

Worksheet 3: Using economic terms answers

- 1 a) Worker A has a high degree of occupational mobility.
b) Worker B has a high degree of geographical mobility.

Example: Worker A has transferable skills to take up a job in a different industry, e.g. a bank employee can take up a job in public administration, while Worker B can commute or relocate to a different region/country to do the same job.

- 2 a) Money acts as a store of value.
b) Money needs to possess durability.

Store of value is one of the functions of money, which enables saving. This is possible due to its characteristic – durability, which means anything acting as money should retain its value over time.

- 3 a) The central bank is a lender of last resort.
b) Commercial banks can lend to individuals and firms.

The central bank can lend to commercial banks if they have liquidity problems, while commercial banks in turn, can lend to individuals and firms who are in need of borrowing.

- 4 a) High-income households spend a larger total amount of their income.
b) High-income households spend a smaller proportion of their income.

Rich households spend a larger total amount of money than poor households per period of time, but this takes a smaller proportion of their income, since the rich tend to have a lower average propensity to consume.

- 5 a) Interest rate is the cost of borrowing money.
b) Interest rate is the reward for saving.

Interest rate is both the cost of borrowing money and at the same time the reward for saving, since in the banking system saving fuels investment (e.g. saving enables commercial banks to lend to borrowers).

- 6 a) An increase in the wages of dentists will cause a contraction of the demand for dentists.
b) An increase in the wages of dentists will cause a decrease in the supply of workers in related occupations.

An increase in the wages of dentists will cause a movement up along the demand curve for dentists with fewer of them demanded, as the cost of employing one dentist to the firm increases. At the same time, this increase in wages will make this occupation relatively more attractive to alternative jobs, since the wage differential increases, thus attracting more individuals to work as dentists and reducing the supply of labour at every given wage for alternative occupations.

- 7 a) Division of labour increases productivity.
b) Specialisation increases total output.

Division of labour means workers do what they are best at, which increases their output per worker per hour, e.g. raises their productivity. Specialisation is division of labour at an international level and enables countries to make more efficient use of resources, thus enabling them to use their productive capacity to the fullest and increasing national output.

- 8 a) An increase in unemployment reduces the bargaining power of trade unions.
b) Trade unions can use collective bargaining to prevent unemployment.

An increase in unemployment increases the pool of available labour to firms and weakens the power of trade unions, since employees become more substitutable. On the other hand, one of the functions of trade unions is to prevent their members from becoming unemployed, e.g. by fighting against unfair dismissals, increasing productivity of members, etc.

- 9 a) Horizontal mergers can reduce competition.
b) Vertical backward mergers can limit access of competitors to important sources of raw materials.

A horizontal merger is one between two competitors at the same stage of production, so there is one competitor less on the market. Vertical backward integration is a merger with a supplier from a previous stage of production, which can be used to block the access of competitors to the source of raw materials, since the supplier is now acquired by the firm.

- 10 a) Internal economies of scale occur as a result of the growth of the firm.
b) External economies of scale occur as a result of the growth of the industry.

Internal are the economies of scale caused by growth of the firm itself, e.g. increasing its scale of production by moving to a larger factory. External economies of scale are caused by growth of the whole industry, e.g. better infrastructure to support a regional industry, which also benefits the firm, while the firm's own size could have remained unchanged.

- 11 a) A firm increases production.
b) A firm increases productivity.

An increase in production means the firm produces more output, e.g. more units are produced. An increase in productivity means an increase in output per worker per hour. Higher productivity is a sign of economic efficiency, but higher production does not necessarily mean the firm is more efficient, e.g. it could be wasting resources.

- 12 a) Firm A employs more workers than Firm B.
b) Firm B is labour-intensive.

The first statement means Firm A uses more units of labour (e.g. 30) than Firm B (e.g. 20) but we cannot be certain whether each firm is labour- or capital-intensive from the information given. The second statement means Firm B uses more labour in relation to capital.

- 13 a) A variable interest on a loan is a fixed cost.
b) A capital cost for purchasing a machine is also a fixed cost.

The variable interest on a loan is independent of output – the firm still has to pay its interest expense regardless of how many units of output it produces. The cost of purchasing a machine is also independent of output. Remember that fixed costs can and do change, but not as a result of changes in output.

- 14 a) Total fixed costs don't change as output increases in the short run.
b) Average fixed cost falls as output increases in the short run.

Total fixed cost is independent of output in the short run – the same cost is paid regardless of how many units are produced. But the average fixed cost falls as output increases because the same value (total fixed cost) is spread over an increasing value (more units of output).



- 15 a) Firm A is a price-taker.
b) Firm B is a price-maker.

Firm A has no control over the selling price of its product; operates in a competitive market and its demand curve is perfectly elastic. The firm's price is set by the ruling market price. Firm B can control its own price and its demand curve is downward sloping.