

# **Suggested Answers to Text Questions and Problems**

and

# **Answers to CourseTutor Homework Questions**



## Suggested Answers to Text Questions and Problems for Chapter 1

1. Yes, clearly going to college instead of going immediately to work represents a choice to get additional skills now and enter the labor force later. Even if you are working and going to school, you are choosing between investing in your education versus another leisure activity. You will see the benefits in the future, when your skills command greater resources.
2. Your study time on Wednesday.
3. Many reasons could be advanced to explain why we think things were better in an earlier time including (a) media attention seems to focus on problems, (b) we romanticize earlier times, (c) we get used to what we have and wish we had more, and so on. Easterbrook provided a long list of other reasons as well.
4. Computers and other technologies require extensive training and experience, and firms must establish the organizational structure to make the investment truly effective. For example, it took Wal-Mart a number of years to develop, collect, process, and analyze the immense data it collects from its stores “to determine specific goods to stock at specific stores at specific times of year as well as their prices.” See “Computer Use and Productivity Growth,” *National Economic Trends*, The Federal Reserve Bank of St. Louis, December 2003.
5. High-tech firms are hiring expensive, sophisticated people who are in high demand. This leads to better treatment of employees. If the firm does not offer these amenities to its employees, they soon become employees of other high-tech companies. Individuals with low skill levels do not command high salaries or benefits. They are not in as high demand as highly skilled people. It is efficient, but many would argue that it is not fair. Markets, as you will see, are efficient allocative mechanisms, but fairness is difficult to determine.
6. All of these groups benefit except the newly married couple trying to purchase their first home. When the housing market declines, the newly married couple gains and the others lose. For example, falling housing sales and prices mean that real estate agents sell fewer houses, at lower prices, so commissions are lower and their income is reduced. If the housing market is booming and the economy enters a recession, we can expect that unemployment will rise, incomes will fall, and sales in housing markets will decline as well.
7. Economic development by individuals in the developing countries means that their children are more likely to be educated, prosper, and less likely to wage war with their neighbors. Micro credit (small loans to poverty stricken people for self-development and small businesses) provides people with a stake in their communities, reducing poverty and promoting entrepreneurship, leading to a reduction in individual susceptibility to extremes in political and violent behavior. As the Nobel committee noted, “Lasting peace can not be achieved unless large population groups find ways in which to break out of poverty.”
8. Some reasons for the increase in economics majors might be: (1) The starting pay for economic majors upon graduation approaches \$50,000 a year; (2) globalization trends are producing a greater interest in knowing how economies interact; and (3) economic analysis is now being applied to a broader range of topics including issues such as crime, AIDS, college and professional sports, and terrorism.
9. It is probably bound to help somewhat. If only some have horns removed, however, poachers might still kill the rhino to keep from having to track this animal

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## Answers

in the future. After all, poachers are concerned with efficiency as well. Thus, the more animals with horns removed, the better the result. Also, dehorning may make the animals more susceptible to predators. But incentives do matter, and removing the horn on balance may help the effort to save the black rhino. See Charles Wheelan, *Naked Economics: Undressing the Dismal Science* (New York: WW Norton), 2002, Chapter 2.

10. The government can subsidize hybrid purchases directly, by offering people, say, \$2,000 to purchase cars that get greater than 40 miles per gallon, or offering tax credits. The government could add significant taxes on gasoline, increasing the price, making hybrid cars more attractive to consumers.
11. Several reasons might account for this phenomenon. Companies that are good to work for generate employee loyalty and high productivity. This makes it easier to hire higher-quality people. Also, many of the top firms are technology-driven firms where breakthroughs generate excitement and pride along with high profits, high wages, and benefits.

### Answers to CourseTutor Homework Questions for Chapter 1

- |      |      |      |      |
|------|------|------|------|
| 1. c | 3. d | 5. b | 7. b |
| 2. c | 4. b | 6. d | 8. d |

### Suggested Answers to Text Questions and Problems for Chapter 2

1. When there are unemployed resources, and the economy is operating within the production possibilities frontier.
2. A straight line PPF curve has constant opportunity costs, whereas the bowed out (concave to the origin) curve has increasing opportunity costs as the production of one good is increased.
3. Economies can grow through increases in the quality or quantity of labor, land, capital, and entrepreneurial activity. Increases in resources expand the PPF outward. Improvements in technological progress can increase growth in an economy.
4. Full employment of resources is represented along the PPF. Thus, if the economy wants to produce more of one product, it must accept less of the other. The output of one product that must be given up for the increased output of the other is the opportunity cost of that new production.
5. Technology will be most important in the how to produce question.
6. Any time the economy is operating inside the PPF, some resources will be unemployed, so any point inside the PPF represents unemployment.
7. Capital goods are those goods used to produce other goods. Producing more capital goods represents an investment in the economy. This investment leads to the ability of the country to produce more goods and services in the future.

8. Costa Rica and Bangladesh, while smaller, have a comparative advantage in the production of shirts, making it profitable for both countries to specialize and ship shirts to the United States.
9. Very much the same thing as for individuals. Nations (rich and poor), like families, have limited resources and are unable to do everything a nation would like to do: providing good roads, communications services, universal health care, and education for its people.
10. Both China and India have huge labor resources relative to available capital, so the job is done with a lot of labor and a little capital. The United States has less labor relative to capital, so wages are higher, and capital is substituted for labor.
11. No. Scarcity still exists in China. Growth alone does not eliminate scarcity: the PPF shifts outward, but still there are tradeoffs between products, and time is still a limited resource for us all. As rich as America is, we still face scarcity. Economic growth typically does improve standards of living, and the level (or degree) of scarcity declines.
12. While trade is typically beneficial to both countries in the aggregate, individuals and groups within each country lose when their product faces competition from a country with a comparative advantage.
13. It makes labor markets sluggish to adapt to changing market conditions and firms will be reluctant to hire new full-time employees so part-time employment will grow as a fraction of total employment. Labor inflexibility from firing and layoff costs along with labor unions have resulted in Europe's unemployment rates typically higher than those in the United States.
14. People living on \$1 to \$2 a day in poor developing nations would probably be more focused on economic growth and undoubtedly find it difficult to fret about the environmental impacts. Once their income reaches a reasonable level, more of their attention would turn to protecting and improving the environment.
- 15.

**Table 1 Initial Consumption-Production Pattern**

	United States	Mexico	Total
Oil	20	10	30
Chips	20	4	24

**Table 2 Production after Mexico Specializes in Producing Crude Oil**

	United States	Mexico	Total
Oil	10	20	30
Chips	30	0	30

**Table 3 Final Consumption Patterns after Trade**

	United States	Mexico	Total
Oil	20	10	30
Chips	23	7	30

Both Mexico and the United States are better off.

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## Answers

16. a. Florida's opportunity cost of oranges:  $2/50 = .04$ , or .04 jar of prickly pear jelly for each orange. The opportunity cost of a jar of prickly pear jelly:  $50/2 = 25$ , or 25 oranges must be given up for each jar of prickly pear jelly.
- b. Arizona's opportunity cost of oranges:  $100/20 = 5$ , or 5 jars of prickly pear jelly for each orange. The opportunity cost of a jar of prickly pear jelly:  $20/100 = .2$ , or .2 orange must be given up for each jar of prickly pear jelly.
- c. Total combined output for both states will rise to 250 oranges and 500 jars of prickly pear jelly. This is larger than the sum of any two combinations available to both states. They will be able to share the excess through trade.
17. a. unemployment  
 b. unattainable  
 c. technical advances in shoe production  
 d. economic growth; increases in resources or factors, or technological advances in both products

### Answers to CourseTutor Homework Questions for Chapter 2

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|--------------|------------|---------|-------|-------|
| 1. <b>b</b>  | 4. b lower | 6a. 10  | 9. a  | 13. d |
| 2. 2/3 bag   | 5a. 20     | b. 15   | 10. c | 14. c |
| 3a. c        | b. 35      | 7. c    | 11. d | 15. b |
| b. 1.33 bags |            | 8. b, c | 12. d |       |

1.

