Chapter 4. Lessons from Microeconomics

True and False

1. True Prices are determined by the value placed on a product by both sellers and buyers.
2. True High elasticity means the product's demand is less responsive to changes in its price.
3. False The opportunity cost of a resource is the income that could be received from any alternative use of that resource.
4. False Fixed costs are those that vary with the volume of business.
5. True Variable costs are those costs that vary with the volume of business.
6. True Direct costs are those costs that are associated directly with production of a specific product or activity.
7. False The economically optimal level of input use is where the last increment of input use costs more than its benefit.
8. True Substitute one input for another if the cost of the substitute is less than the cost of the input being replaced (and output remains the same).
9. True Vertical expansion involves moving up or down the value chain.
10. True The four main forms of market structure are perfect competition, monopolistic competition, oligopoly, and monopoly.

Multiple Choice

11. The income that could be received from the best alternative use of a resource is its:
    a. Opportunity cost
    b. Fixed cost
    c. Variable cost
    d. Overhead cost

12. A cost that occurs no matter what or how much is produced is:
    a. An opportunity cost
    b. A fixed cost
    c. A variable cost
    d. An overhead cost

13. A cost that varies with the volume of business is:
    a. An opportunity cost
    b. A fixed cost
    c. A variable cost
    d. An overhead cost

14. A cost that is hard to assign directly to a particular enterprise is:
    a. An opportunity cost
    b. A fixed cost
    c. A variable cost
    d. An overhead cost

15. The four main forms of market structure are:
    a. Perfect competition, monopoly, oligarchy, and imperfect markets
    b. Perfect competition, monopolistic competition, oligopoly, and monopoly
    c. Perfect competition, market competition, oligopoly, and money markets
    d. Perfect competition, perfect monopoly, perfect oligarchy, and market

16. Most farms face what main form of market structure?
    a. Perfect competition
    b. Monopolistic competition
    c. An oligopoly
    d. A monopoly

Short Answer and Problems

17. What is an opportunity cost? How is it used?

The opportunity cost of a resource is the income that could be received from the best alternative use of that resource. It is used to decide how resources should be used best. For example, the value of a dairy farmer's labor and management ability may be higher when used in the dairy enterprise compared to raising crops. Thus, the dairy farmer should concentrate on the dairy and either contract with another farmer to grow feed or simply buy feed in the market and rent his or her land out without a contract for feed.

18. What does the term "marginal" mean?

"Marginal" means "additional," "the last unit," or "the result of the last unit." The concept of "marginal" is important because marginal returns and costs are used to choose the optimal level of production and input use. The marginal revenue is the value of the additional production. Marginal cost is the additional cost of obtaining the additional production. It is the cost of the combination of additional fertilizer, pesticides, labor, and any other inputs needed to increase production. The key to using this concept is the word "additional." If the marginal cost (added costs) of the additional inputs is less than the marginal return (added returns) from the additional production, the farmer should add more of the inputs and increase production.

19. What is the difference between fixed and variable costs?

Fixed costs are those costs that occur no matter what or how much is produced. Variable costs are those costs that will vary with the volume of business.