

Your name and honor code pledge:

Economics 101
Professor Joyce Jacobsen
Spring Semester 2005-06
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Test #1

Points for each section are shown out of 100 points. Each subsection is weighted equally.

A. (20 pts) Answer True, False, or Uncertain, and briefly explain your answer.

(1) A subsidy on milk production will lower the price of milk and reduce the quantity of milk produced.

(2) If bacon and eggs are complements, a leftward shift in the supply curve for eggs causes an increase in the equilibrium price of bacon and a decrease in the equilibrium quantity of bacon.

(3) If total fixed cost is greater than zero, average fixed cost always slopes downward.

(4) If a price ceiling is imposed on a market, it will cause a higher price and a shortage.

B. (20 pts) Short answers.

(1) Give an example of a monopolistically competitive industry and explain why you think it fits the necessary conditions.

(2) What should a firm do if it finds that at its current production point, $\frac{MPL}{PL} > \frac{MPK}{PK}$?

(3) Give two examples of barriers to entry that could lead to a monopoly in an industry.

(4) Give an example of third degree price discrimination.

C. (20 pts) Circle one answer for each question.

(1) What has happened in the market for milk if both price and quantity have gone down?

- a. demand has shifted leftward
- b. demand has shifted rightward
- c. supply has shifted leftward
- d. supply has shifted rightward

(2) What is the short-run shutdown condition for the firm?

- a. price is less than average total cost
- b. price is less than average variable cost
- c. price is less than average fixed cost
- d. price is less than marginal cost

(3) If I decrease my consumption of beer when my income rises, then I consider beer to be:

- a. a normal good
- b. an inferior good
- c. an ordinary good
- d. a luxury good

(4) Which one of the following statements about isoquants is false?

- a. they cannot cross
- b. they have negative slope
- c. fewer inputs produce more output
- d. balanced inputs are better than unbalanced inputs

(5) What is the current U.S. Federal minimum wage?

- a. \$5.15
- b. \$5.75
- c. \$6.25
- d. \$7.15

D. (20 pts) Draw graphs neatly and label axes and points clearly. Please show any calculations used to arrive at your answers. Round answers to the first decimal place if necessary.

(1) Nat gets a weekly check of \$60. He spends all his money each week and only ever buys two things: books and DVDs. If books cost \$10 each and DVDs cost \$15 each, draw his weekly budget constraint.

(2) Show on the same graph the new budget constraint for when books go on sale for \$5 each.

(3) Now show the budget constraint (using the new price for books) for when Nat gets a bigger check of \$90.

(4) If Nat considers books and DVDs to be perfect substitutes, mark his preferred consumption point on each of the three budget constraints.

E. (20 pts) Draw graphs neatly and label axes and points clearly. Please show any calculations used to arrive at your answers. Round answers to the first decimal place if necessary.

Fearful of foreign competition's effects on the domestic lava lamp industry, Lord Lava of Lampoon is thinking of imposing a quota in the foreign-made lava lamp market. The supply schedule and demand schedule for this market are:

<u>Demand</u>		<u>Supply</u>	
<u>Price</u>	<u>Quantity</u>	<u>Price</u>	<u>Quantity</u>
\$9.00	600	\$6.00	300
\$8.00	800	\$7.00	600
\$7.00	1000	\$8.00	800
\$6.00	1200	\$9.00	1200

(1) Graph the supply and demand curves and indicate the equilibrium point.

(2) Show on the graph what happens when a quota of 600 units is imposed on this market.

(3) Calculate the (arc) price elasticity of demand when the price rises from \$7 to \$8.

(4) What will happen in the domestic-made lava lamp market as a result of this quota?