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Econ 202: Principles of Economics

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Course Guide

Independent Study in Idaho

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Economics 202
Principles of Economics

University of Idaho
3 Semester-Hour Credits

Prepared by:
Steven Peterson
Lecturer in Economics
University of Idaho

RV: 1/03, updated 1/07
3-Econ 202
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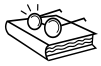
Econ 202: Principles of Economics **3 Semester–Hour Credits: U-Idaho**

Welcome!

Whether you are a new or returning student, welcome to the Independent Study in Idaho (ISI) program. Before beginning this course, read the information provided below, including course description, prerequisites, required materials, course objectives, and information about lessons, exams, and grading.

Policies and Procedures

Important!
As you read this section, you will see the following icon: 

Use this icon to direct yourself to essential ISI information. Students are responsible for following ISI's policies. Refer to ISI's website at ***www.uidaho.edu/isi,*** select *About ISI, Policies* for the most current policies and procedures. If you have any questions or concerns, please contact the ISI office for clarification before beginning your course.

Course Description

Microeconomic principles governing production, price relationships, and income distribution. U-Idaho students: may be used as core credit in J-3-d. Econ 201 or 202 carry only two credits after 272 [Foundations of Economic Analysis].

Recommended: Internet access, computer with CD drive
16 graded lessons, 3 self-study practice exams, 4 self-study practice exams, 4 proctored exams

Course Materials

Required Course Materials

- Parkin, Michael. *Microeconomics*. 5th ed. Reading: Addison-Wesley, 2000. ISBN: 0-201-68025-4 or 0-201-47385-2 (softbound).

Independent Study in Idaho course materials are available for purchase at the VandalStore (University of Idaho bookstore). Your *Registration Confirmation Email* contains the VandalStore's contact information.

Independent Study in Idaho courses are updated and revised periodically. Ordering course materials from the VandalStore at the time of registration allows you to purchase the correct edition(s) of textbooks, course guides, and supplemental materials. Contact the VandalStore directly for questions regarding course materials that you have ordered.

If purchasing textbooks from another source, refer to the ISBN(s) for the textbook(s) listed for this course to ensure that you obtain the correct edition(s).

Course Delivery

This course is available online. An electronic course guide is accessible through BbLearn at no additional cost. Refer to your *Registration Confirmation Email* for instructions on how to access BbLearn.

Course Introduction

Welcome to the world of economics. This course examines an important branch of economics, *microeconomics*, which studies individual decision-makers such as consumers and firms; individual markets; and individual industries. The focus of microeconomics is on incentives, both in private markets

and in institutional settings such as government bureaucracies. Microeconomics wrestles with the important issues such as the California energy crisis. Was the crisis caused by bad government policies (i.e., price controls) or by the market power of the wholesale electrical producers?

Microeconomics even offers insights to national security issues. One important topic is whether airline security should be carried out by private firms or directly by the federal government. This issue arose out of the September 11, 2001 terrorist attack on the World Trade Center in New York City. An important branch of economics known as public choice economics focuses on the public sector and can provide answers as to which security method might be the most appropriate.

Microeconomics differs from another branch of economics, *macroeconomics,* which studies the economy as a whole. Economists specializing in macroeconomics utilize the *aggregate approach* in their analysis.

The roots of microeconomics can be traced to the early Greeks. Its ascendance in modern times began with Adam Smith, the founder of modern economics, who published *The Wealth of Nations* in 1776.

Microeconomics is an incredibly rich and varied branch of economics. It begins with the building blocks of economics: 1) What makes individuals happy, 2) How individuals make decisions, 3) What incentives and disincentives individuals face, and 4) How individuals interact with each other.

On this basis, microeconomics shows how markets develop and operate. Economists develop predictive modes illustrating the impacts of potential policy actions. Some of these models employ sophisticated statistical analysis in their examination of economic activity.

Microeconomics includes the theory of consumer choice; supply and demand analysis; elasticities; theory of the firm; production analysis; market structure including perfect competition, monopolistic competition, oligopoly, and monopoly; public choice economics which includes public decision-making; externalities and pollution; private property rights; market failure and government failure; theory of trade and exchange; and many other important topics.

Your decision to undertake an Independent Study course places you in a special category of student. I have found, on average, that students who complete the course are more motivated and achieve more than students on campus. The reason is the self-motivation and discipline needed to complete an Independent Study course.

Each student develops individual study habits that are often unique. Thus, there is no one “best way” to approach this material. What is important is that you learn the important concepts in the course.

Nonetheless, I will suggest a possible approach which you may find helpful. First of all, read the textbook readings as a first pass through the material. Choose a quiet setting, perhaps with a cup of coffee or your favorite soft drink. The next step is to read the lesson in this study guide, considering how this information fits in with the textbook material. This should be followed by referring to the beginning of each lesson for a listing of the key topics.

The next step is to do the assignments. These will help you understand the important issues in each block of material. Keep in mind the importance of graphing. Be sure to practice these graphs. It takes work to get them down cold!

Always remember to contact your instructor if you have any questions. GOOD LUCK!

Course Objectives

- To introduce the student to basic economic thinking and analysis
- To acquaint the student with economic concepts, terminology, and logic
- To familiarize the student with the tools needed for examining important economic models such as supply and demand, consumer choice, market structures, the theory of the firm, input markets, labor markets, market failure, government failure, externalities, the role of private property rights, and free trade
- To familiarize the student with the incentives facing each individual, how individuals make economic choices, and how these choices lead to markets
- To introduce to the student public decision theory and how governments operate; the incentives and choices facing public decision-makers will be examined.
- To familiarize the student with the debate over the appropriate role and function of government in the economy and its effect on private decision-making
- To introduce to the student the concepts and measures of economic growth, technological development, and human capital development
- To introduce to the student important topics of the new millennium, such as the California energy crisis, economic choices resulting from the September 11, 2001 terrorist attack on the World Trade Center, privatization of the post office, the antitrust actions against Microsoft and other new technology companies, choices resulting from global warming, and other interesting topics
- To illustrate the importance and relevance of microeconomics to the student's life and future career

Lessons

Each lesson may include the following components:

- lesson objectives
- reading assignments
- an introductory lecture
- a written assignment
- Web References: Web references are provided at the beginning of each lesson for your interest but their review is <u>not</u> a course requirement. All of them are related to economics directly or indirectly and I encourage you to become familiar to economics on the web.
- For Your Interest: These are interesting topics of interest that appear at the beginning of several lessons. Again they are for your interest but will not appear as test questions on the exams.

Study Hints

- Keep a copy of every lesson submitted.
- Complete all assigned readings.
- Set a schedule allowing for completion of the course one month prior to your desired deadline. (An *Assignment Submission Log* is provided for this purpose.)
- Complete the entire lesson assignment (partial or incomplete assignments will receive a zero).
- Place your name and V number on each lesson to expedite lesson processing time.
- If submitting multiple lessons (see limits above), submit them in sequence.
- The next step is to read the lesson and lecture in this study guide. Carefully consider how this information fits in with the textbook material. Review the key objectives of each lesson.
- Self-Study Lessons: These lessons are not to be turned into your instructor. The answer key is provided at the back of your study guide. This material is fair game on the exams, however, so you need to study the lessons carefully. The self-study lessons are 5, 10, and 15.
- Lectures: Material labeled “lecture” is included in each of the lessons. Most of these are chapter reviews in staccato format. Some lectures include new material. You should read the chapter(s) in your text first before reviewing the lectures. They will be helpful in preparing for the exams.

- Do the assignments. These will help you understand the important issues in each chapter. Note the importance of graphing. Economic models are often presented in graphically form. You will need to be able to graph and explain many of these economic models. Be sure to practice these graphs. It takes work to get them down cold!
- Practice Exams: Practice tests are provided at the end of each block of material to you to assist in preparing for the exam. They will assist you in identifying the type of questions that will be on the exam (obviously the questions themselves will be different).
- Do not hesitate to contact your instructor if you have any questions.

Lesson Support:

- **Online support:** Considerable resources are available online free of charge from the publisher of your Parkin *Microeconomics* textbook. Instructions for activation are provided in the inside cover of your textbook. An activation ID and password are provided. Log on to the Internet and go to **www.economicsplace.com.** At this site you will be asked for your user ID and password, your name, e-mail address, and some other information. You will be able to select your own personal ID and password. Finally follow the link provided to their Web site. Access to this site is recommended, **but not necessary to take the course.**
- **CD support:** Each text book comes with a free CD-Rom with additional student support services. Start the CD from setup.exe. The CD has an interactive fill-in-the-blank quiz for each chapter to assist you in preparing for the exam. I think you will find these services helpful. The answers to the question are a "click" and "drag" from the possible answer set to the blank (this took me a few minutes to figure out). Access to the CD is recommended, **but not necessary to take the course.**
- Each lesson consists of both multiple-choice questions and essay questions/graphs. *On average*, the typical lesson will have three essay questions/graphs and fifteen multiple-choice questions.
- If you are typing the lessons, simply record the multiple-choice question number and the letter answer that best fits. Do not re-type the question itself.
- Some lessons (i.e., lectures) in your study guide include supplemental materials. Most of the lectures, however, are a review and summary of the textbook material. They provide a concise overview and review of the key issues covered the text. In all cases you should read the chapter first **before** the lecture in the study guide. These lectures are designed to assist you in "digesting" and understanding the concepts covered in the text.
- To understand the concepts of each lesson, adopt a form that assists you in that endeavor. For some students, learning is enhanced when they type the lessons because it helps them organize their thoughts. Other students find typing a learning impediment.

Refer to your *Registration Confirmation Email* for further details on your instructor's lesson guidelines and requirements. Also refer to the *ISI Policies and Procedures* for essential ISI policies on submitting lessons to your instructor.

Exams

- You must wait for grades and comments on lessons prior to taking each subsequent exam.
- For your instructor's exam guidelines, refer to the letter sent in your registration packet and the *Exam Information* sections in this study guide.

See *Grading* for specific information on exams, points, and percentages.

- Submit all lessons preceding each exam prior to requesting it.
- There will be four examinations in the course including the final examination.

  The exams and the chapters in the text they cover:

Examination 1:	Chapters 1–6
Examination 2:	Chapters 7–13

Examination 3: Chapters 14–18
Examination 4: Chapters 19–22

- Each examination is worth a maximum of 170 points. The total possible points for all four examinations is 680.
- The final examination is non-comprehensive
- Each examination will have a combination of multiple-choice questions and essay questions/graphs.
- The number of points that each question is worth will appear on the examination. Generally speaking the essays/graphs are worth 100 points and the multiple choice questions are worth 75 points.
- Although the examinations are intended to take only an hour to complete, you will have two full hours.

Practice Exams
Practice tests are provided at the end of each block of material to assist in preparing for the exam. They will assist you in identifying the type of questions that will be on the exam (obviously the questions themselves will be different). Much of the material in the examinations focuses on problem solving. If a problem appears at length in the practice examination, there is a good chance it will also appear in the real test in some form.

Proctor Selection/Scheduling Exams
All exams require a proctor unless an exam is self-administered.

Refer to the *ISI Policies and Procedures* for guidelines on how to choose a proctor and schedule exams. Complete the *Proctor Information Form* and send it to the ISI office at least two weeks prior to scheduling your first exam.

Grading
The course grade will be based upon the following considerations:

- **Lessons:** This course includes 16 graded lessons worth generally 20 points apiece, for a total of 320 points.
- **Exams:** Each examination is worth a maximum of 170 points and the total possible points for all four examinations is 680. The twenty submitted lessons are worth a combined maximum of 320 points. The total possible points in the course are 1000. A summary follows:

Examination 1: 170 points
Examination 2: 170 points
Examination 3: 170 points
Examination 4: 170 points
16 assignments: 320 points
Total points 1,000 points

The following scale applies in determining your final grade:

minimum required for A 90 percent = 900 points
minimum required for B 80 percent = 800 points
minimum required for C 70 percent = 700 points
minimum required for D 60 percent = 600 points

Your instructor retains the option of applying a grading curve to lower the minimums listed above, in order to make the Independent Study in Idaho grades compatible with those of courses taught on campus. Since the minimums can be lowered but not raised, this will work to your advantage. A hypothetical example would be to lower the minimum of an "A" grade from 90 percent to 88 percent. If you have any questions on grading, contact your instructor.

Optional Extra Credit Paper

320/An extra credit paper may add a maximum of 40 points to your course total, while the downside risk is zero. Therefore, a good paper will add 25 or more points to your course total, an average paper 25 points or so, and a below average paper fewer than 15 points.

The extra credit paper option is not for everyone. It requires an investment in time and research effort. Nonetheless, it offers potential rewards in terms of grade and knowledge enhancement. Furthermore, it allows Independent Study students the same option as offered to on-campus students.

The assignment is to research and write on any aspect of poverty and the distribution of income. This is a particularly relevant topic given the political changes in the 1990s and the economic slowdown beginning in 2001. You may examine general issues such as the appropriateness of the redistributive function of government or examine specific poverty programs. You might wish to examine the effectiveness of in-kind programs such as food stamps versus a negative income tax, which is a cash program. You may choose from a virtually endless number of topics. Contact your instructor if you need any assistance in choosing one.

The paper should be a minimum of seven pages in length, typed or computer-printed, double-spaced, with citations and bibliography in an appropriate format. Contact your instructor if you have any questions.

The final course grade is issued after **all** lessons and exams have been graded.

Refer to the *ISI Policies and Procedures* for information about confidentiality of student grades, course completion, time considerations, and requesting a transcript.

About the Course Developer

Hi. I am a research economist and faculty in the Department of Economics, Finances, and Information Systems at the University of Idaho, where I have been employed for 15 years. My teaching interests are introductory macroeconomics, microeconomics, money and banking, and intermediate macroeconomics. My research interests are regional economic development and impact analysis. I have conducted studies on the economic impacts to local Idaho communities from reductions of timber harvests on federal forests, the economic impact of colleges and universities, the economic impacts of inland ports and dam removal to save salmon, tribal gaming, and other interesting subjects. I look forward to assisting you in your exploration of economics.

Contacting Your Instructor

Instructor contact information is available in BbLearn
.

Disability Support Services

Refer to the *ISI Policies and Procedures* for information on *Disability Support Services (DSS).*

Assignment Submission Log

Lesson	Chapter	Reading	Written Assignment	Date Submitted
1	1–2	pp. 1–34	multiple choice and essay	____
2	3	pp.35–60	multiple choice and essay	____
3	4	pp. 61–86	multiple choice and essay	____
4	5	pp. 87–106	multiple choice and essay	____
5	6	pp.107–126	multiple choice and essay (self-study)	
It is time to make arrangements with your proctor to take Exam 1.				
6	7–8	pp. 127–154	multiple choice and essay	____
7	9	pp. 173–196	multiple choice and essay	____
8	10–11	pp. 197–238	multiple choice and essay	____
9	12	pp. 239–262	multiple choice and essay	____
10	13	pp. 263–284	multiple choice and essay (self-study)	
It is time to make arrangements with your proctor to take Exam 2.				
11	14	pp. 285–316	multiple choice and essay	____
12	15	pp.317–342	multiple choice and essay	____
13	16	pp.343–364	multiple choice and essay	____

14	**17**	**pp.365–390**	**multiple choice and essay**	**____**
15	**18**	**pp. 391–410**	**multiple choice and essay (self-study)**	
It is time to make arrangements with your proctor to take Exam 3.				
16	**19**	**pp. 411–430**	**multiple choice and essay**	**____**
17	**20**	**pp.431–448**	**multiple choice and essay**	**____**
18	**21**	**pp. 449–472**	**multiple choice and essay**	**____**
19	**22**	**pp. 473–502**	**multiple choice and essay**	**____**
It is time to make arrangements with your proctor to take the Final Exam.				

Lesson 1
Economics as a Discipline

Humor in Economics

"Murphy's law of economic policy": Economists have the least influence on policy where they know the most and are most agreed; they have the most influence on policy where they know the least and disagree most vehemently.

— Alan S. Blinder

Source: http://www.etla.fi/pkm/JokEc.html

For your interest
Famous People who Majored in Economics in College

Dick Armey: US Congressman
Steve Balmer: Executive VP, Microsoft
William F. Buckley: Journalist
Jim Bunning: US Congress/Baseball Hall of Fame
George H.W. Bush: Former US President
Sandra Day-O'Connor: US Supreme Court
John Elway: Former NFL quarterback
Phil Gramm: US Senator
William Isaac: Former Chairman of FDIC
Mick Jagger: Rolling Stones
Alex Keaton: TV sitcom character
Young M.C.: Singer
Bernie Kosar: NFL quarterback
Mike Mussina: MLB Pitcher
Merlin Olson: Actor/Former NFL player
Ronald Reagan: Former US President
Roy Romer: Gov. of Colorado
Lionel Ritchie: Singer/Songwriter
George Schultz: Former US Secretary of State
Arnold Schwarzenegger: Actor
Richard Trumka: Pres. United Mine Workers
Ted Turner: CNN, Atlanta Braves/Hawks
Mario Van Peebles: Actor/Director
Lenny Wilkens: NBA Coach

Source: **http://web.centre.edu/~econed/Subpages/famous.htm**

Web-links

A link to biographies of famous economists and their birthdays: **http://www.cpm.ll.ehime-u.ac.jp/AkamacHomePage/Akamac_E-text_Links/Akamac_E-text_Links.html#A**

Resources for Economists on the Web: **http://www.economicsplace.com/mic5e/links/ch01frame.html**

Business News—US News and World Report: **http://www.usnews.com/usnews/home.htm**

Lesson Objectives

- Define Economics
- Explain the five big questions that economists seek to answer
- Explain eight ideas that define the economic way of thinking
- Describe how economists go about their work

Reading Assignments

Parkin, Chapters 1–2, pp 1–34.

Lecture

Introduction

The economics profession is a pie that can be sliced in many ways . . .

Economics is a discipline that examines the allocation of scarce resources to consumers with unlimited wants and desires. The two key focal points of economics are the facts that all economic resources are scarce and that consumer wants and desires are unlimited (i.e. there are competing uses). These points create a conflict, a tension between the unlimited wants and desires by consumers and the scarcity of goods and services. Thus, as noted in your text: *scarcity forces choice.*

Usually, when someone thinks of economics (and economists), they think of money and/or the stock market. In fact, only a small minority of economists specialize in finance or securities. The principal focus of economics is on human welfare. The quest to improve the human condition leads economics into virtually all aspects of peoples' lives and into virtually every profession. In fact, John T. Wenders, an economist at the University of Idaho, has labeled economics an *imperial science*, frequently invading (i.e., offering analysis and insight to) many other professions. Economics as a discipline is perhaps second only to the granddaddy of them all—philosophy—in its scope.

Economics is a way of thinking, a method of analysis. Economics offers a unique viewpoint of the essential elements of the human condition.

Economics is part science. That is, it is based on some fundamental, predictable elements of human behavior. One such assumption, for example, is that people seek to maximize their own utility or welfare. Science also plays an important role in economics where the human world and the physical world come together, such as in the production of goods and services, resource development, technological improvement, and production efficiency. Economics is also subject to the unpredictable elements of human behavior; however, which distinguishes it from professions such as chemistry or physics. Economics is therefore a social science.

The Two Basic Divisions of Economics

Macroeconomics studies "the big picture."It focuses on the economy as a whole. Macroeconomic analysis aggregates across many markets and over a large number of decision-makers. Frequently, a distinction between macroeconomics and microeconomics is the role that money plays. Macroeconomics must usually deal with the impact of money (and monetary systems) in their analysis, whereas microeconomics usually (but not always) ignores or holds constant their effects. Given the size of the U.S. economy and its extremely complex nature, there is far more uncertainty among macroeconomists as to proper policy actions than found among microeconomists. Macroeconomists are sometimes derided as akin to old country doctors, pretending to know more than they really do, and ultimately depending on the long-run vitality of the economy (rather than corrective policy actions) to solve the nation's economic problems. Yet macroeconomists have played an important role in many of the policy decisions that facilitated the long-run growth and stability of the U.S. economy since the 1940s. Many of these issues will be explored in detail in this course.

Microeconomics focuses on individual markets and/or decision-makers. The scientific method has been more successfully used in analyzing many more microeconomic issues than with macroeconomic issues.

Economists have reached many important, generally-agreed-upon conclusions regarding policy issues in microeconomics. Some of these issues will be explored in the beginning of this course.

Normative Versus Positive Economics

Normative statements are value judgments—subjective individual preferences. Normative statements usually include qualifiers such as "should be" or "ought to be." The statement: "We should cut taxes to improve productivity and growth in the economy" is a normative statement. *Positive economics*, on the other hand, deals with facts. The statement: "The national debt is approximately 5 trillion dollars" is a positive statement.

University Institutional Divisions

Economics, Agricultural Economics, Natural Resource Economics (in the College of Forestry), Home Economics, Economics for Primary and Secondary Schools, Economics in the Fields of Geology, Geography, Engineering, etc. are some of the divisions of economics.

At the University of Idaho, the Economics Department is located in the College of Business and Economics. Agricultural Economics, on the other hand, is located in the College of Agriculture. The combined two departments hold most (but not all) of the economists at this university. Other economic courses are taught in Forestry, Education, Geology, Geography, Engineering, and other colleges.

Specialized Fields within Economics

	Macroeconomics	Elements of Both	Microeconomics
1	Money and Banking		
2		International Economics	
3			Regional and Urban Econ.
4			Public-Choice Economics
5			Labor Economics
6			Industrial Economics
7		Development Economics	
8		Econometrics	
9		History of Economic Thought	
10		American Economic Development	
11			Environmental Economics
12		Comparative Economic Systems	
13		Marxism	
14		Public Finance	

General Economics Concepts and Terms

Economics can be defined as a discipline that examines the allocation of scarce resources to consumers with unlimited wants and desires (competing uses).

There are three basic answers to the economic problem: command economy, pure capitalism, and mixed economy. In a *command economy*, such as we once found in China, the economic problem was solved by the government (although many of these countries are currently adopting free-market reforms). The government answers the question of what to produce, how to produce it, and for whom it shall be produced. The government owns all of the economic resources and the means of production. It directs resources.

In *pure capitalism*, private citizens own resources and the means of production. Prices direct resources. Markets and prices determine what is to be produced, how it is to be produced, and for whom. In capitalism, decision-making is *decentralized* in the hands of small producers and consumers. In a command economy, decision-making is *centralized*. These decisions are made by the government. Our economy in the USA is a *mixed economy*. Markets play the dominant role in our country, but the government also plays an important role in resource allocation.

An economic good is, by definition, a scarce resource. **All** economic resources are scarce. A *free good*, on the other hand, is a good of which you can consume all that you could possibly want at zero cost and plenty would remain for everybody else in the world. Sunlight and air are considered examples in many economics textbooks. Can you think of reasons why these examples may not be appropriate?

Ceteris paribus is another important concept in economics. It is a Latin phrase meaning "other things being equal." Thus, when examining the relationship of one economic variable to another, all other factors must be held constant.

Parkin's Key Concepts—Chapter 1

A Definition of Economics
The fundamental economic problem is scarcity. Because the available resources are never enough to satisfy everyone's wants, choices are necessary.
Economics is the science of choice; it explains the choices we make and how the choices we make help us cope with scarcity.

Big Economic Questions
Economic choices can be summarized by five big questions:
- **What** goods and services are produced and in **what** quantities?
- **How** are goods and services produced?
- **When** are goods and services produced?
- **Where** are goods and services produced?
- **Who** consumes the goods and services produced?

Big Ideas of Economics
- A choice involves a *tradeoff*, that is, something is given up to get something else. The *opportunity cost* of a choice is the highest valued alternative foregone. Opportunity cost is not all the alternatives foregone, but is the highest valued alternative foregone.
- Choices are made in small steps, which means choices are made at the margin, and choices are influenced by incentives. When making choices, people compare the *additional* cost—the marginal

cost—of an action to the additional benefit—the marginal benefit—of the action. Changes in marginal cost and/or changes in marginal benefit affect the decisions made.

- Voluntary exchange makes *both* buyers and sellers better off, and markets are an efficient way to organize such an exchange. Both the buyer and seller of a product must benefit from a transaction, or the transaction will not take place.
- The market does not always work efficiently, so sometimes government action is necessary to overcome market failure and lead to a more efficient use of resources.
- For the economy as a whole, expenditure equals income equals the value of production.
- Living standards improve when production per person increases.
- Inflation occurs when the quantity of money increases faster than the production of goods and services.
- Unemployment can result from market failure but some unemployment is productive and can improve the nation's productivity.

What Economists Do

Economics is divided into two branches, microeconomics, the study of individual firms, individual consumers, and individual markets, and macroeconomics, the study of national and global economies and the factors that shape them.

Economists distinguish between:

- Positive statements—statements about what is. These can be shown to be true or false through observation and measurement.
- Normative statements—statements about what ought to be. These are matters of opinion.

Economic science is a collection of positive statements that are consistent with the real world. Economic science uses three steps to progress:

- Observation and measurement - economists observe and record economic data.
- Model building—an economic model contains simplified descriptions of the economic event under study that include only the factors considered most important.
- Testing—a model is tested to determine how well its predictions correspond with the real world.

When developing models and theories, economists use the idea of *ceteris paribus*, which is Latin for "other things being equal," to focus on the effect of one particular factor.

In the development of theories and models, two pitfalls are possible:

- Fallacy of composition—the assertion that what is true for a part must be true for the whole, or what is true for the whole must be true for each of the parts.
- *Post hoc* fallacy—the assertion that one event caused another because the first occurred before the other.

Key Concepts are from Parkin, *Microeconomics.* You may find the study guide helpful. For further assistance, consult the *Study Guides*: *Microeconomics*, ISBN 0-201-63786-3, and *Macroeconomics*, ISBN 0-201-63787-1.

Important Terms

economics	opportunity cost	productivity
economic theory	market failure	scarcity
margin	ceteris paribus	voluntary exchange
marginal benefit/cost	tradeoff	macroeconomics vs. microeconomics

Written Assignment

Please answer the following questions. The Short-Answer/Essay questions are worth five points. The multiple choice questions are worth a total of ten points.

Questions 1 – 3 Short Answer/Essay (10 points)

1. Give some examples of tradeoffs that you have made and the opportunity costs you've incurred today.

2. Define and give examples of marginal costs and marginal benefits.

3. What makes living standards rise?

Question 4–18 Multiple Choice (10 points)

4. All economic questions and economic activity arise from

   a) cooperation.
   b) trade.
   c) competition.
   d) scarcity.

5. The problem of "scarcity" applies

   a) to all economic systems, regardless of their level of development.
   b) only in industrially developed countries because resources are scarce in these countries.
   c) only in underdeveloped countries because there are few productive resources in these countries.
   d) only in economic systems that are just beginning to develop because specialized resources are scarce.

6. Question: Sue, who has a law degree, earns $200,000 a year while Chris, a high school dropout earns $5.00 an hour. This is an example of an economy answering the ____ question.

   a) "who"
   b) "why"
   c) "when"
   d) "how"

7. In economics, positive statements are about

   a) microeconomics not macroeconomics.
   b) the way things are.
   c) the way things ought to be.
   d) macroeconomics not microeconomics.

8. The fallacy of composition is the false belief that

a) what is true for each part is also true for the whole.
b) because event A occurred before event B, event A caused event B.
c) the ceteris paribus condition does not apply.
d) because event A occurred after event B, event A caused event B.

9. The term used to emphasize that making choices in the face of scarcity involves a cost is

a) opportunity cost.
b) utility cost.
c) accounting cost.
d) substitution cost.

10. Which of the following is a microeconomic topic?

a) The effect of the government budget deficit on inflation.
b) The reasons why Kathy buys less orange juice.
c) The cause of why total employment may decrease.
d) The reasons for a decline in average prices.

11. To overcome market failure, governments

a) subsidize the production of some goods.
b) enact environmental protection laws.
c) pass antitrust laws.
d) all of the above.

12. Adam Smith wrote the book

a) The Wealth of Nations.
b) Poverty and Progress.
c) The Dismal Science.
d) First Principles of Economics.

13. Economists point out that scarcity confronts

a) both the poor and the rich.
b) neither the poor nor the rich.
c) the poor but not the rich.
d) the rich but not the poor.

14. Opportunity cost means

a) the accounting cost minus the external cost.
b) the highest-valued alternative forgone.
c) the monetary costs of an activity.
d) the accounting cost minus the indirect cost.

15. Ceteris paribus means

    a) that which will be
    b) what ought to be
    c) other things being equal
    d) what is

16. Making choices at the margin

    a) is about comparing benefits and costs.
    b) results in a good use of resources.
    c) involves making decisions in increments.
    d) all of the above

17. Involuntary exchange

    a) buyers gain at the expense of sellers.
    b) sellers gain at the expense of buyers.
    c) buyers and sellers are both made better off.
    d) buyers and sellers both gain at the expense of the government.

18. The marginal cost of working four days a week instead of three days a week is

    a) the opportunity cost of the fourth day of work.
    b) the wages earned on the fourth day of work.
    c) the opportunity cost of the fourth day of work minus the wages earned on the fourth day of work.
    d) the opportunity cost of the four days of work.