

PRACTICE TEST

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

- 1) Toronto has a large number of retail stores that sell clothes. Each store has its own characteristics which differ from the other stores. The clothing business in Toronto is an example of
- A) a perfectly competitive market.
 - B) a monopolistically competitive market.
 - C) a monopoly.
 - D) a duopoly.
 - E) an oligopoly.

Use the figure below to answer the following questions.

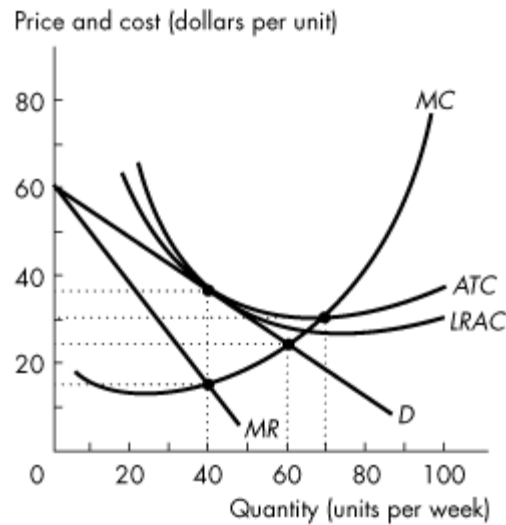


Figure 1

- 2) Refer to Figure 1. To maximize economic profit, this firm in monopolistic competition will charge a price of
- A) \$20 a unit.
 - B) \$15 a unit.
 - C) \$35 a unit.
 - D) \$25 a unit.
 - E) \$32 a unit.

- 3) Refer to Figure 1. To maximize economic profit, this firm in monopolistic competition produces an output
- A) of 40 units.
 - B) of less than 40 units.
 - C) of 60 units.
 - D) of 70 units.
 - E) that cannot be determined without information concerning rival firms.
- 4) If a firm spends \$600 on advertising, its
- A) *MC* curve shifts upward and its *ATC* curve does not shift.
 - B) *ATC* curve shifts upward and its *MC* curve does not shift.
 - C) *ATC* and *MC* curves shift upward.
 - D) *AFC* and *AVC* curves shift upward.
 - E) *ATC* curve shifts upward and its *MC* curve shifts downward.
- 5) Which is *not* a characteristic of oligopoly?
- A) Firms set prices.
 - B) Firms are profit-maximizers.
 - C) The sales of one firm will not have a significant effect on other firms.
 - D) Each firm faces a downward-sloping demand curve.
 - E) There is more than one firm in the industry.
- 6) In the dominant firm model of oligopoly, the dominant firm produces the quantity at which marginal revenue equals
- A) zero.
 - B) price.
 - C) average total cost.
 - D) total revenue.
 - E) marginal cost.

Refer to the table below to answer the following question.

Table 1

		Firm A	
		R&D	No R&D
Firm B	R&D	A: \$25 B: \$15	A: -\$3 B: \$60
	No R&D	A: \$60 B: -\$3	A: \$50 B: \$35

- 7) Refer to Table 1. Firms A and B can conduct research and development (R&D) or not conduct it. R&D is costly but can increase the quality of the product and increase sales. The payoff matrix is the economic profits of the two firms and is given above, where the numbers are millions of dollars. The Nash equilibrium occurs when
- A) both A and B conduct R&D.
 - B) only B conducts R&D.
 - C) only A conducts R&D.
 - D) neither A nor B conduct R&D.
 - E) there is no Nash equilibrium.

Refer to the table below to answer the following question.

Table 2

		Disney	
		Thanksgiving Release	Christmas Release
Fox	Thanksgiving Release	D: \$100 F: \$80	D: \$105 F: \$95
	Christmas Release	D: \$110 F: \$100	D: \$95 F: \$85

- 8) Refer to Table 2. Disney and Fox must decide when to release their next films. The revenues received by each studio depends in part on when the other studio releases its film. Each studio can release its film at Thanksgiving or at Christmas. The revenues received by each studio, in millions of dollars, are given in the payoff matrix above. Which of the following statements correctly describes Fox's strategy given what Disney's release choice may be?
- A) If Disney chooses a Thanksgiving release, Fox should choose a Christmas release.
 - B) If Disney chooses a Christmas release, Fox should choose a Thanksgiving release.
 - C) Fox should release on Christmas regardless of what Disney does.
 - D) Fox should release on Thanksgiving regardless of what Disney does.
 - E) Both answers A and B are correct.

Refer to the table below to answer the following question.

Table 3

		Student 1	
		Work	Don't work
Student 2	Work	1: +10 2: +10	1: +5 2: +5
	Don't Work	1: +5 2: +50	1: 0 2: 0

- 9) Refer to Table 3. Two students are assigned a group project. Each has the option to work or not work to achieve a high grade. The payoffs are shown in the above table. Student 1
- A) works regardless of the decision made by student 2.
 - B) does not work if student 2 works.
 - C) does not work regardless of what student 2 decides.
 - D) works only if student 2 does not work.
 - E) works only if student 2 works.

Use the figure below to answer the following question.

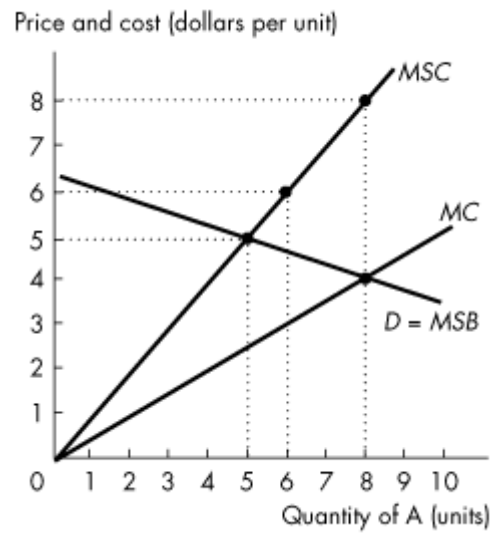


Figure 2

- 10) Refer to Figure 2. This figure shows the demand curve, the marginal private cost curve and the marginal social cost curve of good A. What is the efficient quantity of good A?
- A) 0 units
 - B) 5 units
 - C) 8 units
 - D) 6 units
 - E) impossible to determine without additional information

Use the figure below to answer the following question.

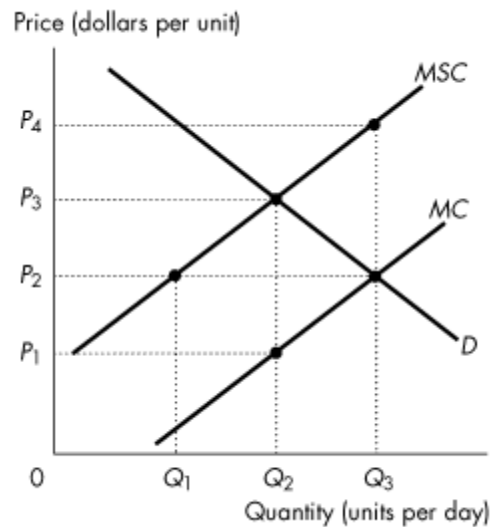


Figure 3

- 11) Refer to Figure 3. The figure shows the private marginal cost curve, the social marginal cost curve and the market demand curve. If a constant per unit tax is imposed that generates an efficient allocation of resources, then the quantity produced is
- A) Q_2 .
 - B) Q_3 .
 - C) greater than Q_3 .
 - D) Q_1 .
 - E) zero.
- 12) When the production of a good has an external cost, the
- A) marginal social benefit curve lies above the marginal private benefit curve.
 - B) equilibrium quantity in an unregulated, competitive market has a marginal social cost less than the marginal social benefit.
 - C) marginal social cost curve lies below the marginal private cost curve.
 - D) equilibrium quantity in an unregulated, competitive market has a marginal social cost greater than the marginal social benefit.
 - E) none of the above.

Use the figure below to answer the following questions.

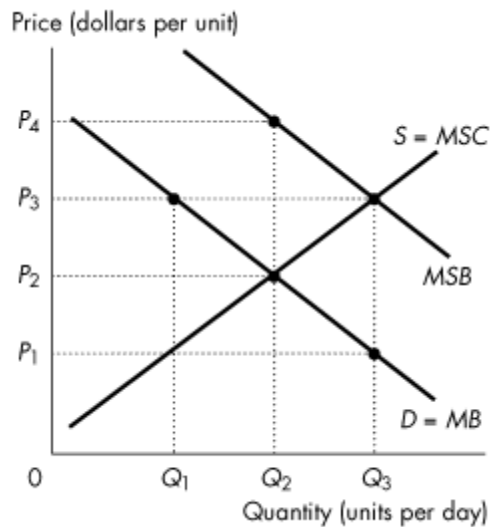


Figure 4

- 13) Refer to Figure 4. The figure shows the marginal private benefit curve, the marginal social benefit curve, and the market supply curve. If production is left to the private market, then the quantity produced is
- A) Q_3 .
 - B) Q_2 .
 - C) Q_1 .
 - D) zero.
 - E) between 0 and Q_1 .
- 14) Refer to Figure 4. The figure shows the marginal private benefit curve, the marginal social benefit curve, and the market supply curve. If a subsidy is granted that generates an efficient quantity, then quantity produced is
- A) Q_3 .
 - B) zero.
 - C) Q_1 .
 - D) Q_2 .
 - E) greater than Q_3 .
- 15) Private goods are
- A) always produced in a non-regulated market.
 - B) nonrival and excludable.
 - C) nonrival and nonexcludable.
 - D) rival and nonexcludable.
 - E) rival and excludable.

- 16) A natural monopoly is
- A) nonrival.
 - B) excludable.
 - C) rival.
 - D) nonexcludable.
 - E) both A and B.
- 17) When a city street is congested, it is
- A) a common resource.
 - B) a private good.
 - C) nonrival and nonexcludable.
 - D) nonrival and excludable.
 - E) a public good.
- 18) Suppose in a country there are only two persons. Person *A* is willing to pay \$50 to have one unit of a public good produced; person *B* is willing to pay \$60 to have one unit of a public good produced and \$50 to have two units produced. A point on the country's marginal social benefit curve for this public good is a price of _____ and quantity demanded of _____.
- A) \$60; 1 unit
 - B) \$110; 1 unit
 - C) \$50; 2 units
 - D) \$55; 1 unit
 - E) \$110; 2 units
- 19) The "tragedy of the commons" refers to
- A) the acceptance of deplorable working conditions by those who lack the human capital to obtain a better job.
 - B) the tendency for bureaucrats to maximize their budget.
 - C) the absence of incentives to prevent the overuse and depletion of a commonly used resource.
 - D) the inability of lower income groups to achieve a higher level of education.
 - E) farmers who allow their livestock to overgraze their fields.
- 20) The value of marginal product of labour is the revenue
- A) needed to cover the cost of producing an additional unit of output.
 - B) generated by selling an additional unit of output.
 - C) generated to cover the cost of hiring an extra unit of labour.
 - D) needed to hire an additional unit of labour.
 - E) generated by the employment of an additional unit of labour.

Use the table below to answer the following question.

Table 4

Labour (workers)	Output (units)
0	0
1	5
2	11
3	18
4	26
5	32
6	37
7	41
8	44
9	46
10	47

- 21) Refer to Table 4. If the firm can sell all the output it wants for the price of \$4 a unit, what is the profit-maximizing number of workers if the wage rate is \$12?
A) 10 B) 6 C) 8 D) 4 E) zero
- 22) A decrease in the price of factors of production that are substitutes for labour shifts the labour
A) demand curve rightward.
B) supply curve leftward.
C) demand curve leftward.
D) supply curve rightward.
E) B and D.
- 23) A decrease in the price of a firm's output
A) increases the supply of labour.
B) decreases the value of marginal product of labour.
C) decreases the quantity of labour demanded.
D) decreases the supply of labour.
E) increases the value of marginal product of labour.
- 24) As the wage rate rises, a household will have a backward-bending supply of labour curve if
A) the income effect dominates the substitution effect.
B) leisure is an inferior good.
C) the wage rate rises above the reservation wage.
D) the substitution effect dominates the income effect.
E) the income effect reinforces the substitution effect.

- 25) The Hotelling Principle states that
- A) we should conserve nonrenewable natural resources.
 - B) the resource will be depleted at a rate equal to the rate of interest.
 - C) natural resources should be depleted only for the production of goods that would help maintain environmental quality.
 - D) equilibrium in natural resource markets occurs when the expected increase in the price of the resource over time is equal to the interest rate.
 - E) hotels will tend to be built next to major highways.
- 26) The demand for capital is determined by _____. The demand for land is determined by _____. The supply of _____ is perfectly _____.
- A) how much capital is renewable and how much is nonrenewable; how much land is renewable and how much is nonrenewable; capital; elastic
 - B) the value of marginal product of capital; the value of marginal product of land; land; elastic
 - C) the value of marginal product of capital; the value of marginal product of land; land; inelastic
 - D) how much capital is renewable and how much is nonrenewable; how much land is renewable and how much is nonrenewable; land; elastic
 - E) the value of marginal product of capital; the value of marginal product of land; capital; inelastic
- 27) All of the following statements are correct *except*
- A) profit-maximizing firms hire the quantity of capital services that makes the value of marginal product of capital equal to the rental rate of capital.
 - B) if the present value of the future rental payments of an item of capital equipment is less than the cost of buying the capital, the firm will rent or lease the equipment.
 - C) the supply of capital is derived from the value of marginal product of capital.
 - D) the lower the rental rate of capital, other things remaining the same, the greater is the quantity of capital demanded.
 - E) the higher the rental rate, other things remaining the same, the greater is the quantity of capital supplied.

Use the information below to answer the following question.

Fact 1

The Burning Belly Taco Stand is considering buying some new special ovens. Each oven will cost \$1,000, and will last for 2 years before it wears out. The ovens will be used to make the Taco Stand's famous "Burning Ring of Fire" tacos, and will generate a value of marginal product of \$600 for the first oven, \$570 for the second oven, and \$530 for the third oven. (Assume all revenues are earned at the end of the year.)

- 28) Refer to Fact 1. If the rate of interest is 5 percent, how many ovens will the Burning Belly Taco Stand buy?
- A) 1
 - B) zero
 - C) 3
 - D) 2
 - E) insufficient information to answer

Use the figure below to answer the following questions.

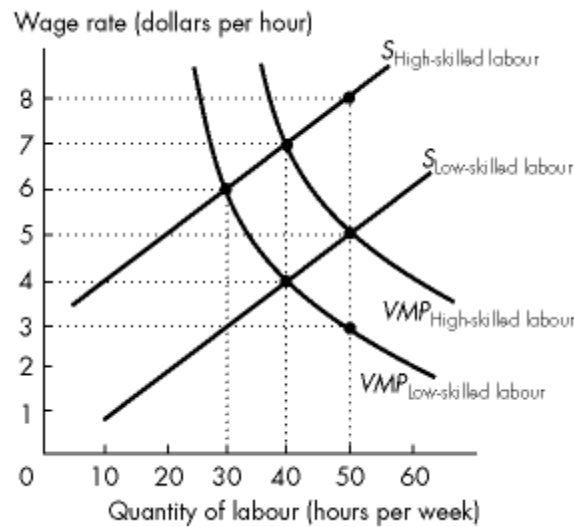


Figure 5

- 29) Refer to Figure 5. This figure shows the labour supply curves and the value of marginal product curves for high-skilled and low-skilled workers. If the labour markets are competitive, then for a 40-hour work week, high-skilled workers must be paid
- A) an extra \$300 to compensate for the cost of acquiring their human capital and for their enhanced productivity.
 - B) an extra \$120 to compensate for the cost of acquiring their human capital and for their increased productivity.
 - C) an extra \$180 to compensate for the cost of acquiring their human capital and for their increased productivity.
 - D) an extra \$3 to compensate for the cost of acquiring their human capital and for their increased productivity.
 - E) an extra \$20 to compensate for the cost of acquiring their human capital and for their increased productivity.
- 30) Refer to Figure 5. This figure shows the labour supply curves and the value of marginal product curves for high-skilled and low-skilled workers. If there is an increase in the supply of high-skilled workers and the supply of high-skilled workers is now equal to the supply of low-skilled workers, then
- A) wages paid to high-skilled workers would fall to \$5 an hour.
 - B) wages paid to high-skilled workers would fall to \$6 an hour.
 - C) there would be no change in the wages of high-skilled workers, because their value of marginal product is unchanged.
 - D) there would be no change in the wages of high-skilled workers, because high-skilled workers always earn more than low-skilled workers.
 - E) wages paid to high-skilled workers would fall to \$4 an hour.

Answer Key

Testname: 1021A003_PRACTICE_TEST_DEC11

- 1) B
- 2) C
- 3) A
- 4) B
- 5) C
- 6) E
- 7) A
- 8) E
- 9) A
- 10) B
- 11) A
- 12) D
- 13) B
- 14) A
- 15) E
- 16) E
- 17) A
- 18) B
- 19) C
- 20) E
- 21) C
- 22) C
- 23) B
- 24) A
- 25) D
- 26) C
- 27) C
- 28) D
- 29) B
- 30) A