

STUDY GUIDE

for use with

ECONOMICS OF SOCIAL ISSUES

Eleventh Edition

Ansel M. Sharp
Charles A. Register
Richard H. Leftwich

Prepared by
Paul W. Grimes

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IRWIN

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Sydney, Australia

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A Note to Students

This *Study Guide* is designed to complement your exploration of the *Economics of Social Issues, Eleventh Edition*, by Sharp, Register, and Leftwich. The consistent pursuit of the material presented here will help you learn basic economic concepts in a systematic fashion. Each chapter provides you with a set of learning objectives, an application article, question, and problems which will lead you through the material presented in the text. Working through the *Study Guide* will test your understanding of basic economic concepts and your ability to apply economic reasoning to important issues that face our modern society. Each chapter of the *Study Guide* consists of several sections which are described below.

Learning Objectives. The learning objectives are brief statements of expected learning outcomes. They require you 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.

Some learning objectives are marked with an asterisk (*). They include economic concepts that are critical to economic understanding. You will use these concepts again as you study other economic issues in the text. You should allocate more time to these learning 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.

Consider This. This section of the *Guide* provides additional content that complements, illustrates, or expands upon the textbook content. Each "Consider This" is followed by a series of questions to help you relate the issues to the economic content of the chapter.

Study Questions. You should use the study questions to check your understanding of the chapter's content. They parallel very closely the learning objectives.

Self-test. This section of the *Guide* contains matching, 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 textbook chapter or the "Answers to the Self-test."

Answers to the Self-test. Answers to the questions of the self-test 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.

Note that all the chapters in the *Study Guide* follow the same organizational structure. You will find the chapters in this guide to be most helpful if you work through the material sequentially. For example, you should review the learning objectives and read the chapter orientation prior to studying the "Consider This" application article. Once you feel confident in your understanding of the relevant concepts and how they can be applied, you should move on and answer the "Self-test" questions and problems. Remember that this *Study Guide* is designed to complement the textbook and is not intended to be a substitute for it. You should always read and study the relevant chapter in the textbook before working through the guide material.

Much of the material contained in this edition was originally prepared by DeVon L. Yoho of Ball State University. Special thanks are extended to Ellen Cleary, Developmental Editor, for her help in bringing this project to completion.

Good Luck!

Paul W. Grimes,
Mississippi State University

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Chapter 1

Human Misery

The Most Important 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 opportunity cost using a production possibilities curve.
5. Define gross domestic product (GDP), per capital GDP, and per capital real GDP.
6. Calculate and interpret price indices.
7. Explain how an economy can provide rising living standards over time.
8. Evaluate the impact of population growth and density on living standards.
9. 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 Domestic Product (GDP) and then relate per capita

real GDP 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 GDP must exceed the rate of growth of its population. Can governments help solve the world poverty problem?

Consider This:

World Poverty Could Soar¹

A fifth of the world's population lives in grinding poverty and the number of poor could rise to 1.5 billion by the year 2000 with the biggest burden falling on women and children, a British charity said on Friday. A report on world poverty trends by the development group Actionaid painted a grim picture of a growing global underclass of people in the poorest regions of the world, barely subsisting and vulnerable to disease and early death.

It said that 1.1 billion people "ousted of a world population of around 5.5 billion" are now in absolute poverty, defined by the World Bank as living on \$420 a year or less.

The problem was particularly acute in Latin America and Africa, where incomes had fallen sharply over the last 20 years, it said. Based on current economic

trends, the poverty figure could reach at least 1.5 billion by the end of the century unless there is a massive global effort to target aid at basic needs such as food security, to boost the economies of developing countries and ease the Third World debt burden, it said.

Africa, already stricken by famine, civil war and falling commodity prices, is likely to see poverty rise at an even sharper rate. Sub-Saharan Africa was said to have the bleakest prospects, with the number of poor expected to rocket from 184 million to 304 million on what the charity called optimistic economic growth forecasts.

The report said that over the last two decades, significant progress had been made to improve living standards for thousands of people but the gap between the world's richest and

the poorest was growing. If action is not taken now to bridge this gap then the millions who exist in grinding poverty will continue to slip through the net, it said.

Going by current trends, the burden of poverty will fall on those least able to bear it "women, children, ethnic minorities, those who are ill, disabled and landless, it said. The number of women in absolute poverty had almost doubled over the last two decades, the report said.

Actionaid, Britain's fourth largest development charity, was founded 21 years ago. It received four million pounds (\$5.8 million) last year from the Overseas Development Administration, the British government agency that distributes state aid, for its work among poor communities in 19 countries.

¹ World Poverty Soar by End-Century, Charity Says, The Reuter Asia-Pacific Business Report, March 19, 1993, Reprinted with permission.

Consider These Questions

1. What are some of the consequences for individuals who live in absolute poverty according to Actionaid?
2. Research by the World Bank indicates that more than a billion people live on less than \$420 a year.

How does this compare to per capita GDP in the United States? ... in Nigeria?

3. Why is poverty "particularly acute in Latin America and Africa?"
4. What groups bear the heaviest burden of poverty? What economic factors explain why?

STUDY QUESTIONS

1. Country A's per capita real GDP is considerably greater than Country B's per capita real GDP. Clearly, Country A has overcome the fundamental economic problem. Evaluate.
2. Can the economic activity of people satisfy all the wants of human beings? Explain.
3. 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?
4. If, for an economy, 20,000 calculators must be given up for 4,000 microcomputers, what is the opportunity cost of a microcomputer?
5. In what sense is per capital real GDP a limited measure of an economy's standard of living?
6. What measures of economic performance are helpful in determining the impact of population growth on living standards?
7. What are the economic roots of world poverty?
8. Is world poverty caused by high rates of population growth and/or population density? Explain.
9. "Governments must solve the world poverty problems." Evaluate. What can governments do to help eliminate world poverty?

Self-Test

MATCHING Match the terms at the top with the definitions below, by putting the appropriate letter in the blank provided.

- | | |
|---------------------------------|---|
| _____ 1. Labor Resources | _____ 7. Real Gross Domestic Product |
| _____ 2. Capital Resources | _____ 8. Production Possibilities Curve |
| _____ 3. Technology | _____ 9. Price Index Numbers |
| _____ 4. Production | _____ 10. Efficiency |
| _____ 5. Opportunity Costs | _____ 11. Lesser Developed Countries |
| _____ 6. Gross Domestic Product | _____ 12. Social Overhead Capital |

- A. The market value of all final goods and services produced within an economy during one year.
- B. Nations with relatively low living standards usually due to relatively low levels of labor quality, capital, and technology.
- C. All human efforts of mind and muscle used in production.
- D. All non-human resources used in production.
- E. The value of alternatives given up when a choice is made.
- F. The means and methods available for combining resources to produce goods and services.
- G. GDP corrected for changes in the price level relative to a base year.
- H. The process of using technology to combine and transform resources to make goods and services.
- I. A set of numbers reflecting price level changes relative to a given base year.
- J. Extraction of the greatest possible value of output from a given set of inputs.
- K. Capital used by the economy as a whole rather than by individual firms.
- L. Curve showing the maximum production possibilities in a two-product economy, given the economy's resources and technology.

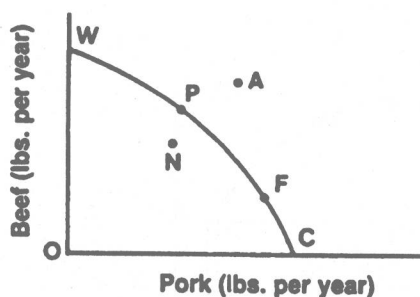
TRUE-FALSE QUESTIONS Circle T (true) or F (false)

- | | | |
|---|---|--|
| T | F | 1. One quarter of the world population survive on no more that \$1.00 per day. |
| 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. GDP is defined as the total value of an economy's annual output of goods and services in final form. |
| T | F | 6. Per capita real GDP is a perfect measure of an economy's living standard despite the unequal distribution of its output among the population. |
| T | F | 7. If production is unchanged from one year to the next but the price index increases, real GDP will increase. |
| T | F | 8. A country's living standard will improve over time if population increases at a faster rate than real GNP. |
| T | F | 9. 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 | 10. There is considerable evidence that population growth by itself has impinged significantly on the living standards of most developed countries. |
| T | F | 11. The economically advanced countries of the world provide economic assistance to LDCs in the form of loans and grants of money, and technical assistance. |
| T | F | 12. A product manufactured in Mexico by an American company is counted as part of the U.S. GDP. |

MULTIPLE-CHOICE QUESTIONS Select the one best answer

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

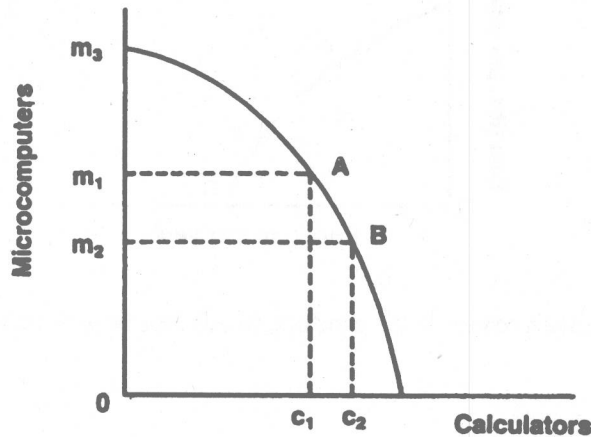
The following diagram applies to Questions 3-5.



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

3. The curve WC is known as a:
 - a. demand curve.
 - b. production possibilities curve.
 - c. budget line.
 - d. None of the above.
4. Which point represents underemployment of resources?
 - a. F
 - b. N
 - c. P
 - d. W
5. 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 6 and 7 below refer to the following diagram.



6. 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.
7. The opportunity 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.
8. The opportunity cost of a video disk player is measured by the:
 - a. money costs of resources bought and/or hired to produce it.
 - b. value of other goods and services that must be given up to obtain it.
 - c. amount of labor required to produce it.
 - d. All of the above.
9. 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.
10. Per capita real GDP:
 - 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.

11. To correct a current dollar GDP for inflation:
 - a. divide GDP in current dollars by the price index for that year.
 - b. multiply GDP in current dollars by the price index for that year.
 - c. divide real GDP by the price index for that year.
 - d. divide current dollar GDP by real GDP.
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. All of the above.
13. The standard of living would decline if:
 - a. real GDP declined and population increased.
 - b. per capita real GDP declined.
 - c. real GDP 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.
17. Which of the following would be included in United States GDP but would not be included in GNP?
 - a. A Nissan pickup built in Tennessee.
 - b. A bottle of white wine produced in France.
 - c. A General Motors car manufactured in Canada.
 - d. A bale of cotton grown in Mississippi.
18. International students from LDC's who decide to remain in the United States to work after college contribute to the:
 - a. Capital Flight.
 - b. Brain Drain.
 - c. Development of social overhead capital.
 - d. Inequality of the U.S. income distribution.

19. Developed countries jointly help LDC's by extending them low interest loans through this organization:

- The U.S. Congress
- The United Nations
- The World Bank
- CARE

20. Incomes in LDC's tend to be:

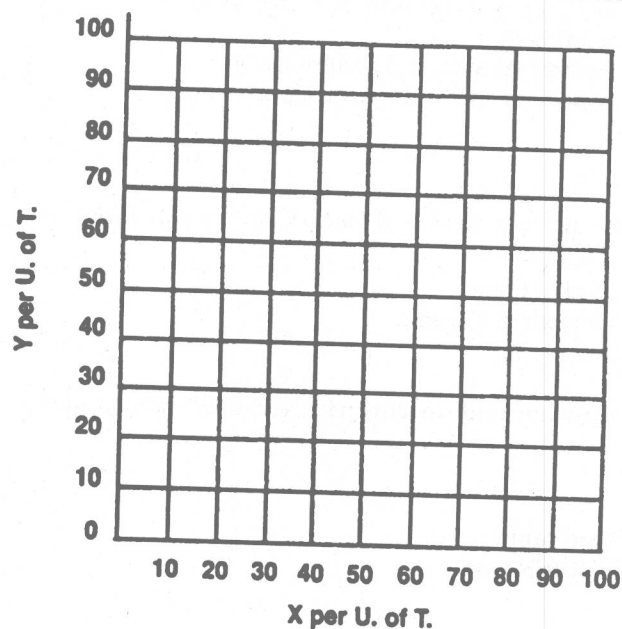
- More equally distributed than in DC's.
- Almost equally distributed.
- Less equally distributed than in DC's.
- Larger than in DC's.

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 (1000)	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 the following table, answer the following questions.

- a. For the years 1970 through 1990, current dollar GDP (increased/decreased).
 b. In what years did real GDP decline?
 c. For the years 1980-1992, population (increased/decreased).
 d. What happened to per capita GDP between 1989 and 1990?

Table 1-2 Gross Domestic Product, United States, current dollars and real, 1970-1992

(1) Year	(2) Current Dollars (Billions)	(3) Implicit Price Deflator	(4) Real or 1987 Dollars (Billions)	(5) Population (Millions)	(6) GDP per Capita 1987 Dollars
1970	\$1,010.7	35.2	\$2,873.9	205.1	\$14,012
1971	1,097.2	37.1	2,955.9	207.7	14,232
1972	1,207.0	38.8	3,107.1	209.9	14,803
1973	1,349.6	41.3	3,268.6	211.9	15,425
1974	1,458.6	44.9	3,248.1	213.9	15,185
1975	1,585.9	49.2	3,221.7	216.0	14,915
1976	1,768.4	52.3	3,380.8	218.0	15,508
1977	1,974.1	55.9	3,533.3	220.2	16,046
1978	2,232.7	60.3	3,703.5	222.6	16,637
1979	2,488.6	65.5	3,796.8	225.1	16,867
1980	2,708.0	71.7	3,776.3	227.7	16,585
1981	3,030.6	78.9	3,843.1	229.8	16,724
1982	3,149.6	83.8	3,760.3	232.1	16,201
1983	3,405.0	87.2	3,906.6	235.5	16,589
1984	3,777.2	91.0	4,148.5	237.6	17,460
1985	4,038.7	94.4	4,279.8	239.3	17,885
1986	4,268.6	96.9	4,404.5	241.6	18,231
1987	4,539.9	100.0	4,539.9	243.8	18,621
1988	4,900.4	103.9	4,718.6	246.4	19,150
1989	5,250.8	108.5	4,838.0	248.8	19,445
1990	5,522.2	113.2	4,877.5	251.3	19,409
1991	5,677.5	117.8	4,821.0	252.7	19,078
1992	5,942.2	120.9	4,915.0	255.4	19,244

Note: Discrepancies in calculations due to rounding.

Source: Economic Report of the President, February 1991, p. 288 and February 1993, p. 348; Survey of Current Business, September 1992, pp. 40-44.

Answers to Self-Test

MATCHING QUESTIONS

- | | | | |
|------|------|------|-------|
| 1. c | 4. h | 7. g | 10. j |
| 2. d | 5. e | 8. l | 11. b |
| 3. f | 6. a | 9. i | 12. k |

TRUE-FALSE QUESTIONS

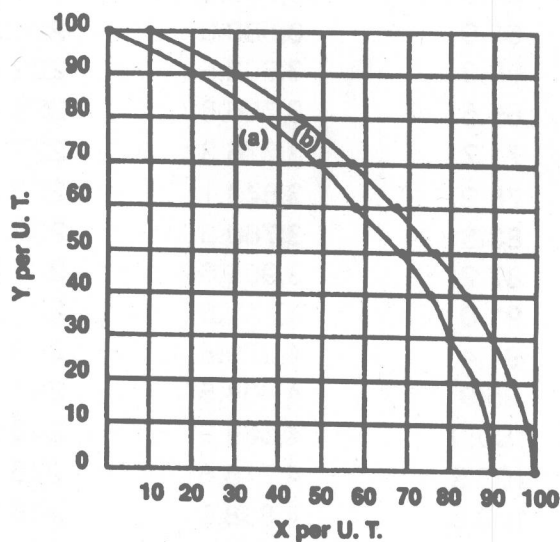
- | | | | |
|------|------|------|-------|
| 1. T | 4. F | 7. F | 10. F |
| 2. T | 5. T | 8. F | 11. T |
| 3. F | 6. F | 9. T | 12. T |

MULTIPLE-CHOICE QUESTIONS

- | | | | |
|------|-------|-------|-------|
| 1. a | 6. c | 11. a | 16. c |
| 2. b | 7. c | 12. d | 17. a |
| 3. b | 8. b | 13. d | 18. b |
| 4. b | 9. b | 14. d | 19. c |
| 5. c | 10. d | 15. c | 20. c |

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) The shift in the product possibilities curve, economic growth, is caused by improvements in the quality of the labor force, investment in capital goods and improved technology.

2. a. increased
b. 1974-75, 1980, 1982
c. increased
d. It fell.

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 labori-

ously 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 communi-

cate 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 comprehensible as a graph.

Table 1A-1

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