Chapter 01

Thinking Like an Economist

**Multiple Choice Questions**

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| 1. | Microeconomics is primarily the study of how      |  |  | | --- | --- | | A. | the stock market works. |  |  |  | | --- | --- | | B. | people choose among alternatives. |  |  |  | | --- | --- | | C. | businesses can make money. |  |  |  | | --- | --- | | D. | the economy functions as a whole. | |

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| 2. | If you are at an all-you-can-eat buffet dinner and you are considering whether to eat another dessert, you, as a rational consumer should decide to eat the desert      |  |  | | --- | --- | | A. | if it brings you any pleasure at all. |  |  |  | | --- | --- | | B. | if it brings you more pleasure than the price you paid for the meal. |  |  |  | | --- | --- | | C. | if it brings you as much pleasure as the desert costs if it is ordered a la carte. |  |  |  | | --- | --- | | D. | no matter what because you want to get more for your money. | |

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| 3. | Say your girlfriend has received two free tickets to the Sunday movie matinee and she wants you to go with her. Nevertheless, the movie plays at the same time you were planning to watch the football game on the TV. As a rational person you should decide to go to the movie      |  |  | | --- | --- | | A. | always, since the tickets were free. |  |  |  | | --- | --- | | B. | only if you would gain some pleasure from it. |  |  |  | | --- | --- | | C. | only if the pleasure you will gain from it outweighs the pleasure you would gain from watching the football game. |  |  |  | | --- | --- | | D. | only if it brings you more pleasure than the cost of the tickets. | |

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| 4. | The reservation price of good X is      |  |  | | --- | --- | | A. | the market price for a good. |  |  |  | | --- | --- | | B. | any price above what you would be willing to pay for the good. |  |  |  | | --- | --- | | C. | the price at which one would be indifferent between good X and simply keeping the money. |  |  |  | | --- | --- | | D. | the cost of producing good X. | |

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| 5. | If the benefits of X = $50 and the price of X = $50, then      |  |  | | --- | --- | | A. | $100 is the reservation price. |  |  |  | | --- | --- | | B. | you will be indifferent between buying X and keeping your money. |  |  |  | | --- | --- | | C. | $0 is the reservation price. |  |  |  | | --- | --- | | D. | you should buy X. | |

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| 6. | Your bank account pays 3% interest per year. You loan a friend $100 for one year at zero interest. Assuming the loan is paid on time the opportunity cost of the loan is      |  |  | | --- | --- | | A. | $3. |  |  |  | | --- | --- | | B. | $100. |  |  |  | | --- | --- | | C. | $103. |  |  |  | | --- | --- | | D. | $0. | |

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| 7. | You decide to go skiing this weekend. It costs $50 for transportation, $50 for lodging, $30 for ski lift tickets and you could have earned $100 as a waiter. What is the total cost of the ski weekend?      |  |  | | --- | --- | | A. | $230 |  |  |  | | --- | --- | | B. | $130 |  |  |  | | --- | --- | | C. | $100 |  |  |  | | --- | --- | | D. | $80 | |

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| 8. | You decide to go skiing this weekend. It costs $50 for transportation, $50 for lodging, $30 for ski lift tickets. You are unemployed. What is the total cost of the ski weekend?      |  |  | | --- | --- | | A. | $230 |  |  |  | | --- | --- | | B. | $130 |  |  |  | | --- | --- | | C. | $100 |  |  |  | | --- | --- | | D. | $80 | |

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| 9. | You decide to go skiing this weekend. It costs $50 for transportation, $50 for lodging, $30 for ski lift tickets and you could have earned $100 as a waiter at a job you love so much you would do it as a volunteer. What is the total cost of the ski weekend?      |  |  | | --- | --- | | A. | $230 |  |  |  | | --- | --- | | B. | $130 |  |  |  | | --- | --- | | C. | $100 |  |  |  | | --- | --- | | D. | $80 | |

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| 10. | Your parents have given you a new car on your 16th birthday for which they paid about $24,000. Assume this is also the price you would get if you decided to sell the car a month after getting it. The monthly costs of driving the car are $100 for oil changes and $200 for gas. If you decide to keep the car, the total costs of the car to you this month will be      |  |  | | --- | --- | | A. | $2,300. |  |  |  | | --- | --- | | B. | $300. |  |  |  | | --- | --- | | C. | $24,300. |  |  |  | | --- | --- | | D. | $0. | |

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| 11. | Your parents have given you a new car on your 16th birthday for which they paid about $24,000. Assume this is also the price you would get if you decided to sell the car a month after getting it. The monthly costs of driving the car are $100 for oil changes and $200 for gas. What are the opportunity costs of driving the car this month?      |  |  | | --- | --- | | A. | $300 |  |  |  | | --- | --- | | B. | $2,000 |  |  |  | | --- | --- | | C. | $24,300 |  |  |  | | --- | --- | | D. | $0 | |

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| 12. | Here are the costs of going to college: tuition $5,000; books $200; housing $1,000; food $1,000; lost income from work $10,000. Studying and work are equally desirable in your mind. Suppose that you could live at home at no cost to you if you worked, but must live on campus if you go to school. What is the total opportunity cost to you of going to school rather than working? (Food costs the same at school or home.)      |  |  | | --- | --- | | A. | $16,200 |  |  |  | | --- | --- | | B. | $7,200 |  |  |  | | --- | --- | | C. | $5,200 |  |  |  | | --- | --- | | D. | $15,200 | |

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| 13. | Here are the costs of going to college: tuition $5,000; books $200; housing $1,000; food $1,000; lost income from work $10,000. Studying and work are equally desirable in your mind. Suppose you must live on your own anyway. What is the cost of going to school?      |  |  | | --- | --- | | A. | $17,200 |  |  |  | | --- | --- | | B. | $7,200 |  |  |  | | --- | --- | | C. | $15,200 |  |  |  | | --- | --- | | D. | $16,200 | |

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| 14. | Here are the costs of going to college: tuition $5,000; books $200; housing $1,000; food $1,000; lost income from work $10,000. Studying and work are equally desirable in your mind. Suppose that you could work part-time and make $5,000 at a job you would volunteer to do. You live on campus instead of at home. What is the cost of going to school?      |  |  | | --- | --- | | A. | $16,200 |  |  |  | | --- | --- | | B. | $7,200 |  |  |  | | --- | --- | | C. | $5,200 |  |  |  | | --- | --- | | D. | $11,200 | |

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| 15. | You decide to lend $100 to a friend interest free for one year. You calculate that you could have earned 10% interest. What is the opportunity cost of the loan if it is paid on time?      |  |  | | --- | --- | | A. | $10 |  |  |  | | --- | --- | | B. | $100 |  |  |  | | --- | --- | | C. | $110 |  |  |  | | --- | --- | | D. | $0 | |

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| 16. | You are considering renting a car for the weekend. It costs $200 for the car plus $0.20 per mile (including gas). If you decide to go on a 300 mile voyage what is the total cost of the rental?      |  |  | | --- | --- | | A. | $200 |  |  |  | | --- | --- | | B. | $60 |  |  |  | | --- | --- | | C. | $260 |  |  |  | | --- | --- | | D. | $0 | |

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| 17. | You are considering renting a car for the weekend. It costs $200 for the car plus $0.20 per mile (including gas). Suppose you have already rented the car for the week and then add the 300 mile addition to your trip. Now what is the cost of the journey?      |  |  | | --- | --- | | A. | $100 |  |  |  | | --- | --- | | B. | $60 |  |  |  | | --- | --- | | C. | $260 |  |  |  | | --- | --- | | D. | $0 | |

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| 18. | You are considering renting a car for the weekend. It costs $200 for the car plus $0.20 per mile (including gas). If you decide to take a detour that adds 50 miles above the 300 miles, what is the cost of the detour?      |  |  | | --- | --- | | A. | $10 |  |  |  | | --- | --- | | B. | $70 |  |  |  | | --- | --- | | C. | $270 |  |  |  | | --- | --- | | D. | $200 | |

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| 19. | Adam Smith in The Wealth of Nations argued that      |  |  | | --- | --- | | A. | society works best when people act in their own interest. |  |  |  | | --- | --- | | B. | society works best when people act unselfishly. |  |  |  | | --- | --- | | C. | society works best when people act as if they were invisible to others. |  |  |  | | --- | --- | | D. | the social order needs the guidance of the government's visible hand. | |

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| 20. | Your textbook costs $100 and the college snack shop sells ice cream for $1. Which of the following statements is true for most people?      |  |  | | --- | --- | | A. | You would be indifferent between a bookstore sale of 1% off on your text and one free ice cream in the snack shop. |  |  |  | | --- | --- | | B. | Most people will get greater satisfaction from the bookstore sale than from the snack shop giveaway. |  |  |  | | --- | --- | | C. | Most people will get greater satisfaction from the snack shop giveaway than from the bookstore sale. |  |  |  | | --- | --- | | D. | Because people are very different there is no general principle that can be suggested regarding the satisfaction people get in these situations. | |

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| 21. | Joe is one mile from the finish of a grueling 26 mile marathon. Tim is at the four mile mark of a five mile run. Which runner is most likely to be emotionally energized for the race to the finish line?      |  |  | | --- | --- | | A. | Joe. |  |  |  | | --- | --- | | B. | Tim. |  |  |  | | --- | --- | | C. | Joe and Tim should be equally energized. |  |  |  | | --- | --- | | D. | Without knowing more about the runners there is no way to predict which runner will be most energized. | |

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| 22. | Suppose you buy two tickets to the concert; one for you and one for your girlfriend. Nevertheless, the day of the concert your car brakes down preventing both of you from attending it. Assuming both you and your girlfriend had the same preferences, which of the two of you stand to lose the most from not being able to attend the concert?      |  |  | | --- | --- | | A. | You. |  |  |  | | --- | --- | | B. | Your girlfriend. |  |  |  | | --- | --- | | C. | Both of you stand to lose the same. |  |  |  | | --- | --- | | D. | None of you would stand to lose anything. | |

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| 23. | When one is considering costs of taking a trip in their car, the average cost per mile includes some items of cost that are not included in the marginal cost of a mile driven. This statement is      |  |  | | --- | --- | | A. | always true. |  |  |  | | --- | --- | | B. | always false. |  |  |  | | --- | --- | | C. | sometimes true and sometimes false depending on the circumstances. |  |  |  | | --- | --- | | D. | absurd because marginal costs do not apply to mileage costs. | |

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| 24. | We say economists are doing positive economics when they      |  |  | | --- | --- | | A. | focus on policies and rhetoric that encourage people to be optimistic about the future. |  |  |  | | --- | --- | | B. | look for regularities and principles in economic life that can help show how the economy works. |  |  |  | | --- | --- | | C. | claim that there is no value free social science so articulating one's values is important. |  |  |  | | --- | --- | | D. | try to improve the welfare of all citizens. | |

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| 25. | You can drive to campus, take a bus, or walk. Driving costs you $1/mile in gas and maintenance, the bus costs $1 for unlimited distance, and walking is free but involves a disutility equivalent to $1/mile. If you live 2 miles from campus, and are a rational decision maker, what is your reservation price for a bus ticket?      |  |  | | --- | --- | | A. | $0 |  |  |  | | --- | --- | | B. | $1 |  |  |  | | --- | --- | | C. | $2 |  |  |  | | --- | --- | | D. | $4 | |

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| 26. | Unbridled self-interest fails to coordinate resource flows most effectively in which of the following cases?      |  |  | | --- | --- | | A. | The production of bread. |  |  |  | | --- | --- | | B. | The building of a tornado warning siren. |  |  |  | | --- | --- | | C. | The production of cars. |  |  |  | | --- | --- | | D. | The production of haircuts. | |

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| 27. | If you receive $18 worth of pleasure from the first hole of golf played and your additional pleasure from succeeding holes drops $1 for each hole played, how many holes of golf would you play if you had to pay $2.10 per hole?      |  |  | | --- | --- | | A. | 9 |  |  |  | | --- | --- | | B. | 12 |  |  |  | | --- | --- | | C. | 14 |  |  |  | | --- | --- | | D. | 16 | |

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| 28. | If you receive $18 worth of pleasure from the first hole of golf played and your additional pleasure from succeeding holes drops $1 for each hole played, if the cost per hole is zero, how many holes of golf will you play?      |  |  | | --- | --- | | A. | 16 |  |  |  | | --- | --- | | B. | 17 |  |  |  | | --- | --- | | C. | 18 |  |  |  | | --- | --- | | D. | 19 | |

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| 29. | If you receive $18 worth of pleasure from the first hole of golf played and your additional pleasure from succeeding holes drops $1 for each hole played. You must pay $25 up front to get on the course but you can then play as many holes as you like for the day without any further charge. How many holes of golf will you play?      |  |  | | --- | --- | | A. | 9 |  |  |  | | --- | --- | | B. | 12 |  |  |  | | --- | --- | | C. | 18 |  |  |  | | --- | --- | | D. | As many holes as can be played from dawn until dusk. | |

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| 30. | Suppose the first hour of study today will allow you to answer 10 correct questions in tomorrow's exam. After the first hour, the marginal benefit of each additional hour of study is reduced by 2 (meaning if you study 2 hours today your total number of correct responses tomorrow will be 18 and if you study 3 hours it will be 24 and so on). If the costs of studying each additional hour are zero, how many hours you should study?      |  |  | | --- | --- | | A. | 18 |  |  |  | | --- | --- | | B. | 10 |  |  |  | | --- | --- | | C. | 6 |  |  |  | | --- | --- | | D. | 0 | |

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| 31. | The marginal benefit of a typical activity      |  |  | | --- | --- | | A. | increases as long as the activity has any value to you. |  |  |  | | --- | --- | | B. | decreases as you do more of the activity. |  |  |  | | --- | --- | | C. | stays the same if the cost of doing the activity stays the same. |  |  |  | | --- | --- | | D. | can never be negative. | |

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| 32. | If the benefits of X = $100 and the price of X = $50, then      |  |  | | --- | --- | | A. | $100 is the reservation price. |  |  |  | | --- | --- | | B. | you will be indifferent between buying X and keeping your money. |  |  |  | | --- | --- | | C. | $0 is the reservation price. |  |  |  | | --- | --- | | D. | you should not buy X. | |

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| 33. | You have just won a ticket to see John Mayer in concert this Saturday evening. Nevertheless, it would cost you around $20 in transportation costs to go to the concert since you would have to drive to the neighboring city (where the concert is taking place). Tickets for the concert are selling for $100 in your town. Assuming you only work Monday-Fridays, the cost of going to the concert is:      |  |  | | --- | --- | | A. | $0 |  |  |  | | --- | --- | | B. | $100 |  |  |  | | --- | --- | | C. | $120 |  |  |  | | --- | --- | | D. | $80 | |

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| 34. | You are in the line to go see a movie when you suddenly realized you have lost your ticket. It would cost you $10 to buy a new ticket. Now you are deciding whether to buy a new ticket or not. Assuming you have enough money to buy a new ticket, you would always buy the new ticket as long as:      |  |  | | --- | --- | | A. | your reservation price for it is equal or larger than $10. |  |  |  | | --- | --- | | B. | the new ticket is free. |  |  |  | | --- | --- | | C. | your reservation price for it is equal or larger than $20. |  |  |  | | --- | --- | | D. | the new ticket is less expensive than the first. | |

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| 35. | Which of the following statements could be considered a normative statement?      |  |  | | --- | --- | | A. | Food stamps are a good way to help low-income people to afford food. |  |  |  | | --- | --- | | B. | Food stamps allow low-income people to buy more food. |  |  |  | | --- | --- | | C. | Most low-income people use Food Stamps to buy food. |  |  |  | | --- | --- | | D. | A large portion of the government budget is used to provide Food Stamps to low-income people. | |

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| 36. | You recently took the car to the mechanic to fix its engine. The mechanic had quoted you a total price for the work of $1000, and you had decided to go ahead with the work. Nevertheless, when you go to pick up the car he tells you that in order to complete the job he needs to buy another part adding about $200 extra to the cost of fixing the car. According to the cost-benefit rule you should pay the extra money to finish the job only if the benefits of using the car are greater or equal to      |  |  | | --- | --- | | A. | $200. |  |  |  | | --- | --- | | B. | $1,000. |  |  |  | | --- | --- | | C. | $1,200. |  |  |  | | --- | --- | | D. | 0. | |

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| 37. | According to the text, standard economic models, based on self-interest where calculations appear to be made for every decision,      |  |  | | --- | --- | | A. | are accurate descriptions of human behavior and the motivations that drive it. |  |  |  | | --- | --- | | B. | describe the motivations of people but fail as useful predictors of behavior. |  |  |  | | --- | --- | | C. | provide good predictions of behavior even if they don't describe what actually happens. |  |  |  | | --- | --- | | D. | are often criticized by other social sciences that use less formal modeling. | |

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| 38. | Adam Smith wrote two very important books. The Wealth of Nations describes how markets work when people exercise self-interest. The other claims that humans      |  |  | | --- | --- | | A. | constantly miscalculate and make bad decisions. |  |  |  | | --- | --- | | B. | have a moral sense which gives them an interest in the wellbeing of others. |  |  |  | | --- | --- | | C. | have not relied enough on the visible hand of government to control markets. |  |  |  | | --- | --- | | D. | who reject religion will be unsuccessful in markets. | |

**Essay Questions**

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| 39. | When you golf you receive 18 units of pleasure from the first hole and on each hole thereafter your pleasure drops by one unit so that the 17th hole gives you 17 units of pleasure etc. If you play 5 holes and the rain hits so that you quit playing, what is the total pleasure, the average pleasure and the marginal pleasure experienced at the last hole played? Answer this with numerical answers and then graph the story. |

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| 40. | Academic institutions frequently talk about academic excellence and how they have superior programs in everything. "If it is not top quality it will not be offered here" seems to be the theme of many college catalogs. Explain, on the basis of material in this chapter, why this public relations noise is not believable. |

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| 41. | Give an example, not similar to the text material, where you erroneously took sunk costs into account where it was inappropriate to do so. |

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| 42. | Give an example, not similar to the text material, where you made a decision based on your private costs only, and should have made a different decision if all costs had been considered. |

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| 43. | One of the reasons why men have shorter lines at public rest rooms is because their bathrooms have many more urinals than toilets so turnover is much faster. The efficiency of urinals in terms of water usage and time savings seems clear, yet no one uses urinals in their own homes. This seems to be a curious puzzle. A good economic naturalist should have some explanation for this lack of urinals in homes. What reasons can you give for this puzzle? |

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| 44. | Say you and two friends are 13,500 feet into a hiking trip to the summit of a 14,000 peak in Colorado. At that point, a rainstorm comes up all of a sudden and makes the last 500 feet trek quite treacherous. One of your friends wants to stop and head down and argues it would be dangerous to continue. He says he doesn't care about the 4 hours he has hiked already to get where he is, he only cares about the final 500 feet. Your other friend, however, wants to continue and argues that it would be stupid to quit so close to the summit, especially after all the hard work you have incurred. Which one of your two friends has a more rational argument? Please explain using the concepts from the textbook. |

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| 45. | Which of the following sentences is a positive claim and which is a normative claim? We need a higher minimum wage. Working people at minimum wage are not above the poverty level. That is not fair. But a higher minimum wage will mean that some low wage workers will be laid off and have no job. |

Chapter 01 Thinking Like an Economist Answer Key

**Multiple Choice Questions**

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| 1. | Microeconomics is primarily the study of how      |  |  | | --- | --- | | A. | the stock market works. |  |  |  | | --- | --- | | **B.** | people choose among alternatives. |  |  |  | | --- | --- | | C. | businesses can make money. |  |  |  | | --- | --- | | D. | the economy functions as a whole. | |

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| *AACSB: Reflective Thinking Accessibility: Keyboard Navigation Blooms: Remember Difficulty: 1 Easy Learning Objective: 01-08 Explain the difference between microeconomics and macroeconomics. Topic: Microeconomics and Macroeconomics* |

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| 2. | If you are at an all-you-can-eat buffet dinner and you are considering whether to eat another dessert, you, as a rational consumer should decide to eat the desert      |  |  | | --- | --- | | **A.** | if it brings you any pleasure at all. |  |  |  | | --- | --- | | B. | if it brings you more pleasure than the price you paid for the meal. |  |  |  | | --- | --- | | C. | if it brings you as much pleasure as the desert costs if it is ordered a la carte. |  |  |  | | --- | --- | | D. | no matter what because you want to get more for your money. | |

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| *AACSB: Reflective Thinking Accessibility: Keyboard Navigation Blooms: Understand Difficulty: 2 Medium Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 3. | Say your girlfriend has received two free tickets to the Sunday movie matinee and she wants you to go with her. Nevertheless, the movie plays at the same time you were planning to watch the football game on the TV. As a rational person you should decide to go to the movie      |  |  | | --- | --- | | A. | always, since the tickets were free. |  |  |  | | --- | --- | | B. | only if you would gain some pleasure from it. |  |  |  | | --- | --- | | **C.** | only if the pleasure you will gain from it outweighs the pleasure you would gain from watching the football game. |  |  |  | | --- | --- | | D. | only if it brings you more pleasure than the cost of the tickets. | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Analyze Difficulty: 3 Hard Learning Objective: 01-01 Explain and apply the cost-benefit principle. Topic: The Cost-Benefit Approach to Decisions* |

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| 4. | The reservation price of good X is      |  |  | | --- | --- | | A. | the market price for a good. |  |  |  | | --- | --- | | B. | any price above what you would be willing to pay for the good. |  |  |  | | --- | --- | | **C.** | the price at which one would be indifferent between good X and simply keeping the money. |  |  |  | | --- | --- | | D. | the cost of producing good X. | |

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| *AACSB: Reflective Thinking Accessibility: Keyboard Navigation Blooms: Understand Difficulty: 2 Medium Learning Objective: 01-01 Explain and apply the cost-benefit principle. Topic: The Cost-Benefit Approach to Decisions* |

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| 5. | If the benefits of X = $50 and the price of X = $50, then      |  |  | | --- | --- | | A. | $100 is the reservation price. |  |  |  | | --- | --- | | **B.** | you will be indifferent between buying X and keeping your money. |  |  |  | | --- | --- | | C. | $0 is the reservation price. |  |  |  | | --- | --- | | D. | you should buy X. | |

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| *AACSB: Reflective Thinking Accessibility: Keyboard Navigation Blooms: Understand Difficulty: 2 Medium Learning Objective: 01-01 Explain and apply the cost-benefit principle. Topic: The Cost-Benefit Approach to Decisions* |

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| 6. | Your bank account pays 3% interest per year. You loan a friend $100 for one year at zero interest. Assuming the loan is paid on time the opportunity cost of the loan is      |  |  | | --- | --- | | **A.** | $3. |  |  |  | | --- | --- | | B. | $100. |  |  |  | | --- | --- | | C. | $103. |  |  |  | | --- | --- | | D. | $0. | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 2 Medium Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 7. | You decide to go skiing this weekend. It costs $50 for transportation, $50 for lodging, $30 for ski lift tickets and you could have earned $100 as a waiter. What is the total cost of the ski weekend?      |  |  | | --- | --- | | **A.** | $230 |  |  |  | | --- | --- | | B. | $130 |  |  |  | | --- | --- | | C. | $100 |  |  |  | | --- | --- | | D. | $80 | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 2 Medium Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 8. | You decide to go skiing this weekend. It costs $50 for transportation, $50 for lodging, $30 for ski lift tickets. You are unemployed. What is the total cost of the ski weekend?      |  |  | | --- | --- | | A. | $230 |  |  |  | | --- | --- | | **B.** | $130 |  |  |  | | --- | --- | | C. | $100 |  |  |  | | --- | --- | | D. | $80 | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 2 Medium Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 9. | You decide to go skiing this weekend. It costs $50 for transportation, $50 for lodging, $30 for ski lift tickets and you could have earned $100 as a waiter at a job you love so much you would do it as a volunteer. What is the total cost of the ski weekend?      |  |  | | --- | --- | | **A.** | $230 |  |  |  | | --- | --- | | B. | $130 |  |  |  | | --- | --- | | C. | $100 |  |  |  | | --- | --- | | D. | $80 | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 2 Medium Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 10. | Your parents have given you a new car on your 16th birthday for which they paid about $24,000. Assume this is also the price you would get if you decided to sell the car a month after getting it. The monthly costs of driving the car are $100 for oil changes and $200 for gas. If you decide to keep the car, the total costs of the car to you this month will be      |  |  | | --- | --- | | A. | $2,300. |  |  |  | | --- | --- | | B. | $300. |  |  |  | | --- | --- | | **C.** | $24,300. |  |  |  | | --- | --- | | D. | $0. | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 3 Hard Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 11. | Your parents have given you a new car on your 16th birthday for which they paid about $24,000. Assume this is also the price you would get if you decided to sell the car a month after getting it. The monthly costs of driving the car are $100 for oil changes and $200 for gas. What are the opportunity costs of driving the car this month?      |  |  | | --- | --- | | A. | $300 |  |  |  | | --- | --- | | B. | $2,000 |  |  |  | | --- | --- | | **C.** | $24,300 |  |  |  | | --- | --- | | D. | $0 | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 3 Hard Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 12. | Here are the costs of going to college: tuition $5,000; books $200; housing $1,000; food $1,000; lost income from work $10,000. Studying and work are equally desirable in your mind. Suppose that you could live at home at no cost to you if you worked, but must live on campus if you go to school. What is the total opportunity cost to you of going to school rather than working? (Food costs the same at school or home.)      |  |  | | --- | --- | | **A.** | $16,200 |  |  |  | | --- | --- | | B. | $7,200 |  |  |  | | --- | --- | | C. | $5,200 |  |  |  | | --- | --- | | D. | $15,200 | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 3 Hard Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 13. | Here are the costs of going to college: tuition $5,000; books $200; housing $1,000; food $1,000; lost income from work $10,000. Studying and work are equally desirable in your mind. Suppose you must live on your own anyway. What is the cost of going to school?      |  |  | | --- | --- | | A. | $17,200 |  |  |  | | --- | --- | | B. | $7,200 |  |  |  | | --- | --- | | **C.** | $15,200 |  |  |  | | --- | --- | | D. | $16,200 | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 3 Hard Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 14. | Here are the costs of going to college: tuition $5,000; books $200; housing $1,000; food $1,000; lost income from work $10,000. Studying and work are equally desirable in your mind. Suppose that you could work part-time and make $5,000 at a job you would volunteer to do. You live on campus instead of at home. What is the cost of going to school?      |  |  | | --- | --- | | A. | $16,200 |  |  |  | | --- | --- | | B. | $7,200 |  |  |  | | --- | --- | | C. | $5,200 |  |  |  | | --- | --- | | **D.** | $11,200 | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 3 Hard Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 15. | You decide to lend $100 to a friend interest free for one year. You calculate that you could have earned 10% interest. What is the opportunity cost of the loan if it is paid on time?      |  |  | | --- | --- | | **A.** | $10 |  |  |  | | --- | --- | | B. | $100 |  |  |  | | --- | --- | | C. | $110 |  |  |  | | --- | --- | | D. | $0 | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 3 Hard Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 16. | You are considering renting a car for the weekend. It costs $200 for the car plus $0.20 per mile (including gas). If you decide to go on a 300 mile voyage what is the total cost of the rental?      |  |  | | --- | --- | | A. | $200 |  |  |  | | --- | --- | | B. | $60 |  |  |  | | --- | --- | | **C.** | $260 |  |  |  | | --- | --- | | D. | $0 | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 2 Medium Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 17. | You are considering renting a car for the weekend. It costs $200 for the car plus $0.20 per mile (including gas). Suppose you have already rented the car for the week and then add the 300 mile addition to your trip. Now what is the cost of the journey?      |  |  | | --- | --- | | A. | $100 |  |  |  | | --- | --- | | **B.** | $60 |  |  |  | | --- | --- | | C. | $260 |  |  |  | | --- | --- | | D. | $0 | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 2 Medium Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 18. | You are considering renting a car for the weekend. It costs $200 for the car plus $0.20 per mile (including gas). If you decide to take a detour that adds 50 miles above the 300 miles, what is the cost of the detour?      |  |  | | --- | --- | | **A.** | $10 |  |  |  | | --- | --- | | B. | $70 |  |  |  | | --- | --- | | C. | $270 |  |  |  | | --- | --- | | D. | $200 | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 2 Medium Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 19. | Adam Smith in The Wealth of Nations argued that      |  |  | | --- | --- | | **A.** | society works best when people act in their own interest. |  |  |  | | --- | --- | | B. | society works best when people act unselfishly. |  |  |  | | --- | --- | | C. | society works best when people act as if they were invisible to others. |  |  |  | | --- | --- | | D. | the social order needs the guidance of the government's visible hand. | |

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| *AACSB: Reflective Thinking Accessibility: Keyboard Navigation Blooms: Remember Difficulty: 1 Easy Learning Objective: 01-05 Describe Adam Smith's invisible hand theory. Topic: The Invisible Hand* |

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| 20. | Your textbook costs $100 and the college snack shop sells ice cream for $1. Which of the following statements is true for most people?      |  |  | | --- | --- | | A. | You would be indifferent between a bookstore sale of 1% off on your text and one free ice cream in the snack shop. |  |  |  | | --- | --- | | B. | Most people will get greater satisfaction from the bookstore sale than from the snack shop giveaway. |  |  |  | | --- | --- | | **C.** | Most people will get greater satisfaction from the snack shop giveaway than from the bookstore sale. |  |  |  | | --- | --- | | D. | Because people are very different there is no general principle that can be suggested regarding the satisfaction people get in these situations. | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Evaluate Difficulty: 3 Hard Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 21. | Joe is one mile from the finish of a grueling 26 mile marathon. Tim is at the four mile mark of a five mile run. Which runner is most likely to be emotionally energized for the race to the finish line?      |  |  | | --- | --- | | **A.** | Joe. |  |  |  | | --- | --- | | B. | Tim. |  |  |  | | --- | --- | | C. | Joe and Tim should be equally energized. |  |  |  | | --- | --- | | D. | Without knowing more about the runners there is no way to predict which runner will be most energized. | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Evaluate Difficulty: 3 Hard Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 22. | Suppose you buy two tickets to the concert; one for you and one for your girlfriend. Nevertheless, the day of the concert your car brakes down preventing both of you from attending it. Assuming both you and your girlfriend had the same preferences, which of the two of you stand to lose the most from not being able to attend the concert?      |  |  | | --- | --- | | A. | You. |  |  |  | | --- | --- | | B. | Your girlfriend. |  |  |  | | --- | --- | | **C.** | Both of you stand to lose the same. |  |  |  | | --- | --- | | D. | None of you would stand to lose anything. | |

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| *AACSB: Reflective Thinking Accessibility: Keyboard Navigation Blooms: Understand Difficulty: 2 Medium Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 23. | When one is considering costs of taking a trip in their car, the average cost per mile includes some items of cost that are not included in the marginal cost of a mile driven. This statement is      |  |  | | --- | --- | | **A.** | always true. |  |  |  | | --- | --- | | B. | always false. |  |  |  | | --- | --- | | C. | sometimes true and sometimes false depending on the circumstances. |  |  |  | | --- | --- | | D. | absurd because marginal costs do not apply to mileage costs. | |

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| *AACSB: Reflective Thinking Accessibility: Keyboard Navigation Blooms: Remember Difficulty: 1 Easy Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 24. | We say economists are doing positive economics when they      |  |  | | --- | --- | | A. | focus on policies and rhetoric that encourage people to be optimistic about the future. |  |  |  | | --- | --- | | **B.** | look for regularities and principles in economic life that can help show how the economy works. |  |  |  | | --- | --- | | C. | claim that there is no value free social science so articulating one's values is important. |  |  |  | | --- | --- | | D. | try to improve the welfare of all citizens. | |

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| *AACSB: Reflective Thinking Accessibility: Keyboard Navigation Blooms: Understand Difficulty: 2 Medium Learning Objective: 01-07 Explain the difference between positive and normative theories. Topic: Positive Questions and Normative Questions* |

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| 25. | You can drive to campus, take a bus, or walk. Driving costs you $1/mile in gas and maintenance, the bus costs $1 for unlimited distance, and walking is free but involves a disutility equivalent to $1/mile. If you live 2 miles from campus, and are a rational decision maker, what is your reservation price for a bus ticket?      |  |  | | --- | --- | | A. | $0 |  |  |  | | --- | --- | | B. | $1 |  |  |  | | --- | --- | | **C.** | $2 |  |  |  | | --- | --- | | D. | $4 | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 3 Hard Learning Objective: 01-01 Explain and apply the cost-benefit principle. Topic: The Cost-Benefit Approach to Decisions* |

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| 26. | Unbridled self-interest fails to coordinate resource flows most effectively in which of the following cases?      |  |  | | --- | --- | | A. | The production of bread. |  |  |  | | --- | --- | | **B.** | The building of a tornado warning siren. |  |  |  | | --- | --- | | C. | The production of cars. |  |  |  | | --- | --- | | D. | The production of haircuts. | |

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| *AACSB: Reflective Thinking Accessibility: Keyboard Navigation Blooms: Understand Difficulty: 2 Medium Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 27. | If you receive $18 worth of pleasure from the first hole of golf played and your additional pleasure from succeeding holes drops $1 for each hole played, how many holes of golf would you play if you had to pay $2.10 per hole?      |  |  | | --- | --- | | A. | 9 |  |  |  | | --- | --- | | B. | 12 |  |  |  | | --- | --- | | C. | 14 |  |  |  | | --- | --- | | **D.** | 16 | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 2 Medium Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 28. | If you receive $18 worth of pleasure from the first hole of golf played and your additional pleasure from succeeding holes drops $1 for each hole played, if the cost per hole is zero, how many holes of golf will you play?      |  |  | | --- | --- | | A. | 16 |  |  |  | | --- | --- | | B. | 17 |  |  |  | | --- | --- | | **C.** | 18 |  |  |  | | --- | --- | | D. | 19 | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 2 Medium Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 29. | If you receive $18 worth of pleasure from the first hole of golf played and your additional pleasure from succeeding holes drops $1 for each hole played. You must pay $25 up front to get on the course but you can then play as many holes as you like for the day without any further charge. How many holes of golf will you play?      |  |  | | --- | --- | | A. | 9 |  |  |  | | --- | --- | | B. | 12 |  |  |  | | --- | --- | | **C.** | 18 |  |  |  | | --- | --- | | D. | As many holes as can be played from dawn until dusk. | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 3 Hard Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 30. | Suppose the first hour of study today will allow you to answer 10 correct questions in tomorrow's exam. After the first hour, the marginal benefit of each additional hour of study is reduced by 2 (meaning if you study 2 hours today your total number of correct responses tomorrow will be 18 and if you study 3 hours it will be 24 and so on). If the costs of studying each additional hour are zero, how many hours you should study?      |  |  | | --- | --- | | A. | 18 |  |  |  | | --- | --- | | B. | 10 |  |  |  | | --- | --- | | **C.** | 6 |  |  |  | | --- | --- | | D. | 0 | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 2 Medium Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 31. | The marginal benefit of a typical activity      |  |  | | --- | --- | | A. | increases as long as the activity has any value to you. |  |  |  | | --- | --- | | **B.** | decreases as you do more of the activity. |  |  |  | | --- | --- | | C. | stays the same if the cost of doing the activity stays the same. |  |  |  | | --- | --- | | D. | can never be negative. | |

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| *AACSB: Reflective Thinking Accessibility: Keyboard Navigation Blooms: Remember Difficulty: 1 Easy Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 32. | If the benefits of X = $100 and the price of X = $50, then      |  |  | | --- | --- | | **A.** | $100 is the reservation price. |  |  |  | | --- | --- | | B. | you will be indifferent between buying X and keeping your money. |  |  |  | | --- | --- | | C. | $0 is the reservation price. |  |  |  | | --- | --- | | D. | you should not buy X. | |

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| *AACSB: Reflective Thinking Accessibility: Keyboard Navigation Blooms: Understand Difficulty: 2 Medium Learning Objective: 01-01 Explain and apply the cost-benefit principle. Topic: The Cost-Benefit Approach to Decisions* |

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| 33. | You have just won a ticket to see John Mayer in concert this Saturday evening. Nevertheless, it would cost you around $20 in transportation costs to go to the concert since you would have to drive to the neighboring city (where the concert is taking place). Tickets for the concert are selling for $100 in your town. Assuming you only work Monday-Fridays, the cost of going to the concert is:      |  |  | | --- | --- | | A. | $0 |  |  |  | | --- | --- | | B. | $100 |  |  |  | | --- | --- | | **C.** | $120 |  |  |  | | --- | --- | | D. | $80 | |

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| *AACSB: Reflective Thinking Accessibility: Keyboard Navigation Blooms: Understand Difficulty: 2 Medium Learning Objective: 01-01 Explain and apply the cost-benefit principle. Topic: The Cost-Benefit Approach to Decisions* |

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| 34. | You are in the line to go see a movie when you suddenly realized you have lost your ticket. It would cost you $10 to buy a new ticket. Now you are deciding whether to buy a new ticket or not. Assuming you have enough money to buy a new ticket, you would always buy the new ticket as long as:      |  |  | | --- | --- | | **A.** | your reservation price for it is equal or larger than $10. |  |  |  | | --- | --- | | B. | the new ticket is free. |  |  |  | | --- | --- | | C. | your reservation price for it is equal or larger than $20. |  |  |  | | --- | --- | | D. | the new ticket is less expensive than the first. | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Analyze Difficulty: 3 Hard Learning Objective: 01-01 Explain and apply the cost-benefit principle. Topic: The Cost-Benefit Approach to Decisions* |

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| 35. | Which of the following statements could be considered a normative statement?      |  |  | | --- | --- | | **A.** | Food stamps are a good way to help low-income people to afford food. |  |  |  | | --- | --- | | B. | Food stamps allow low-income people to buy more food. |  |  |  | | --- | --- | | C. | Most low-income people use Food Stamps to buy food. |  |  |  | | --- | --- | | D. | A large portion of the government budget is used to provide Food Stamps to low-income people. | |

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| *AACSB: Reflective Thinking Accessibility: Keyboard Navigation Blooms: Understand Difficulty: 2 Medium Learning Objective: 01-07 Explain the difference between positive and normative theories. Topic: Positive Questions and Normative Questions* |

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| 36. | You recently took the car to the mechanic to fix its engine. The mechanic had quoted you a total price for the work of $1000, and you had decided to go ahead with the work. Nevertheless, when you go to pick up the car he tells you that in order to complete the job he needs to buy another part adding about $200 extra to the cost of fixing the car. According to the cost-benefit rule you should pay the extra money to finish the job only if the benefits of using the car are greater or equal to      |  |  | | --- | --- | | **A.** | $200. |  |  |  | | --- | --- | | B. | $1,000. |  |  |  | | --- | --- | | C. | $1,200. |  |  |  | | --- | --- | | D. | 0. | |

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| *AACSB: Analytic Accessibility: Keyboard Navigation Blooms: Apply Difficulty: 3 Hard Learning Objective: 01-01 Explain and apply the cost-benefit principle. Topic: The Cost-Benefit Approach to Decisions* |

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| 37. | According to the text, standard economic models, based on self-interest where calculations appear to be made for every decision,      |  |  | | --- | --- | | A. | are accurate descriptions of human behavior and the motivations that drive it. |  |  |  | | --- | --- | | B. | describe the motivations of people but fail as useful predictors of behavior. |  |  |  | | --- | --- | | **C.** | provide good predictions of behavior even if they don't describe what actually happens. |  |  |  | | --- | --- | | D. | are often criticized by other social sciences that use less formal modeling. | |

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| *AACSB: Reflective Thinking Accessibility: Keyboard Navigation Blooms: Remember Difficulty: 1 Easy Learning Objective: 01-02 Explain the uses and limitations of economic models. Topic: The Role of Economic Theory* |

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| 38. | Adam Smith wrote two very important books. The Wealth of Nations describes how markets work when people exercise self-interest. The other claims that humans      |  |  | | --- | --- | | A. | constantly miscalculate and make bad decisions. |  |  |  | | --- | --- | | **B.** | have a moral sense which gives them an interest in the wellbeing of others. |  |  |  | | --- | --- | | C. | have not relied enough on the visible hand of government to control markets. |  |  |  | | --- | --- | | D. | who reject religion will be unsuccessful in markets. | |

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| *AACSB: Reflective Thinking Accessibility: Keyboard Navigation Blooms: Remember Difficulty: 1 Easy Learning Objective: 01-02 Explain the uses and limitations of economic models. Topic: The Invisible Hand* |

**Essay Questions**

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| 39. | When you golf you receive 18 units of pleasure from the first hole and on each hole thereafter your pleasure drops by one unit so that the 17th hole gives you 17 units of pleasure etc. If you play 5 holes and the rain hits so that you quit playing, what is the total pleasure, the average pleasure and the marginal pleasure experienced at the last hole played? Answer this with numerical answers and then graph the story.    The total pleasure is 80, the marginal pleasure is 14, and the average pleasure is 16. On a graph with pleasure on the vertical axis and holes played on the horizontal axis, the pleasure line begins at 18 pleasure and 1 hole. It has a slope of -1 so at 5 holes the area under the dotted lines is the total pleasure. The marginal pleasure is the area under the fifth hole played and the average is the total pleasure divided by 5 holes. It is easy to see that average pleasure does not relate to any given hole. |

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| *AACSB: Analytic Blooms: Apply Difficulty: 2 Medium Learning Objective: 01-04 Translate quantitative information about costs and benefits into graphical form. Topic: Using Marginal Benefit and Marginal Cost Graphically* |

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| 40. | Academic institutions frequently talk about academic excellence and how they have superior programs in everything. "If it is not top quality it will not be offered here" seems to be the theme of many college catalogs. Explain, on the basis of material in this chapter, why this public relations noise is not believable.     Colleges must look at the cost of providing top quality education. If they accepted a bit less quality in several programs and were able to offer a new program or two with the money saved, their constituency may be happier and revenues could go up. Again costs and benefits must be evaluated on all the margins. It may be too costly to provide the best of everything. |

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| *AACSB: Reflective Thinking Blooms: Understand Difficulty: 2 Medium Learning Objective: 01-01 Explain and apply the cost-benefit principle. Topic: The Cost-Benefit Approach to Decisions* |

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| 41. | Give an example, not similar to the text material, where you erroneously took sunk costs into account where it was inappropriate to do so.     Answers may vary. |

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| *AACSB: Reflective Thinking Blooms: Understand Difficulty: 2 Medium Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 42. | Give an example, not similar to the text material, where you made a decision based on your private costs only, and should have made a different decision if all costs had been considered.     Answers may vary. |

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| *AACSB: Reflective Thinking Blooms: Understand Difficulty: 2 Medium Learning Objective: 01-06 Give several clear examples of how basic economic principles can be used to explain patterns of behavior observed in everyday life. Topic: The Economic Naturalist* |

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| 43. | One of the reasons why men have shorter lines at public rest rooms is because their bathrooms have many more urinals than toilets so turnover is much faster. The efficiency of urinals in terms of water usage and time savings seems clear, yet no one uses urinals in their own homes. This seems to be a curious puzzle. A good economic naturalist should have some explanation for this lack of urinals in homes. What reasons can you give for this puzzle?    The most obvious reason is that there are usually no waiting lines in homes. However, water savings must be less than the extra cost of the fixture and the space needed to install it. |

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| *AACSB: Reflective Thinking Blooms: Understand Difficulty: 2 Medium Learning Objective: 01-06 Give several clear examples of how basic economic principles can be used to explain patterns of behavior observed in everyday life. Topic: The Economic Naturalist* |

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| 44. | Say you and two friends are 13,500 feet into a hiking trip to the summit of a 14,000 peak in Colorado. At that point, a rainstorm comes up all of a sudden and makes the last 500 feet trek quite treacherous. One of your friends wants to stop and head down and argues it would be dangerous to continue. He says he doesn't care about the 4 hours he has hiked already to get where he is, he only cares about the final 500 feet. Your other friend, however, wants to continue and argues that it would be stupid to quit so close to the summit, especially after all the hard work you have incurred. Which one of your two friends has a more rational argument? Please explain using the concepts from the textbook.    The 13,500 feet are a sunk cost so only the impact of the last 500 is relevant. Because the cost of the last 500 is very difficult the friend who want to turn back is more rational. |

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| *AACSB: Analytic Blooms: Evaluate Difficulty: 2 Medium Learning Objective: 01-03 Describe the four common decision pitfalls. Topic: Common Pitfalls in Decision Making* |

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| 45. | Which of the following sentences is a positive claim and which is a normative claim? We need a higher minimum wage. Working people at minimum wage are not above the poverty level. That is not fair. But a higher minimum wage will mean that some low wage workers will be laid off and have no job.   The first and third sentences are normative and the other two are positive statements. |
| *AACSB: Reflective Thinking Blooms: Remember Difficulty: 1 Easy Learning Objective: 01-07 Explain the difference between positive and normative theories. Topic: Positive Questions and Normative Questions* | |