

***Business Essentials, 9e (Ebert/Griffin)***  
**Chapter 1 The U.S. Business Environment**

1) The customs, values, and demographic characteristics of the society in which an organization functions are the principal elements of the political-legal environment.

Answer: FALSE

Explanation: These are the main considerations of the sociocultural environment. The political-legal environment reflects the relationship between business and government, usually in the form of government regulation of business.

Page Ref: 5

Difficulty: Easy

Objective: 1.2

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

2) Physical resources include the data and other information used by businesses.

Answer: FALSE

Explanation: Physical resources are the tangible resources that organizations use to conduct their business such as natural resources, raw materials, offices, storage and production facilities, parts and supplies, computers and peripherals, and a variety of other equipment.

Page Ref: 8

Difficulty: Easy

Objective: 1.3

Learning Outcome: Identify the different types of technologies used in business and describe their uses

Skill: Concept

3) Economic systems differ in how factors of production are used.

Answer: TRUE

Explanation: Different types of economic systems manage the factors of production differently. In capitalism, for instance, they are managed by private individuals with capital resources, while in a command economy the government manages the factors of production.

Page Ref: 9

Difficulty: Easy

Objective: 1.3

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

4) The point at which the supply curve and the demand curve intersect is the market price.

Answer: TRUE

Explanation: When demand and supply curves are plotted on the same graph, the point at which they intersect is the point at which demand matches supply, which determines the market price.

Page Ref: 12

Difficulty: Easy

AACSB: Analytic skills

Objective: 1.4

Learning Outcome: Discuss strategies for setting and adjusting prices

Skill: Concept

5) Aggregate output refers to a company's annual production of goods or services.

Answer: FALSE

Explanation: Aggregate output is the total quantity of goods and services produced by an economic system during a given period.

Page Ref: 17

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

6) The United States government manages the collection and spending of its revenues through monetary policy.

Answer: FALSE

Explanation: The United States government manages the collection and spending of its revenues through fiscal policy.

Page Ref: 23

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

7) The pursuit of profits is how a business differs from organizations such as most universities, hospitals, and government agencies.

Answer: TRUE

Explanation: The pursuit of profits distinguishes a business from those organizations—such as most universities, hospitals, and government agencies—that run in much the same way but that generally don't seek profits.

Page Ref: 4

Difficulty: Easy

Objective: 1.1

Learning Outcome: Explain the entrepreneurship process

Skill: Concept

8) The technological environment includes only electronics and telecommunications used to perform business activities.

Answer: FALSE

Explanation: Technology includes human knowledge, work methods, physical equipment, electronics and telecommunications, and various processing systems that are used to perform business activities.

Page Ref: 6

Difficulty: Moderate

AACSB: Analytic skills

Objective: 1.2

Learning Outcome: Identify the different types of technologies used in business and describe their uses

Skill: Concept

9) One of the four elements that are necessary for private enterprise to be carried out is reasonable prices.

Answer: FALSE

Explanation: The four elements that must be present in private enterprise are private property rights, freedom of choice, profits, and competition.

Page Ref: 14

Difficulty: Moderate

Objective: 1.4

Learning Outcome: Discuss strategies for setting and adjusting prices

Skill: Concept

10) In typical modern oligopolies, the large capital investment necessary to enter the market discourages new competitors.

Answer: TRUE

Explanation: A major factor discouraging new competitors in current oligopolistic industries such as automobiles and large commercial aircraft is the huge capital investment that would be needed to start a new company.

Page Ref: 15

Difficulty: Moderate

Objective: 1.4

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

11) Natural monopolies exist partly because duplication of effort and resources would be wasteful in some cases.

Answer: TRUE

Explanation: Many electric companies, for example, are natural monopolies because they can supply all the power needed in a local area.

Page Ref: 16

Difficulty: Moderate

Objective: 1.4

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

12) Economic indicators help to assess the performance of an economy.

Answer: TRUE

Explanation: Specifically, economic growth is measured via aggregate output, standard of living, gross domestic product, and productivity; stability is reflected through levels of inflation and unemployment.

Page Ref: 17

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

13) The primary measure of growth in the business cycle is inflation.

Answer: FALSE

Explanation: The primary measure of growth in the business cycle is aggregate output.

Page Ref: 17

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

14) Gross domestic product (GDP) refers to the total value of goods and services produced by a national economy within a given period regardless of where the factors of production are located.

Answer: FALSE

Explanation: GDP refers to the total value of all goods and services produced within a given period by a national economy through *domestic* factors of production.

Page Ref: 17

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

15) Inflation results in increased purchasing power for the consumer.

Answer: FALSE

Explanation: Inflation occurs when the amount of money injected into an economy exceeds the increase in actual output. When this happens, people will have more money to spend, but there will still be the same quantity of products available for them to buy. As they compete to buy available products, prices go up.

Page Ref: 22

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

16) Tax increases and decreases are a form of fiscal policy.

Answer: TRUE

Explanation: Tax rates can play an important role in fiscal policies, helping to manage the economy.

Page Ref: 23

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

17) The government can influence the availability of capital by working through the Federal Reserve System.

Answer: TRUE

Explanation: The interest rates set by the Federal Reserve System can influence the ability and willingness of banks throughout the country to lend money.

Page Ref: 23

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Application

18) Stabilization policy is made up of both monetary and fiscal policy.

Answer: TRUE

Explanation: The purpose of monetary and fiscal policy is to smooth out fluctuations in output and unemployment and to stabilize prices.

Page Ref: 23

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

19) Product differentiation is common in a market characterized by monopolistic competition.

Answer: TRUE

Explanation: Product differentiation also gives sellers some control over prices.

Page Ref: 15

Difficulty: Easy

Objective: 1.4

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

20) In a natural monopoly, prices tend to be government-regulated.

Answer: TRUE

Explanation: Natural monopolies occur in industries in which one company can efficiently supply all needed goods or services. Since they have little or no competition, their prices have to be regulated so that consumers do not have to pay overly high prices.

Page Ref: 16

Difficulty: Moderate

Objective: 1.4

Learning Outcome: Discuss strategies for setting and adjusting prices

Skill: Application

21) The main measure of growth in the business cycle is aggregate output.

Answer: TRUE

Explanation: Aggregate output is the total quantity of goods and services produced by an economic system during a given period. When it increases, the economy is considered to be in a growth cycle.

Page Ref: 17

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

22) Deflation, an indication that the economy is contracting, is characterized by price stabilization of goods.

Answer: FALSE

Explanation: Deflation occurs when there are widespread price cuts. Deflation generally means that the overall economy is shrinking.

Page Ref: 22

Difficulty: Easy

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

23) If productivity increases, prices charged to consumers will tend to increase as well.

Answer: FALSE

Explanation: If productivity increases, it's likely that prices of products will decrease and the standard of living will increase.

Page Ref: 19

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Discuss strategies for setting and adjusting prices

Skill: Concept

24) The consumer price index is expressed as a percentage of prices as compared to a base period.

Answer: TRUE

Explanation: The current base period used to measure inflation is 1982-1984.

Page Ref: 22

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

25) Which environment is NOT an important dimension of a business organization's external environment?

A) the political-legal environment

B) the sociocultural environment

C) the technological environment

D) the corporate cultural environment

E) the global business environment

Answer: D

Explanation: D) The external environment consists of everything outside an organization's boundaries that might affect it. The corporate cultural environment is internal to the organization.

Page Ref: 6-7

Difficulty: Easy

Objective: 1.2

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

26) What term denotes a nation's basis for allocating its resources among its citizens?

A) capital structure

B) economic system

C) ownership processes

D) distribution network

E) national regulations

Answer: B

Explanation: B) An economic system is a nation's system for allocating its resources among its citizens, both individuals and organizations.

Page Ref: 7

Difficulty: Easy

Objective: 1.3

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

27) What is the process for converting government enterprises into individually owned firms known as?

- A) production allocation
- B) privatization
- C) entrepreneurship
- D) demand assessment
- E) profit maximization

Answer: B

Explanation: B) Privatization is the process of converting government enterprises into privately owned companies, which will then have the right to run such a business for profit.

Page Ref: 10

Difficulty: Easy

Objective: 1.3

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

28) What is the point at which the supply curve and the demand curve intersect on a graph?

- A) equilibrium price
- B) decision point
- C) surplus price
- D) perfect price
- E) parity point

Answer: A

Explanation: A) The equilibrium price is determined by the shape of the supply curve and the demand curve when plotted by amount available and price. The equilibrium price is set at the point at which the supply curve and the demand curve intersect.

Page Ref: 12

Difficulty: Easy

Objective: 1.4

Learning Outcome: Discuss strategies for setting and adjusting prices

Skill: Concept



29) What is the price at which the quantity of goods demanded and the quantity of goods supplied are equal?

- A) the going rate
- B) the margin rate
- C) the market price
- D) the optimum price
- E) the cost price

Answer: C

Explanation: C) The market price is set by the demand and supply for a given good. It is defined as the price at which the quantity of goods demanded and the quantity of goods supplied are equal.

Page Ref: 12

Difficulty: Easy

Objective: 1.4

Learning Outcome: Discuss strategies for setting and adjusting prices

Skill: Concept

30) What occurs when the quantity demanded exceeds the quantity supplied?

- A) demand deficit
- B) surplus
- C) equilibrium point
- D) shortage
- E) supply schedule

Answer: D

Explanation: D) When demand exceeds supply, there will not be enough goods available to meet the demand for them. This is known as a shortage.

Page Ref: 12

Difficulty: Easy

Objective: 1.4

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

31) Which of the following does NOT represent a degree of competition in a private enterprise system?

- A) oligopoly
- B) socialism
- C) monopoly
- D) perfect competition
- E) monopolistic competition

Answer: B

Explanation: B) Competition is the economic condition in which there are certain demands that can be met by more than one business, so businesses in the same industry compete for the same resources or customers.

Page Ref: 14

Difficulty: Easy

Objective: 1.4

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

32) Which of the following exists when an industry or market has only one producer?

- A) competition
- B) oligopoly
- C) monopoly
- D) communism
- E) socialism

Answer: C

Explanation: C) A monopoly is a market or industry in which there is only one producer that supplies a certain product. Monopolies in the United States economy are either discouraged or regulated so that prices are not too high.

Page Ref: 16

Difficulty: Easy

Objective: 1.4

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

33) Which term refers to the pattern of short-term ups and downs in an economy?

- A) aggregate output
- B) business cycle
- C) standard of living
- D) balance of payments
- E) demand and supply schedule

Answer: B

Explanation: B) The business cycle is the short-term pattern of economic expansions and contractions.

Page Ref: 17

Difficulty: Easy

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

34) Which term refers to the total quantity and quality of goods and services that people living in an economic system can purchase?

- A) business cycle
- B) demand and supply schedule
- C) standard of living
- D) aggregate output
- E) consumer price index

Answer: C

Explanation: C) The standard of living is the total quantity and quality of goods and services that people can purchase with the currency used in their economic system. Standard of living is determined by economic conditions such as inflation and purchasing power.

Page Ref: 17

Difficulty: Easy

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

35) Which term refers to the total value of all goods and services produced within a given period by a national economy?

- A) standard of living
- B) aggregate output
- C) gross domestic product
- D) gross national produce
- E) purchasing power parity

Answer: C

Explanation: C) Gross domestic product is the total value of all goods and services produced within a given period by a national economy through domestic factors of production.

Page Ref: 17

Difficulty: Easy

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

36) Which of the following measures indicates the prices of typical products purchased by American consumers living in urban areas?

- A) GDP per capita
- B) standard of living
- C) consumer price index
- D) purchasing power parity
- E) Big Mac index

Answer: C

Explanation: C) The consumer price index is a measure of the prices of typical products purchased by consumers living in urban areas. It is used as a comparative standard, to tell whether inflation or deflation is occurring, for example.

Page Ref: 22

Difficulty: Easy

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

37) What does productivity measure?

- A) the total value of all goods and services produced by a national economy
- B) how much a system produces with the resources needed to produce it
- C) how much output is necessary to produce a certain level of demand
- D) the standard of living relative to purchasing power parity
- E) how much gross national product results from inputs of labor

Answer: B

Explanation: B) Productivity is a measure of economic growth that compares how much a system produces with the resources needed to produce it.

Page Ref: 19

Difficulty: Easy

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

38) What is the economic condition characterized by widespread increased prices without increased purchasing power?

- A) unemployment
- B) inflation
- C) expansion
- D) deflation
- E) recession

Answer: B

Explanation: B) Inflation is the condition that occurs when widespread price increases are present throughout an economic system. This happens when the amount of money in the economy grows faster than the amount of products available to buy.

Page Ref: 21-22

Difficulty: Easy

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

39) What is the condition in an economic system in which the amount of money available and the number of goods and services produced are growing at about the same rate?

- A) unemployment
- B) stability
- C) deflation
- D) inflation
- E) oversupply

Answer: B

Explanation: B) Economic stability happens when the amount of money available in an economic system and the quantity of goods and services produced in it are growing at about the same rate. When this occurs, there is neither inflation nor deflation.

Page Ref: 23

Difficulty: Easy

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

40) What are profits?

- A) total money taken in by a corporation
- B) increases in income from year to year
- C) increases in a corporation's stock price
- D) revenue generated by goods and services
- E) difference between revenues and expenses

Answer: E

Explanation: E) Profits represent the difference between an organization's revenues and its expenses; profits are the goal of most businesses and allow people to open and expand businesses.

Page Ref: 4

Difficulty: Moderate

Objective: 1.1

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

41) A new U.S. company plans to introduce an inexpensive, high-quality line of shoes to the American market. It has found a manufacturer in another country that can produce the shoes at a low enough cost that they will still be cheaper than other brands of the same quality.

Which of the following represents a potential ethical implication that the company should consider before beginning production?

- A) the country's existing labor laws and the factory working conditions
- B) the average exchange rate of the country's currency over a ten-year period
- C) the challenges of doing business in a country with a nonconvertible currency
- D) the energy demands of the manufacturer's facility
- E) the basic international business strategy it will use

Answer: A

Explanation: A) When choosing a country to outsource to, a company should not only consider the financial implications of offshoring, but also the ethical implications of conducting business in a country that may have very different laws and legal standards.

Page Ref: 6

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.1

Learning Outcome: Compare and contrast different economic systems

Skill: Application

42) What marks the key difference between economic systems?

- A) the way they manage the factors of production
- B) the way they transport goods within their borders
- C) the way rules and regulations are legislated
- D) the way workers are relocated to different regions
- E) the way basic necessities are determined

Answer: A

Explanation: A) Economic systems manage the factors of production differently; management of these factors often revolves around the degree of government control of them.

Page Ref: 7

Difficulty: Moderate

Objective: 1.3

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

43) What does a planned economy rely on a centralized government to do?

- A) support free enterprise in every way possible
- B) allocate all or most factors of production
- C) encourage citizens to buy shares of stock in small companies
- D) keep its control activities to a minimum
- E) direct workers to start their own small businesses

Answer: B

Explanation: B) A centralized government controls all or most of the factors of production.

Page Ref: 10

Difficulty: Moderate

AACSB: Dynamics of the global economy

Objective: 1.3

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

44) Which economic system emphasizes the private ownership of most factors of production?

- A) socialism
- B) communism
- C) capitalism
- D) Marxism
- E) federalism

Answer: C

Explanation: C) Capitalism makes use of the profit incentive for private ownership of the factors of production and encourages entrepreneurship by offering profits as an incentive.

Page Ref: 10

Difficulty: Easy

AACSB: Dynamics of the global economy

Objective: 1.3

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

45) A city of 150,000 people has a large commercial sector bringing in businesses from the surrounding region. In 2005, there was 2.75 million square feet of commercial space available. Five years later, after a building boom, there was 5.5 million square feet of commercial space available.

Which effect will most likely occur?

- A) The equilibrium price of commercial real estate will not be effected.
- B) The increase in the supply of commercial real estate will lead to a corresponding increase in its price.
- C) The price of commercial real estate will decrease, absent a dramatic increase in demand.
- D) The increase in the supply of commercial real estate will lead to an increase in resource prices.
- E) The increase in supply will cause a corresponding increase in demand.

Answer: C

Explanation: C) Since the supply of commercial real estate has dramatically increased, unless there was a dramatic increase in demand we would expect the price of commercial real estate to decrease.

Page Ref: 12

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.4

Learning Outcome: Discuss strategies for setting and adjusting prices

Skill: Application

46) A new watch manufacturer would like to determine the market price of a new line of watches. How could the manufacturer most effectively determine the market price?

- A) Place several of the new watches on sale at a watch store and see which sells most quickly.
- B) Arrange to sell the watches in a number of diverse auctions.
- C) Set the price of one watch higher than another and see which sells the most quickly.
- D) Survey potential customers and retailers on what they think the price should be.
- E) Canvass executives from competing companies about what they think the price should be.

Answer: B

Explanation: B) Auctions are an effective way to determine market prices because consumers determine the selling price.

Page Ref: 16

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.4

Learning Outcome: Discuss strategies for setting and adjusting prices

Skill: Application



47) A new feature on the the latest Acme smart phone has made it wildly popular. Which action should Acme take to maximize profits?

- A) Increase the supply of the smart phone.
- B) Decrease the supply of the smart phone.
- C) Reduce the price of the smart phone.
- D) Maintain the current supply until demand falls.
- E) Create a shortage of the smart phone.

Answer: A

Explanation: A) Acme will want to have more phones available when demand is high.

Page Ref: 12

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.4

Learning Outcome: Discuss strategies for setting and adjusting prices

Skill: Application

48) Which of the following is NOT a likely reason why a small business in a free enterprise system should seek the ideal combination of price charged and quantity supplied?

- A) to maintain goodwill among customers
- B) to maximize profits
- C) to avoid surpluses and shortages
- D) to avoid government regulation
- E) to discourage competition

Answer: D

Explanation: D) A small business is unlikely to be a monopoly so how it sets its prices will not attract the attention of government regulators.

Page Ref: 12

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.4

Learning Outcome: Discuss strategies for setting and adjusting prices

Skill: Application

49) In a small town of 3,000 people, the number of car washes has grown from two to five in the last two months.

Which result will likely occur?

- A) The increase in supply will have no effect on the equilibrium price.
- B) The increase in supply will lead to a decrease in demand.
- C) The increase in supply will lead to a decrease in the equilibrium price.
- D) The increase in supply will lead to an increase in demand.
- E) The increase in supply will lead to an increase in equilibrium price.

Answer: C

Explanation: C) In general, greater availability of goods and services leads to a decrease in cost.

Page Ref: 12

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.4

Learning Outcome: Discuss strategies for setting and adjusting prices

Skill: Application

50) Ernesto's Pizza is about to offer customers a new variety of a personal pizza. Which of the following actions by Ernesto's Pizza would most likely prevent a surplus or a shortage of the personal pizzas in its first week?

- A) limit the supply of the personal pizza
- B) lower demand for the personal pizza
- C) set the price of substitute goods
- D) estimate the market price of the personal pizza
- E) lower the price of the pizza throughout the week

Answer: D

Explanation: D) The market price occurs where there is neither a surplus nor a shortage of supply.

Page Ref: 12

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.4

Learning Outcome: Describe the major components of effective distribution

Skill: Application

51) Which of the following is one of the elements required in private enterprise?

- A) adequate representation in the government
- B) freedom from foreign competition
- C) the opportunity for market leadership
- D) the right to ownership of property
- E) numerous regulatory agencies

Answer: D

Explanation: D) Necessary elements of capitalism include private property rights, freedom of choice, profits, and competition.

Page Ref: 14

Difficulty: Moderate

AACSB: Analytic skills

Objective: 1.4

Learning Outcome: Compare and contrast different economic systems

Skill: Application

52) In perfect competition, which of the following conditions must prevail?

- A) All firms must adhere to cost and pricing standards.
- B) The number of firms in the industry must be limited.
- C) A single firm is able to influence the price of its product.
- D) It is relatively difficult to enter the industry.
- E) All firms in a given industry must be small.

Answer: E

Explanation: E) In perfect competition, all firms in a given industry must be small, the number of firms in the industry must be large, and no single firm is powerful enough to influence the price of its product; therefore, prices are determined completely by supply and demand.

Page Ref: 14

Difficulty: Moderate

Objective: 1.4

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

53) How does monopolistic competition differ from perfect competition?

- A) There are more sellers in a market characterized by monopolistic competition.
- B) It is easier for sellers to enter a market or industry characterized by monopolistic competition.
- C) In a perfectly competitive market, products are more dissimilar.
- D) In a market characterized by monopolistic competition, individual firms have some control over price.
- E) In a perfectly competitive market, the size of the firms must be large.

Answer: D

Explanation: D) Individual firms have some control over price in monopolistic competition; in perfect competition price is determined by supply and demand.

Page Ref: 14

Difficulty: Moderate

AACSB: Analytic skills

Objective: 1.4

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

54) Which of the following is characterized by having few sellers, similar prices among sellers, and difficult market entry?

- A) oligopoly
- B) pure competition
- C) monopoly
- D) monopolistic competition
- E) state socialism

Answer: A

Explanation: A) An oligopoly has few sellers. Because there is competition between those sellers, they will offer similar prices. Because those sellers will be large and well-established, it will be difficult for new companies to enter the market.

Page Ref: 15

Difficulty: Moderate

Objective: 1.4

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

55) In an oligopoly, when one firm reduces its prices, how do other sellers react?

- A) There is no reaction from other firms to change their prices.
- B) Other firms reduce their prices also, usually quite quickly.
- C) Other firms may reduce their prices, but usually gradually.
- D) Other firms are not usually aware that price has changed.
- E) There is a combined response from other firms to stabilize prices.

Answer: B

Explanation: B) Because there are few firms competing in an oligopoly, competition between firms tends to be close, and firms thus respond quickly to price reductions by one firm. Therefore, other firms will likely quickly reduce their prices as well. For example, when an airline announces new fare discounts, others adopt the same strategy.

Page Ref: 15

Difficulty: Moderate

AACSB: Analytic skills

Objective: 1.4

Learning Outcome: Compare and contrast different economic systems

Skill: Application

56) Which of the following is the most likely pricing approach for a monopoly?

- A) Charge customers whatever you please.
- B) Give customers a real bargain on price.
- C) Charge a price that will not cause consumer demand to drop.
- D) Undercut the prices of the competition.
- E) Give customers a fair price that cannot be matched by competitors.

Answer: C

Explanation: C) A monopoly happens when one firm dominates the market. The monopolizing firm does not have to factor competitors' prices when determining its own prices, so it only needs to charge a price that will not be so high that it causes demand to drop.

Page Ref: 16

Difficulty: Moderate

Objective: 1.4

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

57) What term do economists use for the pattern of short-term expansions and contractions in the economy?

- A) business cycle
- B) aggregate output
- C) standard of living
- D) consumer price index
- E) purchasing power parity

Answer: A

Explanation: A) Short-term ups and downs are referred to as the *business cycle*.

Page Ref: 17

Difficulty: Easy

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

58) Which indicator refers to the total quantity of goods and services produced by an economic system during a given period?

- A) the business cycle
- B) aggregate output
- C) gross domestic product
- D) the consumer price index
- E) gross national product

Answer: B

Explanation: B) Aggregate output is the primary measure of growth in the business cycle.

Page Ref: 17

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

59) Azucks is a socially responsible American company engaged in the manufacture of sports shoes. The CEO cautions that there is a disadvantage associated with the company planning increased globalization of production.

Which of the following is the most likely disadvantage he is referring to?

- A) Heavy job losses can ensue in the domestic market.
- B) Greater disparities in living standards will emerge.
- C) Trade barriers will be reduced between countries.
- D) Substantial job losses will occur in developing markets.
- E) Increased competition will emerge between companies.

Answer: A

Explanation: A) Developed countries usually have higher labor costs than developing countries so some companies will choose to outsource production to a developing country in order to lower costs. This results in the loss of jobs in the developed countries where the goods were originally produced.

Page Ref: 19

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Application

60) A financial analyst has noticed a serious rise in inflation. What course of action might the financial analyst advise the government to take in order to reduce inflation?

- A) The government can lower taxes.
- B) The government can raise taxes.
- C) Encourage the government to increase spending.
- D) Encourage consumers to increase spending.
- E) Encourage the government to increase spending and lower taxes.

Answer: B

Explanation: B) Raising taxes encourages consumers to spend less, thereby curbing inflation.

Page Ref: 21

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Application

61) Which course of action should the Federal Reserve take if it wishes to reduce inflation and curb consumer spending?

- A) The Federal Reserve should buy securities.
- B) The Federal Reserve should sell securities.
- C) The Federal Reserve should decrease the reserve requirement.
- D) The Federal Reserve should lower the discount rate.
- E) The Federal Reserve should sell securities and lower the discount rate.

Answer: B

Explanation: B) Selling securities reduces the money supply, thus curbing consumer spending and bringing prices down.

Page Ref: 23

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Application

62) The Fed has opted to buy securities and lower the reserve requirement. What will most likely happen as a result of this course of action?

- A) The money supply will increase thereby stimulating the economy.
- B) The money supply will increase thereby reducing inflation.
- C) The money supply will increase thereby causing disinflation.
- D) The money supply will decrease thereby reducing the possibility of a recession.
- E) The money supply will decrease thereby reducing deflation.

Answer: A

Explanation: A) Buying securities and lowering the reserve requirement will increase the money supply, which in turn stimulates the economy.

Page Ref: 23

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Application



63) If the Fed is concerned with a potential recession, what course of action should it take?

- A) Lower the reserve requirement and sell securities.
- B) Lower the discount rate and increase the reserve requirement.
- C) Sell securities and lower the discount rate.
- D) Buy securities and lower the discount rate.
- E) Buy securities and increase the reserve requirement.

Answer: D

Explanation: D) Buying securities and lowering the discount rate increases the money supply, which encourages spending.

Page Ref: 23

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Application

64) The global business environment encompasses many international forces that influence the outcomes of companies doing business in foreign countries.

Which of the following scenarios would best count as evidence of globalization?

- A) Diamonds mined in Country X are sold on the markets in Country Y. The proceeds are then used to fund a coup against the government in Country X.
- B) A natural disaster disables factories in Country X that produce computer chips for Company Y. Company Y reduces the number of employee shifts and raises the price of its products.
- C) Farmers in Country X have lost most of their wheat crops due to a drought. The market price for wheat triples and the government pays the farmers for a percentage of the lost wheat.
- D) Country X has almost mined all of its available natural energy sources. The government has been investing in alternative energy research for years and now an efficient synthetic energy source has been developed.
- E) Country X has raised the tax on oil products. As a result more people are taking public transportation and reducing unnecessary car travel.

Answer: B

Explanation: B) Globalization is the movement toward a more interconnected and interdependent world market. One consequence of this is that countries and companies become more reliant on each other and events in one part of the world can directly affect conditions in another part of the world.

Page Ref: 6

Difficulty: Difficult

AACSB: Reflective thinking skills

Objective: 1.1

Learning Outcome: Compare and contrast different economic systems

Skill: Application

65) The CEOs of Company A and B are investigating expansion into new markets, which will provide greater trade volume.

Which scenario describes an economic environment that is most suitable for an importing-exporting opportunity?

A) Country X invests primarily in its textile industry while Country Y focuses on producing high-yield crops.

B) Company A is willing to provide parts used in the production of equipment by Company B in exchange for discounts on manufacturing equipment.

C) The southern region of Country X over-produces a wide range of produce, while few crops can be efficiently grown in the northern region.

D) Company A and Company B are exploring the possibility of a joint venture to provide goods to Country X.

E) Country X is looking to invest in foreign markets and Country Y currently has a large trade deficit.

Answer: A

Explanation: A) The economic environment refers to relevant conditions, such as import and export opportunities, that exist in the economic system in which a company operates. In the above case, importing and exporting both refer to the movement of goods between different countries. Countries X and Y focus on a particular industry, which implies that these are areas in which they have an import-export opportunity.

Page Ref: 6

Difficulty: Difficult

AACSB: Reflective thinking skills

Objective: 1.1

Learning Outcome: Compare and contrast different economic systems

Skill: Application

66) Robert has established a start-up business manufacturing a range of outdoor wear for the leisure market.

Which possible scenario would best show that Robert is positioning his business for the global business market?

- A) Robert launched a Web site for his business and hired two new employees to handle national and international shipping.
- B) Robert launched a Web site and filmed a commercial for television and recorded a radio version for local stations.
- C) Robert created a page for his business on a networking site and offered store coupons to his first 100 friends.
- D) Robert had his Web site translated into Korean in order to better serve the local Korean community.
- E) Robert took a full page ad out in the state's official tourism brochure.

Answer: A

Explanation: A) By creating a Web site, which can be viewed worldwide, and expanding his business to handle national and international shipping, Robert is actively engaging in market globalization.

Page Ref: 6

Difficulty: Difficult

AACSB: Reflective thinking skills

Objective: 1.1

Learning Outcome: Compare and contrast different economic systems

Skill: Application

67) What is a chief goal of an economic system?

- A) economic stability
- B) income equality
- C) money supply growth
- D) national debt reduction
- E) product innovation

Answer: A

Explanation: A) With stability, the amount of money available in an economic system and the quantity of goods and services produced in it are growing at about the same rate.

Page Ref: 21

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

68) Which of the following best describes *economic stability*?

- A) the measure of economic growth that compares how much a system produces with the resources needed to produce it
- B) a condition in an economic system in which the amount of money available and the number of goods and services produced are growing at about the same rate
- C) the economic condition in which a country's exports exceed its imports
- D) a relative equality between what the government owes its creditors and the revenue it gets from imports
- E) the economic value of all the products that a country exports minus the economic value of all the products it imports

Answer: B

Explanation: B) Economic stability is evident when the amount of money available and the number of goods and services produced are growing at about the same rate; inflation and unemployment, in particular, threaten economic stability.

Page Ref: 21

Difficulty: Moderate

AACSB: Analytic skills

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

69) Which of the following statements about inflation is true?

- A) The consumer price index is a good way of measuring inflation.
- B) Productivity decreases the purchasing power of consumer dollars.
- C) Inflation increases the purchasing power of consumer dollars.
- D) Localized price increases can cause inflation across the economic system.
- E) The amount of money tends to be distributed evenly during inflationary periods.

Answer: A

Explanation: A) The consumer price index is a good measurement of inflation; inflation occurs with widespread price increases.

Page Ref: 22

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

70) How would supply affect the aggregate output of an economy?

- A) Supply would decrease aggregate output.
- B) Increases in both would cause inflation.
- C) Aggregate output would grow with supply.
- D) Supply would have no direct effect on aggregate output.
- E) Aggregate output would increase the money supply.

Answer: C

Explanation: C) Supply is the amount of goods available, and aggregate output is the production of goods, so increased supply would increase aggregate output.

Page Ref: 17

Difficulty: Moderate

Objective: 1.4

Learning Outcome: Explain how economic performance is monitored

Skill: Synthesis

71) Which of the following best describes what the *consumer price index* is used to indicate?

- A) the average wage rate for a given region
- B) the economic performance of key consumer product companies
- C) the changes in the cost of consumer products over time
- D) the percentage of consumers in the total population looking for work
- E) the number of price increases within a given period of time

Answer: C

Explanation: C) The consumer price index is a measure of the prices of typical products purchased by consumers living in urban areas. It is expressed as a percentage of prices as compared to a base period.

Page Ref: 22

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

72) Which of the following is a likely cause of increased prices for products, decreased purchasing power, and decreased profit margins?

- A) low unemployment
- B) stagnant wages
- C) declining living standards
- D) cyclical inflation
- E) limited credit

Answer: A

Explanation: A) Potential results of low unemployment include increased prices, decreased purchasing power, and decreased profits.

Page Ref: 22

Difficulty: Difficult

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Synthesis

73) What type of policy is made up of fiscal and monetary policy?

- A) trade
- B) employment
- C) stabilization
- D) tax
- E) foreign

Answer: C

Explanation: C) A stabilization policy is a government goal to smooth out fluctuations in output and unemployment and to even out prices.

Page Ref: 23

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

74) In the city of Westminster, Christmas trees are being sold for \$25. At this price, buyers are able to satisfy their demand, though some trees remain unsold. What is the term used to describe this market condition?

- A) surplus
- B) stoppage
- C) shortage
- D) demand deficit
- E) equilibrium price

Answer: A

Explanation: A) A surplus is defined as a situation in which quantity supplied exceeds quantity demanded.

Page Ref: 13

Difficulty: Moderate

Objective: 1.4

Learning Outcome: Explain how economic performance is monitored

Skill: Application

75) In the United States, milk is produced on thousands of farms, with no producer dominating the market. Producers sell milk at the going price and are unable to influence this price. Millions of gallons of milk are purchased every day. What type of competition is the market for milk?

- A) a monopoly
- B) an oligopoly
- C) perfect competition
- D) monopolistic competition
- E) a cooperative

Answer: C

Explanation: C) In perfect competition, there are many sellers who are not individually powerful enough to influence price.

Page Ref: 14

Difficulty: Difficult

Objective: 1.4

Learning Outcome: Compare and contrast different economic systems

Skill: Application

76) Which of the following best gives the meaning of the term *gross domestic product*?

- A) total quantity of goods and services produced by an economic system
- B) total quantity of goods that a country's citizens can purchase with the currency used in their economic system
- C) conditions of the economic system in which an organization operates
- D) total value of all goods and services produced within a given period by a national economy through domestic factors of production
- E) indicators of available goods and services produced within a specific domestic market

Answer: D

Explanation: D) Gross domestic product (GDP) is the total value of all goods and services produced within a given period by a national economy through domestic factors of production; this figure does not include goods and services produced by domestic firms overseas.

Page Ref: 17

Difficulty: Difficult

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

77) Which of the following best gives the meaning of the term *business cycle*?

- A) the conditions of the economic system in which an organization operates
- B) the total quantity and quality of goods and services that a country's citizens can purchase with the currency used in their economic system
- C) the measure of economic growth that compares how much a system produces with the resources needed to produce it
- D) the number of businesses started during a given time period
- E) the pattern of short-term ups and downs in an economy

Answer: E

Explanation: E) A business cycle is represented in the short-term ups and downs in the economy, as measured by prosperity, recession, and so on.

Page Ref: 17

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Application

78) Which of the following best gives the meaning of the term *gross national product*?

- A) total quantity of goods and services produced by an economic system
- B) total quantity of goods and services produced within a given period by a national economy, not including foreign production
- C) total value of all goods and services produced within a given period by a national economy through domestic factors of production
- D) total value of all goods and services produced within a given period regardless of where the factors of production are located
- E) total value of all goods and services that are exported

Answer: D

Explanation: D) Gross national product includes even the value of goods and services produced by domestic companies abroad.

Page Ref: 18

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept



79) Which of the following best describes *nominal GDP*?

- A) total quantity of goods and services produced by an economic system
- B) total value of all goods and services produced within a given period by a national economy through domestic factors of production measured in current dollars or with all components valued at current prices
- C) total value of all goods and services produced within a given period by a national economy regardless of where the factors of production are located
- D) total value of all goods and services produced within a given period by a national economy through domestic factors of production adjusted to account for changes in currency values and price changes
- E) total quantity of goods and services that are imported within a given period of time

Answer: B

Explanation: B) Nominal GDP is not adjusted to make up for inflation and/or changes in currency values.

Page Ref: 18

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

80) Which of the following would be included in the gross domestic product of Brazil?

- A) the profits earned by a U.S.-owned automobile plant in Brazil
- B) the profits earned by a Brazilian coffee company operating in the United States
- C) the profits earned by a Brazilian coffee company operating in Peru
- D) the profits earned by U.S. suppliers to Brazil operating in the United States
- E) the profits earned by Peruvian companies operating outside Brazil

Answer: A

Explanation: A) Gross domestic product refers to the value of goods and services produced in a given period domestically.

Page Ref: 18

Difficulty: Difficult

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Application

81) Honata Automobiles is a South Korean-owned company. Honata has factories in Indonesia and Brazil. Which of the following is/are affected by the production of Honata automobiles?

- A) Indonesia, Brazil, and South Korea's GDP
- B) Indonesia and Brazil's GDP
- C) South Korea's GDP
- D) Indonesia and Brazil's GNP
- E) Indonesia, Brazil, and South Korea's GNP

Answer: B

Explanation: B) GDP measures goods and services produced within a country regardless of where the companies are based.

Page Ref: 18

Difficulty: Difficult

AACSB: Reflective thinking skills

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Application

82) Which of the following best describes *purchasing power parity*?

- A) total quantity of goods and services produced by an economic system
- B) total quantity of goods and services that can be purchased with one paycheck
- C) total quantity of goods and services that could have been purchased if one's pay rose in the same proportion as inflation
- D) the principle that exchange rates are set so that prices of similar products in different countries are about the same
- E) the principle that a market economy determines supply and demand for consumer products

Answer: D

Explanation: D) Purchasing power parity gives us a good idea of what people can actually buy with the financial resources allocated to them by their respective economic systems.

Page Ref: 19

Difficulty: Difficult

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

83) Which is the best explanation for why standard of living only increases through productivity?

- A) The more goods that are available, the lower prices will be.
- B) More goods are available without having to come by additional resources.
- C) Productivity increases the money supply in an economy.
- D) Purchasing power increases when there is more consumer choice.
- E) Prices are determined by the standard of living.

Answer: B

Explanation: B) Productivity is the amount of goods that can be made using a given amount of resources. If it takes more resources to produce more goods, prices will not decrease as long as demand keeps pace. But if more goods can be made using the same resources, prices will go down and purchasing power will increase.

Page Ref: 19

Difficulty: Difficult

AACSB: Reflective thinking skills

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Synthesis

84) Why would a government most likely be concerned about its country carrying a trade deficit?

- A) A trade deficit means that the country's productivity is low.
- B) A trade deficit means local companies do not have enough competition.
- C) A trade deficit ties up money that could be used for economic growth.
- D) A trade deficit decreases demand for goods overall.
- E) A trade deficit means that consumers do not have enough purchasing power.

Answer: C

Explanation: C) A trade deficit implies a carrying of debt; when there is a trade deficit imports are not paid for in full.

Page Ref: 20-21

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Application

85) If, in the long run, international trade improves the standards of living in participating countries, why might some countries want to place trade barriers such as extra taxes on imported products?

- A) Imported products compete with domestic products and thus put pressure on local business.
- B) Imported products are usually not as good quality as domestically made products.
- C) Generating government revenue is often more economically valuable than free trade.
- D) This is necessary to keep a country's currency strong.
- E) International trade tends to lead to political tension.

Answer: A

Explanation: A) In the course of international trade, jobs are often initially lost in those industries in which a country does not have a comparative advantage. Trade barriers are used as a way to protect these industries from strenuous competition.

Page Ref: 20

Difficulty: Difficult

AACSB: Reflective thinking skills

Objective: 1.5

Learning Outcome: Explain the benefits and challenges of engaging in international business

Skill: Synthesis

86) Through various stimulus programs, the U.S. government injected money into the economy during the 2008-2009 recession. What was the concern that this type of action would lead to?

- A) increased labor costs
- B) increased spending
- C) increased unemployment
- D) increased inflation
- E) increased trade imbalance

Answer: D

Explanation: D) Some experts feared that increasing the money supply might also lead to inflation.

Page Ref: 23

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Application

87) The government is concerned that the economy is being stifled by low consumer spending. Which course of action should the Federal Reserve take if it wishes to improve the economy?

- A) The Federal Reserve should buy securities.
- B) The Federal Reserve should sell securities.
- C) The Federal Reserve should increase the reserve requirement.
- D) The Federal Reserve should increase the discount rate.
- E) The Federal Reserve should sell securities and lower the discount rate.

Answer: A

Explanation: A) Buying securities will increase the money supply, which will increase consumer spending, thereby improving the economy.

Page Ref: 23

Difficulty: Difficult

AACSB: Reflective thinking skills

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Application

88) What is a business?

Answer: A business is an organization that provides goods or services that are then sold to earn profits.

Explanation: A business is defined as an organization that provides goods or services that are then sold to earn profits.

Page Ref: 4

Difficulty: Easy

Objective: 1.1

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

89) Explain what is meant by the term *profits*.

Answer: Profits are what is left over after expenses of a business have been subtracted from revenues.

Explanation: Profits are the differences between a business's revenues and its expenses.

Page Ref: 5

Difficulty: Easy

Objective: 1.1

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

90) What is meant by the term *capital*?

Answer: Capital is the financial resources needed to start a business.

Explanation: Capital is needed for a business to obtain labor and other resources.

Page Ref: 7

Difficulty: Easy

Objective: 1.3

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

91) What is the main measure of growth in the business cycle?

Answer: The main measure of growth in the business cycle is aggregate output.

Explanation: Aggregate output is the total quantity of goods and services produced by an economic system during a given period and is used to measure economic growth.

Page Ref: 17

Difficulty: Easy

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

92) There is a trend toward mixing business and entertainment. This is an example of which element of the external environment?

Answer: The trend toward mixing business and entertainment is an example of the influence of the sociocultural environment.

Explanation: The sociocultural environment covers the values important to consumers. In this example, consumers are responding positively to business transactions being made more entertaining.

Page Ref: 7

Difficulty: Moderate

AACSB: Analytic skills

Objective: 1.2

Learning Outcome: Compare and contrast different economic systems

Skill: Application

93) Explain what happens when the demand curve intersects with the supply curve.

Answer: The intersection marks the equilibrium, or market price. At this price, there will be neither a shortage nor surplus. Over time, markets tend to price products at the equilibrium price.

Explanation: At the intersection of the demand and supply curve, we have the equilibrium, or market price. At this price, there will be neither a shortage nor surplus. Over time, markets tend to price products at the equilibrium.

Page Ref: 12

Difficulty: Moderate

AACSB: Analytic skills

Objective: 1.4

Learning Outcome: Discuss strategies for setting and adjusting prices

Skill: Concept

94) Explain what is meant by purchasing power parity.

Answer: Purchasing power parity is the principle that exchange rates are set so that the prices of similar products in different countries are about the same.

Explanation: Purchasing power parity is a measure that gives us a much better idea of what people can actually buy with the financial resources allocated to them by their respective economic systems.

Page Ref: 18

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Discuss strategies for setting and adjusting prices

Skill: Concept

95) A chief goal of an economic system is stability. What is meant by *stability* in an economic system?

Answer: Stability is a condition in which the amount of money available in an economic system and the quantity of goods and services produced in it are growing at about the same rate.

Explanation: Stability is a chief goal of an economic system and can be undermined by inflation and unemployment.

Page Ref: 21

Difficulty: Moderate

AACSB: Analytic skills

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

96) How does inflation affect purchasing power?

Answer: Inflation is the occurrence of widespread price increases throughout an economic system. Purchasing power declines as a result of the increased prices associated with inflation.

Explanation: Inflation occurs when an economic system experiences widespread price increases, which has a negative impact on purchasing power.

Page Ref: 21

Difficulty: Moderate

AACSB: Analytic skills

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

97) What is measured by the consumer price index (CPI)?

Answer: The consumer price index measures the prices of typical products purchased by consumers living in urban areas.

Explanation: The consumer price index is expressed as a percentage of prices as compared to a base period.

Page Ref: 22

Difficulty: Easy

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

98) What is cyclical unemployment?

Answer: Cyclical unemployment is unemployment that results from a vicious cycle in which spending drops due to unemployment and employers have to cut back, resulting in more unemployment.

Explanation: Cyclical unemployment is often part of the downturn of the business cycle.

Page Ref: 22

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

99) What is a recession?

Answer: A recession is a period during which aggregate output, as measured by real GDP, declines.

Explanation: A recession is characterized by producers needing fewer employees.

Page Ref: 23

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

100) How does a planned economy differ from a market economy?

Answer: A planned economy relies on a centralized government to control all or most factors of production and to make all or most production and allocation decisions. In a market economy, individuals control production and allocation decisions through supply and demand.

Explanation: Planned economies are systems in which the government owns and operates all or most factors of production. Market economies rely on capitalism and free enterprise to create an environment in which producers and consumers are free to buy and sell what they choose.

Page Ref: 10

Difficulty: Difficult

Objective: 1.3

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

101) What is socialism?

Answer: Socialism is a partially planned system in which the government owns and operates selected major industries. In such mixed market economies, the government may control banking, transportation, or manufacturing industries, for example. Smaller businesses, such as clothing stores and restaurants, are privately owned.

Explanation: In socialist systems the government owns and operates selected major industries.

Page Ref: 11

Difficulty: Difficult

AACSB: Analytic skills

Objective: 1.3

Learning Outcome: Compare and contrast different economic systems

Skill: Concept



102) Describe monopolistic competition.

Answer: In a market characterized by monopolistic competition, there are fewer sellers than in perfect competition. Sellers will attempt to differentiate their product from those of their competitors. Product differentiation gives sellers some control over prices. Monopolistically competitive businesses can be large or small and can enter and exit the market easily.

Explanation: In monopolistic competition, there are numerous sellers trying to make their products appear to be different from those of competitors.

Page Ref: 15

Difficulty: Moderate

AACSB: Analytic skills

Objective: 1.4

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

103) Differentiate between gross national product (GNP) and gross domestic product (GDP).

Answer: Both gross national product (GNP) and gross domestic product (GDP) measure the economic performance of a national economy. Gross domestic product refers to the total value of all goods and services produced within a given period by a national economy through *domestic* factors of production. On the other hand, gross national product measures the total value of goods and services produced by a national economy within a given period regardless of where the factors of production are located.

Explanation: GDP is the total value of all goods and services produced domestically within a given period by a national economy. GNP is the total value of goods and services produced by a national economy within a given period regardless of where the factors of production are located.

Page Ref: 17-18

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

104) Explain the role of both profit-seeking businesses and non-profit organizations in the overall "meaning of business."

Answer: Businesses are organizations that provide goods and services that are then sold to earn profits. Indeed, the prospect of earning profits, the difference between a business's revenue and its expenses, is what encourages people to open and expand businesses. After all, profits are the reward owners get for risking their money and time. The right to pursue profits distinguishes a business from non-profit organizations, such as universities, hospitals, and government agencies, that run in much the same way but that generally do not seek profits. Whereas profits may be considered the final reward in profit-seeking businesses, the final reward for non-profit organizations might be operational efficiency, for example.

Page Ref: 4

Difficulty: Moderate

Objective: 1.1

Skill: Concept

105) How does the external environment affect business?

Answer: All businesses operate within the context of a larger external environment. The external environment consists of everything outside a business's boundaries that might affect it. The domestic business environment refers to the environment in which a firm operates, conducting operations and generating revenues. The global business environment includes the international forces affecting a business. The technological environment refers to human knowledge, work methods, physical equipment, electronics and telecommunications, and various processing systems used to conduct a business. The relationship between business and government describes the political-legal environment. The sociocultural environment includes the customs, mores, values, and demographic characteristics of the society in which a business conducts operations. Finally, the economic environment refers to the economic conditions which exist in the economic system in which a company operates.

Page Ref: 5-6

Difficulty: Moderate

Objective: 1.2

Skill: Concept

106) A nation's economic system is its system for allocating its resources among its citizens, both individuals and organizations. Explain how the three economic systems allocate their resources.

Answer: A nation's resources, often referred to as the *factors of production*, include labor, capital, entrepreneurs, physical resources, and information resources. An economic system is defined by how it manages and allocates these factors of production. In a planned economy, for example, the factors of production are government owned and controlled. In a market economy, such as that of the United States, individual producers and consumers control production and allocation by creating combinations of supply and demand. In a mixed market economy, which features characteristics of both a planned and a market economy, there is some government control of some factors of production, often through the nation's major industries, such as transportation, communication, and information, alongside some private ownership.

Page Ref: 10-11

Difficulty: Moderate

Objective: 1.3

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

107) Explain the roles of demand and supply in a market economy.

Answer: On all economic levels of a market economy, decisions about what to buy and what to sell are determined primarily by the forces of demand and supply. Demand is the willingness and ability of buyers to purchase a product; supply is the willingness and ability of producers to offer a good or service for sale. The law of demand states that buyers will purchase more of a product as its price drops and less as its price increases. The law of supply states that producers will offer more of a product for sale as its price rises and less as its price drops.

Page Ref: 11-13

Difficulty: Difficult

Objective: 1.4

Skill: Concept

108) Explain the role of private enterprise in a market economy. Include an explanation of the elements that comprise free enterprise.

Answer: Market economies rely on a private enterprise system, one that allows individuals to pursue their own interests with minimal government restriction. Private enterprise requires four elements: private property rights, freedom of choice, profits, and competition. Private property rights allow the ownership of resources used to create wealth to be in the hands of individuals. Freedom of choice allows a number of freedoms in the market, including the freedom for a worker to sell his or her labor to any employer he or she chooses, the freedom to choose which products and brands to buy, and the freedom for producers to choose whom they hire and what they will produce. Profits are the incentives for entrepreneurs to assume the risks of business ownership. Competition occurs when businesses vie for the same resources and customers; competition is a driver of quality and price levels. All four of these elements are necessary to a market economy.

Page Ref: 14

Difficulty: Difficult

Objective: 1.4

Learning Outcome: Compare and contrast different economic systems

Skill: Application

109) Compare and contrast the four degrees of competition in a private enterprise system.

Answer: The four degrees of competition include perfect competition, monopolistic competition, oligopoly, and monopoly. In perfect competition, all firms in an industry are small but the number of firms in the industry is large. No single firm is powerful enough to influence price; therefore, price is determined by such market forces as supply and demand. The products in a perfectly competitive market are so similar that buyers view them as identical to those of other firms. In monopolistic competition, there are many buyers and sellers. Often, sellers attempt to differentiate their products and services from others through design, styling, advertising, or the use of brand names; this often gives sellers some control over prices. Monopolistically competitive businesses face few market entry/exit barriers. In an oligopoly, an industry has only a handful of sellers, who are generally quite large. Market entry is difficult because large capital outlays are needed for new start-ups. In an oligopoly, the actions of one firm tend to affect the actions of all firms; for example, when one firm changes price, all firms tend to change price rather quickly. A monopoly exists when an industry or market has only one producer that dominates the entire market. Though monopolies are illegal in the United States, natural monopolies—such as utilities companies—are government-regulated; they are allowed to exist since one such company can often efficiently supply all needed goods or services.

Page Ref: 14-16

Difficulty: Difficult

AACSB: Analytic skills

Objective: 1.4

Learning Outcome: Compare and contrast different economic systems

Skill: Synthesis

Expert Electronics is a manufacturer of computers on the large, but isolated, island nation of New Vermont. Although imports are extremely limited because of difficult navigation to and from New Vermont, there are a handful of computer manufacturers in addition to Expert Electronics. While the government provides some services, such as public education and a well-maintained road system, almost all businesses are privately owned. Home ownership is unusually high, with 80 percent of all families owning their own home. Expert Electronics is selling a state-of-the-art desktop computer system for 1,299 veros (the local currency). At this price, Expert Electronics is able to fill all orders, but they have no waiting list.

110) What type of economic system exists in New Vermont? Support your conclusions.

Answer: It appears that New Vermont operates under a market-based, capitalist economy. In a market economy, there is private ownership of the factors of production. As mentioned in the case, almost all businesses are privately owned and people are able to own their own homes. The political basis for a market economy is capitalism, which sanctions the private ownership of the factors of production and encourages entrepreneurship by offering profits as an incentive.

Page Ref: 8

Difficulty: Moderate

Objective: 1.3

Learning Outcome: Compare and contrast different economic systems

Skill: Application

111) If New Vermont is operating under a capitalistic, market-based economy, what four elements must be present in the economic system to make it work?

Answer: Such systems require private property rights, freedom of choice, profits, and competition.

Page Ref: 11

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Concept

112) A Danish company has built a production facility on the island of New Vermont. Will the value of the goods produced by the Danish company be included in New Vermont's GNP?

Explain.

Answer: The value of the goods won't be included in New Vermont's GNP but will be included in its GDP because they are produced domestically—that is, in New Vermont.

Page Ref: 14

Difficulty: Moderate

AACSB: Analytic skills

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Application

113) Based on the concepts of demand and supply, how is Expert Electronics pricing its computer systems?

Answer: It appears that Expert Electronics is pricing its computers at the equilibrium price, the intersection of the demand and supply curves. At the equilibrium price, the quantity of goods demanded and the quantity of goods supplied is equal.

Page Ref: 9

Difficulty: Moderate

Objective: 1.4

Learning Outcome: Discuss strategies for setting and adjusting prices

Skill: Concept

114) How would you characterize the level of competition for computers in New Vermont? How are prices set in this type of competitive environment?

Answer: Because there are only a few sellers, the market for computers in New Vermont is best described as an oligopoly. In an oligopoly, the prices of comparable products are usually very similar.

Page Ref: 11

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Application

115) If Expert Electronics cuts the prices for its computer system, how will competitors respond?

Answer: In an oligopoly, when one firm cuts prices or offers incentives to increase sales, the others usually protect sales by doing the same.

Page Ref: 12

Difficulty: Moderate

Objective: 1.4

Learning Outcome: Discuss strategies for setting and adjusting prices

Skill: Concept

116) New Vermont underwent a recession two years ago. How might New Vermont's aggregate output have been affected?

Answer: A recession is defined as a period during which aggregate output, as measured by GDP, declines. Therefore, New Vermont's aggregate output would have declined.

Page Ref: 18

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Explain how economic performance is monitored

Skill: Concept

117) Name one factor that may be detrimental to Expert Electronics' productivity.

Answer: Productivity is the measure of economic growth that compares how much a system produces with the resources needed to produce it. Because New Vermont's location prevents the efficient import and export of products, manufacturers are depending more on local materials, which may not provide the highest levels of productivity.

Page Ref: 15

Difficulty: Moderate

Objective: 1.5

Learning Outcome: Compare and contrast different economic systems

Skill: Application

AB Distributors is a company that serves as a shipping intermediary for other companies. Its sales revenue has increased from the previous year. Jonathan, a sales manager at AB, says, "Since the company has increased its revenue, it is now more profitable."

118) Which of the following, if true, would most strongly support Jonathan's contention?

A) AB Distributor is a relatively new company.

B) AB Distributor is a for-profit company.

C) AB Distributor's costs have decreased from the previous year.

D) AB Distributor's competitors have had increased revenue.

E) AB Distributor has hired more employees recently.

Answer: C

Explanation: C) Since profit is revenue minus costs, a decrease in costs while revenue increases would certainly entail higher profitability. Choice A would not be directly relevant to whether the company is more profitable, since it could be more or less profitable regardless of whether the company is new. Choice B simply states that the company's objective is to make profit; it does not tell whether the company has actually succeeded in its profitability. Choice D is not directly relevant to whether the company has been profitable; it may be profitable or unprofitable while its competitors have also increased revenue. Choice E might weaken the claim since it would involve an increase in costs.

Page Ref: 4

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.1

Skill: Critical Thinking

119) Which of the following, if true, would most weaken Jonathan's contention?

- A) AB Distributor's clients are happy with the company's services.
- B) Shipping costs for the industry have significantly increased over the last year.
- C) AB Distributor's employees are dissatisfied with the company's working conditions.
- D) The shipping intermediary industry has experienced a slowdown overall.
- E) Many of AB Distributor's employees are new to the business.

Answer: B

Explanation: B) This would indicate that AB Distributor's shipping costs have increased as well, which would mean that the increase in revenue may be matched by the increase in costs, which indicates that, since profitability is revenue minus costs, the company may not have increased its profitability. Choice A simply indicates that the company is doing business well by its customers and does not indicate the company may not be profitable. Choice C indicates internal problems with the company, but does not indicate that its costs are high and thus does not weaken the case that it is profitable. Choice D does not weaken the case that the company is more profitable, since we already know that AB Distributor's revenue has increased, even if that of other similar companies has not. Choice E is not relevant to whether the company is profitable, given the information in the scenario.

Page Ref: 4

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.1

Skill: Critical Thinking

120) Which of the following points out a flaw in Jonathan's reasoning?

- A) Information about the company's expenses is necessary to tell whether it is profitable.
- B) AB Distributor may have lost money the previous year.
- C) Most of AB Distributor's employees are relatively new.
- D) Not all of the revenue may contribute toward profits.
- E) Many of AB Distributor's competitors may not be doing as well.

Answer: A

Explanation: A) Profitability is revenue minus costs, so not knowing whether costs have increased is a hindrance to knowing whether the company is profitable. Choice B is not directly relevant to how profitable the company is for the current year. Choice C does not undermine the fact that the company's revenues have increased. Choice D cannot undermine the contribution of revenues to profitability, because by definition all revenues contribute to profitability. Choice E is incorrect because it is not relevant to whether AB Distributor has been profitable.

Page Ref: 4

Difficulty: Difficult

AACSB: Reflective thinking skills

Objective: 1.1

Skill: Critical Thinking

121) Another manager at AB Distributor, Shawna, suggests that if the company's revenue had not increased, it would not have been able to increase its profits. Which of the following points out a flaw in Shawna's reasoning?

- A) Other similar companies have increased their profits, too.
- B) Revenue is not always relevant to figuring profitability.
- C) Profitability is not the only objective of the company.
- D) The company can increase revenue only by cutting costs.
- E) It is possible to increase profits by lowering costs.

Answer: E

Explanation: E) Profitability is revenue minus costs, so there are two ways of increasing profits: increasing revenue or lowering costs. Choice A is an issue that is not directly relevant to how AB Distributors can increase its profits. Choice B is incorrect because revenue is always relevant to figuring profitability. Choice C is not relevant to whether or how the company can increase its profits. Choice D is not necessarily true, and if it were true it would support Shawna's contention that increasing revenue was necessary to increase its profits.

Page Ref: 4

Difficulty: Difficult

AACSB: Reflective thinking skills

Objective: 1.1

Skill: Critical Thinking



Flavor Foods runs The Hungry Cow—a chain of fast food restaurants located all over the country. The chain has a loyal customer base and is well-known for its signature dishes like the Big Bite Burger, Springy Fries, and the Orange Float. The company is faced with a critical decision: Should it expand its operations into China?

122) Which of the following, if true, would strengthen the argument for competing in the Chinese market?

- A) Changes in exchange rates can affect the value of sales made in different countries.
- B) Even global brands typically choose to tailor their offerings according to the tastes of consumers in different countries.
- C) The Big Bite Burger has a higher selling price than other items on The Hungry Cow's menu, but it is not the most profitable item because of the cost of its ingredients.
- D) The Hungry Cow's research indicates that reaching new customers in domestic markets will be more expensive than doing so in emerging markets.
- E) Chinese companies tend not to pursue the franchise option when attempting to expand into other countries.

Answer: D

Explanation: D) Expanding into the Chinese market is a complicated decision involving many factors. One of those is the cost of reaching new customers. If Choice D is true, then the cost of reaching customers in emerging markets (China is one of those markets) is relatively low, and so Choice D strengthens the argument. Choice A suggests that expanding would be risky, which doesn't help the argument. Choice B suggests that The Hungry Cow would have to make some changes in order to compete in China, which makes entering China sound harder. Choice C tells us nothing about China or the opportunities there. Choice E refers to the wrong subject. The issue here is expansion into China.

Page Ref: 6

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.2

Skill: Critical Thinking

123) Which of the following, if true, would weaken the argument for competing in the Chinese market?

- A) An American fast food chain found that the time to recoup its investments in China was greater under the franchise model as opposed to the corporate chain store model.
- B) Chinese government policies can impose lengthy delays on businesses seeking food sale licenses.
- C) Studies show that modern Chinese consumers are more likely than previous generations to dine outside the home.
- D) When choosing a restaurant, Chinese consumers seek benefits beyond simple food quality.
- E) Expanding into every market within China would require more resources than The Hungry Cow has at its disposal.

Answer: B

Explanation: B) While the Chinese market sounds attractive, it would be less attractive if Choice B were true and the government could hold up development while sorting out licensing issues. Choice A is on the wrong subject. The issue here is whether expansion into China is a good idea, not the specifics of how to expand. Choice C would only strengthen the argument by suggesting that demand will be strong. Choice D makes no clear difference, because we can't tell whether The Hungry Cow is positioned to offer the benefits that Chinese customers seek. Choice E is a reason not to expand everywhere, but that is not a reason to avoid China entirely.

Page Ref: 6

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.2

Skill: Critical Thinking

In the past, only India's elite could afford to buy a car. But recent dramatic changes in India's economy have produced a growing middle class and rapidly rising incomes. Now, to meet the new demand, established automakers are introducing smaller, more affordable vehicles into India. But they will have to find a way to compete with India's Tata Motors, which has unveiled the least expensive car ever in this market, the Tata Nano. The Nano sells for only 100,000 rupees (about US \$2,200). It seats four passengers, gets 50 miles per gallon, and travels at a top speed of 60 miles per hour.

124) Based on the information above, Tata most likely believed that as a result of recent changes in India's economy, what would be true of a growing number of Indian consumers?

- A) They had become even more cost-conscious than ever before.
- B) They would be willing and able to spend 100,000 rupees on a car.
- C) They would choose a vehicle with high fuel efficiency primarily because of concern about the natural environment.
- D) They will eventually prefer models similar to those currently available in the U.S. and Europe.
- E) They will place a higher value on car safety than fuel economy.

Answer: B

Explanation: B) The changes to India's economy produced a growing middle class and rising incomes. Tata responded to the new demand by producing a new car that sells for 100,000 rupees. Therefore, Tata must believe that a growing number of Indian consumers are willing and able to pay 100,000 rupees for a car, as Choice B indicates. Choice A goes against the discussion, and Indians have more money now. Choice C brings in concern for the environment, which is possible but not mentioned by the passage. Choice D speculates about the future, but the passage doesn't. Choice E, if anything, goes against the passage because the Tata sounds like a fuel-efficient car, but not necessarily a safe one.

Page Ref: 12

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.4

Skill: Critical Thinking

Allied Industries is a manufacturer of basic building materials like ready mix concrete, aggregates, and other construction material. It sells its products primarily to three large real estate companies. One of these companies, Cicada Corporation, has asked for a huge discount for future orders. Allied's CEO feels that this may be a good move to retain a customer, but many senior managers think otherwise.

125) Assume that Allied has required Cicada to not handle any of Allied's competitors' products. Which of the following most strongly suggests that this arrangement is legal?

- A) The pricing demands of Cicada have forced many building suppliers out of business.
- B) Companies similar to Allied have demonstrated strong financial performance in recent years.
- C) Cicada often sells groups of homes to institutions that then resell them to individual consumers.
- D) In the past, Cicada and Allied were part of the same company.
- E) Monopolistic competition is encouraged by the government in some cases.

Answer: B

Explanation: B) Exclusive arrangements are most likely to be illegal when they lessen competition, create a monopoly, or are not entered voluntarily. Choice B suggests that Allied has active and successful competitors, which in turn suggests that there's no monopoly here, making it more likely that the arrangement is legal. Choice A suggests a lessening of competition, which could only make the arrangement sound illegal. Choice C doesn't matter. The number of sellers in the supply chain isn't an important factor when it comes to exclusive dealing. Choice D could only suggest some kind of secret connection between the companies, which wouldn't help in the defense of the requirement. Choice E doesn't matter, because monopolistic competition is not encouraged in this context.

Page Ref: 15

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.4

Skill: Critical Thinking

Many companies start as nichers to get a foothold against larger competitors and then grow into broader competitors. Enterprise Rent-A-Car began by building a network of neighborhood offices rather than competing with Hertz and Avis in airport locations. Enterprise is now the nation's largest car rental company.

126) Which of the following is best supported by the statements above?

- A) The best path to long-term growth is to avoid confrontation with larger competitors for as long as possible.
- B) It is generally better to confront one established competitor at a time rather than many at once.
- C) Even when competing in a niche, a company should act in every respect as if it is targeting every market segment.
- D) The car rental industry is the best example for niche companies to consider when evaluating how to grow into prominence.
- E) A company's initial goals do not place limits on its long-term success.

Answer: E

Explanation: E) The only safe inference here is Choice E. Enterprise started small and had modest aims, but it is now the largest car rental company. So the case of Enterprise is evidence for the notion that your initial goals don't determine your ultimate fate. Choice A goes too far. It's not even clear that Enterprise avoided confrontation as long as possible, and even if it did, Choice A's claim is too strong. The case is about Enterprise and not what must be the case for all companies. Choice B: We don't know if Enterprise took on competitors one at a time or all at once. Choice C goes against the passage; Enterprise started local. Choice D: This might be a good example, but there may be better ones out there.

Page Ref: 8

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.3

Skill: Critical Thinking

Anon Corporation is a manufacturer of Widgets. Faced with increasing input material costs, the company is contemplating a price increase in the range of 15-20 percent. There are significant disagreements among senior personnel in the company about this move.

127) Which of the following, if true, would strengthen the argument in favor of a price increase?

- A) Substitutes for Widgets are available in the market.
- B) The price of materials consumed along with Widgets has gone up.
- C) A change in the environment is likely to stimulate overall demand for Widgets.
- D) Competitors have announced that they intend to keep prices at current levels.
- E) Relaxation of import restrictions would lead to foreign competitors flooding the market.

Answer: C

Explanation: C) If overall demand is expected to go up, Choice C, people will be more willing to pay high prices. So Choice C supports the case for a price increase. Choice A weakens the argument. If substitutes are available, people would be more likely to choose those substitutes if Anon raised its prices. Choice B is relevant to the supply curve but not the demand curve. Increased supply costs do not by themselves make customers willing to pay more. Choice D, if anything, goes against the price increase argument by suggesting that consumers will have lower-priced options. Choice E would normally result in more options (often, lower-priced options) for consumers. This would undercut the case for a price increase.

Page Ref: 12

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.4

Skill: Critical Thinking

128) Which of the following, if true, would weaken the argument for a price increase?

- A) The input costs of raw materials are expected to increase further in the coming months.
- B) Customers are loyal to the brand mainly because they believe in the quality of ingredients used.
- C) Anon's competitors have announced an increase in prices.
- D) One of Anon's major competitors has just declared bankruptcy.
- E) Market research done by the company reveals that demand for Widgets is readily affected by the price.

Answer: E

Explanation: E) If the quantity demanded changes greatly with price, as Choice E indicates, an increase in prices will lead to greatly reduced sales. Choice A suggests that the pressure to raise prices is going to increase in the future. This sounds like it would strengthen the case for a price increase, but even so Choice A doesn't do the job because it doesn't tell us how consumers will react. Choices B, C, and D would strengthen the argument for a price increase by suggesting that customers would be willing to pay a higher price, Choice B, or that customers will have less access to low-cost options, Choices C and D.

Page Ref: 12

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.4

Skill: Critical Thinking

129) Assuming other factors remain constant, Anon would have the most power to raise prices if Widgets were which of the following?

- A) life-saving drugs
- B) automobiles
- C) beverages
- D) toys
- E) jewelry

Answer: A

Explanation: A) Companies have the most power to charge high prices when their products or services are absolutely necessary. People will be more likely to pay high prices when their health is at stake, so Anon would have the most power if Widgets were life-saving drugs, Choice A.

The other choices involve goods that have plenty of substitutes and/or are not clearly necessary.

Page Ref: 12

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.4

Skill: Critical Thinking

The economy in the African nation Sponeto has been stagnant for a long time. The government and central bank of Sponeto have been considering options for what can be done to help stimulate investment and growth in the economy.

130) The Sponeto national bank advocates increasing the money supply to encourage investment within the country. Which of the following, if true, would strengthen the case that this will cause inflation?

- A) Jobs will be created.
- B) Banks will lower interest rates.
- C) Wages will decrease.
- D) Foreign investment will be discouraged.
- E) Only low-technology sectors will benefit.

Answer: B

Explanation: B) Increasing the money supply would cause banks to lower interest rates, since money is less scarce, which tends to lead to higher prices and inflation. The creation of jobs (Choice A) in a growing economy may be accompanied by inflation but does not in itself cause inflation. Choices C and D would not be associated with an inflationary economic environment. Choice E would not strengthen the case that increasing the money supply would cause inflation.

Page Ref: 17

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.5

Skill: Critical Thinking

131) Many in the Sponeto government agree that increasing the money supply to the nation's economy would be of significant help to the country. The national bank's reserve, however, is short on the funds needed, and suggests asking for them from the International Monetary Fund (IMF). Which of the following, if true, would strengthen the case for this course of action?

- A) The IMF has been known to force donor countries to drop tariffs put in place to protect domestic industries.
- B) The IMF has been known to force donor countries to privatize national companies.
- C) The IMF contributes money as well as financial advice to help countries with economies suffering from balance-of-payment problems.
- D) IMF loans typically come with many conditions attached that may result in increased poverty in the donor country.
- E) A number of developing countries have suffered financial disasters from following IMF advice.

Answer: C

Explanation: C) This describes Sponeto's economic situation, and indicates that the IMF's mission would be well suited to its needs. Tariffs (Choice A) and nationalized companies (Choice B) may or may not represent long-term drags on Sponeto's economy, but it's a disadvantage of taking IMF funds if the result is loss of national control over such basic economic decisions. Choices D and E also describe potential, if uncommon, disadvantages to accepting funds from the IMF.

Page Ref: 17

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.5

Skill: Critical Thinking

132) Some in the Sponeto government would like the country to appeal to the World Bank for funding toward economic development, rather than short-term monetary stimulation. Which of the following, if true, would strengthen the case for this course of action?

- A) Sponeto has come under criticism in the United Nations for alleged human rights abuses.
- B) Sponeto has been able to grow enough food to export to surrounding nations.
- C) Corruption is a major problem among Sponeto's government officials.
- D) Sponeto urgently needs humanitarian aid due to a recent natural disaster.
- E) Chronic and widespread poverty is Sponeto's biggest economic problem.

Answer: E

Explanation: E) The World Bank would be able to help address poverty with long-term loans toward economic development. Choices A and C do not relate to Sponeto's economic needs, and weaken the case that they could receive international aid without addressing other problems. Choice B weakens the case that Sponeto is in need of international aid. Choice D suggests that Sponeto needs immediate material aid rather than long-term economic aid.

Page Ref: 17

Difficulty: Moderate

AACSB: Reflective thinking skills

Objective: 1.5

Skill: Critical Thinking