

Name: \_\_\_\_\_

Consider that the United States is experiencing historically **low** unemployment rates and that there is little “excess industrial capacity” (empty or unused factories). Approximately 5% of gross domestic product (GDP, total production of goods and services) in the U.S. consists of military goods.

The major Republican candidates have pledged expanded spending on defense if they are elected. All support development and deployment of a missile defense system, increased spending on military salaries and benefits, and modernizing of land, sea, and air major weapon systems.

a) Is it likely that there will be an opportunity cost to the increased military production? If not, why not? Explain in either case.

**The information (low unemployment & little excess industrial capacity) would tend to indicate that the economy is operating at a point ON the PPF. As such, there will be an opportunity cost to increased military production. But, it is not necessary to mention the PPF at this point. One could argue that any increased military production will require taking workers and factories away from civilian production. Thus, there is an opportunity cost.**

**It might be possible to make an argument that there is no opportunity cost but this would require discussion of why there are significant inefficiencies in the economy so that we appear to be at full employment but could produce more goods if only the inefficiencies were fixed.**

b) Using a production possibilities frontier diagram, show how the opportunity cost, if any, would be determined. Pick a point for the U.S. economy's current position based on the information provided.

**The opportunity cost of military production, in terms of civilian production, is the slope of the PPF. It would be calculated by estimating the slope of a line tangent to the PPF at the current point of production. The tangent line is shown in red on the graph. Its slope is the rise (DCivilian) over the run (DMilitary).**

