

Brigham Young University Department of Economics
Economics 110 – Principles of Economics
Professor Kerk Phillips – Spring Term 2009, section 1

Midterm #2 key

5/28 (Thu) – 5/29 (Fri) Testing Center

This test is multiple choice, fill in your answers on the answer sheet and do not write on this exam. It is closed book and closed notes. There is no time limit and you may use calculators; either those provided by the testing center or your own as long as it is not a programmable calculator. Read all questions carefully before answering.

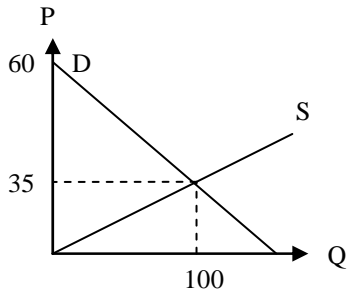
1. A decrease in the sales tax on gasoline would lead to a ___ in the total price paid by motorists, and a ___ in the net price received by gas stations.
 - a) decrease, decrease
 - b) increase, decrease
 - c) decrease, increase**
 - d) increase, increase
 - e) none of the above

2. A binding price floor causes...
 - a) a shortage of the good
 - b) a surplus of the good**
 - c) an equilibrium allocation where supply equals demand
 - d) sometimes a shortage and sometimes a surplus
 - e) none of the above

3. A real world example of a binding price ceiling is...
 - a) the US sugar import quota
 - b) price supports for agricultural products
 - c) minimum wage laws
 - d) all of the above
 - e) none of the above**

4. If the elasticity of supply is less than the elasticity of demand, then the burden of the tax ...
 - a) falls more heavily on consumers than producers
 - b) falls more heavily on producers than consumers**
 - c) falls equally on consumers and producers
 - d) is almost zero
 - e) none of the above

Use the following figure to answer questions 5 & 6. The supply and demand curves are straight lines. Prices are in dollars.



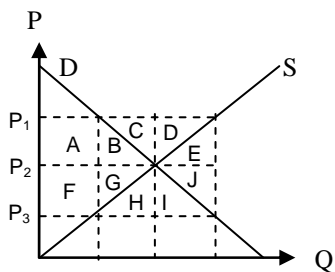
5. The amount of consumer surplus is:

- a) \$3500
- b) \$2500
- c) \$1750
- d) \$1250**
- e) none of the above.

6. The amount of producer surplus is:

- a) \$3500
- b) \$2500
- c) \$1750**
- d) \$1250
- e) none of the above.

Use the following figure to answer questions 7 – 10. This figure illustrates the imposition of a tax. The block letters are labeling sizes of areas (triangles or trapezoids).

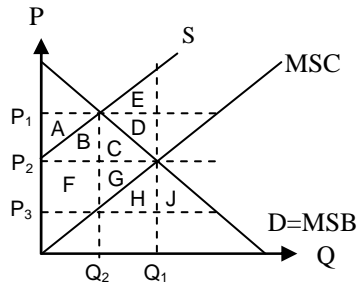


7. The price received by producers before the tax is imposed is...

- a) P_1
- b) P_2**
- c) P_3
- d) zero
- e) none of the above

8. The change in consumer surplus is...
- a) **-(A+B)**
 - b) -(A+B+C+D)
 - c) -(F+G)
 - d) -(F+G+H+I)
 - e) none of the above
9. The change in producer surplus is...
- a) -(A+B)
 - b) -(A+B+C+D)
 - c) **-(F+G)**
 - d) -(F+G+H+I)
 - e) none of the above
10. The net loss to society or deadweight loss (ignoring the minus sign) is...
- a) (C+D)
 - b) **(B+G)**
 - c) (E+J)
 - d) (H+I)
 - e) none of the above
11. A socially efficient policy in the face of a positive production externality is...
- a) **to subsidize production of the good**
 - b) to tax production of the good
 - c) to tax consumption of the good
 - d) to ban any production of the good
 - e) none of the above
12. Consider the case of the owner of a cattle yard. The Coase Theorem suggests that the negative externality associated with the bad smell the yard generates can be efficiently addressed by...
- a) taxing the consumers of beef
 - b) giving the cattle yard owner the right to emit odors and allowing the homeowners to pay whatever it takes for him to shut down or relocate
 - c) giving the neighbors the right to smell-free air and allowing the cattle yard owner to pay whatever it takes for them to let him stay in business
 - d) **both b) and c)**
 - e) none of the above is remotely related to the Coase Theorem

Use the following figure to answer questions 13 – 16. MSB stands for “marginal social benefit” and MSC stands for “marginal social cost”.



13. The figure above can best be described as illustrating...
- A positive consumption externality
 - A negative consumption externality
 - A positive production externality**
 - A negative production externality
 - none of the above
14. The socially optimal quantity in this case is an amount...
- less than Q_2
 - exactly equal to Q_2
 - greater than Q_2 but less than Q_1
 - exactly equal to Q_1**
 - greater than Q_1
15. The socially optimal allocation is arrived at by imposing...
- a subsidy of size $(P_1 - P_3)$**
 - a tax of size $(P_1 - P_3)$
 - a subsidy of size $(P_1 - P_2)$
 - a tax of size $(P_2 - P_3)$
 - none of the above
16. The gain to third parties (neither buyers nor sellers) associated with moving from the market allocation to the socially optimal one is...
- $+(D+E)$
 - $+(C+G)$
 - $+(C+D+E+G)$**
 - $+(C+D+G+H)$
 - none of the above

Use the following information for questions 17 – 18. Assume zero fixed costs.

Demand Curve		Firms'
Q	P	Total Cost
1	\$10	4
2	\$9	8
3	\$8	12
4	\$7	16
5	\$6	20
6	\$5	24
7	\$4	28
8	\$3	32
9	\$2	36
10	\$1	40

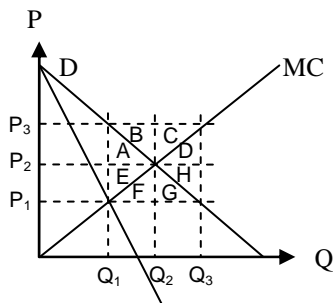
17. With perfect competition the market price is ____ and the quantity produced and consumed is ____.

- a) \$7, 4 units
- b) \$6, 5 units
- c) \$5, 6 units
- d) \$4, 7 units**
- e) none of the above

18. With a monopoly the market price is ____ and the quantity produced and consumed is ____.

- a) \$7, 4 units**
- b) \$6, 5 units
- c) \$5, 6 units
- d) \$4, 7 units
- e) none of the above

Use the following figure to answer questions 19 – 21.



19. The monopolist charges a price of...

- a) P₃**
- b) P₂
- c) P₁
- d) zero
- e) none of the above

20. The monopolist produces quantity ...
- a) Q_3
 - b) Q_2
 - c) **Q_1**
 - d) zero
 - e) none of the above
21. The inefficiency associated with monopoly gives a deadweight loss (again ignoring the negative sign) equal to...
- a) (B+C)
 - b) **(A+E)**
 - c) (D+H)
 - d) (F+G)
 - e) none of the above

Use the following answers for questions 22 – 25

- a) Increasing returns to scale due to a large fixed cost have lead to a natural monopoly which has lower costs than any potential competitor would have when it started up operating on a smaller scale.
 - b) The government has put barriers in place that do not allow potential competitors to enter the market.
 - c) The firm owns a unique and scarce resource that no potential competitor can replicate.
 - d) More than one of the above reasons is an important cause
 - e) None of the above reasons are relevant
22. Why does Alcoa have a virtual monopoly on new aluminum sales? **C**
23. Why does Provo Power have a monopoly on electricity in the City of Provo? **B or D**
24. Why did the Medellin Cartel have a monopoly on cocaine during it's heyday? **C or D or E**
25. Why does the US Postal Service have a monopoly on delivery of letters? **B**
26. A market structure with a large number of producers all producing the same good is called...
- a) monopoly
 - b) oligopoly
 - c) monopolistic competition
 - d) **perfect competition**
 - e) none of the above

27. A market structure where producers must take into account the actions of their competitors when making their own production decision is ...
- a) monopoly
 - b) oligopoly**
 - c) monopolistic competition
 - d) perfect competition
 - e) none of the above
28. A market structure where firms compete by introducing different varieties of a good is ...
- a) monopoly
 - b) oligopoly
 - c) monopolistic competition**
 - d) perfect competition
 - e) none of the above
29. A market structure with a large number of producers, but a small number of consumers is called...
- a) monopoly
 - b) oligopoly
 - c) monopolistic competition
 - d) perfect competition
 - e) none of the above, monopsony**
30. Which statement below is true?
- a) Perfect price discrimination leads to better social welfare than perfect competition.
 - b) Monopolies will never make losses
 - c) Cartels with large numbers of members are easier to enforce than those with small numbers.
 - d) More than one of the above statements is true.
 - e) None of the above statements is true.**