

Winter 2015 Exam 2

Version #1

1. A negative externality in production occurs, when:
 - A. social damage costs on consumers are positive.
 - B. social benefits are less than private benefits.
 - C. the social costs of production are greater than the private costs of production.
 - D. the social benefits of production are less than the private benefits of production.

2. At prices below a consumer's maximum willingness to pay:
 - A. the buyer will not participate in the market because the opportunity cost is more than the benefit from having the good.
 - B. the buyer will not participate in the market because the opportunity cost is less than the benefit from having the good.
 - C. the buyer will participate in the market because the opportunity cost is less than the benefit from having the good.
 - D. the buyer will participate in the market because the opportunity cost is more than the benefit from having the good.

3. In general, price controls have a:
 - A. larger effect in the short run since demand and supply become more elastic over time.
 - B. larger effect in the long run because demand and supply become more elastic over time.
 - C. smaller effect in the long run since demand and supply become less elastic over time.
 - D. smaller effect in the short run because demand and supply become less elastic over time.

4. If the government's provision of a subsidy is too small to counteract the entire effect of a positive externality, the:
 - A. total surplus will not be maximized, but the outcome will be efficient.
 - B. quantity consumed will still be too high.
 - C. total surplus will be maximized, but the outcome will be inefficient.
 - D. quantity consumed will still be too low.

5. External benefits are those that accrue:
 - A. directly to the decision maker of a market exchange.
 - B. indirectly to the decision maker of a market exchange.
 - C. to the government without its direct intervention.
 - D. without compensation to someone other than the person who caused it.

6. All of the following are examples of externalities EXCEPT

- A. heat from a factory that makes the neighbouring tomato patches more productive.
- B. carbon dioxide from energy generation that adds to the worldwide, long-term greenhouse effect.
- C. a chemical plant that pollutes the air in your community.
- D. acidic smoke that produces acid rain.
- E. a defective part that causes an automobile to break down three months after purchase.

7. When a market is efficient,

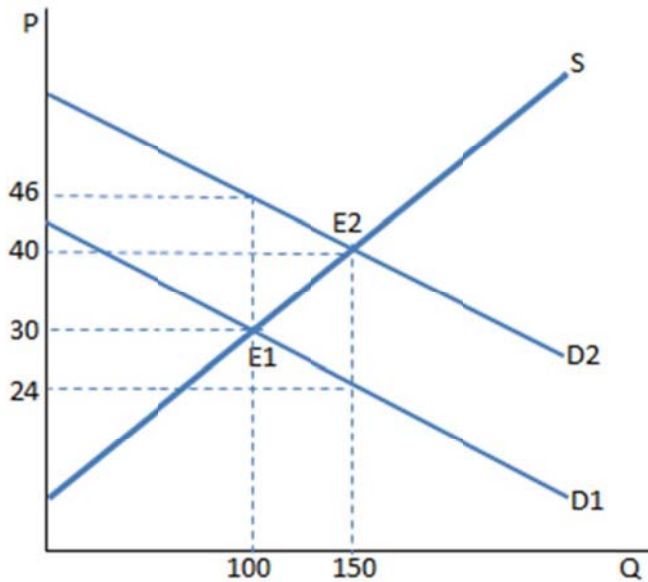
- A. a central planner must be involved.
- B. None of these is true.
- C. there is no exchange that can make anyone better off without someone becoming worse off.
- D. only increased prices can benefit those involved.

8. An effective price ceiling will cause:

- A. quantity supplied to increase.
- B. total economic surplus to rise.
- C. quantity supplied to exceed quantity demanded.
- D. producer surplus to fall.

9. If Thelma's willingness to sell her homemade fudge is \$4, then at which of the following prices would Thelma sell her fudge?

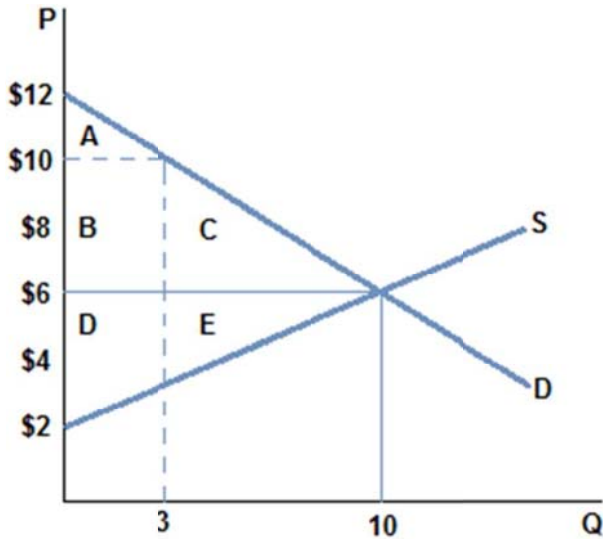
- A. \$4.01
- B. \$3.99
- C. Thelma would not sell her fudge at any of these prices.
- D. \$2



10.

The graph shown portrays a subsidy to buyers. Once the subsidy is in place, the buyers pay _____ and the sellers receive _____; the difference is _____.

- A. \$24; \$40; the amount of government revenue
- B. \$30; \$46; the amount of the subsidy
- C. \$24; \$40; the amount of the subsidy
- D. \$40; \$24; the amount of the subsidy



11.

According to the graph shown, if the market goes from equilibrium to having its price set at \$10 then:

- A. all producer surplus lost is gained by consumers.
- B. all consumer surplus lost is gained by producers.
- C. \$12 gets transferred from producer to consumer in surplus.
- D. \$12 gets transferred from consumer to producer in surplus.

12. A tax of \$1 on each unit a producer sells will:

- A. shift supply to the right.
- B. decrease quantity supplied.
- C. shift supply to the left.
- D. increase quantity supplied.

13. Price floors are:

- A. a legal minimum quantity that can be sold at a particular price.
- B. a legal minimum price.
- C. a legal maximum price.
- D. a legal maximum quantity that can be sold at a particular price.

14. It does not make economic sense to strive for a completely pollution- free environment because:

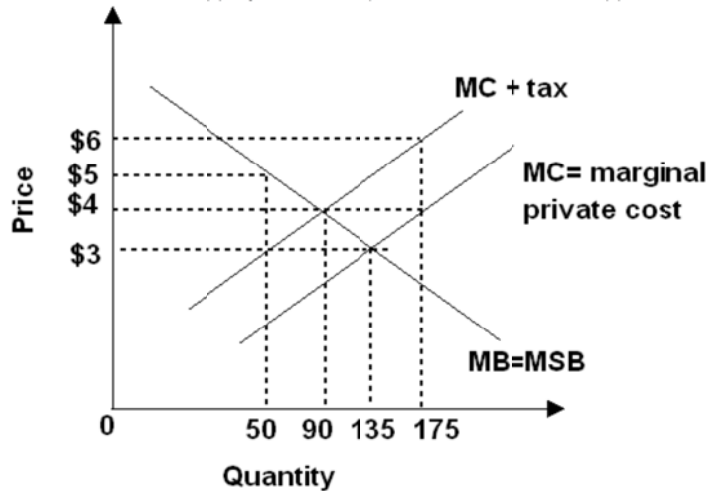
- A. the cost incurred would be greater than the benefit received.
- B. the marginal social benefit would be greater than the marginal social cost.
- C. the total benefit received by society would be greater than the total cost incurred.
- D. society does not want a pollution-free environment.

15. NO QUESTION HERE

16. The government is deciding where to place a tax of \$0.50 because they want to raise revenues. In which market will they likely generate more revenue?

- A. In markets with elastic supply and demand, since the increase in quantity traded will be smaller than in a market with inelastic supply and demand curves
- B. In markets with inelastic supply and demand, since the decrease in quantity traded will be smaller than in a market with elastic supply and demand curves
- C. In markets with elastic supply and demand, since the decrease in quantity traded will be smaller than in a market with inelastic supply and demand curves
- D. In markets with inelastic supply and demand, since the increase in quantity traded will be smaller than in a market with elastic supply and demand curves

17. Refer to the graph below, where MB is marginal benefit and MSB is marginal social benefit.



Assuming there is a marginal external cost equal to the tax shown in the graph, the per-unit tax necessary to induce consumers to purchase the efficient quantity each year is

- A. \$2.
- B. \$3.
- C. \$5.
- D. \$1.
- E. \$4.

18. Is it possible for sellers to benefit more than consumers from a subsidy to buyers?

- A. Yes, if the sellers need it more.
- B. Producers can never benefit more than buyers from a subsidy to buyers.
- C. Yes, if the supply curve is relatively more inelastic than the demand curve.
- D. Yes, if the supply curve is relatively less inelastic than the demand curve.

19. A positive externality in good X exists when:

- A. the marginal social benefit of consuming an extra unit of good X is less than the marginal private benefit of consuming an extra unit of good X.
- B. the marginal social benefit of consuming an extra unit of good X is greater than the marginal private benefit of consuming an extra unit of good X.
- C. no one can be made better off without making someone else worse off.
- D. the marginal social benefit of consuming an extra unit of good X equals the marginal private benefit of consuming an extra unit of good X.

20. If a per unit tax is imposed, the more elastic demand is,

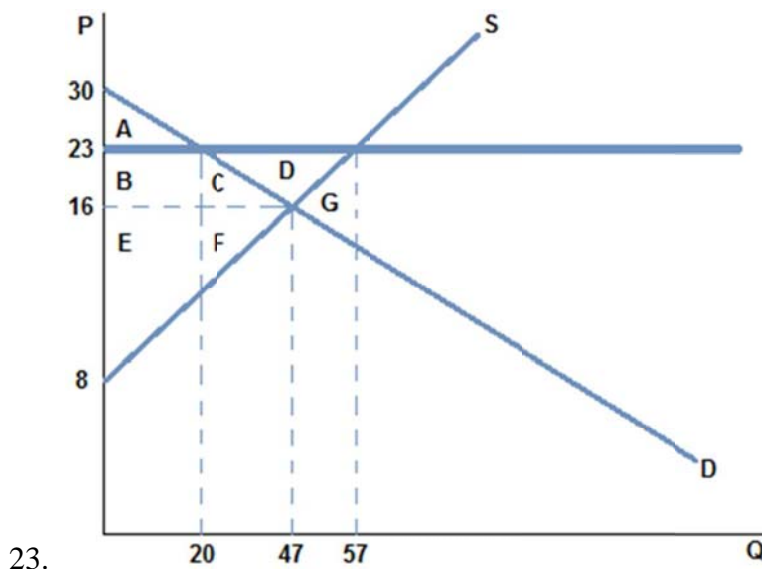
- A. less likely the deadweight loss will be affected.
- B. larger the loss in consumer surplus.
- C. smaller the deadweight loss.
- D. larger the deadweight loss.

21. In a free market, goods with negative externalities will:

- A. have the marginal valuation of the externality reflected in their price.
- B. be overproduced at the market equilibrium.
- C. be under-produced in the market place.
- D. be produced to the point at which the marginal social benefit equals the marginal social cost of the last unit produced.

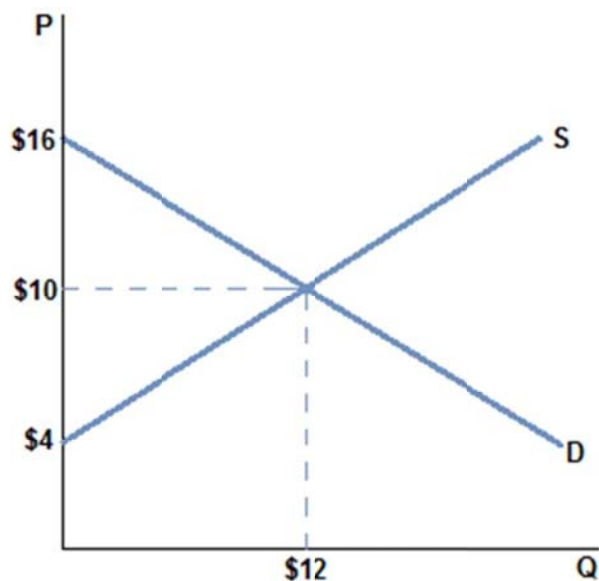
22. Suppose that Veronica is prepared to pay a maximum of \$2.40 for her first glass of fruit juice, but for each subsequent glass she is only prepared to pay 20 cents less than the previous one. If the price of juice is 80 cents per glass, how many glasses will she purchase?

- A. 8 glasses.
- B. 3 glasses.
- C. 10 glasses.
- D. 9 glasses.



A price floor of \$23 placed on the market in the graph shown:

- A. is effective, and causes a shortage.
- B. is effective, and causes a surplus.
- C. is ineffective, and does not prevent the market from reaching equilibrium.
- D. is ineffective, and does not affect the market.



24.

Assume the market was in equilibrium in the graph shown. If the market price gets set to \$14, which of the following is true?

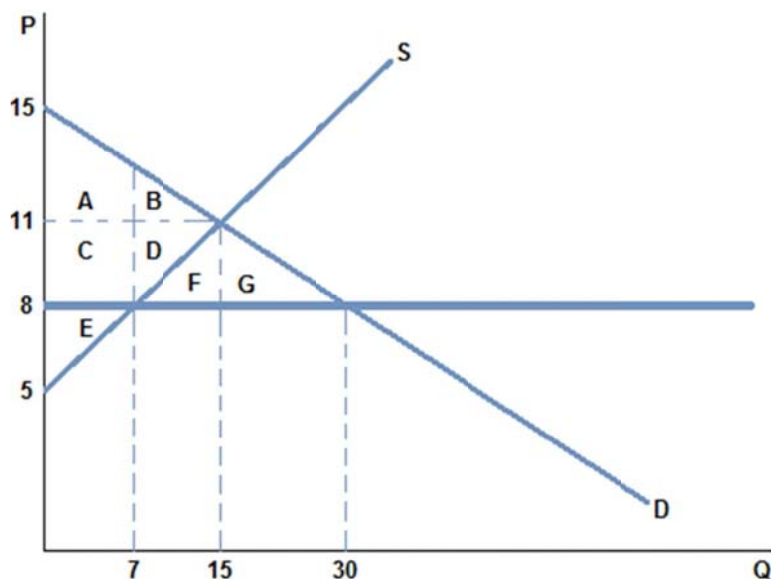
- A. Some consumers gain surplus, but total surplus falls.
- B. Some consumers lose surplus, but total surplus rises.
- C. Some producers lose surplus, but total surplus rises.
- D. Some producers gain surplus, but total surplus falls.

25. An effective price floor:

- A. will cause quantity demanded to exceed quantity supplied.
- B. will cause quantity supplied to exceed quantity demanded.
- C. will set a legal maximum price in a market.
- D. will increase total well being.

26. Suppose the market for coffee is in equilibrium at a price of \$5 per pound. This means:

- A. all remaining producers require less than \$5 to produce coffee.
- B. all consumers who want to buy coffee are satisfied.
- C. all producers who want to sell coffee are pleased.
- D. all remaining consumers value a pound of coffee at less than \$5.



27.

If a price ceiling of \$8 were placed in the market in the graph shown:

- A. a surplus of 15 would occur.
- B. a surplus of 7 would occur.
- C. a surplus of 23 would occur.
- D. None of these is true.

28. Assume a market that has an equilibrium price of \$5. If the market price is set at \$9, producer surplus:

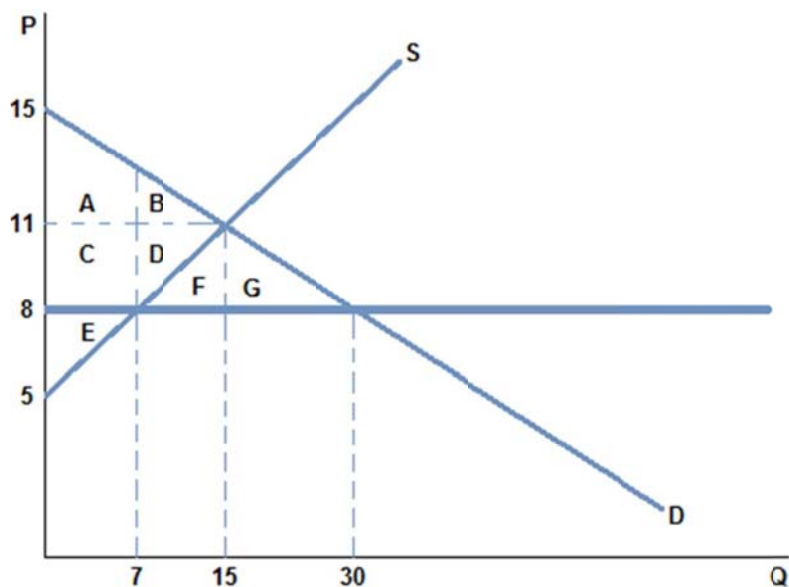
- A. Neither of these statements is true.
- B. rises for some because of the increased price.
- C. Both of these statements are true.
- D. decreases for some because of fewer transactions taking place.

29. Assume that reading produces a positive externality. It will be the case that the _____ than that which is socially optimal.

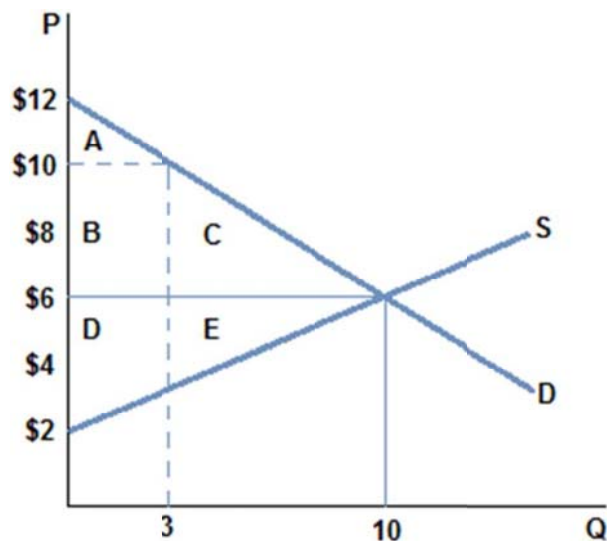
- A. supply of reading will be greater
- B. price of reading will be greater
- C. demand for reading will be greater
- D. supply of reading will be less
- E. demand for reading will be less

30. The idea of the "invisible hand" tells us that individuals will pursue:

- A. trades in which they will be the clear winner and the other will be a loser.
- B. mutually beneficial trades with other individuals to maximize surplus.
- C. as few government policies as possible so the market can act freely.
- D. the most equitable outcome possible.



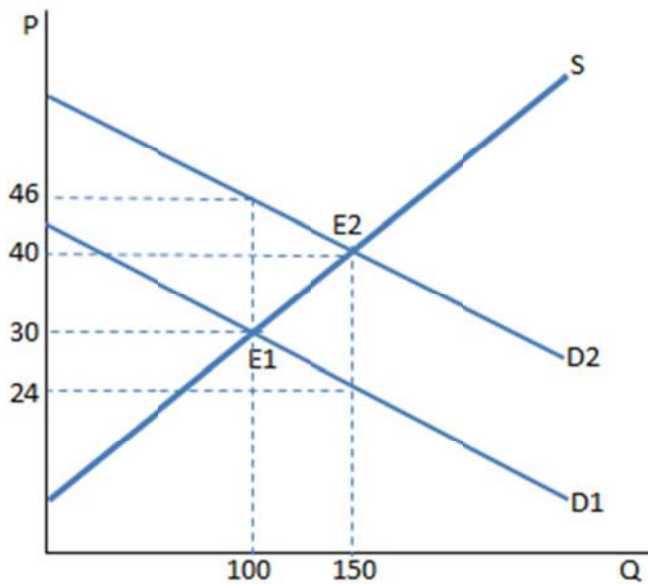
31. After a price ceiling of \$8 is placed on the market in the graph shown, the total number of units traded:
- falls by 15 relative to equilibrium.
 - falls by 23 relative to equilibrium.
 - increases by 15 relative to equilibrium.
 - falls by 8 relative to equilibrium.
32. One way to allocate the scarce good created from an effective price ceiling is to:
- give them to the friends and family of the producers.
 - All of these are examples of allocating using non-price methods.
 - offer it on a first-come, first-served basis.
 - ration a certain quantity per household.



33. According to the graph shown, if the market goes from equilibrium to having its price set at \$10 then:
- A. producer surplus will change from $(D + E)$ to $(D + E + B + C)$.
 - B. producer surplus will change from $(D + E)$ to $(D + B)$.
 - C. producer surplus will change from $(B + C + D + E)$ to D only.
 - D. producer surplus will change from $(D + B)$ to $(D + E)$.

34. Which of the following statements best characterizes the inefficiency induced by a price floor?
- A. Consumers are encouraged to consume too much.
 - B. Producers are encouraged to produce too little.
 - C. The enforcement of the price floor is extremely costly.
 - D. The extra cost of the last unit produced is greater than the extra benefit of the last unit consumed.

35. The loss of total surplus that results when the quantity of a good that is bought and sold is below the market equilibrium quantity is called:
- A. total surplus.
 - B. deadweight loss.
 - C. producer surplus.
 - D. consumer surplus.



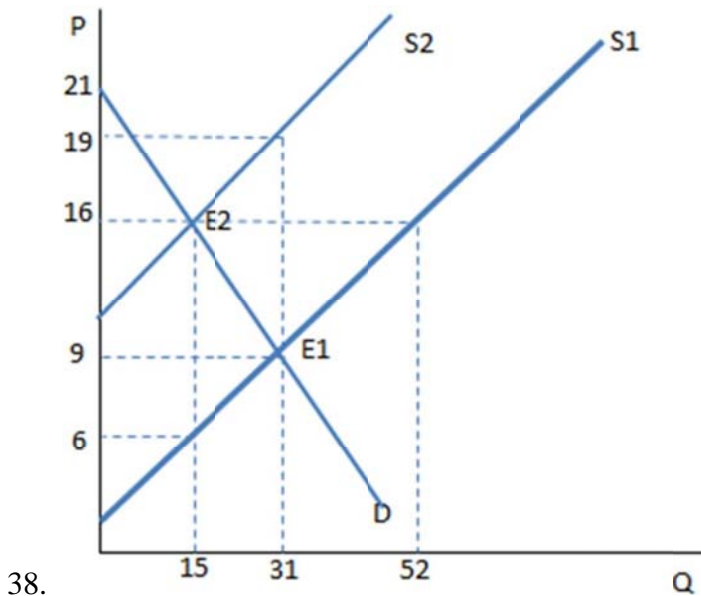
36.

The graph shown portrays a subsidy to buyers. The amount of money spent on this subsidy by the government is:

- A. \$2,400.
- B. \$6,000.
- C. \$800.
- D. \$3,600.

37. A Pigovian tax imposed on consumers _____ the price, and if the same tax were imposed on producers, it would _____ the price.

- A. increases; increase
- B. decreases; increase
- C. decreases; decrease
- D. increases; decrease



The graph shown demonstrates a tax on sellers. Which of the following can be said about the effect of this tax?

- A. The price paid by buyers is less than that received by sellers, and the difference is the total tax revenue.
- B. The price paid by buyers and received by sellers is higher than it was before the tax was imposed.
- C. The price paid by buyers is greater than that received by sellers, and the difference is the tax wedge.
- D. The price paid by buyers is greater than that received by sellers, and the difference is the total tax revenue.

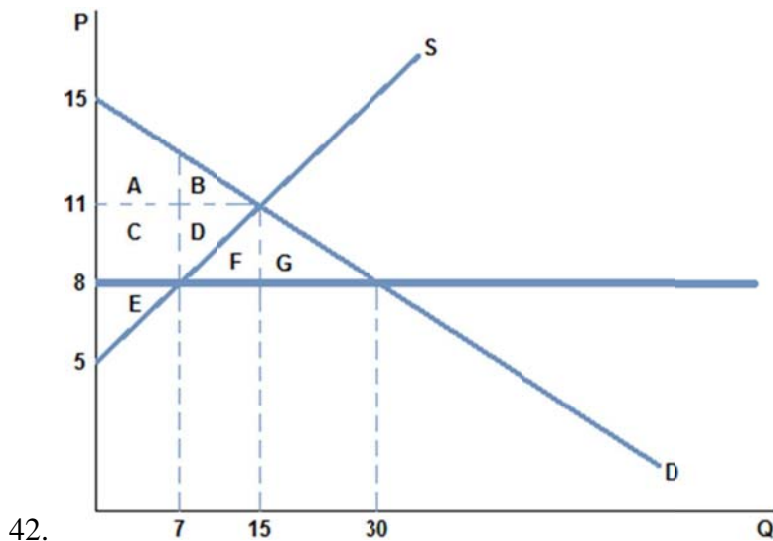
39. NO QUESTION HERE

40. The government imposing a minimum wage is an example of an attempt to:

- A. encourage the consumption of inferior goods.
- B. redistribute surplus in a market.
- C. correct a market failure.
- D. discourage the consumption of inferior goods.

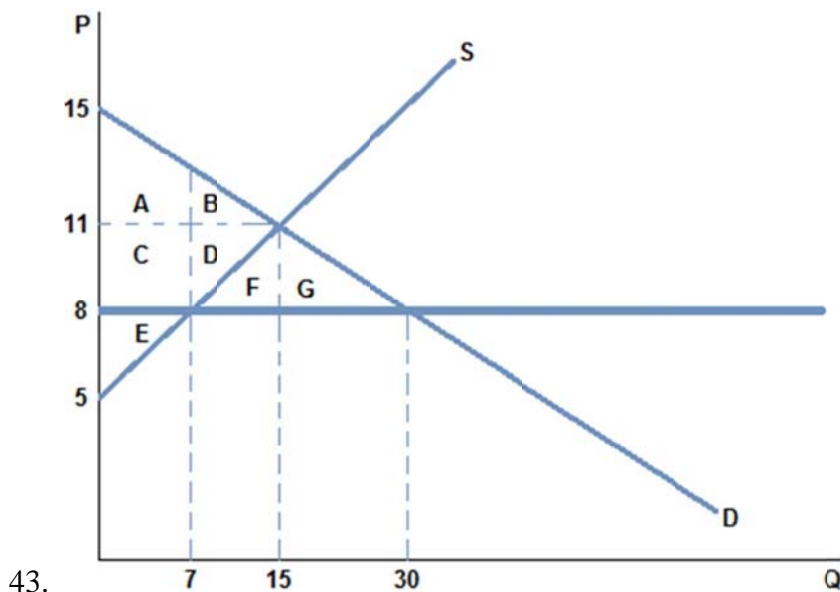
41. Which of the following is not guaranteed by the efficiency of the market equilibrium?

- A. Price represents the value of an extra unit of consumption.
- B. Rich and poor will have adequate access to the goods in the market.
- C. Price represents the cost of an extra unit of production.
- D. Neither shortage nor surplus will exist.



After a price ceiling of \$8 is placed on the market in the graph shown, which area represents consumer surplus?

- A. A + B + C
- B. A + C
- C. A + B
- D. A + B + C + D + F + G



Which of the following changes to the market in the graph shown could cause the price ceiling to become ineffective?

- A. Supply could increase, and shift to the right.
- B. Demand could increase, and shift to the right.
- C. Supply could decrease, and shift to the left.
- D. Supply could increase, and shift to the left.

44. Which one of the following statements is false?

- A. When firms pass on some of their cost of production to society, the market has failed.
- B. Any market equilibrium price always generates a socially optimal allocation of resources.
- C. A socially optimal allocation of resources is attained when market price equals the marginal social cost of producing the last unit of output sold.
- D. If a good is overpriced, there is an under-allocation of resources in the production of the good.

45. Consider the market for flu shots and select the false statement from the following?

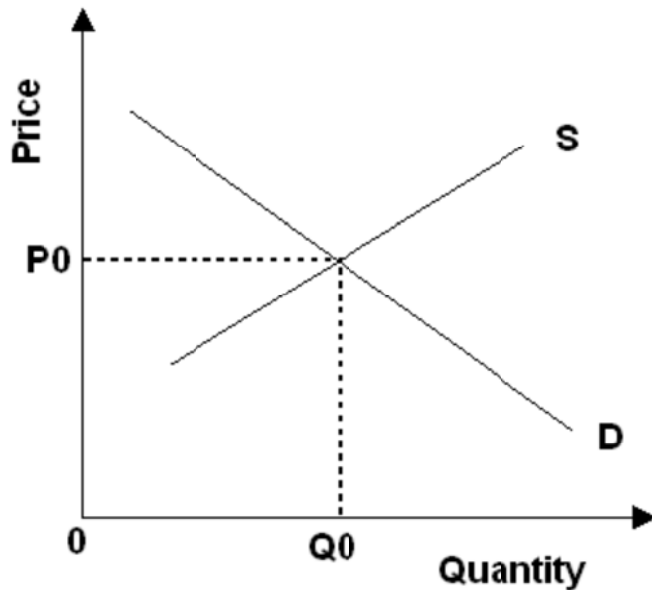
- A. The social demand curve for flu shots is higher than the private demand curve for flu shots.
- B. Free market without subsidization will over-supply flu shots.
- C. Subsidization of flu shots will cover the positive externalities of flu shots.
- D. the marginal social benefit of an extra unit of flu shot is greater than the marginal private benefit of an extra unit of flu shot.

46. Normative analysis:

- A. leads to the best solutions.
- B. examines whether the policy is a good idea.
- C. involves the formulation and testing of hypotheses.
- D. examines if the policy actually accomplished its goal.

47. In the case of either an external cost or an external benefit, the invisible hand fails to generate the efficient outcome because

- A. too little is produced.
- B. buyers and sellers only take their self interest into account.
- C. too much is produced.
- D. the model is not capable of incorporating externalities.
- E. the environment is treated as a common property.



48. Refer to the diagram above. If a positive externality exists in this market, the marginal social benefit from consuming this good at the competitive equilibrium output level is
- equal to P_0 .
 - either greater than or less than P_0 , depending on the elasticity of supply.
 - either equal to or less than P_0 , depending on the elasticity of demand.
 - less than P_0 .
 - greater than P_0 .
49. When Bob's willingness to pay for a cup of coffee is \$1, and the price of a cup of coffee is \$1:
- Bob will get the same surplus whether he purchases the coffee or not.
 - Bob is indifferent about purchasing the coffee.
 - Bob will get no surplus by purchasing the coffee.
 - All of these are true.
50. If the demand curve is less elastic than the supply curve, then:
- the sellers will bear a greater tax incidence.
 - the buyers will bear a smaller tax burden than sellers.
 - the buyers will bear a greater tax incidence.
 - the sellers will bear a greater tax burden than buyers.

Winter 2015 Exam 2 Key

Version #1

1. C
2. C
3. B
4. D
5. D
6. E
7. C
8. D
9. A
10. C
11. D
12. C
13. B
14. A
15. NO QUESTION
16. B
17. A
18. C
19. B
20. D
21. B
22. D
23. B
24. D
25. B
26. D
27. D
28. C
29. E

30. B

31. D

32. B

33. B

34. D

35. B

36. A

37. A

38. C

39. NO QUESTION HERE

40. B

41. B

42. B

43. A

44. B

45. B

46. B

47. B

48. E

49. D

50. C

