Business in Action 8th edition Bovee Test Bank

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Business in Action, 8e **(Bovee)**
Chapter 2 Understanding Basic Economics

1) _____ is the study of how a society uses scarce resources to produce and distribute goods.
A) Opportunity costs
B) Economics
C) Capitalism
D) Entrepreneurship
E) Socialism
Answer: B
Explanation: Economics is the study of how a society uses its scarce resources to produce and distribute goods and services.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

2) Microeconomics is the study of _____.
A) the costs of production as a means of stimulating the economy
B) the application of economic and financial data and statistics
C) the overall working of an economy in the society including its monetary and fiscal policies
D) policies that raise capital and labor output by increasing the incentive to produce
E) economic behavior among consumers and businesses
Answer: E
Explanation: The study of economic behavior among consumers, businesses, and industries that collectively determine the quantity of goods and services demanded and supplied at different prices is termed microeconomics.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

3) Which of the following refers to people and their individual talents and capabilities?
A) natural resources
B) knowledge
C) capital investments
D) human resources
E) entrepreneurship
Answer: D
Explanation: Human resources are people and their individual talents and capacities.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

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4) The money, equipment, and buildings that a business needs in order to produce goods and services are called _____.
A) natural resources
B) human resources
C) capital
D) knowledge
E) entrepreneurship
Answer: C
Explanation: Capital includes money, computers, machines, tools, and buildings that a business needs in order to produce goods and services.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

5) _____ is lead by innovation, initiative, and the willingness to take the risks in creating and operating businesses.
A) Capitalization
B) Socialization
C) Macroeconomics
D) Economic freedom
E) Entrepreneurship
Answer: E
Explanation: Entrepreneurship is the spirit of innovation, the initiative, and the willingness to take the risks involved in creating and operating businesses.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

6) Which of the following has the effect of creating competition for finite resources, thereby forcing trade-offs by participants in the economy?
A) redundancy
B) scarcity
C) opportunity costs
D) free market systems
E) planned systems
Answer: B
Explanation: Scarcity doesn't mean a shortage of a particular resource; rather, it means that the resource has a finite supply. Scarcity has two powerful effects: It creates competition for resources, and it forces trade-offs on the part of every participant in the economy.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

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7) Of all the alternatives not selected, the one with the highest value represents the _____ of the action taken.
A) opportunity cost
B) trade-offs
C) scarcity value
D) finite supply
E) affordability
Answer: A
Explanation: Opportunity cost is a way to measure the value of what you gave up when you pursued a different opportunity.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

8) Who are those employees whose main contribution to an organization is the application of business knowledge?
A) entrepreneurs
B) knowledge workers
C) economists
D) capitalist
E) human resources
Answer: B
Explanation: Knowledge workers, employees whose primary contribution is the acquisition and application of business knowledge, are a key economic resource for businesses in today's economy.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

9) Which factor of production represents the collective intelligence of an organization?
A) natural resources
B) human resources
C) capital
D) entrepreneurship
E) knowledge
Answer: E
Explanation: Each society must decide how to use its economic resources, or factors of production. Knowledge is the collective intelligence of an organization.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

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10) In the global marketplace, which of the following is often a type of key asset needed to successfully utilize an advantage?
A) capital
B) supplies
C) intellectual
D) production location
E) workforce
Answer: C
Explanation: Traditionally, a business or a country was considered to have an advantage if its location offered plentiful supplies of natural resources, human resources, capital, and entrepreneurs. In today's global marketplace, however, intellectual assets are often the key.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

11) Economics is the study of how a society uses its scarce resources to produce and distribute goods and services to its citizens.
Answer: TRUE
Explanation: Economics is the study of how a society uses its scarce resources to produce and distribute goods and services to its citizens.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

12) Macroeconomics studies economic behavior among consumers, businesses, and industries that collectively determine the quantity of goods and services demanded and supplied at different prices.
Answer: FALSE
Explanation: The study of a country's larger economic issues, such as how firms compete, the effect of government policies, and how an economy maintains and allocates its scarce resources, is termed macroeconomics.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

13) Capital includes land and minerals that a business needs in order to produce goods and services.
Answer: FALSE
Explanation: Capital includes money, computers, machines, tools, and buildings that a business needs in order to produce goods and services.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

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14) Capital is the collective intelligence of an organization.
Answer: FALSE
Explanation: Capital includes money, computers, machines, tools, and buildings that a business needs in order to produce goods and services.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

15) Scarcity creates competition for resources, and forces trade-offs on the part of every participant in the economy.
Answer: TRUE
Explanation: Scarcity has two powerful effects: It creates competition for resources, and it forces trade-offs on the part of every participant in the economy.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

16) Deciding how much money to spend on new manufacturing equipment versus launching a new advertising campaign is described as opportunity cost.
Answer: FALSE
Explanation: Opportunity cost refers to the value of the most appealing alternative from all those that weren't chosen. In other words, opportunity cost is a way to measure the value of what you gave up when you pursued a different opportunity.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

17) What is economics? Compare and contrast between microeconomics and macroeconomics.
Answer: Economics is the study of how a society uses its scarce resources to produce and distribute goods and services. Economics is divided into a small-scale perspective and a large-scale perspective. The study of economic behavior among consumers, businesses, and industries that collectively determine the quantity of goods and services demanded and supplied at different prices is termed microeconomics. The study of a country's larger economic issues, such as how firms compete, the effect of government policies, and how an economy maintains and allocates its scarce resources, is termed macroeconomics. While microeconomics looks at the small picture and macroeconomics looks at the big picture, understanding the economy at either scale requires an understanding of how the small and large forces interact. For instance, a number of macro forces and policies determine whether homeowners can afford to install solar energy systems. In turn, the aggregate behavior of all those homeowners at the micro level affects the vitality and direction of the overall economy.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

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18) Explain the different factors of production.
Answer: *Natural resources* are things that are useful in their natural state, such as land, forests, minerals, and water. *Human resources* are people and their individual talents and capacities. *Capital* includes money, computers, machines, tools, and buildings that a business needs in order to produce goods and services. *Entrepreneurship* is the spirit of innovation, the initiative, and the willingness to take the risks involved in creating and operating businesses. *Knowledge* is the collective intelligence of an organization.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

19) Compare and contrast between trade-offs and opportunity costs.
Answer: Due to universal scarcity of resources, consumers, companies, and governments are constantly forced to make trade-offs, meaning they have to give up something to get something else. You have to decide how to spend the 24 hours you have every day, and every choice involves a trade-off–the more time you spend on one activity means less time for every other activity you could possibly pursue. Businesses must make similar trade-offs, such as deciding how much money to spend on advertising a new product versus how much to spend on the materials used to make it, or deciding how many employees to have in sales versus customer support. Opportunity cost refers to the value of the most appealing alternative from all those you didn't choose. In other words, opportunity cost is a way to measure the value of what you gave up when you pursued a different opportunity.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.1: Define economics, and explain why scarcity is central to economic decision making.

20) In a _____, companies can decide what to produce, how to produce, whom to sell to, and at what price to sell.
A) planned system
B) regulated economy
C) socialist economy
D) free-market system
E) communist economy
Answer: D
Explanation: In a free-market system, individuals and companies are largely free to decide what products to produce, how to produce them, whom to sell them to, and at what price to sell them. In other words, they have the chance to succeed–or to fail–by their own efforts.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Differentiate among the major types of economic systems.

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21) The _____ economic system allows individuals to own and operate the majority of businesses with limited economic intervention by the government.
A) mixed
B) planned
C) capitalist
D) free-market
E) communist
Answer: A
Explanation: The practice of limited intervention is characteristic of a mixed economy or mixed capitalism, which is the economic system of the United States and most other countries. For example, government bodies intervene in the U.S. economy in a variety of ways, such as influencing particular allocations of resources through tax incentives, prohibiting or restricting the sale of certain goods and services, or setting price controls.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Differentiate among the major types of economic systems.

22) Which of the following is characteristic of a country with a planned economic system?
A) The economy relies chiefly on market forces to allocate goods and resources and to determine prices.
B) The economic system combines private and state enterprises with limited intervention from the government.
C) The economy subscribes to capitalistic competition, where private parties own and operate the majority of businesses.
D) The economic system is primarily capitalistic but there is some degree of government ownership of the means of production.
E) The economy is largely controlled by the government and freedom of choice is limited in order to accomplish government goals.
Answer: E
Explanation: In a planned system, governments largely control the allocation of resources and limit freedom of choice in order to accomplish government goals. Because social equality is a major goal of planned systems, private enterprise and the pursuit of private gain are generally regarded as wasteful and exploitive.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.2: Differentiate among the major types of economic systems.

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23) The economic system that allows individuals the least degree of economic freedom is _____.
A) socialism
B) communism
C) capitalism
D) authoritarianism
E) mixed capitalism
Answer: B
Explanation: The planned economic system that allows individuals the least degree of economic freedom is communism, which still exists in a few countries, most notably North Korea and China.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.2: Differentiate among the major types of economic systems.

24) When a government takes control of a company or industry, it changes the shape of the entire economy through _____.
A) privatization
B) capitalism
C) nationalization
D) free-market systems
E) socialism
Answer: C
Explanation: The line between socialism and capitalism isn't always easy to define, and it doesn't always stay in the same place, either. Governments can change the structure of the economy by nationalizing–taking ownership of–selected companies or in extreme cases even entire industries.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.2: Differentiate among the major types of economic systems.

25) When the state owns all major productive resources and the country has very few opportunities for entrepreneurship, the country is characterized by which of the following economic systems?
A) anarchism
B) communism
C) capitalism
D) socialism
E) mixed
Answer: B
Explanation: In communism, the state owns all the major productive resources. Economic classes are absent and there are few opportunities for entrepreneurship.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.2: Differentiate among the major types of economic systems.

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26) _____ lies somewhere between capitalism and communism, with a fairly high degree of government planning and some government ownership of capital resources.
A) Totalitarianism
B) Liberalism
C) Authoritarianism
D) Socialism
E) Anarchism
Answer: D
Explanation: Socialism lies somewhere between capitalism and communism, with a fairly high degree of government planning and some government ownership of capital resources.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Differentiate among the major types of economic systems.

27) If the government owns many of the key industrial sectors, such as transportation, health care, and communications, but private ownership is allowed in other industries, what type of economic system does the country have?
A) communism
B) capitalism
C) free-market economy
D) socialism
E) totalitarianism
Answer: D
Explanation: Socialism lies somewhere between capitalism and communism, with a fairly high degree of government planning and some government ownership of capital resources. However, government ownership tends to be focused in industries considered vital to the common welfare, such as transportation, health care, and communications. Private ownership is permitted in other industries.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.2: Differentiate among the major types of economic systems.

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28) Which of the following actions of the government indicates the privatization of an industry?
A) Allowing private businesses to operate in an industry that was previously operated by the government.
B) Discouraging private business to operate in an industry that is critical for the growth of the economy.
C) Acquiring the market leader to gain control of the industry and its resources.
D) Imposing taxes on scarce raw materials to discourage unfair pricing by its suppliers.
E) Imposing regulations on multinational businesses to protect local businesses.
Answer: A
Explanation: Governments can change the structure of the economy by nationalizing–assuming ownership of–selected companies or, in extreme cases, even entire industries. They can also move in the opposite direction, privatizing services once performed by the government by allowing private businesses to perform them instead.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Differentiate among the major types of economic systems.

29) What is a major goal of a planned economic system?
A) creation of wealth
B) social equity
C) price control
D) limited intervention
E) tax incentives
Answer: B
Explanation: Because social equality is a major goal of planned systems, private enterprise and the pursuit of private gain are generally regarded as wasteful and exploitive.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Differentiate among the major types of economic systems.

30) Capitalism is a term used to describe the free-market system, one in which private parties own and operate the majority of businesses and where competition, supply, and demand determine which goods and services are produced.
Answer: TRUE
Explanation: Capitalism is a term used to describe the free-market system, one in which private parties own and operate the majority of businesses and where competition, supply, and demand determine which goods and services are produced.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Differentiate among the major types of economic systems.

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31) In practice, no economy is truly a free-market economy.
Answer: TRUE
Explanation: Free market economy is a situation in which so many buyers and sellers exist that no single buyer or seller can individually influence market prices. In practice, no economy is truly a free-market economy.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Differentiate among the major types of economic systems.

32) As social equality is a major goal of planned systems, private enterprise and the pursuit of private gain are encouraged.
Answer: FALSE
Explanation: In a planned system, governments largely control the allocation of resources and limit freedom of choice in order to accomplish government goals. Private enterprise and the pursuit of private gain are not encouraged in such a system.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Differentiate among the major types of economic systems.

33) Global economists use the terms capitalism and private enterprise to describe centrally planned economic systems.
Answer: FALSE
Explanation: The terms capitalism and private enterprise are often used to describe free-market systems.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.2: Differentiate among the major types of economic systems.

34) Compare and contrast between free-market systems and planned systems.
Answer: In a free-market system, individuals and companies are largely free to decide what products to produce, how to produce them, whom to sell them to, and at what price to sell them. In other words, they have the chance to succeed–or to fail–by their own efforts. Capitalism and private enterprise are the terms most often used to describe the free-market system, one in which private parties (individuals, partnerships, or corporations) own and operate the majority of businesses and where competition, supply, and demand determine which goods and services are produced.
In a planned system, governments largely control the allocation of resources and limit freedom of choice in order to accomplish government goals. Because social equality is a major goal of planned systems, private enterprise and the pursuit of private gain are generally regarded as wasteful and exploitive. The planned system that allows individuals the least degree of economic freedom is communism.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.2: Differentiate among the major types of economic systems.

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35) Is there such a thing as a "free" economy? Explain and support your views.
Answer: In practice, no economy is truly "free."
Local, state, national, and even international governments, such as the European Community, intervene in the economy to accomplish goals that leaders deem socially or economically desirable. This practice of limited intervention is characteristic of a mixed economy or mixed capitalism, which is the economic system of the United States and most other countries. For example, government bodies intervene in the U.S. economy in a variety of ways, such as influencing particular allocations of resources through tax incentives, prohibiting or restricting the sale of certain goods and services, or setting price controls. Price controls can involve maximum allowable prices (such as limiting rent increases) and minimum allowable prices (such as supplementing the prices of agricultural goods to ensure producers a minimum level of income or establishing minimum wage levels).
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.2: Differentiate among the major types of economic systems.

36) What type of economic system lies between capitalism and communism? Explain why it is more effective than other economic systems.
Answer: Socialism is an economic system with a fairly high degree of government planning and some government ownership of capital resources. In a socialist economy, government ownership tends to be focused in industries considered vital to the common welfare, such as transportation, health care, and communications. Private ownership is permitted in other industries. Many European countries, including France and Germany, incorporate varying degrees of socialism.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.2: Differentiate among the major types of economic systems.

37) Explain, with the help of an example, why socialism and capitalism are not mutually exclusive.
Answer: While free-market capitalism remains the foundation of the U.S. economy, some important elements of the U.S. economy are socialized and have been for many years. Public schools, the postal service, much of the transportation infrastructure, various local and regional utilities, and several major health care programs all fit the economic definition of socialism. Socialism and capitalism are competing philosophies, but they are not mutually exclusive, and each approach has strengths and weaknesses, which is why most modern economies combine aspects of both.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.2: Differentiate among the major types of economic systems.

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38) Which of the following refers to the amount of a good or service that customers will buy at a given time?
A) demand
B) utility
C) equilibrium
D) necessity
E) want
Answer: A
Explanation: Demand refers to the amount of a good or service that customers will buy at a given time.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.3: Explain the interaction between demand and supply.

39) _____ refers to the quantities of a good or service that producers will provide on a particular date at various prices.
A) Necessity
B) Supply
C) Demand
D) Utility
E) Want
Answer: B
Explanation: Supply refers to the quantities of a good or service that producers will provide on a particular date at various prices.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.3: Explain the interaction between demand and supply.

40) A(n) _____ shows the relationship between the amount of product that buyers will purchase at various prices, all other factors being equal.
A) supply curve
B) inflation rate
C) demand curve
D) deflation rate
E) competitive balance
Answer: C
Explanation: A demand curve is a graph showing the relationship between the amount of product that buyers will purchase at various prices, all other factors being equal.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.3: Explain the interaction between demand and supply.

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41) Demand curves typically slope downward. This implies that a(n) _____.
A) decrease in price will increase the quantity demanded
B) decrease in price will decrease the quantity demanded
C) increase in price will increase the quantity demanded
D) decrease in price will have no effect on quantity demanded
E) increase in price will have no effect on quantity demanded
Answer: A
Explanation: Demand curves typically slope downward, implying that as price drops, more people are willing to buy.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.3: Explain the interaction between demand and supply.

42) The _____ depicts the relationship between prices and quantities that sellers will offer for sale, regardless of demand.
A) demand curve
B) supply curve
C) equilibrium point
D) business cycle
E) competitive analysis
Answer: B
Explanation: The depiction of the relationship between prices and quantities that sellers will offer for sale is called a supply curve.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.3: Explain the interaction between demand and supply.

43) Movement along the supply curve typically slopes upward because _____.
A) the amount of government regulation in an industry rises with increase in demand
B) the quantity that the sellers are willing to supply rises with decrease in demand
C) the amount of government regulation in an industry rises with increase in price
D) the quantity that the sellers are willing to supply rises with increase in government regulation
E) the quantity that the sellers are willing to supply rises with increase in price
Answer: E
Explanation: Movement along the supply curve typically slopes upward: as prices rise, the quantity that sellers are willing to supply also rises. Similarly, as prices decline, the quantity that sellers are willing to supply declines.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.3: Explain the interaction between demand and supply.

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44) The point at which the demand and supply curves intersect - the point at which the quantity demanded and supplied are balanced is called the _____.
A) equilibrium point
B) aggregation point
C) marginal point
D) break-even point
E) distribution point
Answer: A
Explanation: The point at which the demand and supply curves intersect–the point at which the quantity demanded and supplied are equal–is the equilibrium point.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.3: Explain the interaction between demand and supply.

45) Demand refers to the quantities of a good or service that producers will provide on a particular date at various prices.
Answer: FALSE
Explanation: Demand refers to buyers' willingness and ability to purchase products at various price points.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.3: Explain the interaction between demand and supply.

46) The demand curve will shift to the left if the price of substitute products increases.
Answer: FALSE
Explanation: The demand curve will shift to the right if the price of substitute products increases.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.3: Explain the interaction between demand and supply.

47) Movement along the supply curve typically slopes upward.
Answer: TRUE
Explanation: Movement along the supply curve typically slopes upward: As prices rise, the quantity that sellers are willing to supply also rises. Similarly, as prices decline, the quantity that sellers are willing to supply declines.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.3: Explain the interaction between demand and supply.

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48) The supply curve of a firm will shift to the right if technology increases the firm's production costs.
Answer: FALSE
Explanation: The supply curve of a firm will shift to the left if technology increases the firm's production costs.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.3: Explain the interaction between demand and supply.

49) The equilibrium point is the point at which quantity of a good or service equals the quantity demanded.
Answer: TRUE
Explanation: The point at which quantity of a good or service equals the quantity demanded is known as the equilibrium point.
Difficulty: 1: Easy
AACSB: Analytical thinking
LO: 2.3: Explain the interaction between demand and supply.

50) "As the supply and demand curves are dynamic, so is the equilibrium point." Explain this statement with an example.
Answer: As variables affecting supply and demand change, so will the equilibrium price. For example, increased concerns about airline safety could encourage some travelers to choose alternatives such as automobile travel or web conferencing, thus reducing the demand for air travel at every price and moving the equilibrium point as well. Suppliers might respond to such a reduction in demand by either cutting the number of flights offered or lowering ticket prices in order to restore the equilibrium level.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.3: Explain the interaction between demand and supply.

51) The term _____ is used to characterize the fluctuations in an economy's rate of growth over a period of several years.
A) microeconomics
B) competitive pressures
C) cyclical machinations
D) business cycles
E) economic repercussions
Answer: D
Explanation: Business cycles are fluctuations in the rate of growth that an economy experiences over a period of several years.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

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52) _____ occurs when no single firm is large enough to influence prices and distort the workings of the free-market system.
A) Pure monopoly
B) Pure entrepreneurialism
C) Pure competition
D) Regulated monopoly
E) Stabilized monopoly
Answer: C
Explanation: Pure competition is a situation in which no single firm is large enough to influence prices and distort the workings of the free-market system.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

53) When the number of competitors in a market is small, a situation known as _____ is created.
A) monopoly
B) duopoly
C) oligopoly
D) monopolistic competition
E) pure competition
Answer: C
Explanation: When the number of competitors in a market is quite small, a situation known as oligopoly is created. Customers have some choice, unlike in a monopoly, but not as many choices as in monopolistic competition.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

54) Which of the following is a characteristic feature of economic contraction?
A) decreased unemployment rates
B) decreased consumer spending
C) increased income
D) increased employment
E) increased demand
Answer: B
Explanation: During an economic contraction, spending declines, employment drops, and the economy as a whole slows down.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

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55) The term _____ is defined as having two consecutive quarters of decline in the country's gross domestic product.
A) deflation
B) stagnation
C) depression
D) stagflation
E) recession
Answer: E
Explanation: If the period of downward swing is severe, the nation may enter into a recession, traditionally defined as two consecutive quarters of decline in the gross domestic product.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

56) A deep and prolonged recession is known as a(n) _____.
A) contraction
B) stagnation
C) deflation
D) immobilization
E) depression
Answer: E
Explanation: A deep and prolonged recession can be considered a depression, which doesn't have an official definition but is generally considered to involve a catastrophic collapse of financial markets.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

57) When a downward swing or recession is over, the economy enters into a period of _____.
A) recovery
B) depression
C) contraction
D) stagnation
E) repercussion
Answer: A
Explanation: When a downward swing or recession is over, the economy enters into a period of recovery.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

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58) _____ unemployment is the natural movement of workers into and out of jobs, such as when a person quits one job without first lining up a new job.
A) Structural
B) Intrinsic
C) Frictional
D) Cyclical
E) Seasonal
Answer: C
Explanation: Frictional unemployment is the natural movement of workers into and out of jobs, such as when a person quits one job without first lining up a new one.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

59) When demand for goods and services drops, businesses reduce production, thereby requiring fewer workers. The unemployment resulting because of this phenomenon is known as _____ unemployment.
A) intrinsic
B) cyclical
C) structural
D) seasonal
E) frictional
Answer: B
Explanation: When demand for goods and services drops, businesses reduce production, thereby requiring fewer workers. This leads to cyclical unemployment.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

60) What is gross domestic product?
A) A deep and prolonged recession.
B) An up and down swing in the economy.
C) A measure of a country's economic output.
D) Two consecutive quarters of economic decline
E) An indication of an economy that is growing and consumers are spending more money.
Answer: C
Explanation: Gross domestic product measures a country's output–its production, distribution, and use of goods and services–by computing the sum of all goods and services produced for final use in a country during a specified period (usually a year).
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

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61) Which of the following best describes pure competition?
A) an advanced free-market economy
B) a positive risk-reward relationship within an economy
C) fewer competitors in the marketplace
D) where no single firm can control prices or distort the free-market system
E) one supplier can control prices and force all others out of business
Answer: D
Explanation: Pure competition occurs when no single firm becomes large enough to influence prices and thereby distort the workings of the free-market system.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

62) Which of the following reflects the percentage of the labor force currently without work?
A) economic contraction
B) economic fluctuation
C) deflation
D) monopolistic competition
E) unemployment rate
Answer: E
Explanation: The unemployment rate indicates the percentage of the labor force currently without employment. The labor force consists of people ages 16 and older who are either working or looking for jobs.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

63) Why is inflation a concern for businesses and consumers?
A) Inflation affects the amount of goods and services you can buy for a given amount of money.
B) Inflation affects the amount of government intervention in small businesses.
C) Inflation affects the potential sustained fall in average prices.
D) Inflation affects the ability for sustained economic contraction.
E) Inflation affects the amount of goods and services a firm can produce in a production cycle.
Answer: A
Explanation: Inflation is a steady rise in the average prices of goods and services throughout the economy. Inflation is a major concern for consumers, businesses, and government leaders because of its effect on purchasing power, or the amount of a good or service you can buy for a given amount of money.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

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64) The situation in which one supplier thoroughly dominates a market and essentially shuts out other competitors is called monopoly.
Answer: TRUE
Explanation: The situation in which one supplier thoroughly dominates a market and essentially shuts out other competitors is called monopoly.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

65) A deep and prolonged recession can be considered as a depression.
Answer: TRUE
Explanation: A deep and prolonged recession can be considered a depression, which doesn't have an official definition but is generally considered to involve a catastrophic collapse of financial markets.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

66) Frictional unemployment is caused by economic fluctuations.
Answer: FALSE
Explanation: Frictional unemployment refers to the natural flow of workers into and out of jobs, such as when a person leaves one job without first lining up a new job.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

67) Deflation is an economic condition in which prices fall steadily throughout the economy.
Answer: TRUE
Explanation: Deflation is an economic condition in which prices fall steadily throughout the economy.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

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68) Cyclical unemployment is caused by a mismatch between workers' skills and current employer needs.
Answer: FALSE
Explanation: Cyclical unemployment refers to seasonal unemployment caused by economic fluctuations. When demand for goods and services drops, businesses reduce production, thereby requiring fewer workers.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

69) How does capitalism promote monopolistic competition in the market?
Answer: Most of the competition in advanced free-market economies is monopolistic competition, in which a number of sellers offer products that can be distinguished from competing products in at least some small way. The risk/reward nature of capitalism promotes constant innovation in pursuit of competitive advantage, rewarding companies that do the best job of satisfying customers.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

70) Differentiate between structural and cyclical unemployment.
Answer: Structural unemployment occurs due to a mismatch between the skills of workers and the needs of employers. Workers can't find jobs that match their qualifications, and employers can't find employees with the skills their job openings require. Structural unemployment is an ongoing concern because changes in the external environments of business make some skills obsolete and create demand for new skills.
Cyclical unemployment is caused by economic fluctuations. When demand for goods and services drops, businesses reduce production, thereby requiring fewer workers. Then, an increasing number of people who want to work can't find jobs. During catastrophic depressions, cyclical unemployment can run as high as 20 or 25 percent.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

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71) Define and discuss the term *business cycles*.
Answer: The economy is always in a state of change, expanding or contracting in response to the combined effects of factors such as technological breakthroughs, changes in investment patterns, shifts in consumer attitudes, world events, and basic economic forces. *Business cycles* represent the fluctuations in the rate of growth that an economy experiences over a period of several years. These cycles include *economic expansion*, when the economy is growing and consumers are spending more money, which stimulates higher employment and wages, which then stimulate more consumer purchases. The cycles include *economic contraction*, when spending declines, employment drops, and the economy as a whole slows down. Even though experts call these up-and-down swings business cycles, this term is somewhat misleading, because real economies do not expand and contract in regular and predictable "cycles." More accurately, the behavior of an economy can be characterized as e*conomic fluctuations*.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.4: Identify four macroeconomic issues that are essential to understanding the behavior of the economy.

72) Which of the following is an example of deregulation?
A) lifting redundant restrictions on airline competition
B) banning the sale of tobacco to minors under the age of 18
C) lowering the speed limit on an interstate highway
D) approving a proposed merger between Google and Microsoft
E) establishing economic development zones to attract new businesses
Answer: A
Explanation: Deregulation is the process of removing regulations to allow the market to prevent excesses and correct itself over time.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.5: Outline the debate over deregulation, and identify four key roles that governments play in the economy.

73) _____ laws limit what businesses can and cannot do to ensure that all competitors have an equal chance of succeeding.
A) Fiscal
B) Discrimination
C) Antitrust
D) Stabilization
E) Equilibrium
Answer: C
Explanation: Antitrust laws limit what businesses can and cannot do to ensure that all competitors have an equal chance of succeeding.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.5: Outline the debate over deregulation, and identify four key roles that governments play in the economy.

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74) _____ policy involves increasing or decreasing interest rates to control the nation's money supply.
A) Fiscal
B) Taxation
C) Cyclical
D) Antitrust
E) Monetary
Answer: E
Explanation: Monetary policy involves adjusting the nation's money supply, the amount of "spendable" money in the economy at any given time, by increasing or decreasing interest rates.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.5: Outline the debate over deregulation, and identify four key roles that governments play in the economy.

75) _____ policy involves changes in the government's revenues and expenditures to stimulate a slow economy or dampen a growing economy that is in danger of overheating and causing inflation.
A) Fiscal
B) Taxation
C) Cyclical
D) Antitrust
E) Monetary
Answer: A
Explanation: Fiscal policy involves changes in the government's revenues and expenditures to stimulate a slow economy or dampen a growing economy that is in danger of overheating and causing inflation.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.5: Outline the debate over deregulation, and identify four key roles that governments play in the economy.

76) _____ taxes, levied on the earnings of individuals and businesses, are the government's largest single source of revenue.
A) Income
B) Property
C) Sales
D) Excise
E) Payroll
Answer: A
Explanation: Income taxes are levied on the income earned by individuals and businesses. They are the government's largest single source of revenue.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.5: Outline the debate over deregulation, and identify four key roles that governments play in the economy.

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77) Which of the following allows the market to prevent excesses and correct itself over time?
A) deregulation
B) competition
C) acquisitions
D) monetary policy
E) regulation
Answer: A
Explanation: Much of the debate about the government's role can be framed as a question of regulation versus deregulation - having more rules in place to govern economic activity or having fewer rules in place and relying more on the market to prevent excesses and correct itself over time.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.5: Outline the debate over deregulation, and identify four key roles that governments play in the economy.

78) Which of the following allows all competitors to have an equal chance of succeeding by limiting what a business can and cannot do?
A) merger and acquisition laws
B) antitrust laws
C) innovation and economic development laws
D) monetary policy
E) lagging indicators
Answer: B
Explanation: Antitrust laws limit what businesses can and cannot do, to ensure that all competitors have an equal chance of succeeding.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.5: Outline the debate over deregulation, and identify four key roles that governments play in the economy.

79) Which of the following are areas where the government encourages businesses to locate to by offering financial incentives?
A) tax-free zones
B) financial freedom zones
C) economic development zones
D) job-creation zones
E) reduced utility zones
Answer: C
Explanation: Governments can also encourage businesses to locate or expand in particular geographic areas by establishing economic development zones. These zones typically offer a variety of financial incentives such as tax credits, low-interest loans, and reduced utility rates to businesses that meet specific job-creation and local investment criteria.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.5: Outline the debate over deregulation, and identify four key roles that governments play in the economy.

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80) Why would the government lower the income tax rate?
A) In the hopes that companies will pay their taxes on a timely basis.
B) To encourage the collection of other types of fees from individuals.
C) To dampen an economy that is growing too quickly.
D) To encourage consumers and businesses to spend money not paid in taxes.
E) To stabilize the national economy.
Answer: D
Explanation: When the federal government lowers the income tax rate, for instance, it does so with the hope that consumers and businesses will spend and invest the money they save from lower tax bills. Governments can stimulate the economy by increasing their purchases, sometimes even to the point of creating new programs or projects with the specific purpose of expanding employment opportunities and increasing demand for goods and services.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.5: Outline the debate over deregulation, and identify four key roles that governments play in the economy.

81) Economic development zones, established by governments, offer a variety of financial incentives to businesses that meet specific job creation and local investment criteria.
Answer: TRUE
Explanation: Economic development zones, established by governments, offer a variety of financial incentives to businesses that meet specific job creation and local investment criteria.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.5: Outline the debate over deregulation, and identify four key roles that governments play in the economy.

82) Monetary policy involves changes in the government's revenues and expenditures to stimulate a slow economy or dampen a growing economy that is in danger of overheating and causing inflation.
Answer: FALSE
Explanation: Monetary policy involves adjusting the nation's money supply, the amount of "spendable" money in the economy at any given time, by increasing or decreasing interest rates.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.5: Outline the debate over deregulation, and identify four key roles that governments play in the economy.

83) Sales taxes are the government's largest single source of revenue.
Answer: FALSE
Explanation: Income taxes are the government's largest single source of revenue.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.5: Outline the debate over deregulation, and identify four key roles that governments play in the economy.

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84) Compare and contrast between monetary and fiscal policies.
Answer: Monetary policy involves adjusting the nation's money supply, the amount of "spendable" money in the economy at any given time, by increasing or decreasing interest rates. In the United States, monetary policy is controlled primarily by the Federal Reserve Board (often called "the Fed"), a group of government officials who oversee the country's central banking system.
Fiscal policy involves changes in the government's revenues and expenditures to stimulate a slow economy or dampen a growing economy that is in danger of overheating and causing inflation. On the revenue side, governments can adjust the revenue they bring in by changing tax rates and various fees collected from individuals and businesses. When the federal government lowers the income tax rate, for instance, it does so with the hope that consumers and businesses will spend and invest the money they save by paying lower taxes.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.5: Outline the debate over deregulation, and identify four key roles that governments play in the economy.

85) The _____ measures the rate of inflation by comparing changes in the prices of a representative basket of goods and services such as clothing, food, housing, and utilities.
A) gross domestic product (GDP)
B) producer price index (PPI)
C) inflationary stability index (ISI)
D) consumer price index (CPI)
E) economic stimulus index (ESI)
Answer: D
Explanation: The consumer price index (CPI) measures the rate of inflation by comparing the change in prices of a representative "basket" of consumer goods and services, such as clothing, food, housing, and transportation.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Identify the major ways of measuring economic activity.

86) The _____ measures price at the producer or wholesaler level, reflecting what businesses are paying for the products they need.
A) gross domestic product (GDP)
B) producer price index (PPI)
C) inflationary stability index (ISI)
D) consumer price index (CPI)
E) economic stimulus index (ESI)
Answer: B
Explanation: The producer price index (PPI) measures price at the producer or wholesaler level, reflecting what businesses are paying for the products they need. Like the CPI, the PPI is often referred to as a single index, but it is actually a family of more than 600 industry-specific indexes.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Identify the major ways of measuring economic activity.

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87) Business and political leaders use _____ such as rates of interest or unemployment to measure and monitor economic performance.
A) economic indicators
B) social indexes
C) sustainability rates
D) cost-of-living increases
E) monetary paradigms
Answer: A
Explanation: Economic indicators are statistics such as interest rates, unemployment rates, housing data, and industrial productivity that let leaders in business and politics measure and monitor economic performance.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Identify the major ways of measuring economic activity.

88) The _____ measures a country's production, distribution, and use of goods and services by computing the sum of all goods and services produced for final use during a specified period.
A) gross domestic product (GDP)
B) producer price index (PPI)
C) gross national product (GNP)
D) consumer price index (CPI)
E) economic stability index (ESI)
Answer: A
Explanation: The broadest measure of an economy's health is the gross domestic product (GDP). The GDP measures a country's output–its production, distribution, and use of goods and services–by computing the sum of all goods and services produced for final use in a country during a specified period (usually a year).
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Identify the major ways of measuring economic activity.

89) While gross domestic product (GDP) considers where the production occurs, _____ considers who is responsible for the production.
A) human development index (HDI)
B) producer price index (PPI)
C) gross national product (GNP)
D) consumer price index (CPI)
E) economic stability index (ESI)
Answer: C
Explanation: GDP has largely replaced an earlier measure called the gross national product (GNP), which excludes the value of production from foreign-owned businesses within a nation's boundaries and includes receipts from the overseas operations of domestic companies. GNP considers who is responsible for the production; GDP considers where the production occurs.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Identify the major ways of measuring economic activity.

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90) Which of the following is an indication of an economic change that has happened in the past?
A) leading indicators
B) housing starts
C) lagging indicators
D) durable-goods orders
E) price indexes
Answer: C
Explanation: Leading indicators suggest changes that may happen to the economy in the future and are therefore valuable for planning. In contrast, lagging indicators provide confirmation that something has occurred in the past.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Identify the major ways of measuring economic activity.

91) Which of the following is considered to be one of the key lagging economic indicators?
A) housing starts
B) durable-goods orders
C) price changes
D) corporate profits
E) Social Security
Answer: D
Explanation: Corporate profits and unemployment are among the key lagging indicators. For example, companies tend to reduce their workforces after the economy has slowed down and sales revenues have dropped.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.6: Identify the major ways of measuring economic activity.

92) What is the controversial way the U.S. government adjusts levels of Social Security payments and cost-of-living increases?
A) producer price index
B) gross domestic product
C) inflation rates
D) price-escalation clauses
E) consumer price index
Answer: E
Explanation: The consumer price index (CPI) measures the rate of inflation by comparing the change in prices of a representative "basket" of consumer goods and services, such as clothing, food, housing, and transportation. The CPI has always been a hot topic because the government uses it to adjust Social Security payments, businesses use it to calculate cost-of-living increases for employees, and many use it as a gauge of how well the government is keeping inflation under control.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.6: Identify the major ways of measuring economic activity.

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93) What can companies use to protect themselves in long-term purchasing contracts?
A) producer price index
B) gross domestic product rates
C) inflation rate clauses
D) price-escalation clauses
E) consumer price index
Answer: D
Explanation: In addition to monitoring economic activity, PPIs have a number of managerial uses, from helping companies place an accurate value on inventories to protecting buyers and sellers with price-escalation clauses in long-term purchasing contracts.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.6: Identify the major ways of measuring economic activity.

94) What is the broadest measure of a country's economic health?
A) Social Security
B) gross domestic product
C) inflation rate
D) spending
E) consumer price index
Answer: B
Explanation: The broadest measure of an economy's health is the gross domestic product (GDP), which measures a country's output–its production, distribution, and use of goods and services–by computing the sum of all goods and services produced for final use in a country during a specified period (usually a year).
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.6: Identify the major ways of measuring economic activity.

95) What should a government use to evaluate the success of economic policy and compare current performance to prior?
A) gross national product
B) gross domestic product
C) consumer price index
D) durable-goods orders
E) housing starts
Answer: B
Explanation: Monitoring GDP helps a nation to evaluate its economic policies and compare current performance with prior periods or with the performance of other nations.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.6: Identify the major ways of measuring economic activity.

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96) Leading economic indicators suggest changes that may happen in the economy in the future.
Answer: TRUE
Explanation: Leading economic indicators suggest changes that may happen in the economy in the future.
Difficulty: 1: Easy
AACSB: Application of knowledge
LO: 2.6: Identify the major ways of measuring economic activity.

97) GDP considers who is responsible for the production; GNP considers where the production occurs.
Answer: FALSE
Explanation: GNP considers who is responsible for the production; GDP considers where the production occurs.
Difficulty: 2: Moderate
AACSB: Application of knowledge
LO: 2.6: Identify the major ways of measuring economic activity.

98) What are economic indicators?
Answer: Economic indicators are statistics such as interest rates, unemployment rates, housing data, and industrial productivity that let business and political leaders measure and monitor economic performance. *Leading indicators* (such as durable-goods orders) suggest changes that may happen to the economy in the future, so they are valuable for planning. In contrast, *lagging indicators* (such as rates of unemployment) provide confirmation that something has occurred in the past.
Difficulty: 3: Challenging
AACSB: Analytical thinking
LO: 2.6: Identify the major ways of measuring economic activity.

99) Explain the meaning of a leading indicator with the help of an example.
Answer: Leading indicators suggest changes that may happen to the economy in the future and are therefore valuable for planning. Housing starts, for example, are a leading indicator that shows where several industries are headed. When housing starts drop, the construction industry contracts, and the effect soon ripples through other sectors of the economy, from the manufacture of plumbing fixtures, carpet, and appliances to a variety of services, including furniture retailing, real estate sales, and other areas dependent on housing-related transactions. Another key leading indicator is durable-goods orders, or orders for goods that typically last more than three years (which can mean everything from desk chairs to airplanes). A rise in durable-goods orders is a positive indicator that business spending is turning around. In addition to all these indicators, economists closely monitor several price indexes and the nation's economic output to get a sense of how well the economy is working.
Difficulty: 2: Moderate
AACSB: Analytical thinking
LO: 2.6: Identify the major ways of measuring economic activity.

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100) Explain three commonly known price indexes.
Answer: Government statisticians compute a huge variety of price indexes, each designed to monitor a particular aspect of economic activity. The best known of these, the consumer price index (CPI), measures the rate of inflation by comparing the change in prices of a representative "basket" of consumer goods and services, such as clothing, food, housing, and transportation. In contrast to the CPI, the producer price index (PPI) measures price at the producer or wholesaler level, reflecting what businesses are paying for the products they need. In addition to monitoring economic activity, PPIs have a number of managerial uses, from helping companies place an accurate value on inventories to protecting buyers and sellers with price-escalation clauses in long-term purchasing contracts. The broadest measure of an economy's health is the gross domestic product (GDP). The GDP measures a country's output–its production, distribution, and use of goods and services–by computing the sum of all goods and services produced for final use in a country during a specified period (usually a year). The products may be produced by either domestic or foreign companies as long as the production takes place within a nation's boundaries.
Difficulty: 2: Moderate
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