Question #1 of 49

Question ID: 1456720

The demand for a product tends to be price inelastic if:

A) few good complements for the product are available. ✗

B) few good substitutes for the product are available. ✓

C) people spend a large share of their income on the product. ✗

Explanation

If a large price change results in a small change in quantity demanded, demand is inelastic. Cigarettes are an example of a good with inelastic demand.

(Module 8.1, LOS 8.a)

Question #2 of 49

Question ID: 1456712

If the demand curve for a given product is a straight line with a slope of –5, this indicates that:

A) elasticity is constant along the demand curve. ✗

B) demand is unit elastic. ✗

C) demand is more elastic at higher prices. ✓

Explanation

Elasticities will be greater (in absolute value) at higher prices.

(Module 8.1, LOS 8.a)

Question #3 of 49

Question ID: 1456700

The cross price elasticity of demand for a substitute good and the income elasticity for an inferior good are:

Cross elasticity	Income elasticity

A) < 0 < 0

B) > 0 < 0

C) < 0 > 0

Explanation

The cross price elasticity of substitutes is positive, and the income elasticity of an inferior good is negative.

(Module 8.1, LOS 8.a)

Question #4 of 49

Question ID: 1456730

A decrease in the price of Good Y can result in a decrease of the quantity of Good Y demanded by consumers if the substitution effect:

A) is positive and the income effect is negative and larger than the substitution effect.

B) is negative and larger than the positive income effect.

C) and the income effect are negative.

Explanation

If the price of Good Y decreases, the substitution effect will have a positive impact on the quantity demanded of Good Y. Thus, the only way that quantity demanded of Good Y can decrease is if there is a negative income effect that is greater in magnitude than the substitution effect; i.e., if Good Y is a Giffen good.

(Module 8.2, LOS 8.c)

Question #5 of 49

Question ID: 1456708

If quantity demanded increases 15% when the price drops 1%, demand for this good:

A) elastic, but not perfectly elastic.

B) inelastic, but not perfectly inelastic.

C) perfectly elastic.

Explanation

Whenever quantity demanded for a good changes by a greater percentage than price, the price elasticity of demand will be greater than 1.0 and demand for the product is considered to be elastic.

(Module 8.1, LOS 8.a)

Question #6 of 49

Question ID: 1456734

A firm in a perfectly competitive industry that seeks to maximize profit is *most likely* to continue production in the short run as long which of the following conditions exists? Price is equal to or greater than:

A) average fixed cost.

B) average variable costs.

C) marginal cost.

Explanation

If a firm is covering its average variable costs, it will continue to operate in the short run since it is covering some portion of its fixed costs.

(Module 8.2, LOS 8.d)

Question #7 of 49

Question ID: 1456704

If quantity demanded increases 20% when the price drops 2%, this good exhibits:

A) inelastic, but not perfectly inelastic, demand.

B) elastic, but not perfectly elastic, demand.

C) perfectly inelastic demand.

Explanation

If quantity demanded increases 20% when the price drops 2%, this good exhibits elastic demand. Whenever demand changes by a greater percentage than price, demand is considered to be elastic.

(Module 8.1, LOS 8.a)

Question #8 of 49

Question ID: 1462770

When two goods are complements, the cross elasticity of demand is:

A) negative, and for substitutes the cross price elasticity of demand is negative. ✗

B) negative, and for substitutes the cross price elasticity of demand is positive. ✓

C) positive, and for substitutes the cross price elasticity of demand is negative. ✗

Explanation

The cross elasticity of demand for goods that are complements is negative because an increase in the price of one would tend to decrease the quantity demanded of the other. The cross elasticity of demand for substitute goods is positive because an increase in the price of one would tend to increase the quantity demanded of the other. (Module 8.1, LOS 8.a)

Question #9 of 49

Question ID: 1456738

A firm that is experiencing diseconomies of scale should:

A) decrease its plant size. ✓

B) decrease output in the short run. ✗

C) shut down in the long run. ✗

Explanation

If a firm is experiencing diseconomies of scale, it should decrease its plant size to the efficient scale, which is the size that minimizes long-run average total cost. Plant size can be adjusted in the long run but not in the short run.

(Module 8.2, LOS 8.e)

Question #10 of 49

Question ID: 1456699

A good is *most likely* to demonstrate higher price elasticity of demand:

A) if it represents a small portion of the consumer's budget, than if it represents a large portion. ✗

B) in the long run than the short run. ✓

C) when there are few substitutes for the good, than when there are many good substitutes.

Explanation

A good is likely to show a high price elasticity of demand when there are good substitutes, it represents a large proportion of consumer spending, and in the long run as consumers make changes that take time to implement in response to price changes for the good.

(Module 8.1, LOS 8.a)

Question #11 of 49

Question ID: 1456732

A distinction between Giffen goods and Veblen goods is that:

A) demand curves for Giffen goods slope upward, while demand curves for Veblen goods slope downward.

B) Giffen goods are inferior goods, while Veblen goods are not inferior goods.

C) the substitution effect is positive for a Veblen good but negative for a Giffen good.

Explanation

Giffen goods are inferior goods for which the quantity demanded decreases when the price decreases, because the negative income effect is larger than the positive substitution effect. Veblen goods are goods for which the quantity demand increases when the price increases, such as a high-status good for which the consumer gains utility from being seen to consume the good. Giffen goods and Veblen goods, if they exist, have demand curves that slope upward over at least some range of prices. The substitution effect is positive for all goods.

(Module 8.2, LOS 8.c)

Question #12 of 49

Question ID: 1456737

Suppose a price-taker firm produces baseball bats that sell at a price of $100 each. This firm's average total cost at the current level of production is $150 per bat, and the average fixed cost is $40 per bat. Which of the following statements is *most accurate* regarding this firm? They should:

A) continue producing baseball bats because they are covering their fixed costs.

B) shut down in the short run because their average total cost is greater than their price.

C) shut down in the short run because their average variable cost is greater than their price.

Explanation

Variable costs = $150 (ATC) – $40 (AFC) = $110 (AVC). At a selling price of $100 the firm is not covering its variable costs and will have losses greater than its fixed costs if it stays in business.

(Module 8.2, LOS 8.d)

Question #13 of 49

Question ID: 1456727

When the price of a good decreases, how do the income effect and the substitution effect change the quantity demanded of the good?

A) Both the income effect and the substitution effect increase the quantity demanded.

B) The income effect increases the quantity consumed, but the substitution effect may increase or decrease the quantity demanded.

C) The substitution effect increases the quantity demanded, but the income effect may increase or decrease the quantity demanded.

Explanation

The substitution effect is a shift in consumption toward a larger quantity of a good that decreases in price. A decrease in the price of a good also has an income effect because the old bundle costs less. The income effect may result in consumption of a larger or smaller quantity of the good that has decreased in price, depending on whether it is a normal good or an inferior good.

(Module 8.2, LOS 8.b)

Question #14 of 49

Question ID: 1456743

According to the law of diminishing returns, doubling the number of salespeople for a firm will *most likely* result in:

A) decreasing the total sales of the firm as a result of competition amongst salespeople. ✗

B) doubling the total sales of the firm. ✗

C) increasing the total sales of the firm and reducing the average sales per salesperson. ✓

Explanation

The law of diminishing returns states that as more of a resource is added to a production process, holding other resource use constant, increases in output will eventually decrease. Therefore, as more salespeople are added they will generate more sales at a decreasing rate. Total sales will increase and the average sales per salesperson will decrease.

(Module 8.2, LOS 8.f)

Question #15 of 49

Question ID: 1462772

A company has estimated that the price elasticity of demand for its output is –1.1. If the company increases the price of its product by 5%, it is *most likely* that:

A) both total revenue and profits will decrease. ✗

B) total revenue will decrease but profits may increase. ✓

C) total revenue will increase but profits may decrease. ✗

Explanation

Price elasticity of –1.1 tells us that a 5% increase in price will reduce sales by more than 5%, so total revenue will decrease. Whether profits increase or decrease will depend on whether the cost reduction from producing less output is greater or less than the decrease in total revenue. (Module 8.1, LOS 8.a)

Question #16 of 49

Question ID: 1456747

At a fixed level of capital, output increases as the quantity of labor increases, but at a decreasing rate. This phenomenon is an example of:

A) diminishing costs to labor. ✗

B) diminishing returns to capital.

C) diminishing returns to labor.

Explanation

The law of diminishing returns states that at some point, as more and more of a resource (e.g., labor) is devoted to a production process, holding the quantity of other inputs constant, the output increases, but at a decreasing rate.

(Module 8.2, LOS 8.f)

Question #17 of 49

Question ID: 1456733

When household incomes go down and the quantity of a product demanded goes up, the product is:

A) a normal good.

B) a Veblen good.

C) an inferior good.

Explanation

When household incomes go down and the quantity demanded of a product goes up, the product is an inferior good. Inferior goods include things like bus travel and margarine.

(Module 8.2, LOS 8.c)

Question #18 of 49

Question ID: 1456731

A good is considered an inferior good if it exhibits a negative:

A) elasticity of demand.

B) income effect.

C) substitution effect.

Explanation

The income effect is negative for an inferior good. An increase in income results in a decrease in the quantity demanded.

(Module 8.2, LOS 8.c)

Question #19 of 49

Question ID: 1456706

If a good has elastic demand, a small percentage price increase will cause:

A) a larger percentage decrease in the quantity demanded. ✓

B) a smaller percentage increase in the quantity demanded. ✗

C) a larger percentage increase in the quantity demanded. ✗

Explanation

If a good has elastic demand, a small price increase will cause a larger decrease in the quantity demanded. Demand is elastic when the percentage change in quantity demanded is larger than the percentage change in price.

(Module 8.1, LOS 8.a)

Question #20 of 49

Question ID: 1456716

Income elasticity is defined as the:

A) change in quantity demanded divided by the change in income. ✗

B) percentage change in the quantity demanded divided by the percentage change in income. ✓

C) percentage change in income divided by the percentage change in the quantity demanded. ✗

Explanation

Income elasticity is defined as the percentage change in quantity demanded divided by the percentage change in income. Normal goods have positive values for income elasticity and inferior goods have negative income elasticities.

(Module 8.1, LOS 8.a)

Question #21 of 49

Question ID: 1456739

Which of the following *most accurately* describes economies of scale? Economies of scale:

A) are dependent on short-run average costs. ✗

B) increase at a decreasing rate. ✗

C) occur when long-run unit costs fall as output increases. ✓

Explanation

Economies of scale occur when the percentage increase in output is greater than the percentage increase in the cost of all inputs. Economies of scale occur over the range where the long-run average cost curve slopes downward.

(Module 8.2, LOS 8.e)

Question #22 of 49

Question ID: 1456718

The percent change in demand for a good divided by the percent change in the price of another good is known as the:

A) price elasticity of demand. ✗

B) cross price elasticity of demand. ✓

C) income elasticity of demand. ✗

Explanation

$$\text{Cross price elasticity of demand} = \frac{\text{Percent change in quantity demanded}}{\text{Percent change in price of another good}}$$

(Module 8.1, LOS 8.a)

Question #23 of 49

Question ID: 1456702

Income elasticity is defined as the percentage change in:

A) income divided by the percentage change in the quantity demanded. ✗

B) quantity demanded divided by the percentage change in income. ✓

C) quantity demanded divided by the percentage change in the price of the product.

Explanation

Income elasticity is defined as the percentage change in quantity demanded divided by the percentage change in income. Normal goods have positive values for income elasticity, and inferior goods have negative income elasticity.

(Module 8.1, LOS 8.a)

Question #24 of 49

Question ID: 1456746

The law of diminishing returns states that for a given production process, as more and more of a resource (such as labor) are added, holding the quantities of other resources fixed:

A) output increases at a decreasing rate.

B) cost declines at a decreasing rate.

C) cost declines at an increasing rate.

Explanation

The law of diminishing returns states that for a given production process, as more and more resources (such as labor) are added holding the quantities of other resources fixed, output increases at a decreasing rate. This occurs because, at some point, adding more workers results in inefficiencies.

(Module 8.2, LOS 8.f)

Question #25 of 49

Question ID: 1456705

The primary factors that influence the price elasticity of demand for a product are:

A) changes in consumers' incomes, the time since the price change occurred, and the availability of substitute goods.

B) the availability of substitute goods, the time that has elapsed since the price of the good changed, and the proportions of consumers' budgets spent on the product.

the proportions of consumers' budgets spent on the product, the size of the

C) shift in the demand curve for a product, and changes in consumers' price expectations.

Explanation

The three primary factors influencing the price elasticity of demand for a good are the availability of substitute goods, the proportions of consumers' budgets spent on the good, and the time since the price change. If there are good substitutes, when the price of the good goes up, some customers will switch to substitute goods. For goods that represent a relatively small proportion of consumers' budgets, a change in price will have little effect on the quantity demanded. For most goods, the price elasticity of demand is greater in the long run than in the short run.

(Module 8.1, LOS 8.a)

Question #26 of 49

Question ID: 1456717

Price elasticity of demand is *most* accurately defined as the change in:

A) market price in response to a change in the quantity demanded.

B) quantity demanded in response to a change in income.

C) quantity demanded in response to a change in market price.

Explanation

Price elasticity of demand is the percent change in quantity demanded relative to a percent change in price.

(Module 8.1, LOS 8.a)

Question #27 of 49

Question ID: 1456715

If the price elasticity of demand is -1.5 and the price of the product increases 2%, the quantity demanded will:

A) decrease approximately 0.75%.

B) decrease approximately 1.5%.

C) decrease approximately 3%.

Explanation

If the price elasticity of demand is -1.5, and you increase the price of the product 2%, the quantity demanded will decrease approximately 3%. When the price elasticity is negative, it means that price and demand move in opposite directions. Given a price decrease, demand will increase and vice versa. The absolute value, 1.5, indicates that demand will move one-and-a-half times as much as price.

(Module 8.1, LOS 8.a)

Question #28 of 49

Question ID: 1462773

A firm is operating in a perfectly competitive market. Market price is greater than average variable cost (AVC) but lower than average total cost (ATC). Which of the following statements is *most* accurate?

A) The firm should continue to produce and sell its product in the short run but not in the long run, unless the price increases. ✓

B) The firm should decrease its production in the short run in order to increase price and either reduce losses or produce profits. ✗

C) If the owner thinks the price eventually will exceed ATC, the firm should shut down its operations temporarily and resume when price exceeds ATC. ✗

Explanation

Because the price exceeds the average variable cost, each item sold covers part of the firm's fixed cost, so in the short run the firm should continue to produce and sell its product. If the firm shuts down temporarily, the costs incurred (fixed costs) will not be recovered partially. In the long run, however, the firm should shut down unless the price is greater than average total cost. Since the firm is a price taker, reducing the firm's output will have no effect on the price since each firm is small relative to the market. (Module 8.2, LOS 8.e)

Question #29 of 49

Question ID: 1456719

Gene Bawerk, an economics professor, is lecturing on the factors that influence the price elasticity of demand. He makes the following assertions:

> Statement 1: For most goods, demand is more elastic in the long run than the short run.
>
> Statement 2: Demand for a good becomes more elastic when a close substitute for it becomes available on the market.

With respect to Bawerk's statements:

A) only statement 1 is correct. ✗

B) only statement 2 is correct. ✗

C) both are correct. ✓

Explanation

Both of these statements are accurate. Price elasticity for most goods is greater in the long run because individuals can make long-term decisions that require different quantities of the good, such as buying more fuel efficient vehicles to use less gasoline. Price elasticity is greater the better the available substitutes because an increase in price will lead more buyers to switch to the substitute products.

(Module 8.1, LOS 8.a)

Question #30 of 49

Question ID: 1456714

If the price elasticity of demand is –1.5 and a change in the price of the product increases the quantity demanded by 4%, then what is the percent change in price?

A) –0.375%. ✗

B) –2.667%. ✓

C) –6.000%. ✗

Explanation

Price elasticity of demand is calculated by dividing the percent change in quantity demanded by the percent change in price. The percent change in price is, therefore, the percent change in quantity demanded divided by the price elasticity of demand = 4 / –1.5 = –2.667.

(Module 8.1, LOS 8.a)

Question #31 of 49

Question ID: 1456744

Based on the concept of diminishing returns, as the quantity of output increases, the short-run marginal costs of production eventually:

A) fall at a decreasing rate. ✗

B) rise at a decreasing rate. ✗

C) rise at an increasing rate. ✓

Explanation

The law of diminishing returns states that as more variable resources are a production process combined with a fixed input, output will eventually increase at a decreasing rate. In the short run, as the quantity produced rises, costs rise at an increasing rate.

(Module 8.2, LOS 8.f)

Question #32 of 49

Question ID: 1456713

If the price elasticity of demand for a good is –4.0, then a 10% increase in price would result in a:

A) 10% decrease in the quantity demanded. ✗

B) 4% decrease in the quantity demanded. ✗

C) 40% decrease in the quantity demanded. ✓

Explanation

Price elasticity of demand = (% change in Q demanded / % change in price). Given the price elasticity of demand and the percentage change in price, we can solve for the percentage change in quantity demanded = price elasticity of demand × percentage change in price. Here, –4.0 × 10% = –40%.

(Module 8.1, LOS 8.a)

Question #33 of 49

Question ID: 1456736

Under perfect competition, if the price of a firm's product is below its average total cost, in the short run the firm should:

A) shut down, but operate in the long run if it is covering its variable costs.

B) operate if it is covering its variable costs.

C) increase the product price to at least cover its average total cost.

Explanation

If the firm is covering its average variable costs and some of its fixed costs it will minimize its losses by continuing to operate in the short run. If the price remains below average total cost in the long run, the firm should shut down. Under perfect competition, firms have no pricing power and must take the market price.

(Module 8.2, LOS 8.d)

Question #34 of 49

Question ID: 1456709

If a good has elastic demand, a small price decrease will cause:

A) a larger decrease in the quantity demanded.

B) a larger increase in quantity demanded.

C) no change in the quantity demanded.

Explanation

If a good has elastic demand, a small price decrease will cause a larger increase in the quantity demanded.

(Module 8.1, LOS 8.a)

Question #35 of 49

Question ID: 1462769

The price of milk in a country increases from €1.00 per liter to €1.10 per liter, and the quantity supplied does not change. This suggests the elasticity of the short-run supply of milk in this country is equal to:

A) infinity, and supply is perfectly elastic.

B) infinity, and supply is perfectly inelastic.

C) zero, and supply is perfectly inelastic.

Explanation

If quantity supplied does not respond to a change in price, supply is perfectly inelastic. For perfectly inelastic supply, elasticity equals zero. (Module 8.1, LOS 8.a)

Question #36 of 49

Question ID: 1456725

With respect to utility theory, the income effect for a decrease in the price of a good:

A) may increase or decrease consumption of the good. ✓

B) will increase consumption of the good. ✗

C) will decrease consumption of the good. ✗

Explanation

The income effect for a decrease in price may be positive (for a normal good) or negative (for an inferior good). Therefore, the income effect from a price decrease may be to increase or decrease consumption of a good.

(Module 8.2, LOS 8.b)

Question #37 of 49

Question ID: 1462771

The daily demand curve for olive oil (in liters) for a particular distributor is estimated as:

$$\text{Price}_{\text{olive oil}} = 20 - Q_{\text{olive oil}} / 150$$

At a price of $10 per liter, the price elasticity of demand for olive oil is *closest* to:

A) −0.007. ✗

B) −1.000. ✓

C) −1.300. ✗

Explanation

The demand function for olive oil is Q = 3000 − 150 P.

At a price of 10, Q = 3000 − 150(10) = 1500.

$$\text{Elasticity} = P_0/Q_0 \times \Delta Q/\Delta P = 10/1500 \times (-150) = -1.$$ (Module 8.1, LOS 8.a)

Question #38 of 49

Question ID: 1456726

With respect to utility theory, the substitution effect for a decrease in the price of a good:

A) will decrease consumption of the good. ✗

B) may increase or decrease consumption of the good. ✗

C) will increase consumption of the good. ✓

Explanation

In utility theory, if the price of one good decreases, the substitution effect causes consumption of that good to increase.

(Module 8.2, LOS 8.b)

Question #39 of 49

Question ID: 1456729

A good for which consumers exhibit a negative income effect that is smaller than the substitution effect is *most accurately* described as a(n):

A) Giffen good. ✗

B) inferior good. ✓

C) Veblen good. ✗

Explanation

For an inferior good the income effect is negative. A Giffen good is an inferior good for which the negative income effect is larger than the positive substitution effect, resulting in a decrease in consumption in response to a decrease in price. A Veblen good is not an inferior good, but rather a good that provides more utility to a consumer at a higher price than it provides at a lower price because the status benefits of ownership are greater at higher prices.

(Module 8.2, LOS 8.c)

Question #40 of 49

Question ID: 1456703

If the price elasticity of a linear demand curve is –1 at the current price, an increase in price will lead to:

A) an increase in total revenue. ✗

B) a decrease in total revenue. ✓

C) no change in total revenue. ✗

Explanation

On a linear demand curve, demand is elastic at prices above the point of unitary elasticity, so a price increase will decrease total revenue.

(Module 8.1, LOS 8.a)

Question #41 of 49

Question ID: 1456742

Which of the following statements regarding diminishing marginal returns is *most* accurate?

A) The total cost curve arches downward. ✗

B) As the quantity produced rises, costs begin to rise at an increasing rate. ✓

C) As the quantity produced rises, costs begin to rise at a decreasing rate. ✗

Explanation

At production levels that are consistent with decreasing marginal returns, costs will increase at an increasing rate as production rises.

(Module 8.2, LOS 8.f)

Question #42 of 49

Question ID: 1456740

The upward sloping segment of a long-run average total cost curve represents the existence of:

A) diseconomies of scale. ✓

B) economies of scale. ✗

C) efficiencies of scale. ✗

Explanation

Diseconomies of scale occur along the upward sloping segment of the long-run average total cost curve where costs rise as output increases. The flat portion at the bottom of the long-run average total costs curve represents constant returns to scale.

(Module 8.2, LOS 8.e)

Question #43 of 49

Question ID: 1456745

The law of diminishing returns states that at some point as:

A) more of a resource is devoted to production, holding the quantity of other inputs constant, the output will increase, but at a decreasing rate. ✓

B) more of a resource is devoted to production, holding the quantity of other inputs constant, at some point output will begin to decrease. ✗

C) less of a resource are devoted to production, holding the quantity of other inputs constant, the output will decrease, but at an increasing rate. ✗

Explanation

At low levels of output, increasing marginal returns will exist corresponding to the downward sloping portion of the marginal cost curve. As marginal costs begin to increase diminishing marginal returns will occur.

(Module 8.2, LOS 8.f)

Question #44 of 49

Question ID: 1456710

When demand for a good is relatively inelastic, a higher price will:

A) fail to reduce the quantity demanded for the good. ✗

B) have no impact on the demand for the good. ✗

C) lead to an increase in total expenditures for the good. ✓

Explanation

When demand is relatively inelastic, consumers do not reduce their quantity demanded very much when the price increases. That is, a given percentage increase in price results in a smaller percentage reduction in quantity demanded. Thus, total expenditures on the good increase. "Fail to reduce the quantity demanded for the good" is inaccurate because that would only be true if demand was *perfectly* inelastic.

(Module 8.1, LOS 8.a)

Question #45 of 49

Question ID: 1456711

If the price of World Cup Soccer tickets increases from $40 a ticket to $50 a ticket and the quantity demanded of tickets stays the same, demand for the tickets is:

A) elastic, but not perfectly elastic.

B) inelastic, but not perfectly inelastic.

C) perfectly inelastic.

Explanation

Since the quantity of tickets demanded stayed the same after the price changed, the demand curve would have to be vertical which is a perfectly inelastic demand curve.

(Module 8.1, LOS 8.a)

Question #46 of 49

Question ID: 1456707

For a linear demand curve, at the price where elasticity is -2.0, reducing prices will:

A) decrease total revenue and we are not at the point of maximum total revenue.

B) increase total revenue and we are at the point of maximum total revenue.

C) increase total revenue and we are not at the point of maximum total revenue.

Explanation

If the price elasticity of demand is -2.0, this indicates that the percentage change in quantity demanded is twice the percentage change in price. Thus, a decrease in price will be more than offset by the increase in quantity, and total revenue will increase. We are not at the point of maximum total revenue which is where elasticity is -1.0—the point of unit elastic demand.

(Module 8.1, LOS 8.a)

Question #47 of 49

Question ID: 1456735

If the price of its product is less than its average total cost in the long run, a firm operating under perfect competition should:

A) keep operating only if it is covering its variable costs. ✗

B) shut down. ✓

C) keep operating and attempt to eliminate its fixed costs. ✗

Explanation

If the price is below average total cost then the firm is losing money. In the short run a firm should keep operating if it is covering its variable costs, but in the long run if the firm believes the price will never exceed average total cost, the only way to eliminate fixed costs is to go out of business.

(Module 8.2, LOS 8.d)

Question #48 of 49

Question ID: 1456728

Which of the following is *most likely* to cause a decrease in the consumption of a good in response to a decline in the price of the good?

A) Income effect. ✓

B) Law of demand. ✗

C) Substitution effect. ✗

Explanation

The income effect can be negative if the good is an inferior good. The substitution effect is always positive and will cause consumption of a good to increase if the price declines. The law of demand assumes that a decrease in the price of a good will cause an increase in the quantity demanded.

(Module 8.2, LOS 8.b)

Question #49 of 49

Question ID: 1456701

If the price elasticity of demand is –2 and the price of the product decreases by 5%, the quantity demanded will:

A) decrease 2.5%. ✗

B) increase 10%. ✓

C) increase 7%. ✗

Explanation

If the price elasticity of demand is –2, and the price of the product decreases by 5%, the quantity demanded will increase 10%. The value –2 indicates that the percentage increase in the quantity demanded will be twice the percentage decrease in price.

(Module 8.1, LOS 8.a)