

## Unit 6

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### Lesson 26

1. What is a market?
2. Give an example of how markets are interrelated.
3. Define: capital goods, producer goods, consumer goods, durable goods.
4. What are three functions that markets serve in the economy?
5. Define: perfect competition, monopoly, monopolistic competition, natural monopoly.
6. Define: oligopoly, monopsony, oligopsony.
7. Define: collusion, cartel, boycott.
8. How does Walter Williams say that income is earned in a free society?
9. What two factors determine whether an entrepreneur makes a profit?
10. What does “Williams’ law” state?

### Lesson 27

Create supply and demand schedules and draw a graph with the corresponding supply and demand curves for spiral bound notebooks. Be sure to put price and quantity on the correct axes and label them. Label the supply and demand curves. Use this information:

Supply: at \$.25 each, none supplied; at \$.50 each, 100 supplied; at \$.75 each, 200 supplied; at \$1.00 each, 300 supplied; at \$1.25 each, 400 supplied.

Demand: at \$.25 each, 400 demanded; at \$.50 each, 300 demanded; at \$.75 each, 200 demanded; at \$1.00 each, 100 demanded; at \$1.25 each, none demanded.

Label the areas of the graph that indicate surplus and shortage. Label the equilibrium.

1. What is the equilibrium or market-clearing price?
2. What is the equilibrium or market-clearing quantity?

### Lesson 28

1. What are some ways that price is a factor in an economy?
2. What is a price maker, and what is a price taker?
3. What is a relative price?
4. How has most of America’s wealth and economic strength come about?
5. What is price discrimination?
6. What is a price ceiling? Give an example.
7. What is a price floor? Give an example.
8. John Davenport says that the market requires a framework of what?
9. What are the two basic ways to allocate resources that Davenport describes?
10. Davenport says that “you do your thing and I’ll do mine” is really an invitation to what?

## Lesson 29

1. How does a change in price affect supply?
2. In what ways does demand change?
3. When price changes, how does the demand curve on a graph change?
4. When a factor other than price changes, how does the demand curve change?
5. What is price elasticity of demand?
6. What is cross-price elasticity of demand?
7. What is income elasticity of demand?
8. What is price elasticity of supply?
9. What is the economic meaning of the term sticky?
10. What are menu costs?

## Lesson 30

1. What is market failure?
2. How does a monopoly cause market failure?
3. How do taxes cause market failure?
4. How do price and quantity regulations cause market failure?
5. How do externalities cause market failure?
6. Why does a failure to enforce property rights cause market failure?
7. What are public goods?
8. In what sense do public goods reflect market failure?
9. How did Communist central planners create market failure?
10. What do we need to keep in mind regarding markets and an uncertain economy?

## Unit 6 Quiz

### Matching

- |                                     |  |
|-------------------------------------|--|
| _____ 1. Perfect competition        | A. Creates a surplus                                   |
| _____ 2. Oligopsony                 | B. As price increases, demand falls                    |
| _____ 3. Law of demand              | C. Demand increases when price for another increases   |
| _____ 4. Law of supply              | D. Many sellers and buyers                             |
| _____ 5. Relative price             | E. How much demand changes when price changes          |
| _____ 6. Price floor                | F. Resources not allocated efficiently                 |
| _____ 7. Price elasticity of demand | G. Only a few major buyers                             |
| _____ 8. Substitute good            | H. As price increases, production increases            |
| _____ 9. Market failure             | I. Can be used by more than one person at a time       |
| _____ 10. Public goods              | J. Price of one item expressed as the price of another |

**Second Exam (Units 6-10)**

On the following four pages, write the word or phrase in the blank on the left that matches each description on the right. For each page, choose from the list of twelve terms at the top. Each page has two terms which do not fit in any blank on that page. Two points each (100 points total).

business cycle  
child labor  
closed shop laws  
international trade  
law of demand  
markets

price ceiling  
price of labor  
real exchange rate  
reasons businesses succeed or fail  
Say's Law  
sole proprietorship

1. \_\_\_\_\_ when the price of a good or service rises, demand falls
2. \_\_\_\_\_ creates a shortage
3. \_\_\_\_\_ Bob's Plumbing Service, for example
4. \_\_\_\_\_ expansion, peak, recession, trough
5. \_\_\_\_\_ the rate of exchange for goods and services between one country and another
6. \_\_\_\_\_ accomplish the allocation of resources, determine prices
7. \_\_\_\_\_ require that in certain industries, workers have to be members of a labor union
8. \_\_\_\_\_ management, planning, money, location, overexpansion
9. \_\_\_\_\_ wages and salary
10. \_\_\_\_\_ supply creates its own demand for what is produced

absolute advantage  
 cause market failures  
 determinants of supply  
 factors of production  
 inflation  
 interest

marginal analysis  
 money  
 price floor  
 securities  
 unemployment  
 variable costs

11. \_\_\_\_\_ when one person or country can produce goods with a smaller input of resources than another
12. \_\_\_\_\_ study of factors that lead to a change in business behavior
13. \_\_\_\_\_ the price of money
14. \_\_\_\_\_ price of the good, disposable income, price of resources
15. \_\_\_\_\_ a medium of exchange
16. \_\_\_\_\_ monopolies, taxes, regulations
17. \_\_\_\_\_ frictional, structural, seasonal, cyclical
18. \_\_\_\_\_ expenses that change depending on the amount of production taking place
19. \_\_\_\_\_ a broad term used to encompass stocks, bonds, and other financial investments
20. \_\_\_\_\_ creates a surplus

corporation  
 deadweight loss  
 discount rate  
 factors that increase trade  
 functional distribution of income  
 inflation

influx  
 law of supply  
 multiple-deposit expansion  
 mutual funds  
 price  
 production possibility

21. \_\_\_\_\_ how banks use deposits to make loans and thus enable more buying and selling of goods and services
22. \_\_\_\_\_ a separate entity from the owners and directors, is chartered, has a board of directors
23. \_\_\_\_\_ better communication, better transportation, lower transaction costs
24. \_\_\_\_\_ investment companies that offer shares to the public
25. \_\_\_\_\_ as the price for a product or service increases, production will increase
26. \_\_\_\_\_ a measure of income among different businesses and occupations in the economy
27. \_\_\_\_\_ the interest that the Fed charges banks for loans of its funds
28. \_\_\_\_\_ a change in it causes a shift along the supply or demand curve
29. \_\_\_\_\_ a general increase in prices for goods and services
30. \_\_\_\_\_ a reduction in efficiency that leads to a loss in profit or a loss to society

complementary goods  
 derived demand  
 dividend  
 economic profit  
 fiat currency  
 fractional reserve banking

open market operations  
 price elasticity of demand  
 root cause of inflation  
 small business  
 stock market  
 trade restrictions

31. \_\_\_\_\_ the practice of loaning out the majority of the money that a bank has on deposit
32. \_\_\_\_\_ demand by a producer for a factor of production that occurs as a result of the production of another product or service
33. \_\_\_\_\_ money that has value by the declaration of a nation's government that the money is legal tender
34. \_\_\_\_\_ determined by subtracting the opportunity cost as well as the ledger costs from the revenue
35. \_\_\_\_\_ the buying and selling of U.S. Treasury bonds and other Federally-issued securities by the Federal Reserve
36. \_\_\_\_\_ goods that are commonly bought together, so much so that a change in price for one product leads to a change in demand for the other
37. \_\_\_\_\_ when the quantity of money rises more rapidly than the output of goods and services
38. \_\_\_\_\_ a measure of how much demand changes in response to changes in price
39. \_\_\_\_\_ accounts for 60-80% of new jobs each year in America
40. \_\_\_\_\_ tariffs, quotas, sanctions, subsidies

capital gains  
 comparative advantage  
 currency exchange rate  
 earned income  
 law of diminishing marginal returns  
 law of supply and demand

liquidity  
 minimum wage  
 public goods  
 real interest rates  
 ridiculously difficult  
 supply or demand curve shifts

41. \_\_\_\_\_ goods and services that can be used by more than one person at a time
42. \_\_\_\_\_ when one producer has a smaller opportunity cost of producing a good or service compared to another producer
43. \_\_\_\_\_ the price of one country's currency expressed in terms of another country's currency
44. \_\_\_\_\_ when a factor other than price changes
45. \_\_\_\_\_ the ease with which an asset can be turned into money
46. \_\_\_\_\_ the increase in value of capital assets
47. \_\_\_\_\_ the price of a product or service adjusts to bring supply and demand into balance
48. \_\_\_\_\_ price floor on wages
49. \_\_\_\_\_ the productivity of an input decreases as the quantity of the input increases
50. \_\_\_\_\_ this exam

*extra credit activity on next page*

## Extra Credit (10 points)

## The Prisoner's Dilemma Game

Lefty and Bugsy were arrested and charged with the armed robbery of a bank. They were kept in separate cells. Each suspect was questioned (with his attorney present), and the district attorney made this proposal to each man:

"If you remain silent, we can convict you of an illegal weapons charge and you'll get one year in prison. We might convict you of the bank robbery and you'll get twenty years. If you confess and implicate your partner, we will drop all charges against you; and your partner will get twenty years if he's convicted. But we're making the same offer to your partner. If you both confess, we can convict you both and you'll each get ten years in prison."

The options and the possible outcomes that the two suspects face can be illustrated in the chart below.

		Lefty	
		Stay Silent	Confess
Bugsy	Stay Silent	Lefty gets 1 year, Bugsy gets 1 year	Lefty goes free, Bugsy gets 20 years
	Confess	Lefty gets 20 years, Bugsy goes free	Lefty gets 10 years, Bugsy gets 10 years

Each suspect has four possible outcomes: go free, serve one year, serve ten years, or serve twenty years. Each suspect has an influence on what happens to him; but the outcome is also dependent on what the other suspect does, and neither will know what the other decides to do. Even if the two suspects had made an agreement on what they would do if they were caught, neither is sure that he can trust his accomplice to keep their agreement.

What should each suspect do? Should he just look out for himself, or should he try to cooperate with his partner? What is the cost-benefit analysis that each prisoner should do for each option?

One application of the prisoner's dilemma game is in showing how difficult it is for a cartel to accomplish the goal of cooperation when each partner weighs his self-interest against the interests of the cartel.

## Sources:

1. Steven Kuhn, "Prisoner's Dilemma", *The Stanford Encyclopedia of Philosophy* (Spring 2009 Edition), Edward N. Zalta, ed., <http://plato.stanford.edu/archives/spr2009/entries/prisoner-dilemma/>, retrieved November 16, 2009
2. N. Gregory Mankiw, *Principles of Economics* (Fort Worth: The Dryden Press, 1998), pp. 345-354