement balances rate is the
- A) proportion of outstanding loans from chartered banks that are resolved.
  - B) interest rate that the Bank of Canada charges the big banks on loans.
  - C) interest rate paid to chartered banks on their reserves held at the Bank of Canada.
  - D) ratio of the value securities sold by the Bank of Canada to securities outstanding.
  - E) proportion of overnight inter-bank loans that are resolved.

Answer: C

Diff: 1 Type: MC

Topic: The Conduct of Monetary Policy

- 7) The policy tools used by the Bank of Canada include
- A) prime rate and bank rate.
  - B) the operating band and open market operations.
  - C) open market operations and prime rate.
  - D) prime rate and the exchange rate.
  - E) the exchange rate and open market operations.

Answer: B

Diff: 2 Type: MC

Topic: The Conduct of Monetary Policy

- 8) How does the Bank of Canada set the bank rate?
- A) The Bank of Canada does not determine the bank rate.
  - B) The bank rate is set at a quarter percentage point above the prime lending rate.
  - C) The bank rate is set at a quarter percentage point above the target overnight loans rate.
  - D) The bank rate is set at a quarter percentage point below the overnight loans rate.
  - E) The bank rate is set at 25 basis points above the operating band.

Answer: C

Diff: 2 Type: MC

Topic: The Conduct of Monetary Policy

9) An open market operation

A) refers to the Bank of Canada's sales and purchases of corporate stock.

B) can change bank deposits but cannot alter the quantity of money.

C) is the purchase or sale of government of Canada securities by the Bank of Canada from or to a chartered bank or the public.

D) refers to loans made by the Bank of Canada to chartered banks.

E) refers to the purchase or sale of Canadian currency in exchange for foreign currency.

Answer: C

Diff: 1 Type: MC

Topic: The Conduct of Monetary Policy

10) The bank rate is the interest rate

A) banks charge their very best loan customers.

B) banks pay on term deposits.

C) the Bank of Canada pays on reserves held by banks.

D) the Bank of Canada charges when it lends reserves to the big banks.

E) received for holding Government of Canada Treasury Bills.

Answer: D

Diff: 1 Type: MC

Topic: The Conduct of Monetary Policy

Source: Study Guide

11) The overnight loans rate is the interest rate

A) banks charge their best loan customers.

B) banks pay on term deposits.

C) the Bank of Canada pays on reserves held by banks.

D) the Bank of Canada charges when it lends reserves to banks.

E) on overnight loans that the big banks make to each other.

Answer: E

Diff: 2 Type: MC

Topic: The Conduct of Monetary Policy

12) The Bank of Canada can lower the overnight loans rate by

A) raising the bank rate.

B) lowering the bank rate.

C) raising the settlement balances rate.

D) lowering the settlement balances rate.

E) both B and D.

Answer: E

Diff: 2 Type: MC

Topic: The Conduct of Monetary Policy

13) The sale of government bonds by the Bank of Canada

- A) lowers interest rates.
- B) decreases bank reserves.
- C) increases the quantity of money.
- D) increases the banks' loans to the public.
- E) increases bank reserves.

Answer: B

Diff: 2 Type: MC

Topic: The Conduct of Monetary Policy

14) The purchase of government bonds by the Bank of Canada

- A) decreases bank reserves.
- B) increases bank loans.
- C) decreases the price of bonds.
- D) fights inflation.
- E) tightens credit conditions.

Answer: B

Diff: 2 Type: MC

Topic: The Conduct of Monetary Policy

15) If the Bank of Canada aims to lower the overnight rate, it will

- A) lower the bank rate and settlement balances rate, as well as buy government securities.
- B) lower the bank rate, increase the settlement balances rate, as well as buy government securities.
- C) lower the bank rate and settlement balances rate, as well as sell government securities.
- D) raise the bank rate and settlement balances rate, as well as buy government securities.
- E) raise the bank rate and settlement balances rate, as well as sell government securities.

Answer: A

Type: MC

Topic: The Conduct of Monetary Policy

Source: Study Guide

16) In an open market operation aimed at increasing expenditure, the Bank of Canada

- A) sells government bonds, decreasing bank reserves, decreasing lending, decreasing the overnight rate.
- B) sells government bonds, decreasing bank reserves, decreasing lending, increasing the overnight rate.
- C) sells government bonds, decreasing bank reserves, increasing lending, increasing the overnight rate.
- D) buys government bonds, increasing bank reserves, increasing lending, decreasing the overnight rate.
- E) buys government bonds, increasing bank reserves, increasing lending, increasing the overnight rate.

Answer: D

Type: MC

Topic: The Conduct of Monetary Policy

Source: Study Guide

- 17) The current overnight loans rate is 3 percent, with the Bank of Canada's operating band set at 2.75 to 3.25 percent. If the Bank of Canada lowers their operating band to 2.25 to 2.75 percent, which of the following is one of the reasons the overnight rate will fall to within this new range?
- A) Since the banking system can now borrow from the Bank of Canada at 2.75 percent, no bank would borrow on the overnight loan market at 3 percent.
  - B) Since the banking system can now borrow from the Bank of Canada at 2.25 percent, no bank would borrow on the overnight loan market at 3 percent.
  - C) Since the banking system can now earn 2.75 percent from the Bank of Canada, no bank would lend on the overnight loan market at 3 percent.
  - D) Since the banking system can now earn 2.25 percent from the Bank of Canada, no bank would lend on the overnight loan market at 3 percent.
  - E) There is a legal requirement that the overnight rate must be within the Bank of Canada's operating band.

Answer: A

Type: MC

Topic: The Conduct of Monetary Policy

Source: Study Guide

- 18) The overnight rate is determined by equilibrium in the market for \_\_\_\_\_. The overnight rate \_\_\_\_\_.

- A) loanable funds; equals the real interest rate minus the inflation rate
- B) reserves; is the rate that sets the quantity of reserves demanded equal to the quantity of reserves supplied
- C) loanable funds; equals the real interest rate
- D) reserves; equals the real interest rate minus the inflation rate
- E) money; equals the real interest rate

Answer: B

Type: MC

Topic: The Conduct of Monetary Policy

Source: MyEconLab

- 19) Choose the statement that is *incorrect*.

- A) The Bank of Canada's choice of policy instrument is the overnight loans rate.
- B) When the Bank of Canada wants to slow inflation, it raises the overnight loans rate.
- C) The Bank has established 12 fixed dates each year on which it announces its overnight rate target for the coming period.
- D) Recently, the overnight loans rate has been at historically low levels because the Bank is leaning in the direction of avoiding recession.
- E) The overnight rate was a bit more than 8 percent a year in 1995.

Answer: C

Type: MC

20) If the overnight rate is above target, the Bank \_\_\_\_\_ securities to \_\_\_\_\_ reserves, which \_\_\_\_\_ the supply of overnight funds and \_\_\_\_\_ the overnight rate.

- A) buys; increase; decreases; raises
- B) sells; increase; increases; lowers
- C) buys; decrease; decreases; raises
- D) sells; decrease; decreases; raises
- E) buys; increase; increases; lowers

Answer: E

Type: MC

21) If the overnight rate is below target, the Bank \_\_\_\_\_ securities to \_\_\_\_\_ reserves, which \_\_\_\_\_ the supply of overnight funds and \_\_\_\_\_ the overnight rate.

- A) buys; increase; decreases; raises
- B) sells; increase; increases; lowers
- C) buys; decrease; decreases; raises
- D) sells; decrease; decreases; raises
- E) buys; increase; increases; lowers

Answer: D

Type: MC

### 30.3 Monetary Policy Transmission

1) If the Bank of Canada buys government bonds, all of the following happens *except*

- A) bank reserves increase.
- B) the quantity of money increases.
- C) the supply of loanable funds increases.
- D) the bank rate rises.
- E) net exports increase.

Answer: D

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

2) Which of the following quotations *correctly* describes the impact of monetary policy on the economy?

- A) "House sales are down lots, due to the higher money growth."
- B) "The extra money pumped into the economy by the central bank is creating less exports."
- C) "The tightening of money growth is helping sell goods abroad."
- D) "Businesses are investing more, now that monetary policy has become less expansionary."
- E) "The extra money pumped into the economy by the central bank is creating more jobs."

Answer: E

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

3) Which of the following quotations *correctly* describes the impact of monetary policy on the economy?

- A) "House sales are down lots, due to the higher money growth."
- B) "The extra money pumped into the economy by the central bank is creating more exports."
- C) "The tightening of money growth is helping sell goods abroad."
- D) "Businesses are investing more, now that monetary policy has become less expansionary."
- E) "The extra money pumped into the economy by the central bank is creating fewer jobs."

Answer: B

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

4) Monetary policy is difficult to conduct because

- A) the monetary policy transmission process is long and drawn out.
- B) the tools available don't work.
- C) politicians frequently block the policy's intended outcomes.
- D) the interest rate always rises.
- E) it takes several years for the real GDP growth rate to respond to a change in the interest rate.

Answer: A

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

5) To lower interest rates, the Bank of Canada can

- A) increase the treasury bill rate.
- B) raise the exchange rate.
- C) buy government securities.
- D) decrease bank reserves.
- E) raise the bank rate.

Answer: C

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

6) To decrease aggregate demand, the Bank of Canada can

- A) raise the overnight loans rate, which decreases the quantity of money.
- B) lower the overnight loans rate, which increases the quantity of money.
- C) lower the overnight loans rate, which decreases the quantity of money.
- D) raise the overnight loans rate, which increases the quantity of money.
- E) raise the overnight loans rate, which decreases the government budget deficit.

Answer: A

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

7) Which of the following statements *correctly* describes an anti-inflationary monetary policy?

- A) "The Bank of Canada's recent purchases of government securities is stimulating the housing sector."
- B) "The Bank of Canada's recent moves to lower interest rates are behind the recent decreases in the value of the Canadian dollar."
- C) "The Bank of Canada's recent moves to increase the overnight loans rate are leading to less lending and less consumer spending."
- D) "The Bank of Canada's recent sales of government securities are stimulating the housing sector."
- E) "The Bank of Canada's recent moves to decrease the value of the Canadian dollar are leading to more spending in the economy."

Answer: C

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

8) Which statement below best expresses the relationship between the 3-month Treasury bill rate and the overnight loans rate? The rates are

- A) not similar because banks can not readily substitute between them.
- B) similar because they are both required to remain with the Bank of Canada's operating band.
- C) similar because banks can readily substitute between them.
- D) not similar because the treasury bill rate is established through the financial markets whereas the overnight loans rate is set by the Bank of Canada.
- E) not similar because the treasury bill rate is set by the Government of Canada whereas the overnight loans rate is set by the Bank of Canada.

Answer: C

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

9) An increase in the quantity of money leads to

- A) an increase in short-run aggregate supply.
- B) a decrease in net exports.
- C) a decrease in real GDP.
- D) a decrease in the price level.
- E) an increase in aggregate demand.

Answer: E

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

10) In a situation of inflationary pressure, an increase in the overnight loans rate results in

- A) an increase in real GDP and the price level.
- B) an increase in real GDP, but a fall in the price level.
- C) an increase in real GDP, but no change in the price level.
- D) a rise in the price level, but no change in real GDP.
- E) a fall in the price level and a decrease in real GDP.

Answer: E

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

11) The purchase of government bonds by the Bank of Canada

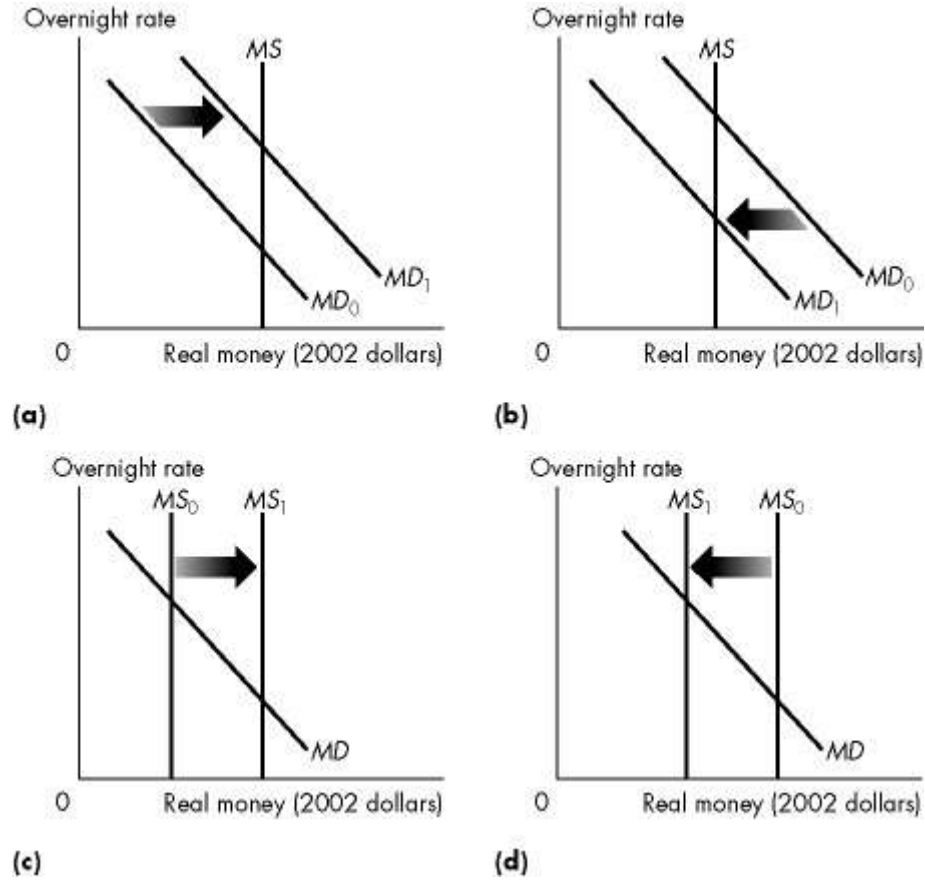
- A) raises the overnight loans rate.
- B) decreases bank reserves.
- C) decreases the supply of loanable funds.
- D) increases aggregate demand.
- E) decreases the quantity of money.

Answer: D

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

Use the figure below to answer the following questions.



**Figure 30.3.1**

12) Refer to Figure 30.3.1. Everything else remaining the same, which graph best illustrates the effect of the Bank of Canada lowering the overnight rate?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) none of the above

Answer: C

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

13) Refer to Figure 30.3.1. Everything else remaining the same, which graph best illustrates the effect of the Bank of Canada raising the overnight rate?

- A) (a)
- B) (b)
- C) (c)
- D) (d)
- E) none of the above

Answer: D

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

14) If the Bank of Canada buys government securities in the open market, the supply curve of real money shifts

- A) leftward and the overnight rate rises.
- B) leftward and the overnight rate falls.
- C) rightward and the overnight rate rises.
- D) rightward and the overnight rate remains constant because the demand for money increases at the same time.
- E) none of the above.

Answer: E

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

Source: Study Guide

15) Which of the following statements about the overnight loans rate is false?

- A) The overnight loans rate and the treasury bill rate move closely together.
- B) The overnight loans rate and the long-term bond rate trend in the same direction.
- C) The overnight loans rate is most often less than the long-term bond rate.
- D) The long-term bond rate fluctuates less than the short-term rates.
- E) The higher the overnight loans rate, the greater the quantity of money.

Answer: E

Diff: 3 Type: MC

Topic: Monetary Policy Transmission

16) If the Bank of Canada lowers the overnight loans rate, the exchange rate \_\_\_\_\_, imports \_\_\_\_\_, and exports \_\_\_\_\_.

- A) rises; increase; increase
- B) rises; increase; decrease
- C) falls; decrease; increase
- D) falls; decrease; decrease
- E) falls; increase; decrease

Answer: C

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

17) If Canadian interest rates rise, the exchange rate value of the dollar \_\_\_\_\_ and net exports \_\_\_\_\_.

- A) rises; increase
- B) rises; decrease
- C) falls; increase
- D) falls; decrease
- E) rises only if the U.S. interest rates fall concurrently; decrease

Answer: B

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

18) When the Bank of Canada lowers the overnight loans rate, the Canadian dollar \_\_\_\_\_ on the foreign exchange market and \_\_\_\_\_.

- A) falls; aggregate demand decreases
- B) rises; aggregate demand decreases
- C) falls; the increase in imports is greater than the increase in exports
- D) falls; aggregate demand increases
- E) rises; U.S. aggregate demand decreases

Answer: D

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

19) The ripple effects that occur when the Bank of Canada raises the overnight loan rate include \_\_\_\_\_.

- A) a decrease in consumption expenditure and investment
- B) an increase in net exports
- C) a decrease in short-run interest rates
- D) an increase in short-run aggregate supply
- E) a decrease in short-run aggregate supply

Answer: A

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

20) The Bank of Canada raises the overnight loans rate. In the foreign exchange market people \_\_\_\_\_ dollars and the price of the dollar \_\_\_\_\_ because the Canadian interest rate differential \_\_\_\_\_.

- A) sell; rises; falls
- B) sell; falls; falls
- C) buy; rises; rises
- D) buy; falls; rises
- E) buy; rises; falls

Answer: C

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

21) If the Bank of Canada lowers the overnight loans rate,

- A) other short-term interest rates fall.
- B) other short-term interest rates rise.
- C) the exchange rate falls.
- D) the long-term interest rate falls.
- E) A, C and D are correct.

Answer: E

Diff: 1 Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

22) When the Bank of Canada lowers the overnight loans rate, the Canadian interest rate differential \_\_\_\_\_ and the Canadian dollar \_\_\_\_\_ on the foreign exchange market.

- A) rises; appreciates
- B) rises; depreciates
- C) falls; appreciates
- D) falls; depreciates
- E) falls; changes to equal the value of the U.S. dollar

Answer: D

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

23) If the Bank of Canada lowers the overnight loans rate, other short-term interest rates \_\_\_\_\_ and the exchange rate \_\_\_\_\_.

- A) fall; falls
- B) fall; does not change
- C) fall; rises
- D) do not change; falls
- E) fall, and the long-term interest rate rises; falls

Answer: A

Diff: 1 Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

24) When the Bank of Canada raises the overnight loans rate, other short-term interest rates  
A) fall, consumption expenditure, investment and net exports increase, and the aggregate demand curve shifts rightward.

B) fall, consumption expenditure, investment and net exports decrease, and the aggregate demand curve shifts leftward.

C) rise, consumption expenditure, investment and net exports decrease, and the aggregate demand curve shifts leftward.

D) rise, consumption expenditure, investment and net exports increase, and the aggregate demand curve shifts rightward.

E) none of the above.

Answer: C

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

25) A decrease in the overnight loans rate

A) increases other short-term interest rates, decreases investment, and decreases aggregate demand.

B) lowers the exchange rate, increases the supply of loanable funds, and increases aggregate demand.

C) lowers other short-term interest rates, raises the real interest rate, and increases aggregate demand.

D) decreases the demand for loanable funds, lowers the real interest rate, and decreases aggregate demand.

E) lowers the exchange rate, increases the demand for loanable funds, and increases aggregate demand.

Answer: B

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

26) A decrease in the overnight loans rate leads to

- A) an increase in the quantity of money.
- B) a fall in the exchange rate.
- C) an increase in exports.
- D) an increase in consumption expenditure.
- E) all of the above.

Answer: E

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

27) If the Bank of Canada is concerned with recession it will \_\_\_\_\_ the overnight loans rate to \_\_\_\_\_.

- A) raise; increase aggregate demand
- B) lower; increase aggregate demand
- C) raise; decrease aggregate demand
- D) lower; decrease aggregate demand
- E) lower; increase potential GDP

Answer: B

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

28) When the Bank of Canada fights recession by lowering the overnight loan rate, the supply of loanable funds curve shifts \_\_\_\_\_ and the aggregate demand curve shifts \_\_\_\_\_.

- A) leftward; leftward
- B) leftward; rightward
- C) rightward; leftward
- D) rightward; rightward
- E) rightward and the demand for loanable funds curve shifts rightward; rightward

Answer: D

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Analytical Skills

29) If the Bank of Canada wants to stimulate the economy to limit the effects of a recessionary gap, then it \_\_\_\_\_ the overnight loans rate to \_\_\_\_\_ the real interest rate and \_\_\_\_\_ investment.

- A) lowers; lower; increase
- B) lowers; raise; increase
- C) raises; raise; decrease
- D) lowers; lower; decrease
- E) lowers; raise; decrease

Answer: A

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

30) When the Bank of Canada lowers the overnight loans rate, there is a \_\_\_\_\_ shift of the \_\_\_\_\_ curve.

- A) rightward; *AD*
- B) leftward; *AD*
- C) rightward; *SAS*
- D) leftward; *SAS*
- E) rightward; *LAS*

Answer: A

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

31) In the short run, lowering the overnight loans rate shifts the \_\_\_\_\_ curve \_\_\_\_\_ and \_\_\_\_\_ real GDP.

- A) aggregate demand; leftward; decreases
- B) aggregate demand; rightward; increases
- C) short-run aggregate supply; rightward; increases
- D) aggregate demand; leftward; increases
- E) long-run aggregate supply; rightward; increases

Answer: B

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

- 32) The short-run effect of lowering the overnight loans rate is that the
- A) price level rises and real GDP increases.
  - B) price level rises and real GDP decreases.
  - C) price level lowers and real GDP increases.
  - D) price level lowers and real GDP decreases.
  - E) none of the above.

Answer: A

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

- 33) When the Bank of Canada fights recession by lowering the overnight loans rate, the supply of reserves curve shifts \_\_\_\_\_ and the supply of money curve shifts \_\_\_\_\_.

- A) leftward; leftward
- B) leftward; rightward
- C) rightward; leftward
- D) rightward; rightward
- E) rightward; rightward, and the demand for loanable funds increases

Answer: D

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

- 34) To combat a recession, the Bank of Canada \_\_\_\_\_ the overnight loans rate, which \_\_\_\_\_ the quantity of money.

- A) raises; increases
- B) lowers; increases
- C) raises; decreases
- D) lowers; decreases
- E) lowers; decreases the demand for bank reserves and increases

Answer: B

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

35) In response to an inflationary gap, the Bank of Canada

- A) waits until the price level falls before acting.
- B) lowers the overnight loans rate by selling securities.
- C) raises the overnight loans rate by selling securities.
- D) lowers the overnight loans rate by buying securities.
- E) raises the overnight loans rate by buying securities.

Answer: C

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

36) If the Bank of Canada wants to eliminate an inflationary gap, which of the following would be an appropriate policy?

- A) Raise the overnight loans rate.
- B) Lower the overnight loans rate.
- C) Buy government securities.
- D) Decrease the government budget deficit.
- E) Lower the exchange rate.

Answer: A

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

37) If the Bank of Canada is concerned with inflation it will \_\_\_\_\_ the overnight loans rate to \_\_\_\_\_.

- A) raise; increase aggregate demand
- B) lower; increase aggregate demand
- C) raise; decrease aggregate demand
- D) lower; decrease aggregate demand
- E) raise; increase potential GDP

Answer: C

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

38) If the Bank of Canada fears inflation it will undertake an open market \_\_\_\_\_ of securities, the overnight loans rate will \_\_\_\_\_ and the long-term real interest rate will \_\_\_\_\_.

- A) sale; rise; fall
- B) sale; rise; rise
- C) purchase; rise; fall
- D) purchase; fall; rise
- E) sale; fall; fall

Answer: B

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

39) If a central bank wants to implement a contractionary policy that decreases real GDP, it conducts an open market operation by \_\_\_\_\_ securities. Bank reserves \_\_\_\_\_ and the supply of loanable funds \_\_\_\_\_. The quantity of money \_\_\_\_\_.

- A) selling; decrease; decreases; decreases
- B) purchasing; decrease; decreases; decreases
- C) purchasing; decrease; increases; decreases
- D) selling; increase; increases; increases
- E) purchasing; increase; increases; increases

Answer: A

Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Reflective Thinking

40) When the Bank of Canada fights inflation by implementing an open market operation, the supply of reserves curve shifts \_\_\_\_\_ and the supply of money curve shifts \_\_\_\_\_.

- A) leftward; leftward
- B) leftward; rightward
- C) rightward; leftward
- D) rightward; rightward
- E) none of the above

Answer: A

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Analytical Skills

41) When the Bank of Canada fights inflation by implementing open market operations, the supply of loanable funds curve shifts \_\_\_\_\_ and the aggregate demand curve shifts \_\_\_\_\_.

- A) leftward; leftward
- B) leftward; rightward
- C) rightward; leftward
- D) rightward; rightward
- E) leftward; leftward, and potential GDP decreases

Answer: A

Diff: 2 Type: MC

Topic: Monetary Policy Transmission

Skill: Conceptual

AACSB: Analytical Skills

42) The headline "The Bank of Canada Has Cut the Bank Rate" suggests that the Bank of Canada is trying to

- A) lower inflationary pressures.
- B) increase the overnight loans rate.
- C) stimulate aggregate demand.
- D) raise the value of the Canadian dollar.
- E) help banks make profits.

Answer: C

Type: MC

Topic: Monetary Policy Transmission

Source: Study Guide

43) A monetary policy aimed at increasing domestic expenditure will

- A) increase interest rates and decrease the exchange rate.
- B) have no impact on interest rates, but increase the exchange rate.
- C) have no impact on interest rates nor on the exchange rate.
- D) decrease interest rates and increase the exchange rate.
- E) decrease interest rates and the exchange rate.

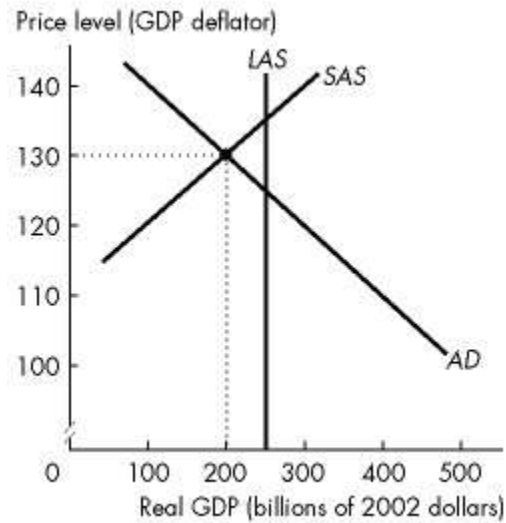
Answer: E

Type: MC

Topic: Monetary Policy Transmission

Source: Study Guide

Use the figure below to answer the following question.



**Figure 30.3.2**

44) Refer to Figure 30.3.2. The figure shows the economy of Freezone. Potential GDP is \$250 billion.

To return the economy to full employment, the central bank can \_\_\_\_\_ the overnight rate and \_\_\_\_\_ securities.

- A) lower; sell
- B) raise; sell
- C) raise; buy
- D) lower; buy
- E) lower; not change its holdings of

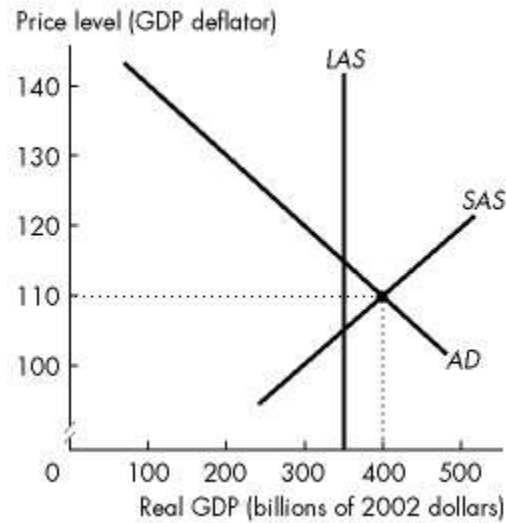
Answer: D

Type: MC

Topic: Monetary Policy Transmission

Source: MyEconLab

Use the figure below to answer the following question.



**Figure 30.3.3**

45) Refer to Figure 30.3.3. The figure shows the economy of Freezone. Potential GDP is \$350 billion.

To return the economy to full employment, the central bank can \_\_\_\_\_ the overnight rate and \_\_\_\_\_ securities.

- A) raise; sell
- B) lower; sell
- C) lower; buy
- D) raise; buy
- E) lower; not change its holdings of

Answer: A

Type: MC

Topic: Monetary Policy Transmission

Source: MyEconLab

46) Which of the following does *not* occur as a result of the Bank of Canada lowering the overnight loans rate?

- A) the supply of loanable funds increase
- B) the long-term real interest rate falls
- C) exports increase
- D) the inflation rate decreases
- E) imports decrease

Answer: D

Type: MC

47) Which of the following does not occur as a result of the Bank of Canada raising the overnight loans rate?

- A) the supply of loanable funds decrease
- B) the long-term real interest rate rises
- C) exports decrease
- D) aggregate demand increases
- E) imports increase

Answer: D

Type: MC

48) Choose the correct statement.

- A) Demand and supply in the loanable funds market determine the long-term real interest rate.
- B) The long-term real interest rate influences expenditure decisions.
- C) In the short run, the supply of loanable funds is influenced by the supply of bank loans.
- D) A fall in the overnight loans rate that increases the supply of bank loans increases the supply of loanable funds and lowers the equilibrium real interest rate.
- E) All of the above are correct.

Answer: E

Type: MC

### 30.4 Extraordinary Monetary Stimulus

1) What is the Taylor Rule?

- A) The overnight loan rate is set in response to the current inflation rate and to the current estimate of the output gap.
- B) The monetary base is set in response to the current inflation rate and to the current estimate of the output gap.
- C) The monetary base should grow at a rate equal to the target inflation rate plus the long-term real GDP growth rate minus the medium-term velocity growth rate.
- D) The money supply should grow at a rate equal to the long-run real growth rate.
- E) The money supply should be regulated by setting the exchange rate equal to purchasing power parity with other countries.

Answer: A

Diff: 2 Type: MC

Topic: Extraordinary Monetary Stimulus

2) Suppose the Bank of Canada uses the Taylor rule to set the overnight loans rate. If the inflation rate is 3 percent, and the output gap is 0 percent, then the Taylor rule sets the overnight rate equal to

- A) 5 percent.
- B) 5.5 percent.
- C) 0 percent.
- D) 2.5 percent.
- E) 6 percent.

Answer: B

Diff: 2 Type: MC

Topic: Extraordinary Monetary Stimulus

3) Suppose the inflation rate is 2.5 percent, and the output gap is 1 percent. Using the Taylor rule, the Bank of Canada sets the overnight loans rate equal to

- A) 3 percent.
- B) 3.5 percent.
- C) 5.25 percent.
- D) 5.5 percent.
- E) 5.75 percent.

Answer: C

Diff: 3 Type: MC

Topic: Extraordinary Monetary Stimulus

Skill: Analytical

AACSB: Analytical Skills

4) Suppose the inflation rate is 3 percent and the output gap is -1 percent. Using the Taylor rule, the Bank of Canada sets the overnight loans rate equal to

- A) 5 percent.
- B) 6 percent.
- C) 4 percent.
- D) 1 percent.
- E) 5.5 percent.

Answer: A

Type: MC

Topic: Extraordinary Monetary Stimulus

Skill: Analytical

AACSB: Analytical Skills

5) Which of the following can put a bank under stress?

- A) a widespread fall in asset prices
- B) a significant currency drain
- C) an increase in the number of customers using tellers
- D) an increase in the number of customers applying for loans
- E) Both A and B are correct.

Answer: E

Type: MC

6) Which of the following central banks does *not* follow an inflation rate targeting strategy?

- A) The Federal Reserve (the central bank of the United States)
- B) The Bank of Canada
- C) The Reserve Bank of Australia
- D) The Bank of England
- E) The European Central Bank (the central bank of the Eurozone)

Answer: A

Type: MC

7) Consider policy actions in a financial and banking crisis.

\_\_\_\_\_ addresses the problem of \_\_\_\_\_.

- A) The extension of deposit insurance; solvency
- B) An open market operation; liquidity
- C) Swapping government securities for toxic assets; solvency
- D) Buying bank shares; liquidity
- E) Fair value accounting; liquidity

Answer: B

Type: MC

## Chapter 31 International Trade Policy

### 31.1 How Global Markets Work

1) Goods and services that we buy from other countries are our

- A) balance of payments.

- B) exports.
- C) imports.
- D) terms of trade.
- E) comparative goods and services.

Answer: C

Type: MC

Topic: How Global Markets Work

Skill: Recognition

AACSB: Reflective Thinking

2) The goods and services we sell to people in other countries are our

- A) tariffs.
- B) quotas.
- C) exports.
- D) imports.
- E) investment goods and services.

Answer: C

Type: MC

Topic: How Global Markets Work

Skill: Recognition

AACSB: Reflective Thinking

3) The fundamental force that drives international trade is

- A) absolute advantage.
- B) importation duties.
- C) the advantage of execution.
- D) export advantage.
- E) comparative advantage.

Answer: E

Type: MC

Topic: How Global Markets Work

Skill: Recognition

AACSB: Reflective Thinking

4) The fundamental force that drives international trade is

- A) comparative advantage.
- B) absolute advantage.
- C) a countries' desire to increase their trade surplus.
- D) cheap labour in countries like China and India.
- E) unemployment of factors of production.

Answer: A

Diff: 2 Type: MC

Topic: How Global Markets Work

Skill: Recognition

AACSB: Reflective Thinking

5) A country

- A) imports those goods in which it has a comparative advantage.
- B) exports those goods in which it has a comparative advantage.
- C) imports goods produced in countries with lower wage rates.
- D) exports goods produced by domestic industries with low wages relative to its trading partners.
- E) B and D are correct.

Answer: B

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

AACSB: Reflective Thinking

6) Canada has a comparative advantage in producing airplanes if

- A) it can produce them at a lower dollar cost than another country.
- B) it can produce a larger quantity than another country.
- C) it has a larger quantity of skilled workers than another country.
- D) it can produce them at a higher opportunity cost than another country.
- E) it can produce them at a lower opportunity cost than another country.

Answer: E

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

AACSB: Reflective Thinking

7) Prior to international trade, if the price of good X is lower in country A than in country B,

- A) country B has an absolute advantage in the production of good X.
- B) country B has a comparative advantage in the production of good X.
- C) country A has an absolute advantage in the production of good X.
- D) country A has a comparative advantage in the production of good X.
- E) country B should stop producing good A.

Answer: D

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

AACSB: Reflective Thinking

8) Which of the following statements about Canada's international trade in 2010 is correct?

- A) The value of Canada's imports exceeded the value of Canada's exports.
- B) The value of Canada's exports was about 45 percent of the value of total expenditure in Canada.
- C) Canada imported only goods.
- D) Canada was the world's second largest trader.
- E) Canada exported only goods.

Answer: A

Type: MC

Topic: How Global Markets Work

Skill: Recognition

AACSB: Reflective Thinking

9) Canada has a comparative advantage in producing hardwood if the Canadian price of hardwood before international trade is \_\_\_\_\_ the world price.

- A) equal to
- B) greater than
- C) not comparable to
- D) at least double
- E) less than

Answer: E

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

AACSB: Reflective Thinking

10) Compared to the situation before international trade, after Canada exports a good, production in Canada \_\_\_\_\_ and consumption in Canada \_\_\_\_\_.

- A) increases; increases
- B) increases; decreases
- C) decreases; increases
- D) decreases; decreases
- E) increases; does not change

Answer: B

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

AACSB: Analytical Skills

11) Compared to the situation before international trade, after Canada imports a good, production in Canada \_\_\_\_\_ and consumption in Canada \_\_\_\_\_.

- A) increases; increases
- B) increases; decreases
- C) decreases; increases
- D) decreases; decreases
- E) does not change; increases

Answer: C

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

AACSB: Analytical Skills

12) Which of the following is a Canadian service export?

- A) A Canadian buys dinner while travelling in Switzerland.
- B) A Swiss buys dinner while travelling in Canada.
- C) A Canadian buys a clock made in Switzerland.
- D) A Swiss buys a computer made in Canada.
- E) A Canadian buys a Canadian computer in Switzerland.

Answer: B

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

Refer to the table below to answer the following questions.

**Table 31.1.1**  
Glazeland's Doughnut Market

Price (dollars per doughnut)	Glazeland's Supply (millions)	Glazeland's Demand (millions)
0.20	1	10
0.30	2	8
0.40	3	6
0.50	4	4
0.60	5	2
0.70	6	0

13) Table 31.1.1 shows Glazeland's doughnut market before international trade. Glazeland opens up to international trade. If the world price is \$0.60, then Glazeland will produce \_\_\_\_\_ doughnuts and will \_\_\_\_\_ doughnuts.

- A) 2 million; import 3 million
- B) 4 million; import 1 million
- C) 4 million; export 1 million
- D) 5 million; import 3 million
- E) 5 million; export 3 million

Answer: E

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

14) Table 31.1.1 shows Glazeland's doughnut market before international trade. Glazeland opens up to international trade. If the world price is \$0.40, then Glazeland will produce \_\_\_\_\_ doughnuts and will \_\_\_\_\_ doughnuts.

- A) 3 million; import 3 million
- B) 3 million; export 3 million
- C) 4 million; import 1 million
- D) 4 million; export 1 million
- E) 6 million; export 3 million

Answer: A

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

15) Canada produces both lumber and wine. Canada exports lumber and imports wine. The rest of the world imports Canadian lumber and exports wine to Canada. If Canada did *not* trade with the rest of the world, then the equilibrium price of lumber would be \_\_\_\_\_ in Canada than the rest of the world, and the equilibrium price of wine would be \_\_\_\_\_ in Canada than the rest of the world.

- A) lower; higher
- B) higher; lower
- C) higher; higher
- D) lower; lower
- E) the same or lower; the same or higher

Answer: A

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

Source: MyEconLab

AACSB: Analytical Skills

16) Canada produces both lumber and wine. Canada exports lumber and imports wine. The rest of the world imports Canadian lumber and exports wine to Canada. Canada has a comparative advantage in producing \_\_\_\_\_. The rest of the world has a comparative advantage in producing \_\_\_\_\_.

- A) lumber; wine
- B) wine; lumber
- C) wine; wine
- D) lumber; lumber
- E) a good other than lumber or wine; wine

Answer: A

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

Source: MyEconLab

AACSB: Analytical Skills

17) Consider a country that sells some of its goods as exports. Who does *NOT* benefit?

- A) domestic consumers
- B) domestic producers
- C) workers in the industry
- D) foreign consumers
- E) everyone benefits

Answer: A

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

AACSB: Analytical Skills

18) Who benefits from imports?

- A) domestic consumers
- B) domestic producers
- C) foreign consumers
- D) domestic workers in the industry
- E) everyone benefits

Answer: A

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

AACSB: Analytical Skills

19) A country opens up to trade. In an import industry,

- A) domestic producers lose and domestic consumers gain.
- B) domestic consumers lose and domestic producers gain.
- C) the government loses and domestic consumers gain.
- D) domestic producers lose and the government gains.
- E) none of the above.

Answer: A

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

AACSB: Analytical Skills

Refer to the table below to answer the following questions.

**Table 31.1.2**

Price (dollars)	Quantity demanded (units)	Quantity supplied (units)
2	100	70
4	95	75
6	90	80
8	85	85
10	80	90
12	75	95

20) Refer to Table 31.1.2. The table shows a country's demand and supply schedules. At what world price would the country import?

- A) at exactly \$8 a unit
- B) any price above \$8 a unit
- C) a price of \$10 a unit
- D) a price of \$20 a unit
- E) a price below \$8 a unit

Answer: E

Type: MC

Topic: How Global Markets Work

Skill: Analytical

AACSB: Analytical Skills

21) Refer to Table 31.1.2. The table shows a country's demand and supply schedules. Suppose the world price is \$4 a unit. The country

- A) imports 20 units.
- B) exports 20 units.
- C) imports 10 units.
- D) exports 10 units.
- E) imports 30 units.

Answer: A

Type: MC

Topic: How Global Markets Work

Skill: Analytical

AACSB: Analytical Skills

22) A market is open to international trade. At the world price, the quantity demanded is 150 units and the quantity supplied is 200 units. This country will

- A) import 50 units.
- B) export 200 units.
- C) import 150 units.
- D) import 200 units.
- E) export 50 units.

Answer: E

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

AACSB: Analytical Skills

23) A country opens up to trade. In an export industry,

- A) domestic consumers lose and domestic producers win.
- B) domestic producers lose and domestic consumers win.
- C) domestic producers lose and the government wins.
- D) the government loses and domestic consumers win.
- E) none of the above.

Answer: A

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

AACSB: Communication

Refer to the table below to answer the following question.

**Table 31.1.3**

Price (dollars)	Quantity demanded (units)	Quantity supplied (units)
2	100	70
4	95	75
6	90	80
8	85	85
10	80	90
12	75	95

24) Refer to Table 31.1.3. The table shows a country's demand and supply schedules. At what world price would the country export?

- A) at only \$8 a unit
- B) any price below \$8
- C) a price of \$6 a unit
- D) a price of \$4 a unit
- E) any price above \$8 a unit

Answer: E

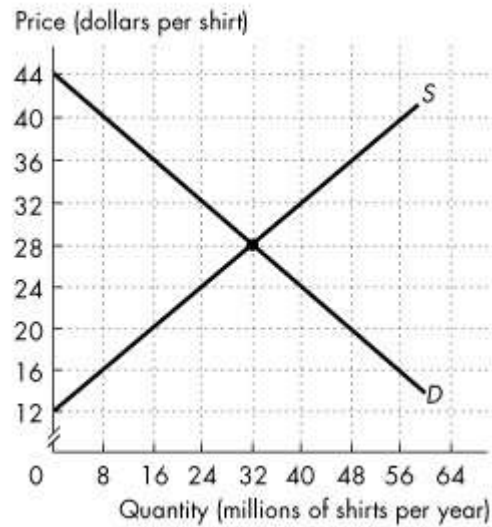
Type: MC

Topic: How Global Markets Work

Skill: Analytical

AACSB: Analytical Skills

Refer to the figure below to answer the following questions.



The figure shows the market for shirts in Canada, where  $D$  is the domestic demand curve and  $S$  is the domestic supply curve. The world price is \$20 per shirt.

**Figure 31.1.1**

25) In Figure 31.1.1, with international trade Canadians buy \_\_\_\_\_ million shirts per year.

- A) 48
- B) 32
- C) 16
- D) 24
- E) 56

Answer: A

Diff: 2 Type: MC

Topic: How Global Markets Work

Skill: Analytical

AACSB: Analytical Skills

26) In Figure 31.1.1, with international trade \_\_\_\_\_ million shirts per year are produced in Canada.

- A) 48
- B) 32
- C) 20
- D) 56
- E) 16

Answer: E

Diff: 2 Type: MC

Topic: How Global Markets Work

Skill: Analytical

AACSB: Analytical Skills

27) In Figure 31.1.1, with international trade Canada \_\_\_\_\_ million shirts per year.

- A) imports 32
- B) imports 48
- C) exports 16
- D) exports 32
- E) imports 16

Answer: A

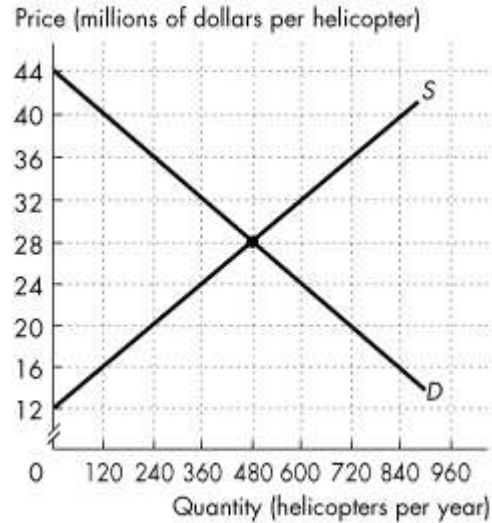
Diff: 2 Type: MC

Topic: How Global Markets Work

Skill: Analytical

AACSB: Analytical Skills

*Refer to the figure below to answer the following questions.*



The figure shows the market for helicopters in Canada, where  $D$  is the domestic demand curve and  $S$  is the domestic supply curve. Canada trades helicopters with the rest of the world at a price of \$36 million per helicopter.

**Figure 31.1.2**

28) In Figure 31.1.2, with international trade Canadian firms buy \_\_\_\_\_ helicopters per year.

- A) 240
- B) 480
- C) 720
- D) 360
- E) 600

Answer: A

Diff: 2 Type: MC

Topic: How Global Markets Work  
Skill: Analytical  
AACSB: Analytical Skills

29) In Figure 31.1.2, with international trade \_\_\_\_\_ helicopters per year are produced in Canada.

- A) 360
- B) 480
- C) 720
- D) 240
- E) 600

Answer: C

Diff: 2 Type: MC

Topic: How Global Markets Work  
Skill: Analytical  
AACSB: Analytical Skills

30) In Figure 31.1.2, Canada \_\_\_\_\_ helicopters per year.

- A) exports 480
- B) exports 720
- C) imports 480
- D) imports 240
- E) exports 240

Answer: A

Diff: 2 Type: MC

Topic: How Global Markets Work  
Skill: Analytical  
AACSB: Analytical Skills

31) Consider a market that sells some of its goods as exports. Who does *NOT* benefit?

- A) domestic consumers
- B) domestic producers
- C) workers in the industry
- D) foreign consumers
- E) all of the above benefit

Answer: A

Diff: 2 Type: MC

Topic: How Global Markets Work  
Skill: Analytical  
AACSB: Analytical Skills

- 32) Who benefits from imports?  
A) domestic consumers  
B) domestic producers  
C) foreign consumers  
D) domestic workers in the industry  
E) none of the above benefit

Answer: A

Diff: 2 Type: MC

Topic: How Global Markets Work

Skill: Analytical

AACSB: Analytical Skills

- 33) Canada produces both lumber and wine. Canada exports lumber and imports wine. The rest of the world imports Canadian lumber and exports wine to Canada. When Canada exports lumber to the rest of the world and the rest of the world exports wine to Canada \_\_\_\_\_.  
A) lumber producers in the rest of the world lose and wine producers in the rest of the world gain  
B) Canada's lumber producers gain  
C) Canada's wine producers lose  
D) all of the above  
E) none of the above

Answer: D

Diff: 2 Type: MC

Topic: How Global Markets Work

Skill: Analytical

Source: MyEconLab

AACSB: Analytical Skills

- 34) Canada produces both lumber and wine. Canada exports lumber and imports wine. The rest of the world imports Canadian lumber and exports wine to Canada. If Canada did *not* trade with the rest of the world, then the equilibrium price of lumber would be \_\_\_\_\_ in Canada than the rest of the world, and the equilibrium price of wine would be \_\_\_\_\_ in Canada than the rest of the world.  
A) lower; higher  
B) higher; lower  
C) higher; higher  
D) lower; lower  
E) sometimes higher and sometimes lower; always higher

Answer: A

Type: MC

Topic: How Global Markets Work

Skill: Conceptual

Source: MyEconLab

AACSB: Analytical Skills

35) Canada produces both lumber and wine. Canada exports lumber and imports wine. The rest of the world imports Canadian lumber and exports wine to Canada. Canada has a comparative advantage in producing \_\_\_\_\_. The rest of the world has a comparative advantage in producing \_\_\_\_\_.

- A) lumber ; wine
- B) wine; lumber
- C) wine; wine
- D) lumber; lumber
- E) both lumber and wine; neither lumber nor wine

Answer: A

Diff: 2 Type: MC

Topic: How Global Markets Work

Skill: Analytical

Source: MyEconLab

AACSB: Analytical Skills

36) Suppose that the world price of oats is 30 cents a kilogram. Canada does *not* trade internationally, and the equilibrium price of oats in Canada is 40 cents a kilogram. Canada then begins to trade internationally. The price of oats in Canada \_\_\_\_\_. Canadian consumers buy \_\_\_\_\_ oats. Canadian firms produce \_\_\_\_\_ oats. Canada \_\_\_\_\_ oats.

- A) rises; less; more; exports
- B) falls; less; more; imports
- C) falls; more; less; imports
- D) rises; more; less; exports
- E) falls; more; less; exports

Answer: C

Diff: 2 Type: MC

Topic: How Global Markets Work

Skill: Analytical

Source: MyEconLab

AACSB: Analytical Skills

37) In one year, Brazil exported more than 1.8 billion kilograms of coffee to the rest of the world. We can conclude that

- A) Brazil has comparative advantage in coffee production.
- B) Brazil has an absolute advantage in coffee production.
- C) the rest of the world has a comparative advantage in coffee production.
- D) the rest of the world has an absolute advantage in coffee production.
- E) Brazil's government has placed a tariff on coffee.

Answer: A

Type: MC

38) Choose the correct statement.

- A) Exports include goods and services.
- B) Imports include goods but not services.
- C) Imports include services but not goods.
- D) Exports include goods but not services.
- E) Exports include services but not goods.

Answer: A

Type: MC

39) In one year, Brazil exported more than 1.8 billion kilograms of coffee to the rest of the world. We can conclude that

- A) Brazil's coffee producers lose from this trade.
- B) coffee consumers in the rest of the world lose from this trade.
- C) Brazil's coffee consumers lose from this trade.
- D) coffee producers in the rest of the world gain from this trade.
- E) Brazil's government loses from this trade.

Answer: C

Type: MC

40) In a market that moves from a situation of no trade to a situation where a good is exported, the price of the good \_\_\_\_\_ and the quantity produced by the domestic industry \_\_\_\_\_.

- A) rises; increases
- B) falls; decreases
- C) does not change; increases
- D) does not change; decreases
- E) rises; does not change

Answer: A

Type: MC

41) In a market that moves from a situation of no trade to a situation where a good is imported, the price of the good \_\_\_\_\_ and the quantity produced by the domestic industry \_\_\_\_\_.

- A) rises; increases
- B) falls; decreases
- C) does not change; increases
- D) does not change; decreases
- E) rises; does not change

Answer: B

Type: MC

## 31.2 International Trade Restrictions

1) A tariff is a tax that is imposed by the \_\_\_\_\_ country when an \_\_\_\_\_ good crosses its international boundary.

- A) exporting; imported
- B) importing; exported
- C) exporting; exported
- D) importing; imported
- E) importing or exporting; imported or exported

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Reflective Thinking

2) A tax that is imposed by the importing country when an imported good crosses its international boundary is called

- A) an import quota.
- B) dumping.
- C) a voluntary export restraint.
- D) a tariff.
- E) a sales tax.

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Reflective Thinking

3) Tariffs and import quotas differ in that

- A) one is a form of trade restriction, while the other is not.
- B) one is a tax, while the other is a limit.
- C) one is imposed by the government, while the other is imposed by the private sector.
- D) one is legal, while the other is not.
- E) one increases imports, while the other decreases imports.

Answer: B

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Reflective Thinking

- 4) Tariffs and import quotas both result in
- A) lower levels of domestic production.
  - B) the domestic government gaining revenue.
  - C) lower levels of imports.
  - D) higher levels of domestic consumption.
  - E) an increase in demand.

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

- 5) If Canada imposes a tariff on imported cars,
- A) Canada's demand curve for cars shifts rightward.
  - B) Canada's demand curve for cars shifts leftward.
  - C) Canada's supply curve of cars shifts rightward.
  - D) Canada's supply curve of cars shifts leftward.
  - E) the price in Canada rises but neither Canada's demand curve nor Canada's supply curve shifts.

Answer: E

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Analytical Skills

- 6) Which of the following statements concerning tariffs is *NOT* true?
- A) A tariff increases domestic production.
  - B) A tariff creates revenue for the government.
  - C) A tariff decreases international trade.
  - D) A tariff leaves the price of imports unchanged.
  - E) A tariff decreases domestic consumption.

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Communication

7) If a country imposes a tariff on an imported good, the tariff \_\_\_\_\_ the price in the importing country and \_\_\_\_\_ the quantity of imports.

- A) raises; increases
- B) raises; does not change
- C) lowers; does not change
- D) lowers; increases
- E) raises; decreases

Answer: E

Type: MC

Topic: International Trade Restrictions

Skill: Analytical

AACSB: Analytical Skills

8) A tariff imposed by Canada on Japanese cars \_\_\_\_\_ the price of cars in Canada and \_\_\_\_\_ the quantity of Japanese cars imported into Canada.

- A) raises; increases
- B) raises; decreases
- C) lowers; increases
- D) lowers; decreases
- E) raises; does not change

Answer: B

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

9) If Canada imposes a tariff of \$1 per imported shirt, the tariff

- A) raises the price of a shirt paid by Canadian consumers.
- B) benefits Canadian shirt producers.
- C) decreases imports of shirts into Canada.
- D) creates a social loss.
- E) all of the above.

Answer: E

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Communication

- 10) If Canada imposes a tariff on imported steel, the tariff
- A) raises the Canadian price of imported steel.
  - B) decreases the Canadian production of steel.
  - C) increases the total Canadian consumption of steel.
  - D) decreases employment in the Canadian steel industry.
  - E) all of the above.

Answer: A

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

- 11) Suppose the country of Mooland imposes tariffs on imported beef from the country of Aqualand. As a result of the tariffs, the
- A) price of beef in Mooland falls.
  - B) quantity of beef exported by Mooland increases.
  - C) quantity of beef imported by Mooland decreases.
  - D) quantity of beef imported by Mooland increases.
  - E) price of beef in Mooland does not change.

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

- 12) Reducing a tariff \_\_\_\_\_ the domestic production of the good and \_\_\_\_\_ the total domestic consumption of the good.
- A) increases; increases
  - B) increases; decreases
  - C) decreases; increases
  - D) decreases; decreases
  - E) does not change; increases

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

13) Increasing a tariff \_\_\_\_\_ the domestic quantity consumed of the good and \_\_\_\_\_ the domestic production of the good.

- A) increases; increases
- B) increases; decreases
- C) decreases; increases
- D) decreases; decreases
- E) decreases; does not change

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

14) Tariffs

- A) generate revenue for consumers.
- B) generate revenue for the government.
- C) encourage domestic consumers to buy more imports.
- D) encourage domestic producers to produce less.
- E) lower prices for consumers.

Answer: B

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Reflective Thinking

15) Canada imports cars from Japan. If Canada imposes a tariff on cars imported from Japan, Canadian

- A) consumers will lose and Japanese producers will gain.
- B) tariff revenue will equal the loss of Canadian consumers.
- C) consumers will lose and Canadian producers will gain.
- D) car manufacturers will gain revenue equal to the revenue lost by Japanese car manufacturers.
- E) producers will lose and Japanese consumers will gain.

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Analytical

AACSB: Analytical Skills

16) A Canadian tariff imposed on items that can be produced more cheaply abroad

- A) benefits Canadians by making these goods cheaper.
- B) makes the goods more expensive in foreign markets.
- C) creates a social loss.
- D) equalizes the cost of production between Canada and foreign producers.
- E) All of the above.

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Reflective Thinking

17) The winners from a tariff on imports are

- A) producers and government.
- B) producers only.
- C) consumers only.
- D) consumers, producers, and government.
- E) government only.

Answer: A

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Ethical Reasoning

18) A tariff is imposed on a good. This \_\_\_\_\_ the quantity supplied, \_\_\_\_\_ the quantity demanded, and \_\_\_\_\_ the price in the home country.

- A) increases; decreases; raises
- B) increases; does not change; does not change
- C) increases; increases; raises
- D) increases; decreases; lowers
- E) decreases; increases; lowers

Answer: A

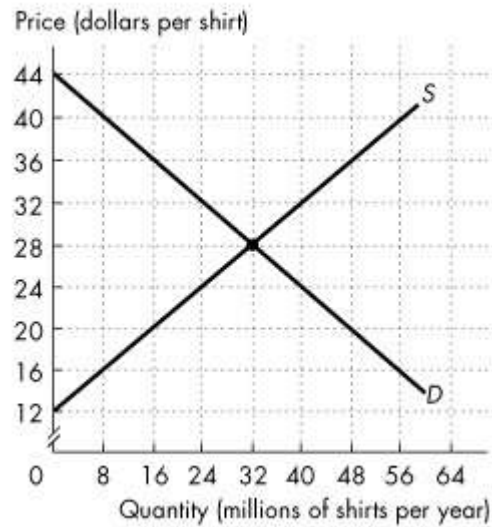
Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Reflective Thinking

Refer to the figure below to answer the following questions.



The figure shows the market for shirts in Canada, where D is the domestic demand curve and S is the domestic supply curve. The world price is \$20 per shirt. Canada imposes a tariff on imported shirts of \$4 per shirt.

**Figure 31.2.1**

19) Refer to Figure 31.2.1, with the tariff Canadians buy \_\_\_\_\_ million shirts per year.

- A) 48
- B) 32
- C) 16
- D) 24
- E) 40

Answer: E

Diff: 2 Type: MC

Topic: International Trade Restrictions

Skill: Analytical

AACSB: Analytical Skills

20) Refer to Figure 31.2.1, with the tariff Canada imports \_\_\_\_\_ million shirts per year.

- A) 24
- B) 8
- C) 32
- D) 16
- E) 40

Answer: D

Diff: 2 Type: MC

Topic: International Trade Restrictions

Skill: Analytical

AACSB: Analytical Skills

21) Refer to Figure 31.2.1, the tariff \_\_\_\_\_ Canada's imports of shirts by \_\_\_\_\_ million shirts per year.

- A) decreases; 16
- B) decreases; 8
- C) increases; 8
- D) increases; 4
- E) increases; 16

Answer: A

Diff: 2 Type: MC

Topic: International Trade Restrictions

Skill: Analytical

AACSB: Analytical Skills

22) Refer to Figure 31.2.1, the tariff \_\_\_\_\_ the domestic production of shirts in Canada by \_\_\_\_\_ per year.

- A) increases; 8 million
- B) decreases; 16 million
- C) increases; 4 million
- D) decreases; 8 million
- E) increases; 24 million

Answer: A

Diff: 2 Type: MC

Topic: International Trade Restrictions

Skill: Analytical

AACSB: Analytical Skills

23) Refer to Figure 31.2.1, the Canadian government's revenue from the tariff is \_\_\_\_\_.

- A) \$64 million
- B) \$32 million
- C) \$128 million
- D) \$48 million
- E) \$480 million

Answer: A

Diff: 2 Type: MC

Topic: International Trade Restrictions

Skill: Analytical

AACSB: Analytical Skills

24) Of the following, in which decade were Canada's tariffs at their lowest level?

- A) 1990s
- B) 1970s
- C) 1950s
- D) 1930s
- E) 1890s

Answer: A

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Reflective Thinking

25) An import quota is

- A) a tariff that is a fixed percentage of the price of a good.
- B) a tariff that is a fixed dollar amount per unit of a good.
- C) an agreed upon price for a good to be imported at a specified future date.
- D) a restriction that specifies the maximum amount of a good that may be imported.
- E) the same as an export subsidy.

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Reflective Thinking

26) \_\_\_\_\_ specifies the maximum amount of a good that may be imported in a given period of time.

- A) An import restriction
- B) A legislative restriction
- C) A trade restriction
- D) An import quota
- E) An import subsidy

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Reflective Thinking

27) Import quotas

- A) are the same as tariffs.
- B) are not used by Canada.
- C) set the minimum percentage of the value of a product that must consist of imported components.
- D) benefit society.
- E) set the maximum number of units of a good that can be imported in a given time period.

Answer: E

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Reflective Thinking

28) An import quota is a

- A) tariff imposed on goods that are dumped in the country.
- B) law that prevents ecologically damaging goods from being imported into a country.
- C) market-imposed balancing factor that keeps prices of imports and exports in equilibrium.
- D) government-imposed restriction on the quantity of a specific good that can be imported.
- E) tax in an international market.

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Recognition

AACSB: Reflective Thinking

29) An import quota directly restricts \_\_\_\_\_ and is designed to protect domestic \_\_\_\_\_.

- A) exports; consumers only
- B) exports; producers only
- C) imports; consumers only
- D) imports; producers only
- E) imports; producers and consumers

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

30) Import quotas \_\_\_\_\_ the price of imported goods and \_\_\_\_\_ the quantity consumed in the country imposing the quota.

- A) raise; increase
- B) raise; decrease
- C) lower; increase
- D) lower; decrease
- E) raise; do not change

Answer: B

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

31) If a government imposes a quota on imports of a popular doll, the price of the doll in the country \_\_\_\_\_ and the quantity purchased in the country \_\_\_\_\_.

- A) rises; increases
- B) rises; decreases
- C) falls; increases
- D) falls; decreases
- E) rises; does not change

Answer: B

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

32) A key difference between tariffs and import quotas is that

- A) consumers are hurt with import quotas but not with tariffs.
- B) consumers are hurt with tariffs but not with import quotas.
- C) the government receives revenue with a tariff, but the importer makes a profit with an import quota.
- D) the government receives revenue with an import quota, but the importer makes a profit with a tariff.
- E) domestic producers gain with a tariff and lose with an import quota.

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Reflective Thinking

- 33) A difference between a quota and a tariff is that
- A) a tariff generates a higher price than does an import quota.
  - B) a tariff generates a greater reduction in exports than does an import quota.
  - C) an import quota increases profits of domestic producers more than a tariff.
  - D) the government collects revenue from a tariff but does not collect revenue from an import quota.
  - E) an import quota creates a social loss and a tariff does not.

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Reflective Thinking

- 34) A tariff \_\_\_\_\_ the domestic price of the good and an import quota \_\_\_\_\_ the domestic price of the good.

- A) lowers; lowers
- B) lowers; raises
- C) raises; lowers
- D) raises; raises
- E) does not change; does not change

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

Refer to the table below to answer the following questions.

**Table 31.2.1**  
Canada's Market for Widgets

Price (dollars per widgets)	Canadian Supply (millions)	Canadian Demand (millions)
5	12	52
6	16	48
7	20	44
8	24	40
9	28	36
10	32	32
12	36	28

35) Table 31.2.1 shows the Canadian supply of and demand for widgets. Widgets are available on the world market for \$7. If the Canadian government imposes a tariff of \$1, the domestic selling price will be \_\_\_\_\_ and quantity bought will be \_\_\_\_\_.

- A) \$6; 48 million
- B) \$7; 44 million
- C) \$8; 16 million
- D) \$8; 24 million
- E) \$8; 40 million

Answer: E

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

36) Table 31.2.1 shows the Canadian supply of and demand for widgets. Widgets are available on the world market for \$7. If the Canadian government imposes a tariff of \$1, how many widgets will Canada import?

- A) 32 million
- B) 24 million
- C) 16 million
- D) 28 million
- E) 40 million

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

37) Table 31.2.1 shows the Canadian supply of and demand for widgets. Widgets are available on the world market for \$7. Canadian widget producers convince the government to protect the domestic industry from cheap imports. If the Canadian government sets an import quota of 8 million widgets, the resulting price of a widget in Canada will be \_\_\_\_\_, and domestic production will be \_\_\_\_\_.

- A) \$6; 40 million
- B) \$7; 36 million
- C) \$8; 32 million
- D) \$9; 28 million
- E) \$10; 32 million

Answer: D

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

38) A tariff on watches which are imported by Atlantis \_\_\_\_\_ the price of watches in Atlantis and \_\_\_\_\_.

- A) lowers; imports of watches increase
- B) raises; watch production in Atlantis increases
- C) raises; watch production in Atlantis decreases
- D) lowers; watch production in Atlantis increases
- E) lowers; watch production in Atlantis decreases

Answer: B

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

39) When an *import quota* is imposed, the gap between the domestic price and the price received in the exporting country is captured by

- A) consumers in the importing country.
- B) the domestic producers of the good.
- C) the government of the importing country.
- D) foreign exporters.
- E) the importers of the good.

Answer: E

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

40) When a *tariff* is imposed, the gap between the domestic price and the price received in the exporting country is captured by

- A) consumers in the importing country.
- B) the domestic producers of the good.
- C) the government of the importing country.
- D) foreign exporters.
- E) the domestic importers of the good.

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

Source: Study Guide

AACSB: Analytical Skills

41) Canada imposes a tariff on \$1 per imported shirt, the higher tariff

- A) raises the price of a shirt to Canadian consumers.
- B) benefits Canadian shirt producers.
- C) decreases imports of shirts into Canada.
- D) creates a social loss.
- E) all of the above.

Answer: E

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

42) If Canada imposes a tariff on imported steel, the tariff

- A) raises the Canadian price of imported steel.
- B) decreases Canadian production of steel.
- C) increases the total Canadian consumption of steel.
- D) decreases employment in the Canadian steel industry.
- E) both B and D are correct.

Answer: A

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

43) Lowering the tariff on good X

- A) increases domestic employment in industry X.
- B) increases domestic imports of good X.
- C) increases the domestic price of good X.
- D) has no effect unless the nation's trading partners also lower their tariffs on good X.
- E) increases government revenue.

Answer: B

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

AACSB: Analytical Skills

44) When the Canadian government imposes a tariff \_\_\_\_\_.

- A) Canadian consumers gain and Canadian producers lose, and the gain exceeds the loss
- B) the tariff revenue earned by the government is a social loss
- C) a social loss occurs because increased domestic production could have been obtained at a lower cost as an import
- D) Canadian producers lose
- E) A and B are both correct

Answer: C

Type: MC

Topic: International Trade Restrictions

Skill: Conceptual

Source: MyEconLab

AACSB: Analytical Skills

45) Among the following, the domestic government gains the most revenue when it

- A) imposes an import quota.
- B) eliminates an import quota.
- C) encourages freer trade.
- D) imposes a tariff.
- E) increases the demand for a domestically-produced good.

Answer: D

Type: MC

46) If a quota is set at the same quantity of imports that results from a tariff in Country A,

- A) the quantity consumed in Country A is less under the quota than under the tariff.
- B) the quantity consumed in Country A is the same under the quota and under the tariff.
- C) the quantity consumed in Country A is more under the quota than under the tariff.
- D) the government tariff revenue is greater than the importers' profit from the import quota.
- E) the government tariff revenue is less than the importers' profit from the import quota.

Answer: B

Type: MC

### 31.3 The Case Against Protection

1) Economists usually agree with which of the following arguments that favour protectionism?

- A) the competition with cheap foreign labour defence
- B) the job protection defence
- C) the dumping defence
- D) the infant-industry defence
- E) None of the above. Economists generally agree that arguments in favor of protection are flawed.

Answer: E

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Ethical Reasoning

2) Which of the following are valid reasons advanced by almost all economists? Protection

- A) saves jobs.
- B) prevents rich countries from exploiting developing countries.
- C) is a good way for governments in developed nations to raise revenue.
- D) penalizes lax environmental standards.
- E) Economists would not support any of the above reasons.

Answer: E

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Ethical Reasoning

3) Which of the following are reasons economists consider valid for trade protection?

- I. Protection penalizes countries that have weak environmental standards.
- II. Protection limits dumping of low-wage jobs into the domestic economy.
- III. Protection prevents low-wage jobs in foreign countries from lowering wages in Canada.

- A) I and II
- B) II and III
- C) I, II, and III
- D) I and III
- E) None of the above

Answer: E

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Ethical Reasoning

4) The idea of dynamic comparative advantage is the basis for which of the following arguments for protection from foreign competition?

- A) the cheap foreign labour argument
- B) the infant-industry argument
- C) the dumping argument
- D) the saves jobs argument
- E) the prevents rich countries from exploiting developing countries argument

Answer: B

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Reflective Thinking

5) The most efficient way to encourage the growth of an infant-industry is through

- A) a voluntary export restraint.
- B) a tariff.
- C) a subsidy.
- D) an import quota.
- E) none of the above.

Answer: C

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Reflective Thinking

6) The proposition that protection is necessary to allow an infant industry to grow into a mature industry so that it can compete in world markets is the \_\_\_\_\_.

- A) infant-maturity argument
- B) infant-industry argument
- C) new industry proposition
- D) growth proposition
- E) dynamic comparative advantage argument

Answer: B

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Reflective Thinking

7) Dumping occurs when a foreign firm \_\_\_\_\_.

- A) pollutes international waters
- B) disposes of waste material internationally
- C) sells inferior output to foreigners
- D) sells its exports at a lower price than its cost of production
- E) sells its output at a lower price in a foreign country than in the country where it produces the good

Answer: D

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Reflective Thinking

8) \_\_\_\_\_ occurs when a foreign firm sells its exports at a lower price than its cost of production.

- A) Comparative advantage
- B) Learning-by-doing
- C) A tariff
- D) An infant industry
- E) Dumping

Answer: E

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Reflective Thinking

9) Suppose that the country of Pacifica sold its cars in Atlantica for less than it costs to produce the cars. Pacifica could be accused of

- A) avoiding import quotas.
- B) increasing its gains from trade.
- C) dumping.
- D) engaging in learning-by-doing.
- E) exploiting a comparative advantage.

Answer: C

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Reflective Thinking

- 10) When a firm "dumps" some of its output in another country, it
- A) creates an environmental hazard in the receiving country.
  - B) sells its output abroad at a price lower than it costs to produce the output.
  - C) increases the total level of employment in the importing country.
  - D) is specializing according to comparative advantage.
  - E) creates for itself an absolute advantage.

Answer: B

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Reflective Thinking

- 11) In poorer countries, free trade \_\_\_\_\_ the demand for labour in these countries and \_\_\_\_\_ the wages paid in these countries.

- A) decreases; lowers
- B) decreases; raises
- C) increases; lowers
- D) increases; raises
- E) increases the supply and decreases; lowers

Answer: D

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Reflective Thinking

- 12) Which of the following statements is true?

- A) International trade raises wages in developing countries.
- B) International trade with rich industrial countries forces people in the developing countries to work for lower wages.
- C) International trade leads to job losses in both import competing industries and exporting industries.
- D) Unlike other types of international trade, offshoring does not bring any gains from trade.
- E) All of the above.

Answer: A

Diff: 2 Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Reflective Thinking

- 13) The argument that protection \_\_\_\_\_.
- A) penalizes poor environmental standards is true
  - B) allows us to compete with cheap foreign wages is true
  - C) is necessary for infant industries is true
  - D) saves jobs is flawed
  - E) prevents rich countries from exploiting poor countries is true.

Answer: D

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Reflective Thinking

- 14) Which of the following is an explanation for the existence of trade restrictions?

- A) tariffs generate revenue for the government
- B) rent seeking
- C) inefficient quotas
- D) both A and B
- E) both A and C

Answer: D

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Reflective Thinking

- 15) In industrial countries, there is more reliance on \_\_\_\_\_, as opposed to \_\_\_\_\_ for government revenue.

- A) tariffs; tax collection
- B) import quotas; tariffs
- C) tariffs; import quotas
- D) import quotas; tax collection
- E) tax collection; tariffs

Answer: E

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Reflective Thinking

16) In developing countries, there is more reliance on \_\_\_\_\_ as opposed to \_\_\_\_\_ for government revenue.

- A) tariffs; tax collection
- B) import quotas; tariffs
- C) tax collection; tariffs
- D) tariffs; import quotas
- E) import quotas; tax collection

Answer: A

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Reflective Thinking

17) Of the groups listed below, which is most likely to lobby for protection?

- A) workers in the import industry
- B) workers in the export industry
- C) consumers in the import industry
- D) producers in the export industry
- E) All of the above.

Answer: A

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Ethical Reasoning

18) Rent seeking is one reason why countries choose to

- A) export and import the same goods.
- B) work for freer trade.
- C) follow the theory of comparative advantage.
- D) hire foreign labour.
- E) restrict trade.

Answer: E

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Reflective Thinking

19) When considering rent seeking, which of the following is *TRUE*?

- A) The anti-free trade group generally will lobby more than the pro-free trade group.
- B) The pro-free trade group generally will lobby more than the anti-free trade group.
- C) Usually only the anti-free trade group is concerned about what is best for society at large.
- D) Only the pro-free trade group is concerned about the government's revenue from tariffs.
- E) None of the above.

Answer: A

Type: MC

Topic: The Case Against Protection

Skill: Recognition

AACSB: Reflective Thinking

20) One reason that international trade is restricted is that

- A) the individual gain to parties who benefit from the protection will be much larger than the individual loss to parties who lose.
- B) the government completely pays the losers from international trade for their losses.
- C) protectionism benefits consumers.
- D) the government cannot measure the cost of protectionism.
- E) tariff revenue raises more income than income taxes in industrial countries.

Answer: A

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Ethical Reasoning

21) Usually the *removal* of trade barriers affecting a particular good benefits \_\_\_\_\_ people domestically, each of whom gains a \_\_\_\_\_.

- A) a few; little
- B) a few; lot
- C) many; little
- D) many; lot
- E) We can't determine the relative benefits from the removal of trade barriers.

Answer: C

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Ethical Reasoning

22) Usually the *imposition* of trade barriers affecting a particular good benefits \_\_\_\_\_ people domestically, each of whom gains a \_\_\_\_\_.

A) a few; little

B) a few; lot

C) many; little

D) many; lot

E) We can't determine the relative benefits from the imposition of trade barriers.

Answer: B

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Ethical Reasoning

23) The gains from free trade are enjoyed by a \_\_\_\_\_ number of people and the costs of free trade are imposed on a \_\_\_\_\_ number of people.

A) small; large

B) large; small

C) small; small

D) large; large

E) We can't determine the relative number of people who benefit and lose from free trade.

Answer: B

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

AACSB: Reflective Thinking

24) The effects of offshoring from opening up call centres in India are similar to the effects from

A) free trade.

B) tariffs.

C) import quota.

D) voluntary export restraints.

E) export subsidies.

Answer: A

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

Source: Study Guide

AACSB: Reflective Thinking

25) Two reasons that explain why international trade in 2010 remains restricted is that restricted international trade \_\_\_\_\_.

- A) benefits domestic producers of import-competing goods and services and generates tariff revenue in developing countries
- B) prevents developed countries from exploiting third world countries and saves jobs in those countries
- C) brings diversity and stability to the whole economy and saves jobs in developing countries
- D) saves jobs and penalizes developing countries that have lax environmental standards
- E) brings diversity to the whole economy and penalizes countries that have lax environmental standards

Answer: A

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

Source: MyEconLab

AACSB: Reflective Thinking

26) Offshore outsourcing occurs when a firm in Canada \_\_\_\_\_.

- A) hires foreign labour and produces in other countries
- B) buys finished goods, components, or services from other firms in other countries
- C) buys finished goods, components, or services from other firms in Canada
- D) hires Canadian labour and produces in Canada
- E) hires foreign workers who work in Canada

Answer: B

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

Source: MyEconLab

AACSB: Reflective Thinking

27) When a firm implements offshore outsourcing, consumers in Canada \_\_\_\_\_, workers in Canada in the industry that is being outsourced \_\_\_\_\_ and workers in the foreign country in the industry that is being outsourced \_\_\_\_\_.

- A) gain; lose; lose
- B) lose; lose; gain
- C) lose; gain; lose
- D) gain; lose; gain
- E) gain; gain; gain

Answer: D

Type: MC

Topic: The Case Against Protection

Skill: Conceptual

Source: MyEconLab

AACSB: Reflective Thinking

28) The infant industry argument is based on the idea of

- A) global comparative advantage.
- B) global absolute advantage.
- C) tariff maximization.
- D) learning-by-doing.
- E) tariff minimization.

Answer: D

Type: MC

29) Offshoring occurs when a firm in Canada

- A) hires foreign labour and produces in other countries.
- B) buys finished goods, components, or services from other firms in other countries.
- C) hires Canadian labour and produces in Canada.
- D) buys finished goods, components, or services from other firms in Canada.
- E) Both A and B are correct.

Answer: E

Type: MC