

Exam

Name \_\_\_\_\_

**MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.**

- 1) Other things being equal, the increase in rents that occurs after rent controls are abolished is smaller when 1) \_\_\_\_\_
- A) the own price elasticity of demand for rental homes is price inelastic.
  - B) the own price elasticity of demand for rental homes is price elastic.**
  - C) rented homes and owned homes are complements.
  - D) rented homes and owned homes are substitutes.
  - E) the own price elasticity of demand for rental homes has unitary price elasticity.
- 2) What happens if price falls below the market clearing price? 2) \_\_\_\_\_
- A) Quantity demanded decreases, quantity supplied increases, and price falls.
  - B) Quantity demanded increases, quantity supplied decreases, and price rises.**
  - C) Supply shifts in.
  - D) Demand shifts out.
- 3) Consider the demand curve of the form  $Q = a - bP$ . If  $a$  is a positive real number, and  $b = 0$ , then demand is 3) \_\_\_\_\_
- A) elastic, but not infinitely.
  - B) completely inelastic.**
  - C) unit elastic.
  - D) inelastic, but not completely.
- 4) Suppose the supply of textbooks is upward sloping and shifts leftward due to higher ink and paper costs. Which of the following events would leave the equilibrium price of textbooks at the same level observed before the supply shift? 4) \_\_\_\_\_
- A) Demand is perfectly elastic (horizontal).
  - B) Demand is downward sloping and shifts leftward.
  - C) all of the above**
  - D) none of the above
- 5) The principle of revealed preference would say that if Xavier chooses market basket A over market basket B then: 5) \_\_\_\_\_
- A) if A is more expensive than B, then Xavier must prefer A over B.**
  - B) if A is less expensive than B, then Xavier must prefer A over B.
  - C) if A is more expensive than B, then Xavier must prefer B over A.
  - D) if A is less expensive than B, then Xavier must prefer B over A.
- 6) When a person consumes two goods (A and B), that person's utility is maximized when the budget is allocated such that: 6) \_\_\_\_\_
- A) the marginal utility of A times the price of A equals the marginal utility of B times the price of B
  - B) the ratio of the marginal utility of A to the price of A equals the ratio of the marginal utility of B to the price of B.**
  - C) the ratio of total utility of A to the price of A equals the ratio of the marginal utility of B to the price of A.
  - D) the marginal utility of A equals the marginal utility of B.

7) Gary Franklin is a movie critic. He invented the Franklin Scale with which he rates movies from 1 to 10 (10 being best). When asked about his scale, Mr. Franklin explained "that it is a subjective measure of movie quality. A movie with a ranking of 10 is not necessarily 10 times better than a movie with a ranking of 1, but it is better. A movie with a ranking of 5 is better than a movie with a ranking of 1, but is not as good a movie with a ranking of 10. That's all it really tells you." Based on Mr. Franklin's description, his scale is: 7) \_\_\_\_\_

- A) an objective standard to judge movies.
- B) neither cardinal nor ordinal.
- C) **ordinal but not cardinal.**
- D) cardinal but not ordinal.

8) Which of the following goods has a low, but positive, income elasticity of demand? 8) \_\_\_\_\_

- A) new cars.
- B) furniture.
- C) **health insurance.**
- D) all of the above
- E) none of the above

9) The point price elasticity of demand for red herring is -4. The demand curve for red herring is:  $Q = 120 - P$ . What is the price of red herring? 9) \_\_\_\_\_

- A) \$80
- B) \$120
- C) **\$96**
- D) \$100
- E) none of the above

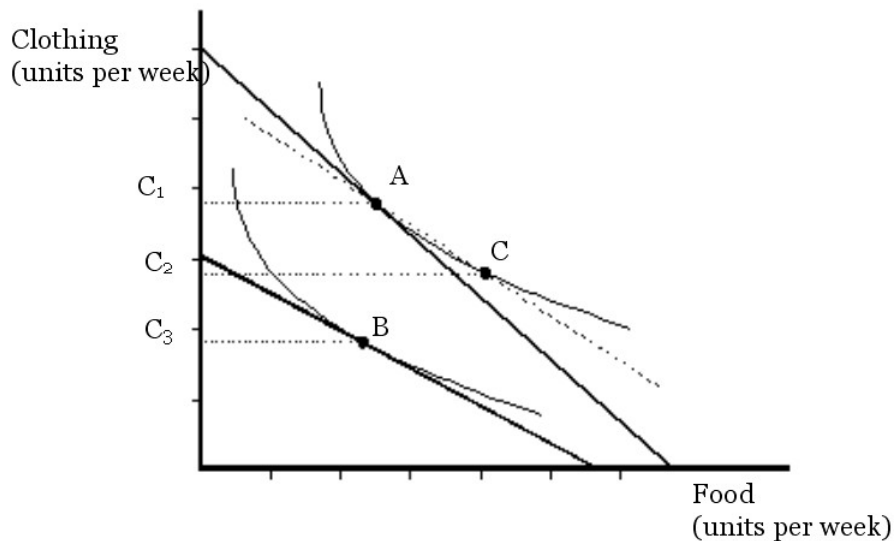


Figure 4.2

**CANCELLED**

A consumer's original utility maximizing market basket of goods is shown in Figure 4.2 as point A. Following a price change, the consumer's utility maximizing market basket is at point B.

10) Based Figure 4.2, clothing is: 10) \_\_\_\_\_

- A) an inferior good, but not a Giffen good.
- B) a Giffen good.
- C) **a normal good.**
- D) none of the above

- 11) An investment opportunity has two possible outcomes. The expected value of the investment opportunity is \$250. One outcome yields a \$100 payoff and has a probability of 0.25. What is the payoff of the other outcome? 11) \_\_\_\_\_
- A) \$150
  - B) \$0
  - C) \$300**
  - D) -\$400
  - E) none of the above
- 12) Nervous Norman holds 70% of his assets in cash, earning 0%, and 30% of his assets in an insured savings account, earning 2%. The expected return on his portfolio 12) \_\_\_\_\_
- A) is 2%.
  - B) is 0%.
  - C) is 0.6%**
  - D) is 1%.
  - E) cannot be determined without knowing what the dollar value of his assets is.
- 13) When facing a 50% chance of receiving \$50 and a 50% chance of receiving \$100, the individual pictured in Figure 5.2 13) \_\_\_\_\_
- A) would pay a risk premium of 10 utils to avoid facing the two outcomes.
  - B) would want to be paid a risk premium of \$7.50 to avoid facing the two outcomes.
  - C) would want to be paid a risk premium of 10 utils to give up the opportunity of facing the two outcomes.
  - D) would pay a risk premium of \$7.50 to avoid facing the two outcomes.**
  - E) has a risk premium of 10 utils.

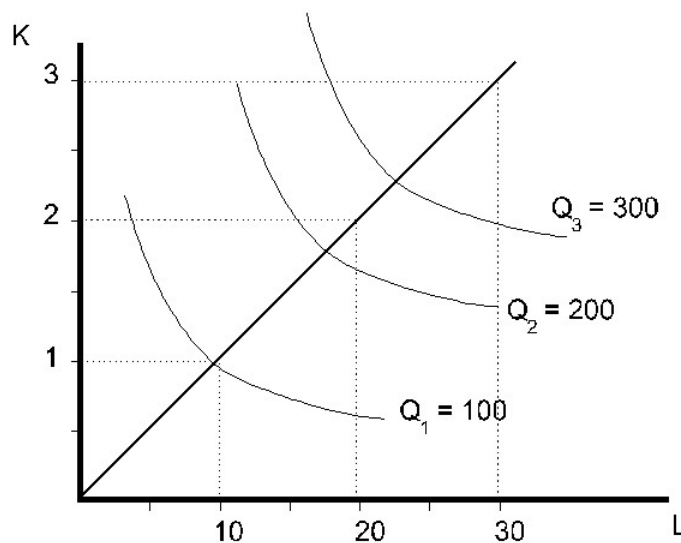


Figure 6.2

- 14) Refer to Figure 6.2. The situation pictured is one of 14) \_\_\_\_\_
- A) increasing returns to scale, because doubling inputs results in more than double the amount of output.**

- B) decreasing returns to scale, because the isoquants are convex.
- C) constant returns to scale, because the line through the origin is linear.
- D) increasing returns to scale, because the isoquants are convex.
- E) decreasing returns to scale, because doubling inputs results in less than double the amount of output.

**READ NOTE VERY IMPORTANT**

- 15) The Malthusian dilemma relates to marginal product in that 15) \_\_\_\_\_
- A) because of diminishing marginal product, the amount of food produced by each additional member of the population increases.
  - B) because of diminishing average product, the population will not have additional capital to work with.
  - C) because of diminishing marginal product, the amount of food produced by each additional member of the population decreases.**
  - D) because of diminishing marginal product, the wage falls as the population decreases.
  - E) starvation can be averted only if marginal product is constant.
- 16) A Cobb–Douglas production function: 16) \_\_\_\_\_
- A) exhibits constant returns to scale.
  - B) exhibits increasing returns to scale.
  - C) can exhibit constant, increasing, or decreasing returns to scale.**
  - D) exhibits decreasing returns to scale.
- 17) The total cost (TC) of producing computer software diskettes (Q) is given as:  $TC = 200 + 5Q$ . 17) \_\_\_\_\_  
 What is the average fixed cost?
- A)  $5Q$
  - B)  $5 + (200/Q)$
  - C) 5
  - D) 500
  - E) none of the above**
- 18) In long–run competitive equilibrium, a firm that owns factors of production will have an 18) \_\_\_\_\_
- A) economic and accounting profit can take any value.
  - B) economic and accounting profit = \$0.
  - C) economic profit = \$0 and accounting profit > \$0.**
  - D) economic and accounting profit > \$0.
  - E) economic profit > \$0 and accounting profit = \$0.
- 19) In a constant–cost industry, an increase in demand will be followed by 19) \_\_\_\_\_
- A) no increase in supply.
  - B) a decrease in demand to keep price constant.
  - C) an increase in supply that will bring price down to the level it was before the demand shift.**
  - D) an increase in supply that will bring price down below the level it was before the demand shift.
  - E) an increase in supply that will not change price from the higher level that occurs after the demand shift.

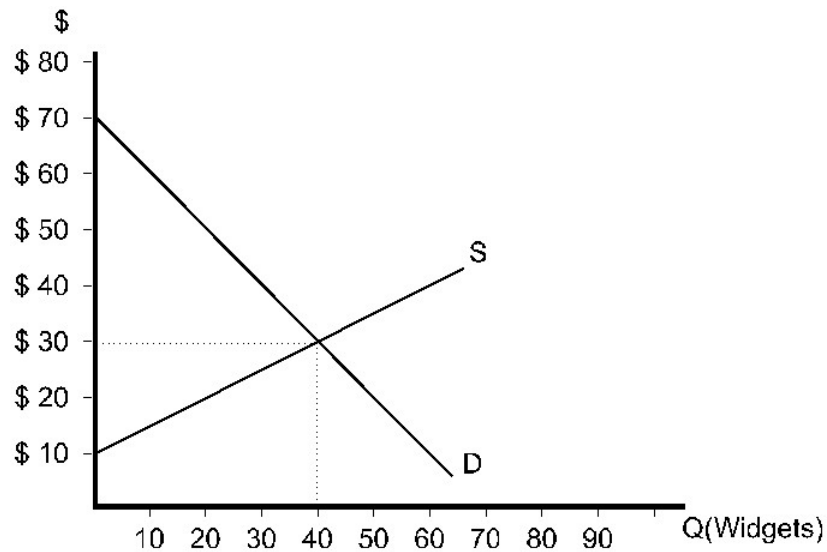


Figure 9.4

- 20) Suppose the market in Figure 9.4 is currently in equilibrium. If the government establishes a price floor of \$40, consumer surplus will \_\_\_\_\_
- A) fall by \$50.
  - B) rise by \$350.
  - C) fall by \$350.**
  - D) remain the same.
  - E) rise by \$50.
- 21) The consumer's gain from the imposition of a price ceiling is higher when \_\_\_\_\_
- A) the own price elasticity of market demand is high and the price elasticity of market supply is low.**
  - B) the own price elasticity of market demand is low and the price elasticity of market supply is low.
  - C) the own price elasticity of market demand is low and the price elasticity of market supply is high.
  - D) the own price elasticity of market demand is high and the price elasticity of market supply is high.
- 22) Ford Motor Company was one of the first major companies to adopt a wage structure that is comparable to efficiency wages. What was the outcome of Ford's experiment with efficiency wages? \_\_\_\_\_
- A) Less absenteeism
  - B) Higher labor productivity
  - C) Lower labor force turnover
  - D) all of the above**
- 23) If households could be charged differently for different types of garbage, \_\_\_\_\_
- A) billing for garbage collection would be much easier.
  - B) recycling would be more difficult.
  - C) the total amount of garbage would be reduced.
  - D) there would be a change in the types of items that are disposed of as garbage.**
  - E) costs of collecting garbage could be kept much lower.

- 24) From 1970 to 1993, the real price of a college education increased, and total enrollment increased. 24) \_\_\_\_\_  
Which of the following *could* have caused this increase in price and enrollment?  
A) A shift to the right in the supply curve for college education and a shift to the left in the demand curve for college education.  
B) A shift to the left in the supply curve for college education and a shift to the left in the demand curve for college education.  
**C) A shift to the left in the supply curve for college education and a shift to the right in the demand curve for college education.**  
D) none of the above
- 25) Sue views hot dogs and hot dog buns as perfect complements in her consumption, and the corners of her indifference curves follow the 45-degree line. Suppose the price of hot dogs is \$5 per package (8 hot dogs), the price of buns is \$3 per package (8 hot dog buns), and Sue's budget is \$48 per month. What is her optimal choice under this scenario? 25) \_\_\_\_\_  
A) 8 packages of hot dogs and 8 packages of buns  
B) 8 packages of hot dogs and 6 packages of buns  
**C) 6 packages of hot dogs and 6 packages of buns**  
D) 6 packages of hot dogs and 8 packages of buns
- 26) Which of the following is true regarding utility along a price-consumption curve? 26) \_\_\_\_\_  
A) It changes only if income changes. **B) It changes from point to point.**  
C) It changes only for normal goods. D) It is constant.
- 27) The indifference curves of two investors are plotted against a single budget line. Indifference curve A is shown as tangent to the budget line at a point to the left of indifference curve B's tangency to the same line. 27) \_\_\_\_\_  
A) Investors A and B will have different portfolios but have the same level of risk aversion.  
B) Investors A and B will hold the same portfolio.  
C) Investors A and B will have different portfolios of the same rate of return.  
**D) Investor A will expect to earn a lower rate of return than investor B.**  
E) Investors A and B will have different portfolios of the same standard deviation.
- 28) The law of diminishing returns refers to diminishing 28) \_\_\_\_\_  
A) average returns. **B) marginal returns.**  
C) total returns. D) all of these.
- 29) Which of the following costs always declines as output increases? 29) \_\_\_\_\_  
A) Marginal cost  
**B) Average fixed cost**  
C) Fixed cost  
D) Average cost  
E) Average variable cost

- 30) Suppose the state legislature in your state imposes a state licensing fee of \$100 per year to be paid by all firms that file state tax revenue reports. This new business tax: 30) \_\_\_\_\_
- A) decreases marginal cost.
  - B) decreases marginal revenue.
  - C) increases marginal cost.
  - D) increases marginal revenue.
  - E) **none of the above**

- 31) Consider a good whose own price elasticity of demand is  $-0.5$  and price elasticity of supply is  $1.5$ . The fraction of a specific tax that will be passed through to consumers is \_\_\_\_\_. 31) \_\_\_\_\_
- A) 1                      B) 0                      C) 0.25                      D) **0.75**                      E) 0.5

**Scenario 17.3**

Consider the following information:

The probability of a fire in a factory without a fire prevention program is 0.01. The probability of a fire in a factory with a fire protection program is 0.001. If a fire occurred, the value of the loss would be \$300,000. A fire prevention program would cost \$80 to run.

- 32) Refer to Scenario 17.3. If there is no insurance and no fire protection program in place, the expected loss from fire for this company is 32) \_\_\_\_\_
- A) \$6,000.                      B) \$300.                      C) \$300,000.                      D) \$0.                      E) **\$3,000.**

- 33) Which of the following is a public good? 33) \_\_\_\_\_
- A) **Broadcast TV**
  - B) A daily newspaper
  - C) The Red Cross
  - D) Telephone service
  - E) all of the above

- 34) Which of the following is NOT an application of supply and demand analysis? 34) \_\_\_\_\_
- A) Evaluating the effects of government price controls on the agricultural industry
  - B) Determining how taxes affect aggregate consumption spending patterns
  - C) Understanding changing world economic conditions and their effects on prices
  - D) all of the above
  - E) **none of the above**

- 35) Denise is shopping for lobsters and eclairs. When she faces budget line  $b_1$ , she chooses market basket A over market basket B. When she faces budget line  $b_2$ , she chooses basket B over basket C. Which assumption of consumer theory helps us determine Denise's preference ordering over basket A and basket C? 35) \_\_\_\_\_
- A) Convexity    B) More is better than less  
C) **Transitivity**    D) Completeness

- 36) The demand for sirloin steak is probably more elastic than the demand for all meat because 36) \_\_\_\_\_
- A) cattle raising is not very profitable.

- B) steak is very expensive.
- C) there are more substitutes for sirloin steak than for all meats.**
- D) people are worried about cholesterol.

The information in the table below describes choices for a new doctor. The outcomes represent different macroeconomic environments, which the individual cannot predict.

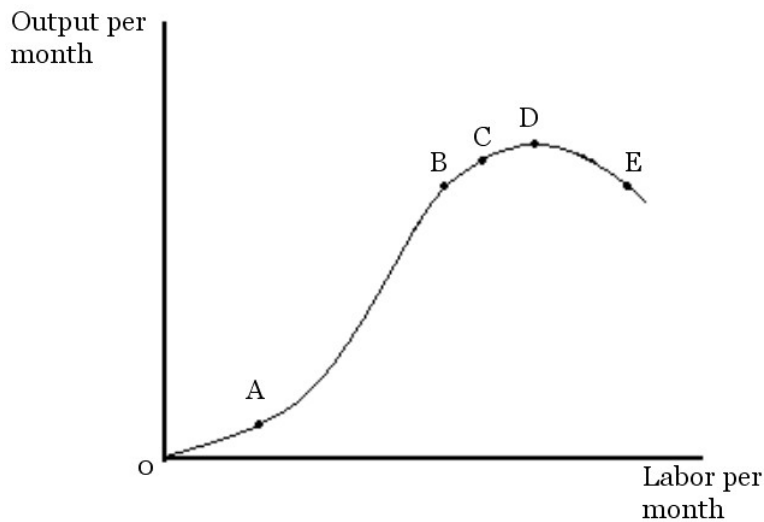
**Table 5.3**

Job Choice	Outcome 1		Outcome 2	
	Prob.	Income	Prob.	Income
Work for HMO	0.95	\$100,000	0.05	\$60,000
Own practice	0.2	\$250,000	0.8	\$30,000
Research	0.1	\$500,000	0.9	\$50,000

37) Refer to Table 5.3. The expected returns are highest for the physician who

37) \_\_\_\_\_

- A) works for an HMO.**
- B) either works for an HMO or does research.
- C) either opens her own practice or does research.
- D) does research.
- E) opens her own practice.



**Figure 6.1**

38) Refer to Figure 6.1. At point C

38) \_\_\_\_\_

- A) the marginal product of labor and the average product of labor are equal.
- B) the marginal product of labor is greater than the average product of labor.
- C) the average product of labor is greater than the marginal product of labor.**
- D) the marginal product of labor and the average product of labor are both increasing.
- E) Both B and D are correct.

39) We typically think of labor as a variable cost, even in the very short run. However, some labor costs may be fixed. Which of the following items represents an example of a fixed labor cost?

39) \_\_\_\_\_

- A) A temporary worker who is paid by the hour
- B) An hourly employee
- C) A salaried manager who has a three-year employment contract**

D) none of the above

40) The demand curve facing a perfectly competitive firm is

40) \_\_\_\_\_

**A) perfectly horizontal.**

B) downward-sloping and less flat than the market demand curve.

C) the same as the market demand curve.

D) downward-sloping and more flat than the market demand curve.

E) perfectly vertical.