

## Chapter 2—Scarcity and Choice

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### MULTIPLE CHOICE

1. In economics, scarcity means that
- there are not enough resources for everything that people want.
  - we can never feed every person in the country.
  - the price of goods has increased more rapidly than the general price level.
  - there is not enough of a particular good for everyone to buy all they want at the prevailing price.

ANS: A                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Communication  
TOP: A-Head: Scarcity and Choice                      KEY: Bloom's: Knowledge

2. Which of the following is true of scarcity?
- It applies to raw materials; manufactured goods are not scarce.
  - It affects all countries except the United States and Canada.
  - It affects only poor nations.
  - It is a basic problem of economics that affects all nations.

ANS: D                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Analytic  
TOP: A-Head: Scarcity and Choice                      KEY: Bloom's: Knowledge

3. People must make choices because
- wants are limited.
  - resources are unlimited.
  - they are unequally endowed with talent.
  - wants are unlimited and resources are scarce.

ANS: D                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Analytic  
TOP: A-Head: Nations Must Make Choices                      KEY: Bloom's: Knowledge

4. A need to make choices exists because of
- scarcity of resources.
  - the abundance of goods.
  - unlimited human needs and wants.
  - both scarcity of resources and unlimited human needs and wants.

ANS: D                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Analytic  
TOP: A-Head: Nations Must Make Choices                      KEY: Bloom's: Knowledge

5. Individuals are forced to make choices because
- wants are unlimited.
  - the supply of resources is infinite.
  - wants are unlimited and resources are scarce.
  - resources exceed wants.

ANS: C                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Analytic  
TOP: A-Head: Nations Must Make Choices                      KEY: Bloom's: Knowledge

6. A movement downward toward the right along a typical production possibilities curve represents
- decreasing production of both goods under consideration.
  - increasing production of both goods under consideration.
  - increasing production of one good and decreasing production of the other.
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d. increasing production of one good with no change in production of the other.

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Analytic  
TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Analysis

7. A society will be at a point inside its production possibilities curve whenever

- a. all resources are fully employed.
- b. income is equally distributed.
- c. some resources are unemployed.
- d. resources are scarce.

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Analytic  
TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Analysis

8. If an economy is producing a combination of goods inside its production possibilities curve, it may mean that the nation

- a. is overproducing.
- b. is maximizing its production.
- c. is underutilizing its resources.
- d. has no room to grow.

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Analytic  
TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Analysis

9. An economy's production possibilities curve could shift outward as a result of a(n)

- a. increased level of technology.
- b. reduction in the quantity of capital goods.
- c. decrease in the production of goods.
- d. decrease in the amount of available resources.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Analytic  
TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Synthesis

10. In 2011, the per capita output of goods and services in the United States was approximately

- a. \$15,000.
- b. \$45,000.
- c. \$8,000.
- d. \$25,000.

ANS: B                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Diversity  
TOP: B-Head: Aid to Developing Nations                      KEY: Bloom's: Knowledge

11. In 2011, total output of goods and services in the United States was approximately

- a. \$10 trillion.
- b. \$12 trillion.
- c. \$15 trillion.
- d. \$20 trillion.

ANS: C                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Diversity  
TOP: A-Head: Scarcity and Choice in the United States                      KEY: Bloom's: Knowledge

12. A nation that has done well economically in spite of a lack of natural resources is

- a. the United States.
  - b. Japan.
  - c. Canada.
  - d. Australia.
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ANS: B                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Diversity  
TOP: B-Head: A Solution: Increased Productivity                      KEY: Bloom's: Knowledge

13. A nation that lacks sufficient capital given its size even though it has ample natural resources is
- the United States.
  - Japan.
  - Canada.
  - China.

ANS: D                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Diversity  
TOP: B-Head: Nature and Scope of Problems                      KEY: Bloom's: Knowledge

14. Developing nations
- often lack the natural resources, skilled labor, or capital to improve their standards of living.
  - typically do not need outside help.
  - generally experience productivity increases greater than their population growth rates.
  - should not accept long-term aid in the form of technical assistance and capital.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Diversity  
TOP: B-Head: Aid to Developing Nations                      KEY: Bloom's: Evaluation

15. The process of specialization and exchange allows a producer to become
- proficient in one or a few areas of production.
  - proficient in all areas of production.
  - self-sufficient.
  - independent.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Analytic  
TOP: A-Head: Specialization and Exchange                      KEY: Bloom's: Comprehension

16. Use of the principle of comparative advantage involves
- specialization only.
  - exchange only.
  - both specialization and exchange.
  - money only.

ANS: C                      PTS: 1                      DIF: Moderate  
NAT: BUSPROG: Reflective Thinking                      TOP: A-Head: Absolute and Comparative Advantage  
KEY: Bloom's: Synthesis

17. An example of technological development is to increase output through
- raising pay.
  - working longer hours.
  - hiring more workers.
  - using better machines.

ANS: D                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Technology  
TOP: B-Head: A Solution: Increased Productivity                      KEY: Bloom's: Application

18. Productivity per worker has increased in the past primarily through
- hiring more teenagers.
  - hiring more women.
  - medical benefits.
  - technological development.
-

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Technology  
TOP: B-Head: A Solution: Increased Productivity                      KEY: Bloom's: Application

19. The bowed-out shape of the production possibilities curve shows that as more of one product is produced,
- the opportunity cost per unit will increase.
  - the opportunity cost per unit will decrease.
  - the opportunity cost per unit stays the same.
  - the production possibilities curve shifts inward.

ANS: A                      PTS: 1                      DIF: Challenging                      NAT: BUSPROG: Ethics  
TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Synthesis

20. If a firm uses technological development to change its production possibilities curve, it can move
- only in a vertical direction.
  - only in a horizontal direction.
  - only inward.
  - outward in any direction.

ANS: D                      PTS: 1                      DIF: Challenging                      NAT: BUSPROG: Technology  
TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Synthesis

21. The United States is academically unique in having so many
- trade schools.
  - colleges of arts and sciences.
  - business schools.
  - fine arts schools.

ANS: C                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Technology  
TOP: A-Head: Scarcity and Choice in the United States                      KEY: Bloom's: Knowledge

22. To solve their basic long-term economic problems, developing countries primarily need
- food.
  - clothing.
  - technical assistance.
  - shelter.

ANS: C                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Technology  
TOP: B-Head: Aid to Developing Nations                      KEY: Bloom's: Synthesis

23. When using the principle of comparative advantage, the person with no absolute advantage should perform the job in which he or she has
- a 50 percent disadvantage.
  - a 75 percent disadvantage.
  - a lesser disadvantage.
  - been trained.

ANS: C                      PTS: 1                      DIF: Challenging  
NAT: BUSPROG: Reflective Thinking                      TOP: A-Head: Absolute and Comparative Advantage  
KEY: Bloom's: Analysis

24. To exercise the law of comparative advantage, a nation
- must produce some goods using fewer resources than its trading partner.
  - does not have to produce any goods using fewer resources than its trading partner.
  - must produce some goods on an equal footing with its trading partner.
-

d. must show a lower absolute cost of production than its trading partner.

ANS: B                      PTS: 1                      DIF: Challenging  
NAT: BUSPROG: Reflective Thinking      TOP: B-Head: Comparative Advantage Between Nations  
KEY: Bloom's: Evaluation

25. The principle of comparative advantage applies to
- individuals only.
  - business firms only.
  - nations only.
  - individuals, businesses, and nations.

ANS: D                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Analytic  
TOP: B-Head: Comparative Advantage Between Nations      KEY: Bloom's: Application

26. Exercising the principle of comparative advantage between nations primarily involves
- specialization.
  - transportation costs.
  - currency exchange rates.
  - domestic income tax rates.

ANS: A                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Diversity  
TOP: B-Head: Comparative Advantage Between Nations      KEY: Bloom's: Synthesis

27. The process by which individuals limit their productive efforts to a particular activity instead of trying to produce directly everything that they need is known as
- specialization.
  - using absolute advantage.
  - using exchange.
  - scarcity.

ANS: A                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Technology  
TOP: A-Head: Specialization and Exchange      KEY: Bloom's: Comprehension

28. Specialization
- can increase total output without an increase in resources.
  - is beneficial only if exchange takes place.
  - should be based on the principle of comparative advantage.
  - All of the above are correct.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Technology  
TOP: A-Head: Specialization and Exchange      KEY: Bloom's: Synthesis

29. The greatest increase in productivity per capita results from
- a larger population.
  - more land.
  - specialization and exchange.
  - atmospheric conditions.

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Technology  
TOP: A-Head: Specialization and Exchange      KEY: Bloom's: Evaluation

30. When different regions of a country produce different goods,
- the production possibilities curve shifts to the left.
  - the country becomes worse off.
  - the principle of comparative advantage has been breached.
-

d. the country becomes better off if the regions are pursuing their comparative advantages.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Technology  
TOP: A-Head: Absolute and Comparative Advantage                      KEY: Bloom's: Synthesis

31. Assume that Country A produces 60 tons of sugar using 6 productive units and that Country B produces 40 tons of sugar using 6 productive units. Assume further that Country A produces 120 tons of coffee using 4 units of production and that Country B produces 90 tons of coffee using 4 units of production. It follows that
- Country A has a comparative advantage over Country B in the production of coffee.
  - Country A has a comparative advantage over Country B in the production of coffee and sugar.
  - Country A has a comparative advantage over Country B in the production of sugar.
  - Country B has a comparative advantage over Country A in the production of sugar.

ANS: C                      PTS: 1                      DIF: Challenging                      NAT: BUSPROG: Technology  
TOP: A-Head: Absolute and Comparative Advantage                      KEY: Bloom's: Evaluation

32. Every economic system must decide
- what and how much to produce.
  - how to produce.
  - how to distribute goods and services to the population.
  - All of these.

ANS: D                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Diversity  
TOP: A-Head: Scarcity and Choice                      KEY: Bloom's: Application

33. The opportunity cost of a choice is defined as the value of
- the next best alternative that must be sacrificed.
  - all the alternatives that must be sacrificed.
  - the chosen option minus the value of the next best alternative.
  - the chosen option minus the value of all the alternatives.

ANS: A                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Communication  
TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Knowledge

34. The typical production possibilities curve is bowed outward due to
- constant opportunity costs.
  - increasing opportunity costs.
  - decreasing opportunity costs.
  - technological innovations.

ANS: B                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Analytic  
TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Comprehension

35. When an economic unit limits the scope of its productive efforts instead of trying to produce everything it needs, it is engaging in
- exchange.
  - comparative production.
  - specialization.
  - self-sufficiency.

ANS: C                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Communication  
TOP: A-Head: Specialization and Exchange                      KEY: Bloom's: Knowledge

36. The ability to produce a good or service using fewer resources than other producers use is known as

- a. absolute advantage.
- b. comparative advantage.
- c. comparative specialization.
- d. absolute specialization.

ANS: A                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Analytic  
TOP: A-Head: Absolute and Comparative Advantage                      KEY: Bloom's: Knowledge

37. The ability to produce a good or service at a lower opportunity cost than other producers incur is known as
- a. absolute advantage.
  - b. comparative advantage.
  - c. comparative specialization.
  - d. absolute specialization.

ANS: B                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Analytic  
TOP: A-Head: Absolute and Comparative Advantage                      KEY: Bloom's: Knowledge

38. Suppose that Country A has an absolute advantage over Country B in the production of both wheat and cloth. The opportunity cost of 1 unit of wheat is 2 units of cloth in Country A and 3 units of cloth in Country B. It follows that
- a. Country A has a comparative advantage in both wheat and cloth.
  - b. Country A has a comparative advantage in wheat.
  - c. Country B has a comparative advantage in wheat.
  - d. Country A has a comparative advantage in cloth.

ANS: B                      PTS: 1                      DIF: Challenging  
NAT: BUSPROG: Reflective Thinking                      TOP: B-Head: Comparative Advantage Between Nations  
KEY: Bloom's: Evaluation

39. Suppose that Country A has an absolute advantage over Country B in the production of both wheat and cloth. The opportunity cost of 1 unit of wheat is 2 units of cloth in Country A and 3 units of cloth in Country B. It follows that production of both wheat and cloth will be maximized if
- a. Country A specializes in cloth.
  - b. Country A specializes in wheat.
  - c. Country A produces both goods.
  - d. both countries produce both goods.

ANS: B                      PTS: 1                      DIF: Challenging  
NAT: BUSPROG: Reflective Thinking                      TOP: B-Head: Comparative Advantage Between Nations  
KEY: Bloom's: Evaluation

40. Suppose that Country A has an absolute advantage over country B in the production of both wheat and cloth. The opportunity cost of 1 unit of wheat is 2 units of cloth in Country A and 3 units of cloth in Country B. If each country specializes in producing the good in which it is relatively more efficient and then trades for the other good, it follows that
- a. all the resulting gains in consumption will go to Country A.
  - b. all the resulting gains in consumption will go to Country B.
  - c. each country will experience half the resulting gains in consumption.
  - d. the allocation of the resulting consumption gains will be determined by bargaining between the two countries.

ANS: D                      PTS: 1                      DIF: Challenging  
NAT: BUSPROG: Reflective Thinking                      TOP: B-Head: Comparative Advantage Between Nations  
KEY: Bloom's: Evaluation

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41. Which of the following would shift a nation's entire production possibilities curve outward?
- moving from less than full employment to full employment.
  - developing a more efficient technology.
  - more efficiently allocating productive resources already available.
  - All of these.

ANS: B                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Technology  
TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Synthesis

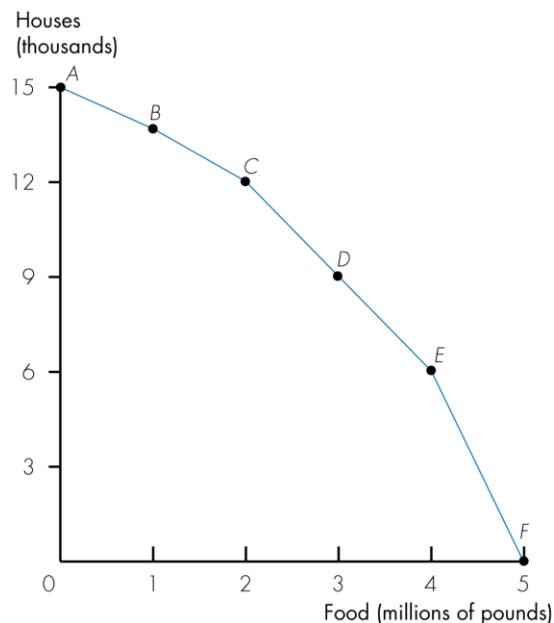
42. Sources of economic growth include
- additional amounts of more highly skilled and educated labor.
  - additional amounts of capital.
  - new technology.
  - All of these.

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Analytic  
TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Synthesis

43. Which of the following is true about a nation's production possibilities curve?
- a point inside the curve is a combination of products that is currently impossible to produce.
  - a point outside the curve is a combination of products that is below capacity.
  - a rightward shift of the curve illustrates economic growth.
  - full employment is illustrated by a point inside the curve.

ANS: C                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Analytic  
TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Synthesis

44. Refer to the following figure. Which of the following production possibilities would result in the greatest rate of economic growth over time?

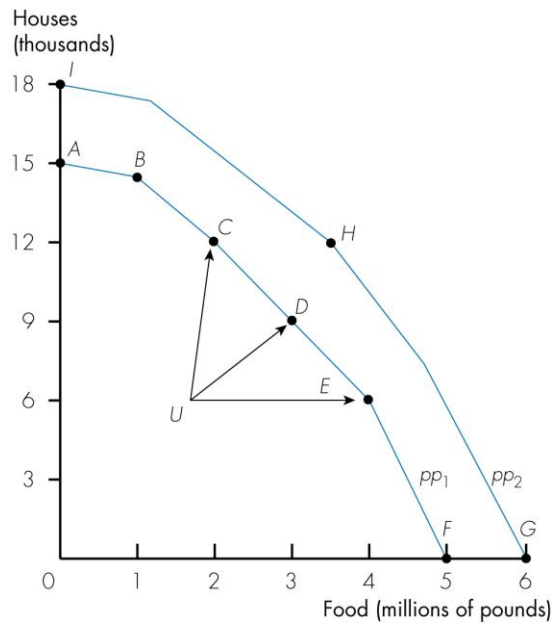


- Point B
  - Point C
  - Point D
  - Point E
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ANS: A                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Analytic  
 TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Synthesis

45. Refer to the following figure. Which of the following expresses economic growth?



- Movement from Point U to Point C
- Movement from Point U to Point D
- Movement from Point U to Point E
- A shift of the Production Possibilities Curve from PP1 to PP2

ANS: D                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Analytic  
 TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Synthesis

**TRUE/FALSE**

1. The basic function of any economic system is to provide the framework for allocating scarce resources in a way that adequately satisfies unlimited wants.

ANS: T                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Communication  
 TOP: A-Head: Scarcity and Choice                      KEY: Bloom's: Knowledge

2. Economics can be defined as the study of choices.

ANS: T                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Communication  
 TOP: A-Head: Nations Must Make Choices                      KEY: Bloom's: Application

3. The United States has an abundance of resources and thus does not face the problem of scarcity.

ANS: F                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Communication  
 TOP: A-Head: Scarcity and Choice                      KEY: Bloom's: Comprehension

4. The standard of living in most countries in the past has risen primarily as a result of a more skilled workforce and better machinery and equipment.

ANS: T                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Technology  
TOP: A-Head: Nations Must Make Choices                      KEY: Bloom's: Knowledge

5. A nation needs an abundance of all productive resources in order to attain a high standard of living.

ANS: F                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Technology  
TOP: A-Head: Nations Must Make Choices                      KEY: Bloom's: Comprehension

6. If a society is producing at a point on its production possibilities curve, it does not have the problem of scarce resources.

ANS: F                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Communication  
TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Application

7. The process of specialization can be carried out by business firms as well as by regions and nations.

ANS: T                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Technology  
TOP: A-Head: Specialization and Exchange                      KEY: Bloom's: Application

8. The extent to which a society can engage in specialization and exchange is limited by the size of the market.

ANS: T                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Technology  
TOP: A-Head: Specialization and Exchange                      KEY: Bloom's: Application

9. Government regulations which affect entrepreneurial activities within a nation also affect total output and the standard of living.

ANS: T                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Technology  
TOP: A-Head: Nations Must Make Choices                      KEY: Bloom's: Comprehension

10. A nation's raw materials and sources of energy are considered part of its capital resources.

ANS: F                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Communication  
TOP: A-Head: Nations Must Make Choices                      KEY: Bloom's: Knowledge

11. When the entire production possibilities curve shifts inward, the economy is growing.

ANS: F                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Analytic  
TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Comprehension

12. A production possibilities curve shows the use of resources and the alternative combinations of goods that a society can produce.

ANS: T                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Communication  
TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Knowledge

13. The opportunity cost of a choice is defined as the value of all the alternative choices.

ANS: F                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Communication  
TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Knowledge

14. If a nation is producing a combination of goods inside its production possibilities curve, it is ~~underutilizing its resources.~~
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ANS: T                    PTS: 1                    DIF: Easy                    NAT: BUSPROG: Analytic  
TOP: A-Head: Production Possibilities Curve                    KEY: Bloom's: Knowledge

15. A nation's production possibilities curve can be shifted outward by technological development.

ANS: T                    PTS: 1                    DIF: Easy                    NAT: BUSPROG: Technology  
TOP: A-Head: Production Possibilities Curve                    KEY: Bloom's: Synthesis

16. A production possibilities curve will shift outward when additional resources are found.

ANS: T                    PTS: 1                    DIF: Easy                    NAT: BUSPROG: Analytic  
TOP: A-Head: Production Possibilities Curve                    KEY: Bloom's: Comprehension

17. Because of the high level of output in the United States, there is little need for choosing among alternative output combinations.

ANS: F                    PTS: 1                    DIF: Easy  
NAT: BUSPROG: Reflective Thinking                    TOP: A-Head: Scarcity and Choice in the United States  
KEY: Bloom's: Comprehension

18. Total annual production in the United States is in excess of \$14 trillion.

ANS: T                    PTS: 1                    DIF: Easy                    NAT: BUSPROG: Communication  
TOP: A-Head: Scarcity and Choice in the United States                    KEY: Bloom's: Knowledge

19. The ability to produce a good or service using fewer resources than other producers use is known as comparative advantage.

ANS: F                    PTS: 1                    DIF: Easy                    NAT: BUSPROG: Communication  
TOP: A-Head: Absolute and Comparative Advantage                    KEY: Bloom's: Knowledge

20. Japan has a low standard of living because of its shortage of resources.

ANS: F                    PTS: 1                    DIF: Easy                    NAT: BUSPROG: Diversity  
TOP: B-Head: Nature and Scope of Problems                    KEY: Bloom's: Knowledge

21. Technological development can be applied to the improvement of human capital as well as physical capital.

ANS: T                    PTS: 1                    DIF: Moderate                    NAT: BUSPROG: Technology  
TOP: B-Head: Nature and Scope of Problems                    KEY: Bloom's: Comprehension

22. The ability to produce a good or service at a lower opportunity cost than other producers face is known as comparative advantage.

ANS: T                    PTS: 1                    DIF: Easy                    NAT: BUSPROG: Technology  
TOP: A-Head: Absolute and Comparative Advantage                    KEY: Bloom's: Knowledge

23. The ability of a nation to gain from specialization and exchange is affected by factors such as shipping costs and exchange rates.

ANS: T                    PTS: 1                    DIF: Moderate                    NAT: BUSPROG: Analytic  
~~TOP: B-Head: Comparative Advantage in Practice                    KEY: Bloom's: Comprehension~~

24. One cause for the uneven standard of living throughout the world is the uneven distribution of resources.

ANS: T                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Diversity  
TOP: A-Head: Problems of Scarcity                      KEY: Bloom's: Application

25. The application of the principle of comparative advantage requires each of two trading partners to have an absolute advantage over the other in the production of some particular commodity.

ANS: F                      PTS: 1                      DIF: Challenging                      NAT: BUSPROG: Analytic  
TOP: B-Head: Comparative Advantage Between Nations                      KEY: Bloom's: Synthesis

26. If a nation has an absolute advantage over another nation in the production of all commodities, it is not feasible to take advantage of the principle of comparative advantage.

ANS: F                      PTS: 1                      DIF: Challenging                      NAT: BUSPROG: Analytic  
TOP: B-Head: Comparative Advantage Between Nations                      KEY: Bloom's: Evaluation

27. Comparative advantage cannot be applied to activities of individuals.

ANS: F                      PTS: 1                      DIF: Easy                      NAT: BUSPROG: Analytic  
TOP: B-Head: Comparative Advantage Between Nations                      KEY: Bloom's: Comprehension

28. Overspecialization and the resulting dependence on one or a few products by a nation can lead to severe economic fluctuations if demand for those products varies widely.

ANS: T                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Analytic  
TOP: B-Head: Comparative Advantage in Practice                      KEY: Bloom's: Application

29. In exercising the principle of comparative advantage, a nation with no absolute advantage should produce a commodity in which it faces a lower opportunity cost than its trading partners face.

ANS: T                      PTS: 1                      DIF: Challenging  
NAT: BUSPROG: Reflective Thinking                      TOP: B-Head: Comparative Advantage Between Nations  
KEY: Bloom's: Evaluation

30. In the long run, a nation cannot overcome a shortage of labor or land.

ANS: F                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Technology  
TOP: B-Head: Nature and Scope of Problems                      KEY: Bloom's: Evaluation

31. Increasing opportunity costs occur along the production possibilities curve because not all resources are alike in producing different goods.

ANS: T                      PTS: 1                      DIF: Moderate                      NAT: BUSPROG: Analytic  
TOP: A-Head: Production Possibilities Curve                      KEY: Bloom's: Comprehension

## ESSAY

1. Relate the declaration of war by the United States against terrorism to the production possibilities curve.
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ANS:

As the need or desire for military goods and services increases, the nation will need to devote more resources to military use. This can be represented by a movement along a production possibilities curve with military goods on one axis and consumer goods or investment on the other axis.

PTS: 1                    DIF: Challenging    NAT: BUSPROG: Reflective Thinking  
TOP: A-Head: Production Possibilities Curve                    KEY: Bloom's: Evaluation

2. The North American Free Trade Agreement signed in 1993 lowered tariffs among the United States, Canada, and Mexico. What would proponents of the treaty consider to be the likely benefits?

ANS:

By permitting freer exchange, the treaty will promote more specialization and exchange in keeping with the principle of comparative advantage, thereby increasing income and wealth.

PTS: 1                    DIF: Challenging    NAT: BUSPROG: Technology  
TOP: A-Head: Specialization and Exchange                    KEY: Bloom's: Evaluation

3. Assume that you have won a prize of \$10,000. Make a list of how you would spend and save the money, from most important to least important.

ANS:

The answer will depend on the judgment of the individual student. But in making the list, the student should remember that there is no more than \$10,000 to spend.

PTS: 1                    DIF: Easy                    NAT: BUSPROG: Analytic  
TOP: A-Head: Production Possibilities Curve                    KEY: Bloom's: Application

4. Give some examples of the operation of the principle of comparative advantage.

ANS:

Here the student might note that many auto producers buy parts for their cars from specialized suppliers, even though the auto company might be able to make them more cheaply. The automobile company benefits by concentrating on the assembly of autos rather than on making parts. Restaurants, such as McDonald's, Burger King, and Wendy's, construct new restaurants every year. Rather than own and operate these restaurants, most are sold as franchises for individuals to operate.

PTS: 1                    DIF: Moderate           NAT: BUSPROG: Analytic  
TOP: A-Head: Absolute and Comparative Advantage                    KEY: Bloom's: Application