

Managerial Economics and Strategy (Perloff/Brander)
Chapter 1 Introduction

1.1 Managerial Decision Making

- 1) Microeconomics studies the allocation of
- A) decision makers.
 - B) scarce resources.
 - C) models.
 - D) unlimited resources.

Answer: B

Difficulty: Analytical

AACSB: Analytic Skills

Status: Old

- 2) Society faces trade-offs because of
- A) government regulations.
 - B) profit motive.
 - C) price setting by firms.
 - D) scarcity.

Answer: D

Difficulty: Analytical

AACSB: Analytic Skills

Status: New

- 3) Managerial economics
- A) describes how pay for managers is set.
 - B) ensures managers always make good decisions.
 - C) helps managers make decisions in the face of scarcity.
 - D) explains which products consumers will buy.

Answer: C

Difficulty: Analytical

AACSB: Analytic Skills

Status: New

- 4) CEOs should focus on
- A) beating their competitors.
 - B) maximizing firm profits.
 - C) getting the best pay package for the senior management team.
 - D) minimizing costs.

Answer: B

Difficulty: Analytical

AACSB: Analytic Skills

Status: New

5) Profit is

- A) maximized when the marketing department coordinates with the production department.
- B) maximized when revenue is maximized.
- C) used to beat a company's rivals.
- D) the difference between a firm's revenues and its costs.

Answer: D

Difficulty: Analytical

AACSB: Analytic Skills

Status: New

6) Firms face tradeoffs because

- A) managers don't know which inputs to use.
- B) inputs are scarce.
- C) markets set prices of goods they sell.
- D) marginal reasoning leads to uncertainty.

Answer: B

Difficulty: Analytical

AACSB: Analytic Skills

Status: New

7) A firm's managers are constrained by

- A) consumers.
- B) workers.
- C) government.
- D) All of the above.

Answer: D

Difficulty: Conceptual

AACSB: Analytic Skills

Status: New

8) A market

- A) always involves the personal exchange of goods for money.
- B) allows interactions between consumers and firms.
- C) always takes place at a physical location.
- D) has no influence on prices.

Answer: B

Difficulty: Analytical

AACSB: Analytic Skills

Status: Old

- 9) In a market
A) the primary participants are consumers and firms.
B) government policies play a very small part.
C) decision makers always maximize.
D) the goods sold are always closely related.

Answer: A

Difficulty: Definition

AACSB: Analytic Skills

Status: New

- 10) Which of the following would NOT be considered part of a firm's strategy?
A) production levels
B) which inputs to use
C) sales strategy
D) None of the above - all are part of a firm's strategy.

Answer: D

Difficulty: Analytical

AACSB: Analytic Skills

Status: New

- 11) What is the purpose of having a strategy?

Answer: A strategy defines for a manager the actions to be taken to maximize the firm's profits.

Difficulty: Conceptual

AACSB: Communication

Status: New

- 12) Explain what the statement "We can't have everything we want" means.

Answer: Because resources are scarce, we face tradeoffs. For example, a baker cannot use a piece of dough she has for both pizza and a croissant, so she has to decide which to make.

Difficulty: Conceptual

AACSB: Reflective Thinking

Status: New

- 13) What is profit?

Answer: Profit is the difference between a firm's revenue or income and its costs or expenses.

Difficulty: Definition

AACSB: Communication

Status: New

- 14) Give an example of a tradeoff a pizza restaurant might face.

Answer: Whether to make pepperoni or combination pizzas.

Difficulty: Definition

AACSB: Analytic Skills

Status: New

15) Why might raising the price of a good by a dollar lead to lower profits?

Answer: If the extra profit margin made on the units sold does not cover the lost profit from selling fewer units, then profits will actually decrease if the price is raised.

Difficulty: Analytical

AACSB: Analytic Skills

Status: New

16) Why might raising the price of a good by a dollar lead to higher profits?

Answer: If the extra profit margin made on the units sold covers the profit lost from selling fewer units, then profits will increase if the price is raised.

Difficulty: Analytical

AACSB: Analytic Skills

Status: New

17) Raising the price of a good by one dollar

A) increases profits.

B) decreases profits.

C) leaves profits unchanged.

D) leads to an indeterminant change in profits.

Answer: D

Difficulty: Analytical

AACSB: Analytic Skills

Status: New

18) All private firms seek to

A) maximize revenue.

B) maximize profit.

C) minimize headcount.

D) maximize employee salaries.

Answer: B

Difficulty: Analytical

AACSB: Analytic Skills

Status: New

19) Behavioral economics

A) studies why people choose not to maximize.

B) studies why people maximize.

C) studies why people sometimes don't maximize.

D) studies why people behave badly when buying and selling.

Answer: C

Difficulty: Definition

AACSB: Analytic Skills

Status: New

For the following, please answer "True" or "False" and explain why.

20) Managers have to understand the decision making of others.

Answer: True. Other entities such as governments and rivals may undertake actions that constrain a firm. Consumers and workers make decisions on how to spend their scarce resources, such as budgets and time. To maximize profits, the manager must understand how these other entities will behave.

Difficulty: Conceptual

AACSB: Analytic Skills

Status: New

1.2 Economic Models

1) The purpose of making assumptions in economic model building is to

- A) force the model to yield the correct answer.
- B) minimize the amount of work an economist must do.
- C) simplify the model while keeping important details.
- D) express the relationship mathematically.

Answer: C

Difficulty: Analytical

AACSB: Analytic Skills

Status: Old

2) Einstein was quoted saying "Everything should be made as simple as possible, but not simpler." When it comes to economic models this means that

- A) models shouldn't be too complex.
- B) models shouldn't be too simple.
- C) models should have a level of abstraction appropriate to the topic investigated.
- D) All of the above.

Answer: D

Difficulty: Analytical

AACSB: Analytic Skills

Status: Old

3) If a model's predictions are correct, then

- A) its assumptions must have been correct.
- B) it is proven to be correct.
- C) Both A and B above.
- D) None of the above.

Answer: D

Difficulty: Analytical

AACSB: Analytic Skills

Status: Old

4) Economists tend to judge a model based upon

- A) the reality of its assumptions.
- B) the accuracy of its predictions.
- C) its simplicity.
- D) its complexity.

Answer: B

Difficulty: Analytical

AACSB: Analytic Skills

Status: Old

5) Which of the following is an example of a normative statement?

- A) A higher price for a good causes people to want to buy less of that good.
- B) A lower price for a good causes people to want to buy more of that good.
- C) To make the good available to more people, a lower price should be set.
- D) If you consume this good, you will be better off.

Answer: C

Difficulty: Analytical

AACSB: Analytic Skills

Status: Old

6) Which of the following is an example of a normative statement?

- A) Since this food is bad for you, you should not consume it.
- B) This food has negative health effects.
- C) If you consume this food, you will get sick.
- D) People usually get sick after consuming this food.

Answer: A

Difficulty: Analytical

AACSB: Analytic Skills

Status: New

7) Which of the following is an example of a positive statement?

- A) Since this food is bad for you, you should not consume it.
- B) If this food is bad for you, you should not consume it.
- C) If you consume this food, you will get sick.
- D) None of the above.

Answer: C

Difficulty: Analytical

AACSB: Analytic Skills

Status: New

8) If an important assumption is omitted from an economic model

- A) the model's predictions will be accurate 50% of the time.
- B) the model's predictions will be inaccurate.
- C) the model will not predict anything.
- D) the model will be rejected by other economists.

Answer: B

Difficulty: Analytical

AACSB: Analytic Skills

Status: Old

9) Economic models are most useful in

- A) explaining outcomes resulting from management decisions.
- B) predicting the direction of the stock market.
- C) explaining the future with the past.
- D) generating untestable hypotheses.

Answer: A

Difficulty: Analytical

AACSB: Analytic Skills

Status: New

10) Economic models are most useful in

- A) predicting changes in one variable due to a change in one or more other variables.
- B) predicting the direction of the stock market.
- C) explaining the future with the past.
- D) generating untestable hypotheses.

Answer: A

Difficulty: Analytical

AACSB: Analytic Skills

Status: Old

11) Economic models are most often tested

- A) using computer simulations.
- B) using data from the distant past.
- C) using data from the real world.
- D) using logic alone.

Answer: C

Difficulty: Analytical

AACSB: Analytic Skills

Status: Old

- 12) A microeconomic model CANNOT be used to
- A) evaluate the impact of a price change on a firm's revenue.
 - B) predict the impact of an increase in the minimum wage on unemployment.
 - C) evaluate the fairness of a proposal to nationalize health insurance.
 - D) evaluate the effect of an increase in stadium size on the price of a sport team's tickets.

Answer: C

Difficulty: Analytical

AACSB: Analytic Skills

Status: Old

- 13) Economic models are only useful in analyzing government policy.
- A) True, individuals are irrational and therefore economic models are useless.
 - B) False, economic models can be used to predict individual and firm behavior.
 - C) True, economists only model those questions for which they are hired.
 - D) False, economic models are not even useful in analyzing government policy.

Answer: B

Difficulty: Analytical

AACSB: Analytic Skills

Status: Old

- 14) Microeconomic models are used to
- A) make predictions.
 - B) explain real-life phenomena.
 - C) evaluate production alternatives.
 - D) All of the above.

Answer: D

Difficulty: Analytical

AACSB: Analytic Skills

Status: New

- 15) If a theory's predictions are incorrect
- A) then economists always reject it.
 - B) then the data used was clearly faulty.
 - C) then economists will likely reduce their confidence in the theory.
 - D) then the model must be too simple.

Answer: C

Difficulty: Analytical

AACSB: Analytic Skills

Status: New

16) Legislators argue that a minimum wage law is instituted to help poor people. Economists can attack the minimum wage law on two fronts. First, some argue that government should not help the poor. Second, some argue that minimum wage laws actually hurt the poor because it creates unemployment. Which argument is normative and which is positive?

Answer: An opinion about the role of government is a normative statement. An observation about the impact of a law is a positive statement.

Difficulty: Analytical

AACSB: Analytic Skills

Status: Old

17) Explain why a model that delivers good enough approximations is a good model.

Answer: Models make simplifying assumptions in order to make them less complex and complicated and therefore usable. But when we simplify, we do leave out parts of the real world that have an impact on the results. If a model gives predictions or approximations that are close to reality, then the model is useful.

Difficulty: Analytical

AACSB: Analytic Skills

Status: New

18) Explain why economists might disagree on the content of a model.

Answer: Economists might have different theories or might make different simplifying assumptions.

Difficulty: Conceptual

AACSB: Analytic Skills

Status: New

For the following, please answer "True" or "False" and explain why.

19) Normative analysis offers decision makers the most valuable information when choosing among alternatives.

Answer: False. Normative analysis states subjective goals but not how those goals can be achieved. To choose among alternatives a decision maker uses positive analysis.

Difficulty: Analytical

AACSB: Analytic Skills

Status: Old

20) If a model fits reality but doesn't generate testable predictions, it is of little value to economists.

Answer: True. If the model doesn't deliver testable predictions it cannot be tested against competing models.

Difficulty: Analytical

AACSB: Analytic Skills

Status: Old

21) If actual experience supports two competing theories, then both theories are proven to be true.

Answer: False. Neither theory can be rejected but if they are competing, then the test is inconclusive.

Difficulty: Analytical

AACSB: Analytic Skills

Status: Old