Problem Set # 1–Due September 8

1. Which of the following best describes the disagreements among economists?
   a. Economists usually agree on positive, but not normative, economic issues.
   b. Economists usually agree on negative, but not normative, economic issues.
   c. Economists do not agree on the positive or the normative economic issues.
   d. Economists agree on the positive and the normative economic issues.

2. Which of the following illustrates the fallacy of composition?
   a. A occurred before B. Thus, A caused B.
   b. A and B are positively correlated. Thus, A caused B.
   c. If everyone expects inflation, there will be an inflation.
   d. If I increase my demand for beer, the price of beer will not rise. Therefore, if everyone buys more beer, the price of beer will not change.

3. Which of the following best illustrates a self-fulfilling prophecy?
   a. A occurred before B. Thus, A caused B.
   b. A and B are positively correlated. Thus, A caused B.
   c. If everyone expects inflation, there will be an inflation.
   d. If I increase my demand for beer, the price of beer will not rise. Therefore, if everyone buys more beer, the price of beer will not change.

4. Economic theories are:
   a. questionable since they abstract from reality.
   b. unreliable since they make many simplifications.
   c. generalizations concerning the workings of an economy.
   d. accurate representations concerning workings of the economy.

5. Where there are two variables and an increase in one variable causes an increase in the second variable, the relationship is shown graphically by a line that is:
   a. positively sloped
   b. negatively sloped
   c. positively then negatively sloped
   d. negatively then positively sloped

Answer questions 6 - 8 based on the following demand and supply schedules for grain.

<table>
<thead>
<tr>
<th>Price</th>
<th>Quantity Demanded</th>
<th>Quantity Supplied</th>
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<tbody>
<tr>
<td>1</td>
<td>10</td>
<td>4</td>
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<tr>
<td>2</td>
<td>9</td>
<td>6</td>
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<td>3</td>
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<td>4</td>
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<td>10</td>
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<td>5</td>
<td>6</td>
<td>12</td>
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</tbody>
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6. At a price of 2, there is:
   a. a surplus of 3   b. a shortage of 3   c. an excess supply of 3   d. none of the above

7. The equilibrium price is ______ and the equilibrium quantity is _______.
   a. 1; 10   b. 2; 6   c. 3; 8   d. none of the above

8. Suppose that the government imposes a price floor of 4. The result will be:
   a. a surplus of 3   b. a shortage of 3   c. an excess demand of 3   d. none of the above
9. The difference between normal and inferior goods is that:

a. normal goods are of better quality than inferior goods.
b. an increase in price will shift the demand curve for a normal good rightward and the demand curve for an inferior good leftward.
c. if the price of a normal good increases, individuals who buy it are poorer; with inferior goods, the opposite is true.
d. an inferior good is something that will not be demanded until quantities of the normal good have been exhausted.
e. an increase in income will shift the demand curve for a normal good rightward and the demand curve for an inferior good leftward.

10. Sugar and honey are viewed as substitutes for each other in many cooking applications. If the price of sugar rises, we would expect

a. the demand for honey to increase.
b. the demand for honey to decrease.
c. the quantity demanded of honey to decrease.
d. the price of honey to decrease.
e. the quantity demanded of honey to increase.

Use the demand and supply curves for cookies shown Figure 1 to answer questions 11 - 16. The line labeled S is the initial supply curve.

11. The equilibrium price is _______ and the equilibrium quantity is ________:

a. 0a; ag  b. 0a; af  c. 0b ; be  d. none of the above

12. A movement along S from point g to point c is called:

a. an increase in supply  b. an increase in the quantity supplied.
c. an increase in the supply curve  d. none of the above.

13. If the price of cookies is fixed at 0a, there is:

a. an equilibrium quantity of ag units supplied  b. an equilibrium quantity of af demanded
   c. a shortage of gf  d. a surplus of gf

![Figure 1](image_url)
14. Which of the following could not shift the supply curve of cookies from S to S’?
   a. a decline in the price of cookies  
   b. an improvement in technology  
   c. a decline in the price of an flour  
   d. an increase in the number of bakeries

15. The shift in the supply curve from S to S’ is called:
   a. a fall in supply  
   b. an increase in the quantity supplied  
   c. an increase in supply  
   d. a change in technology

16. If the supply curve of cookies shifts of S to S’, the equilibrium price will _____ and the equilibrium quantity will ______ .
   a. fall from 0b to 0a; rise from bc to af  
   b. fall from 0b to 0a; rise from bc to be  
   c. rise from 0a to 0b; fall from bc to af  
   d. fall from 0b to 0a; fall from bc to ag

17. The immediate effect on GDP of John’s purchasing a government bond is
   a. a decrease in consumption because he has less money to spend.  
   b. an increase in government spending.  
   c. an increase in investment.  
   d. a decrease in investment because less money is available to him for further investment.  
   e. nonexistent, since no real goods and services have been produced.

18. A farmer grows wheat and sells it to a bakery for $5. The bakery bakes the wheat into bread, which it sells to a distributor for $20. The distributor sells the bread to a supermarket for $30, which sells the bread to customers for $50. Which of the following is true?
   a. The value added by the distributor is $30.  
   b. The supermarket contributed more, in value added, than the bakery.  
   c. As a result of this activity GDP rises by $50 minus the value added at each stage of production.  
   d. Counting the value added at each stage instead of the final selling price creates a problem of double counting.  
   e. The value added by the farmer is $20, because the wheat, which is worth $5, is necessary for each of the three remaining stages of production.

19. Which of the following would add to this year’s GDP?
   a. The 100 shares of stock that Jane bought this month.  
   b. The used car Bill sold to Sam.  
   c. The $10 that I gave to my son last week.  
   d. The herbs and spices MacDonald’s bought for its special sauce last month.

Answer questions 20 - 24 based on the Figure 2. Note that D is the initial demand curve.
20. A movement along the demand curve from f to c is called:
   a. a decrease in demand           b. a decrease in the quantity demanded
   c. a fall in demand               d. all of the above are correct

21. Given D and S, the equilibrium price is _____ and quantity is ______.
   a. 0a; af                         b. 0a; ag                         c. 0b; bc                         d. be; af

22. Which of the following could result in the shift from D to D’?
   a. an increase in the price of a substitute good   b. a increase in the price of a complementary good
   c. a decline in the price of the product in question  d. a decrease in the cost of manufacturing the product

23. Given D and S, a price floor of 0b will result in:
   a. a shortage of be               b. a shortage of ce               c. a surplus of ce             d. a surplus of be

24. Which of the following is best illustrated by Figure 2?
   a. If firms produce more of a product, people will buy more.
   b. If people want more of a product, more of that product will be produced.
   c. Price should be fixed at 0a.
   d. all of the above are correct.

25. When a demand schedule is drawn as a graph,
   a. price is measured on the vertical axis.  b. quantity is measured on the horizontal axis.
   c. the resulting curve has a negative slope.  d. other variables are held constant.
   e. All of the above are correct.

26. If the government has stated that it will buy any amount of good X offered at $30, then which demand curve in Figure 4-2 is appropriate?

27. A 1985 Harvard study showed that the price of cigarettes does not affect how much an individual smokes but whether he smokes. If this is correct, which graph in Figure 4-3 shows the typical individual's demand curve for cigarettes?
28. Gross domestic product is best described as:
   a. the nation’s measure of economic welfare.
   b. total national output, including all nonmarket activities.
   c. total national output less the ecological impact.
   d. the sum of the money values of all final goods and services produced in the nation within the year.

29. How are intermediate goods treated in the GDP accounts?
   a. They are omitted.
   b. They are included at market value.
   c. They are included in the year they are produced, but omitted in the year they are sold.
   d. They are included at the time of production and at the time of sale within the finished good.
   e. Depends on whether the good is imported or exported.

30. Real GDP is another term for
   a. constant dollar GDP.
   b. current dollar GDP.
   c. actual GDP.
   d. tangible GDP.
   e. All of the above.

31. Suppose that over the course of three decades, the average workweek becomes 15% shorter. In this case:
   a. GDP generally overestimates the level of economic well-being.
   b. GDP is increasingly useful as a measure of economic well-being.
   c. GDP must necessarily rise very slowly.
   d. GDP per person must necessarily fall over this time period.
   e. GDP systematically underestimates the growth of economic well-being.

32. In Figure 5-2, if the aggregate demand curve continues to shift outward over time, the economy will
   a. experience inflation.
   b. suffer from economic stagnation.
   c. see a sustained decrease in the price level.
   d. experience a significant increase in unemployment.
33. In Figure 5-2, if the aggregate demand curve continues to shift to the left over time, the economy will
   a. experience an increase in domestic product.
   b. experience a recession.
   c. be subjected to an inflationary price level.
   d. enter the expansionary phase of the business cycle.

34. Using an aggregate supply and demand diagram, if aggregate demand shifts to the left,
   a. both prices and nominal GDP will rise.
   b. both prices and nominal GDP will fall.
   c. prices will fall and nominal GDP may either rise or fall; not enough information is given to tell which.
   d. nominal GDP will fall and prices may either rise or fall; not enough information is given to tell which.

35. During an inflationary period, stabilization policy should seek to
   a. expand aggregate demand.
   b. contract aggregate demand.
   c. neutralize aggregate demand.
   d. find new sources of aggregate demand.

36. In the circular flow diagram above, consumption is:
   a. 100  
   b. 25  
   c. 75  
   d. none of the above

37. In the circular flow diagram above, investment is:
   a. 100  
   b. 25  
   c. 75  
   d. none of the above

38. In the circular flow diagram above, income of the households is:
   a. 100  
   b. 25  
   c. 75  
   d. none of the above

**PART II.**
Log on to www.etrade.com and sign up for the e-trade game. Note that the game allows you to select a portfolio of stocks and cash equal to $100,000. E-trade pays the player earning largest return in any month $1000.

(As discussed in class, if you prefer, you can keep track of your portfolio using a newspaper).

Your assignment is to turn in the page containing your hypothetical portfolio.