1. a) Both leisure and income (or the things that can be purchased with this income) can be considered “goods.” Increased consumption of one, reduces the amount of the other. “All else constant” consumption of more leisure will reduce income (since one works less). We assume leisure is enjoyable and work is not. In simple economics problems, we do not consider the possibility that people enjoy work – we assume they work to get money, which they use to buy things that make them happier.

b) If you buy (and consume) more A, you must buy (and consume) less of B

c) If you have children, you derive more utility from good schools. If you are sensitive to noise, derive more utility from living in a quiet neighborhood. Since home buyers have limited financial resources, they typically must give up some home characteristics they desire, in order to obtain other favorable characteristics which they value even more.

d) Your goal is not clear to economists. If we assume your primary goal is to keep your job, you would then allocate the police in such a way that you keep your job. If you are elected, you would have an incentive to allocate more police to areas with active voters, or where potential campaign contributors live.

2) The invisible hand guides people who are behaving selfishly to do things that benefit other members of society.

3) A good economic model should predict or explain some important element of the real world. It need not have realistic assumptions.

4) Money flowing out of firms and into to households are costs to firms and income to households.

5) i) Individuals have an incentive to have many children, so that at least one of them will survive to adulthood and be in a position to help their elderly parents; ii) If people are poor, the chance that their children will die is larger, and the need for financial assistance in their old age is greater; iii) If women are not typically employed outside the home, it will be less costly for them to spend time rearing their children (they won’t be giving up a high paying job); iv) On farms, children can be more of a benefit and less of a cost, since they can help with productive chores. People respond to incentives

6) When in doubt, make the same assumptions as N.G. Mankiw, (the author of our text) and accept his logic. It is very important that you understand how economists think (you need not personally think this way outside of class).

7) No – It seems likely that production of more computers, would lead to improvements in the production technology used to make them (the same might also be true for cars). It might be better to use corn and wheat, since increasing the level of production of either is less likely to change the production technology used.

8) Figure 3.1 assumes constant opportunity cost (and is therefore a straight line). Figure 2.2 assumes opportunity cost per unit of a good (e.g., cars) increases as more of this good is produced.

9) Either i or ii will shift out the PPF

10) Whistles

300 whistles, & 300 bells
200 whistles, & 300 bells: A workers make whistles and B workers make bells (b, iii)
100 whistles, & 100 bells: A workers make bells and B workers make whistles (b, iv) - inefficient

Bells