Economics Questions

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Table of Contents

Question 1 3

Question 2 3

Question 3 4

Question 4 5

Question 5 6

Question 6 7

Question 7 7

Question 8 8

Question 9 9

Question 10 10

References: 12

# Question 1

**Explain and evaluate: “If resources were infinitely abundant in relation to the demand for them, the economizing problem would dissolve in a sea of affluence.”**

Economists and experts have said that economics is all about choosing options. The first lesson that economics teaches is to be able to choose the options when supply is limited. Infinitely abundant resources signifies never-ending supply, this mean that consumers can get what they want. They do not have to choose from the limited supply set. In this hypothetical case there won’t be any issue of economics involved. People would just get what they need. (O’Boyle, 1999, pp 48) Consumers would be happy that they do not have to make tough choices as they have access to unlimited supply. Hence it is said, “If resources were infinitely abundant in relation to the demand for them, the economizing problem would dissolve in a sea of affluence”. However this can never be the case in real world. In real world there is always a demand supply mismatch and consequently economics come into play. It is a social science that analyzes and manages the production, distribution and consumption of different goods and services.

# Question 2

**Can ticket “scalping” be justified? Explain using economic analysis.**

Ticker Scalping refer to the secondary market of tickets, wherein people can but tickets. The basic economic problem of ‘scarcity of resources’ holds here. In a football match there can be thousands of seats in stadium, however there are tens of thousands of people who want to get tickets. Hence tickets are sold in secondary market. To some people watching the match in stadium matters more to money, therefore they buy the ticket at twice, thrice or ten times it original price. (Azar, 2003, pp 1084)

Ethically ticket scalping may be wrong, however economically it is not as much wrong unless and until law prohibits it. The entire structure of scalping is based on speculation. People can earn profit if they guess right however they have to bear losses also if they guess wrong. Whenever any person is buying ticket from scalper, they both are making a rational choice, what seems to be correct to both of them. In economic terms it is just another market exchange. In places where scalping is banned many organizations use dynamic ticket pricing, in which prices of tickets are not fixed and the price tend to increase if demand of tickets is more than supply.

# Question 3

**What are the economic effects of an appreciation of the dollar in foreign exchange markets?**

An increase in the value of currency related to another currency is termed as appreciation of currency. Lets take an example: -

**Case 1**

$1 = 1 Euro (say)

**Case 2**

$ .80 = 1 Euro (say)

In case two value of dollar is appreciated. Previously I USD was required to but 1 Euro, however now (in case 2), only .80 USD is required to purchase 1 Euro. Hence the imports of the country would get a boost. Previously companies need to spend 1 dollar to but an article that costs 1 Euro in London. However once the dollar value is appreciated companies can get that same article in .80 dollars. With the appreciation of currency imports are less expensive and country can import in good quantities. (Choudhury, 1995, pp 69) This is one of the reason that developed countries like USA can import good quantities of goods from developing nations of China and India as USD has more value as compared to Indian and Chinese currency. There is an advantage to imports, however at the same time exports also became more expensive, therefore countries have to have a balance approach while maintaining the value of currency.

# Question 4

**Explain the perspective that tougher enforcement of drug laws for cocaine or other drug laws may actually increase the crime rate. Use the concepts of demand, supply, and elasticity in your explanation.**

Drugs like cocaine are highly inelastic in nature. People who are drug addicts do not care much about the price rise, or they are addicts therefore they have to buy drugs even when the price is high. With the enforcement of tough and stringent drug laws, there would be a reduction in the open supply of drugs, but the demand would remain same. (Duhs, 1994, pp 30) This supply level would not able to meet the existing demand hence the prices would rise. However the income of the drug addicts has not increased, therefore they would be forced to do something illegal and earn money so that they can buy drugs. This might give a push to the crime rate and crime incidents can actually increase. This is one of the reasons that the aim of government is to reduce the mania of drug and convince people that they should not use these harmful drugs. Government is ware that only limiting the supply of drugs is not going to help.

# Question 5

**A vice president of a company argues that the president of the company should raise workers’ wages if the president wants less absenteeism. The president says that wages probably should be cut so that the workers could not afford to miss so much work. Evaluate the two views using the income and substitution effects in your analysis.**

It is not clear that what does company’s workers prefer, do they prefer leisure or work. When the income is high workers can obviously afford more leisure (Income effect), hence there would be an increase in absenteeism. (Maddala, 1998, pp 70) However at the same time if their wages are high, it would be costly for them to ignore work and have leisure (Substitution effect).

Both these effects work in opposite to each other. It all depends that what effect is strong (income or substitution). If income effect is stronger than substitution effect then president is correct, as if workers are paid more they might reduce their working hours in order to have more of leisure time. With increase salary they would be able to earn sufficient in less time. This would offset the substitution effect, which has made the leisure expensive.

The second case is when substitution effect outweighs income effect. In this case president is wrong and vice president is right. In this case workers are getting less alary for their work, hence they can substitute the work with leisure, as they are not losing much. In this case absenteeism might also increase. Therefore either of the president or vice president may be correct in their approach. It depends on the attitude of the workers and effect of income and substitution effect. This again depends on lot of other factors like opportunities to use leisure time, level of disposable income etc.

# Question 6

**What is the real cost of putting an unemployed laborer to work raking leaves or digging holes and refilling them during a serious depression? Explain**

As presented in the question, the laborer was unemployed before; it implies that he was not earning anything before. As the productivity of the unemployed laborer was nil before this task of raking leaves of digging holes hence the real or true cost of employing this laborer is zero. It can be said that production at any stage is not compromised due to this laborer. Therefore this person can continue to rake leaves or dig holes. (Wolnicki, 2004, pp 300)

However the only true cost is the opportunity cost of the laborer. He might have done something other for his leisure. This opportunity cost is compromised when he is raking leaves or digging holes.

# Question 7

**How does pure competition differ from other basic market models?**

The basic market models are pure competition, monopoly, oligopoly and pure competition. These market models can be differentiated on the basis of five main factors. These are: -

* The number of firms operating in the market
* The type of existing product in the market
* Firm’s control over existing price
* Entry conditions in the industry
* The non-price competition

In pure competition there are large number of firms selling standardized products. Product differentiation is less and these independent firms are ‘price takers’. These firms do not have any control over the price levels and they have to accept the market price of the product. The entry in this industry is relatively easy and not price competition is also nil because companies produce standardized products. (Mavrommatis, 1998, pp 1570)

Pure monopoly is the exact opposite of pure competition. In pure monopoly there is one large firm dominating the market. This firm decides the price level in the market and entry barriers are also high. There are les substitute in the market and product standardization is low, other companies cannot produce the same type of goods.

# Question 8

**What are the basic characteristics of oligopoly? How does oligopoly compare with the other market structures?**

The four important market structures are pure competition, monopoly, oligopoly and monopolistic competition. In oligopoly market or industry is dominated by small number of sellers. These firms are known as oligopolists, as numbers of firms are less, these firms are aware of the actions of other firms. The decision of one firm is dependent on the decision of other firms. An example of oligopoly would be Verizon, AT & T, T – Mobile and Sprint in fourth quarter of 2008. These four firms combine had 89% of American cellular market. (Duhs, 1994, pp 4)

Oligopolies are similar to monopoly as these are also price makers, though they have less control over prices as compared to pure monopoly. However they are unlike pure competition that are pure price takers. Entry and exit barriers are also high in oligopoly, unlike pure competition where firms can easily enter and exit the market. Two of the most important barriers are patents protection and economies of scale. As discussed above number of firms in oligopoly are very less, this is in high contrast to pure competition. Oligopoly is somewhat similar to monopoly, however in monopoly there is only a single firm whereas in oligopoly there are few firms but more than 1. The product may be standardized or differentiated in an oligopoly. When there exists product differentiation that there also exists non-price competition.

# Question 9

**What are the case against and the case for the minimum wage? What does the evidence indicate?**

Minimum wage tend to promise a minimum wage to workers for their work. It men’s if government has said that minimum wages for car driver should be $8 per hour then car drivers can not be employed at $7 per hours. Many experts and economists have argued against this concept of minimum wages. They are of the opinion that minimum wage can de motivate employers to employee low skilled workers. For example if minimum wage is set above the existing equilibrium wage rate in the market then employers might remove some of the employees. Employment would be reduced because the marginal revenue earned for some of the workers would be less than the marginal costs.

However other experts and government favors the policy of minimum wages as they say that these are basic level of wages that should be given to every worker for their living. (Mandeville, 1998, pp 364) This wage rate is designed to get people out of poverty, though there is always a risk attached of reduction in employment levels of low skilled and unskilled workers.

The evidence of 1980s has suggested that there was a reduction in the levels of employment for youth and teenage people due to minimum wage hike. At that time there was near about 10% increase in wages that ultimately resulted in 2-3% reduction in employment.

# Question 10

**How can the economic perspective help us understand the behavior of fast-food consumers? Explain several insights it provides about customer behavior.**

The behavior of consumers can be analyzed at fast food chain restaurants. Some of the economic perspectives that can be applied are: -

* People always tend to choose the shortest queue; this is done to reduce the ‘time’ cost or the cost associated with time.
* People keep on shifting from one queue to another, therefore most of the times lines have equal lengths.
* Very often people choose the queue based on the number of people in that queue, they overlook the other factors. Probably the cost of obtaining more information is not worth the benefits that can be derived from that information. However in these cases false or incomplete information may ultimately results in longer waiting time. (Lutz, 2002, pp 27)
* Some people can also leave if the queue is much longer. For them the opportunity cost of standing in queue is high.
* Finally when any customer reaches the counter he would make the purchase decision, this choice would be made after he has analyzed different options and he has done the cost benefit analysis of different choices.

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