

Managerial Economics and Strategy, 3e (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

Skill: Definition

AACSB: Analytical Thinking

Status: Old

2) Society faces trade-offs because of

- A) government regulations.
- B) the profit motive.
- C) price setting by firms.
- D) scarcity.

Answer: D

Skill: Conceptual

AACSB: Analytical Thinking

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

Skill: Conceptual

AACSB: Analytical Thinking

Status: Old

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

Skill: Conceptual

AACSB: Analytical Thinking

Status: Old

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

Skill: Definition

AACSB: Analytical Thinking

Status: Old

6) Firms face trade-offs 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

Skill: Conceptual

AACSB: Analytical Thinking

Status: Old

7) A firm's managers are constrained by

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

Answer: D

Skill: Conceptual

AACSB: Analytical Thinking

Status: Old

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

Skill: Conceptual

AACSB: Analytical Thinking

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 not closely related.

Answer: A

Skill: Conceptual

AACSB: Analytical Thinking

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

Skill: Conceptual

AACSB: Analytical Thinking

Status: Old

- 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.

Skill: Conceptual

AACSB: Written and Oral Communication

Status: Old

- 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.

Skill: Conceptual

AACSB: Reflective Thinking

Status: Old

- 13) What is profit?

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

Skill: Definition

AACSB: Written and Oral Communication

Status: Old

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

Answer: Whether to make pepperoni or combination pizzas.

Skill: Definition

AACSB: Analytical Thinking

Status: Old

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.

Skill: Analytical

AACSB: Analytical Thinking

Status: Old

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.

Skill: Analytical

AACSB: Analytical Thinking

Status: Old

17) Raising the price of a good by one dollar

A) increases profits.

B) decreases profits.

C) leaves profits unchanged.

D) leads to an indeterminate change in profits.

Answer: D

Skill: Analytical

AACSB: Analytical Thinking

Status: Old

18) Most private firms seek to

A) maximize revenue.

B) maximize profit.

C) minimize headcount.

D) maximize employee salaries.

Answer: B

Skill: Conceptual

AACSB: Analytical Thinking

Status: Old

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

19) 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.

Skill: Conceptual

AACSB: Analytical Thinking

Status: Old

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

Skill: Conceptual

AACSB: Analytical Thinking

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

Skill: Analytical

AACSB: Analytical Thinking

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

Skill: Conceptual

AACSB: Analytical Thinking

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

Skill: Conceptual

AACSB: Analytical Thinking

Status: Old

- 5) 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

Skill: Conceptual

AACSB: Analytical Thinking

Status: Old

- 6) If an important assumption is omitted from an economic model,
- A) the model's predictions will only be accurate 50% of the time.
 - B) the model's predictions may be inaccurate.
 - C) the model will not predict anything.
 - D) the model is not simple enough.

Answer: B

Skill: Conceptual

AACSB: Analytical Thinking

Status: Old

- 7) 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

Skill: Conceptual

AACSB: Analytical Thinking

Status: Old

- 8) 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

Skill: Analytical

AACSB: Analytical Thinking

Status: Old

- 9) 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

Skill: Conceptual

AACSB: Analytical Thinking

Status: Old

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

Answer: D

Skill: Conceptual

AACSB: Analytical Thinking

Status: Old

- 11) 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

Skill: Conceptual

AACSB: Analytical Thinking

Status: Old

- 12) 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 decrease the amount of sugar in soda drinks, sales to children will decrease.

Answer: C

Skill: Conceptual

AACSB: Analytical Thinking

Status: New

13) 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

Skill: Conceptual

AACSB: Analytical Thinking

Status: Old

14) 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

Skill: Conceptual

AACSB: Analytical Thinking

Status: Old

15) Behavioral economics is the study of why people

- A) choose not to optimize.
- B) optimize.
- C) sometimes don't optimize.
- D) behave badly when buying and selling.

Answer: C

Skill: Definition

AACSB: Analytical Thinking

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.

Skill: Analytical

AACSB: Analytical Thinking

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.

Skill: Analytical

AACSB: Analytical Thinking

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.

Skill: Conceptual

AACSB: Analytical Thinking

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.

Skill: Analytical

AACSB: Analytical Thinking

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.

Skill: Analytical

AACSB: Analytical Thinking

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.

Skill: Analytical

AACSB: Analytical Thinking

Status: Old