

University of British Columbia
Econ 101
Midterm 1
Fall 2012

Instructor: Alfred Kong
Time allowed: 50 minutes
Total marks: 25

Name:
Student Number:

This exam has 15 multiple choice questions in Part A and 4 short questions in Part B. Complete all the questions. Good luck.

Part A.
Multiple choice questions. Each question is worth 1 point.

- 1) Farm land can be used to produce either cattle or corn. If the demand for cattle increases, then the
 - A) demand for corn increases.
 - B) supply of corn increases.
 - C) demand for corn decreases.
 - D) supply of corn decreases.**
 - E) both B and C.

- 2) "As domestic car prices have increased, consumers have found foreign cars to be a better bargain. Consequently, domestic car sales have fallen and foreign car sales have risen." Based on this information alone, there has been a
 - A) shift in the demand curves for both domestic and foreign cars.
 - B) shift in the supply curves for both domestic and foreign cars.
 - C) movement along the demand curves for both domestic and foreign cars.
 - D) movement along the demand curve for domestic cars and a shift of the demand curve for foreign cars.**
 - E) shift of the demand curve for domestic cars and a movement along the demand curve for foreign cars.

- 3) Suppose we observe a rise in the price of good A and a decrease in the quantity of good A bought and sold. Which one of the following is a likely explanation?
 - A) The law of supply is violated.
 - B) The demand for A decreased.
 - C) The demand for A increased.
 - D) The supply of A increased.
 - E) The supply of A decreased.**

- 4) The price of a good will tend to fall if
 - A) there is a surplus at the current price.
 - B) the current price is below the equilibrium price.
 - C) the quantity supplied exceeds the quantity demanded at the current price.
 - D) both A and C are true.**
 - E) none of the above are true.

- 5) Which one of the following illustrates an inelastic demand?
- A) **A 10 percent rise in price leads to a 5 percent decrease in quantity demanded.**
 - B) A 10 percent rise in price leads to a 20 percent decrease in quantity demanded.
 - C) A price elasticity of demand equal to infinity.
 - D) A price elasticity of demand equal to 1.0.
 - E) A price elasticity of demand equal to 2.0.
- 6) Luxury goods tend to have income elasticities of demand that are
- A) **greater than 1.**
 - B) greater than zero but less than 1.
 - C) less than the income elasticities of demand for necessary goods.
 - D) negative.
 - E) first positive and then negative as income increases.
- 7) A rise in the price of good *A* shifts the
- A) demand curve for good *B* rightward if the cross elasticity of demand between *A* and *B* is negative.
 - B) **demand curve for good *B* rightward if the cross elasticity of demand between *A* and *B* is positive.**
 - C) supply curve of *B* rightward if the cross elasticity of demand between *A* and *B* is negative.
 - D) supply curve of *B* rightward if the cross elasticity of demand between *A* and *B* is positive.
 - E) demand curve for *B* rightward if the income elasticity of demand for *B* is positive.
- 8) When the price of a bicycle falls from \$220 to \$180 and other things remain the same
- I. the quantity demanded of bicycles increases from 150 to 250 an hour
 - II. the quantity demanded of skateboards decreases from 125 to 75 an hour
 - III. the quantity demanded of bicycle helmets increases from 170 to 230 an hour.
- Skateboards and bicycles are _____ because a fall in the price of a bicycle brings _____ in the quantity demanded of skateboards. The cross elasticity of demand for skateboards with respect to bicycles is _____.
- A) complements; an increase; -0.4
 - B) complements; a decrease; 0.4
 - C) substitutes; an increase; -2.5
 - D) **substitutes; a decrease; 2.5**
 - E) substitutes; a decrease; 0.4
- 9) Preferences for brussels sprouts increase. The price of brussels sprouts will not change if the price elasticity of
- A) demand is 0.
 - B) demand is 1.
 - C) supply is 0.
 - D) supply is 1.
 - E) **supply is infinity.**
- 10) During the next hour John can choose one of the following three activities: playing basketball, watching television, or reading a book. The opportunity cost of reading a book
- A) depends on how much the book cost when it was purchased.
 - B) **is the value of playing basketball if John prefers that to watching television.**
 - C) is the value of playing basketball *and* the value of watching television.
 - D) depends on how much John enjoys the book.
 - E) is the value of watching television if John prefers playing basketball to watching television.

- 11) "There can be too much of a good thing." This statement suggests that
- A) choices made in self-interest cannot be applied to many economic decisions.
 - B) a good may be produced to the point where its marginal cost exceeds its marginal benefit.**
 - C) certain goods and services such as education and health care are inherently desirable and should be produced regardless of costs and benefits.
 - D) a good may be produced to the point where its marginal benefit exceeds its marginal cost.
 - E) a good may be produced to the point where its marginal benefit is equal to its marginal cost.

- 12) If Sam is producing at a point inside his production possibilities curve, then he
- A) can increase production of both goods with zero opportunity cost.**
 - B) is fully using all his resources and allocating his resources to their best use.
 - C) must be doing the best he can with limited resources.
 - D) is unaffected by costs and technology.
 - E) has a high opportunity cost of moving from this point.

- 13) In general, if country *A* is accumulating capital at a faster rate than country *B*, then country *A*
- A) will soon have a comparative advantage in the production of most goods.
 - B) is using a larger proportion of resources to produce consumption goods.
 - C) will have a production possibilities frontier that is shifting out faster than country *B*'s.**
 - D) will have a higher rate of inflation than country *B*.
 - E) will have more unemployment than country *B*.

- 14) Which one of the following concepts is *not* illustrated by a production possibilities curve?
- A) scarcity
 - B) monetary exchange**
 - C) opportunity cost
 - D) attainable and unattainable points
 - E) the tradeoff between producing one good versus another
- Use the figure below to answer question 15.

- 15) Charlene is willing to pay \$5.00 for a sandwich. If the price of a sandwich is _____, Charlene _____.
- A) \$4.00; does not receive any consumer surplus
 - B) \$4.00; receives a consumer surplus**
 - C) \$6.00; receives a consumer surplus
 - D) \$6.00; receives a marginal cost
 - E) \$4.00; receives a producer surplus

Part B.
Short questions.

Question 1.

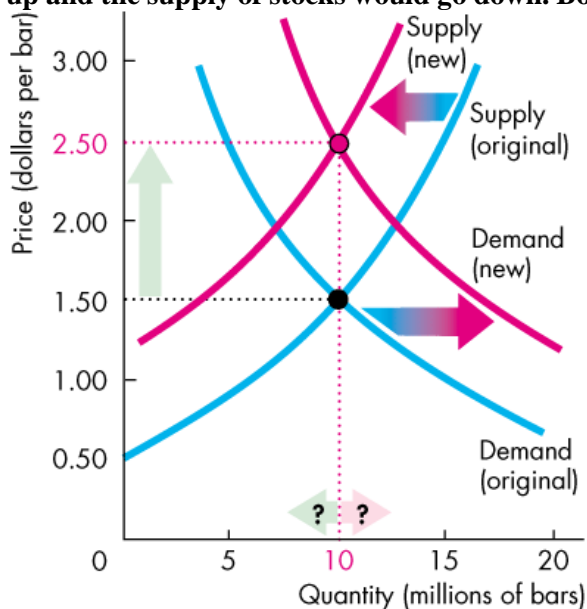
Your uncle owns a bakery shop, and he has never studied economics. He believes raising the price of his breads would increase his revenue. Explain to your uncle why that might not be the case. (2 points)

Whether his revenue would go up depends on the elasticity of demand for his breads. If the demand for his breads is elastic, then his revenue would actually fall when he increases the price. His thinking is only true if the demand for his breads is inelastic.

Question 2.

In the late 1990s the prices of company shares on stock markets rose to levels which, for many firms, were much higher than warranted by the values of their assets and their profits. How can demand and supply analysis explain why this “bubble” in stock market prices was caused by expectations that share prices would continue to rise? Use a graph to illustrate the outcome. (3 points)

If both buyers and sellers expect share prices would continue to rise, the demand of stocks would go up and the supply of stocks would go down. Both resulting in a higher stock prices.



(h) Increase in demand and decrease in supply

Question 3.

Netflix to Offer Online Movie Viewing

Online movie rental service Netflix introduced a new feature Tuesday to allow customers to watch movies and television series on their personal computers. ... Netflix has been competing with video rental retailer Blockbuster, which has added an online rental service to the in-store rental service.

CNN, January 16 2007

a. How will the offering of online movie viewing influence the price elasticity of demand for in-store movie rentals? (1 point)

The price elasticity of demand for store rental movies will increase because online movie viewing is another substitute for renting movies.

b. Would the cross elasticity of demand for online movies and in-store movie rentals be negative or positive? Explain. (1 point)

Online movies and in-store rental movies are substitutes, so their cross elasticity of demand is positive.

c. Would the cross elasticity of demand for online movies with respect to high-speed internet service be negative or positive? Explain. (1 point)

Online movies and high-speed Internet service are complements, so their cross elasticity of demand is negative.

Question 4.

Define the law of increasing opportunity cost. Briefly explain why the opportunity cost would increase. (2 points)

The law of increasing opportunity cost says when a society produces more and more Y, the opportunity cost of producing another unit of Y would be higher and higher. That is because not all the resources are suitable for producing Y. As the society produces more and more Y, some resources which are good for producing other goods are used to produce Y, so extra unit of Y would result in sacrificing more of other goods than before.