**Reading Assignment: Economic Lessons 1 & 2 on pages 20-24 of *Agricultural Marketing and Price Analysis***

***Lesson #1: Think Toys, Not Dollars***

1. *[1 Point] Fill in the blank…*Hail damaged roofs may increase the number of people working and even profits made by a community. "However, people will not have as many toys, they will be replacing

_____toys they once had_____."

2. *[1 Point]* The false thinking that destruction of property, and the increase in associated economic activity to restore that property, is good for an economy's wealth is referred

to as the *broken __window____ __fallacy_*.

3. *[2 Points]* China considers itself economically successful because it exports more goods to the U.S. than the U.S. exports to China. In a few clear and logical sentences, explain how China maintains its exports above its import level and why this is a stupid idea.

I'll grade this

When China exports goods to the U.S., Americans pay for those goods in U.S. dollars. Normally, the exporting country would immediately spend those U.S. dollars on U.S. goods, importing goods to China. In this normal case, the value of Chinese exports equals the value of Chinese imports. However, instead of spending U.S. dollars on U.S. goods, China locks them away in its vaults, forgoing the ability to consume American products, all for the sake of bragging rights that it exports more than it imports.

For China, this is a stupid idea. A successful business should seek to sell goods in greater value than the inputs it purchases, but this analogy does not extend to what a country sales and purchases abroad. China thinks it is growing rich by exporting more than it is importing, but all it is doing is accumulating dollars in vaults, and Chinese get no pleasure from dollar bills, only the toys those dollar bills could purchase. By pursuing this policy, China decreases its wealth by reducing its ability to consume toys.

4. *[1 Point]* In 1960, the per person income was around $3,000, while in 2005 it was $42,300.

However, using the __consumer____ ____price____ index, $3,000 in 1960 is

equivalent to $__20,000_____ in 2005. Thus, we are 2 times richer than we were in 1960, not 14 times richer.

5. *[1 Point]* A ___parity_ price is a price in one time period that has the same purchasing power as a price in another time period.

6. *[1 Point]* Farmers during the Great Depression wanted crop prices to have a "parity price" equivalent to crop prices in 1910-1914….why?

I'll grade this

The real price of agricultural commodities was high during the 1910-1914 period. Each bushel of corn sold in this period could purchase many other toys. The purchasing power of a bushel of grain fell in later periods, so farmers sought political influence to artificially raise the nominal price of an agricultural commodity until it had the same purchasing power as the same commodity in the 1910-1914 period.

*Economic Lesson #2: Beware the Law of Unintended Consequences*

7. *[2 Points]* To cut down on air emissions in Mexico City, the government enacted an ordinance saying each car must stay off the streets one day per week. The license plate tag indicated which particular day of the week the car could not be driven. The idea was that since these cars would remain idle one day each week, total emissions from cars would fall and air pollution would fall also. Clearly explain why this policy had the unintended consequence of increasing air pollution.

I'll grade this.

Having your car idled for one day is inconvenient, so inconvenient that many Mexicans purchased a second car to run on that one day. Because this second car would only run one day of the year, they tended to purchase older cars. These older cars consequently produce dirtier emissions. The effect of the dirtier emissions from these older cars overwhelmed the effect of less emissions from those who did not purchase a second car, leading to dirtier air. The policy intended to create cleaner air had the unintended consequence of produce more air pollution. Ironically, this policy made air pollution worse.

8. *[1 Point]* An _economic__ __model__ is a simplified version of the real world where many complexities are assumed away to concentrate on a single question.