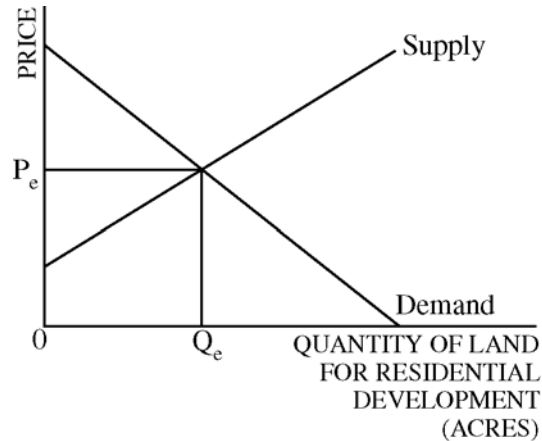


2006 AP[®] MICROECONOMICS FREE-RESPONSE QUESTIONS



3. The supply and demand for land for residential development is shown in the diagram above. The land supplied for such development comes from privately held open-space land or privately held farmland.
- (a) Redraw the graph above and show how an increase in income will affect the equilibrium price and quantity of land converted into residential development, assuming that land for residential development is a normal good.
 - (b) Redraw the graph above and show how a decrease in government per-unit subsidies to farmers will affect the equilibrium price and quantity of land converted into residential development.
 - (c) Assume that the conversion of open-space land and farmland imposes costs on the general population, which can no longer enjoy the scenic vistas.
 - (i) Indicate whether the marginal social cost of converting land is greater than, less than, or equal to the marginal private cost of converting land.
 - (ii) Explain whether the private market quantity of land converted into residential development is socially optimal.

STOP

END OF EXAM

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2006 SCORING GUIDELINES

Question 3

6 points (2 + 2 + 2)

(a) 2 points:

- One point is earned for showing a rightward shift of the demand curve.
- One point is earned for showing that equilibrium price increases and quantity increases.

(b) 2 points:

- One point is earned for showing a rightward shift of the supply curve.
- One point is earned for showing that equilibrium price decreases and quantity increases.

(c) 2 points:

- One point is earned for indicating that MSC is greater than MPC.
- One point is earned for stating that the conversion of land to residential development is not socially optimum because $MSC > MSB(P)$.