

CHAPTER 1 Basic Economic Ideas and Resource Allocation

Pg 7 Short Answers to Review Questions

1. Economics is a human science which studies the relationships between limited resources and unlimited wants.
2. Scarcity is the central problem in Economics.
3. Examples given are up to the students.
4. Human wants are essentially insatiable, but these wants can grow and change over time.
5. Opportunity cost is the benefit of the next best alternative forgone; sunk cost is the cost that cannot be recovered; financial cost is the amount of money needed to buy an asset or run a business.
6. In measuring opportunity cost, the best alternative is the only one alternative.

Pg 10 Short Answers to Review Questions

1. Economics is a human science that studies human behaviour that varies according to individuals, time and place.
2. Yes, because Economics is a social science.
3. Economists want to understand the relationship between two variables only.
4. Assumptions allow economists to study the relationships between two variables.
5. Neither. The importance of positive or negative economics depends on what one wants to study.
6. Long run is a period where all factor inputs are variable; long term is defined as a specific length of time.
7. No, the term 'short run' is not precisely defined and can change depending on context.

Pg 17 Short Answers to Review Questions

1. Examples given are up to the students.
2. Examples given are up to the students.
3. Yes. A government can analyse the factors of production available, and formulate and execute economic growth strategy.
4. A government can encourage and support small firms, provide incentives to entrepreneurs like tax breaks, and invest in efficient transport, utilities and communication infrastructure.

Pg 22 Short Answers to Review Questions

1. The questions are: What to produce? How to produce? For whom is it to be produced?
2. The possible reasons are slow feedback, lack of motivation and complex planning.
3. Competition results in many firms producing similar products, resulting in waste.
4. Common criticisms include income inequality, resource wastage and unemployment during economic recession.
5. These factors do not limit economic growth. Such a system provides a well-trained and highly educated workforce, reduces income inequality and attracts foreign investment.

Pg 27 Short Answers to Review Questions

1. Inward shift: Natural disaster, plague, war, outward migration.
Outward shift: An increase in any of the following—workforce, investment, inward migration, technological advancement.
2. In the production possibility curve (PPC) model, less will be produced of another good as more unit of one good is produced. The quantity of the other good forgone is the opportunity cost.
3. Economic growth is the expansion of productive capacity; economic recovery is an increase in output with productive capacity remaining the same.
4. The following happens to a country's PPC when:

- New machinery is purchased to produce cars: Outward shift of PPC
- The level of unemployment is reduced: Movement within the PPC
- Labour joining the workforce is better educated: Outward shift of PPC
- More women enter workforce: Outward shift of PPC

Pg 31 Short Answers to Review Questions

1. Imperfect information causes the under-consumption of merit goods and the overproduction of demerit goods.
2. Examples given are up to the students. Possible answers include water, wood.
3. Whether the following are public goods or private goods:
 - Public telephone: Private good (excludable because it requires payment; rivalrous because only one person can use it at a time)
 - Public bus: Private good (excludable because it requires payment; rival because consumption of the good by one person reduces the availability of seats for others)
 - Public toilet: Private good (excludable because it requires payment; rival because consumption of the good by one person reduces the availability for others)
 - Armed forces: Public goods (non-excludable because it is difficult to exclude anyone from being protected by defence; non-rival because one's protection does not diminish other's protection)
 - Streetlights: Public goods (non-excludable because light benefits all; non-rival because one's use does not affect others)
4. Yes, a government provides economic goods such as infrastructure, education, healthcare, and public safety to meet the needs of citizens.
5. Yes. However, due to the non-excludable and non-rival nature of public goods, consumption, the private sector may not profit from the provision.

CHAPTER 2 The Price System and the Microeconomy

Pg 45 Short Answers to Review Questions

1. The wish to want a good is not supported by purchasing power.
2. Market demand is the total demand in a market.
3. Change in demand causes a shift in the demand curve; change in quantity demanded causes a movement along the demand curve.
4. Explanation is up to the students. Possible determinants include income, price of substitutes.
5. Overall demand for coffee will increase. However, demand for a rival coffee shop will decrease.
6. Supply curve is upward sloping because more producers supply at higher prices.
Market equilibrium occurs when quantity demanded equals quantity supplied. Equilibrium will change with an increase in the supply of a good.

Pg 54 Short Answers to Review Questions

1. Price elasticity of demand (PED) measures the responsiveness in quantity demanded due to a change in its price.
2. Availability of substitutes
3. Arguments do not hold up in every situation.
4. Examples given are up to the students.
5. Necessity goods are not influenced by changes in income.
6. Value of income elasticity shows whether demand is sensitive to changes in income.
7. Cross elasticity of demand determines the relationship between two separate goods.

Pg 57 Short Answers to Review Questions

1. Price elasticity of supply (PES) measures the responsiveness in quantity supplied due to a change in its price.
2. Availability of spare capacity, perishability, production period, availability of substitutes for factor inputs, time.
3. Yes, the understanding of PES is important to hotel owners. This is because the knowledge can assist hotel operators to manage empty rooms during non-peak season.
4. The proportional change in price and quantity supplied will be the same when price changes.
5. The nation is a small buyer in the global market of commodities.
6. Perfectly inelastic supply has many examples like the number of exotic resort islands and seats in a stadium; perfectly inelastic demand does not.

Pg 61 Short Answers to Review Questions

1. Complementary demand: When two goods are demanded together to satisfy a want. Competitive demand: When one good can be replaced by another to satisfy a want.
2. Reasons for the following pairs to be both complements and substitutes:
 - Milk and coffee: Complements when consumed together (e.g. coffee with milk); substitutes when consumers choose one over the other for caffeine or taste preferences.
 - Electricity and petrol: Complements when used in electric vehicles (EVs); substitutes when consumers decide between conventional cars (petrol) or EVs (electricity).
 - Bus and railbus: Complements when both are part of a public transit system, serving different routes or providing backup service; substitutes when passengers choose one mode of transport over the other based on convenience or cost.
3. The automobile industry (heavy industry) derives demand for parts, tyres, technicians, seats and services (light industry), creating positive impacts of different industries on an economy.
4. Examples given are up to the students. Possible answers include restaurants, barbershops, fitness centres, shopping complexes, theme parks, hotels.

Pg 65 Short Answers to Review Questions

1. Consumer surplus is the difference between what consumers are willing to pay and what they actually pay; producer surplus is the difference between the amount producers actually receive and the minimum amount required for the producers to produce.
2. Consumer surplus: Affected by a change in PED of a good.
Producer surplus: Not affected by a change in PED of a good.
3. Equilibrium price can maximise the total consumer surplus and producer surplus.

CHAPTER 3 Government Microeconomic Intervention

Pg 73 Short Answers to Review Questions

1. Market failure occurs when the market cannot allocate resources efficiently.
2. Missing market occurs when a good is not provided in the market. It is a market failure because the good is non-excludable in nature, creating the free-rider problem.
3. Merit goods: Under-provided due to imperfect information (e.g. healthcare).
Demerit goods: Overconsumed due to imperfect information (e.g. alcohol).
4. The demand and supply of such goods are both price inelastic.
5. The party with more information can exploit the situation to their advantage.

Pg 82 Short Answers to Review Questions

1. Maximum price becomes effective when it is set below the market equilibrium price.
2. Drawbacks include shortages, long queues, low-quality products, emergence of black market.
3. Rent control is imposed to prevent landlords from exploiting tenants with high rentals. Increasing the supply of affordable housing can be one way of resolving housing problems for the poor.
4. Minimum price can raise the price of demerit goods, making them unaffordable to children and young adults.
5. There are positive externalities by having a larger pool of educated workers.
6. In the short run, indirect tax directly increases the price of demerit goods, discouraging consumption. In the long run, awareness campaign educates consumers about the harm of such goods, leading to behavioural change and reduced demand.
7. Examples given are up to the students. Possible answers include subsidies, education campaigns, tax incentives.

Pg 89 Short Answers to Review Questions

1. Equality is about each person getting the same treatment; equity is each person being treated fairly.
2. The 45° line in the Lorenz curve represents perfect equality.
3. The Lorenz curve that is further away from the 45° line indicates greater inequality.
4. The lesser the value of the Gini index, the lesser the inequality.
5. Income inequality allows the higher-income group to invest in and hire more workers.
6. Severe income inequality can result in low economic growth due weak demand, high levels of crime, health issues and political instability.
7. Minimum wage legislation can lead employers to reduce hiring or cut jobs to manage increased labour costs, causing greater unemployment.
8. Poverty trap occurs when workers choose to remain unemployed due to low wages relative to unemployment benefits.

CHAPTER 4 The Macroeconomy

Pg 101 Short Answers to Review Questions

1. Governments: To formulate economic policies.
Entrepreneurs: To make investment decisions.
Economists: To study and understand an economy.
2. In an economy, the spending of one person is equal to the income of another. Thus, total expenditure is equal to total income.
3. Gross domestic product (GDP) measures the total economic output within a country; gross national product includes the economic output generated by a country's residents domestically and abroad. GDP is used more often because it provides a more comprehensive picture of a country's economic activity within its borders.
4. Nominal GDP cannot be used to compare economic growth between different years because it does not account for inflation.
5. National income statistics are too narrow as they only consider actual goods and services produced. Many important aspects of living standards such as pollution, work hours, income distribution and literacy are not accounted for.

Pg 105 Short Answers to Review Questions

1. A closed economy is an economy without trade.
2. Injections are income flows that go into the circular flow of an economy; leakages are income flows that leak out of the circular flow.
3. Households are owners of all factors of production; firms are the private sector; government is the public sector; and foreign sector consists of foreigners that trade with an economy through exports and imports.
4. An economy arrives at its income equilibrium when the total injections are equal to total leakages.

Pg 116 Short Answers to Review Questions

1. Consumption (C): Demand for goods and services by the household sector.
Investment (I): Demand for goods and services by the private sector.
Government expenditure (G): Spending by a government.
Net exports (X – M): Total exports less total imports.
2. The downward slope of the aggregate demand (AD) curve is due to the real balance effect, the interest rate effect and the exchange rate effect.
3. The AD curve will shift to the right when there is an increase in any of the AD components (C, I, G, X – M).
4. An economy achieves income equilibrium when AD equals aggregate supply (AS).
5. The Classical long-run AS (LRAS) curve is a vertical line at the potential output level of an economy; Keynesian LRAS curve starts with a horizontal line and bends upwards vertically at the potential output level.

Pg 121 Short Answers to Review Questions

1. Real economic growth is the rate after adjusting for inflation; nominal economic growth is the rate before adjusting for inflation.
2. Countries aim to attain steady economic growth to improve living standards, increase job opportunities, encourage more investment and enhance general economic stability.
3. Trickle-down economics means economic growth begins with a small group of very wealthy people whose wealth gradually trickles down to lower-income groups through spending and job creation. This economic policy approach seldom works because the wealthy usually do not spend a large proportion of their income.
4. The middle-income trap is the difficulty faced by developing countries that are moving towards becoming developed countries. The key challenges are the lack of skilled workers due to brain drain and lack of innovation.
5. Technological advancement enables more goods and services to be produced with less resources.

Pg 127 Short Answers to Review Questions

1. Between claimant count and labour force survey, labour force survey is a better measurement method for unemployment because its statistical approach is more accurate.
2. Yes, it is possible for unemployment rates to fall but for the number of jobless people to increase. This happens when individuals stop actively seeking work (discouraged workers) and are no longer counted in the labour force.
3. Frictional unemployment is regarded desirable because workers are more likely to find jobs that are suited to their skills and aptitude.
4. Consequences of high unemployment within an economy include loss of income, output and human capital formation.
5. Cyclical unemployment happens during a downturn in the economy; structural unemployment happens when there is a mismatch of skills between the workers and the jobs available. Structural unemployment is more difficult to overcome because it takes a long time to reskill workers.
6. Hidden unemployment is a situation where workers are not fully employed, either working in jobs they are overqualified for or working less than 40 hours a week.

Pg 134 Short Answers to Review Questions

1. Rate of inflation is measured by determining the base year and basket of goods. Weights are then assigned, data collected and the Consumer Price Index (CPI) calculated.
2. Assigning weights in calculating CPI will make the CPI more accurate in reflecting changes in price levels to an average household expenditure.
3. Cost-push inflation is more damaging to an economy than demand-pull inflation. This is because an economy is hit with unemployment and inflation simultaneously.
4. Fixed income earners, their salary is often not adjusted to keep up with inflation; savers, the real value of their savings fall.
5. People buy more things when the inflation rate accelerates because they expect prices to go up further in future.
6. Deflation is a fall in the price level. The effects on deflation include a fall in consumer spending, mass retrenchment, and firms' shutdown as the real value of debts rises.
7. Yes, deflation is a bigger problem than inflation. This is because deflation causes a vicious cycle of low demand and unemployment, making the situation very difficult to overcome.
8. Deflation is a fall in the price level; disinflation is a fall in the rate of inflation.

CHAPTER 5 Government Macroeconomic Intervention

Pg 144 Short Answers to Review Questions

1. The redistributive macroeconomic role of government aims to reduce income inequality through taxes and subsidies; the allocative role aims to ensure the sufficient provision of public goods, merit goods and private goods.
2. A government's main macroeconomic goals include stable growth, price stability, full employment, poverty eradication and sustainability.
3. 'Gas' is government spending to spur economic activity; 'brake' refers to taxation that slows an economy.
4. The largest source of income of a government is personal income tax and indirect tax.
5. Current expenditure is spending on operating expenses like salaries to civil servants, maintenance, and various supplies; capital expenditure is spending on assets like buildings, infrastructure and machine.
6. The United States government raised taxes and reduced expenditures to balance the budget.

Pg 146 Short Answers to Review Questions

1. A government can control the supply of money through monetary policy.
2. The tools available to a government to manage the money supply in an economy include interest rates, open market operation and reserve requirement.
3. An increase in money supply will cause interest rates to fall, stimulating consumption and investment. This can cause economic growth. However, the effect will depend on the response of consumers and investors. If consumers are not optimistic (lack animal spirits), lower interest rates may have no impact.

Pg 148 Short Answers to Review Questions

1. Supply-side policy aims to increase the productive capacity of an economy through greater efficiency and productivity growth; monetary/fiscal policy targets the demand side of the economy, attempting to influence AD.
2. Red tape or excessive bureaucracy frustrates economic growth as it results in delay, higher costs of doing business and opportunities for corruption.
3. Cost of doing business means the cost of complying with regulations, taxes, transportation and wages. Supply-side policy attempts to reduce the cost of compliance through deregulation, investment in infrastructure and an increase in the supply of skilled labour.
4. The Mass Rapid Transit allows firms to relocate to places farther from the central district of Klang Valley, Malaysia, reducing rental costs. Firms can also hire workers living in a much larger area as they can travel easily to their offices.

CHAPTER 6 International Economic Issues

Pg 160 Short Answers to Review Questions

1. The theory of absolute advantage compares the average cost per unit; the theory of comparative advantage compares the opportunity cost.
2. Yes. Perfect mobility of labour is not realistic, as retraining and reskilling workers takes a long time and a lot of money.
3. Mercantilism is a school of thought that aims to protect domestic industries and jobs against foreign competition. It is often considered 'bad' because it ignores the advantages of trade that can be mutually beneficial.
4. Imports are as important as exports because imports allow nations to specialise and free up resources to focus on producing goods that the nation is efficient in.
5. Absolute advantage is derived from factor endowments, such as mineral deposits, soil fertility, suitable climate, existence of navigable rivers and strategic location.
6. Terms of trade have to be between the opportunity cost ratios because only then both countries can benefit from trading with one another.

Pg 168 Short Answers to Review Questions

1. Winners: Domestic producers, selling at higher quantities at higher prices; losers: Consumers, having to pay higher prices, receiving lower quantities of goods, and enjoying lesser choices.
2. The common justifications are: Infant industry argument, strategic industry argument and diversification.
3. Yes, protection allows new industries to reap economies of scale and gain experience to improve efficiency over the long run. However, industries may not develop competitiveness if they become reliant on protection.
4. Protectionism results in domestic industries not developing competitiveness due to a lack of foreign competition.

Pg 172 Short Answers to Review Questions

1. Balance of payments (BOP) is an account that records all financial transactions between one country and the rest of the world.
2. BOP is an indicator to assist governments in understanding an economy and in planning economic policies for the future.
3. BOP balances in theory because each credit transaction in the current account will have an equal corresponding debit transaction in the capital or financial accounts.
4. Current account deficit (CAD) means the country is spending (imports) more than it is earning (exports).
5. Factors that can cause an increase in a CAD include inflation, loss of competitiveness and rising income.
6. On one hand, a CAD requires financing through either debt or equity and the weakening of the currency. On the other hand, consumers enjoy more goods and services and the import of capital goods is healthy for economic growth in the future.
7. A country would welcome a CAD when it experiences a persistent current account surplus. It would not welcome a CAD when the country is experiencing excessive consumption and debt.
8. A CAD occurs when the total value of imports is greater than exports; budget deficit occurs when a government's planned expenditure is greater than the planned income.

Pg 180 Short Answers to Review Questions

1. The exchange rate of a currency is determined through the demand and supply of the currency in the foreign exchange market.
2. Common causes for an appreciation of an exchange rate include an increase in exports, foreign investment and relative interest rates.
3. The effects of a currency appreciation include a fall in trade and foreign investment as uncertainties increase.
4. Yes, there is a positive impact when the exchange rate weakens significantly. The world price of exports falls, encouraging more demand for exports. As imports become relatively more expensive, there will be an increase in demand for domestically produced goods.
5. Rapid inflation causes a fall in tourist arrivals and a rise in imports. In a fixed exchange rate, these effects are likely to be permanent. In a floating exchange rate regime, the exchange rate will depreciate and cushion the impact of these negative impacts.
6. Yes, changes in the exchange rate affect a CAD. However, these depend on the elasticities of exports and imports of the nation.
7. The 'beggar-they-neighbour' policy means boosting an economy at the expense of trading partners.

Pg 184 Short Answers to Review Questions

1. A government wants to reduce a persistent and rising CAD to avoid depreciation of the currency and a rise in foreign debt and/or foreign equity.
2. Small trading nations generally prefer fiscal policy to protectionist policy as they are more afraid of retaliation from trading partners.
3. Expanding the supply-side factors in an economy is a complex and time-consuming endeavour.
4. Devaluation can only be effective if the demand for imports and exports is elastic. Otherwise, it can worsen a CAD.
5. Supply-side policies can bring down a CAD by making an economy more efficient, lowering costs of production and increasing export competitiveness.

CHAPTER 7 The Price System and the Microeconomy

Pg 201 Short Answers to Review Questions

1. Rational consumers maximise utility through the equi-marginal principle.
2. The assumptions of the marginal utility theory are: Satisfaction can be quantified, consumers are rational, consumption is continuous and each unit consumed is identical.
3. Derive the marginal utility curve and convert utility to dollar.
4. Substitution effect: When the price of a good falls, it becomes relatively cheaper than other goods. A rational consumer will buy more of it, and less of other goods. Income effect: As the price of a good falls, real income rises. As a result, a rational consumer will buy more of the good.
5. The convex shape of the indifference curve shows that an additional unit of one good needs to be forgone for one extra unit of another good to remain at the same level of satisfaction.

Pg 205 Short Answers to Review Questions

1. Productive efficiency: Producing at the least cost. Allocative efficiency: Resources are allocated to produce goods that consumers want.
2. Price equals marginal cost is allocative efficient because the marginal utility of the last unit equals the marginal cost of the last unit.
3. Pareto optimality occurs when one cannot be made better off without another being made worse off.
4. Creative destruction is the process where innovation replaces old industries and technologies, driving economic progress.

Pg 210 Short Answers to Review Questions

1. Negative consumption externality is the external cost of consumption; positive consumption externality is the external benefit of consumption.
2. Private costs are the costs incurred by the user, while social costs are the costs incurred to the society.
3. Students to draw a diagram to illustrate an inefficient allocation of resources as a result of traffic congestion.
4. For a cost-benefit analysis, there is difficulty in identifying the costs and benefits, selecting the relevant ones, and monetising them.
5. Net present value adjusts all future costs and benefits for inflation and provides a better gauge of the feasibility of a project.
6. Advantages include the consideration of external costs and benefits; disadvantages include the inability to accurately determine costs and benefits.

Pg 224 Short Answers to Review Questions

1. Output will initially rise and then fall as more and more variable inputs are added to a fixed input because production is limited by the fixed input.
2. The average cost and marginal cost curves are U-shaped due to the law of diminishing returns.
3. Sources of economies of scale (EOS) include technical, managerial, marketing, financial and risk-bearing economies.
4. The kind of EOS that exists in hypermarkets includes purchasing, managerial and technical EOS.
5. The downward shift of the long-run average cost curve is due to technological advancement, external EOS and taxation.
6. The Economic concept of profit considers opportunity cost, the Accounting one does not.

Pg 224 Short Answers to Review Questions

1. There are many alternative aims of firms besides profit maximisation. The aims include sales/revenue maximisation, growth maximisation, and managerial and behavioural theory.
2. Natural barriers to entry exist in the nature of the industry itself; man-made barriers are erected by firms or professional bodies to limit supply.
3. Economists consider the following when analysing a market structure: Number of firms, barriers to entry, product homogeneity and knowledge.
4. An individual would start a business in a market without barriers to entry because he/she will be attracted by the abnormal profit that can be earned in the short run.
5. Industries that are highly competitive are those with low barriers to entry.
6. A perfectly competitive market is not always more efficient than a monopoly. This is because the former may not be able to exploit EOS and lack dynamic efficiency.
7. Firms attempt to differentiate their product through the following: Product attributes, promotion, promotion and relationship with customers.
8. A natural monopoly is an industry where even a single firm cannot fully exploit EOS.
9. Oligopoly is the most common type of market structure in an economy. This is due to EOS and the large marketing budget of large firms.

Pg 242 Short Answers to Review Questions

1. Firms grow in size to maximise profit, reduce competition and exploit EOS.
2. The advantages of growing the size of a firm through mergers over organic growth include: Faster market entry, synergies, cost savings, and enhanced market power.
3. Firms merge with another in the same industry and stage of production due to small market size, lack of capital and skills and profit satisficing.
4. Horizontal integration occurs with firms at the same stage of production; vertical integration occurs with firms at different stages of production;
5. Firms undergo vertical backward integration to ensure the supply of materials, enjoy lower costs and be able to control the quality of materials.
6. Small firms survive by capitalising on niche markets, building relationships with clients, being innovative, and supplying to large firms.
7. Governments make more effort to support and encourage small firms because they stimulate job creation and are aggressive in introducing new, innovative products to the market.
8. The strength of a cartel is determined by the following: Member commitment, barriers to entry, effective monitoring and enforcement mechanisms.

Pg 246 Short Answers to Review Questions

1. A firm maximises its profit in the long run by building customer loyalty.
2. The principal-agent problem occurs in some business organisations due to the conflicting objectives between the business owners and managers.
3. Management rewards refer to the pecuniary and non-pecuniary benefits to management.
4. Two conditions for practising price discrimination are distinct markets with different PEDs and ability to separate the markets.
5. The benefits of price discrimination include the following: An increase in profits, usage of services, cross-subsidisation.
6. Predatory pricing aims to eliminate competition; limit pricing aims to deter new entrants.

CHAPTER 8 Government Microeconomic Intervention

Pg 258 Short Answers to Review Questions

1. Privatisation is the transfer of ownership from the public sector to the private sector. Its benefits include: Less burden to the state, ability to focus on the core role, wider share ownership, greater efficiency.
2. Example given is up to the students.
3. Regulations can be an effective policy tool when there is a clear objective, flexibility and consistent enforcement to address market failures efficiently.
4. For pollution permits, firms are required to bid where the most efficient firms are able to bid the highest.
5. Strengths of the Nudge theory: Low costs, effective and choices are available to consumers. Disadvantages of the Nudge theory: Applies only in very few areas and some regard nudge as manipulative.

Pg 261 Short Answers to Review Questions

1. Universal benefits are given to those with specific conditions; means-tested benefits are given after evaluating the overall wealth and income level of a person. Means-tested benefits are less susceptible to being taken advantage of.
2. When tax avoidance is tackled, there will be more tax revenue available for governments to redistribute to lower-income groups.
3. Universal basic income sounds appealing because every citizen receives a regular, unconditional cash payment from their government. Its concerns include: Lack of incentive to work, the financial viability of the scheme and the absurdity of giving money to the rich.
4. Absolute poverty means the inability to afford basic necessities; relative poverty refers to low income relative to the median income.
5. No, negative income tax encourages more people to work.

Pg 276 Short Answers to Review Questions

1. Marginal revenue product is the extra revenue earned by a firm in employing another unit of labour.
2. Labour is regarded as a derived demand because the demand for labour is derived from the demand for other goods.
3. Work is assumed to be an inferior good because as income rises, demand for the good (work) falls.
4. The shape of the individual supply curve of labour is backward bending because at a higher income level, the substitution effect of higher wages is less than the income effect.
5. The supply curve of labour is perfectly elastic in a perfectly competitive labour market. This is because firms can hire more workers at the same wage rate.
6. Wages are determined by the demand and supply of labour.
7. All workers receive the same wage in a perfectly competitive labour market because workers are assumed to be equally productive, with perfect mobility and knowledge.
8. In a monopsony, a single buyer of labour has wage-setting power, leading to lower wages than in competitive markets.
9. A trade union would possess strong bargaining power under the following circumstances: Proportion of membership, lack of substitute workers, degree of militancy and regulation of labour union.

CHAPTER 9 The Macroeconomy

Pg 290 Short Answers to Review Questions

1. Macroeconomics study the economy as a whole.
2. Demand refers to demand for one product; AD refers to the total demand for goods and services in the economy.
3. The AD curve is downward sloping due to the real balance effect, interest rate effect and exchange rate effect.
4. Components in AD: Household consumption, private investment, government expenditure and foreign sector expenditure. Household consumption is usually the largest component in a developed economy.
5. Economists place a lot of emphasis on the level of investment in an economy because investment creates jobs and determines the prospect of economic growth for the nation.
6. Firms may feel there are no feasible projects for investment. Firms may keep profit as retained profit or distribute it as dividends to shareholders.
7. Animal spirits refers to investors' confidence as a whole. Excessive optimism or pessimism can affect spending and investment decisions, causing an economic downturn.
8. A rise in interest rates would cause both consumption and investment to fall.
9. Various incentives offered by governments to encourage investment include: Tax exemption, development of industrial parks, construction of efficient transportation systems and utilities infrastructure.

Pg 296 Short Answers to Review Questions

1. The typical features of an economy during the recovery phase of the business cycle include: Falling unemployment, optimistic consumer sentiments, new products and businesses, increase in the rental of shops and offices.
2. A government would seek to intervene in a business cycle to mitigate the shocks of a downturn and moderate a sudden upswing in the cycle.
3. Economic growth is important because it creates jobs, raises living standards and enables greater investment for the future. However, it may cause severe destruction to the environment, greater income inequality and unequal distribution of income.
4. Example given is up to the student.
5. Limitless growth is not possible. Supply-side factors can act as limitations to economic growth.
6. Inclusive economic growth is one that benefits all segments of the society.

Pg 303 Short Answers to Review Questions

1. The natural rate of unemployment arises when an economy is operating at the level of full employment and there is no voluntary unemployment.
2. Yes, unemployment can be pushed below the natural rate.
3. Cyclical unemployment occurs during an economic downturn; structural unemployment results from a mismatch between skills and jobs available. Structural unemployment is more difficult to tackle because it requires retraining and reallocation of resources, all of which take time and effort.
4. Frictional unemployment is regarded as desirable because as workers move between jobs, they are more likely to find one that is more suited to their aptitude and attitude.
5. It is possible for unemployment rates to fall but the number of people without jobs increases when the labour participation rate falls.
6. Consequences of high unemployment in an economy include: Fall in output, loss of human capital formation, cost of unemployment benefits, fall in tax revenue, loss of dignity.
7. Hidden unemployment refers to those who are underemployed or working part-time.
8. Between labour force survey and claimant count, labour force survey is a better measure of unemployment because it is more comprehensive and its statistical approach is more accurate.

9. The Monetarist long-run Phillips curve is a vertical line because Monetarists believe the unemployment rate will eventually go back to the natural rate.

Pg 323 Short Answers to Review Questions

1. The main reasons for people to hold money according to the liquidity preference theory include: Transactional, precautionary and speculative motives.
2. The central bank's role as a 'lender of last resort' means it can lend money to commercial banks if they are insolvent or in illiquidity situations.
3. The situation where consumers suddenly rush to withdraw their deposits is called a 'bank run'. If this happens, the banking system will collapse as it does not hold sufficient cash.
4. If there are no banks and credits available, consumers will keep excess cash at home and investors will not be able to borrow money for their businesses.
5. Commercial banks would want to hold as little excess reserves as possible to avoid needing to borrow from other banks in the event of a sudden withdrawal.
6. Factors that determine the size of the credit multiplier include: Cash ratio, amount of excess cash people keep outside the banking system, amount of deposit.
7. Commercial banks can be more aggressive in giving out loans as they know depositors are being guaranteed by federal deposit insurance.
8. A government prints new money using quantitative easing.
9. Interest rates are determined by the demand and supply of money.
10. Velocity is the amount of time money changes hands; transactions refer the value of all transactions in an economy.
11. Monetary policy affects an economy by changing interest rates, influencing borrowing, spending and investment decisions, ultimately impacting AD and economic activity.

CHAPTER 10 Government Macroeconomic Intervention

Pg 333 Short Answers to Review Questions

1. Internal value of money is measured by the rate of inflation; external value is measured by the exchange rate of the currency.
2. When the internal value of money falls, prices of exports will rise, causing a fall in the demand for exports. This will reduce the value of the exchange rate.
3. Expenditure-dampening policies to reduce a CAD can cause the rate of inflation to fall as well.
4. Raising interest rates, for example, to control inflation can cause higher unemployment.

Pg 344 Short Answers to Review Questions

1. Monetary policy is 'flexible' because interest rates, a monetary policy tool, can be changed easily; fiscal policy is 'inflexible' because additional expenditure, for example, needs to go through a lengthy process before it can be spent.
2. According to Monetarist economists, inflation is a bigger problem than unemployment because unemployment can resolve itself and an economy will return to full employment eventually.
3. Keynesian economists regard unemployment as a more critical problem than inflation because unemployment can go on for a long time if nothing is done to stimulate AD. The situation will worsen by the paradox of thrift.
4. The sentence means that an economy faces problems with supply-side factors and high costs of doing business. Such problems include: Lack of skilled workers, too many regulations, high taxes, inefficient infrastructure.
5. Supply-side policies are often referred to as microeconomic and structural reforms because they attempt to raise efficiency at the micro level (for example, deregulation in one industry).
6. The free-market supply-side policy approach tries to reduce the size of government intervention and encourage greater competition among the private firms; the interventionist approach refers to government spending on constructing various infrastructures that increase market efficiency.
7. Government failure is government intervention that results in unintended consequences.
8. Conflicting objectives can lead to government failure by causing policies that satisfy one goal to undermine another, creating inefficiency or unintended consequences.

CHAPTER 11 International Economic Issues

Pg 353 Short Answers to Review Questions

1. Expenditure-reducing policy is a policy that aims to reduce AD.
2. With expenditure-switching policies, people will save more and spend less on imports when there is a rise in interest rates. This reduces a CAD.
3. Expenditure-reducing policies may cause widespread economic recession, while expenditure-switching can cause retaliation. Factors that need to be considered in the discussion include: The country's export and import elasticities and the degree of trade.

Pg 357 Short Answers to Review Questions

1. The trade-weighted index is measured to provide a more accurate picture of the exchange rate.
2. The central bank sets the country's currency exchange rate against another currency at a fixed rate. Foreign exchange reserves are maintained to intervene, by buying and selling reserves, when necessary.
3. A floating exchange rate allows the rate to be determined by the actual demand and supply of the currency in the market, giving it a more true and fair value. There is no need to keep foreign exchange reserves.
4. The J-curve states that devaluation causes a worsening of a CAD in the short run, while improving it in the long run. The Marshall-Lerner condition says that devaluation can work only when the sum of the elasticity of imports and exports is greater than one.

Pg 363 Short Answers to Review Questions

1. Economic development is considered more important than economic growth because it includes improving living standards, reducing inequality, and addressing well-being.
2. The three dimensions of the Human Development Index are economic growth, literacy and life expectancy.
3. It is difficult to account for environmental costs in economic development due to diverse, intangible and long-term environmental impacts.
4. The Kuznets curve states that inequality tends to get worse initially before getting better, when an economy of a country improves.

Pg 366 Short Answers to Review Questions

1. Developing countries have a triangle-shaped age structure, with a larger proportion of younger age groups; developed countries have an inverted triangle, with a larger proportion of older age groups.
2. Low-income countries usually have a large primary sector; middle-income countries have a large secondary sector; high-income countries have a large tertiary sector.
3. Rapid urbanisation can lead the following: Congestion, lack of infrastructure to support rising urban population, lack of workers in rural areas.

Pg 370 Short Answers to Review Questions

1. Developing countries prefer trade over aid because trade offers sustainable income and development opportunities.
2. By limiting the profits earned by multinational corporations in developing countries, local interests may be protected but investment will be deterred.
3. East Asian economies used savings, foreign investments and export revenues to finance their early investments in the 1980's and 1990's.
4. Institutions are important to the economic development of poor countries because they provide stable frameworks for economic growth by ensuring property rights, reducing corruption and enforcing contracts.

5. Two main policies that a developing country can use to promote economic growth include promoting growth through infrastructure investment and education reforms.

Pg 371 Short Answers to Review Questions

1. Globalisation is the increased interconnectedness of economies, impacting trade, finance and culture.
2. Advantages of globalisation include: Economic growth, access to goods; disadvantages of globalisation include: Inequality, cultural erosion.
3. International trade organisations facilitate globalisation by reducing barriers and promoting trade agreements.

Pg 377 Short Answers to Review Questions

1. Producers and consumers benefit from a free trade area through increased choices and competitive pricing.
2. A common external tariff in a customs union creates uniform import duties, preventing members from setting individual rates.
3. A customs union harmonises tariffs; an economic union involves economic policy coordination and potentially a common currency.
4. Benefits of a common current include price stability; limitations involve loss of monetary policy control.
5. Globalisation is increased global interconnectedness, impacting trade, finance and culture.
6. Winners of globalisation include global corporations; losers may be small businesses and cultural diversity.
7. Developing countries benefit through access to markets, technology, and investments, but may face challenges like inequality.