

Name _____ Class _____ Date _____
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Chapter 01: The Role and Method of Economics

True / False

1. As resources are abundant, we do not have to make choices about their use.

- a. True
- b. False

ANSWER: False

2. Scarcity forces us to choose, and choices are costly because we must give up other opportunities that we value.

- a. True
- b. False

ANSWER: True

3. Tractors, shovels, copy machines, and computer programming expertise are all examples of scarce resources.

- a. True
- b. False

ANSWER: True

4. Wealthy consumers do not have to make decisions on what to buy or how much to save.

- a. True
- b. False

ANSWER: False

5. It is possible to completely eliminate scarcity.

- a. True
- b. False

ANSWER: False

6. Economists assume that most individuals act as if they are motivated by self-interest and respond in predictable ways to changing circumstances.

- a. True
- b. False

ANSWER: True

7. Economists believe that human behavior cannot be explained and predicted by assuming that most people act as if they are motivated by their own self-interest.

- a. True
- b. False

ANSWER: False

8. Self-interest can never include benevolence

- a. True
- b. False

ANSWER: False

9. To an economist, individuals act rationally if they strive to do their best to achieve their goals

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- a. True
- b. False

ANSWER: True

10. Economists presume that while making a decision, individuals consider both the current action and the expected future consequences of that action.

- a. True
- b. False

ANSWER: True

11. At the time of making their choices, people typically know with certainty which choice is best.

- a. True
- b. False

ANSWER: False

12. Economic models are of very limited use since they cannot be tested empirically.

- a. True
- b. False

ANSWER: False

13. A hypothesis is a normative statement

- a. True
- b. False

ANSWER: False

14. *Ceteris paribus* is a Latin expression that means "holding everything else constant."

- a. True
- b. False

ANSWER: True

15. . It is possible to predict with certainty how a given individual will respond to a price change.

- a. True
- b. False

ANSWER: False

16. The fallacy of composition states that even if something is true for an individual, it is not necessarily true for many individuals as a group.

- a. True
- b. False

ANSWER: True

17. When two variables repeatedly change at the same time, there must be a causal relationship between them.

- a. True
- b. False

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ANSWER: False

18. Most disagreements among economists stem from normative issues.

- a. True
- b. False

ANSWER: True

19. To be a positive economic statement, an assertion must be true.

- a. True
- b. False

ANSWER: False

20. Normative analysis focuses on statements that can be tested against data.

- a. True
- b. False

ANSWER: False

21. A tax cut will lead to higher inflation. This is an example of a positive economic statement.

- a. True
- b. False

ANSWER: True

Multiple Choice

22. Economics is the study of:

- a. Economics is the study of:
- b. limited desires pursuing unlimited resources.
- c. the production and the distribution of goods in a world with limited resources.
- d. the evolution of society and human behavior over the ages.
- e. the psychological aspect of economic decision making.

ANSWER: c

23. The central question in economics is how to:

- a. regulate the supply of money in an economy.
- b. make the best use of scarce resources to satisfy our unlimited wants.
- c. reduce the demands of individuals, businesses, and governments.
- d. find more resources to satisfy everyone's wants.
- e. restrict the role of the government in economic activities.

ANSWER: b

24. Incorrect. Economics is the study of the choices we make among our many wants and desires given our limited resources. See 1-1: Economics: A Brief Introduction

- a. typically uses controlled experiments to learn about consumer and firm behavior.
- b. uses models that cannot be tested empirically because of the complex nature of the economy.

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- c. explores how choices are made between conflicting wants and desires in a world of scarcity.
- d. relies entirely on normative analysis to validate all hypotheses.
- e. relies entirely on empirical analysis to validate all hypotheses.

ANSWER:

c

25. The problem of scarcity:

- a. exists because resources are limited relative to wants.
- b. exists because wants are limited relative to resources.
- c. can be eliminated through appropriate government intervention in markets.
- d. does not exist in communist societies.
- e. does not exist in a barter economy.

ANSWER:

a

26. Which of the following forces us to choose among alternatives?

- a. Marginal utility
- b. Scarcity
- c. Deflation
- d. Rational ignorance
- e. The fallacy of composition

ANSWER:

b

27. Scarcity is:

- a. a problem only in modern industrialized economies.
- b. a problem only in underdeveloped economies
- c. a problem only in centrally planned economies.
- d. a problem that necessitates tradeoffs
- e. a problem that can only be eliminated by the government

ANSWER:

d

28. Scarcity:

- a. occurs only in command economies
- b. can be eliminated by technological progress.
- c. exists only in capitalist economies
- d. occurs if there are insufficient resources to provide for all human wants
- e. can be eliminated by investment in human capital.

ANSWER:

d

29. Economists believe that individuals:

- a. aim to maximize social welfare.
- b. aim to maximize their material consumption.
- c. are motivated by self-interest and rational behavior
- d. are motivated by altruism and selflessness.
- e. always ensure an efficient allocation of resources in the market economy.

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ANSWER:

c

30. Economists assume that when people act rationally they:

- a. make decisions based on complete and accurate information
- b. make decisions that they will not regret later on.
- c. make decisions based on what they believe is best for themselves, using available information.
- d. make decisions based on what they believe is best for themselves, using available information.
- e. make decisions that cannot be altered in the future.

ANSWER:

c

31. From an economist's perspective, which of the following observations is *not* true?

- a. Self-interest is purely monetary in nature
- b. Self-interest can include benevolence
- c. Self-interest is a good predictor of human behavior in most situations
- d. Self-interest is not the same as selfishness
- e. Self-interest makes people respond in predictable ways.

ANSWER:

a

32. When making decisions, economists believe that individuals act rationally if they:

- a. seek to improve their own situations and do not try to anticipate the future consequences of their actions.
- b. only pursue the goals of the community.
- c. seek to improve their own situations.
- d. always choose alternatives that offer the greatest financial reward.
- e. always choose alternatives that offer the greatest financial reward.

ANSWER:

c

33. Economists believe that individuals:

- a. are motivated primarily by the opinions of their peers.
- b. can eradicate scarcity by acting rationally
- c. respond in predictable ways to changing circumstances.
- d. are concerned only about the welfare of the community and ignore their self-interest.
- e. can eradicate scarcity by limiting their demands.

ANSWER:

c

34. A person behaving rationally will:

- a. always avoid illegal actions.
- b. explain or rationalize his or her decision
- c. refrain from normative analysis and base his or her decisions on facts.
- d. consider the future consequences of his or her behavior.
- e. never face scarcity

ANSWER:

d

35. Individuals:

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- a. respond to incentives in predictable ways.
- b. increase the level of an activity in response to negative incentives.
- c. decrease the level of an activity in response to positive incentives
- d. respond to incentives in unpredictable ways.
- e. offer more help when the cost of helping others is high.

ANSWER:

a

36. Which of the following is an example of a positive incentive?

- a. Jim expects to be grounded if his grades slip below a B average
- b. Sam expects to receive a scholarship if his grades remain high.
- c. Desserts will be unavailable at the cafeteria if you arrive after 7:00 p.m
- d. The college campus police institutes a policy of impounding cars parked in delivery zone spaces.
- e. Sam chooses piano lessons over martial arts classes.

ANSWER:

b

37. If a university begins a policy of permanently expelling any student caught cheating in any way, you would expect that:

- a. no students would cheat.
- b. fewer students would cheat.
- c. there would be no difference in the amount of cheating.
- d. the enrollment of students would triple
- e. the enrollment of students would double

ANSWER:

b

38. Suppose the government decides to impose a tax on each child born. Then, it is likely that:

- a. families would have the same number of children, but parents would wait longer to start a family.
- b. more children would be born, with substantial age gaps between them.
- c. more children would be adopted
- d. fewer children would be born.
- e. families would have the same number of children, but parents would not wait long to start a family.

ANSWER:

d

39. Several political leaders have proposed that parents be granted a substantially large reduction in their annual personal income taxes for each child that they parent. The economic logic behind this type of legislation is that:

- a. it will make it more expensive for parents to provide for their children
- b. it will increase the cost of education and, therefore, lead to a reduction in the birth rate
- c. it will reduce the after-tax cost of raising children and, therefore, increase the birth rate.
- d. it will have no impact on either the cost of raising children or the birth rate because parenting children is a non-economic activity.
- e. it will increase the after-tax cost of raising children and, therefore, decrease the birth rate.

ANSWER:

c

40. When economists speak of markets, they primarily refer to:

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- a. the places where the exchange of services takes place
- b. those locations where the stocks and bonds of corporations are bought.
- c. the mechanisms that coordinate the actions of buyers and sellers.
- d. the foreign exchange markets where trillions of dollars change hands.
- e. the goods market where tangible products are bought and sold.

ANSWER:

c

41. In a market system, decisions about how to allocate resources are made:
- a. by central planning boards in each industry.
 - b. by a lottery system
 - c. by individuals and firms interacting in markets coordinated by market prices.
 - d. by large conglomerates working cooperatively with the government.
 - e. by cartels of the largest firms in an economy.

ANSWER:

c

42. Which of the following serves as the language of the market system?

- a. Fiscal policies
- b. Monetary policies
- c. Market prices
- d. Governments
- e. Exchange rates

ANSWER:

c

43. A decrease in the price of corn signals to consumers and producers that:

- a. consumers are buying more corn than before.
- b. corn is relatively more abundant than before.
- c. corn is relatively less abundant than before.
- d. producers are stocking up on corn.
- e. producers are more willing to supply corn in the current period.

ANSWER:

b

44. Government price controls:

- a. undermine the market's ability to communicate relative scarcities to buyers and sellers.
- b. always impose a cost on the people they try to assist
- c. always force prices above what they would be in a market economy.
- d. always force prices below what they would be in a market economy
- e. result in increased market efficiency.

ANSWER:

a

45. Market failure occurs when

- a. stock markets crash because of the heavy selling of equities.
- b. an economy fails to allocate resources efficiently on its own
- c. consumer demand shows signs of slowing down

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- d. an economy cannot produce a good or service at a lower opportunity cost than others.
- e. there is a scarcity or surplus of goods in a market.

ANSWER:

b

46.

Which of the following is an example of market failure?

- a. Industrial water pollution
- b. eBay transactions
- c. Tradable pollution permits
- d. Brokers reselling tickets for concerts
- e. Excess demand for wheat

ANSWER:

a

47. In a market system, one symptom of market failure is:

- a. competition
- b. falling prices
- c. scarcity of resources.
- d. air pollution.
- e. surplus.

ANSWER:

d

48. The circular flow of economic activity is a model that shows:

- a. the exchange of goods, services, and income between households and firms
- b. the influence of government on the level of economic activity in a country.
- c. the role of labor unions and government in the economy
- d. the interaction among taxes, prices, and profits in an economy.
- e. the taxes levied by the government and the revenue earned by the government.

ANSWER:

a

49. The circular flow model shows that

- a. households receive income from businesses in exchange for providing inputs and use the income to buy goods and services from businesses.
- b. businesses receive rent from households in exchange for providing goods and services and use the income to buy inputs from households
- c. households receive revenue for selling goods and services to businesses and use the revenue to buy inputs from businesses.
- d. businesses receive revenue for providing inputs to households and use the revenue to buy goods and services.
- e. businesses receive wages and interest, which they use to invest for the growth of an economy as a whole.

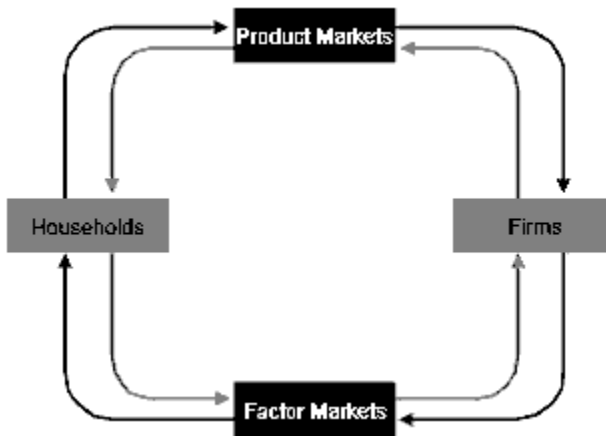
ANSWER:

a

50. Refer to the figure given below. Goods and services:

Figure 1-1

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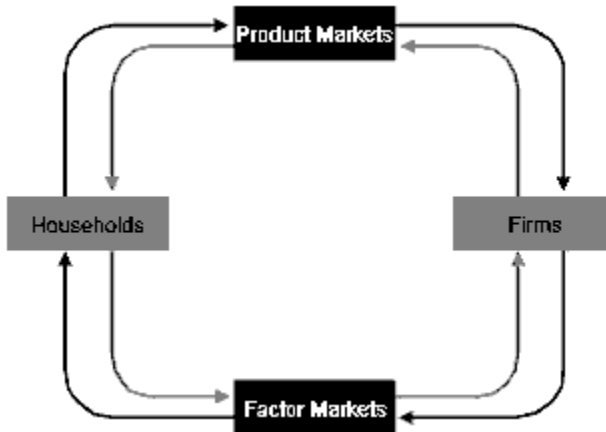
- flow in a clockwise direction.
- flow in a counterclockwise direction.
- are sold by businesses in the factor market.
- are sold by households in the factor market
- are sold by households in the product market.

ANSWER:

b

51. Refer to the figure given below. Payments for goods and services:

Figure 1-1



- flow in a clockwise direction.
- flow in a counterclockwise direction
- are received by firms in the factor market
- are received by households in the factor market
- are received by households in the product market.

ANSWER:

a

52. The circular flow model indicates that:

- households demand resources
- firms demand final products
- firms demand resources.
- households supply goods and services.

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- e. firms supply resources.

ANSWER:

c

53. The simple circular flow model shows that workers and the owners of land and capital offer their resources through:

- a. product markets
- b. factor markets.
- c. money markets.
- d. the government.
- e. foreign exchange markets.

ANSWER:

b

54. The simple circular flow model shows that:

- a. firms are the suppliers of resources and the buyers of products.
- b. households are the suppliers of products and the buyers of resources.
- c. households are the buyers of products and the suppliers of resources.
- d. firms are the suppliers of both resources and products.
- e. firms demand both resources and products.

ANSWER:

c

55. A good economic theory:

- a. must be based on assumptions
- b. explains economic behavior and predicts well.
- c. can always be proved by past economic events.
- d. always provides a highly detailed analysis of an economic sector.
- e. must be based on rigorous mathematical calculations.

ANSWER:

b

56. An economic theory:

- a. should be as detailed as possible in order to model the complexity of an economy.
- b. is an abstraction from reality.
- c. is only useful if it is based on assumptions and mathematical calculations.
- d. should be based on observable facts and events
- e. is based on controlled experimentation

ANSWER:

b

57. An economic theory

- a. always includes every detail that affects the economic behavior of individuals
- b. often relies on simplifying assumptions in order to explain economic behavior.
- c. is rigid in its approach and does not change with changes in empirical evidence.
- d. arrives at a conclusion only after conducting controlled experiments
- e. always nullifies empirical evidence.

ANSWER:

b

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58. Economics is different from other disciplines like physics because:

- a. economists do not use mathematical calculations to prove their theories.
- b. economics is easier to study than physics.
- c. economists must explain their theories to policy makers who lack formal mathematical training.
- d. economists cannot easily control all the variables that might influence human behavior.
- e. economists must prove their hypothesis based on normative analysis.

ANSWER:

d

59. An economic hypothesis:

- a. can be tested using empirical analysis.
- b. can be tested using normative analysis.
- c. cannot be tested since it is normative in nature.
- d. cannot be tested since it is a positive economic statement.
- e. cannot be tested using empirical analysis.

ANSWER:

a

60. A hypothesis is a:

- a. normative economic statement
- b. testable proposition.
- c. statement that cannot be evaluated using real-world data.
- d. model with no connection to the real world.
- e. positive economic statement.

ANSWER:

b

61. An economic theory is tested by:

- a. assessing the realism of its assumptions.
- b. polling economists to see if there is consensus on the validity of the hypothesis.
- c. comparing and contrasting its simplicity with other related theories.
- d. comparing its predictions with real-world data
- e. polling the general public to see if people agree with the theory.

ANSWER:

d

62. Which of the following is true of hypothesis and theory?

- a. They are interchangeable terms meaning the same thing
- b. A hypothesis may result from a tested and confirmed theory.
- c. A theory may result from a tested and confirmed hypothesis.
- d. A hypothesis is a theory whose formulation relies on mathematics.
- e. They are economic terms with opposite meanings.

ANSWER:

c

63. The term *ceteris paribus* means that:

- a. the causal relationship between two economic variables cannot be determined.
- b. an analysis is true for the individual but not for the economy as a whole.

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- c. all other variables except the ones specified are assumed to be constant
- d. conclusions are based on normative rather than on positive economic analysis.
- e. one variable causes another to occur if certain conditions are satisfied.

ANSWER:

c

64. The importance of the *ceteris paribus* assumption is that it:

- a. allows one to separate normative economic issues from positive economic ones.
- b. allows one to generalize from the whole to the individual.
- c. allows one to analyze the relationship between two variables apart from the influence of other variables
- d. allows one to hold all variables constant so that an economy can be carefully observed in a suspended state.
- e. allows one to generalize from the individual to the whole.

ANSWER:

c

65. Economic theory asserts that manufacturers are willing to sell fewer units of output as the price of a good decreases, *ceteris paribus*. However, as the price of computers decreased throughout the 1990s, more computers were sold. Which of the following best explains the apparent conflict between theory and data

- a. The theory must be invalid.
- b. The theory was based on assumptions that were too simplistic.
- c. It is likely that variables other than the price and the quantity of computers sold had changed
- d. All variables other than the price and the quantity of computers sold were unchanged.
- e. The empirical evidence gathered to support the theory was manipulated.

ANSWER:

c

66. A leading game console manufacturer reduces the price of its flagship product by 10 percent. Holding other things such as income and preferences constant, which of the following is the most likely group behavior prediction?

- a. The price reduction will have no impact on purchase patterns.
- b. The price reduction will be associated with a reduction in quality.
- c. The price reduction will increase the quantity of game consoles demanded.
- d. Group behavior cannot be predicted for consumer goods
- e. Group behavior can be predicted for consumer goods only if the *ceteris paribus* assumption does not hold.

ANSWER:

c

67. The relationship between the price of a good and its quantity supplied can be determined through:

- a. normative analysis
- b. positive analysis.
- c. the collective behavior of a group of producers
- d. the individual reactions of producers.
- e. hypothesis testing.

ANSWER:

c

68. Economists prefer:

- a. measuring declared preferences for forecasting because participants in a survey always declare the truth.
- b. measuring revealed preferences because it gives more accurate results.

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- c. predicting individual behavior as it is easy to collect data from individuals.
- d. predicting individual behavior as it is easy to draw inferences from such data.
- e. measuring revealed preferences because cost-benefit analysis can be conducted with such data

ANSWER:

b

69. In the context of correlation and causation, correlation means that:

- a. two sets of phenomena occur together
- b. two sets of phenomena are positively related
- c. one phenomenon must cause the other when two sets of phenomena are repeatedly observed together.
- d. one phenomenon must cause the other when two sets of phenomena are repeatedly observed together
- e. two sets of phenomena are negatively related.

ANSWER:

a

70. Suppose it is observed in a school that students who sit at the back of a classroom, on average, receive lower grades in economics than the rest of the class. This leads to the teachers at the school assuming that sitting at the back rows leads to lower grades. This is an example of:

- a. the fallacy of composition.
- b. the *ceteris paribus* assumption.
- c. mistaking correlation for causation
- d. normative analysis.
- e. marginal analysis.

ANSWER:

c

71. Ten-year-old Josh observes that people who play football are taller than other people and tells his mom that he is going to play football because it will make him big and strong. Josh is:

- a. committing the fallacy of composition.
- b. violating the *ceteris paribus* assumption
- c. mistaking correlation for causation.
- d. performing hypothesis testing.
- e. comparing the marginal benefits and the marginal costs of playing football.

ANSWER:

c

72. The fallacy of composition is essentially the error of:

- a. confusing association with causation
- b. confusing normative economics with positive economics.
- c. generalizing from the individual to the whole.
- d. omitting relevant variables from an economic model
- e. ignoring the effects of secondary variables on a primary variable

ANSWER:

c

73. The fallacy of composition is:

- a. the erroneous view that an economic activity can sometimes exceed the sum of its components.
- b. the erroneous view that what is true for an individual must also be true for the group

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- c. the view that the aggregation of economic activity will necessarily lead to an outcome that is different from the outcome generated by each individual in a group
- d. the idea that association need not imply causation.
- e. the idea that association always implies causation.

ANSWER:

b

74. When one basketball team spends a large sum of money acquiring better players, it is better off. If all teams do the same thing, all of them will be better off." These statements demonstrate:

- a. the fallacy of composition
- b. the fallacy that association is causation.
- c. a misunderstanding of the direction of causality.
- d. the *ceteris paribus* condition
- e. the rational expectations theory.

ANSWER:

a

75. Which of the following statements best illustrates the fallacy of composition?

- a. If I stand up at a baseball game, I will be able to see the game better; if everybody stands up, everyone will be able to see the game better.
- b. If I stand up at a baseball game, I will be able to see the game better; if everybody stands up, everyone will be able to see the game better.
- c. If I purchase fewer tickets at a baseball game, I will save money; if everybody purchases fewer tickets, they can all save money.
- d. If I yell more during a baseball game, it will be loud; if everybody yells more during the game, it will be much louder
- e. If I support the Red Sox, the team will win; if everybody in Boston supports the Red Sox, the team will win all the matches

ANSWER:

a

76. Which of the following statements best illustrates the fallacy of composition?

- a. If the price of a product increases, the quantity of the product supplied will decline, *ceteris paribus*.
- b. The average wage rate tends to increase at approximately the same rate as inflation; hence, wage increases must cause inflation.
- c. Resources are scarce; therefore, there is no such thing as a free lunch.
- d. If I talk loudly at a party, I have a better chance of being heard by my listeners; if everyone at the party talks loudly, everyone can be heard more clearly.
- e. If the price of a product increases, the quantity of the product supplied will increase, *ceteris paribus*.

ANSWER:

d

77. Which of the following statements best illustrates the fallacy of composition?

- a. If I have more money, I will be better off; if we all had more money, we l would all be better off.
- b. If the sale of women's clothing is higher this year, the Dow Jones Industrial Average will fall.
- c. If I spend more time studying, I will get good grades; if all students spend more time studying, they will all get good grades.
- d. If the sale of women's clothing is higher this year, the Dow Jones Industrial Average will fall.

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e. If the sale of men's clothing is lower this year, the Dow Jones Industrial Average will rise.

ANSWER:

a

78. Which of the following is a difference between positive economics and normative economics?

- a. Positive economics helps us understand an economy's response to a particular policy, while normative economics reflects value judgments.
- b. Positive economics helps us understand the positive effects of a policy change, while normative economics helps us understand the negative results of a policy change.
- c. Positive economics is a branch of microeconomics, while normative economics is a branch of macroeconomics
- d. Positive economics is a branch of macroeconomics, while normative economics is a branch of microeconomics.
- e. Positive economics is used by economists to evaluate the performance of an economy, while normative economics is used by governments to formulate economic policies.

ANSWER:

a

79. Which of the following is a statement of positive economics?

- a. New tax laws are needed to help the poor.
- b. Teenage unemployment should be reduced.
- c. We should increase Social Security payments to the elderly
- d. An increase in tax rates will reduce unemployment.
- e. The poorest quintile of the population should receive 10 percent of total income.

ANSWER:

d

80. Which of the following is a statement of positive economics?

- a. Income tax reduces the after-tax income of the rich.
- b. A reduction in tax rates makes the after-tax distribution of income fair.
- c. A reduction in tax rates makes people work more.
- d. People should involve themselves in charitable works.
- e. People above the age of 60 should stop working more and take more vacations.

ANSWER:

a

81. Which of the following is a statement of positive economics?

- a. Unemployment is a more severe problem than inflation.
- b. Our current unemployment rate is a serious problem.
- c. The current rate of unemployment in an economy is 4 percent.
- d. An unemployment rate of 4 percent would be too low
- e. Unemployment is a more severe problem than illiteracy

ANSWER:

c

82. Positive statements are:

- a. prescriptive, making claims about how the world ought to be.
- b. descriptive, making claims about how the world is.
- c. optimistic, putting forward the best possible interpretation of things.

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- d. affirmative, justifying existing economic policy.
- e. affirmative, explaining the positive effects of economic policies.

ANSWER:

b

83. An economic study concludes that an investment tax credit would increase business investment next year. This is an example of:

- a. normative analysis.
- b. positive analysis.
- c. mistaking correlation for causation.
- d. the fallacy of composition
- e. ignoring secondary effects.

ANSWER:

b

84. Which of the following is an example of a positive statement?

- a. New tax laws implemented by the government are likely to benefit the poor.
- b. An increase in cigarette smoking will increase the likelihood of getting lung cancer.
- c. The government should encourage all able-bodied citizens to enroll in the army.
- d. The government should provide tax benefits to parents with more than two kids
- e. There should be equality in the distribution of income in an economy

ANSWER:

b

85. A reduction in the rate at which dividends are taxed will lead to greater investment in the stock market. This is an example of:

- a. a positive economic statement.
- b. a negative economic statement.
- c. the fallacy of composition
- d. a normative economic statement.
- e. the *ceteris paribus* assumption.

ANSWER:

a

86. Normative statements are:

- a. Normative statements are
- b. descriptive, making claims about how the world is.
- c. optimistic, putting the best possible interpretation on things.
- d. statements that establish the production goals for an economy.
- e. statements that establish the pattern for the distribution of income in an economy.

ANSWER:

a

87. Which of the following represents a normative statement?

- a. A decrease in price leads to an increase in quantity demanded.
- b. The study of economics is more important than the study of history.
- c. People will buy less butter at \$1.50 per pound than they will at \$1.00 per pound
- d. As an economy develops, the nation's birth rate tends to decrease.

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- e. As an economy develops, the employment rate in the service sector tends to increase.

ANSWER:

b

88. Which of the following is an example of a normative statement?

- a. Higher unemployment rates are common among young people
- b. Young people should learn how to prepare their own taxes.
- c. Auto insurance rates are generally lower for younger drivers.
- d. Persons under the age of 30 watch more movies than those over the age of 30.
- e. The production of certain goods generates negative externalities.

ANSWER:

b

89. Which of the following is a normative statement?

- a. An increase in taxes will cause higher unemployment in an economy.
- b. An increase in tariffs in a country will increase the prices paid by domestic consumers.
- c. Income should be redistributed from the top 2 percent of wage earners to the low-income group.
- d. Income should be redistributed from the top 2 percent of wage earners to the low-income group.
- e. National debt imposes a burden on both current and future generations.

ANSWER:

c

90. Suppose senators, members of Congress, and other experts made the following five statements in a congressional debate about agricultural price supports. Which of these is a normative statement?

- a. Price supports are important because America should preserve small family farms.
- b. Without price supports, the price of wheat and corn will decrease by over twenty percent.
- c. The decrease in commodity prices caused by the removal of price supports will result in fewer but larger farms
- d. The decrease in commodity prices caused by the removal of price supports will reduce the number of tractors sold in the United States.
- e. The decrease in commodity prices caused by the removal of price supports will decrease the demand for fertilizers in the United States.

ANSWER:

a

91. Bill says, "The imposition of a tax on tequila will increase its price." Bob says, "Taxes should be imposed on tequila because college students drink too much."

- a. Both the statements are normative
- b. Both the statements are positive.
- c. Bill's statement is normative, and Bob's statement is positive.
- d. Bill's statement is positive, and Bob's statement is normative
- e. Bill's statement is an example of the fallacy of composition, and Bob's statement is an example of the *ceteris paribus* assumption.

ANSWER:

d

Essay

92. "Wanting more goods makes us greedy." How would an economist respond to this statement?

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ANSWER: Answers will vary. Economists do not view the unlimited human desire for goods and services to be an indication of "greediness." Economists assume that all individuals want more resources in order to reach greater levels of satisfaction. REJ: Please see the section "Economics: A Brief Introduction" for more information.

93. Can activities like driving above the speed limit or driving without wearing a seat belt be considered rational behavior? Why or why not?

ANSWER: Answers will vary. These activities would be considered rational if the perceived benefits are greater than the perceived costs. The decision to act in a certain way can be rational even if the action turns out to be something that the individual later regrets. REJ: Please see the section "Economic Behavior" for more information.

94. What is the difference between positive and negative incentives?

ANSWER: Answers will vary. Positive incentives either increase benefits or reduce costs and, thus, result in an increased level of the related activity or behavior. Negative incentives either reduce benefits or increase costs, resulting in a decreased level of the related activity or behavior. REJ: Please see the section "Economic Behavior" for more information.

95. How can market failure occur in the market for hybrid automobiles? What can the government do to improve the situation?

ANSWER: Answers will vary. If the market for hybrid automobiles were unregulated, it would produce too few hybrid automobiles because these cars provide benefits to people other than the buyers and the sellers. The government could provide a subsidy or a tax credit to the consumers who purchase hybrid or other fuel efficient automobiles in an effort to promote more purchases and the usage of fuel efficient vehicles. REJ: Please see the section "Markets" for more information.

96. What is the difference between a hypothesis and a theory?

ANSWER: Answers will vary. A hypothesis is the first step in developing and constructing a theory. A hypothesis is testable and makes a prediction about behavior in response to changed circumstances. If a hypothesis is shown to be consistent with real-world data, it can be tentatively accepted as a theory. REJ: Please see the section "Economic Theories and Models" for more information.

97. Why is abstraction important in developing economic theories?

ANSWER: Answers will vary. Economic theories cannot realistically include every event that has ever occurred. A theory weeds out the irrelevant facts from the relevant ones. An economic theory provides a broad view, not a detailed examination, of human economic behavior. REJ: Please see the section "Economic Theories and Models" for more information.

98. Darla is surprised to find that the quality of in-flight service has remained the same despite a steep hike in airfares recently. What could be wrong in her assumption that a higher price naturally translates into better quality?

ANSWER: Answers will vary. The fact that two variables might be related does not necessarily mean that one causes the other to occur. Darla could be ignoring other variables involved in this scenario. The increase in fares might have been caused by other factors such as an increase in aviation fuel prices and may not necessarily guarantee better services. REJ: Please see the section "Pitfalls to Avoid in Scientific Thinking" for more information.

99. "If the price of wine increases, the quantity purchased will increase." Is this a positive or a normative economic statement? Explain your answer.

ANSWER: Answers will vary. As it is a testable proposition, it is a positive economic statement. The statement need not

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be true, only testable, for it to be a positive statement. REJ: Please see the section “Positive and Normative Analysis” for more information.

100. "The government should do all it can to slow the process of global warming." Is this a positive or a normative statement? Explain your answer.

ANSWER: Answers will vary. This is a normative statement. The key is the inclusion of the word "should" in the statement, which indicates a value judgment. REJ: Please see the section “Positive and Normative Analysis” for more information.