Principles of Microeconomics 12th edition Case Test Bank

SKU: 9780134078816-TEST-BANK

Principles of Microeconomics, 12e **(Case/Fair/Oster)**
Chapter 2 The Economic Problem: Scarcity and Choice

2.1 Scarcity, Choice, and Opportunity Cost

1) The process by which resources are transformed into useful forms is
A) capitalization.
B) consumption.
C) production.
D) allocation.
Answer: C
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

2) Outputs in the production process are
A) pollution.
B) money.
C) goods and services of value to households.
D) resources.
Answer: C
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

3) Which of the following is *not* a resource as the term is used by economists?
A) land
B) labor
C) buildings
D) money
Answer: D
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

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4) Which of the following would an economist classify as capital?
A) a $50 bill
B) a corporate bond
C) a post office employee
D) a guitar used by a musician
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

5) Capital, as economists use the term,
A) is the money the firm spends to hire resources.
B) is money the firm raises from selling stock.
C) refers to the process by which resources are transformed into useful forms.
D) refers to things that have already been produced that are in turn used to produce other goods and services.
Answer: D
Diff: 3
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

6) The concept of opportunity cost is based on the principle of
A) need.
B) consumption.
C) scarcity.
D) profit.
Answer: C
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

7) The concept of trade-offs would become irrelevant if
A) we were dealing with a very simple, one-person economy.
B) poverty were eliminated.
C) scarcity were eliminated.
D) capital were eliminated.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-4

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8) Suppose you are deciding whether to spend your tax rebate check on a new iPod or a new digital camera. You are dealing with the concept of
A) equity.
B) comparative advantage.
C) opportunity costs.
D) the fallacy of composition.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

9) According to the theory of comparative advantage, specialization and free trade will benefit
A) only that trading party that has both an absolute advantage and a comparative advantage in the production of all goods.
B) all trading parties, even when some are absolutely more efficient producers than others.
C) only that trading party that has an absolute advantage in the production of all goods.
D) only that trading party that has a comparative advantage in the production of all goods.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-3

Refer to the information provided in Table 2.1 below to answer the following question(s).

Table 2.1

	Krystal	Mark
Writing Poems	8	12
Writing TV Commercials	2	4

10) Refer to Table 2.1. For Krystal, the opportunity cost of writing one TV commercial is
A) 1/4 of a poem.
B) 2 poems.
C) 4 poems.
D) 6 poems.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

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11) Refer to Table 2.1. For Mark, the opportunity cost of writing one TV commercial is
A) 1/3 of a poem.
B) 2 poems.
C) 3 poems.
D) 8 poems.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

12) Refer to Table 2.1. Which of the following statements is true?
A) Krystal has a comparative advantage in both writing TV commercials and writing poems.
B) Mark has a comparative advantage in both writing TV commercials and writing poems.
C) Krystal has a comparative advantage in writing TV commercials, and Mark has a comparative advantage in writing poems.
D) Mark has a comparative advantage in writing TV commercials, and Krystal has a comparative advantage in writing poems.
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

13) Refer to Table 2.1. To maximize total production,
A) Krystal should specialize in writing TV commercials, and Mark should specialize in writing poems.
B) Mark should specialize in writing TV commercials, and Krystal should specialize in writing poems.
C) Krystal and Mark should both split their time between writing poems and writing TV commercials.
D) Krystal should write poems and write TV commercials, but Mark should only write poems.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

14) Refer to Table 2.1. For Mark, the opportunity cost of writing six TV commercials is _____ poems.
A) 2
B) 18
C) 24
D) an indeterminate number of
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

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15) Refer to Table 2.1. For Krystal, the opportunity cost of writing four TV commercials is _____ poems.
A) 2
B) 8
C) 16
D) 32
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

16) According to the theory of comparative advantage, _____ raise(s) productivity by lowering opportunity costs.
A) trade and specialization
B) investment in capital goods
C) economic growth
D) exchange and consumption
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-3

17) When two people trade,
A) both of them expect to be made worse off by the exchange.
B) they are trying to help out each other.
C) they know one of them will get the better of the other.
D) they both expect to be made better off by the exchange.
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

18) Someone has a comparative advantage in producing a good if she can produce that good
A) in greater quantities.
B) at a lower opportunity cost.
C) using more capital and less labor.
D) using more labor and less capital.
Answer: B
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

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19) If someone has a comparative advantage in growing pineapples,
A) she can grow pineapples at a lower opportunity cost than other pineapple growers.
B) she also has an absolute advantage in growing pineapples.
C) she can grow more pineapples using the same resources than other pineapple growers.
D) pineapples are the only product she can grow.
Answer: A
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

20) Which of the following does *not* constitute an act of "investment" as economists use the term?
A) The city council authorizes the construction of a new fire station.
B) A retiree buys 50 shares of stock at $10 a share and then sells the stock at a profit for $20 a share.
C) An accountant attends a seminar on changes in the federal tax code.
D) A department store increases its inventory of football jerseys before the Super Bowl.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

21) In economics, investment always refers to
A) the act of buying stocks or bonds.
B) the creation of capital.
C) increasing the quantity of labor.
D) an increase in per capita output.
Answer: B
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-18

22) The process of using resources to produce new capital is
A) research and development.
B) investment.
C) consumption.
D) economic growth.
Answer: B
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-18

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23) An example of forgoing present benefits in order to receive future benefits is
A) production.
B) saving.
C) consumption.
D) growth.
Answer: B
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-18

24) Because resources are scarce, the opportunity cost of investment in capital is
A) zero.
B) forgone future consumption.
C) forgone present consumption.
D) infinite.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

25) An example of an investment is
A) the purchase of a share of Google stock.
B) the purchase of an ExxonMobil bond.
C) the purchase of a Hewlett Packard laser printer for use by a business.
D) all of the above.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-18

26) The opportunity cost of investment in capital is forgone present consumption because
A) capital takes a long time to produce.
B) capital increases the productivity of labor.
C) resources are scarce.
D) capital is an intangible good.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

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27) If the unemployment rate increases from 10% to 14%, the economy will
A) move closer to a point on the ppf.
B) move away from the ppf toward the origin.
C) remain on the ppf.
D) remain on the origin.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Macro-14

28) Periods of less than full employment correspond to
A) points outside the ppf.
B) points underneath the ppf.
C) points on the ppf.
D) either points inside or outside the ppf.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

Refer to the information provided in Figure 2.1 below for the economy of Macroland to answer the question(s) that follow.

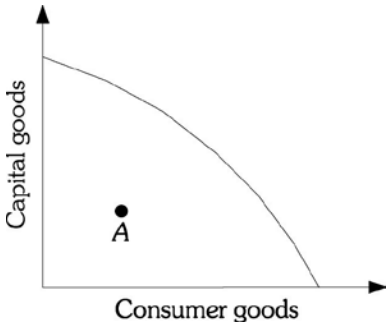


Figure 2.1

29) Refer to Figure 2.1. Macroland is currently operating at Point *A*. The best explanation for this is that
A) the economy has very poor technology.
B) the economy's resources are being used inefficiently.
C) the economy has very few resources.
D) the economy operates as an efficient market.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-19

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30) Refer to Figure 2.1. Macroland's production possibility frontier is bowed out from the origin due to
A) decreasing opportunity costs.
B) trade.
C) unemployment.
D) specialized resources.
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

31) Refer to Figure 2.1. The shape of Macroland's production possibility frontier shows
A) increasing opportunity costs.
B) constant opportunity costs.
C) decreasing opportunity costs.
D) random opportunity costs.
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

32) Refer to Figure 2.1. If Macroland's economy is at Point A, it could produce more consumer goods
A) without sacrificing any capital goods.
B) only by sacrificing some capital goods.
C) only with technological improvements.
D) only with additional resources.
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

33) Refer to Figure 2.1. If Macroland's economy is at Point A, it could produce more capital goods
A) without sacrificing any consumer goods.
B) only by sacrificing some consumer goods.
C) only with technological improvements.
D) only with additional resources.
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

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34) The production possibility frontier is used to illustrate the concept of
A) the laissez-faire economy.
B) opportunity costs.
C) equilibrium.
D) aggregate demand.
Answer: B
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

Refer to the information provided in Figure 2.2 below for the economy of Microland to answer the question(s) that follow.

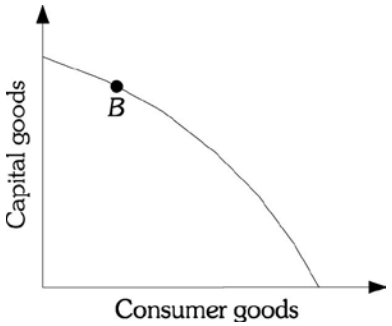


Figure 2.2

35) Refer to Figure 2.2. Point *B* represents a situation of
A) full employment but production inefficiency.
B) less than full employment but production efficiency.
C) both full resource employment and production efficiency.
D) less than full employment and production inefficiency.
Answer: C
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-19

36) Refer to Figure 2.2. Microland is currently operating at Point *B*. You correctly deduce that
A) in Microland, all resources are fully employed and there are no production inefficiencies.
B) Microland has achieved a position of inefficiency.
C) Microland has recently experienced some type of technological breakthrough.
D) Microland has overcome the problem of scarcity.
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-19

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37) Refer to Figure 2.2. If Microland's economy is at Point A, it could produce more consumer goods
A) without sacrificing any capital goods.
B) by sacrificing some capital goods.
C) only with technological improvements.
D) only with additional resources.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

38) Refer to Figure 2.2. If Microland's economy is at Point A, it could produce more capital goods
A) without sacrificing any consumer goods.
B) by sacrificing some consumer goods.
C) only with technological improvements.
D) only with additional resources.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

39) Refer to Figure 2.2. Full resource employment and production efficiency is represented by a point
A) inside the production possibility frontier.
B) along the production possibility frontier.
C) outside the production possibility frontier.
D) either inside or along the production possibility frontier.
Answer: B
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-19

40) Refer to Figure 2.2. You correctly deduce that all resources are fully employed and there are no production inefficiencies if this economy is currently operating at a point
A) inside the production possibility frontier.
B) along the production possibility frontier.
C) outside the production possibility frontier.
D) either inside or along the production possibility frontier.
Answer: B
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-19

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41) The production possibility frontier is a graph that shows
A) all the combinations of goods and services that are consumed over time if all of society's resources are used efficiently.
B) the amount of goods and services consumed at various average price levels.
C) the rate at which an economy's output will grow over time if all resources are used efficiently.
D) all the combinations of goods and services that can be produced if all of society's resources are used efficiently.
Answer: D
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-19

42) Production inefficiency occurs
A) only when an economy produces underneath its production possibility frontier.
B) only when an economy produces at the wrong point on the production possibility frontier.
C) either when an economy produces underneath the production possibility frontier or when the economy is producing the wrong combination of goods on the production possibility frontier.
D) only when the economy produces outside the production possibility frontier.
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-19

43) An economy that is producing on the production possibility frontier at some point other than the output of efficient allocation is
A) efficient, as it is on the production possibility frontier.
B) inefficient, as the combination of goods and services produced is not what people want.
C) efficient, as the economy is producing goods at the lowest possible cost.
D) inefficient, as that combination of goods could be produced at a lower cost if more efficient technology were employed.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-19

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44) If resources are combined efficiently in production, then the society
A) is producing at the most-desirable point on the production possibility frontier.
B) is producing at a point on the production possibility frontier but not necessarily at the most-desirable point.
C) is producing at a point outside the production possibility frontier.
D) is experiencing economic growth.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-19

45) If an economy begins to use its resources more efficiently, it will move
A) closer to its ppf.
B) farther away from its ppf.
C) from a point along its ppf to a point outside its ppf.
D) from one point to another point along its ppf.
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-19

46) The value of the slope of a society's production possibility frontier is called its
A) marginal rate of substitution.
B) inflation rate.
C) unemployment rate.
D) marginal rate of transformation.
Answer: D
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-19

47) The marginal rate of transformation is the
A) slope of the production possibility frontier.
B) dollar value of the best forgone alternative.
C) process of using resources to produce new capital.
D) transformation of resources into a form that is useful to people.
Answer: A
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-19

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Refer to the information provided in Figure 2.3 below to answer the question(s) that follow.

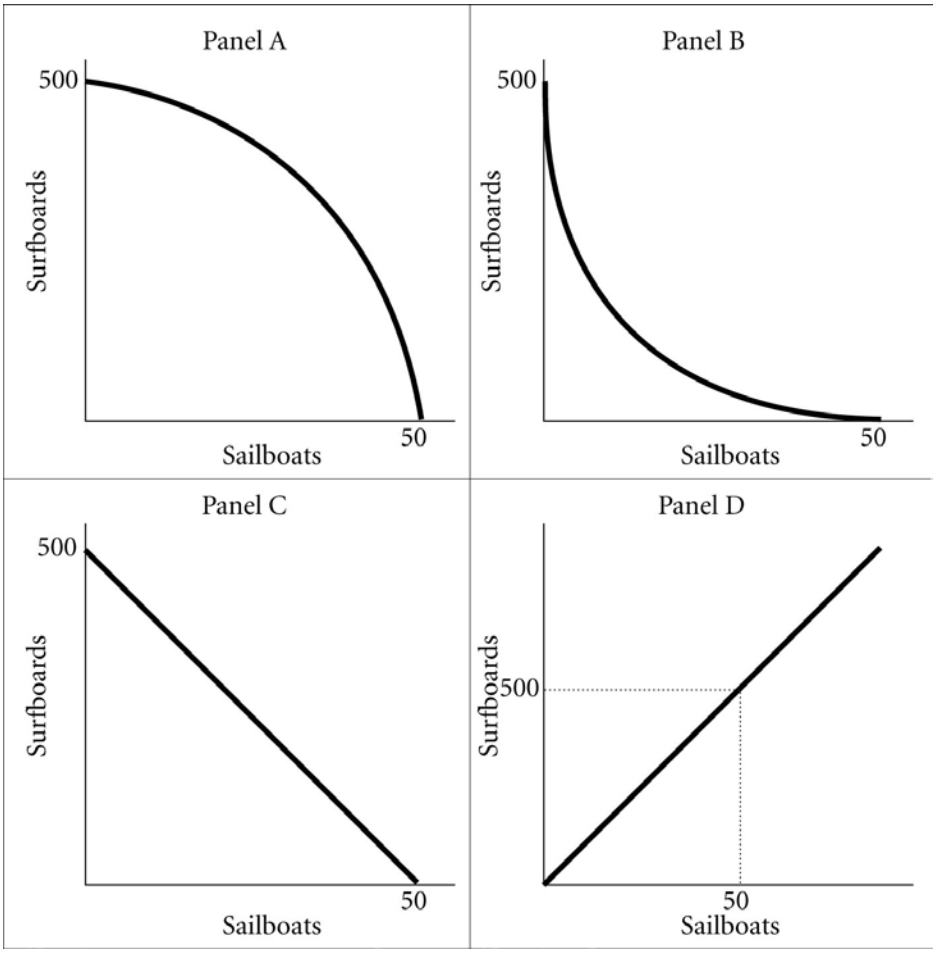


Figure 2.3

48) Refer to Figure 2.3. Assume that in this society the marginal rate of transformation of sailboats for surfboards is constant and equal to -10. A graph of this society's production possibility frontier will be represented by Panel
A) A.
B) B.
C) C.
D) D.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-19

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49) Refer to Figure 2.3. Assume that in this society the opportunity cost of sailboats in terms of surfboards is increasing. A graph of this society's production possibility frontier will be represented by Panel
A) A.
B) B.
C) C.
D) D.
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

50) Refer to Figure 2.3. The law of _____ opportunity costs is best depicted by the production possibilities frontier in Panel A.
A) increasing
B) constant
C) decreasing
D) zero
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

51) Refer to Figure 2.3. Assume that this society's production possibility frontier is represented by Panel C. The marginal rate of transformation of sailboats for surfboards is
A) 1/10.
B) -1/10.
C) 10.
D) -10.
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-19

52) Refer to Figure 2.3. Assume that this society's production possibility frontier is represented by Panel C. The opportunity cost of sailboats in terms of surfboards is
A) constant.
B) increasing.
C) decreasing.
D) infinite.
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

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53) Refer to Figure 2.3. Increasing opportunity costs are best depicted by the production possibility frontier in Panel
A) A.
B) B.
C) C.
D) D.
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

54) A society can produce two goods: donuts and beer. The society's production possibility frontier is negatively sloped and "bowed outward" from the origin. As this society moves up its production possibility frontier, producing more and more units of donuts, the opportunity cost of producing beer
A) decreases.
B) remains constant.
C) increases.
D) could decrease or increase depending on the technology.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

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Refer to the information provided in Figure 2.4 below to answer the question(s) that follow.

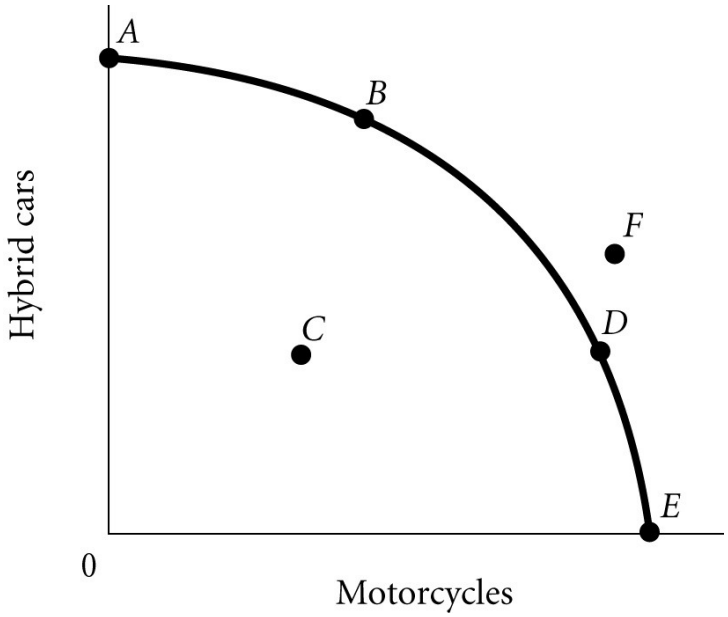


Figure 2.4

55) According to Figure 2.4, the point where only motorcycles are produced is
A) *A*.
B) *B*.
C) *C*.
D) *E*.
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

56) According to Figure 2.4, the optimal point for the economy is
A) *A*.
B) *B*.
C) *F*.
D) indeterminate from the information given.
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

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57) According to Figure 2.4, which point cannot be produced with the current state of technology?
A) *A*
B) *B*
C) *C*
D) *F*
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

58) According to Figure 2.4, the point where only hybrid cars are produced is
A) *A*.
B) *B*.
C) *C*.
D) *D*.
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

59) According to Figure 2.4, a decrease in unemployment may be represented by the movement from
A) *B* to *A*.
B) *B* to *D*.
C) *C* to *D*.
D) *A* to *C*.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

60) According to Figure 2.4, as the economy moves from Point *A* to Point *E*, the opportunity cost of motorcycles, measured in terms of hybrid cars,
A) decreases.
B) increases.
C) remains constant.
D) initially increases, then decreases.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

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61) According to Figure 2.4, as the economy moves from Point *E* to Point *A*, the opportunity cost of hybrid cars, measured in terms of motorcycles,
A) increases.
B) decreases.
C) remains constant.
D) initially increases, then decreases.
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

62) Refer to Figure 2.4. The economy moves from Point *A* to Point *D*. This could be explained by
A) a reduction in unemployment.
B) an improvement in technology.
C) an increase in economic growth.
D) a change in society's preferences for motorcycles versus hybrid cars.
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-10

63) According to Figure 2.4, Point *A* necessarily represents
A) an unattainable production point.
B) only hybrid cars being produced.
C) the economy's optimal production point.
D) what society wants.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

64) According to Figure 2.4, Point *F*
A) is efficient and attainable.
B) represents underallocation of resources.
C) represents what the people want.
D) cannot be produced with the current state of technology.
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

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65) According to Figure 2.4, Point *E* necessarily represents
A) an impossible production point.
B) technological advancement.
C) overallocation of resources.
D) only motorcycles being produced.
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

66) According to Figure 2.4, an increase in unemployment may be represented by the movement from
A) *B* to *A*.
B) *B* to *D*.
C) *C* to *D*.
D) *A* to *C*.
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

67) According to Figure 2.4, as the economy moves from Point *B* to Point *D*, the opportunity cost of motorcycles, measured in terms of hybrid cars
A) remains constant.
B) decreases.
C) increases
D) initially increases, then decreases.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

68) According to Figure 2.4, as the economy moves from Point *D* to Point *B*, the opportunity cost of hybrid cars, measured in terms of motorcycles
A) remains constant.
B) decreases.
C) increases.
D) initially increases, then decreases.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

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69) Refer to Figure 2.4. The economy moves from Point *E* to Point *B*. This could be explained by
A) an increase in unemployment.
B) a reduction in unemployment.
C) a change in society's preferences for hybrid cars versus motorcycles.
D) an increase in economic growth.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-10

Refer to the information provided in Figure 2.5 below to answer the question(s) that follow.

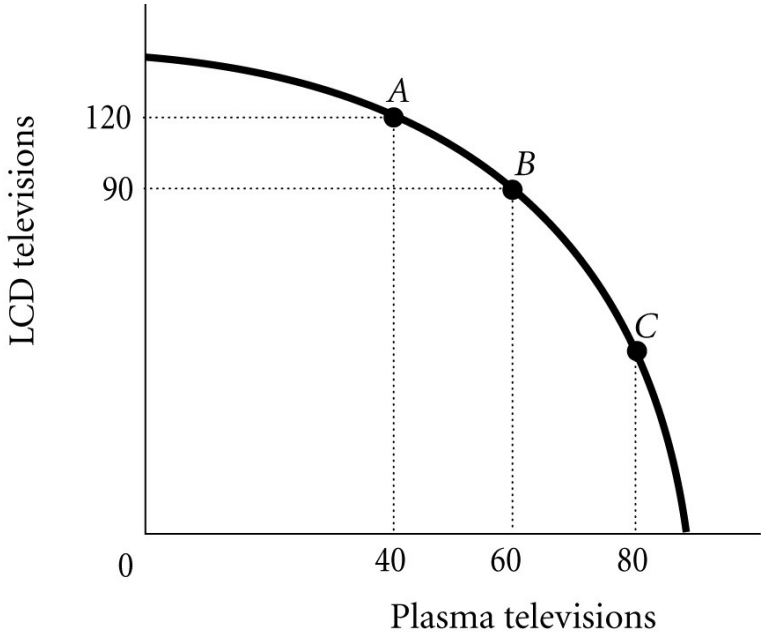


Figure 2.5

70) Refer to Figure 2.5. The economy is currently at Point *A*. The opportunity cost of moving from Point *A* to Point *B* is the
A) 90 LCD televisions that must be forgone to produce 20 additional plasma televisions.
B) 30 LCD televisions that must be forgone to produce 60 additional plasma televisions.
C) 120 LCD televisions that must be forgone to produce 40 additional plasma televisions.
D) 30 LCD televisions that must be forgone to produce 20 additional plasma televisions.
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

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71) Refer to Figure 2.5. The marginal rate of transformation in moving from Point *A* to Point *B* is
A) -2/3.
B) -1.5.
C) -3.
D) -30.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

72) Refer to Figure 2.5. For this economy to move from Point *B* to Point *C* so that an additional 20 plasma televisions could be produced, production of LCD televisions would have to be reduced by
A) exactly 30.
B) fewer than 30.
C) more than 30.
D) exactly 60.
Answer: C
Diff: 3
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

73) Refer to Figure 2.5. The best point for society would be
A) Point *C*, as at this point there are approximately equal amounts of LCD and plasma televisions being produced.
B) either Point *B* or Point *C*, as the total amount being produced at either of these points is approximately the same.
C) at any of the labeled points, as all of the points represent an efficient allocation of resources.
D) indeterminate from this information, as we don't have any information about the society's desires.
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

74) Refer to Figure 2.5. The economy is currently at Point *B*. The opportunity cost of moving from Point *B* to Point *A* is the
A) 40 plasma TVs that must be forgone to produce 120 additional LCD TVs.
B) 20 plasma TVs that must be forgone to produce 30 additional LCD TVs.
C) 30 LCD TVs that must be forgone to produce 40 additional plasma TVs.
D) 120 LCD TVs that must be forgone to produce 20 additional plasma TVs.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

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75) Refer to Figure 2.5. The marginal rate of transformation in moving from Point *B* to Point *A* is
A) -2/3.
B) -3/4.
C) -1.5.
D) -20.
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

76) Refer to Figure 2.5. For this economy to move from Point *A* to Point *B*, _____ additional plasma TVs could be produced when the production of LCD TVs is reduced by 30.
A) exactly 20
B) fewer than 20
C) more than 20
D) exactly 90
Answer: A
Diff: 3
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

77) Refer to Figure 2.5. For this economy to move from Point *C* to Point *B*, _____ additional LCD TVs could be produced when the production of plasma TVs is reduced by 20.
A) exactly 30
B) fewer than 30
C) more than 30
D) exactly 60
Answer: B
Diff: 3
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

78) If the opportunity costs of producing a good increase as more of that good is produced, the economy's production possibility frontier will be
A) negatively sloped and "bowed inward" toward the origin.
B) negatively sloped and "bowed outward" from the origin.
C) a negatively sloped straight line.
D) a positively sloped straight line.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

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79) As you move down the production possibility frontier, the absolute value of the marginal rate of transformation
A) increases.
B) decreases.
C) initially increases, then decreases.
D) initially decreases, then increases.
Answer: A
Diff: 3
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

80) As more of a good, such as television sets, is produced, the opportunity costs of producing it increases. This most likely occurs because
A) as more of a good is produced, the inputs used to produce that good will increase in price.
B) consumers would be willing to pay higher prices for the good as more of the good is produced.
C) resources are not equally well suited to producing all goods, and as more of a good is produced, it is necessary to use resources less well suited to the production of that good.
D) as more of a good is produced, the quality of that good declines, and therefore the costs of production increase.
Answer: C
Diff: 3
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

81) Economic growth most likely occurs when
A) a society moves inside its production possibility frontier.
B) a society learns to produce more using existing resources.
C) the society begins to produce the combination of goods society wants most.
D) a society moves along its production possibilities frontier.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

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Refer to the information provided in Figure 2.6 below to answer the question(s) that follow.

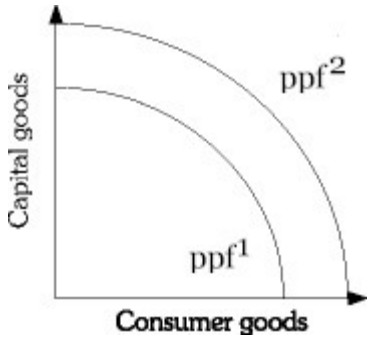


Figure 2.6

82) Refer to Figure 2.6. Economic growth is represented by a
A) shift from *ppf*2 to *ppf*1.
B) shift from *ppf*1 to *ppf*2.
C) movement along *ppf*1.
D) movement along *ppf*2.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-2

83) Refer to Figure 2.6. An improvement in technology may be represented by a
A) shift from *ppf*2 to *ppf*1.
B) shift from *ppf*1 to *ppf*2.
C) movement along *ppf*2.
D) movement along *ppf*1.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-2

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84) Refer to Figure 2.6. Which of the following will shift an economy's production possibility frontier from ppf_1 to ppf_2?
A) a decrease in unemployment
B) an increase in production efficiency
C) a change in consumers' tastes
D) an increase in the economy's capital stock
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-2

85) Refer to Figure 2.6. Which of the following will *not* cause the production possibility frontier to shift from ppf_1 to ppf_2?
A) the discovery of previously unknown oil fields
B) an improvement in technology
C) an increase in the stock of capital
D) a decrease in the unemployment rate
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

86) Refer to Figure 2.6. Which of the following is most likely to shift the production possibility frontier from ppf_1 to ppf_2?
A) a change in consumer tastes
B) the purchase of stocks on the New York Stock Exchange
C) moving resources from capital to consumer goods
D) an increase in the general educational level of the population
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-2

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87) Refer to Figure 2.6. If the economy is at ppf_1, a change in consumer preferences would be shown by a
A) shift from ppf_2 to ppf_1.
B) movement along ppf_1.
C) movement along ppf_2.
D) shift from ppf_1 to ppf_2.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-2

88) Refer to Figure 2.6. An increase in the economy's capital stock is represented by a
A) shift from ppf_2 to ppf_1.
B) shift from ppf_1 to ppf_2.
C) movement along ppf_1.
D) movement along ppf_2.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-2

89) Refer to Figure 2.6. A shift from ppf_1 to ppf_2 may be caused by
A) an increase in inflation.
B) an increased desire for consumer goods.
C) a change in consumer tastes.
D) an improvement in technology.
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-2

90) Refer to Figure 2.6. Which of the following will shift an economy's production possibility frontier from ppf_2 to ppf_1?
A) a decrease in the economy's capital stock
B) an increase in production efficiency
C) a change in consumer's tastes
D) economic growth
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-2

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91) Refer to Figure 2.6. Which of the following is most likely to shift the production possibility frontier from ppf_2 to ppf_1?
A) a change in consumer tastes
B) the purchase of government Treasury bills
C) moving resources from consumer goods to capital goods
D) a decrease in the general educational level of the population
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-2

92) Refer to Figure 2.6. If the economy is at ppf_2, a change in consumer taste would be shown by a
A) shift from ppf_2 to ppf_1.
B) movement along ppf_1.
C) movement along ppf_2.
D) shift from ppf_1 to ppf_2.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-2

93) During the Iraq War, many of Iraq's oil refineries were destroyed. This would best be represented by a
A) movement down Iraq's production possibility frontier.
B) movement off Iraq's production possibility frontier to some point inside the frontier.
C) shift of Iraq's production possibility frontier toward the origin.
D) movement up Iraq's production possibility frontier.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

94) For an economy to produce at a point beyond its current ppf, the economy must
A) waste less.
B) be more efficient.
C) reduce inputs.
D) increase its resource base.
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

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95) In terms of the production possibility frontier, an increase in productivity attributable to new technology would best be shown by
A) a movement along the frontier.
B) the production possibility frontier shifting outward, away from the origin.
C) a movement from a point inside the frontier to a point on it.
D) a movement toward the origin.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

96) An improvement in technology will cause the
A) production possibility frontier to shift outward.
B) production possibility frontier to shift inward.
C) economy to move down the production possibility frontier.
D) economy to move closer to its production possibility frontier.
Answer: A
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

97) Consider two countries, Japan and Malaysia. Japan devotes a smaller portion of its production to capital. All other things equal, which of the following statements is most likely true?
A) Japan is a poorer country than Malaysia.
B) Japan will move up its production possibility curve faster than Malaysia.
C) Malaysia is producing inside its production possibility frontier, whereas Japan is producing at a point on its production possibility frontier.
D) Malaysia's production possibility frontier will shift up and out farther and faster than Japan's.
Answer: D
Diff: 3
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

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98) The gap between rich and poor countries
A) has decreased over time because poor countries can more easily devote resources to capital production.
B) has increased over time because poor countries find it difficult to devote resources to capital production.
C) has remained constant over time because technological advances can be easily shared among nations.
D) has remained constant over time because the rate of capital production has remained constant in rich and poor nations.
Answer: B
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Fact
Learning Outcome: Micro-19

99) An economy produces capital goods and consumer goods. This economy is operating at a point on its production possibility frontier associated with a small amount of capital goods and a large amount of consumer goods. This is most likely to be a
A) "poor" country because such a nation has difficulty devoting many resources to the production of capital goods.
B) "rich" country because such a nation can afford to sacrifice.
C) country with a free market.
D) country with a command economy.
Answer: A
Diff: 3
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-19

100) The economic problem can best be stated as
A) How can the economy improve technology so as to shift the production possibility frontier up and to the right?
B) Given scarce resources, how exactly do societies go about deciding what to produce, how to produce it, and for whom to produce?
C) Given the fact that the economy is inefficient, how much and what type of government intervention should be used to improve the efficiency of the economy?
D) What is the best rate of economic growth for a society?
Answer: B
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

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101) Related to the *Economics in Practice* on page 25: Which one of the following occurs when an individual enters the paid work force?
A) The opportunity cost of time for housework increases, because time spent on housework could be spent on money-earning activities.
B) The opportunity cost of time for housework increases, because money earned at a job can allow individuals to pay someone to do household chores that the individuals used to do themselves.
C) The opportunity cost of time for housework decreases, because increased earning power makes individuals less likely to do their own housework.
D) The opportunity cost of time for housework decreases, because as more people enter the work force, businesses have greater incentives to develop innovations that make housework more efficient.
Answer: A
Diff: 3
Topic: Scarcity, Choice, and Opportunity Cost: Economics in Practice
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

102) Related to the *Economics in Practice* on page 25: How did the introduction of the microwave oven in 1960 affect the market for frozen food?
A) It encouraged people to leave the work force by making cooking easier and less time-consuming.
B) It reduced the opportunity cost of eating frozen food by decreasing the amount of time required to prepare frozen meals.
C) It increased the financial cost of alternative methods of food preparation, such as conventional ovens.
D) It made frozen foods more appealing by increasing the variety of meals that could be frozen and reheated.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost: Economics in Practice
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

103) Related to the *Economics in Practice* on page 35: In the survey conducted by Esther Duflo and Abhijit Banerjee, the extremely poor were found to consume _____ of their budgets on food compared to people in the United States.
A) a significantly higher percentage
B) about the same percentage
C) a slightly lower percentage
D) approximately 50 percent less
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost: Economics in Practice
Skill: Fact
Learning Outcome: Micro-25

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104) Related to the *Economics in Practice* on page 35: The results of the survey conducted by Esther Duflo and Abhijit Banerjee found that in extremely poor societies,
A) household choice plays no role in consumption decisions.
B) all consumption decisions are made by the government.
C) household choice even plays a role in non-food-related consumption decisions.
D) the only consumption decisions in which household choice plays a role is in the consumption of biological needs such as food.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost: Economics in Practice
Skill: Fact
Learning Outcome: Micro-25

105) Production is the process by which
A) products are used by consumers.
B) resources are transformed into useful forms.
C) products are converted into capital.
D) resources are allocated and distributed.
Answer: B
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

106) Goods and services of value to households are
A) inputs in the production process.
B) outputs in the production process.
C) both inputs and outputs in the production process.
D) unrelated to the production process.
Answer: B
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

107) Which of the following is a resource as the term is used by economists?
A) buildings
B) labor
C) land
D) all of the above
Answer: D
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

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108) Which of the following would an economist classify as capital?
A) a new deposit of natural gas
B) a government savings bond
C) a police car
D) a $100 traveler's check
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

109) Economists refer to things that have already been produced that are in turn used to produce other goods and services as
A) land.
B) labor.
C) entrepreneurship.
D) capital.
Answer: D
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

110) The principle that the cost of something is equal to what is sacrificed to get it is known as the
A) marginal principle.
B) principle of opportunity cost.
C) principle of diminishing returns.
D) reality principle.
Answer: B
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-20

111) If scarcity was eliminated,
A) trade would become unnecessary.
B) opportunity costs would increase.
C) all nations would have an absolute advantage in producing all products.
D) the concept of trade-offs would become irrelevant.
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-4

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112) According to the theory of _____, specialization and free trade will benefit all trade partners, even when some are absolutely more efficient producers than others.
A) comparative advantage
B) absolute advantage
C) social equity
D) laissez-faire
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-3

Refer to the information provided in Table 2.2 below to answer the following question(s).

Table 2.2

	Molly	Pete
Avatar Design	6	8
Tattoo Design	3	2

113) Refer to Table 2.2. For Molly, the opportunity cost of designing one tattoo is
A) 1/2 of an avatar design.
B) 1 avatar design.
C) 2 avatar designs.
D) 3 avatar designs.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

114) Refer to Table 2.2. For Pete, the opportunity cost of designing one tattoo is
A) 1/4 of an avatar design.
B) 2 avatar designs.
C) 4 avatar designs.
D) 6 avatar designs.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

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115) Refer to Table 2.2. Which of the following statements is true?
A) Molly has a comparative advantage in both avatar design and tattoo design.
B) Pete has a comparative advantage in both avatar design and tattoo design.
C) Molly has a comparative advantage in avatar design and Pete has a comparative advantage in tattoo design.
D) Pete has a comparative advantage in avatar design and Molly has a comparative advantage in tattoo design.
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

116) Refer to Table 2.2. To maximize total production,
A) Molly should specialize in avatar design and Pete should specialize in tattoo design.
B) Pete should specialize in avatar design and Molly should specialize in tattoo design.
C) Molly and Pete should both split their time between designing avatars and tattoos.
D) Molly should design avatars and tattoos, but Pete should only design avatars.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

117) Refer to Table 2.2. For Pete, the opportunity cost of designing three tattoos is _____ avatar designs.
A) 6
B) 12
C) 24
D) an indeterminate number of
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

118) Refer to Table 2.2. For Molly, the opportunity cost of designing four tattoos is _____ avatar designs.
A) 6
B) 8
C) 12
D) 24
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

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119) According to the theory of comparative advantage, trade and specialization _____ productivity by _____ opportunity costs.
A) raise; raising
B) raise; lowering
C) lower; raising
D) lower; lowering
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-3

120) Specialization and trade exploit differences in productivity across workers and
A) only benefit the exporter.
B) only benefit the importer.
C) make everyone better off.
D) make everyone worse off.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

121) If someone can produce a good at a lower opportunity cost, she _____ in producing that good.
A) has a comparative advantage
B) has an absolute advantage
C) experiences no diminishing returns
D) experiences no marginal costs
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

122) If a vintner has a comparative advantage in producing wine,
A) he can produce more wine using the same resources than other vintners.
B) wine is the only product he can produce.
C) he can produce wine at a lower opportunity cost than other vintners.
D) he also has an absolute advantage in producing wine.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

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123) Which of the following is an act of economic "investment"?
A) The state legislature authorizes the sale of a state park.
B) An entrepreneur buys 5,000 shares of stock at $5 a share and then sells the stock at a profit for $60 a share.
C) A brewer purchases a new fermentation system for his beer.
D) A teacher deposits $500 in a retirement account.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

124) In economics, the creation of capital is referred to as
A) investment.
B) comparative advantage.
C) consumption.
D) allocation.
Answer: A
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-18

125) The process of using resources to produce _____ is known as investment.
A) money
B) new capital
C) profit
D) inputs
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-18

126) Saving is an example of
A) exchanging capital for cash.
B) exchanging scarce resources for unlimited resources.
C) trading present benefits for future benefits.
D) trading future benefits for present benefits.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-18

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127) An example of an investment is
A) the purchase of an iPhone by a company for one of its salesmen.
B) the purchase of a share of Berkshire Hathaway stock.
C) the purchase of a government Treasury bill.
D) all of the above
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-18

128) Because resources are scarce, the opportunity cost of investment in capital is
A) past investment.
B) past consumption.
C) foregone present consumption.
D) future consumption.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

129) If the unemployment rate decreases from 9% to 6%, the economy will
A) move closer to a point on the ppf.
B) move away from the ppf toward the origin.
C) remain on the ppf.
D) remain on the origin.
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-14

130) Periods of full employment correspond to
A) points outside the ppf.
B) points inside the ppf.
C) points on the ppf.
D) either points inside or outside the ppf.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

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131) If an economy is fully utilizing its resources, it can produce more of one product only if it
A) doubles manufacturing of the product.
B) produces less of another product.
C) adds more people to the labor force.
D) reduces the price of the most expensive products.
Answer: B
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

132) All the combinations of goods and services that can be produced if all of society's resources are used efficiently are represented on an economy's
A) production possibility frontier.
B) resource availability diagram.
C) factors of production statement.
D) allocative allotment graph.
Answer: A
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-19

133) When an economy is producing inside its production possibility frontier,
A) production inefficiency occurs.
B) only technological advances will allow it to increase production.
C) it is efficient so long as it is producing what people want.
D) it must overcompensate by producing outside the curve to achieve efficiency.
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-19

134) If an economy is producing on its production possibility frontier but is not producing what people want, the economy
A) is experiencing technological advancement.
B) is producing at more than one point on the production possibility frontier.
C) is not achieving output efficiency.
D) is not being productively efficient.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-19

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135) If a society is producing at a point along its production possibility frontier, then the society
A) is fully employing its resources so it must be achieving output efficiency.
B) is fully employing its resources, but not necessarily achieving output efficiency.
C) is underallocating resources so it must be inefficient.
D) is overallocating resources so efficiency is indeterminate.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-19

136) If an economy begins to use its resources less efficiently, it will move
A) to a point closer to its ppf.
B) to a point farther away from its ppf.
C) from a point along its ppf to a point outside its ppf.
D) from one point to another point along its ppf.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-19

137) Assume a society can produce either beer or wine. If the marginal rate of transformation of gallons of beer into gallons of wine is 0.5, then the opportunity cost of beer is
A) the 2 gallons of beer that must be forgone.
B) the 2 gallons of wine that must be forgone.
C) the 0.5 gallons of beer that must be forgone.
D) the additional 0.5 gallons of beer that can be produced.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
Learning Outcome: Micro-19

138) Assume a society can produce either beer or wine. If the marginal rate of transformation of gallons of beer into gallons of wine is 0.5, then the opportunity cost of wine is
A) the 2 gallons of beer that must be forgone.
B) the 2 gallons of wine that must be forgone.
C) the 0.5 gallons of beer that must be forgone.
D) the additional 0.5 gallons of beer that can be produced.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
Learning Outcome: Micro-19

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139) Assume a society can produce either olives or grapes. If the marginal rate of transformation of bushels of olives into bushels of grapes is 0.2, then the opportunity cost of grapes is
A) the 5 bushels of olives that must be forgone.
B) the 5 bushels of grapes that must be forgone.
C) the 0.2 bushels of olives that must be forgone.
D) the additional 0.2 gallons of olives that can be produced.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
Learning Outcome: Micro-19

140) Assume a society can produce either olives or grapes. If the marginal rate of transformation of bushels of olives into bushels of grapes is 0.2, then the opportunity cost of olives is
A) the 5 bushels of olives that must be forgone.
B) the 5 bushels of grapes that must be forgone.
C) the 0.2 bushels of olives that must be forgone.
D) the additional 0.2 gallons of olives that can be produced.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
Learning Outcome: Micro-19

141) A society can produce two goods: green tea and vitamin water. As this society moves down its production possibility frontier, producing more and more units of vitamin water, the opportunity cost of producing vitamin water increases. The society's production possibilities frontier will be
A) positively sloped and bowed outward.
B) positively sloped and bowed inward.
C) negatively sloped and bowed outward.
D) negatively sloped and bowed inward.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

142) If an economy's production possibility frontier is negatively sloped and "bowed outward" from the origin, then the opportunity cost of producing a good
A) increases as more of that good is produced.
B) decreases as more of that good is produced.
C) remains constant as more of that good is produced.
D) remains constant as less of that good is produced.
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

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143) As you move up the production possibility frontier, the absolute value of the marginal rate of transformation
A) increases.
B) decreases.
C) initially increases, then decreases.
D) initially decreases, then increases.
Answer: A
Diff: 3
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

144) Because resources are not equally well suited to producing all goods,
A) as more of a good is produced, the inputs used to produce that good will increase in price.
B) the opportunity costs of producing a good will increase as more of that good is produced.
C) the opportunity costs of producing a good will decrease as more of that good is produced.
D) as more of a good is produced, the quality of that good declines and therefore the costs of production increase.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

145) Economic growth may occur when
A) a society acquires new resources.
B) a society decides to produce less using existing resources.
C) the society begins to produce the combination of goods society wants most.
D) technology remains unchanged but unemployment increases.
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

146) Due to a mild winter, Florida experienced a bumper crop of oranges. This would best be represented by a(n)
A) movement down the U.S. production possibility frontier.
B) movement off the U.S. production possibility frontier to some point inside the frontier.
C) movement up the U.S. production possibility frontier.
D) outward shift of the U.S. production possibility frontier away from the origin.
Answer: D
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Analytical
AACSB: Analytical Thinking
Learning Outcome: Micro-20

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147) In terms of the production possibility frontier, _____ would best be shown by the production possibility frontier shifting outward.
A) an increase in productivity attributable to an increase in the capital stock
B) a decrease in the unemployment rate
C) a shift in resources from capital goods to consumer goods
D) a change in consumer tastes
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

148) An increase in the stock of capital will cause the
A) production possibility frontier to shift outward.
B) production possibility frontier to shift inward.
C) economy to move down the production possibility frontier.
D) economy to move closer to its production possibility frontier.
Answer: A
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

149) A decrease in the stock of capital will cause the
A) production possibility frontier to shift outward.
B) production possibility frontier to shift inward.
C) economy to move down the production possibility frontier.
D) economy to move closer to its production possibility frontier.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

150) Consider two countries, Estonia and Ukraine. Estonia devotes a larger portion of its production to capital. All other things equal, which of the following statements is most likely true?
A) Estonia is a poorer country than Ukraine.
B) Estonia will move up its production possibility curve faster than Ukraine.
C) Estonia's production possibility frontier will shift up and out farther and faster than Ukraine's.
D) Ukraine is producing inside its production possibility frontier, whereas Estonia is producing at a point on its production possibility frontier.
Answer: C
Diff: 3
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

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151) From 1935 to 2009, the yield per acre for corn has _____ in the United States.
A) slightly declined
B) roughly doubled
C) almost tripled
D) increased more than 6-fold
Answer: D
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Fact
Learning Outcome: Micro-19

152) From 1935 to 2009, the yield per acre for wheat has _____ in the United States.
A) slightly declined
B) roughly doubled
C) more than tripled
D) increased more than 6-fold
Answer: C
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Fact
Learning Outcome: Micro-19

153) An economy produces capital goods and consumer goods. This economy is operating at a point on its production possibility frontier associated with a large amount of capital goods and a small amount of consumer goods. This is most likely to be a
A) "poor" country because such a nation has difficulty devoting many resources to the production of consumer goods.
B) "rich" country because such a nation can afford to sacrifice.
C) country with a free market.
D) country with a command economy.
Answer: B
Diff: 3
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-19

154) Given scarce resources, how societies go about deciding what to produce, how to produce it, and for whom to produce best describes
A) decreasing opportunity costs.
B) the fallacy of composition.
C) Ockham's razor.
D) the economic problem.
Answer: D
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

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155) Related to the *Economics in Practice* on p. 25: Based on the increase in the number of women in the labor force over the past 50 years, the opportunity cost of preparing a home-cooked meal
A) decreased.
B) increased.
C) remained constant.
D) dropped to zero.
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost: Economics in Practice
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

156) Related to the *Economics in Practice* on p. 25: One reason for the increase in sales of frozen foods from $1 billion in 1950 to $44 billion in 2012 is the
A) increased opportunity cost of cooking frozen meals.
B) decrease in the number of women in the labor force.
C) increased opportunity cost of preparing home-cooked meals.
D) decrease in popularity of the microwave oven.
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost: Economics in Practice
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-20

157) Related to the *Economics in Practice* on p. 35: In the survey conducted by Esther Duflo and Abhijit Banerjee, the extremely poor were found to consume _____ of their budgets on weddings, funerals, and other festivals.
A) virtually none
B) less than 5 percent
C) almost 10 percent
D) over half
Answer: C
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost: Economics in Practice
Skill: Fact
Learning Outcome: Micro-25

158) Related to the *Economics in Practice* on p. 35: In all societies, resources are limited relative to people's demands, and there are _____ trade-offs individuals face in rich countries versus poor countries.
A) fewer
B) large differences in the kinds of
C) virtually no differences in the types of
D) more important
Answer: B
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost: Economics in Practice
Skill: Fact
Learning Outcome: Micro-25

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159) In economics, the term *capital* refers only to some form of money.
Answer: FALSE
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

160) Among the resources used in production are labor and capital.
Answer: TRUE
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

161) Things that have already been produced that are in turn used to produce other goods and services over time are called "capital."
Answer: TRUE
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

162) Points outside a production possibility frontier represent inefficiency.
Answer: FALSE
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-3

163) Economic growth shifts a society's production possibility frontier away from the origin.
Answer: TRUE
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-3

164) A society's production possibility frontier is bowed in from the origin due to specialized resources.
Answer: FALSE
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-3

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165) The "economic problem" is that given scarce resources, how do large societies go about answering the basic economic questions of what will be produced, how it will be produced, and who will get it.
Answer: TRUE
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

166) Comparative advantage refers to the ability to produce better quality goods than a competitor.
Answer: FALSE
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

167) Comparative advantage refers to the ability to produce at a lower opportunity cost than a competitor.
Answer: TRUE
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

168) The marginal rate of transformation is the slope of the production possibility frontier.
Answer: TRUE
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

169) In economics, the term "investment" refers to the purchase of stocks and bonds.
Answer: FALSE
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

170) Resources are also referred to as outputs.
Answer: FALSE
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

171) The inputs into the process of production are called factors of production.
Answer: TRUE
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

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172) When two people trade, one must lose for the other to win.
Answer: FALSE
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-3

173) A bowed-out production possibility frontier represents decreasing opportunity costs.
Answer: FALSE
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-3

174) A society's production possibility frontier is bowed out from the origin because some resources are better suited for producing one good as opposed to the other.
Answer: TRUE
Diff: 2
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-3

175) The marginal rate of transformation represents the slope of the production possibility frontier.
Answer: TRUE
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

176) Comparative advantage refers to the ability to produce goods at a lower opportunity cost, and therefore more efficiently, than a competitor.
Answer: TRUE
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

177) Comparative advantage refers to the ability to produce at a lower financial cost than a competitor.
Answer: FALSE
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Definition
Learning Outcome: Micro-1

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178) Manufacturers produce only what the market is willing to pay for.
Answer: FALSE
Diff: 1
Topic: Scarcity, Choice, and Opportunity Cost
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

2.2 Economic Systems and the Role of Government

1) An economy in which a central authority draws up a plan that establishes what will be produced and when, sets production goals, and makes rules for distribution is a
A) free-market economy.
B) laissez-faire economy.
C) public-goods economy.
D) command economy.
Answer: D
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Definition
Learning Outcome: Micro-1

2) An economy in which individual people and firms pursue their own self-interest without any central direction or regulation is a(n)
A) command economy.
B) laissez-faire economy.
C) invisible-hand economy.
D) private-sector economy.
Answer: B
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Definition
Learning Outcome: Micro-1

3) Private enterprise plays some role in production decisions for
A) all countries in the world.
B) most countries in the world.
C) about half of the countries in the world.
D) few countries in the world.
Answer: B
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Fact
AACSB: Reflective Thinking
Learning Outcome: Micro-19

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4) Which of the following is an element of a command economy?
A) The market decides distribution.
B) The means of production are privately owned.
C) Production decisions are centralized.
D) The market decides what will be produced.
Answer: C
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

5) Which of the following statements is *not* true for a command economy?
A) Consumers have some choices concerning what they buy.
B) The government decides what is produced.
C) The amount of a good supplied always equals the amount of the good demanded.
D) The state decides how to distribute what is produced.
Answer: C
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

6) In a laissez-faire economy, _____ what gets produced, how it is produced, and who gets it.
A) the behavior of buyers and sellers determines
B) the central government authority determines
C) firms but not consumers determine
D) consumers but not firms determine
Answer: A
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

7) An institution through which buyers and sellers interact and engage in exchange is
A) a central authority.
B) "laissez-faire."
C) a market.
D) a production frontier.
Answer: C
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Definition
Learning Outcome: Micro-1

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8) A poorly functioning government can do which of the following to an economy?
A) destroy incentives
B) lead to corruption
C) waste society's resources
D) all of the above
Answer: D
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

9) Consumer sovereignty
A) is dependent on profits.
B) is the idea that consumers can buy whatever they want to.
C) is the idea that consumers determine what is produced in the economy through their demands.
D) is only possible in a monarchy.
Answer: C
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Definition
Learning Outcome: Micro-1

10) The idea that consumers ultimately dictate what not to produce by choosing what not to purchase is known as
A) laissez-faire.
B) the economic problem.
C) centralized decision making.
D) consumer sovereignty.
Answer: D
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Definition
Learning Outcome: Micro-1

11) The amount that households have accumulated out of past income through saving and inheritance is
A) future income.
B) wealth.
C) consumption.
D) present income.
Answer: B
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Definition
Learning Outcome: Micro-1

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12) In a free-market system, the amount of output that any one household gets depends on its
A) income.
B) wealth.
C) wage and interest income.
D) income and wealth.
Answer: D
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

13) Advocates of an unregulated market system argue that
A) competition promotes efficiency.
B) competition leads to innovation.
C) competition leads to product variety and quality.
D) all of the above
Answer: D
Diff: 2
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-3

14) The basic coordinating mechanism in a free-market system is
A) quantity.
B) price.
C) a central government authority.
D) the corporation.
Answer: B
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-3

15) Which of the following statements is *false*?
A) In a free-market system, the basic economic questions are answered without the help of a central government plan or directive.
B) Individuals guided by their own self-interest will produce products and services that other people want.
C) The basic coordinating mechanism in a free-market system is quantity adjustments toward equilibrium.
D) In a free-market system, competition forces firms to adopt efficient production techniques.
Answer: C
Diff: 2
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-3

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16) Some economists advocate government intervention in a market economy
A) to produce collective goods and services.
B) when resource costs for a private producer do not reflect the full cost to society.
C) to stabilize the economy.
D) all of the above
Answer: D
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-5

17) In a command economy, _____ establish(es) what will be produced and when, set(s) production goals, and make(s) rules for distribution.
A) individuals and households
B) only privately owned firms
C) a centralized authority
D) individuals, households and privately owned firms
Answer: C
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Definition
Learning Outcome: Micro-1

18) In a laissez-faire economy,
A) individual people and firms pursue their own self-interest.
B) the government decides how to distribute goods and services.
C) a centralized authority establishes what will be produced.
D) consumers do not exercise choice.
Answer: A
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Definition
Learning Outcome: Micro-1

19) Which of the following statements is true?
A) Planned economies have fared very well in recent years, with many of these economies thriving.
B) Command economies operate the most efficiently because the government makes all the production decisions.
C) In command economies consumers still exercise choice.
D) In a command economy, consumers answer the questions of what to produce, how to produce it, and how to distribute it.
Answer: C
Diff: 2
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-19

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20) Production decisions are centralized in a(n)
A) laissez-faire economy.
B) command economy.
C) invisible-hand economy.
D) utopian economy.
Answer: B
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

21) Which of the following statements is true for a command economy?
A) Consumers have no choice concerning what they buy.
B) Manufacturers decide what is produced.
C) The amount of a good supplied always equals the amount of the good demanded.
D) The state decides how to distribute what is produced.
Answer: D
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

22) In a _____ economy, the behavior of buyers and sellers determines what gets produced, how it is produced, and who gets it.
A) command
B) laissez-faire
C) socialist
D) utopian
Answer: B
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

23) In a market system, self-interest motivates most people to
A) avoid paying insurance premiums.
B) remain self-sufficient.
C) provide products for other people.
D) rely on government central planning.
Answer: C
Diff: 2
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

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24) Which of the following is true of a market economy?
A) In its pure form, it is also known as a command economy.
B) Decisions are regulated by a central agency.
C) The government answers the basic economic questions of what gets produced, how it gets produced, and who gets it.
D) It relies on millions of individual economic decisions to determine economic outcomes.
Answer: D
Diff: 2
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

25) The idea that consumers determine what is produced in the economy through their demands is known as
A) a laissez-faire economy.
B) a command economy.
C) consumer sovereignty.
D) free enterprise.
Answer: C
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Definition
Learning Outcome: Micro-1

26) The freedom of individuals to start and operate private business in search of profits is known as
A) laissez-faire.
B) free enterprise.
C) centralized decision making.
D) consumer sovereignty.
Answer: B
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Definition
Learning Outcome: Micro-1

27) The amount that _____ have accumulated out of past income through saving and inheritance is wealth.
A) governments
B) households
C) markets
D) corporations
Answer: B
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Definition
Learning Outcome: Micro-1

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28) In a _____, the amount of output that any one household gets depends on its income and wealth.
A) Marxist economy
B) socialist economy
C) command system
D) free-market system
Answer: D
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

29) In which system are decisions made by thousands of people who have information about resources, production technology and consumer desires?
A) market system
B) centrally planned system
C) command system
D) socialist system
Answer: A
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-3

30) In a laissez-faire economy, what provides individuals the information needed to make decisions?
A) insurance
B) prices
C) patents
D) government
Answer: B
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-3

31) Combined, local, state, and federal governments in the United States directly employ about _____ percent of all workers.
A) 2
B) 6
C) 14
D) 27
Answer: C
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Fact
AACSB: Reflective Thinking
Learning Outcome: Micro-3

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32) Some economists advocate government intervention in a market economy when resource costs for a private producer _____ to society.
A) are greater than the full cost
B) are equal to the full cost
C) do not reflect the full cost
D) have no relevant cost
Answer: C
Diff: 2
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-5

33) A laissez-faire economy is one in which individual people and firms pursue their own self-interest without any central direction or regulation.
Answer: TRUE
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Definition
Learning Outcome: Micro-1

34) A command economy is one in which a central government sets output targets, incomes, and prices.
Answer: TRUE
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Definition
Learning Outcome: Micro-1

35) A command economy eliminates markets.
Answer: FALSE
Diff: 2
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

36) Price is the coordinating mechanism in a planned economy.
Answer: FALSE
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

37) The notion that buyers determine what will be produced by choosing what they purchase is called consumer sovereignty.
Answer: TRUE
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Definition
Learning Outcome: Micro-1

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38) The market system works by getting each person, motivated by his or her own self-interest, to produce products for other people.
Answer: TRUE
Diff: 2
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

39) All markets involve buyers and sellers engaging in exchange.
Answer: TRUE
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Definition
Learning Outcome: Micro-1

40) In their pure forms, laissez-faire economies and command economies do not exist in the world.
Answer: TRUE
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Fact
AACSB: Reflective Thinking
Learning Outcome: Micro-1

41) Price is the coordinating mechanism in a laissez-faire economy.
Answer: TRUE
Diff: 2
Topic: Economic Systems and the Role of Government
Skill: Conceptual
AACSB: Reflective Thinking
Learning Outcome: Micro-1

42) No market economies exist without government involvement and government regulation.
Answer: TRUE
Diff: 1
Topic: Economic Systems and the Role of Government
Skill: Conceptual
Learning Outcome: Micro-1

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Chapter 2

The Economic Problem: Scarcity and Choice

SCARCITY, CHOICE AND OPPORTUNITY COST

1. What are resources? Describe two different types of resources.

   Resources are anything provided by nature or previous generations that can be used directly, or indirectly, to satisfy human wants. Capital resources include machinery, equipment, and structures used to produce other goods and services. Human resources include labor, skills, and knowledge. Products of nature can also be used as resources.

   Diff: 1 Skill: Definitional Topic: Resources
   AACSB:

2. List the three basic *economic* questions that all societies must answer.

   (1.) What will be produced?
   (2.) How will it be produced?
   (3.) Who will get what is produced?

   Diff: 1 Skill: Factual Topic: Choice
   AACSB:

3. Explain the economic concept of *opportunity cost*.

   The opportunity cost of something is the best alternative that we give up when we make a choice or a decision.

   Diff: 1 Skill: Definitional Topic: Opportunity Cost
   AACSB:

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4. Explain how it might be possible to discuss costs of production of a good or service without using monetary values.

All costs are essentially opportunity costs. That is to say that it is simply the value of the next best available alternative. Therefore, it is possible to discuss costs without mentioning monetary costs by analyzing what was given up to produce a good or a service.

Diff: 1 Skill: Definitional Topic: Opportunity Cost
AACSB:

5. What critical resource is likely to be the culprit for the impending doom of Social Security regarding tax collection? Explain.

Because the baby-boom generation gave birth to fewer children these people will be part of the labor force that will be supporting the baby-boomers when they retire. Because their numbers are so much smaller the amount of taxes collected will be smaller as well.

Diff: 1 Skill: Definitional Topic: Resources
AACSB:

6. Suppose you have saved $300. You can spend it on a new stereo or on a weekend skiing trip. What is the opportunity cost of going on the skiing trip?

The opportunity cost of the skiing trip is the value of the next best alternative for using the $300 you have saved. If the next best alternative is purchasing the stereo, then the opportunity cost of going skiing is the enjoyment foregone by not purchasing the stereo.

Diff: 1 Skill: Conceptual Topic: Opportunity Cost
AACSB: Reflective Thinking

7. Suppose there is a new technological invention that will allow you to put any resource into a special black box and in an instant anything that you program it to produce will be produced? Does this invention end scarcity? Why or why not?

It does not end scarcity for the simple reason that you still need to use human labor to place the resources in the black box and the natural resources themselves of course are still scarce. In addition, this device will not limit our wants.

Diff: 1 Skill: Conceptual Topic: Scarcity
AACSB: Analytic Skills

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8. What is the opportunity cost of attending class today?

The opportunity cost of attending class today is the next best alternative for your time including sleeping, studying for another class, or earning income at a job. But it can't be all of these things since you can only do one of these things at a time.

Diff: 1 Skill: Conceptual Topic: Opportunity Cost
AACSB:

9. Suppose you could measure the value in monetary terms for the following three things that you could do with your time this Friday evening: a) doing your homework - $50, 2) spending time with your friends - $40 or c) taking a nap - $30. Armed with only this information which activity has the lowest opportunity cost? Which two activities have the same opportunity cost? Based on what you have discovered what is the best use of your time and why?

The opportunity cost of doing your homework is only $40 which is the next best available alternative. Spending time with your friends has an opportunity cost of $50 since this is the next best available alternative. And it turns out this is also the opportunity cost of taking a nap as well. Therefore, the best use of your time is to spend it doing your homework since the opportunity cost of doing so is lower than the other two alternatives.

Diff: 2 Skill: Conceptual Topic: Opportunity Cost
AACSB:

10. Critically evaluate the following statement. "Only poor nations face scarcity. Rich nations have everything they need and have therefore conquered scarcity."

Rich nations simply face different choices than do poor nations. The existence of choices naturally presumes that there is scarcity. Since all resources are limited there is only so many goods and services that can be produced by any nation whether it is poor or rich.

Diff: 2 Skill: Conceptual Topic: Scarcity
AACSB: Reflective Thinking

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11. Comment on the following statement: "I decided to buy a car from a dealer in a town 100 miles away because he was offering a price that was $100 lower than the dealer in my hometown. Therefore, I saved $100."

Assuming that the individual had no other reason to travel the 100 miles, the savings from the purchase of the car is less than $100. Travel costs should be taken into account, including the opportunity cost of time.

Diff: 1 Skill: Conceptual Topic: Opportunity Cost
AACSB: Analytic Skills

12. Explain why some researchers conclude that Americans are becoming more obese because of the existence of fast-food restaurants. If fast-food restaurants have been around for over 50 years why is the trend toward obesity only a recent one? Explain.

Essentially fast-food restaurants have become more prolific. The costs has fallen dramatically and coupled with their convenience and proximity to neighborhoods in both urban and suburban areas this has lowered the opportunity cost of eating out.

Diff: 2 Skill: Conceptual Topic: Opportunity Cost
AACSB: Analytical Skills

13. Suppose that a local government decides to provide more funds to the local police department in order for the department to hire additional police officers. Is there an opportunity cost of this action? If so, how would you measure it?

Yes, there is an opportunity cost. The opportunity cost should be measured by the next best alternative use of the funds provided to the police department.

Diff: 1 Skill: Conceptual Topic: Opportunity Cost
AACSB:

14. At which time is the opportunity cost likely to be higher to go to war, during a recession or during an economic boom? Explain your answer fully.

It is likely that going to war during an economic boom is more costly because many men and women who join the military or are drafted will more than likely be leaving behind a productive job. The rest of the country will experience a permanent sacrifice in terms of all the goods and services that will not be produced by them. During a recession many men and women are without jobs so the opportunity cost of deploying them in war is lower.

Diff: 2 Skill: Conceptual Topic: Opportunity Cost
AACSB: Reflective Thinking

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15. Michael Jordan has more athletic ability than most individuals. Thus, he is more productive at most tasks involving physical skill. Explain why then, it is more efficient for Michael Jordan to pay someone else to mow his lawn.

While Michael Jordan probably has an absolute advantage in mowing his lawn, the opportunity cost of his time is very high. He could spend the time it takes to mow his lawn in a variety of ways including earning a large amount of money making a commercial endorsement. Thus, it is likely that he does not have a comparative advantage in mowing his lawn.

Diff: 1 Skill: Conceptual Topic: Opportunity Cost
AACSB:

16. Because of the quantity and quality of its resources, the U.S. has an absolute advantage in the production of many goods and services. Does this imply that the U.S. cannot benefit from trading with a developing country that has less productive ability? Why or why not?

The U.S. can benefit from trading with less productive countries as long as it produces the goods for which it has a comparative advantage and trades to receive the goods for which it does not.

Diff: 2 Skill: Conceptual Topic: Absolute and comparative advantage
AACSB:

17. Assume that two countries are considering trading with each other for the first time. Also assume that one of the countries has an absolute disadvantage in producing everything compared to the other country. How would it still be possible for these two nations to benefit from trade with each other?

The reason that it would still be beneficial for each nation to trade with each other is because trade is not dependent on absolute advantage but rather comparative advantage. That means that one nation may be operating at an absolute disadvantage vis-à-vis another nation but still have a comparative advantage in at least one good or service.

Diff: 3 Skill: Conceptual Topic: Absolute and comparative advantage
AACSB:

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18. Evaluate the following statement. "The nation of Berundi has an absolute disadvantage in the production of everything compared to the United States. Therefore, the United States will have no reason to trade with Berundi".

This statement is false. The reason is that nations don't trade according to their absolute advantage but rather their comparative advantage. Even though the nation of Berdundi has an absolute disadvantage in the production of everything it is very unlikely that it won't have a comparative advantage in the production of at least one good or service vis-à-vis the United States.

Diff: 2 Skill: Conceptual Topic: Comparative advantage
AACSB: Reflective Thinking

19. Explain Ricardo's theory of comparative advantage.

Specialization and free trade will benefit all trading partners, including those that may be absolutely more efficient producers.

Diff: 1 Skill: Definitional Topic: Comparative Advantage
AACSB:

20. Mexico has lower wages than the United States. Does this necessarily mean that it will have a comparative advantage in the production of everything compared to the United States?

Wages are only one factor in the input mix. What matters is the overall opportunity cost of production. If wages are 1/5 the in Mexico compared to what they are in the United States and workers in Mexico are 1/5 as productive as American workers this doesn't translate necessarily into a comparative advantage for Mexico. Also, goods that are produced with a lot of capital which turns out to be more expensive in Mexico and less expensive in the U.S. will tip the comparative advantage to the United States.

Diff: 2 Skill: Conceptual Topic: Comparative Advantage
AACSB: Analytic Skills

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21. The following table shows output per hour for Martha and Stewart who make gift baskets and potholders:

	Output per Hour	
	Martha	**Stewart**
Giftbaskets	10	8
Potholders	20	12

What is the opportunity cost of a gift basket for Martha? What is the opportunity cost of a gift basket for Stewart? Who has a comparative advantage in producing gift baskets? How can you tell?

The opportunity cost of a gift basket for Martha is 2 potholders. The opportunity cost of a gift basket for Stewart is 1.5 potholders. Stewart has a comparative advantage in the production of gift baskets. His opportunity cost of producing a gift basket is lower.

Diff: 2 Skill: Analytical Topic: Opportunity cost and comparative advantage
AACSB:

22. Explain the difference between absolute advantage and comparative advantage.

A person has an absolute advantage in the production of a good if he or she is more productive at producing the good. A person has a comparative advantage in the production of a good if he or she can produce it at the lowest opportunity cost.

Diff: 1 Skill: Definitional Topic: Comparative and absolute advantage
AACSB:

23. Critically evaluate the following statement. "If a country has an absolute advantage in the production of everything it necessarily follows that it will have a comparative advantage in the production of everything."

This is patently false. Absolute advantage only implies that a good can be produced with fewer inputs versus a rival. Comparative advantage means that a good can be produced at lower opportunity cost than a rival. That means that a rival could have an absolute disadvantage in the production of a good or a service and still have a comparative advantage because of its lower opportunity costs.

Diff: 3 Skill: Analytical Topic: Comparative and absolute advantage
AACSB: Reflective Thinking

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24. Critically evaluate the following statement. "If a country can produce a good using fewer inputs than other country then that means that country enjoys a comparative advantage."

This is not true. What is being described here is an absolute advantage. In order to have a comparative advantage all that is needed is that a country produce the good with a lower opportunity cost but not necessarily with fewer inputs.

Diff: 3 Skill: Analytical Topic: Comparative and absolute advantage
AACSB: Reflective Thinking

25. If a comparative advantage implies that a country can produce a product at a lower opportunity cost than another country then why do we see two countries often trading the same goods? For instance, for most agricultural products the U.S. has a comparative advantage. Japan, one of America's largest trading partners has a comparative advantage in the production of most economy cars. Explain what is going on here when we still see the U.S. exporting cars to Japan and the U.S. importing some foods from Japan.

First of all not all goods are homogeneous. The U.S. may import some food from Japan that either is not available here or is produced at lower cost or has a higher perceived or actual quality differential. On the other hand while Japan has a comparative advantage in the production of many economy cars there is a cost difference and a quality difference across makes a models that doesn't allow for a apples-to-apples comparison.

Diff: 3 Skill: Definitional Topic: Comparative advantage and trade
AACSB: Reflective Thinking

26. Assume that a lawyer and a secretary have been working together for two years. The lawyer suddenly realizes that he prepares legal briefs and types faster than the secretary. Upon learning this he decides to let his secretary go. Why might this be a mistake?

It might be a mistake if it turns out that the secretary had a comparative advantage in typing over the lawyer. In other words it is very likely and possible that the secretary and type at a lower opportunity cost than the lawyer. By firing the secretary he has confused absolute advantage with comparative advantage.

Diff: 3 Skill: Definitional Topic: Comparative advantage and trade
AACSB: Reflective Thinking

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27. The following table shows output per hour for Martha and Stewart who make gift baskets and potholders:

	Output per Hour	
	Martha	**Stewart**
Gift Baskets	10	8
Potholders	20	12

What is the opportunity cost of a potholder for Martha? What is the opportunity cost of a potholder for Stewart? Who has an absolute advantage in producing potholders? Who has a comparative advantage in producing potholders?

The opportunity cost of a potholder for Martha is 1/2 of a gift basket. The opportunity cost of a potholder for Stewart is 2/3 of a gift basket. Martha has an absolute advantage and a comparative advantage in the production of potholders.

Diff: 2 Skill: Analytical Topic: Opportunity cost
AACSB:

28. The following table shows output per hour for Fred and Barney who mow lawns and trim hedges:

	Output per Hour	
	Fred	**Barney**
Lawns Cut	2	1
Hedges Trimmed	8	6

What is the opportunity cost of mowing a lawn for Fred? What is the opportunity cost of trimming a hedge for Fred? Who has a comparative advantage in mowing lawns? How can you tell?

The opportunity cost of mowing a lawn for Fred is 4 hedges trimmed. The opportunity cost of a trimming a hedge for Fred is 1/4 of a lawn mowed. Fred has a comparative advantage in mowing lawns. His opportunity cost of mowing a lawn is 4 hedges trimmed and Barney's opportunity cost of mowing a lawn is 6 hedges trimmed.

Diff: 2 Skill: Analytical Topic: Comparative advantage
AACSB:

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29. The following table shows output per hour for Mexico and Canada, two countries that produce beer and T-shirts:

	Output per Hour	
	Mexico	**Canada**
Beer (thousands of bottles)	5	10
T-shirts (thousands)	10	12

What is the opportunity cost of a bottle of beer for Mexico? What is the opportunity cost of a T-shirt for Mexico? Who has a comparative advantage in producing beer? How can you tell?

The opportunity cost of a bottle of beer for Mexico is 2 T-shirts. The opportunity cost of a T-shirt for Mexico is 1/2 bottle of beer. Canada has a comparative advantage in the production of beer. Canada's opportunity cost of producing a bottle of beer is 1.2 T-shirts and Mexico's opportunity cost of producing a bottle of beer is 2 T-shirts.

Diff: 2 Skill: Analytical Topic: Opportunity cost and comparative advantage
AACSB:

30. Suppose that Rosie and Betty spend their free time making cakes and cookies. Is it possible for Betty to have an absolute advantage in the production of both cakes and cookies? Is it possible for Betty to have a comparative advantage in the production of both cakes and cookies? Explain.

Yes, it is possible for Betty to have an absolute advantage in the production of cakes and cookies. This simply means that she is able to produce more per hour. However, Betty cannot have a comparative advantage in producing both cakes and cookies. Because the opportunity cost of producing a cookie is the reciprocal of the opportunity cost of making a cake, it is impossible to have the lower opportunity cost of each.

Diff: 1 Skill: Conceptual Topic: Absolute and comparative advantage
AACSB: Analytic Skills

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31. Papa Ray owns a pizzeria. He is more efficient at making pizza than anyone he could hire. Does this mean that he should make all of the pizzas himself?

No. This simply means that Papa Ray has an absolute advantage in making pizza. This does not mean that he has a comparative advantage in making pizza. It is possible that the opportunity cost of his time is high (he could be out selling franchises, for example).

Diff: 1 Skill: Conceptual Topic: Comparative advantage
AACSB:

32. Suppose the CEO of a major corporation has five subsidiary companies. Only one of these companies is making better than the return on similar investments that the company could be making if it invested its financial capital outside the company. The CEO tells each of these subsidiary companies that the rate of return that they are earning is not acceptable and must rise to the level of these identified companies. He tells them if they can't come up with a plan in twelve months that their companies will be sold. If each of these companies was actually making money can you come up with an economic argument for why it is still rational for this CEO to sell them if they don't abide by his directive.

The question really boils down to opportunity cost. If stock holders realize that their investments could do better elsewhere then they will be upset with the CEO even if the company is making money. The opportunity cost of hanging on to these companies is the difference between what they are making and what they could make. By selling of the ones that can't comply with the directive the company can take the proceeds and investment them in a way that will raise their return and profitability.

Diff: 3 Skill: Conceptual Topic: Opportunity cost
AACSB: Analytic Skills

33. Suppose that the opportunity cost of a student's time is greater when he studies than when he works. What mistake is he making and why?

By arguing that his opportunity cost is higher for studying than when he works the student is saying that work has a more highly valued use for his time than studying. Working has a lower opportunity cost because the value of studying is less than the value or working. He should be working, not studying.

Diff: 2 Skill: Conceptual Topic: Opportunity cost
AACSB:

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34. Suppose that you have saved $100. You can spend it today or you can put it in your savings account for a year and earn 5% interest. What is the opportunity cost of spending the money today?

If you put the money in your savings account, you will have $105 to spend next year on the item (or items) of your choice. Thus, the opportunity cost of spending the money today is the enjoyment you give up by not having the $105 to buy something next year.

Diff: 1 Skill: Conceptual Topic: Opportunity cost
AACSB:

35. Assume that yields on bonds (rate of return) begin to fall while the stock market is booming, what should we see happen to the demand and price of stocks and why? What can we say about the opportunity cost of holding on to bonds in this situation?

Lower bond yields will push many investors into stocks where they are seeking a higher rate of return. This should increase the demand for stocks and push up asset prices as well. The opportunity cost of holding on to bonds is high compared to owning stocks.

Diff: 2 Skill: Conceptual Topic: Opportunity cost
AACSB:

36. What is the difference between *capital goods* and *consumer goods*?

Capital goods are goods that will be used to produce other goods in the future. Consumer goods are goods that are used for current consumption.

Diff: 1 Skill: Definitional Topic: Capital goods and consumer goods
AACSB:

37. What is the opportunity cost of producing capital goods such as a new road?

The opportunity cost of producing a new road can be measured by the next best alternative that could have been produced with the same resources.

Diff: 1 Skill: Conceptual Topic: Capital goods
AACSB:

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38. In economic terminology, what is the meaning of *investment*?

Investment is the process of using resources to produce new capital. The new capital produced can be physical (new machinery) or human (education) in nature.

Diff: 1 Skill: Definitional Topic: Investment
AACSB:

39. How does an individual know whether or not an investment in education is worthwhile?

A worthwhile investment is one for which the expected present value of future benefits exceeds the present value of costs.

Diff: 1 Skill: Conceptual Topic: Investment
AACSB:

40. Define opportunity cost. Given the definition of opportunity cost, explain what is meant by the statement "There is no such thing as a free lunch."

Opportunity cost is what we give up, or forgo, when we make a choice. There is no such thing as a free lunch because everything involves a cost, even if it is just a time cost.

Diff: 2 Skill: Definitional Topic: Free lunch
AACSB:

41. Kathy and Amy paint pictures and do caricatures to sell to tourists. In one day, Kathy can either paint two pictures or do four caricatures. In one day, Amy can either paint three pictures or do three caricatures. For both Kathy and Amy, what is the opportunity cost of painting one picture? Who has the comparative advantage in painting pictures and who has the comparative advantage in doing caricatures? How might they be able to increase their total output?

Kathy's opportunity cost of painting a picture is two caricatures. Amy's opportunity cost of painting a picture is one caricature. Amy has a comparative advantage in painting and Kathy has a comparative advantage in doing caricatures. They could increase output by specializing in producing the goods for which they have a comparative advantage.

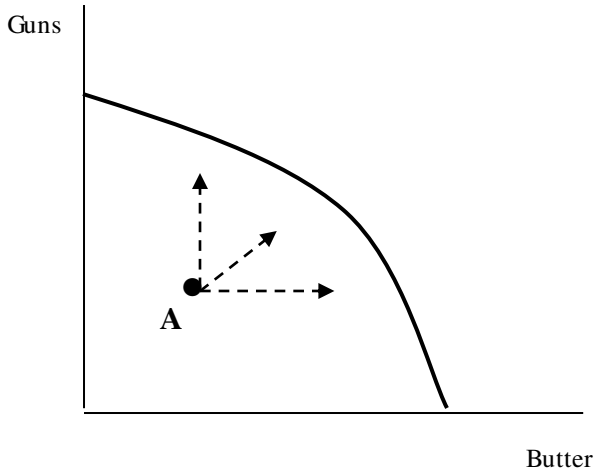
Diff: 2 Skill: Conceptual Topic: Opportunity cost
AACSB: Analytic Skills

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42. Use a graph and comment on the following statement: "If an economy is producing inside its production possibilities frontier, it could possibly produce more of one good without giving up any of the other."

In the graph below, we can see that, at point A, the economy has three options if it begins to produce more efficiently. First, it could continue producing the same level of guns and produce more butter. Second, it could continue producing the same level of butter and produce more guns. Last, the economy could increase production of both guns and butter.



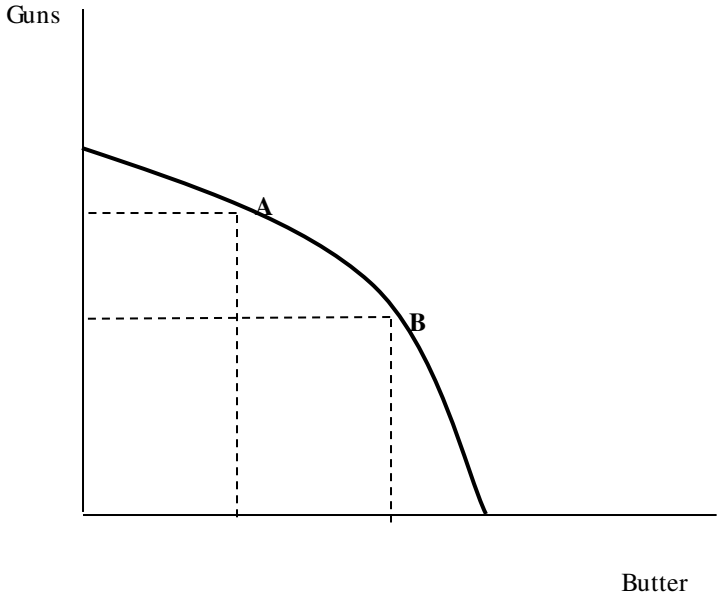
Diff: 1 Skill: Conceptual Topic: Production possibilities
AACSB:

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43. Use a graph and comment on the following statement: "If an economy is producing at a point on its production possibilities frontier, it could possibly produce more of one good without giving up any of the other."

This statement is false. In the graph above, we can see that if the economy moves from point A to point B (to increase the production of butter), some guns must be sacrificed.



Diff: 1 Skill: Conceptual Topic: Production Possibilities
AACSB:

44. What does a *production possibility frontier* represent?

A production possibility frontier is a graph that shows all of the combinations of goods and services that can be produced if all of society's resources are used efficiently.

Diff: 1 Skill: Definitional Topic: Production Possibilities
AACSB:

45. What can we say about the employment of resources if the economy is at a point on its production possibility frontier?

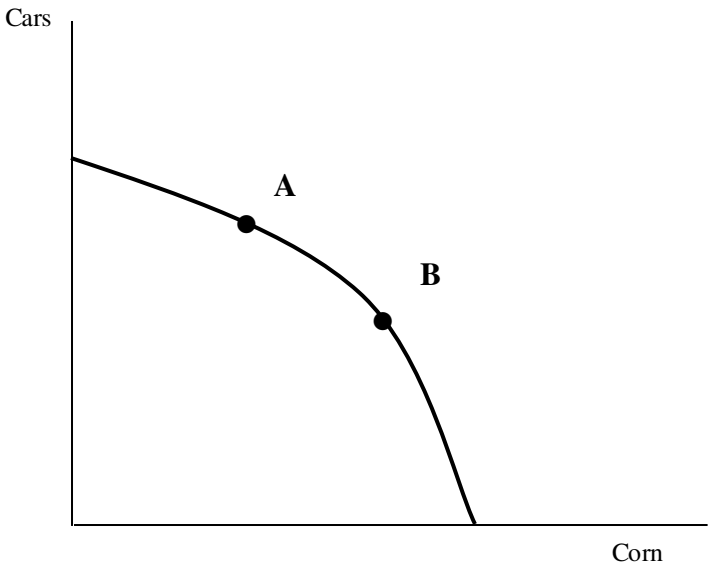
If the economy is at a point on its production possibility frontier, this implies that there is full resource employment and productive efficiency.

Diff: 1 Skill: Conceptual Topic: Production possibilities
AACSB:

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46.



Refer to the graph above. In what way could point A be considered more efficient than point B?

Both points represent productive efficiency since they are on the production possibility frontier. However, point A could be considered more efficient than point B if it represents the combination of cars and corn that members of society most want.

Diff: 1 Skill: Conceptual Topic: Productive efficiency
AACSB:

47. What can we say about the employment of resources if the economy is at a point inside its production possibility frontier?

If the economy is at a point inside its production possibility frontier, this implies that there is either unemployment of resources or productive inefficiency.

Diff: 1 Skill: Conceptual Topic: Inefficiency
AACSB:

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48. Is it possible in the present to produce at a point that is outside the production possibilities frontier? Why or why not? With the passage of time how might a point outside the present production possibilities frontier be possible?

In the present, points outside the production possibilities frontier are not possible because the frontier represents the current inputs and technology that are available to the economy. With the passage of time this points will become attainable when and if there is a positive change in technology and/or a discovery of new resources.

Diff: 1 Skill: Conceptual Topic: Production possibilities
AACSB:

49. What are the implications for economic growth for countries specializing in consumer goods rather than capital goods? Assume that they cannot trade what they produce.

All else equal, countries that specialize in consumer goods will likely grow less than those that specialize in capital goods, because specializing in capital goods will allow for more goods to be produced in the future.

Difficult: M Skill: Conceptual Topic: Economic growth
AACSB: Reflective Thinking

50. Why might an economist argue that it could be damaging to the economic growth of a nation if it focused mostly on the production of consumer goods?

The reason for concern is that focusing too much on the production of consumer goods necessarily implies cutting back on the production of capital goods. The problem is that economic growth is dependent on the production of capital goods.

Difficult: M Skill: Conceptual Topic: Economic growth
AACSB: Reflective Thinking

51. Without drawing a graph explain what probably happened to the production possibility frontier during the Black Plague.

The Black Plague killed off about one-third of the world's population during its rampage. This no doubt resulted in a decline in the labor force which pushed the production possibilities frontier inward.

Difficult: E Skill: Conceptual Topic: Production possibilities
AACSB:

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52. Assume that there were decreasing opportunity costs of production in an island economy that only produced two goods. What would the shape of the production possibilities frontier look like and why?

The production possibilities frontier would be downward-sloping and bowed into the origin. It would have this shape because as you move down the production possibilities frontier the amount of one good that you must give up will get smaller and smaller as you produce the second good.

Difficult: E Skill: Conceptual Topic: Production possibilities
AACSB:

53. Why does the production possibility frontier have a negative slope?

Because of scarce resources, increasing the production of one good or service implies that the production of the other good or service must be reduced. Thus, there is a negative relationship between the two goods and the production possibility frontier is downward sloping.

Diff: 1 Skill: Conceptual Topic: Production possibilities
AACSB:

54. What is meant by the *marginal rate of transformation*?

The marginal rate of transformation is the slope of the production possibility frontier. It is the ratio of the change in the good (or service) on the *y*-axis to the change in the good (or service) on the *x*-axis.

Diff: 1 Skill: Definitional Topic: Marginal rate of transformation
AACSB:

55. If the *marginal rate of transformation* is constant what can be said of the shape of the production possibilities frontier and why?

The marginal rate of transformation is the slope of the production possibility frontier. It is the ratio of the change in the good (or service) on the *y*-axis to the change in the good (or service) on the *x*-axis. If it is constant that means that the production possibilities frontier is a straight line. This is true because it would mean that the slope of the production possibilities frontier is the same throughout which of course is precisely one of the properties of a straight line.

Diff: 1 Skill: Conceptual Topic: Marginal rate of transformation
AACSB:

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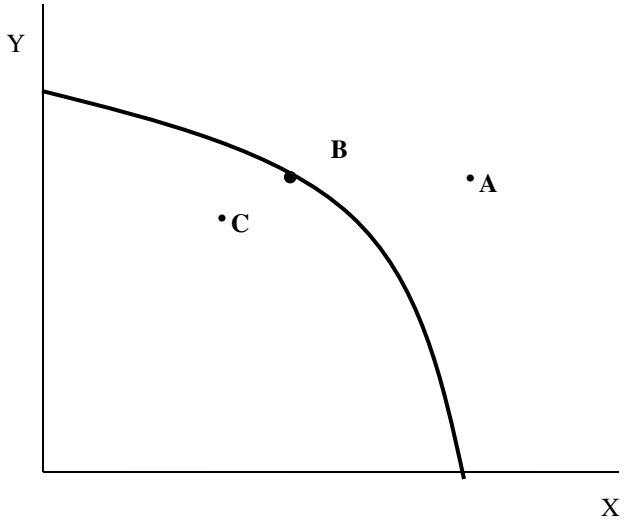
56. Suppose that there are two goods that a small island nation can produce – coconuts and breadfruit. If the inputs for both goods are perfectly interchangeable and there is never a rise or fall in opportunity cost explain what the production possibilities frontier should look like and why.

Production possibilities frontier are typically concave to the origin which reflects the law of increasing opportunity cost. In the present example this is not the case. The opportunity cost is constant which would lead to a downward-sloping but linear production possibilities frontier.

Diff: 1 Skill: Conceptual Topic: Law of increasing opportunity costs
AACSB:

57. Draw a production possibility frontier. Find a point that represents a combination of outputs that is not currently feasible. Label it point A. Find a point that represents efficient production. Label it point B. Find a point that represents inefficient production. Label it point C.

There are many possible answers here, but point A should be drawn outside of the production possibility frontier, point B should be on the production possibility frontier, and point C should be inside the production possibility frontier.



Diff: 1 Skill: Conceptual Topic: Production possibilities
AACSB:

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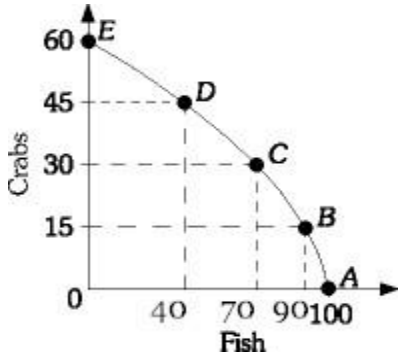
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Refer to the information provided in Scenario 1 below to answer the following questions.

SCENARIO 1: Consider the following data for the harvest of crabs versus the harvest of fish off the coast of Virginia in answering the following questions.

Combination	Fish	Crabs
A	100	0
B	90	15
C	70	30
D	40	45
E	0	60

58. Refer to Scenario 1. Graph the production possibilities frontier and calculate the average opportunity cost of any of the first fifteen crabs produced.



The opportunity cost of the first fifteen crabs is of course the 10 fish given up (15C = 10F). Therefore, the opportunity cost of any one crab is 10/15 F or 2/3 of a fish.

Diff: 2 Skill: Analytical Topic: Opportunity cost
AACSB:

59. Refer to Scenario 1. What is the economic significance of 25 fish captured and 25 crabs captured?

The economic significance of capturing 25 fish and 50 crabs is that the harvest would be inside the production possibilities frontier, which suggests some resource unemployment. That resource unemployment could be land, labor or capital. It could also be the result of an inefficient use of resources.

Diff: 2 Skill: Conceptual Topic: Inefficiencies
AACSB:

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60. Refer to Scenario 1. Explain how this economy might be able to produce 45 fish and 45 crabs?

The economy could do this with the benefits of an increase in resources or a technological advance in fishing.

Diff: 2 Skill: Conceptual Topic: Technology

61. Refer to Scenario 1. If this economy is currently producing 30 crabs and 40 fish how is it possible for it to produce more of both?

The reason that the economy can produce more crabs and more fish is because it is currently operating inside the production possibilities frontier. As it stands now there are idle or inefficiently used resources that can be put to work to produce more of both goods.

Diff: 2 Skill: Conceptual Topic: Inefficiencies
AACSB:

62. Refer to Scenario 1. Assume this economy could either be at Point B or Point C. From which of these points is it more costly to produce more crabs? Explain your answer.

It's more costly to produce more crabs from Point C than it is to produce more crabs from Point B. The reason is that as you move up the production possibilities frontier the more crabs you produce the greater the amount of fish the economy will have to give up to produce them. For example from Point B the opportunity cost of producing 15 more crabs is twenty fish. However, if we start from Point C and wish to produce 15 more crabs we have to give up 30 fish.

Diff: 3 Skill: Conceptual Topic: Inefficiencies
AACSB:

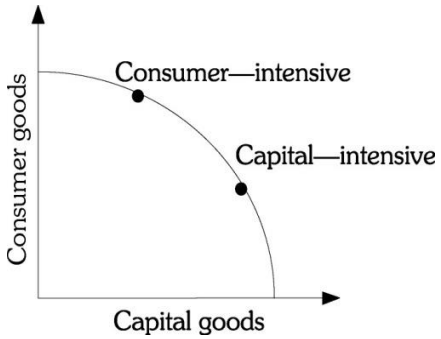
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Refer to the information provided in Scenario 2 below to answer the questions that follow.

SCENARIO 2: Assume that two countries are the same in every way except that one allocated more of its resources to the production of capital goods as opposed to consumer goods.

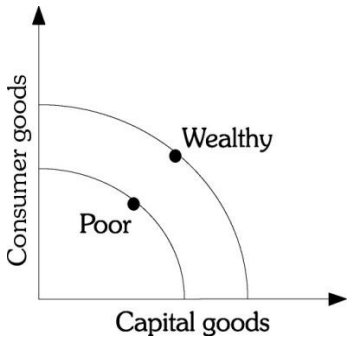
63. Refer to Scenario 2. Graphically illustrate the production choices on a production possibilities frontier. Which country's PPF will likely move out farther in the future and why?



The country with the capital intensive allocation will have its PPF move out farther since the economy will have greater productive capacity.

Diff: 1 Skill: Conceptual Topic: Production possibilities
AACSB:

64. Refer to Scenario 2. Now assume that the countries are not alike, but that one is wealthier than the other in that it has more resources. Graphically illustrate this scenario using the production possibilities frontiers.



Diff: 2 Skill: Conceptual Topic: Production possibilites
AACSB:

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65. Refer to Scenario 2. What would be the impact of improvements in technology assuming that each country spends one-half of its resources on capital goods?

There should be a greater improvement in wealth for the wealthier country if each country continues to spend the same percentages.

Diff: 1 Skill: Conceptual Topic: production possibilities
AACSB:

66. Refer to Scenario 2. What happens to the relative income distribution between the two countries under the conditions in the previous question? Explain.

The relative income distributions, with income of the capital-good intensive country greater than the consumer-good intensive country, would be expected to widen as the growth is greater in the capital-good intensive country.

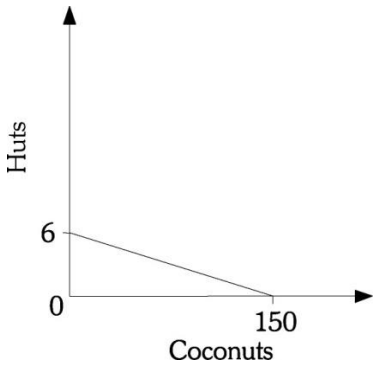
Diff: 3 Skill: Conceptual Topic: Income distribution
AACSB:

Refer to the information provided in Scenario 3 below to answer the questions that follow.

SCENARIO 3: Assume a desert island economy in which labor is the only scarce resource and labor can be used to gather food (coconuts) or to build huts. There are six equally productive individuals on the island. Each inhabitant can gather 25 coconuts in one day or build one hut in one day.

67. Refer to Scenario 3. Draw the production possibilities frontier of the trade-off between coconuts and huts.

Diff: 2 Skill: Analytical Topic: Production Possibilities
AACSB:



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68. Refer to Scenario 3. Compute the opportunity cost of building two more huts in one day.

First we start off by calculating what the opportunity cost is of building all 6 huts. We can set this up as an algebraic expression 6H = 150C. Therefore 1H = 25C and 2H = 50C or 50 coconuts.

Diff: 2 Skill: Analytical Topic: Opportunity Cost
AACSB:

69. Refer to Scenario 3. If half the workers build huts and half of the workers gather coconuts, what would be the production on the island?

In one day, the inhabitants would produce three huts and 75 coconuts.

Diff: 2 Skill: Analytical Topic: Production possibilities
AACSB:

70. Refer to Scenario 3. Assume that in one day, two huts were built and 75 coconuts were gathered. What does this situation depict?

The situation depicts the inefficient use of resources as the production point represents one that is inside the production possibilities frontier.

Diff: 2 Skill: Analytical Topic: Inefficiencies
AACSB:

71. Refer to Scenario 3. What is the maximum potential increase in coconut production and maximum potential increase in hut production described in the previous question?

The maximum potential increase in production is either one more hut or 25 more coconuts.

Diff: 2 Skill: Analytical Topic: Production possibilities
AACSB:

72. Refer to Scenario 3. What would have to occur for three huts to be produced along with 100 coconuts?

Some form of economic growth or technological improvement would have to occur.

Diff: 2 Skill: Analytical Topic: Economic growth
AACSB:

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Refer to the information provided in Scenario 4 below to answer the questions that follow.

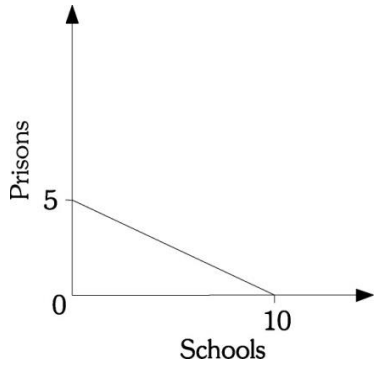
SCENARIO 4: Suppose that a state needs to build both prisons and schools with a budget limited to 10 million dollars. Schools cost $1 million each to build and prisons cost $2 million each to build.

73. Refer to Scenario 4. What is the maximum number of schools that can be built? The maximum number of prisons?

Ten is the maximum number of schools and five is the maximum number of prisons.

Diff: 2 Skill: Analytical Topic: Production possibilities
AACSB:

74. Refer to Scenario 4. Draw the state's production possibilities frontier for the trade-off between schools and prisons.



Diff: 2 Skill: Analytical Topic: Production possibilities
AACSB:

75. Refer to Scenario 4. What is the opportunity cost of building one more prison?

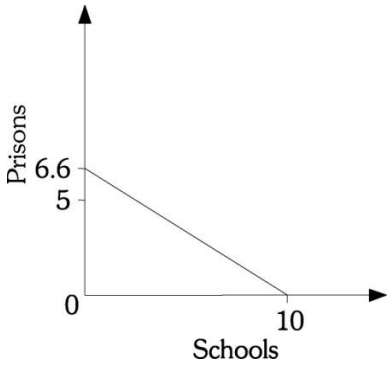
The opportunity cost of building one more prison is two schools. This is gleaned from the fact that the opportunity cost of 5 prisons is 10 schools or 5P = 10S. Solving for P leaves you with 2S or two schools

Diff: 2 Skill: Analytical Topic: Opportunity cost
AACSB:

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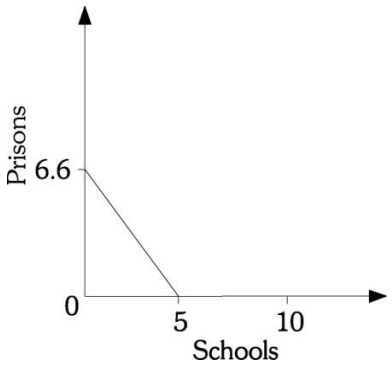
76. Refer to Scenario 4. Assume that the price of prison production falls to $1.5 million each. Draw the new production possibilities frontier. In addition, what is the new opportunity cost of producing one more prison?



One more prison now costs one and one-half schools (10/6.66).

Diff: 2 Skill: Analytical Topic: Opportunity cost
AACSB:

77. Refer to Scenario 4. Assume that the price of a prison falls to $1.5 million and that the price of school production rises to $2 million each. Draw the new production possibilities frontier. What is the new opportunity cost of producing one more prison?



In the new situation, the opportunity cost of producing one more prison is three quarters of a school.

Diff: 2 Skill: Analytical Topic: Opportunity cost
AACSB:

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78. Refer to Scenario 4. Assume that the state originally spent one-half of its budget on schools and one-half on prisons. What was the production of schools and prisons? Could the same number be achieved after the price of producing prisons falls to $1.5 million and the price of producing schools rises to $2 million? Explain.

Production is five schools and two and one-half prisons. No, the same number of schools and prisons could not be built after the price of production changes. If the state continues to divide its budget equally, production would be two and one-half schools and three and one-third prisons. If the budget were juggled, the maximum number of schools that could be built is five, but no prisons could be built. And, if two and one-half prisons were built, there would be enough left in the budget to build just over three schools.

Diff: 2 Skill: Analytical Topic: Production Possibilities
AACSB:

79. Why does the opportunity cost of producing a good rise as more resources are devoted to producing that good?

The opportunity cost of a good rises as we devote more resources to producing it because some resources are better suited to the production of one good than another. This is known as the law of increasing opportunity cost.

Diff: 1 Skill: Conceptual Topic: Law of increasing opportunity cost
AACSB:

	A	B	C	D	E
Rugs	50	45	35	20	0
Wheat	0	10	20	30	40

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80. The table above represents five points on the production possibility frontier for the small country of Baca, which produces only rugs (measured in thousands) and wheat (measured in thousands of bushels):

If the economy is currently at point A, what is the opportunity cost of producing an additional 10,000 bushels of wheat? If the economy is currently at point B, what is the opportunity cost of producing an additional 10,000 bushels of wheat? What if the economy is currently at point D?

If the economy is currently at point A, the opportunity cost of producing an additional 10,000 bushels of wheat is 5,000 rugs. If the economy is currently at point B, the opportunity cost of producing an additional 10,000 bushels of wheat is 10,000 rugs. If the economy is currently at point D, the opportunity cost of producing an additional 10,000 bushels of wheat is 20,000 rugs.

Diff: 1 Skill: Analytical Topic: Opportunity cost
AACSB:

81. The table above represents five points on the production possibility frontier for the small country of Baca, which produces only rugs (measured in thousands) and wheat (measured in thousands of bushels):

Does the production possibility frontier demonstrate the law of increasing opportunity cost? How can you tell?

Yes. The opportunity cost of increasing the production of wheat rises as more wheat is produced. The opportunity cost of the first 10,000 bushels of wheat is only 5,000 rugs, but the opportunity cost of the fourth 10,000 bushels of wheat is 20,000 rugs.

Diff: 2 Skill: Analytical Topic: Opportunity cost
AACSB:

82. If the law of increasing opportunity cost holds, can the production possibility frontier be a straight line?

No. If the production possibility curve is a straight line, this would imply that the marginal rate of transformation is constant. This cannot be the case if the law of increasing opportunity costs holds.

Diff: 2 Skill: Conceptual Topic: Law of increasing opportunity cost
AACSB:

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83. Explain why the costs of most services like haircuts and college education have risen at a faster rate relative to the costs of manufactured goods?

Manufactured goods enjoy more productivity gains most of the time over services. The reason is that machines can do more and more of the work with technological breakthroughs. However, gains in productivity in cutting hair and college education are harder to come by as the primary input in both is human and requires a relatively fixed mix of human and capital inputs in the production process.

Diff: 2 Skill: Conceptual Topic: Law of increasing opportunity cost
AACSB:

84. The table below represents five points on the production possibility frontier for the small country of Ponderosa, which produces only cowboy boots (measured in thousands of pairs) and saddles (measured in thousands):

	A	**B**	**C**	**D**	**E**
Cowboy Boots	80	50	10	50	0
Saddles	0	20	40	50	30

What is the opportunity cost of moving from point A to point B? What is the opportunity cost of moving from point D to point C?

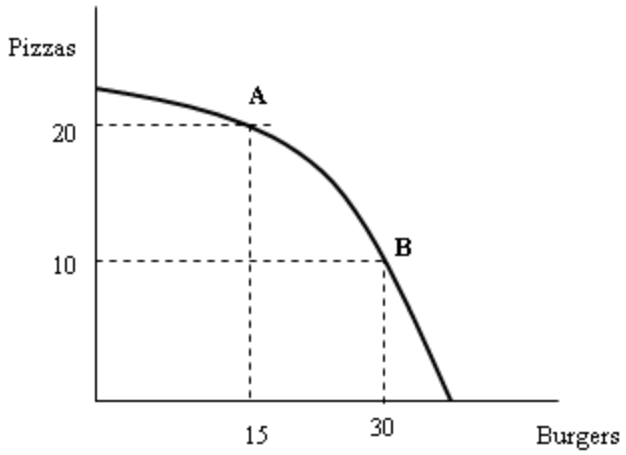
The opportunity cost of moving from point A to point B is 30,000 pairs of cowboy boots. The opportunity cost of moving from point D to point C is 20,000 saddles.

Diff: 1 Skill: Analytical Topic: Opportunity cost
AACSB:

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85.



Refer to the graph above. What is the opportunity cost of going from point A to point B? What is the opportunity cost of going from point B to point A?

The opportunity cost of going from point A to point B is 10 pizzas. The opportunity cost of going from point B to point A is 15 burgers.

Diff: 1 Skill: Analytical Topic: Opportunity cost
AACSB:

86. What is meant by the term *economic growth*?

Economic growth occurs when the total output in an economy increases.

Diff: 1 Skill: Definitional Topic: Economic growth
AACSB:

87. What are the implications for economic growth for countries specializing in consumer goods rather than capital goods? Assume the countries consume what they produce.

All else equal, countries that specialize in consumer goods will likely grow less than those that specialize in capital goods, because specializing in capital goods will allow for more goods to be produced in the future.

Diff: 2 Skill: Conceptual Topic: Economic growth
AACSB: Reflective Thinking

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88. What are the implications for economic growth for countries specializing in capital goods rather than consumer goods? What is the opportunity cost of this decision?

All else equal, countries that specialize in capital goods will likely grow more than those that specialize in consumer goods, because specializing in capital goods will allow for more goods to be produced in the future. The opportunity cost of this decision is that the economy will experience a lower standard of living in the present than they would otherwise.

Diff: 2 Skill: Conceptual Topic: Economic growth
AACSB: Reflective Thinking

89. The table below represents five points on the production possibility frontier for the small country of Bistro, which produces only crackers (measured in thousands of boxes) and cheese (measured in thousands of pounds):

	A	B	C	D	E
Crackers	40	30	20	10	0
Cheese	0	5	10	15	20

Does the production possibility frontier demonstrate the law of increasing opportunity cost? How can you tell?

No. The opportunity cost of increasing the production of cheese remains the same as more cheese is produced. The opportunity cost of the first 5,000 pounds of cheese is 10,000 boxes of crackers, and the opportunity cost of the fourth 5,000 pounds of cheese is also 10,000 boxes of crackers.

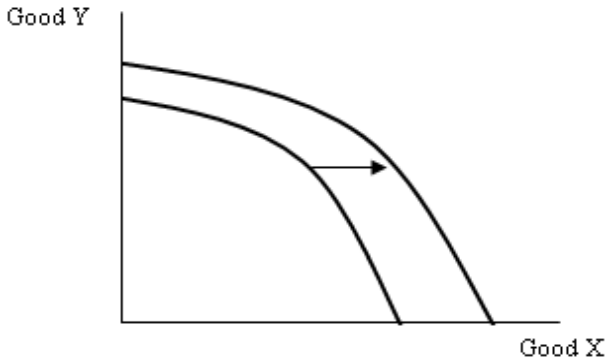
Diff: 2 Skill: Analytical Topic: Law of increasing opportunity cost
AACSB:

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90. Using a graph, show how economic growth affects the production possibility frontier.

When economic growth occurs, the economy can produce more goods and services. Therefore, the production possibility curve shifts outward.



Diff: 1 Skill: Conceptual Topic: Economic growth

91. List two things that can cause economic growth to occur.

(1.) New resources are acquired.
(2.) Society learns to produce more with existing resources.

Diff: 1 Skill: Conceptual Topic: Economic growth
AACSB:

92. In what ways are technological advancements like capital?

Both require an investment in terms of current consumption foregone. Both can lead to increases in the amount an economy can produce.

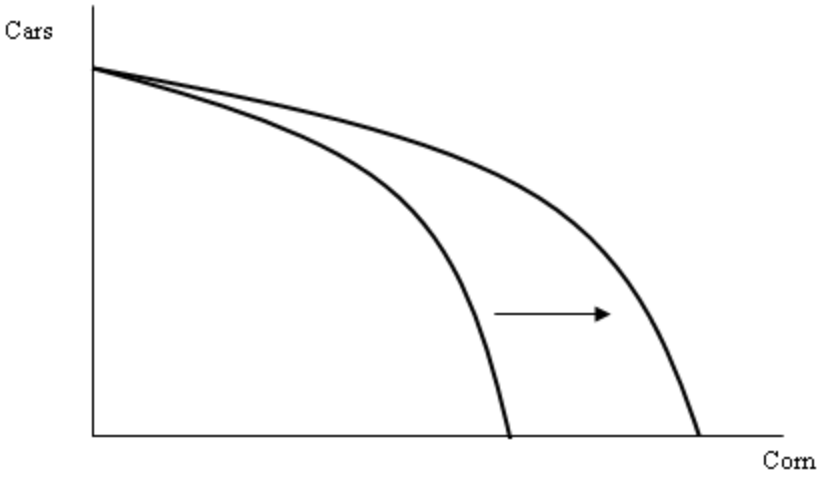
Diff: 2 Skill: Conceptual Topic: Technological advancement
AACSB:

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93. Suppose a country produces two goods: corn and cars. New technology is developed that increases the amount of corn that can be produced. Use a graph to show the effect of this graph on the country's production possibility frontier. Explain what occurs in the graph.

The production possibility frontier shifts outward. The *y*-intercept is unaffected, however. At the *y*-intercept, the country would be producing all cars and no corn and the new technology would have no effect.



Diff: 1 Skill: Conceptual Topic: Technological advancement
AACSB:

94. Why do poor countries often have lower rates of economic growth than richer countries?

If a large part of a country's population is poor, it is very difficult to forgo current consumption to invest in research and development of new technologies or new capital equipment. With less investment, the rate of economic growth in the country will be lower.

Diff: 2 Skill: Conceptual Topic: Economic growth
AACSB:

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95. What happens to a country's production possibility frontier if it experiences a natural disaster such as a hurricane or an earthquake? Explain.

The production possibility frontier will shift in. This occurs because the destruction from the hurricane or earthquake likely destroys resources such as capital and natural resources that are used to produce goods and services. Since the quantity of resources in the country is now lower, the country will not be able to produce as much output.

Diff: 2 Skill: Conceptual Topic: Production possibilities
AACSB:

ECONOMIC SYSTEMS AND THE ROLE OF GOVERNMENT

96. What is the *economic problem*?

The economic problem is finding a way for a society to answer the three basic economic questions (what will be produced?, how will it be produced?, and who will get what is produced?) given that resources are scarce.

Diff: 1 Skill: Definitional Topic: The economic problem

97. What are the two basic types of economic systems?

(1.) Command economies.
(2.) Laissez-faire economies.

Diff: 1 Skill: Factual Topic: Economic systems
AACSB:

98. What is a *command economy*?

A command economy is one in which a central government either directly, or indirectly, sets output targets, incomes, and prices. It may even involve direct government ownership of the means of production and central planning of the economy.

Diff: 1 Skill: Definitional Topic: Economic systems
AACSB:

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99. What is a *laissez-faire economy*?

A laissez-faire economy is one in which individuals and firms pursue their own self-interests without any central direction or regulation.

Diff: 1 Skill: Definitional Topic: Economic systems
AACSB:

100. Is the United States a command economy, a laissez-faire economy, or neither? Explain.

The United States is neither a command economy nor a laissez-faire economy. It is more accurate to describe it as a mixed economy. The U.S. basically has a free market economy, but the government is a large purchaser of goods and services and also produces some goods and services as well. In addition, the U.S. economy has significant amounts of government regulation of business.

Diff: 1 Skill: Conceptual Topic: Economic systems
AACSB:

101. What is meant by *consumer sovereignty*?

Consumer sovereignty is the idea that consumers ultimately dictate what will be produced (or not produced) by choosing what to purchase (or not to purchase).

Diff: 1 Skill: Definitional Topic: Consumer sovereignty
AACSB:

102. According to the idea of consumer sovereignty, what will happen in the market for widgets if consumers decide they no longer desire widgets?

If consumers no longer desire widgets, they will send a message to producers by not purchasing widgets. Since firms will be unable to make a profit selling widgets, widget-producing firms will go out of business (or switch to producing something else) and widgets will no longer be produced. Thus, the consumers' preferences dictate what is produced.

Diff: 2 Skill: Analytical Topic: Consumer sovereignty
AACSB:

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103. What are some of the problems that exist with a laissez-faire economy?

Free markets may not always produce the goods and services that people want at the lowest cost. They are not always efficient. Also, income may be distributed unequally.

Diff: 1 Skill: Factual Topic: Economic systems
AACSB:

104. Why is microeconomic theory often referred to as *price theory*?

The reason is that much of microeconomic theory focuses on the factors which influence and determine prices.

Diff: 1 Skill: Definitional Topic: Microeconomic theory
AACSB:

105. What is the difference between a command economy and a laissez-faire economy?

The major difference lies in how the two types of economies answer the three basic questions. In a command economy, a central government either directly or indirectly sets output targets, incomes, and prices. In a laissez-faire economy, individual people and firms pursue their own self-interests without any central direction or regulation.

Diff: 1 Skill: Conceptual Topic: Economic systems
AACSB:

106. What is the economic problem? How does a command economy solve the economic problem?

The economic problem is that given scarce resources, how exactly do large, complex societies go about answering the basic economic questions? A command economy answers the questions through some centralized authority making decisions about what to produce, how to produce it, and how to distribute it.

Diff: 2 Skill: Conceptual Topic: Economic systems
AACSB:

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107. What problems does a command economy face when it tries to determine what to produce for the economy?

The biggest difficulty that a command economy faces in determining which goods to produce is the fact that there are no prices in the economy which signal which goods and services are more highly valued than others. As a consequence since the decision to produce is often centralized either too little of some products are produced or too much is produced.

Diff: 2 Skill: Conceptual Topic: Economic systems
AACSB:

108. In a laissez-faire economy, what determines the distribution of output?

It is determined by income and wealth. These in part depend on the skills an individual can offer in the labor market.

Diff: 1 Skill: Factual Topic: Economic systems
AACSB:

109. What is the difference between *income* and *wealth*?

Income is a flow variable. It is the amount a household earns over a period of time such as a year. Wealth is a stock variable. It is the amount of assets a household has accumulated at a point in time from past income or through saving or inheritance.

Diff: 1 Skill: Definitional Topic: Income and wealth
AACSB:

110. Explain how it is possible for a recently retired postal worker to be more wealthy than a rookie professional football player even though it is widely recognized that football players earn more than postal workers.

The reason is that the postal worker in all likelihood has been spending years or decades building up wealth from his income. A rookie professional football player however, may earn a higher wage but has not had the opportunity to build up much if any wealth at all since his career has just begun.

Diff: 1 Skill: Conceptual Topic: Income and wealth
AACSB:

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111. Evaluate the following two statements:

"He is income rich but he is not very wealthy"
"He is income poor but he is wealthy"

The first person might be making a lot of income but hasn't acquired much wealth in the form of savings account balances or real estate. The second person might not have an income or have a really low income but accumulated a lot of wealth from the past.

Diff: 1 Skill: Conceptual Topic: Income and wealth
AACSB:

112. Explain three of the shortcomings of the free-enterprise system.

The shortcomings of the free-enterprise system are: products may not always be produced at lowest cost, income may be unevenly distributed, and periods of inflation and unemployment may recur.

Diff: 1 Skill: Conceptual Topic: Economic systems
AACSB:

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