Study Guide

for use with

ECONOMICS OF SOCIAL ISSUES

Prepared by

DeVon L. Yoho

Eighth Edition

Ansel M. Sharp

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Prepared by
DeVon L. Yoho
Department of Economics
Ball State University

Ansel M. Sharp
Frank W. Wilson Professor
of The University of the South

Charles A. Register
of Kent State University

Richard H. Leftwich
of Leftwich Associates

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Preface

I hope that this **Student's Guide and Workbook** will help you learn basic economics as you study the *Economics of Social Issues*. It has two major purposes: (a) to help you study systematically and, therefore, more effectively, and (2) to provide you with learning objectives, questions, and problems that will help you understand the tools of economic analysis and enable you to apply them to social issues and problems. The **Guide** consists of several major components. Their purposes and how best to use them are discussed below.

Learning Objectives. The learning objectives are brief statements of expected learning outcomes. They require you to define, list, distinguish among, explain, and evaluate. You should do what they suggest in writing.

The arrangement of the learning objectives follows the content sequence of the chapter. Therefore, the first objective is not necessarily more important than any of the other objectives.

The objectives are not meant to be ends in themselves. They are designed to help you identify quickly the important chapter content. In this way, they should aid you in using your study time efficiently and guide you to a satisfactory performance.

Chapter Orientation. This section of the **Guide** highlights the chapter content. In addition, it indicates, as does the chapter, that the learning objectives are interrelated and how they are interrelated. You may find it helpful to read the "Chapter Orientation" immediately after reading the learning objectives and before reading the chapter. Both sections of the **Guide** should help you focus your reading of the chapter upon its main points.

Checklist of Economic Concepts. This is a list of important economic concepts used in the chapter. The list is referenced by page number to the textbook. You should try to understand the meaning of the concept – avoid memorization.

Consider This. This section of the **Guide** provides additional content that complements, illustrates, or expands upon the textbook content. Each "Consider This" is self-contained and therefore its content is not included explicitly in the learning objectives, study questions, or self-test.

Study Questions. You should use the study questions to check your understanding of the chapter's content. They parallel very closely the learning objectives. Each study question is referenced by page number with the relevant discussion in the chapter.

Self-test. This section of the **Guide** contains true-false questions, multiple-choice questions, and problems that you can use to assess your attainment of the learning objectives. You should do the self-test without reference to the text-book chapter or the "Answers to the Self-test."

Answers to the Self-test. Answers to the questions of the self-test as well as page references to the relevant discussion in the chapter are provided in this section of the **Guide.** If you score 90

percent or better on the self-test, you probably have a good understanding of the chapter's content.

May I suggest that you use the **Guide** to study economics systematically. First, read quickly the learning objectives and chapter orientation and then examine the "Checklist of Economic Concepts." You should not be surprised to encounter some unfamiliar terminology, concepts, and ideas. Remember that they represent the challenges of the learning experience. Second, read the chapter. As you read, mark beside the learning objectives the textbook page numbers which contain information relevant to the objectives. Third, read the chapter more carefully and begin to outline your answers to the study questions. Write out your answers to the study questions. After you have answered all the study questions you are ready to take the self-test.

Every chapter in the *Economics of Social Issues* has the same general organization. First, the problem posed by the issue is identified. Second, the basic economic tools necessary to analyze the issue are developed. Third, those economic tools are applied to the problem in order to analyze it and to explore possible solutions to it. You should find it helpful to keep this organizational structure in mind.

I am grateful to Denise Kinney for putting the manuscript in final typewritten form. But I assume the responsibility for the remaining errors and for collecting royalties.

DEVON L. YOHO

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Chapter 1
Human Misery

The Biggest Issue of Them All

LEARNING OBJECTIVES

After studying this issue, you should be able to:

1. State the reasons for a growing awareness of the world poverty problem.
2. Explain the fundamental economic problem facing all societies.
3. Explain what a production possibilities curve measures, what points lying inside and outside the curve mean, and what a shift of the curve indicates.
4. Calculate and explain alternative cost using a production possibilities curve.
5. Define gross national product (GNP), per capital GNP, and per capital real GNP.
6. Explain how an economy can provide rising living standards over time.
7. Evaluate the impact of population growth on living standards.
8. Evaluate alternative government antipoverty policies.

CHAPTER ORIENTATION

As you read the chapter try to discover what has caused people's recent concern for world poverty, what causes world poverty, and how it can be alleviated. To investigate these concerns you will need to know the determinants of living standards as well as a few other basic economic concepts.

Economics is the study of how people cope with scarcity. Our wants are virtually infinite but the resources that we use to satisfy our wants are limited. It is this inequality between wants and resources that forces persons to choose. When resources—labor, capital—are used to satisfy one want, they are unavailable for use in the satisfaction of other wants.

The production possibilities curve can be used to illustrate decision making as a consequence of scarcity. Given our limited resources, we can have more of one thing only by giving up some of something else. What is given up is the alternative cost (opportunity costs) of our choice. You must develop an appreciation for the proper labeling of a production possibilities curve. Only real quantities of goods and services appear on the axes. Resources used in the production of consumer goods are not available for use in the production of capital goods—plant, equipment, and net changes in inventories. Or, as another example of labeling, resources used in the production of loaves of bread cannot be used in the production of quarts of milk.

Pay particular attention to the assumptions on which a production possibilities curve is based. Your understanding of them will enable you to explain the impact of unemployed resources and economic growth on output combinations and to explain why some combinations of real output (consumer goods plus capital goods) are unattainable.

When you are familiar with the technical aspects of production possibilities curves, you will want to relate production possibilities curves to Gross National Product (GNP) and then relate per capital real GNP to the measurement of living standards. How do we measure living standards?

Armed with the knowledge of a few basic economic concepts you can begin to analyze the world poverty problem. To break out of the poverty trap a country must improve its resource base, efficiency, and technology. The rate of growth in the economy's real GNP must exceed the rate of growth of its population. Can governments help solve the world poverty problem?

CHECKLIST OF ECONOMIC CONCEPTS

Malthusian Theory (p. 5)
Wants (p. 6)
Labor Resources (p. 7)
Capital Resources (p. 7)
Technology (p. 8)
Production (p. 8)
Alternative Costs (p. 10)
Gross National Product, Current Dollars (p. 8)
Gross National Product, Real (p. 11)
Production Possibilities Curve (pp. 8-9)
Living Standards (pp. 10-12)
Price Index Numbers (p. 11)
Efficiency (p. 14)
Lesser Developed Countries (p. 15)
Developed Countries (p. 15)
Social Overhead Capital (p. 18)
Gross National Product, Per Capita (p. 11)

CONSIDER THIS: ECONOMISTS DISAGREE

Throughout the text, the phrase "most economists agree" is often used. Thus, it follows that sometimes economists disagree. Why do economists disagree?

Economists sometimes disagree about what the facts are because economic systems are very complex and often defy their best efforts to understand them. Furthermore, their ability to know exactly how effectively the economy functions is frequently limited by difficulties in obtaining accurate and timely measurements of economic activity. Finally, many unanticipated events affect economic activity making it difficult to predict accurately the results of many specific economic decisions.

However, even if the above constraints could be eliminated, economists would sometimes disagree on matters of appropriate economic policy because of difference in judgments about the actual or predicted effects of specific decisions. In addition, the disagreements are likely to persist because individual economists, as do most other people, hold different sets of values.

Despite disagreements and in some instances because of the disagreements, economics has contributed and continues to contribute to our understanding of social issues. Our failure to distinguish between positive economic analysis (what is) and value judgments (what ought to be) is the source of much confusion in many discussions of economic issues. In studying social issues you would be well advised to attempt to separate questions of fact from questions of value judgment.

STUDY QUESTIONS

1. Which one of the factors generating concern for the world poverty problem has influenced you the most? Why? (pp. 4-5)
2. "Country A's per capita real GNP is considerably greater than Country B's per capital real GNP. Clearly, Country A has overcome the fundamental economic problem." Evaluate. (pp. 6-8)
3. Can the economic activity of people satisfy all the wants of human beings? Explain. (pp. 6-10)
4. Draw a production possibilities curve for the choice between capital goods and services and all other goods and services. Label the diagram fully and discuss what a production possibilities curve measures. What do points lying inside and outside of the curve mean? What does a shift of the curve indicate? What causes it? (pp. 8-10)
5. If, for an economy, 20,000 calculators must be given up for 4,000 microcomputers, what is the alternative cost of a microcomputer? (p. 10)

6. In what sense is per capital real GNP a limited measure of an economy's standard of living? (p.11)
7. What measures of economic performance are helpful in determining the impact of population growth on living standards? (pp. 10-12)
8. What are the economic roots of world poverty? (pp. 12-15)
9. Is world poverty caused by high rates of population growth and/or population density? Explain. (pp. 15-17)
10. "Governments must solve the world poverty problems." Evaluate. What can governments do to help eliminate world poverty? (pp. 17-20)

SELF-TEST

TRUE-FALSE QUESTIONS Circle T (true) or F (false)

T F 1. Mass Communication has contributed to people's growing awareness of world poverty problems.

T F 2. The basic economic problem of all societies is that human wants exceed the resources available to satisfy them.

T F 3. If it is on its production possibilities curve, an economy is using its available resources inefficiently.

T F 4. For an economy producing output combinations on its production possibilities curve, the cost of an increase in the output of a good or service is the resources used to produce the output.

T F 5. GNP is defined as the total value of an economy's annual output of goods and services in final form.

T F 6. Per capital real GNP is a perfect measure of an economy's living standard despite the unequal distribution of its output among the population.

T F 7. A country's living standard will improve over time if population increases at a faster rate than real GNP.

T F 8. If an economy is to provide rising living standards over time, it must experience improvements in labor force quality, capital accumulation, and technological development.

T F 9. There is considerable evidence that population growth by itself has impinged significantly on the living standards of most developed countries.

T F 10. The economically advanced countries of the world provide economic assistance to LDCs in the form of loans and grants of money, and technical assistance.

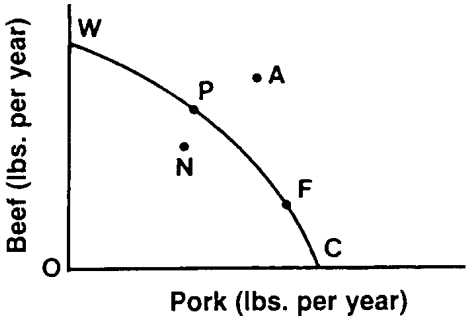
MULTIPLE CHOICE QUESTIONS Select the one best answer

1. Which of the following is a factor generating concern for the world poverty problem?
   a. Increased travel abroad
   b. Improved mass communication
   c. Rivalry between the United States and the Soviet Union
   d. All of the above.

2. Which of the following is a capital resource?
   a. Petroleum
   b. The services of an economist
   c. Money
   d. All of the above except (b).

3. With regard to human wants and economic resources, which one of the following statements is correct?
   a. Human wants are limited or scarce relative to the economic resources available for satisfying them.
   b. Human wants are unlimited while the economic resources available are scarce.
   c. Both human wants and human resources are unlimited, but nonhuman resources are limited.
   d. Both human wants and human resources are limited, but nonhuman resources are superabundant.

The following diagram applies to Questions 4-6.



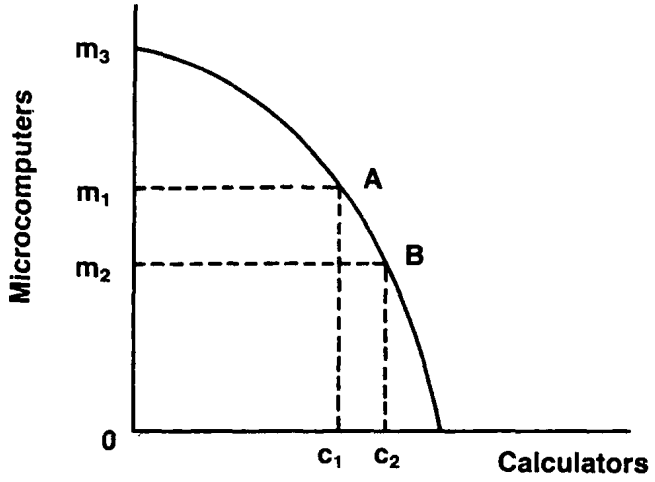
The diagram represents all that an economy can produce, in this case, of beef, pork, or some combination of them, per year.

4. The curve WC is known as a:
   a. demand curve.
   b. production possibilities curve.
   c. budget line.
   d. None of the above.

5. Which point represents underemployment of resources?
   a. F
   b. N
   c. P
   d. W

6. With given quantities of resources and constant technology, which combination of beef and pork is currently unattainable?
   a. F
   b. N
   c. A
   d. W

Questions 7 and 8 below refer to the following diagram:



7. If none of an economy's scarce resources are to be used to produce calculators, then:
   a. by giving up $0c_2$ of calculators, m_2m_3 additional units of microcomputers can be produced.
   b. an increase of m_1m_3 of microcomputers could be obtained by giving up $0c_1$ of calculators.
   c. $0m_3$ of microcomputers could be produced.
   d. All of the above.

8. The alternative cost of producing additional calculators, c_1c_2, is:
   a. $0m_2$ of microcomputers.
   b. m_2m_3 of microcomputers.
   c. m_2m_1 of microcomputers
   d. $0m_1$ of microcomputers.

9. The alternative cost of a video disk player is measured by the:
   a. the money costs of resources bought and/or hired to produce it.
   b. the value of another good or service that must be given up to obtain it.
   c. amount of labor required to produce it.
   d. All of the above.

10. The production possibilities curve illustrates the basic principle that:
    a. an economy's capacity to produce increases in proportion to its population size.
    b. if all the resources of an economy are used efficiently, more of one good can be produced only if less of another good is produced.
    c. an economy will automatically seek that level of output at which all of its resources are employed.
    d. the production of more of any one good requires no sacrifice of other goods employed.

11. Per capita real GNP:
    a. measures an economy's standard of living.
    b. has typically increased over the years.
    c. indicates the comparative economic performances of countries.
    d. All of the above.

12. To provide rising living standards over time, an economy should:
    a. improve the quality of the labor force.
    b. enhance capital accumulation.
    c. raise levels of technology.
    d. increase efficiency.
    e. All of the above.

13. The standard of living would decline if:
    a. real GNP declined and population increased.
    b. per capita real GNP declined.
    c. real GNP increased but population increased relatively more.
    d. All of the above.

14. Which one of the following statements correctly indicates the impact of population growth on living standards?
    a. Without exception, population growth by itself has reduced living standards significantly.
    b. There is considerable evidence that population growth by itself has impinged significantly on the living standards of most developed countries.
    c. Population growth and the standard of living are unrelated.
    d. A few countries may have experienced a decreased standard of living essentially as a result of population growth.

15. The greatest obstacle to economic development in LDCs is:
    a. exploitation by multinational corporations.
    b. illiteracy.
    c. political instability.
    d. None of the above.

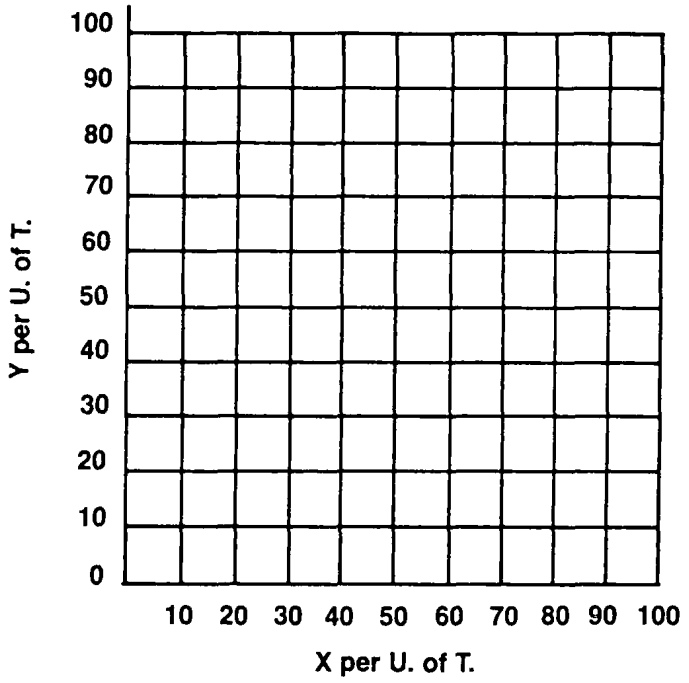
16. An LDC government can help in the capital accumulation process by:
    a. creating new capital resources directly.
    b. taxing away the returns that accrue from capital accumulation.
    c. pursuing monetary and fiscal policies conducive to economic stability.
    d. None of the above.

PROBLEMS

1. Assuming that an economy produces two goods X and Y only:

    a. plot its production possibilities curve on the graph using the following schedule:

Product X (1,000)	Product Y (1,000)
90	0
88	10
85	20
80	30
74	40
66	50
57	60
47	70
35	80
20	90
0	100



b. How much X must be given up to increase the output of Y from 40,000 to 50,000?
c. Indicate a combination of X and Y that is (1) produced inefficiently, (2) not currently attainable.
d. If the economy is able to produce an additional 10,000 units of X at each output level of Y,
   1) draw the new production possibility curve on the graph above.
   2) explain what might have caused the shift in the production possibilities curve.

2. Using Table 1-1 from the text, answer the following questions.
   a. For the years 1970 through 1985, current dollar GNP (increased/decreased).
   b. In what years did real GNP decline?
   c. For the years 1982-1985, population (increased/decreased).
   d. What has happened to the standard of living during the period 1970 through 1985?
   e. Was the increase in population responsible for the decline in the standard of living in the years 1974-75, 1980, and 1982? Explain.

ANSWERS TO SELF-TEST

TRUE-FALSE QUESTIONS

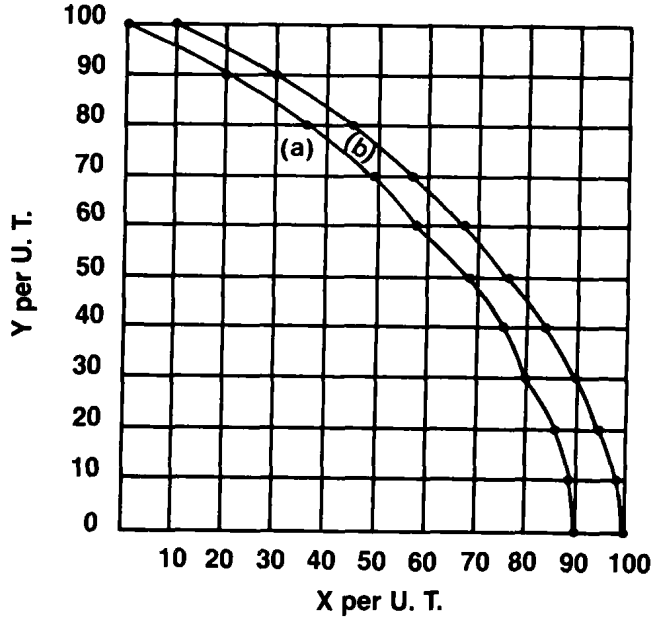
1. T (p. 5)
2. T (p. 7)
3. F (pp. 8-10)
4. F (pp. 8-10)
5. T (p. 8)
6. F (pp. 11-12)
7. F (pp.10-12)
8. T (p. 12)
9. F (p. 17)
10. T (p. 19)

MULTIPLE CHOICE QUESTIONS

1. d (pp. 4-5)
2. a (p. 7)
3. b (pp. 6-8)
4. b (pp. 8-10)
5. b (pp. 8-10)
6. c (pp. 8-10)
7. c (pp. 8-10)
8. c (pp. 8-10)
9. b (p. 10)
10. b (pp. 8-10)
11. d (pp. 10-12)
12. e (pp. 12-15)
13. d (pp. 10-12)
14. d (pp. 15-17)
15. c (pp. 17-20)
16. c (pp. 17-20)

PROBLEMS

1. a.



   b. 8,000 units of X must be given up.
   c. 1) Any combination below the production possibilities curve.
      2) Any combination outside the production possibilities curve.
   d. 1) See (b) on graph.
      2) Increases in resource quantities; improvements in resource qualities; improvements in techniques of production.

2. a. increased
   b. 1974-75, 1980, 1982
   c. increased
   d. The standard of living increased in every year except 1974-75, 1980, and 1982.
   e. No. The decline in real GNP caused the reduction in the standard of living.

Appendix: Graphic Tools of Analysis

LEARNING OBJECTIVES

After studying this appendix, you should be able to:

1. Explain why economists use graphs.
2. Construct a graph showing the relationship between two variables and explain the relationship in writing.
3. Distinguish between direct (positive) and inverse (negative) relationships.
4. Identify and explain three typical economic graphs.

If you are already familiar with the use of graphs and thus can accomplish the learning objectives, you will want to omit the following and do the self-test.

CONSIDER THIS: GRAPHS, A TOOL OF ANALYSIS

What is a graph? A graph is an illustration picturing how two sets of numbers are related to one another. Graphs are an efficient means of relating a great deal of information. A good graph reveals things which might otherwise be very difficult to grasp.

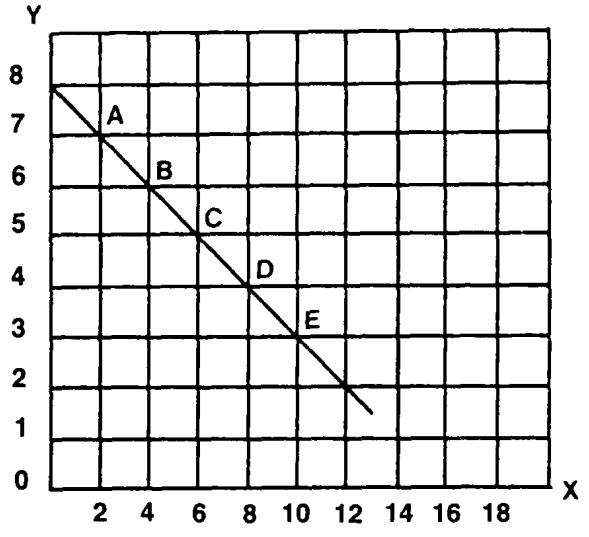
There is nothing difficult about graphs. They are shorthand ways of presenting information that could be described more laboriously in written or tabular form. The table below contains two sets of numbers – one set for the variable Y and another for the variable X. Each XY pair in the data set is identified with a capital letter, e.g., for D, X = 8 and Y = 4. From the data of Table 1A-1 you should note that variables X and Y are inversely related – as X increases, Y decreases. Without the tabular form, we would have been able to communicate sufficient information to establish the inverse relationship between X and Y but it would have involved more space and effort. Like the tabular form, a graph indicates the relationship between two variables but does so visually. Much more information can be communicated with considerably fewer resources and the information is more readily comprehensive as a graph.

Table 1A-1

	X	Y
A	2	7
B	4	6
C	6	5
D	8	4
E	10	3

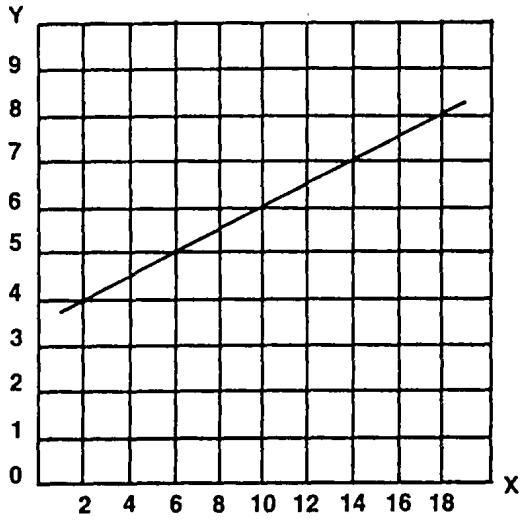
The information in tabular form may be presented as a graph. The lines placed at right angles to each other are called the coordinate axes. The X value is measured along the horizontal axis, while the vertical axis is marked off into units for measuring the Y value. In the space between the axes, the XY pairs may be plotted. For example, point E is plotted in the space by counting 10 units to the right along the horizontal axis and by counting up 3 units parallel to the Y axis. When all points are plotted they are usually connected by a smooth line or curve. Using the graph, Figure 1A-1, you can see at a glance that as the X value increases, Y value decreases. We know then that X and Y are inversely related.

FIGURE 1A-1
X AND Y INVERSELY RELATED



On the other hand, Figure 1A-2 indicates at a glance a situation in which the variables X and Y are directly related since X and Y increase together.

FIGURE 1A-2
X AND Y DIRECTLY RELATED



Economists use graphs with many different kinds of labels on the coordinate axes. The relationship between price and quantity demanded is frequently graphed by economists. Figure 1A-3 presents the relationship between the price of wheat and the number of units demanded at any given price for the data of Table 1A-2. As is clear at a glance, price and quantity demanded are inversely related. As a matter of convention, the vertical axis measures price and the horizontal axis measures quantity.

Table 1A-2

A Demand Schedule for Wheat

Price (dollars)	Quantity (bushels per month)	Price (dollars)	Quantity (bushels per month)
$10	1,000	$5	6,000
9	2,000	4	7,000
8	3,000	3	8,000
7	4,000	2	9,000
6	5,000	1	10,000

FIGURE 1A-3
A DEMAND CURVE FOR WHEAT

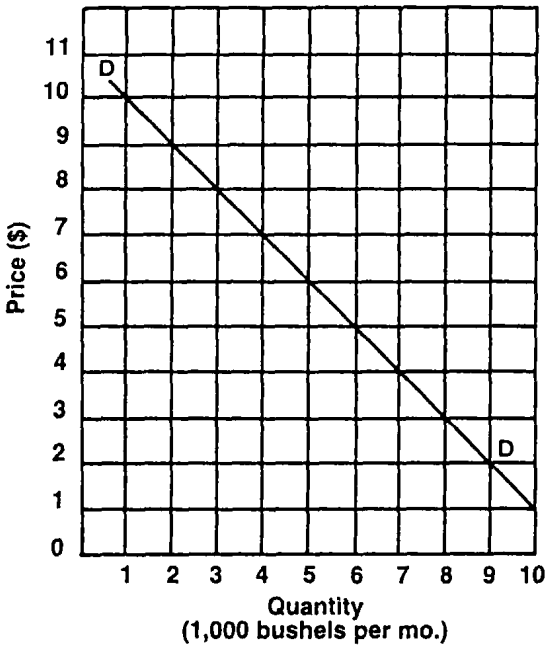
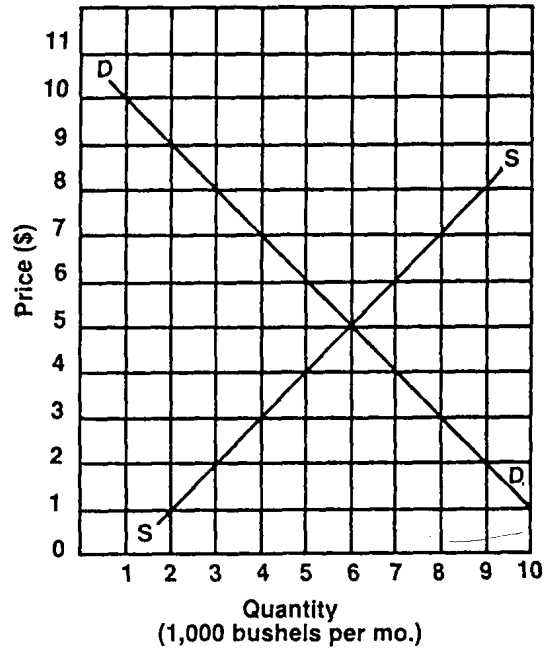


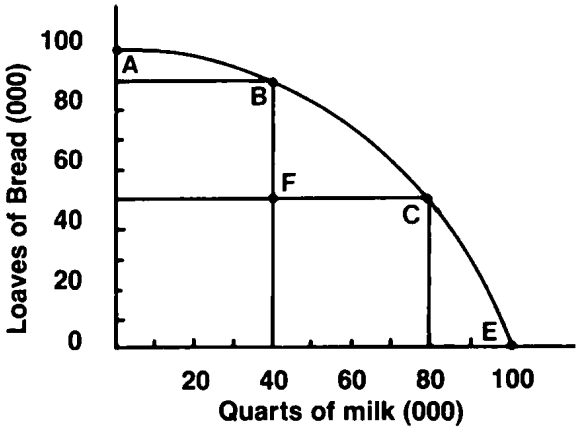
FIGURE 1A-4
MARKET FOR WHEAT



Often you will find the relationship between price and quantity supplied drawn on the same graph with a demand curve as a Figure 1A-4. This is an acceptable practice since the axes of both graphs are labeled the same – price on the vertical axis, quantity on the horizontal axis. When demand and supply are combined on the same graph, you can see at a glance that the quantity demanded equals the quantity supplied at a single price.

Another commonly used graph in basic economics depicts a production possibilities curve like that of Figure 1A-5. A production possibilities graph presents the relationship between the quantities of two products that an economy can produce. The intersection with the vertical axis indicates the maximum number of loaves of bread that the economy can produce if all resources are employed efficiently and no other products are produced. The horizontal axis intercepts under the same assumptions as above; indicates the maximum number of quarts of milk the economy can produce. All points on and to the left of the production possibilities curve between these extremes indicate the combinations of bread and milk the economy can produce. Combinations of products lying to the right of the curve are unattainable.

FIGURE 1A-5
PRODUCTION POSSIBILITIES CURVE FOR AN ECONOMY



Economists frequently use graphs to indicate how an economic magnitude changes over time. Figure 1A-6, U.S. Imports of Crude Oil since 1966, is drawn with time on the horizontal axis and billions of barrels of imported crude oil on the vertical axis. At a glance you can see that before 1978 the amount of crude oil imported increased substantially.

You will find that economists, often in texts and even more often in lecture, use abstract graphs to express general principles. When the general form of the economic relationship is known but the exact numbers are not known or are not critical to the discussion, the numbers along the axes may not be specified. The abstract graph of the agricultural product market, Figure 1A-7, captures what we know generally about demand, supply, market price, and market forces. It is unnecessary to specify price and quantity numbers. Graphs with numbers on the axes are used to summarize specific known information.

By now it should be clear that graphs are a highly efficient communication tool and relatively easy to understand. With a knowledge and appreciation of graphic methods, you will undoubtedly find the study of economics easier and more meaningful.

FIGURE 1A-7
AGRICULTURAL PRODUCT MARKET

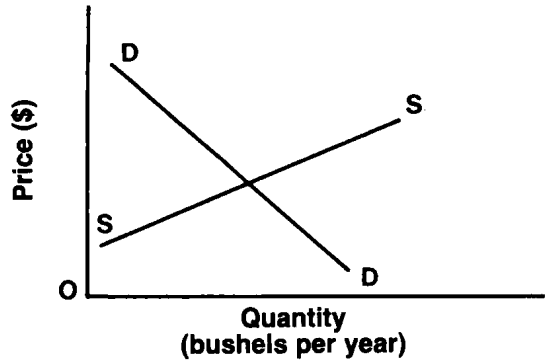


FIGURE 1A-6
U.S. IMPORTS OF CRUDE OIL, 1965-1986

Sources: U.S. Department of the Interior, Bureau of Mines, Mineral Industry Surveys, *Crude Petroleum, Petroleum Products, and Natural Gas Liquids*, 1960 and 1966–67 issues; and Department of Energy, Energy Information Administration, *Crude Petroleum, Petroleum Products, and Natural Gas Liquids*, December 1969, pp. 2, 16; *Petroleum Supply Monthly*, August 1986, pg. 24; and Department of Commerce, *Statistical Abstract, 1985*, December 1984, p. 561.