

# Q U E S T I O N S

The pages in parentheses are where answers to these questions can be found.

## PART I: PRICES AND MARKETS

1. Can there be a growing scarcity without a growing shortage— or a growing shortage without a growing scarcity? Explain with examples. (pages 49–51)
2. Can a decision be economic, if there is no money involved? Why or why not? (pages 6–7)
3. Can there be surplus food in a society where people are hungry? Explain why or why not. (pages 59–60)
4. When a housing shortage suddenly disappears, within a time period too short for any new housing to have been built, and yet people no longer have any trouble finding a vacant home or apartment, what has probably happened? What will probably happen in the longer run? Explain. (pages 41–42, 47)
5. Which of the following are— or are not— affected by price controls that limit how high the product's price can go: (a) the quantity supplied, (b) the quantity demanded, (c) the quality of the product, (d) a black market for the product, (e) hoarding of the product (f) the supply of auxiliary services that usually go with the product, or (g) efficiency in the allocation of resources? Explain in each case. (a: pages 43–47; b: pages 41–43; c: pages 56–58; d: pages 54–56; e: pages 52–54; f: pages 44–45, 52; g: 52–53, 64–65)

6. Building ordinary housing and building luxury housing involves using many of the same resources, such as bricks, pipes, and construction labor. How does the allocation of these resources between ordinary housing and luxury housing tend to change after rent control laws are passed? (page 45, 49)
7. Are prices usually higher or lower in low-income neighborhoods? Why? Include among prices the interest rate on money borrowed and the cost of getting paychecks cashed. (pages 69–72)
8. When a government institution or program produces counterproductive results, is that necessarily a sign of irrationality or incompetence on the part of those who run that particular institution or program? Explain with examples. (pages 73–74)
9. We all consider some things more important than others. Why then can there be a problem when some official government policy establishes “national priorities”? (pages 84–85)
10. We tend to think of costs as the money we pay for things. But does that mean that there would be no costs in a primitive society that did not yet use money or in a modern cooperative community, where people collectively produce the goods and services they use and do not charge each other for them? (pages 87–89)
11. Adam Smith had a high opinion of capitalism, despite his low opinion of capitalists. How does this relate to the difference between systemic causation and intentional causation? (pages 68–72)
12. Back in the days of the Soviet Union, the government owned and operated most of the enterprises in the economy. Most prices were set by central planners, rather than by supply and demand, and the success or failure of Soviet enterprises was judged primarily by how well they met the numerical targets for production, which were set by the central

- planners. Specify five ways in which this arrangement produced different economic end results from those in market economies. (pages 5, 17–18, 25–26, 29, 51, 54–55, 74)
13. How can the price of baseball bats be affected by the demand for paper or the price of catchers' mitts be affected by the demand for cheese? (pages 21–22)
14. Why are price controls likely to cause more of a shortage of gasoline than of strawberries? (page 53)
15. How does rent control affect the quality of housing, the average age of housing, and the number of people per apartment? (pages 42–43, 44–45)

## **PART II: INDUSTRY AND COMMERCE**

1. Why would a big corporation pay millions of dollars in severance money to an executive who has been a complete failure who has turned corporate profits into corporate losses? (page 155)
2. Why has Toyota manufactured cars with only enough inventory of parts to last a few hours? Why did Soviet industries have nearly enough inventory to last for a year? (pages 144–146)
3. Why do American manufacturers of computers or television sets tend to have them transported by others while Chinese manufacturers tend to transport them themselves? (page 144)]
4. How did the movement of population from rural to urban America affect the economics of retail selling in the early twentieth century? How did the later movement of population from urban to suburban America in the second half of the twentieth century affect the economics of

- department stores and grocery stores? Explain with examples. (pages 98–100, 102–104)
5. Why is it that General Motors can make millions of automobiles, without making a single tire to go on them, while Soviet enterprises not only tended to make all their own components, but sometimes even made the bricks for the buildings in which they operated? (pages 143–144, 146–147)
  6. How did diseconomies of scale in agriculture affect the way tractor drivers plowed fields in the Soviet Union? What if agricultural enterprises had been privately owned and the tractor drivers were plowing their own fields? Would the work have been done differently and would the farm be likely to be as large? Explain why. (pages 132–133)
  7. When an economic project such as building a railroad or creating an airline requires far more money than any given individual can or will invest, what are some of the things that can facilitate or impede the pooling of the money of millions of people to finance the project? (pages 150–152)
  8. Advertising, even when it is successful, is often considered to be a benefit only to those who advertise, but of no benefit to consumers, who have to pay the cost of the advertisements in the higher price of the products they buy. Evaluate this view from an economic perspective. (pages 130, 573–578)
  9. “Under both capitalism and socialism, the scarcity of knowledge is the same, but the way these different economies deal with it can be quite different.” Explain. (pages 112–117)

10. Why are retired people able to get much lower priced travel rates— on cruise ships, for example— than most other people? Explain the economic reasons. (pages 134–135)
11. Why is the perennial desire to “eliminate the middleman” perennially frustrated? (pages 139–143)
12. After the A & P grocery chain cut its profit margins on the goods it sold, back in the early twentieth century, its rate of profit on its investment rose well above the national average. Why? (page 127)
13. Why would luxury hotels be charging lower rates than economy hotels in the same city? (pages 135–136)
14. What is the difference between the government’s protecting competition and protecting competitors? How does that affect the consumers’ standard of living through its effect on the allocation of scarce resources which have alternative uses? (pages 170–173)
15. Stores in low-income neighborhoods tend to charge higher prices, in order to try to compensate for higher costs and for slower rates of turnover in their inventory. What limits the ability of these stores to completely compensate for these higher costs, so as to make the same rates of profits as stores in higher-income neighborhoods? (pages 127–128)

### **PART III: WORK AND PAY**

1. What have been some of the economic and social consequences of the substitution of machine power for human strength, as a result of industrialization, and the growing importance of knowledge, skills, and experience in a high-tech economy? (pages 222–223)

2. Would you expect the average hammer to drive more nails per year in a richer country or a poorer country? Would you expect the average worker to produce more output per hour in a richer country or a poorer country? Explain the reasons in each case. (pages 230–231)
3. Some studies have attempted to determine how employment has changed in the wake of a minimum wage increase by surveying individual firms before and after the increase to find out how their employment has changed, and then adding up the results. What is the problem with this procedure? (pages 242–243)
4. How can per capita income be increasing by 50 percent over a period of years, while average family income and average household income remain almost stationary over those same years? (pages 217–218)
5. When the difference in income between the top and bottom brackets increases, does that necessarily mean that a given set of individuals are falling further behind another given set of individuals? (pages 218–220)
6. Would a country in transition between a communist economy and a capitalist economy, such as China, tend to have more equality of income or less, compared to an economy that was continuing to be communist or continuing to be capitalist? (pages 277–278)
7. Although maximum wage laws existed long before minimum wage laws, only the latter are common today. However, in those special cases where there have been maximum wage laws— as under wage and price controls during World War II, for example, what effects would such laws have on the allocation of scarce resources— and on discrimination against minorities and women? How would maximum wage laws and minimum wage laws differ in their effects on discrimination? (pages 229, 243–244, 246, 249–251)

8. Does inequality of income tend to be greater or less in the long run than in the short run? Greater or less than inequalities in consumption? Why do many statistics about “the rich” and “the poor” include people who are neither rich nor poor in reality? (pages 213–215, 278–279)
9. A New York Times columnist once used per capita income statistics to judge the economic performance of the administration of President Lyndon Johnson and, in later years, used household income statistics to judge the economic performance of the administration of President Ronald Reagan. Which set of statistics would tend to make the economic progress of the country look better and why? (pages 217–218)
10. How can differences in the quality of transportation systems or in the level of corruption in different countries affect the value of labor? (pages 211–212)
11. Why would a South African manufacturer expand production by opening a plant in Poland, when there were large numbers of workers available in South Africa, where the unemployment rate was 26 percent, and where the average output per hour of South African workers was higher than the average output per hour of Polish workers? (pages 246–247)
12. Why is the productivity of an individual not the same as the efficiency of that individual? Give examples comparing workers in Third World countries with workers in more prosperous countries and comparing different baseball players in different kinds of situations. (pages 209–212)
13. It has often been said that, over time, a higher percentage of the nation’s total income goes to the rich. In what sense is this true and in what sense is it not true? (pages 209–221)

14. Why are wages lower, and working conditions worse, in Third World countries? What are the likely consequences of various possible ways of trying to improve either or both? (pages 265–267)
15. What are the implications of the fact that most people today reach their peak earnings years at later ages than in generations past— and that these peak earnings are now usually a larger number of times greater than the earnings of beginners than in times past? What further implications does this have for the changing differences in male and female earnings? (pages 222–223)

#### **PART IV: TIME AND RISK**

1. Does it make economic sense for a ninety-year-old man, with no heirs, to plant trees that will take 20 years to grow to maturity and bear fruit? (page 317)
2. Businesses raise money by issuing both stocks and bonds but individuals usually raise money by borrowing— the equivalent of issuing bonds. In some circumstances, however, individuals acquire resources by the equivalent of issuing stocks. What are those circumstances? Give specific examples and reasons. (pages 339–340)
3. Why may the statistics on the known reserves of a natural resource provide a misleading picture of how much of that resource there is in the ground? (pages 320–326)
4. Why is it common for “payday loans” to have annual interest rates of more than 100 percent, when other loans usually have interest rates that are a small fraction of that? (pages 314–315)

5. How does commodity speculation differ from gambling? What is the effect of commodity speculation on output? On the allocation of scarce resources which have alternative uses? (pages 305, 308)
6. Why does it pay an insurance company or a commodity speculator to offer a deal in which they guarantee to pay a given sum of money to someone under given circumstances? And why does it pay for that person to accept the offer? (pages 308, 341)
7. Why would a bus company owned or controlled by the government charge fares too low to replace existing buses as they wear out? What if the executives of a privately owned and privately controlled bus company decided to divert part of the money they received from bus fares toward paying themselves higher salaries, instead of setting aside enough money to replace buses as they wear out? What would happen to the value of the stock in their company and how would the stockholders be likely to react? (pages 360–361)
8. Many poor countries have confiscated businesses or land owned by wealthy foreign companies. Why has this seldom made the poor country more prosperous? (pages 363–364)
9. Can complex international commodity markets have much impact on small farmers in a Third World country? Can those Third World farmers, who are often poor and poorly educated, participate in international commodity markets? (pages 306–307)
10. Why does it make sense for an individual driver to get insurance on his automobile? Why then doesn't Hertz buy insurance for its automobiles? (page 342)
11. How can government regulation of insurance companies improve the efficiency of the industry? How can it make the industry less efficient? Explain with examples of both. (pages 345–348)

12. Why do manufacturers in some countries keep an inventory of many months' supply of the materials needed in production, while manufacturers in some other countries do not keep an inventory of such materials sufficient to last all day? What are the implications for the allocation of scarce resources which have alternative uses? (pages 144–147, 308–309)
13. What kinds of income are called “unearned income” and why? What have been the consequences when groups that live on “unearned income” have left the country in large numbers, either voluntarily or because of being expelled? (pages 303, 311–312)
14. How does the interest rate allocate resources among contemporaries and between different present and future uses? (pages 299–302, 313–316)
15. Why would a state's bonds be downgraded by a bond-rating agency like Standard & Poor's, when that state was paying its bond-holders regularly and had a surplus in its treasury? (page 318)

## **PART V: THE NATIONAL ECONOMY**

1. “While taxes are often thought of as simply transfers of money from the people to the government, the economic consequences of taxation include changes in behavior that can affect the whole economy for better or worse.” Explain with examples. (pages 447–451)
2. Does the presence or absence of property rights make any difference to people who own no property? For example, are tenants affected economically by whether the community in which they rent apartments or houses allows unbridled property rights or reduces those property rights through zoning laws, open space laws, height restrictions on buildings, or rent control laws? (pages 422–427)

3. How does the level of honesty or corruption in a country affect the effectiveness of its economy? How do economic policies affect the level of honesty and corruption? (pages 427–432)
4. During the Great Depression of the 1930s, both Republican President Herbert Hoover and his successor, Democratic President Franklin D. Roosevelt, tried to keep up the prices of goods and labor. What was the rationale for these policies and what are the economic and social problems with such policies? (pages 396–397)
5. During a period of inflation, does money circulate faster or slower— and why? What are the consequences? What do you suppose happens during a period of deflation— and what are the consequences then? (pages 394, 397)
6. During an all-out war, how can a country’s military consumption plus civilian consumption add up to more than its output, without borrowing from other countries? (page 375)
7. Why is it difficult to make meaningful comparisons between the standard of living in a country whose population is, on average, many years younger than the population of another country with which it is being compared? (pages 379–380)
8. “The nationalization of banks in India was not simply a matter of transferring ownership of an enterprise to the government. This transfer changed all the incentives and constraints from those of the marketplace to those of politics and bureaucracy.” Explain what consequences followed and why. (pages 489–490)
9. Those who favor increases in tax rates are often disappointed that the additional revenue turns out to be less than they expected. Conversely, those who fear that cuts in tax rates will substantially reduce the government’s revenues have often been surprised to find the government’s revenues rising. Explain both phenomena. (pages 447–451)

10. Even if detailed statistics are available, why is it difficult to compare the national output at the beginning of the twentieth century with the national output at the beginning of the twenty-first century, and say by what percentage it has increased? Why is it hard even to say how much prices for particular goods have increased from one century to another? (pages 376–379)
11. Why would an Albanian bank, with 83 percent of the country's bank deposits, refuse to make any loans? And what were the consequences for the Albanian economy? (page 409)
12. Explain “the fallacy of composition” and give economic examples. (pages 370–371)
13. Since “money talks” in the marketplace, why would rich people want to shift some decisions out of the marketplace and have these decisions made politically or by courts? (Hint: housing is a classic example.) (pages 424–425)
14. Under what conditions is the burden of the national debt passed on to future generations? Under what conditions is it not? (pages 460–461)
15. From time to time there are conflicting estimates of how much of the total taxes are paid for by various individuals and organizations. Why is it not easy to tell who is really bearing the burden of taxation? Give specific examples. (pages 452–457)

**PART VI: THE INTERNATIONAL ECONOMY**

1. If laws restrict the importation of a particular foreign product, in order to protect the jobs of domestic workers who produce that product, how is it possible that this can end up reducing domestic employment? (pages 513–516)
2. Britain began importing farm products at a time when its own farmers were more efficient than the foreign farmers whose products it was importing. How could this be beneficial to Britain? How did this affect the international allocation of scarce resources which have alternative uses? (pages 506–507)
3. What are the three most important benefits of international trade? Explain each in terms of its effect on the efficient allocation of scarce resources which have alternative uses. (pages 502–509)
4. Why might the government of a Third World country prefer to receive a smaller amount of money as foreign aid, rather than a larger amount of money as private investment? (pages 556–557)
5. What is meant by a “favorable balance of trade”? Why was it considered favorable? Is it also favorable to producing prosperity in the economy? (pages 500–501, 619–621)
6. When foreigners annually take more wealth out of the U.S. economy than the Gross Domestic Product of Egypt or Malaysia, how can that fail to make Americans poorer? (page 540)
7. What economic difference does it make when the level of honesty in one country is very different from that in another country? (page 525)
8. In the absence of restrictions on international trade, would low-wage countries tend to take jobs away from high-wage countries through lower

- production costs that would allow them to sell at lower prices? Explain. (pages 511–513)
9. The United States has often been a “debtor nation” owing more to people in other countries than people in other countries owe to Americans, while Switzerland has often been a “creditor nation,” to whom others owe more to the Swiss than the Swiss owe to others. What tends to lead to this difference and is it economically beneficial or harmful to Americans or Swiss? (pages 528–530)
  10. What were the causes and effects of a large worldwide decline in international trade in the 1930s compared to the 1920s? (pages 513–515)
  11. What are some of the ways in which financial capital is transferred from one country to another? (pages 523–524)
  12. “Theoretically, investments might be expected to flow from where capital is abundant to where it is in short supply, much like water seeking its own level.” What are some of the reasons why countries with abundant capital seldom invest much of it in countries where capital is much more scarce? (pages 525–526)
  13. Nokia is one of the world’s leading producers of cellular phones, which are sold in many other countries besides Finland, where they are produced. What if laws prevented Nokia cell phones from being exported but allowed other cell phones to be imported into Finland? Would Nokia be likely to be able to hold its own within Finland, in competition against imported cell phones? (pages 508–509)
  14. What are some of the problems in applying laws against “dumping”? (pages 518–519)
  15. Why is free trade more likely to be more valuable to producers in a small economy than to producers in a large economy? (pages 506, 507–509)

**PART VII: SPECIAL ECONOMIC ISSUES**

1. Costly safety devices or policies have often been defended on grounds that “if it saves just one life, it is worth it.” What is the problem with that reasoning? (pages 612–614)
2. What are some of the reasons why different prices are charged for things that are physically identical? (pages 568–570)
3. How did the mercantilist economists differ from classical economists such as Adam Smith? (pages 619–622)
4. What is the point of having different brands of the same product if in fact all the brands are of pretty much the same quality and sell for about the same price? What would happen in this situation if laws did away with brands, so that each consumer could only identify what the product was, but not who made it? (pages 573–578)
5. For about a century— from the 1770s to the 1870s— most of the leading economists believed that the relative prices of goods reflected their relative costs of production, especially the amount of labor they required. What are some of the problems with that theory? (pages 628–630)
6. Explain how the presence or absence of the profit motive affects an organization’s likelihood of achieving the purpose for which it was created, to the maximum extent possible with the resources at its disposal. (pages 581–587)
7. What are the problems with the “trickle-down theory”? (pages 587–590)
8. Critics have claimed that profits exceed the value of the services performed by those who receive those profits. What empirical evidence could be used to test this belief? (pages 580–581, 586–587)

9. When fighting a war leads to a diversion of a substantial amount of resources from civilian to military purposes, most people would be more concerned to see that the poor could still get bread than that the rich could still get caviar. Then why not put price controls on bread but not on caviar? (pages 648–649)
10. Some people regard economics as just the opinions of economists, reflecting their various ideological biases. Examine that belief in the light of the history of economics. (pages 637–643)
11. Can government-imposed prices for medical care reduce the costs of that care? (pages 570–571)
12. It is common for politicians to set out to create a law or policy to solve a particular economic problem, and many in the media and among the public urge them to do that. In the light of economic theory in general, and general equilibrium theory in particular, what is wrong with that approach? (pages 632–634)
13. What is “predatory pricing” and what are the problems with it? (pages 571–573)
14. A government official in India said: “I don’t want multinational companies getting rich selling face creams to poor Indians.” What does that statement imply? (pages 595–596)
15. Nobel Prizewinning economist F. A. Hayek said: “We shall not grow wiser before we learn that much that we have done was very foolish.” What do you consider to be the three most foolish policies discussed in this book? Would you have considered those policies foolish before reading *Basic Economics*?