EC101 DD/EE F14 Practice Midterm 2

INSTRUCTIONS (***Read Carefully***):

**ON YOUR QUESTION BOOKLET:**
Fill in your name, Student ID, Discussion Section Number (e.g. D5) and your signature.

**ON YOUR SCANTRON:**
Enter the Course Number (EC101 DD or EE) and date on the lines at the top-left. In the boxes below, enter your Student ID, your DISCUSSION SECTION number (D1 - D9, E0 - E9), your NAME and your EXAM VERSION into the Scantron computer sheet. Be sure that you “bubble” all entries. I will subtract up to 5 points as punishment for errors in these data!

**DURING THE EXAM:**
Students who wish to leave the room for any reason must leave the Question Booklet and Scantron sheet with the instructor or teaching fellow. Students in EC101DD MUST turn in both the Question Booklet and the Scantron sheet at the end of the exam and exit from the front of the room. Students in EC101EE should keep their Question Booklet and turn in only their Scantrons. All students must show their BU Student IDs as they leave the exam room.

**MULTIPLE-CHOICE QUESTIONS:**
Choose the BEST answer for each of the multiple-choice questions. (Only ONE answer is allowed, even when more than one of the answers is technically correct.) On the Question Booklet, CIRCLE the letter that you chose, so that you have a record of your answers. Then BUBBLE it on the Scantron sheet for grading.

Never cross out an answer on your Scantron. Use a pencil to bubble your answers, and keep a good eraser with you. If you bubble the wrong answer on the Scantron, erase your mark COMPLETELY, and then bubble the correct answer.

***YOU MAY NOT USE A CALCULATOR, CELL PHONE OR LAPTOP.***

***However, INTERNATIONAL STUDENTS may use electronic translators or dictionaries.***

You have 60 minutes to complete the exam. Good luck!

DO NOT OPEN THIS BOOKLET OR TURN IT OVER
[until told to do so]
1. If students are economically rational and discussion sections create no externalities, then Manove’s policy of requiring attendance in discussion sections would
   a. decrease surplus by forcing students to attend even when they have better things to do.
   b. have no effect on total surplus from discussion sections.
   c. increase total surplus by increasing learning opportunities.
   d. None of the above

2. Which is a likely outcome inside the United States of an increase in the importation of manufactured goods?
   a. Unemployment in the industrial sector.
   b. Some manufacturing firms go out of business.
   c. Producers of manufactured products lose surplus.
   d. All of the above

3. Suppose the equilibrium price of baguettes (bread) in France is €2, but the French government puts a price ceiling of €1 on the baguette. An important reason why this is inefficient may be that
   a. consumers who obtain the baguettes may value them less than those who do not.
   b. the price ceiling causes the wholesale price of baguettes to rise.
   c. too many baguettes will be produced.
   d. some surplus will be transferred from producers to consumers.

4. For competitive firms without fixed costs, an increasing marginal cost curve is the same as the
   a. demand curve.
   b. production-possibility curve.
   c. supply curve.
   d. None of the above

5. To internalize a positive externality, an appropriate government policy would be to
   a. ban the good that creates the externality.
   b. subsidize the good.
   c. tax the good.
   d. produce the good until the value of an additional unit is zero.

6. Willingness to pay may not measure a consumer’s benefit from a product accurately, because the consumer
   a. may not know his own preferences.
   b. may have an elastic demand.
   c. may wish to spend his money on other things.
   d. does not find the product sufficiently expensive.

7. Suppose the US has comparative advantage in the production of computers with respect to Canada. As a result of free international trade, the US exports computers to Canada. What is the most likely outcome?
   a. US consumers of computers are better off.
   b. Everyone in both countries is better off.
   c. Canadian consumers of computers are better off.
   d. Producer surplus in the US increases, and consumer surplus in the US decreases.

8. See Figure WPE. Emily’s total willingness to pay for 4 plums is about $_____. [Choose the closest value.]
   a. 8
   b. 32
   c. 0
   d. 41

9. See Figure WPE. At a price of $3, how many plums will Emily demand?
   a. 10
   b. 0
   c. 6
   d. 5

10. See Figure WPE. If the price is $8, Emily’s consumer surplus will be about $_____. [Choose the closest value.]
    a. 9
    b. 32
    c. 0
    d. 41
11. See Figure BMC. If the price of cakes is $4, the bakery will obtain about $_____ of producer surplus. [Choose the closest value.]
   a. 8.50  
   b. 4.00  
   c. 0.00  
   d. 20.00
12. See Figure BMC. How many cakes will the bakery produce when the price of cakes is $10?
   a. 7  
   b. 8  
   c. 10  
   d. more information needed
13. See Figure BMC. The variable cost of producing 5 cakes is about $_____.
    [Choose the closest value.]
   a. 5.00  
   b. 20.00  
   c. 11.50  
   d. more than 100.00
14. Maximizing social surplus may be a bad idea, because
   a. surplus may be distributed unfairly.  
   b. there is often too much surplus.  
   c. surplus is not related to willingness to pay.  
   d. surplus maximization is inefficient.
15. If a product creates a negative externality, then
   a. the social cost of production is lower than the marginal cost.  
   b. the marginal benefit of an additional unit of production is increased.  
   c. the free-market equilibrium quantity is the efficient one.  
   d. the free-market equilibrium output of the product is greater than the efficient level.
16. Charlie buys sneakers for $80, but after he wears them for a day, he decides that they are not comfortable. Unfortunately the store will not refund his money, so Charlie goes to a different store and buys better sneakers for $90. The opportunity cost of the new sneakers is
   a. $10.  
   b. $170.  
   c. $90.  
   d. NONE of the above
17. US politicians don’t like high gasoline taxes, because
   a. gasoline taxes are unpopular.  
   b. gasoline taxes are low in Europe.  
   c. gasoline taxes reduce economic efficiency.  
   d. ALL of the above
18. Economic analysis suggests that the government should
   a. prohibit activities that cause pollution.  
   b. use taxes to discourage activities that cause pollution.  
   c. require polluters to install equipment that prevents pollution.  
   d. not interfere with markets for pollution-causing products.
19. Removing rent controls is NOT likely to
   a. yield a Pareto improvement.  
   b. increase social surplus.  
   c. improve the quality of rented apartments.  
   d. reduce the bribery of landlords.
20. Trade raises the economic well-being of a nation in the sense that
   a. exported goods yield more revenue than imports cost.  
   b. the gains of the winners exceed the losses of the losers.  
   c. everyone in an economy gains from trade.  
   d. the nation joins the international community when it begins to engage in trade.
21. According to the Coase theorem, private markets will solve externality problems and allocate resources efficiently as long as
   a. the externalities that are present are positive, not negative.  
   b. businesses determine an appropriate level of production.  
   c. government assigns property rights to the harmed party.  
   d. private parties can bargain with sufficiently low transaction costs.
22. Gangsters are in charge of the cocaine business, because
   a. gangsters have a comparative advantage in operating illegal activities.
   b. profits in the cocaine business are insufficient to attract ordinary business executives.
   c. most business people find the cocaine business to be immoral.
   d. in countries where cocaine is produced, most business executives are gangsters.

23. A consumer is willing to pay $11 for his first beer, $7 for his second beer, $4 for his third beer, $2 for his fourth beer, and $1 for his fifth beer. If the price is $2, his total consumer surplus is:
   a. $22.
   b. $18.
   c. $16.
   d. $20.

24. Jane decides to open her own business and earns $50,000 in accounting profit the first year. When deciding to open her own business, she turned down three separate full-time job offers with annual salaries of $30,000, $40,000, and $45,000. What is Jane's economic profit from running her own business?
   a. $-5,000
   b. $20,000
   c. $-65,000
   d. $5,000

25. For a construction company that builds houses, which of the following costs would be a fixed cost?
   a. the $30,000 per year salary paid to the company's bookkeeper
   b. the $10,000 per year premium paid to an insurance company
   c. the $50,000 per year salary paid to their construction supervisor
   d. **ALL** of the above are correct.

26. Suppose an excise tax is placed on goods in a perfectly competitive market. If firms have no fixed costs and increasing marginal costs, then
   a. the consumer’s WTP is greater than the firm’s MC for every good sold.
   b. consumers who buy the good have a higher WTP than those who do not.
   c. firms that produce the good have a lower MC than those that do not.
   d. **ALL** of the above

27. Which of the following statements is **not** correct about a market in equilibrium?
   a. Those sellers whose costs are less than the price choose to produce and sell the good.
   b. Those buyers who value the good more than the price choose to buy the good.
   c. Consumer surplus will be equal to producer surplus.
   d. The price determines which buyers and which sellers participate in the market.

28. Tom has $5. He wants to drink a bottle of soda, and he is willing to pay $3 for one. Anna produces soda at a marginal cost of $4 per bottle. Then Tom would
   a. maximize social surplus by doing nothing.
   b. create a Pareto improvement over the existing situation by buying soda from Anna.
   c. maximize social surplus by buying soda from Anna for $4.
   d. minimize social surplus by doing nothing.

29. David can work as many hours as he wants. If he is economically rational and his wage rate increases, then
   a. he will work more.
   b. he will consider leisure to be more expensive.
   c. he will work less.
   d. he will work the same number of hours as before.

30. When firms have an incentive to exit a competitive market, their exit will
   a. necessarily raise the costs of firms that remain in the market.
   b. lower market price.
   c. reduce demand for the product.
   d. raise profits for firms that remain in the market.

31. In market economies, goods are usually consumed by
   a. those who are willing to pay the most for them.
   b. those who work the hardest.
   c. those who are most deserving.
   d. those who are politically well connected.

32. The particular price that results in quantity supplied being equal to quantity demanded is the best price because it
   a. minimizes the expenditure of buyers.
   b. minimizes costs of the seller.
   c. maximizes tax revenue.
   d. maximizes the combined welfare of buyers and sellers.
Figure PEX. The graph below shows the supply, demand and social value of trinkets.

33. See Figure PEX. The graph indicates that trinkets
   a. have a positive externality.
   b. have a negative externality.
   c. have no externality.
   d. CANNOT be determined from the graph

34. See Figure PEX. The socially optimal output of trinkets is
   a. 280.
   b. 0.
   c. 160.
   d. CANNOT be determined from the graph

35. See Figure PEX. To maximize social surplus, the government should
   a. pay a subsidy of $12 per trinket.
   b. pay a subsidy of $18 per trinket.
   c. impose a tax of $12 per trinket.
   d. impose a tax of $18 per trinket.

36. Suppose the market price of a calculator is $20. If you are the CEO of a calculator company with no fixed costs and a rising marginal cost, how many calculators would you produce?
   a. maximum possible output with a total cost of production less than the total revenue
   b. as many as can be produced
   c. all the calculators whose marginal cost is less than $20
   d. more information is needed

Figure CPS. The US Textile Market Suppose $S$ represents the market supply curve of domestic producers. After imports are allowed, foreign producers shift the market supply to $S'$. $D$ is market demand.

37. See Figure CPS. Before the foreign producers enter, the producer surplus of domestic producers in the US market is ________.
   a. $100
   b. $400
   c. $50
   d. $225

38. See Figure CPS. After the foreign producers enter, total producer surplus of both domestic and foreign producers in the US market is ________.
   a. $400
   b. $50
   c. $225
   d. $100

39. See Figure CPS. The positions of the supply curves $S$ and $S'$ imply that some of the foreign firms ______ any of the domestic firms.
   a. are less competitive
   b. are larger
   c. have lower costs
   d. charge higher prices

40. See Figure CPS. After the foreign producers enter, the producer surplus of domestic producers
   a. decreases by $25.
   b. decreases by $75.
   c. increases by $75.
   d. increases by $25.
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Answer Section

MULTIPLE CHOICE

1. ANS: A    REF: P1
2. ANS: D    REF: P2
3. ANS: A    REF: P3
4. ANS: C    REF: P4
5. ANS: B    REF: P5
6. ANS: A    REF: P6
7. ANS: D    REF: P7
8. ANS: D    REF: P8
9. ANS: D    REF: P9
10. ANS: A   REF: P10
11. ANS: A   REF: P11
12. ANS: A   REF: P12
13. ANS: C   REF: P13
14. ANS: A   REF: P14
15. ANS: D   REF: P15
16. ANS: C   REF: P16
17. ANS: A   REF: P17
18. ANS: B   REF: P18
19. ANS: A   REF: P19
20. ANS: B   REF: P20
21. ANS: D   REF: P21
22. ANS: A   REF: P22
23. ANS: C   REF: P23
24. ANS: D   REF: P24
25. ANS: D   REF: P25
26. ANS: D   REF: P26
27. ANS: C   REF: P27
28. ANS: A   REF: P28
29. ANS: B   REF: P29
30. ANS: D   REF: P30
31. ANS: A   REF: P31
32. ANS: D   REF: P32
33. ANS: A   REF: P33
34. ANS: A   REF: P34
35. ANS: B   REF: P35
36. ANS: C   REF: P36
37. ANS: A   REF: P37
38. ANS: C   REF: P38
39. ANS: C   REF: P39
40. ANS: B   REF: P40