

MIDTERM EXAM 1

Version A

FULL NAME: _____
STUDENT ID: _____

Your TA is (circle one) EBRAHIM REZA

TUTORIAL SECTION:

INSTRUCTIONS: you have 1 hour 30 minutes to complete the exam. Write all your answers in the space provided; any work on the backside of the pages will be given zero credit. You can write in either pen or pencil. If you write in pencil your exam cannot be regraded.

The exam has 2 sections:

15 multiple choice questions

4 written answer questions

MC _____

WRITTEN PART _____

TOTAL _____

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

- 1) Kristian has 21 pairs of jeans and 12 t-shirts in his closet, denote this bundle as (21; 12). He would be just as happy (indifferent) to hold bundles (20;18) and (22; 8) where the first number is the number of jeans and the second number is the T-shirts. Price of a pair of jeans is 30 and price of a T-shirt is 15 dollars. Based in this information we can conclude that Kristian _____
- A) has too many jeans
 - B) has too many t-shirts
 - C) has the right amount of jeans and t-shirts
 - D) can be in equilibrium or not - impossible to tell without knowing his demands.
- 2) When Ana's income was 60,000 she consumed 125 units of good X per year. When her income became 90,000 she purchased 100 units. Her income elasticity of demand is _____
- A) -0.083
 - B) -2.5
 - C) -0.4
 - D) -25/30,000
 - E) -0.75
- 3) Demand is $P=40-0.25Q$. At quantity $Q=120$ the **point** elasticity of demand is _____
- A) -1/3
 - B) -0.25
 - C) -1/30
 - D) -3
 - E) -30
- 4) If demand is perfectly inelastic _____
- A) the slope of the demand curve is zero
 - B) a 10% increase in price will have no impact on consumer's spending
 - C) a 10% increase in price will lower consumer's spending on the good by 10%
 - D) a 10% increase in price will increase consumer's spending by 10%
 - E) a 10% increase in price will lower consumer's spending by 10%
- 5) Consider a market with a fixed supply and an inelastic demand. If supply increases _____
- A) both sellers and buyers will be better off because total gains from trade increase
 - B) buyers will be better-off while impact on seller's well-being is ambiguous
 - C) buyers will be better-off while sellers will be worse-off
 - D) it is impossible to predict how the well-being of buyers and sellers will be affected because gains from trade are not shared equally in a market.
- 6) Anders and Julie are sitting in a sushi restaurant. At a-la-carte price of 2.00 a piece each of them would order 8 pieces. All-you-can-eat option costs 20 dollars. In the end Julie goes with a-la-carte option and Anders buys all-he-can-eat dinner. From this information we can conclude that at the price of 2 dollars _____
- A) Julie's demand must be unit elastic and Anders's demand can be elastic or inelastic
 - B) Julie must have perfectly inelastic demand while Anders has downward-sloping demand
 - C) Anders has relatively inelastic demand while Julie's demand is relatively elastic
 - D) Anders has relatively elastic demand while Julie's demand is relatively inelastic
 - E) Anders' demand is perfectly elastic while Julie's demand is perfectly inelastic

- 7) If a good is not scarce then 7) _____
- A) people must place no value on it whatsoever
 - B) the quantity available is greater than quantity demanded at zero price
 - C) quantity available is lower than what is demanded at zero price, but at current price everyone can buy as much as they want.
 - D) current price of the good is above equilibrium, so there is a surplus of it in the market
- 8) Lola and Dale have the following monthly marginal values of strawberries $MV_L=20-2Q_L$ and $MV_D=10-Q_D$, where Q is pounds of strawberries. Lola has a garden in which every month exactly $Q=14$ pounds of strawberries magically appear. If she sells half of her crop to Dale (7 units) the situation will be 8) _____
- A) inefficient, she should sell less than that
 - B) efficient or inefficient depending on the price of the strawberries at which they trade.
 - C) inefficient, she should sell more than that
 - D) efficient because they will have equal amounts of the good
- 9) Demand must be elastic if 9) _____
- A) lowering price by one dollar increases quantity by more than one unit
 - B) lower prices lead to lower consumption
 - C) lower prices lead to higher spending on the good
 - D) lowering price by one dollar increases quantity by less than one unit
 - E) lower prices lead to lower spending on the good
- 10) If consumers incomes increase by 10% while prices rise by 20% 10) _____
- A) demands for normal goods will increase
 - B) demands will not change because relative prices did not change
 - C) demands for inferior good will increase
 - D) prices will have to fall by 10% to restore equilibrium
- 11) The value paradox (water-diamond paradox) 11) _____
- A) demonstrates that sometimes prices do not reflect the marginal value of the goods
 - B) is explained by the difference in people's preferences towards diamonds and water (demand for diamonds must be higher)
 - C) is explained by the negative relationship between total value and spending on a good
 - D) is explained by the negative relationship between total value and marginal value.

- 12) Other things equal, elasticity of demand for clothing for consumers with lower incomes compared to high-income consumers 12) _____
- A) should be the same because clothing is a necessity
 - B) should be lower because low income consumers have less options available
 - C) can be higher or lower, because price elasticity of demand does not depend on income.
 - D) should be higher because clothing takes up larger share of income when a person does not have much money
- 13) At price $P=50$ dollars a store sells 200 tank tops a month. The store manager wants to increase quantity sold to 236 units/month. The absolute value of price elasticity is 2. What price should he charge? 13) _____
- A) 32
 - B) 54.5
 - C) 45.5
 - D) 48
 - E) it is impossible to sell that quantity given the numbers provided.
- 14) Demand for public transit in Vancouver will decrease if 14) _____
- A) incomes increase and it is an inferior good.
 - B) TransLink increases bus fares
 - C) price of cars falls
 - D) all of the above
 - E) (B) and (C)
- 15) Consumer's demand for a good is $P=50-2Q$. The highest amount this consumer is willing to pay for a box with ten units of the good rather than have none of it at all is 15) _____
- A) 400
 - B) 300
 - C) 30
 - D) 100
 - E) none of the above

3. (10 marks) Market demand for one-bedroom apartments is $P=1,200-0.5Q$. In short-run there are $Q=1,000$ units available. Calculate the monthly rent if the housing market is in equilibrium, calculate the gains for tenants and landlords. What will happen if government imposes rent controls at 500 dollars/mo? Explain fully how this policy affects the market.

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4. (8 marks) Ana tells John a story about prices of limes, the summary of which is as follows:
- normally the average price of limes is 33 cents/piece;
 - last year due to a combination of fungus infection, heavy rain and drug cartels raiding the lime farms price of limes went over a dollar and at the highest reached 1.50/piece.
 - now the price is back to `three per dollar`.

John listened carefully and then said: Of course it eventually must return to normal! When price rises like that, no one wants to pay that much and the demand will eventually fall so that the price adjust to reflect the true value people place on the product.

Demonstrate this situation on a demand-supply diagram. Explain what you think has happened and comment on John's statement (is it correct, partially correct or completely incorrect). **Explain fully.**

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