

TEST BANK



Essentials of
Business Statistics
Communicating with Numbers



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Chapter 2

True/False

Indicate whether the statement is true or false.

- 1. An economy is both a social and a financial system.
- 2. Financial or social systems are not essential to the development of a strong economy.
- 3. The study of economics focuses on how people, businesses, and governments choose to allocate resources.
- 4. A key economic goal is to provide a deep understanding of past choices that can be used to guide future business decisions.
- 5. Economists forecast business needs based on a deep understanding of past choices.
- 6. A surprisingly small number of key variables have a significant impact on the performance of the economy.
- 7. The complexity of the economy makes economic forecasting an inexact process.
- 8. Broad economic trends in employment, inflation, and economic growth provide a context that has an important impact on businesses throughout the economy.
- 9. Microeconomics is the study of broad, economy-wide issues such as the unemployment rate, gross domestic product and inflation.
- 10. Macroeconomic conditions impact day-to-day life by influencing variables such as the availability of jobs, the amount of take home pay households have available after paying taxes, and the buying power of those incomes.
- 11. The study of economics falls into two broad categories called meta-economics and econometrics.
- 12. Luke is taking an economics class that focuses on decisions made by individual business firms and consumers. Luke's class is concerned with microeconomic issues.
- 13. Capitalism is based on private ownership, economic freedom, and fair competition.
- 14. Capitalism places paramount importance on the need for the government to intervene in the economy to ensure a fair and equitable distribution of income.
- 15. Market equilibrium is the point at which the supply curve intersects the demand curve.
- 16. Federal law has made all types of monopolies illegal in the United States.
- 17. A typical supply curve shows that an increase in the price of a good will cause producers to decrease the quantity they supply.
- 18. Market equilibrium identifies the price at which quantity supplied is equal to quantity demanded.
- 19. Consumers will see prices fall when the quantity demanded exceeds quantity supplied.
- 20. The price paid for goods and services will rise when the quantity demanded exceeds quantity supplied.

- ___ 21. Everlene's Bakery competes against many other bakeries in the same city. However, each bakery uses different recipes and each claims to offer better products than their rivals. For example, Everlene's advertises that it produces the "World's Best" chocolate chip cookies. This suggests that Everlene's market is an example of pure competition.
- ___ 22. The fundamental rights of capitalism guarantee that businesses will be profitable and taxes will be low, thus providing a strong motivation to start a business.
- ___ 23. In the United States, the government places no restrictions on the right to own property and the freedom to will that property to family members.
- ___ 24. An entrepreneur with limited funds who wants to start a new business would probably be most successful in an oligopolistic market, because the amount of competition in such markets is very limited.
- ___ 25. Government policies promoting free trade are consistent with the right to free choice which is fundamental to capitalism.
- ___ 26. Brooklyn's Beachfront Bed and Breakfast loses money due to a sharp drop in the number of guests during the winter months. If Brooklyn's demand curve is like most demand curves, one way to attract more guests would be to offer lower rates during the off season.
- ___ 27. Morgan's Moped and Bicycle Store is located on the property of a five-star resort in southern Florida. The mopeds and bikes are rented based on one-hour increments. Morgan lowers her standard prices to attract patrons during daily rain storms in June and August. This is an example of decreasing supply.
- ___ 28. In a planned economy the government plays only a minor role in the operation of the economy.
- ___ 29. In capitalism what gets produced is largely determined by central government planning.
- ___ 30. The North Korean and Cuban governments still own most of their nation's enterprises and actively control the performance of their nation's economies.
- ___ 31. Communism is an economic and political system in which a strong central government owns and controls almost all productive enterprises.
- ___ 32. By the end of the 1980's, communism began collapsing across the Soviet Union and its satellite nations.
- ___ 33. The few nations that still rely on a communist economic system have actually seen major improvements in their economic performance over the past decade.
- ___ 34. Karl Marx envisioned communism as a system that would improve the lot of the common worker.
- ___ 35. One problem that plagued many communist economies was that the absence of free markets resulted in crippling shortages and surpluses of goods and services.
- ___ 36. A strength of a pure planned economy is that it is likely to grow rapidly and produce enough products and services to support its people in the long term.
- ___ 37. In the U.S. economy, various branches of government own major enterprises such as the postal service, schools, parks, libraries, universities, and the military.
- ___ 38. The U.S. federal government is the nation's largest employer.
- ___ 39. The federal government creates regulations that prohibit competition and stimulate consumers to work.

- ___ 40. Privatization is the conversion of government-owned enterprises to private ownership.
- ___ 41. Many countries that have restructured to become more market-oriented have seen dramatic increases in the standard of living for most of their people.
- ___ 42. The economic restructuring necessary to move toward greater reliance on markets has proven to be relatively easy for most previously planned economies to achieve.
- ___ 43. While the U.S. relies heavily on free markets, it is actually a mixed economy in which the government owns several major enterprises and regulates many aspects of business operations.
- ___ 44. The two most common types of real world economies are pure capitalism and pure socialism.
- ___ 45. Competition encourages companies to operate efficiently and responsively. The government does its part to stimulate fair competition by creating regulations to protect consumers and workers.
- ___ 46. Privatization is an important element of the movement toward a greater market orientation in many nations.
- ___ 47. Gross domestic product (GDP) includes the value of output produced within a nation even if that output is produced by a foreign-owned company.
- ___ 48. Gross Domestic Product (GDP) measures the total value of all goods and services produced within a nation's physical boundaries over a given period of time.
- ___ 49. GDP tends to overstate the amount of output produced by a nation's economy.
- ___ 50. GDP, as the measurement of the total value of goods and services, includes the output produced within households and output produced by illegal activities.
- ___ 51. The value of a Hyundai Sonata built in Montgomery, Alabama would be included in U.S. GDP even though Hyundai is actually a Korean corporation.
- ___ 52. The unemployment rate includes only individuals over the age of 21 who were involuntarily laid off or fired from their previous jobs.
- ___ 53. The unemployment rate measures individuals 16 years of age and older without jobs who are actively seeking employment.
- ___ 54. Individuals quitting their jobs experience structural unemployment.
- ___ 55. Cyclical unemployment results from layoffs during recessionary periods.
- ___ 56. Frictional unemployment may occur even when the economy is healthy, and may ultimately result in a better match between workers and jobs.
- ___ 57. The predictable nature of the business cycle makes it easy to forecast when the next upturn or downturn in business activity will occur.
- ___ 58. An economy is said to be in a recession when GDP decreases for two consecutive quarters..
- ___ 59. The two key phases of the business cycle are contraction and expansion.
- ___ 60. Contraction is a period of economic downturn marked by rising unemployment, business cutbacks, and decreases in consumer spending.
- ___ 61. Recovery is a period of increasing employment, business expansion, and increased consumer spending.
- ___ 62. Unfortunately, depressions are a common problem in most free-market economies.

- ___ 63. Inflation occurs as the average prices of goods and services rise.
- ___ 64. Less expensive labor pools overseas might create layoffs at a U.S.-based engine plant. This is an example of structural unemployment.
- ___ 65. To measure productivity, multiply the number of inputs by the cost of each input.
- ___ 66. During the peak season, retail workers are hired in great numbers to meet the demands of holiday shoppers. At the end of the holiday season many of those workers are released from their jobs, thus creating seasonal unemployment.
- ___ 67. It is important that any government examine multiple measures of its own economic health, rather than relying on simply one or two dimensions.
- ___ 68. Fiscal policy is the government's effort to influence the economy through taxation and spending decisions to encourage growth and boost employment while curbing inflation.
- ___ 69. The federal government experiences a budget deficit when its revenue from taxes is higher than its expenditures.
- ___ 70. The government experiences a budget surplus when its tax revenue exceeds its expenditures.
- ___ 71. The M1 money supply consists solely of currency (coins and paper money) issued by the government.
- ___ 72. The discount rate is the interest rate the Federal Reserve charges on its loans to commercial banks.
- ___ 73. Constant change is the most predictable economic force in the last few decades.

Multiple Choice

Identify the choice that best completes the statement or answers the question.

- ___ 74. The economy, as a system, represents
 - a. the non-efficient use of material resources.
 - b. the flow of resources from production through consumption.
 - c. the means of production only.
 - d. the means of capitalistic systems.
- ___ 75. In the broadest sense, economics studies the choices that
 - a. people make in disposing of unnecessary resources.
 - b. governments make in creating natural resources.
 - c. companies make in producing goods and services for corporate use.
 - d. people, governments, and companies make in allocating resources.
- ___ 76. From the business perspective, a key reason to study economics is to
 - a. gain a better understanding of past business choices in order to make better future decisions.
 - b. avoid the temptation to focus on past events.
 - c. ensure that demand exceeds supply.
 - d. learn how to achieve a monopoly position in markets with the potential to generate high profits..
- ___ 77. The study of economics is divided into two core categories known as:

- a. production and consumption.
- b. data collection and forecasting.
- c. macroeconomics and microeconomics.
- d. supply economics and demand economics.

___ 78. An economic system is a structure for

- a. measuring gross domestic products.
- b. allocating limited resources.
- c. forecasting trends.
- d. none of the above

___ 79. Macroeconomics focuses on:

- a. the major issues facing the national economy, and has little or no relevance to individuals.
- b. the small individual units operating within the economy.
- c. the major issues facing the national economy, but these issues often impact an individual's well-being.
- d. the role of government, while microeconomics focuses on the private sector.

___ 80. _____ is a structure for allocating scarce resources.

- a. An economic system
- b. An econometric plan
- c. A factor distributor
- d. The gross domestic product

___ 81. Microeconomic analysis would be best suited for:

- a. helping a firm determine the best pricing strategy for its products.
- b. determining the best government tax policies to deal with a high rate of inflation.
- c. explaining the reasons for an increase in the nation's unemployment rate.
- d. measuring the total output produced by a nation's economy.

___ 82. Which of the following would be studied in the greatest detail in a macroeconomics course?

- a. How a large automobile manufacturer decides how many SUVs to produce in a given model year.
- b. How consumers would respond if a restaurant raised its prices.
- c. How a firm in an oligopolistic market would respond to a change in the pricing strategy of other firms in its market.
- d. Factors that influence the nation's unemployment rate.

___ 83. Changes in key industries hold the potential to transform a nation's economy. Which changes would most likely create that effect in the U.S.?

- a. Cure for cancer
- b. New database for accounting
- c. Greater number of college graduates with computer science degrees
- d. Decreased number of individuals on welfare

- ___ 84. GeeGee's is a community-based bakery known for its scrumptious tea cakes. The recipe calls for expensive spices imported from Asia. Recently the cost of these spices has risen dramatically, leading GeeGee's to consider increasing its prices. In order to analyze how this change would affect consumer choices, GG's management could perform a
- a. microeconomic analysis.
 - b. macroeconomic analysis.
 - c. transformational economic analysis.
 - d. structural analysis.
- ___ 85. If low cost solar power were to become a viable energy source in households across the U.S., what would be the economic impact on energy prices?
- a. Energy costs across the country would increase with adoption of the new energy source.
 - b. Housing prices would decrease as new homes are built with this new energy source.
 - c. Prices would increase as this is a new energy source.
 - d. Prices would decrease as competition increases in energy production.
- ___ 86. In capitalism people strive to raise their standard of living. Businesses contribute to this goal by _____.
- a. offering value to the consumer.
 - b. using available resources.
 - c. attracting available talent.
 - d. forming oligopolistic markets.
- ___ 87. A basic characteristic of _____ is that both producers and consumers are free to make their own economic decisions on many basic issues.
- a. socialism
 - b. capitalism
 - c. communism
 - d. mercantilism
- ___ 88. In _____ many firms compete by selling differentiated products.
- a. monopoly
 - b. monopolistic competition
 - c. oligopoly
 - d. natural monopoly
- ___ 89. _____ is a market structure with many competitors selling virtually identical products.
- a. Natural competition
 - b. Pure competition
 - c. Oligopoly
 - d. Monopolistic competition
- ___ 90. Firms in oligopolistic markets tend to
- a. keep prices as low as possible.
 - b. avoid price competition whenever possible.
 - c. be very concerned about the possibility of new firms entering their market.

- d. have very small market shares.
- ___ 91. Which of the following is not a fundamental right of capitalism?
- a. Right to own property
 - b. Right to compete
 - c. Right to keep profits and not pay taxes
 - d. Right to run a business
- ___ 92. Which of the following is not a degree of competition?
- a. Oligopolistic competition
 - b. Monopolistic competition
 - c. Natural competition
 - d. Pure competition
- ___ 93. Companies that attempt to monopolize a particular market are likely to violate the:
- a. Fair Competition Standards Act of 1911
 - b. Taft-Sharpley Free Enterprise Act of 1957
 - c. Sherman Anti-Trust Act of 1890
 - d. Market Competition Enhancement Act of 1978
- ___ 94. Competition among businesses
- a. is consistent with the goals of socialism.
 - b. is a primary feature of a communist economic system.
 - c. ensures that everyone is a winner.
 - d. drives higher quality and lower prices in capitalism.
- ___ 95. According to your textbook, the “Happy Cows” campaign, created by the California Milk Board, has directly increased sales of California cheese by more 1 billion pounds. This benefits
- a. Wisconsin dairy farmers and the consumers of Wisconsin cheeses.
 - b. California dairy farmers and the consumers of California cheeses.
 - c. U. S. cheese producers.
 - d. European cheese producers.
- ___ 96. Prior to 1999, most consumers believed that there was virtually no difference between cheese produced by the thousands of dairy farms in different states. But the “Happy Cows” campaign created by the California Milk Board created a perception that California cheese is better. This successful product differentiation means that the cheese market is no longer:
- a. purely competitive
 - b. monopolistic
 - c. consistent with capitalism.
 - d. oligopolistic
- ___ 97. In 1999, Coca-Cola considered a plan to install thermometers in vending machines that would charge more for cold beverages on particularly hot days. If the demand curve for Coke is like most demand curves, on hot days such a strategy would have:
- a. resulted in a shortage of Coca Cola.
 - b. resulted in a lower quantity of Coke demanded than at the lower price.
 - c. increased the available supply of competing soft drinks.
 - d. had no effect on the amount of Coke consumers would buy.

- ___ 98. If the cost of an ice-cold Coke is more expensive during the summer months, consumers will
- not buy at all.
 - buy no more or less due to the increase in price.
 - buy more due to the increase in price.
 - buy less due to the increase in price.
- ___ 99. In 2005, General Motors introduced a blockbuster promotion by offering customers the employee discount prices for any vehicle. Chrysler and Ford followed the trend and offered the same program. This intense price competition among three major automobile producers resulted in lower profits for all three companies. This outcome illustrates a problem for firms in:
- pure competition.
 - pure monopoly.
 - monopolistic competition.
 - oligopolistic markets.
- ___ 100. The government often allows only one company to provide electricity in a given geographic area because allowing several companies to do so would result in an inefficient duplication of infrastructure. This suggests that electric utilities are
- trust busters.
 - oligopolies.
 - natural monopolies.
 - pure players.
- ___ 101. A market structure with pure competition has all of the following characteristics except:
- the firms use product differentiation allowing consumers to easily identify their favorite brands.
 - there are many firms competing in the market.
 - firms can easily enter and leave the market.
 - no individual firm has any control over the price of the product.
- ___ 102. _____ is the market structure that is most likely to result in higher prices, lower quality and fewer choices for consumers.
- Pure competition
 - Monopolistic competition
 - Oligopoly
 - Monopoly
- ___ 103. During the second half of the 20th century the economies of many European nations became more socialistic, especially when compared to the economy of the United States. This suggests that these European countries had _____ than the United States:
- more government owned enterprises
 - lower taxes
 - a more unequal distribution of income
 - a much faster rate of economic growth
- ___ 104. The main economic goal of the government in a socialist economy is to:
- keep taxes as low as possible.
 - operate key economic enterprises in the best interests of the general public.
 - achieve the highest possible rate of economic growth.

- d. provide the widest array of economic freedoms to its citizens.
- ___ 105. Compared to capitalism, in a socialist system we would expect to find:
- a. a smaller role for the government.
 - b. more emphasis on economic growth and a higher standard of living for the typical household.
 - c. a greater incentive for entrepreneurs to start new businesses.
 - d. more taxpayer subsidized social programs intended to promote a more equal distribution of wealth.
- ___ 106. The ideas of political philosopher Karl Marx are most closely linked to the economic system known as:
- a. communism.
 - b. capitalism.
 - c. socialism.
 - d. mercantilism.
- ___ 107. Communist economies have faced a number of issues that have interfered with their effectiveness. The issues include all of the following EXCEPT
- a. crippling shortages and surpluses.
 - b. abundant natural resources.
 - c. corruption
 - d. suspension of individual rights and choices.
- ___ 108. Government laws against monopolies are
- a. a key way the government promotes competition in a capitalist system.
 - b. inconsistent with the role of government in a capitalist system.
 - c. the main reason the U.S. economy is best classified as a socialist system.
 - d. the main way the government ensures an equal distribution of income in the U.S. economy.
- ___ 109. Abraham Lincoln once stated, "You cannot help the poor by destroying the rich. You cannot lift the wage earner by pulling down the wage payer." This quote is most consistent with the philosophy of a:
- a. socialist economy.
 - b. communist economy.
 - c. planned economy.
 - d. capitalist economy.
- ___ 110. Today the economies of virtually all nations would be classified as:
- a. pure socialism.
 - b. mixed economies.
 - c. pure capitalism.
 - d. pure communism.
- ___ 111. One reason pure market economies are non-existent is because
- a. they are too expensive to maintain.
 - b. they don't adequately provide for the the sick, the elderly, and the environment.
 - c. they result in very high tax rates that undermine incentives.

- d. they don't do enough to encourage entrepreneurship.
- ___ 112. Most business enterprises in the United States are privately owned, but the federal government owns a number of major enterprises (e.g., U.S. Postal Service, U.S. Department of Education, etc.). This suggests that the U.S. economy is best classified as a:
- pure market economy.
 - mixed economy.
 - true command economy.
 - pure planned economy.
- ___ 113. To stimulate competition and protect both consumers and workers, the federal government
- places heavy taxes on firms in monopolistic competition.
 - places limits on international trade in order to stimulate domestic production.
 - creates regulations to intervene in the free market.
 - creates business systems to meet the needs of all consumers.
- ___ 114. In the United States, the federal government:
- consistently runs a budget surplus since it operates most of its enterprises at a profit.
 - has been very reluctant to regulate business behavior.
 - plays only a very minor role in the economy.
 - is the largest employer, providing jobs for nearly three million Americans.
- ___ 115. In recent years, the most common reason for tax reforms in formerly planned economies has been to:
- create a more equal distribution of income.
 - create new incentives for domestic and foreign investment.
 - eliminate the threat of hyperinflation.
 - protect the environment.
- ___ 116. _____ is the process of converting government-owned businesses to private ownership.
- Privatization
 - Globalization
 - Competition
 - Collusion
- ___ 117. The Rainland government enjoys a socialist economic system, but in recent years has found that new business growth has stalled. In an effort to stimulate more growth the government will probably
- create regulations giving consumers and workers more protection.
 - take over most new businesses and operate them as government enterprises.
 - reduce taxes and cut back on some social programs.
 - increase the number of citizens who qualify for free education and healthcare.
- ___ 118. The government of Puritania has begun a program to restructure of the economy, with a goal of moving toward a more market-oriented system. Which of the following is least likely to occur as the result of this restructuring?
- A rise in social unrest as citizens try to adjust to the economic reforms.
 - Privatization of formerly government owned enterprises.
 - Cuts in social programs such as free or low cost healthcare.

- d. Slower rates of economic growth and lower standards of living for the majority of citizens.
- ___ 119. The Shero nation was founded on a capitalistic market system. The newly elected Prime Minister won by campaigning on the platform based on socialist principles. If the Prime Minister of Shero implements her campaign promises, which of the following trends will the citizens of the country be most likely to experience?
- a. A dramatic decrease in government corruption.
 - b. More rapid economic growth for businesses.
 - c. Lower tax rates for all people and an emphasis on free markets.
 - d. Higher taxes for wealthier citizens and more services for the poor and elderly.
- ___ 120. Natasha is very unhappy with conditions in her country. She has very little economic or political freedom. Virtually all productive enterprises are owned by the government, and they seem to be run very inefficiently. The result is frequent shortages and surpluses of goods and services. These conditions suggest that Natasha's country relies on a _____ economic system.
- a. communist
 - b. socialist
 - c. capitalist
 - d. monopolistic
- ___ 121. _____ measures the total value of all goods and services produced within a nation's borders over a given period of time.
- a. The consumer price index
 - b. Gross domestic product
 - c. Net national production
 - d. The production function
- ___ 122. The economic measure that provides the most information about what is happening to prices of consumer goods is the:
- a. GDP.
 - b. Dow Jones Index.
 - c. GNP.
 - d. CPI.
- ___ 123. The four basic types of unemployment are
- a. natural, artificial, voluntary, and induced.
 - b. cyclical, seasonal, structural, and frictional.
 - c. recovery, expansion, contraction, and stagnation.
 - d. micro, macro, industrial, and market-specific.
- ___ 124. Two key phases of the business cycle are
- a. trend and random variation.
 - b. inflation and recession.
 - c. contraction and expansion.
 - d. inflation and deflation.
- ___ 125. In the business cycle, a period in which GDP declines for at least two consecutive quarters is known as a(n):

- a. expansion.
- b. depression.
- c. trough.
- d. recession.

___ 126. In the business cycle, a period of rising economic growth and increasing employment is a

- a. recovery.
- b. peak.
- c. contraction.
- d. disinflation.

___ 127. _____ is a period of robust economic growth and high employment indicating that businesses are capitalizing on new market opportunities.

- a. Expansion
- b. Recovery
- c. Depression
- d. Contraction

___ 128. _____ means that prices on average are rising.

- a. Deflation
- b. Inflation
- c. Disinflation
- d. Hyperinflation

___ 129. To evaluate the impact of inflation, the government uses

- a. inflation and disinflation.
- b. the consumer price index (CPI) and producer price index (PPI).
- c. productivity and unemployment.
- d. monetary policy and fiscal policy.

___ 130. The Consumer Price Index (CPI) measures the

- a. change in the rate of inflation over time.
- b. change in weighted average price over time in a "market basket" of goods and services bought by the typical consumer.
- c. change in prices of a set of goods that represent the minimum acceptable standard of living for the nation's consumers.
- d. percentage of their income consumers must use to pay for goods relative to their average incomes in the same time period.

___ 131. Changes in the PPI can predict changes in the Consumer Price Index (CPI) because

- a. consumers pay what retailers charge.
- b. they are computed using the same market basket.
- c. producers often pass along price increases to consumers.
- d. consumers and producers often buy the same goods.

___ 132. The amount of goods and services produced by an economy divided by the number of resources used to make those goods and services, measures economic

- a. consumer price index.
- b. deflation.

- c. inflation.
 - d. productivity.
- ___ 133. The nation of High Land has seen a steady increase in the output of goods and services produced within its borders in the last year. This would indicate
- a. a rise in High Land's GDP.
 - b. a rise in High Land's CPI.
 - c. a rise in High Land's unemployment rate.
 - d. a decline of the national tax rate.
- ___ 134. A decrease in _____ indicates that it now takes more resources (inputs) to produce a given amount of goods and services (outputs) than in the past.
- a. inflation
 - b. productivity
 - c. structural unemployment
 - d. the business cycle
- ___ 135. Manufacturing jobs have migrated overseas due to increased productivity and low wages of workers in other countries. This contributes to _____ unemployment for American workers in the manufacturing sector.
- a. structural
 - b. frictional
 - c. seasonal
 - d. cyclical
- ___ 136. An economy is experiencing hyperinflation when average prices of goods and services:
- a. rise faster than productivity.
 - b. increase by more than 100% in a year.
 - c. increase more than 50% per month.
 - d. decrease more than 50% per day.
- ___ 137. Denise is a hard worker, but within the last year she and her boss have not seen eye to eye. Angela, her boss, has become more demanding and harder to reach to get clarification on projects. After one too many long working days with little or no job satisfaction, Denise walks into Angela's office and submits her resignation. Denise knows that her resume is strong and feels confident she will find work. Denise is now facing
- a. seasonal unemployment.
 - b. structural unemployment.
 - c. frictional unemployment.
 - d. cyclical unemployment.
- ___ 138. With the tragedy of the 9/11 attacks and the devastation of Hurricane Katrina, workers in both New York City and New Orleans experienced
- a. structural unemployment.
 - b. frictional unemployment.
 - c. cyclical unemployment.
 - d. seasonal unemployment.
- ___ 139. The items included in the CPI's "market basket" are chosen to represent:

- a. goods and services bought by the average consumer.
 - b. goods and services bought by the business sector.
 - c. the cost of government supplied goods and services.
 - d. all goods and services produced by domestic businesses.
- ___ 140. Pampered Pooch is a dog groomer in the area looking to increase productivity for the business. Currently, in an eight hour day, Pampered Pooch can wash and groom 12 large dogs. To calculate productivity the management of Pampered Pooch would
- a. divide the number of dogs groomed per day (12) by the amount of labor per day (8 hours).
 - b. divide the total weight of the dogs by 12, then multiply the results by the number of hours of labor per day (8 hours).
 - c. divide 8 hours by 12 dogs per day.
 - d. divide 12 dogs by a 7 day work week and multiply the result by 8.
- ___ 141. Martha has noticed that the CPI has increased by 7% over the past year. The best conclusion for Martha to make based on this information is that
- a. her cost of living has increased by 7%.
 - b. her income has increased by 7%.
 - c. the weighted average of prices of goods and services in a market basket bought by a typical consumer have increased by 7%.
 - d. the price of necessities such as food, rent, and medicine have increased by an average of 7%.
- ___ 142. _____ refers to government efforts to influence the economy through taxation and spending decisions designed to encourage growth, boost employment, and curb inflation.
- a. Monetary policy
 - b. Fiscal policy
 - c. Pricing policy
 - d. Production policy
- ___ 143. When tax revenue is higher than government expenditures, the government incurs a
- a. budget deficit.
 - b. windfall.
 - c. budget surplus.
 - d. national debt.
- ___ 144. The federal government runs a budget deficit when its
- a. spending outpaces revenue from taxes.
 - b. tax revenue outpaces its expenditures.
 - c. monetary policies reduce the amount of money in circulation.
 - d. gold reserves are inadequate to support the existing money supply.
- ___ 145. _____ refers to actions that shape the economy by influencing interest rates and the supply of money.
- a. Fiscal policy
 - b. Monetary policy
 - c. Revenue policy
 - d. Deficit policy

- ___ 146. The Federal Reserve is primarily responsible for conducting:
- fiscal policy.
 - treasury policy.
 - tax policy.
 - monetary policy.
- ___ 147. The M2 money supply includes
- all currency, credit cards, and most savings accounts.
 - all currency, most savings accounts, money market accounts, and certificates of deposit.
 - only currency and short term money market accounts.
 - all currency.
- ___ 148. In the U.S., the control of the money supply is the responsibility of
- the U.S. Department of the Treasury.
 - the Federal Reserve.
 - the U.S. Department of State.
 - the U.S. Congress.
- ___ 149. Banks help increase the money supply by
- printing more money.
 - extending loans to credit-worthy consumers.
 - holding more money in their accounts with the Federal Reserve.
 - sending more money to the Treasury Department.
- ___ 150. The primary way the Fed controls the supply of money is by:
- establishing the amount of currency the U.S. Treasury is allowed to print each month.
 - changing the reserve requirement.
 - buying and selling government securities on the open market.
 - allowing banks to borrow more money from the U.S. Treasury.
- ___ 151. If the Fed wants to increase the money supply it should:
- raise the reserve requirement.
 - raise the discount rate.
 - cut taxes.
 - buy government securities.
- ___ 152. Members of the U.S. Congress have voted themselves an annual pay raise while the country is operating under a budget deficit. The pay raise for all members of Congress will generate
- an increase in the federal debt.
 - a decrease in social programs.
 - an increase in the reserve requirement.
 - a decrease in the interest rate.
- ___ 153. In an effort to instill public confidence in the banking system after the 1929 stock market crash, Congress established the _____ to protect deposits in banks and thrift institutions for up to \$100,000 per customer, per bank.

- a. Federal Deposit Insurance Corporation (FDIC)
- b. Federal Reserve System
- c. Federal Open Market Committee
- d. Federal Reserve Requirement

_____ 154. Michael has inherited \$500,000 from the sale of a family business. His banker is advising he find multiple banks to deposit his money. Why?

- a. The Open Market Operations of the Federal Reserve would invest his money in other securities and might lose it without needing to justify the expenditure.
- b. The Federal Reserve does not keep that much money in any one bank due to federal regulations prohibiting the buying and selling of securities.
- c. The Federal Deposit Insurance Corporation will only insure up to \$100,000 in each account per customer, per bank. He would need more than one bank to ensure his money is federally protected in the event of an economic collapse of the banking system.
- d. He needs to diversify his holdings in more than one bank to protect himself against fraudulent lending practices of banks.

_____ 155. Early in his first term, President George W. Bush faced an economy in the beginnings of a recession. Which of the following would represent an example of a fiscal policy President Bush might suggest to deal with this situation?

- a. Ask Congress to cut total spending on social programs to avoid running a budget deficit.
- b. Ask Congress to cut taxes in order to give consumers and businesses more income to spend and invest.
- c. Order the Fed to raise the required reserve ratio.
- d. Urge Congress to give the U.S. Treasury the authority to print more money.

Essay

- 156. Explain how macroeconomics differs from microeconomics. Illustrate these differences by identifying some specific topics these two branches would examine.
- 157. Define transformational economic trends and describe the impact they have on today's domestic and international businesses.
- 158. What are the fundamental rights of capitalism? Include an example of each to support your answer.
- 159. Define the four degrees of competition. Include at least one example for each.
- 160. What is supply? How can the supply relationship be illustrated? What is demand? How can this relationship be illustrated? How can supply and demand be used to determine the market price of a good?.
- 161. What is a business cycle? Describe the basic phases of a typical business cycle.
- 162. Define the differences and similarities between the command economies of socialism and communism.
- 163. What is gross domestic product? How well does it measure what it is intended to measure?
- 164. Explain the reason for the current trend toward a mixed market system. Include in your answer examples of this trend.

165. What is unemployment? Identify and describe the four types and each one's effect on the economy.
166. Compare and contrast the Consumer Price Index (CPI) and Producer Price Index (PPI) as measures of price changes in the economy.
167. Explain the difference between monetary and fiscal policy and explain how they are formulated.
168. Explain how the Fed can use the reserve requirement to influence interest rates and the availability of loans. Why is the Fed reluctant to make frequent changes in the reserve requirement?
169. Identify and explain the three key tools the Federal Reserve uses to expand and contract the money supply.

Chapter 2 Answer Section

TRUE/FALSE

1. ANS: T OBJ: 1	PTS: 0	DIF: LL1	REF: Page 15
2. ANS: F OBJ: 1	PTS: 1	DIF: LL1	REF: Page 15
3. ANS: T OBJ: 1	PTS: 1	DIF: LL1	REF: Page 15
4. ANS: T OBJ: 1	PTS: 1	DIF: LL1	REF: Page 15
5. ANS: T OBJ: 1	PTS: 1	DIF: LL1	REF: Page 15
6. ANS: F OBJ: 1	PTS: 1	DIF: LL1	REF: Page 15
7. ANS: T OBJ: 1	PTS: 1	DIF: LL1	REF: Page 15
8. ANS: T OBJ: 1	PTS: 1	DIF: LL2	REF: Page 15
9. ANS: F OBJ: 1	PTS: 1	DIF: LL2	REF: Page 15
10. ANS: T OBJ: 1	PTS: 1	DIF: LL2	REF: Page 15
11. ANS: F OBJ: 1	PTS: 1	DIF: LL2	REF: Page 15
12. ANS: T OBJ: 1	PTS: 1	DIF: LL2	REF: Page 15
13. ANS: T OBJ: 2	PTS: 1	DIF: LL2	REF: Page 16
14. ANS: F OBJ: 2	PTS: 1	DIF: LL2	REF: Page 16
15. ANS: T OBJ: 2	PTS: 1	DIF: LL2	REF: Page 20
16. ANS: F OBJ: 2	PTS: 1	DIF: LL2	REF: Page 19
17. ANS: F OBJ: 2	PTS: 1	DIF: LL2	REF: Page 20
18. ANS: T OBJ: 2	PTS: 1	DIF: LL2	REF: Page 20
19. ANS: F OBJ: 2	PTS: 1	DIF: LL2	REF: Page 20
20. ANS: T OBJ: 2	PTS: 1	DIF: LL2	REF: Page 20
21. ANS: F OBJ: 2	PTS: 1	DIF: LL2	REF: Page 18
22. ANS: F	PTS: 1	DIF: LL2	REF: Page 17

23.	ANS: F OBJ: 2	PTS: 1	DIF: LL2	REF: Page 17
24.	ANS: F OBJ: 2	PTS: 1	DIF: LL2	REF: Page 19
25.	ANS: T OBJ: 2	PTS: 1	DIF: LL2	REF: Page 18
26.	ANS: T OBJ: 2	PTS: 1	DIF: LL3	REF: Page 20
27.	ANS: F OBJ: 2	PTS: 1	DIF: LL3	REF: Page 20
28.	ANS: F OBJ: 3	PTS: 1	DIF: LL1	REF: Page 20-21
29.	ANS: F OBJ: 3	PTS: 1	DIF: LL2	REF: Page 20
30.	ANS: T OBJ: 3	PTS: 1	DIF: LL2	REF: Page 22
31.	ANS: T OBJ: 3	PTS: 1	DIF: LL2	REF: Page 22
32.	ANS: T OBJ: 3	PTS: 1	DIF: LL2	REF: Page 22
33.	ANS: F OBJ: 3	PTS: 1	DIF: LL2	REF: Page 22
34.	ANS: T OBJ: 3	PTS: 1	DIF: LL2	REF: Page 22
35.	ANS: T OBJ: 3	PTS: 1	DIF: LL2	REF: Page 22
36.	ANS: F OBJ: 4	PTS: 0	DIF: LL 1	REF: Page 22
37.	ANS: T OBJ: 4	PTS: 0	DIF: LL 1	REF: Page 22
38.	ANS: T OBJ: 4	PTS: 0	DIF: LL 1	REF: Page 22
39.	ANS: F OBJ: 4	PTS: 1	DIF: LL 1	REF: Page 22
40.	ANS: T OBJ: 4	PTS: 1	DIF: LL 1	REF: Page 22
41.	ANS: T OBJ: 4	PTS: 1	DIF: LL 1	REF: Page 22
42.	ANS: F OBJ: 4	PTS: 1	DIF: LL 1	REF: Page 22
43.	ANS: T OBJ: 4	PTS: 1	DIF: LL 2	REF: Page 22
44.	ANS: F OBJ: 4	PTS: 1	DIF: LL 2	REF: Page 22
45.	ANS: T OBJ: 4	PTS: 1	DIF: LL 2	REF: Page 22
46.	ANS: T	PTS: 1	DIF: LL 2	REF: Page 22

47.	OBJ: 4 ANS: T OBJ: 5	PTS: 1	DIF: LL 2	REF: Page 22
48.	ANS: T OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 22
49.	ANS: F OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 23
50.	ANS: F OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 22
51.	ANS: T OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 22
52.	ANS: F OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 23
53.	ANS: T OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 23
54.	ANS: F OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 23
55.	ANS: T OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 23
56.	ANS: T OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 23
57.	ANS: F OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 23
58.	ANS: T OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 24
59.	ANS: T OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 23
60.	ANS: T OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 24
61.	ANS: T OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 24
62.	ANS: F OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 24
63.	ANS: T OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 24
64.	ANS: T OBJ: 5	PTS: 1	DIF: LL 2	REF: Page 23
65.	ANS: F OBJ: 5	PTS: 1	DIF: LL 2	REF: Page 25
66.	ANS: T OBJ: 5	PTS: 1	DIF: LL 2	REF: Page 23
67.	ANS: T OBJ: 5	PTS: 1	DIF: LL 2	REF: Page 22
68.	ANS: T OBJ: 6	PTS: 1	DIF: LL 1	REF: Page 26
69.	ANS: F OBJ: 6	PTS: 1	DIF: LL 1	REF: Page 26
70.	ANS: T	PTS: 1	DIF: LL 1	REF: Page 26

71.	ANS: F OBJ: 6	PTS: 1	DIF: LL 1	REF: Page 27
72.	ANS: T OBJ: 6	PTS: 1	DIF: LL 1	REF: Page 28
73.	ANS: T OBJ: 1	PTS: 1	DIF: LL 1	REF: Page 15

MULTIPLE CHOICE

74.	ANS: B OBJ: 1	PTS: 1	DIF: LL1	REF: Page 15
75.	ANS: D OBJ: 1	PTS: 0	DIF: LL1	REF: Page 15
76.	ANS: A OBJ: 1	PTS: 1	DIF: LL1	REF: Page 15
77.	ANS: C OBJ: 1	PTS: 1	DIF: LL1	REF: Page 15
78.	ANS: B OBJ: 1	PTS: 1	DIF: LL1	REF: Page 15
79.	ANS: C OBJ: 1	PTS: 1	DIF: LL2	REF: Page 15
80.	ANS: A OBJ: 1	PTS: 1	DIF: LL1	REF: Page 16
81.	ANS: A OBJ: 1	PTS: 1	DIF: LL2	REF: Page 15
82.	ANS: D OBJ: 1	PTS: 1	DIF: LL2	REF: Page 15
83.	ANS: A OBJ: 1	PTS: 1	DIF: LL2	REF: Page 16
84.	ANS: A OBJ: 1	PTS: 1	DIF: LL3	REF: Page 15
85.	ANS: D OBJ: 1	PTS: 1	DIF: LL3	REF: Page 16
86.	ANS: A OBJ: 2	PTS: 1	DIF: LL1	REF: Page 17
87.	ANS: B OBJ: 2	PTS: 1	DIF: LL1	REF: Page 17
88.	ANS: B OBJ: 2	PTS: 1	DIF: LL1	REF: Page 18
89.	ANS: B OBJ: 2	PTS: 1	DIF: LL1	REF: Page 18
90.	ANS: B OBJ: 2	PTS: 1	DIF: LL2	REF: Page 19
91.	ANS: C OBJ: 2	PTS: 1	DIF: LL2	REF: Page 17-18
92.	ANS: C OBJ: 2	PTS: 1	DIF: LL2	REF: Page 18-19

93.	ANS: C OBJ: 2	PTS: 1	DIF: LL2	REF: Page 19
94.	ANS: D OBJ: 2	PTS: 1	DIF: LL2	REF: Page 18
95.	ANS: B OBJ: 2	PTS: 1	DIF: LL2	REF: Page 19
96.	ANS: A OBJ: 2	PTS: 1	DIF: LL2	REF: Page 19
97.	ANS: B OBJ: 2	PTS: 1	DIF: LL2	REF: Page 21
98.	ANS: D OBJ: 2	PTS: 1	DIF: LL2	REF: Page 21
99.	ANS: D OBJ: 2	PTS: 1	DIF: LL3	REF: Page 19
100.	ANS: C OBJ: 2	PTS: 1	DIF: LL3	REF: Page 19
101.	ANS: A OBJ: 2	PTS: 1	DIF: LL3	REF: Page 18
102.	ANS: D OBJ: 2	PTS: 1	DIF: LL3	REF: Page 19
103.	ANS: A OBJ: 3	PTS: 1	DIF: LL1	REF: Page 21
104.	ANS: B OBJ: 3	PTS: 1	DIF: LL1	REF: Page 21
105.	ANS: D OBJ: 3	PTS: 1	DIF: LL1	REF: Page 21
106.	ANS: A OBJ: 3	PTS: 1	DIF: LL2	REF: Page 22
107.	ANS: B OBJ: 3	PTS: 1	DIF: LL2	REF: Page 22
108.	ANS: A OBJ: 2	PTS: 1	DIF: LL2	REF: Page 19
109.	ANS: D OBJ: 2	PTS: 1	DIF: LL3	REF: Page 16-17
110.	ANS: B OBJ: 4	PTS: 1	DIF: LL 1	REF: Page 22
111.	ANS: B OBJ: 4	PTS: 1	DIF: LL 1	REF: Page 22
112.	ANS: B OBJ: 4	PTS: 1	DIF: LL 1	REF: Page 22
113.	ANS: C OBJ: 4	PTS: 1	DIF: LL 1	REF: Page 22
114.	ANS: D OBJ: 4	PTS: 1	DIF: LL 1	REF: Page 22
115.	ANS: B OBJ: 4	PTS: 1	DIF: LL 1	REF: Page 22
116.	ANS: A OBJ: 4	PTS: 1	DIF: LL 1	REF: Page 22

117.	ANS: C OBJ: 4	PTS: 1	DIF: LL 2	REF: Page 22
118.	ANS: D OBJ: 4	PTS: 1	DIF: LL 2	REF: Page 22
119.	ANS: D OBJ: 4	PTS: 1	DIF: LL 3	REF: Page 22
120.	ANS: A OBJ: 3	PTS: 1	DIF: LL 3	REF: Page 22
121.	ANS: B OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 22
122.	ANS: D OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 25
123.	ANS: B OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 23
124.	ANS: C OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 24
125.	ANS: D OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 24
126.	ANS: A OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 24
127.	ANS: A OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 24
128.	ANS: B OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 24
129.	ANS: B OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 25
130.	ANS: B OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 25
131.	ANS: C OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 25
132.	ANS: D OBJ: 5	PTS: 1	DIF: LL 1	REF: Page 25
133.	ANS: A OBJ: 5	PTS: 1	DIF: LL 2	REF: Page 22
134.	ANS: B OBJ: 5	PTS: 1	DIF: LL 2	REF: Page 25
135.	ANS: A OBJ: 5	PTS: 1	DIF: LL2	REF: Page 23
136.	ANS: C OBJ: 5	PTS: 1	DIF: LL 2	REF: Page 24
137.	ANS: C OBJ: 5	PTS: 1	DIF: LL 2	REF: Page 23
138.	ANS: A OBJ: 5	PTS: 1	DIF: LL 3	REF: Page 23
139.	ANS: A OBJ: 5	PTS: 1	DIF: LL 3	REF: Page 25
140.	ANS: A OBJ: 5	PTS: 1	DIF: LL 3	REF: Page 25

141.	ANS: C OBJ: 5	PTS: 1	DIF: LL 3	REF: Page 25
142.	ANS: B OBJ: 6	PTS: 1	DIF: LL 1	REF: Page 26
143.	ANS: C OBJ: 6	PTS: 1	DIF: LL 1	REF: Page 26
144.	ANS: A OBJ: 6	PTS: 1	DIF: LL 1	REF: Page 26
145.	ANS: B OBJ: 6	PTS: 1	DIF: LL1	REF: Page 26
146.	ANS: D OBJ: 6	PTS: 1	DIF: LL 1	REF: Page 26
147.	ANS: B OBJ: 6	PTS: 1	DIF: LL 1	REF: Page 27
148.	ANS: B OBJ: 6	PTS: 1	DIF: LL 1	REF: Page 26-27
149.	ANS: B OBJ: 6	PTS: 1	DIF: LL2	REF: Page 27
150.	ANS: C OBJ: 6	PTS: 1	DIF: LL2	REF: Page 28
151.	ANS: D OBJ: 6	PTS: 1	DIF: LL 2	REF: Page 27
152.	ANS: A OBJ: 6	PTS: 1	DIF: LL 2	REF: Page 26
153.	ANS: A OBJ: 6	PTS: 1	DIF: LL 2	REF: Page 27
154.	ANS: C OBJ: 6	PTS: 1	DIF: LL 3	REF: Page 27
155.	ANS: B OBJ: 6	PTS: 1	DIF: LL 3	REF: Page 26

ESSAY

156. ANS:

Macroeconomics is the study of a country's overall economic issues, such as the employment rate, the gross domestic product, and taxation policies. While macroeconomic issues may seem abstract, they directly impact your day-to-day life, influencing key variables such as what jobs will be available for you, how much cash you'll actually take home after taxes, or how much you can buy with that cash in any given month.

Microeconomics focuses on smaller economic units such as individual consumers, families, and individual businesses. Thus, microeconomics would look at how individual firms decide how much output to produce, what prices to charge, and how much labor to hire. It would also look at how consumers decide which products to buy, and why the wage rates of some workers are higher than the wages earned by other workers.

On a broader scale, the constant, changing interplay between micro and macroeconomic factors—individual behavior and broad trends—determines the shape of the entire economy.

159. ANS:

Pure Competition: A market structure with many competitors selling virtually identical products. In today's U.S. economy, examples of pure competition have virtually disappeared. Examples might include agricultural products.

Monopolistic Competition: A market structure with many competitors selling differentiated products. Producers have some control over the price of their wares depending on the value that they offer their customers. And new producers can fairly easily enter categories marked by monopolistic competition. Examples might include colleges and fast food establishments.

Oligopoly: A market structure with only a handful of competitors selling products that are either similar or different. The retail gasoline business and the car manufacturing industry, for instance, are both oligopolies. Other examples might include breakfast cereals and soft drinks.

Monopoly: A market structure with just a single producer completely dominating the industry, leaving no room for any significant competitors. Monopolies usually aren't good for anyone but the company that has control, since without competition there isn't any incentive to hold down prices or increase quality and choices. Because of these undesirable drawbacks, most attempts to monopolize markets in the United States are illegal. However, the government does allow monopolies to operate in certain special cases. The classic example is a natural monopoly, such as a cable television system, water company, or electric utility. (The pricing and output decisions of such natural monopolies are often regulated by the government to protect the public interest.) The government also fosters temporary monopolies when it grants patents or copyrights.

NOTE: Student answers should include a specific definition, however the examples will vary based on the text and classroom discussions.

PTS: 1

DIF: LL3

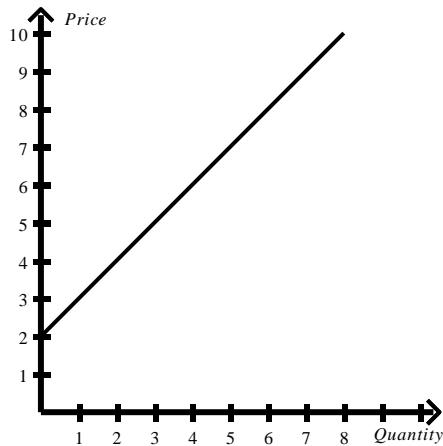
REF: Page 18-19

OBJ: 2

160. ANS:

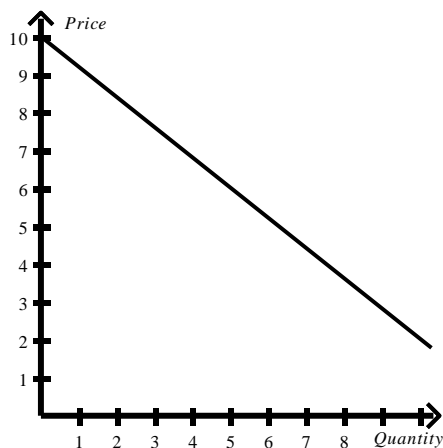
Supply: Supply refers to the quantity of products that producers are willing to offer for sale at different market prices. Because businesses seek to make as much profit as possible, they are likely to produce more of a product that commands a higher market price, and less of a product that commands a lower price.

The relationship between price and quantity from a supplier standpoint can be shown on a graph called the **supply curve**. The supply curve maps quantity on the x-axis (or horizontal axis) and price on the y-axis (or vertical axis). An example of a supply curve is shown below:

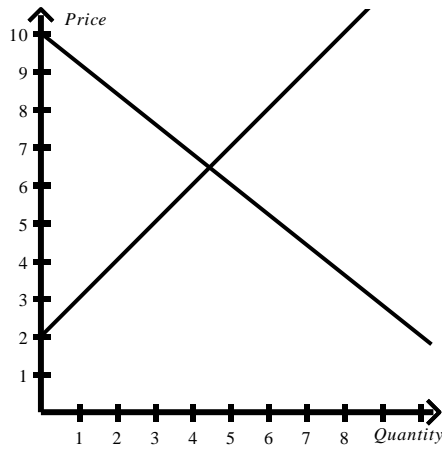


Demand: Demand refers to the quantity of products that consumers are willing to buy at different market prices. Since consumers generally seek to get the products they need (or want) at the lowest possible prices, they tend to buy more of products with lower prices and less of products with higher prices.

The relationship between price and quantity from a demand standpoint can be shown on a graph called the **demand curve**. Like the supply curve, the demand curve maps quantity on the x-axis and price on the y-axis. But different from the supply curve, the demand curves for most goods and services slopes down as it moves to the right, since quantity demanded tends to drop as prices rise. An example of a demand curve is show below:



The concepts of supply and demand can be combined to locate market equilibrium. The equilibrium price is the price at which the quantity supplied is equal to the quantity demanded--which can be found by graphing the supply and demand curves and finding the point where they intersect. The market price moves toward its equilibrium value and tends to stabilize at that value (unless something disturbs the supply or demand curve). If we combine the above supply and demand curves, we can see that the equilibrium price in this market is approximately \$6.45.



PTS: 1 DIF: LL3 REF: Page 20 OBJ: 2

161. ANS:

The business cycle is the periodic expansion and contraction of economic activity that occurs in a nation's economy over a period of years. The two key phases of a business cycle are contraction, when output (GDP), income, and employment are falling, and expansion when production, incomes and employment are rising. The bottom of a contraction is called a trough, while the high point of an expansion is called a peak. If a contraction results in a decline in GDP for at least two consecutive quarters the downturn is classified as a recession. A depression is an extremely severe and long-lasting recession. Depressions are rare; the last full-blown depression in the United States occurred in the 1930s.

PTS: 1 DIF: LL5 REF: Page 23 OBJ: 2

162. ANS:

Socialism is an economic system based on the principle that the government should own and operate key enterprises that directly affect public welfare, such as utilities, telecommunications, and healthcare. While the official government goal is to run these enterprises in the best interest of the overall public, inefficiencies and corruption often interfere with effectiveness. Socialist economies also tend to have higher taxes, which are designed to distribute wealth more evenly through society.

Communism is an economic and political system that calls for public ownership of virtually all enterprises, under the direction of a strong central government. The communist concept was the brainchild of political philosopher Karl Marx, who outlined its core principles in his 1848 *Communist Manifesto*. Marx's approach was idealistic. He aimed to create a fair society in which each individual would contribute according to his or her ability and consume according to his or her needs. The communism that Marx envisioned was supposed to dramatically improve the lot of the worker at the expense of the extremely wealthy "capitalists" who owned the factories and other means of production.

PTS: 1 DIF: LL3 REF: Page 21 OBJ: 3

163. ANS:

Gross domestic product (GDP) is a measure of the total value of goods and services produced within a nation in a given time period. Conceptually, all goods produced within a nation's borders should be included in its GDP, even if the firm producing the output is a foreign owned corporation. Thus, Hondas produced in the United States are included in U.S. GDP even though Honda is a Japanese firm. But Mattel toys produced in China are not included in U.S. GDP even though Mattel is considered to be a U.S. corporation.

GDP tends to understate a nation's total production because it does not include output produced illegally, nor does it include the value of output that is not reported because the producer is trying to avoid paying taxes. Another major omission is the work done within households. When households cook their own meals, mow their own lawns, or do their own household repairs, the value of their labor is not included in GDP. But if they hire others to do these tasks, the value of these goods and services is included in GDP (assuming of course that the people performing these services report their incomes).

PTS: 1 DIF: LL3 REF: Page 22 OBJ: 5

164. ANS:

Virtually all nations have mixed economies, falling somewhere along a spectrum that ranges from pure planned at one extreme to pure market at the other. Over the past thirty years, most major economies around the world have moved toward the market end of the spectrum.

Government-owned businesses have converted to private ownership. Socialist governments have reduced red tape, cracked down on corruption, and established new laws to protect economic rights. Lavish human services have shrunk. And tax reform has created new incentives for investment.

Examples will vary among students. Students should mention the social aspect of market economies with the government running the postal service, road maintenance, and education. The government stimulates economic growth with regulations that protect consumers and workers as well (Federal Product Safety Commission standards, Food & Drug Administration guidelines, etc.)

PTS: 0 DIF: LL 3 REF: Page 22 OBJ: 4

165. ANS:

The United States Department of Labor tracks employment levels largely through the **unemployment rate**, which includes everyone age 16 and older who doesn't have a job and is actively seeking one.

Frictional unemployment involves a worker quitting or being terminated and has a short term impact on the economy as the worker is able to find new employment within a relatively short amount of time.

Structural unemployment, on the other hand, is usually longer term. This category encompasses people who don't have jobs because the economy no longer needs their skills. In the U.S. growing numbers of workers in the past decade have found themselves victims of structural unemployment as manufacturing jobs have moved overseas. Often their only option is expensive retraining.

Two other categories of unemployment are **cyclical**, which involves layoffs during recessions, and **seasonal**, which involves job loss related to the time of year. An example of seasonal unemployment is the loss of jobs by landscapers during cold winter months.

PTS: 0 DIF: LL 3 REF: Page 23 OBJ: 5

166. ANS:

The government uses two major price indexes to evaluate inflation: the **Consumer Price Index (CPI)**, and the **Producer Price Index (PPI)**.

The CPI measures the change in weighted average price over time in a consumer “market basket” of goods and services that the average person buys each month. The U.S. Bureau of Labor Statistics creates the basket—which includes hundreds of items such as housing, transportation, haircuts, wine, and pet care—using data from more than 30,000 consumers. While the market basket is meant to represent the average consumer, keep in mind that the “average” includes a lot of variation, so the CPI may not reflect individual personal experience. If you don’t have a pet, for example, changes in veterinary costs wouldn’t affect you, although they would (slightly) impact the CPI.

The PPI measures the change over time in weighted average wholesale prices, or the prices that businesses pay each other for goods and services. Changes in the PPI can sometimes predict changes in the CPI, because producers tend to pass on price increases (and sometimes also price decreases) to consumers within a month or two of the changes.

PTS: 0 DIF: LL 3 REF: Page 25 OBJ: 5

167. ANS:

Fiscal policy refers to government efforts to influence the economy through taxation and spending decisions that are designed to encourage growth, boost employment, and curb inflation. This type of policy is enacted by Congress through the budget process.

Monetary policy refers to actions that shape the economy by influencing interest rates and the supply of money. The Federal Reserve System, better known as the Fed, manages U.S. monetary policy. It does so by controlling the amount of reserves banks have available for making loans. The most important tool for this purpose is open market operations, which consist of the Fed’s purchase and sale of government securities.

PTS: 0 DIF: LL 3 REF: Page 26 OBJ: 6

168. ANS:

The Fed requires that all of its member banks hold funds, called reserves, equal to a stated percentage of the deposits held by their customers. This percentage is called the reserve requirement (or required reserve ratio). The reserve requirement helps protect depositors, who may want to withdraw their money without notice.

Currently, the reserve requirement stands at about 10%, depending on the size and type of a bank’s deposits. If the **Fed increases the reserve requirement**, banks must hold more funds, meaning they will have fewer funds available to make loans. This **makes credit tighter and causes interest rates to rise**.

If the **Fed decreases the reserve requirement**, some of the funds that banks were required to hold become available for loans. This **increases the availability of credit and causes interest rates to drop**. Since changes in the reserve requirement can have a dramatic impact on both the economy and the financial health of individual banks, the Fed uses this tool quite infrequently.

PTS: 0 DIF: LL 3 REF: Page 28 OBJ: 6

169. ANS:

The Fed uses three key tools expand and contract the money supply:

- Open market operations
- Discount rate changes
- Reserve requirement changes

Open Market Operations: This is the Fed's most frequently used tool. Open market operations involve buying and selling government securities, which include treasury bonds, notes, and bills. These securities are the IOUs the government issues to finance its deficit spending.

When the economy is weak, the Fed *buys* government securities on the open market. When the Fed pays the sellers of these securities, money previously held by the Fed is put into circulation. This directly stimulates spending. In addition, any of the additional funds supplied by the Fed that are deposited in banks will allow banks to make more loans, making credit more readily available. This encourages even more spending and further stimulates the economy.

When inflation is a concern, the Fed *sells* securities. Buyers of the securities write checks to the Fed to pay for securities they bought, and the Fed withdraws these funds from banks. With fewer funds, banks must cut back on the loans they make, credit becomes tighter and the money supply shrinks. This reduces spending and cools off the inflationary pressures in the economy.

Discount Rate Changes: The discount rate is the interest rate the Fed charges on its loans to commercial banks. When the Fed reduces the discount rate, banks can obtain funds at a lower cost and use these funds to make more loans to their own customers. With the cost of acquiring funds from the Fed lower, interest rates on bank loans also tend to fall. The result: businesses and individuals are more likely to borrow money and spend it, which stimulates the economy.

Reserve Requirement Changes: The Fed requires that all of its member banks hold funds, called reserves, equal to a stated percentage of the deposits held by their customers. This percentage is called the reserve requirement (or required reserve ratio). The reserve requirement helps protect depositors, who may want to withdraw their money without notice.

If the Fed increases the reserve requirement, banks must hold more funds, meaning they will have fewer funds available to make loans. This makes credit tighter and causes interest rates to rise. If the Fed decreases the reserve requirement, some of the funds that banks were required to hold become available for loans. This increases the availability of credit and causes interest rates to drop.

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