

First Midterm (October 20, 2016)

Instructions: Please fill in your name/initials and student number on every page of this questionnaire and on the Answer Sheet provided. Use the Answer Sheet to answer the Multiple Choice questions. Answer the Short Answer questions in the space provided on this questionnaire. There are 34 questions in total (31 multiple choice plus 3 short answers). This exam has 11 pages -- check that this copy has all of them. You may use a non-programmable calculator. Good luck !!

Multiple Choice Questions (62 points -- 2 points per question)

Identify the letter of the choice that best completes the statement or answers the question.

1. If a price ceiling in a market is binding, which of the following is true?
 - a. The equilibrium price must be below the price ceiling.
 - b. The equilibrium price must be above the price ceiling.
 - c. The forces of supply and demand must be in equilibrium.
 - d. The price ceiling will have no effect on supply or demand.

2. How do economists view positive statements?
 - a. Affirmative, justifying existing economic policy.
 - b. Descriptive, making a claim about how the world is.
 - c. Prescriptive, making a claim about how the world ought to be.
 - d. Optimistic, putting the best possible interpretation on things.

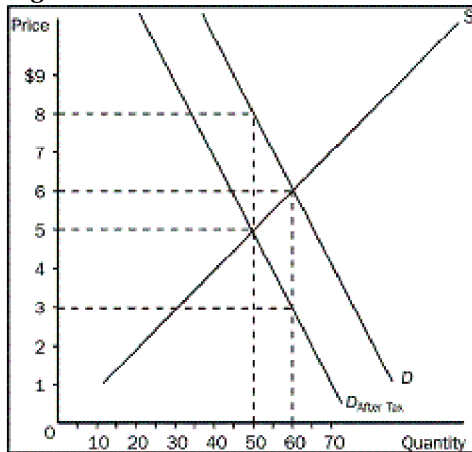
3. Why are workers with high skills and much experience not affected by the minimum wage?
 - a. They generally earn wages less than the minimum wage.
 - b. They belong to unions.
 - c. Their equilibrium wages are well above the minimum wage.
 - d. They are not legally guaranteed the minimum wage.

4. What can the income elasticity of demand tell us?
 - a. Whether goods are normal or inferior.
 - b. Whether goods are elastic or inelastic.
 - c. Whether goods are essential or non-essential.
 - d. Whether goods are complements or substitutes.

5. What impact would a higher price for batteries tend to have?
 - a. Increase the demand for batteries.
 - b. Decrease the demand for electricity.
 - c. Increase the demand for electricity.
 - d. Increase the demand for flashlights.

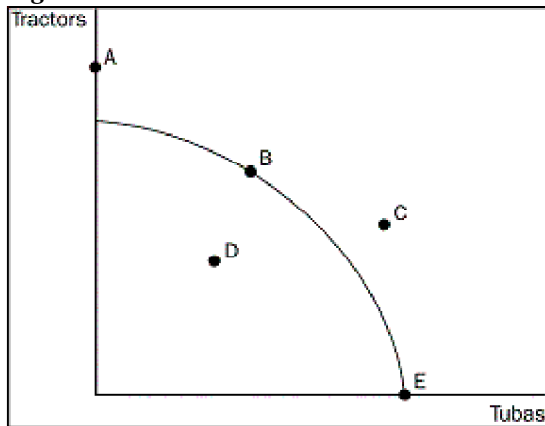
6. What is the amount of the good buyers are willing and able to purchase?
 - a. Supply.
 - b. Demand.
 - c. Quantity supplied.
 - d. Quantity demanded.

Figure 1



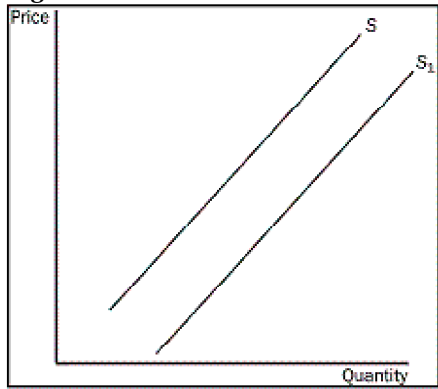
7. Refer to Figure 1. What is the amount of the tax imposed in this market?
- \$1.00 per unit
 - \$1.50 per unit
 - \$2.50 per unit
 - \$3.00 per unit

Figure 2



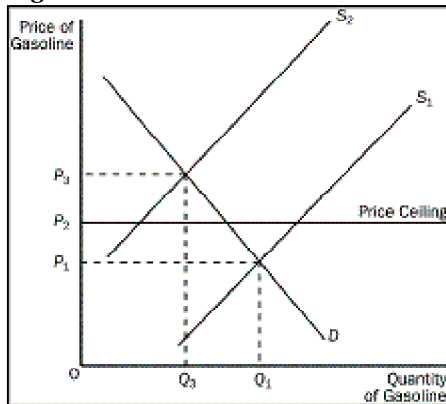
8. Refer to Figure 2. Which point or points are inefficient?
- Points A and C.
 - Points D and C.
 - Points D and C.
 - Point D.
9. Which of the following is NOT true about most economic models?
- They are useful to economists, but not to policymakers.
 - They are built using the tools of mathematics.
 - They do not include every feature of the economy.
 - They are built using assumptions.

Figure 3



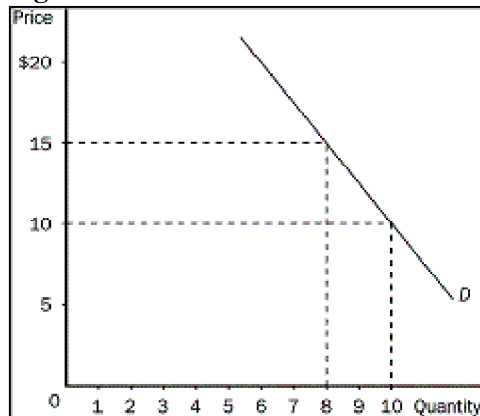
10. Refer to Figure 3. What is the movement from S to S_1 called?
- An increase in supply.
 - A decrease in quantity supplied.
 - A decrease in supply.
 - An increase in quantity supplied.

Figure 4



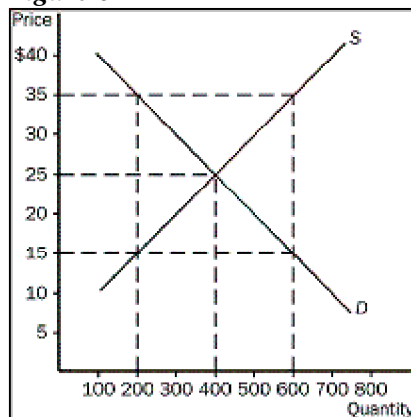
11. Refer to Figure 4. With a price ceiling present in this market, what will happen when the supply curve for gasoline shifts up from S_1 to S_2 ?
- A shortage will occur at the price ceiling of P_2 .
 - A surplus will occur at the new market price of P_2 .
 - The market price will stay at P_1 due to the price ceiling.
 - The price will increase to P_3 .
12. Why do policymakers choose to enact price controls in a market?
- Enacting price controls will directly increase tax revenues.
 - They believe the market's outcome to be unfair.
 - They believe that the market system is inefficient and their actions will improve efficiency.
 - They are required by law to improve market conditions.

Figure 5



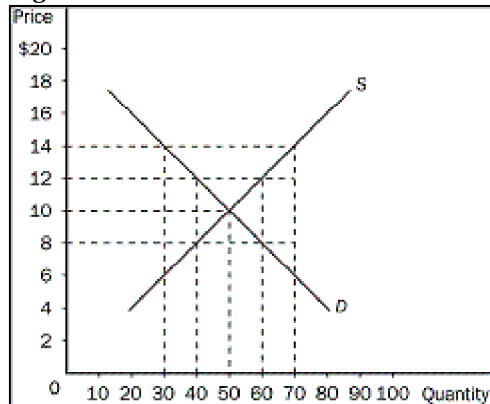
13. Refer to Figure 5. What is the price elasticity of this demand curve between \$10 and \$15?
- Unit elastic.
 - Perfectly elastic.
 - Elastic.
 - Inelastic.

Figure 6



14. Refer to Figure 6. What are the equilibrium price and quantity?
- \$35 and 600
 - \$35 and 200
 - \$15 and 200
 - \$25 and 400
15. If there is trade, which of the following is most likely?
- A country's consumption possibilities frontier can be outside its production possibilities frontier.
 - A country will produce a greater variety of goods and services to trade.
 - A country is worse off because it becomes dependent on other countries.
 - A country will experience a lower unemployment rate.

Figure 7



16. Refer to Figure 7. If the market price were currently \$8, what would happen?
- There would be a surplus of 20 units and the price would tend to fall.
 - There would be a surplus of 20 units and the price would tend to rise.
 - There would be a shortage of 20 units and the price would tend to rise.
 - There would be a shortage of 20 units and the price would tend to fall.
17. What will happen to the equilibrium price of new cars if the price of gasoline falls, the price of steel increases, public transportation becomes more expensive and less comfortable, auto workers receive higher wages, and automobile insurance becomes less expensive?
- The price change will be ambiguous.
 - Price will stay exactly the same.
 - Price will rise.
 - Price will fall.
18. Workers at a bicycle assembly plant currently make minimum wage. If the provincial government increases the minimum wage by \$1.00 an hour, what will likely happen?
- The firm must increase output to maintain profit levels.
 - Supply of bicycles will shift to the left.
 - Supply of bicycles will shift to the right.
 - Demand for bicycle assembly workers will increase.
19. When the price of a slice of pizza is \$4, Denise buys 5 slices per month. When the price is \$3, she buys 9 slices per month. Is Denise's demand for pizza slices elastic or inelastic, and what can be said about the slope of her demand curve?
- Her demand is inelastic and the curve would be relatively steep.
 - Her demand is inelastic and the curve would be relatively flat.
 - Her demand is elastic and the curve would be relatively steep.
 - Her demand is elastic and the curve would be relatively flat.
20. Which of the following is true in a competitive market?
- If one seller withholds his product from the market, prices will rise.
 - Only a few sellers sell the same product.
 - Each seller has limited control over the price of his product.
 - If one buyer chooses to purchase a large quantity of the product, the price will rise.

21. Suppose that the incomes of buyers in a particular market for an inferior good increase and there is also a reduction in input prices. Which of the following would occur in this market?
- Both equilibrium price and equilibrium quantity would increase.
 - Equilibrium quantity would increase, but the impact on equilibrium price would be ambiguous.
 - The equilibrium price would increase, but the impact on equilibrium quantity would be ambiguous.
 - The equilibrium price would decrease, but the impact on equilibrium quantity would be ambiguous.

Table 1

	Labour hours needed to make one unit of		Amount produced in 40 hours	
	Cheese	Bread	Cheese	Bread
England	1	2	40	20
Spain	2	8	20	5

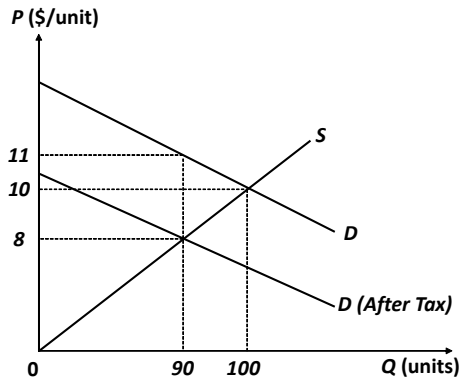
22. **Refer to Table 1.** What is the opportunity cost of 1 unit of bread in England?
- 2 cheeses.
 - 1 cheese.
 - 4 cheeses.
 - 1/4 cheese.
23. Harry's Barber Shop increased its total monthly revenue from \$1,500 to \$1,800 when it raised the price of a haircut from \$5 to \$9. What is the price elasticity of demand for Harry's haircuts?
- 0.318
 - 0.416
 - 0.700
 - 0.816
24. What do economists illustrate when they use the phrase "There is no such thing as a free lunch"?
- That to get one thing, we must give up something else.
 - That if something looks too good to be true, it probably is.
 - How inflation increases prices.
 - That nothing is free in a market economy.
25. What usually happens when government policies are designed to achieve a social objective?
- Increased efficiency results from more equity.
 - There is a tradeoff between equity and efficiency.
 - Equity can be achieved without any loss in efficiency.
 - Equity is independent of efficiency.
26. What is one necessary role of government to play in a market economy?
- To maintain welfare programs for the poor.
 - To provide services such as pensions.
 - To tax goods and services that are most desired by consumers.
 - To enforce property rights.

27. The demand for cigarettes is price inelastic and the supply of cigarettes is price elastic. The demand for champagne is price elastic and the supply of champagne is price inelastic. Suppose that a tax of \$1 per pack is levied on the sellers of cigarettes and a tax of \$1 per bottle is levied on the buyers of champagne. Who would have to pay most of these taxes?
- The buyers of cigarettes and the buyers of champagne.
 - The buyers of cigarettes and the sellers of champagne.
 - The sellers of cigarettes and the sellers of champagne.
 - The sellers of cigarettes and the buyers of champagne.
28. What does the price elasticity of demand for a good measure?
- How willing consumers are to buy more of a good as price rises.
 - How willing firms are to produce more of a good as price rises.
 - How willing consumers are to buy more of a good as price falls.
 - How willing firms are to produce more of a good as price falls.
29. If an increase in the price of a good results in an increase in total revenue for the firm, what must the supply of the good be?
- Nothing can be said about price elasticity of supply from the information given.
 - Elastic.
 - Inelastic.
 - Unit elastic.
30. If market demand is given as $Q_d = 250 - P/2$ and market supply is given as $Q_s = 2P$, which of the following would result if the market price were \$120?
- A surplus of 50.
 - A shortage of 50.
 - A shortage of 100.
 - A surplus of 100.
31. What would happen to the equilibrium price and quantity of peanut butter if the price of peanuts fell, the price of jelly (a complementary good) decreased, more firms decided to produce peanut butter, and health officials announced that eating peanut butter was good for you?
- Price will fall and the effect on quantity is ambiguous.
 - Quantity will increase and the effect on price is ambiguous.
 - Price will rise and the effect on quantity is ambiguous.
 - Quantity will fall and the effect on price is ambiguous.

Short Answer Questions (38 points)

Answer in the space provided. Clearly label all diagrams.

32. (7 points) Using the graph below, answer the following questions.



- What was the equilibrium price in this market before the tax?
- What is the amount of the tax?
- How much of the tax will the buyers pay?
- How much of the tax will the sellers pay?
- How much will the buyer pay for the product after the tax is imposed?
- How much will the seller receive after the tax is imposed?
- As a result of the tax, what has happened to the level of market activity?

33. (15 points in total) Suppose the government introduces a binding price floor in the market for unskilled labour.
- a. (11 points; 5 points for the diagram) Using a supply and demand diagram, explain how the binding price floor will affect the market. What will happen to the quantity of unskilled labour supplied and demanded? Who is helped by this policy and who is hurt?
- b. (4 points) What are four characteristics of Canadians who earn the minimum wage?

34. (16 points in total) Suppose person A and person B each work 48 hours per week. Person A can complete one tax return using 2 hours of labour and one policy report using 1 hour of labour. Person B can complete one tax return using 6 hours of labour and one policy report using 1.5 hours of labour. Assume the opportunity cost of tax returns is constant.
- a. (6 points) Draw the production possibility frontier for person A for one week of work and the production possibility frontier for person B for one week of work.
- b. (2 points) In what sense does it cost less for person A to prepare tax returns and policy reports? (*Hint: Think about absolute advantage and/or comparative advantage.*)
- c. (2 points) In what sense does it cost less for person B to prepare policy reports? (*Hint: Think about absolute advantage and/or comparative advantage.*)

- d. (2 points) If the two persons were to engage in trade, who would trade which good?
- e. (4 points) Suppose that each person initially spends half his/her time producing each of the two goods. Would each person benefit from trade if person A were to instead produce 19 tax returns per week, while person B specialized in the production of policy reports, and 15 policy reports were traded in exchange for 5 tax returns?