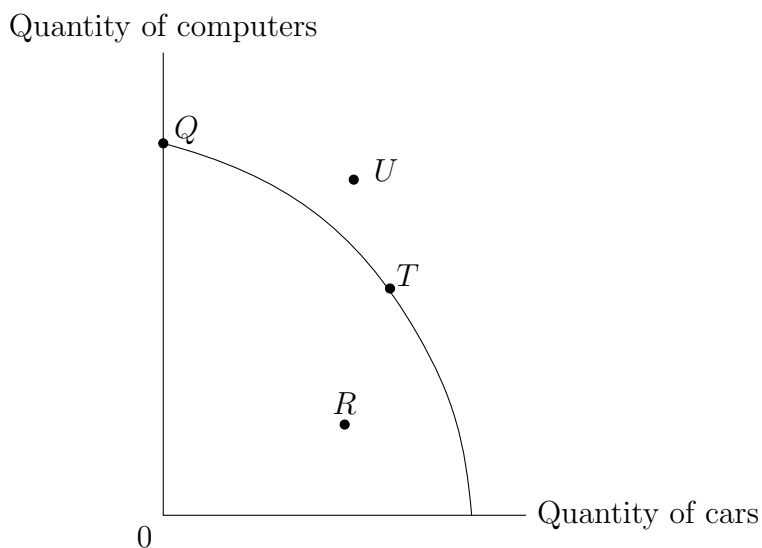


Problem Set 1

Multiple Choice

- (2 points) Normative statements are
 - not usually made by economists.
 - claims about how the world should be.
 - claims about how variables in the economy normally behave.
 - pessimistic interpretations of the economy.
- (2 points) The following graph shows a production possibilities frontier.



This economy has the ability to produce at which point(s)?

- Q, R, T, U
- Q, R, T
- Q, T
- U

3. (2 points) Another term for factors of production is
 - A. inputs.
 - B. outputs.
 - C. goods.
 - D. services
4. (2 points) Rational people make decisions “at the margin” by comparing
 - A. average costs and benefits
 - B. total costs and benefits
 - C. marginal costs and benefits
 - D. opportunity costs and benefits
5. (2 points) Suppose that demand for a good increases and, at the same time, supply of the good decreases. What would happen in the market for the good?
 - A. Equilibrium price would decrease, but the impact on equilibrium quantity would be ambiguous.
 - B. Equilibrium price would increase, but the impact on equilibrium quantity would be ambiguous.
 - C. Equilibrium quantity would decrease, but the impact on equilibrium price would be ambiguous
 - D. Equilibrium quantity would increase, but the impact on equilibrium price would be ambiguous
6. (2 points) In the simple circular-flow diagram, households
 - A. are the only decision makers.
 - B. own the factors of production.
 - C. are buyers of inputs.
 - D. consume only some of the goods and services that firms produce.
7. (2 points) A production possibilities frontier shifts outward when
 - A. the economy experiences economic growth.
 - B. the desire of the economy’s citizens change.
 - C. at least some of the basic principles of economics is violated
 - D. opportunity costs are lessened.
8. (2 points) Suppose the cost of flying a 100-seat plane for an airline is \$50,000 and there are 10 empty seats on a flight. The marginal cost of flying a passenger is
 - A. \$50
 - B. \$500
 - C. \$50,000
 - D. This cannot be determined from the information given

-
9. (2 points) A decrease in the price of a good would
- A. increase the supply of the good
 - B. increase the quantity demanded of the good
 - C. give producers an incentive to produce more to keep profits from falling
 - D. shift the supply curve for the good to the left
10. (2 points) Jake spends an hour studying instead of watching TV with his friends. The opportunity cost to him of studying is
- A. the improvement in his grades from studying for the hour
 - B. the improvement in his grades from studying minus the enjoyment of watching TV
 - C. the enjoyment he would have received if he had watched TV with his friends
 - D. zero. Since Jake chose to study rather than to watch TV, the value of studying must have been greater to him than the value of watching TV.

Short Answer Questions

1. (5 points) Spain and Portugal both produce wine and cheese. Suppose that a Spanish worker can produce 5 bottles of wine in one day or 3 pound of cheese in one day. Suppose that a Portuguese worker can produce 4 bottles of wine per day or 2 pounds of cheese per day.
 - (a) Which country has the absolute advantage in the production of each good? Which country has the comparative advantage?

 - (b) If Spain and Portugal decide to trade, which commodity will Portugal export to Spain? Explain.

-
2. (5 points) Use a production possibilities frontier to illustrate society's trade-off between two goods: wheat and computers. What do you suppose determines the shape and position of the frontier? Show what happens to the frontier if scientists develop a new fertilizer that allows wheat to be grown on otherwise infertile land?
3. (5 points) Universal basic income (UBI) is a policy that guarantees a certain minimum annual income for all citizens. Suppose that you are the President and one of your advisers suggests implementing UBI as a way to eliminate poverty in the United States. Your adviser suggests paying for this policy by raising taxes on the wealthiest Americans.
- (a) How might this policy affect the incentives for working?
- (b) How might this change represent a trade-off between equality and efficiency?