

CHAPTER 1

ECONOMICS AND LIFE

Solutions to End-of-Chapter Questions

Review Questions

1. Suppose you are shopping for new clothes to wear to job interviews, but you're on a tight budget. In this situation, what are your wants and constraints? What does it mean to behave rationally in the face of scarcity? **[LO 1.1]**

Answer: If you are deciding what to buy for a job interview, your want is to buy clothing that looks clean and professional, so you can present the best possible impression to potential employers. Your constraint is the amount of money you can spend on this clothing. A person behaving rationally would buy the nicest clothes they could afford.

2. You are a student with a demanding schedule of classes. You also work part-time and your supervisor allows you to determine your schedule. In this situation, what is your scarce resource? How do you decide how many hours to work? **[LO 1.1]**

Answer: Your scarce resource is time. You need both time to study and time to work. Presumably, you want to do well in school and also make money. You will try to balance your schedule so that you work as much as possible while still having enough time to study and do well in school.

3. Think about the definition of scarcity that you learned in this chapter. Name three ways that you confront scarcity in your own life. **[LO 1.1]**

Answer: We face scarcity in many aspects of our lives. I love to travel and explore new places. I face scarcity in both time and money that keeps me from traveling as often as I would like. In my professional life, I also face scarcity. There are lots of worthy projects I would like my department to take on, but I am limited in my available resources of employees, time, and budget. Collectively, as a society, we want more camping sites in the summer months. But there are limited number of sites available.

4. When shopping for your interview clothes, what are some trade-offs you face? What is the opportunity cost of buying new clothes? What are the benefits? How do you balance the two? **[LO 1.2]**

Answer: One trade-off is that the money you spend on clothes for a job interview could be spent on other things instead. One opportunity cost of buying new clothes is other things forgone. Another opportunity cost is the time you spend shopping, which could be spent preparing for your interview or playing Frisbee. The benefits include looking put-together during the interview, which provides a boost to your job prospects. You balance the costs and benefits by accepting costs that are less than (or no greater than) the benefits they provide.

5. You have an 8:00 class this morning but you are feeling extremely tired. How do you decide whether to get some extra sleep or go to class? **[LO 1.2]**

Answer: If you are behaving rationally, you decide by comparing the trade-offs. The opportunity cost of going to class is missing out on some extra sleep. Depending on what else is on your schedule that day (perhaps an important job interview), it may make sense to choose extra sleep over class. The opportunity cost of extra sleep is that you will miss the lecture. If your grade will suffer significantly by your absence, you may want to grab some coffee and go to class!

6. It's Friday night. You already have a ticket to a concert, which cost you \$30. A friend invites you to go out for a game of paintball instead. Admission would cost you \$25, and you think you'd get \$25 worth of enjoyment out of it. Your concert ticket is nonrefundable. What is your opportunity cost (in dollars) of playing paintball? **[LO 1.2]**

Answer: The opportunity cost of going to play paintball is whatever amount of enjoyment (in dollars) you would get out of going to the concert. The thirty dollars you paid for the concert ticket is not relevant to the decision, as it is a sunk cost and is nonrefundable regardless of what you do.

7. Suppose you have two job offers and are considering the trade-offs between them. Job A pays \$45,000 per year and includes health insurance and two weeks of paid vacation. Job B pays \$30,000 per year and includes four weeks of paid vacation but no health insurance. **[LO 1.2]**
 - a. List the benefits of Job A and the benefits of Job B.
 - b. List the opportunity cost of Job A and the opportunity cost of Job B.

Answer:

- a. The benefits of Job A are the extra pay and health insurance. For Job B, the benefit is two extra weeks of vacation.
- b. The opportunity cost of Job A is losing out on the extra two weeks of vacation that comes with Job B. For Job B, the opportunity costs are the extra \$15,000 in salary along with the health insurance.

8. Your former neighbor gave you his lawnmower when he moved. You are thinking of using this gift to mow lawns in your neighborhood this summer for extra cash. As you think about what to charge your neighbors and whether this idea is worth your effort, what opportunity costs do you need to consider? **[LO 1.2]**

Answer: You need to consider the opportunity cost of mowing lawns. Your lawn mowing business would need to cover the opportunity cost of what you could earn in another summer job. You also need to consider the cost lawn mowing (e.g. of gasoline for the mower) and the value of the lawn mower itself. Just because it was a gift does not mean that it has no opportunity cost. The opportunity cost of using the lawnmower for your business is its sale value, if you decide to sell the gift rather than use it yourself. Your lawn mowing business needs to cover all of these costs (the value of your time in another job, gasoline, and the sale value of the lawnmower) in order for it to be a worthwhile endeavor.

9. Think of a few examples of incentives in your daily life. How do you respond to those incentives? **[LO 1.2]**

Answer: Throughout the day, I am reminded to not park in the wrong spot (lest I get a ticket), get five cents for every glass I recycle, and set aside five percent of my income to a RRSP. For the most part, I respond rather favorably to these incentives.

10. You supervise a team of salespeople. Your employees already receive a company discount. Suggest a positive incentive and a negative incentive you could use to improve their productivity. **[LO 1.3]**

Answer: For a positive incentive, you could offer a reward such as a bonus, a gift certificate, or an extra discount on company merchandise to the most productive employee of the month. For a negative incentive, you could announce that employees who fail to meet targets will lose their company discount.

11. Your boss decides to pair workers in teams and offer bonuses to the most productive team. Why might your boss offer team bonuses instead of individual bonuses? **[LO 1.3]**

Answer: Your boss is creating a reward system for a project that requires group effort. Even if you are not motivated to compete for an individual bonus, you are likely to feel responsibility to your teammate and make a greater effort to be productive. Your teammate can encourage, pressure, and/or help you to achieve greater productivity.

12. Think of a public policy—a local or national law, tax, or public service—that offers an incentive for a particular behavior. Explain what the incentive is, who is offering it, and what they are trying encourage or discourage. Does the incentive work? **[LO 1.3]**

Answer: Provincial and federal governments provide subsidy on green energy projects. This provides an incentive for electricity producers to switch their production to renewable sources. They are trying to encourage the production of green energy to reduce the carbon emission in Canada. This incentive will help reduce greenhouse gas emission by changing the composition of electricity production in the long run.

13. Why do individuals or firms usually provide the goods and services people want? **[LO 1.4]**

Answer: It is for their own private interests that Individuals or firms provide goods and services people want. By fulfilling what people (buyers) want, individuals and firms also receive what they themselves want. If firms didn't produce goods that people want, no one would buy their goods. These firms would lose money and go out of business, and would be replaced by firms that did produce goods that customers want.

14. You may have seen TV advertisements for products or programs that claim to teach a surefire way to make millions on the stock market. Apply the *Why isn't everyone already doing it?* test to this situation. Do you believe the ads? Why or why not? **[LO 1.4]**