Answers to End-of-Chapter Review Questions

1. First, markets are physical places where there is a reasonable expectation of finding both buyers and sellers for the same product or service. Second, markets are institutions that bring buyers and sellers into communication with each other, structuring and coordinating their actions. Third, “the market” is an abstract situation of pure exchange, or a global system of exchange.

2. Agricultural output per worker increased dramatically during the Industrial Revolution, with a corresponding decline in the proportion of the labor force needed to produce a nation’s food and mass migration into cities. Production was transformed from processes that used hand tools in households and small enterprises, to processes using machines and power tools in factories and other large enterprises. Trade also expanded both in the sense that people increased their reliance on formal markets and in the sense that international trade increased.

3. Changes in cultural attitudes that accompanied the Industrial Revolution included increased emphasis on individualism, instrumental rationality, materialism, and worker norms of punctuality and willingness to take orders.

4. Individualist institutions include private property, the ability to make decisions on an individual basis, and having prices set through the interaction of market participants. Social institutions of trust reduce the risk of transactions, and include factors of relationships, reputation, norms, implicit and explicit contracts, and institutions such as credit bureaus and government agencies that enforce regulations. Infrastructure institutions include buildings, equipment, transportation systems, and information technology. Money is also an institution that people must trust to hold its value and have minimal storage and handling costs.

5. Trustworthiness can be established through direct, one-to-one relationships, by establishing a reputation, by cultural norms, by ethical or religious codes, by implicit or explicit contracts, and by private and public agencies.

6. Examples of the infrastructure necessary for market functioning include physical infrastructure such as roads, vehicles, and warehouses, information technology infrastructure, and a system of money.

7. Ways in which the Industrial Revolution and marketization have improved life include freedom in individual decision-making, some beneficial forms of innovation and social cooperation, the development of many new products, jobs with better pay and working conditions, and an improved standard of living for many, including access to running water, warmer clothes and houses, better and more varied food, a great variety of products for leisure enjoyment, and a growing choice of other consumer goods.
8. Ways in which the Industrial Revolution and marketization have created problems include a failure to internalize the costs of environmental damage, an inability to deal with problems of maldistribution, insufficient supply of public goods, questionable impacts on the tastes of children, and concerns about the quantity and quality of jobs.

9. Nine types of markets are (1) retail markets (selling goods and services to consumers), (2) wholesale markets (selling to producers), (3) markets for intermediate goods (selling unfinished products), (4) product markets (selling newly produced goods and services; retail, wholesale and intermediate goods markets are both types of product markets), (5) resale markets (selling previously owned goods), (6) labor markets (selling labor services), (7) factor markets (selling inputs used to create new goods and services; labor markets are a subset of factor markets), (8) financial markets (selling debt and equity finance credit), and (9) underground markets (selling illegal goods and services).

10. Three major types of markets by how prices are set include (1) posted price markets (a fixed price is set by the seller), (2) auction markets (selling to the highest bidder), and (3) bargaining markets (a seller and buyer negotiate a price).

11. Three types of markets by time period covered are (1) spot markets (immediate delivery of the good or service), (2) futures markets (later delivery of a good), and (3) long-term contracts.