Must – try Practice Questions for Test 2

Demand and supply for GPS units in a competitive market is given by Qd = 750 – 2P and supply is Qs = 3P. Each identical firm has marginal costs MC = 6Q and average total costs ATC = 3Q.

a) What is equilibrium price and quantity traded in the market?

b) How much does each firm produce?

c) What is each firm's average revenue?

d) Are firms making positive, normal or negative economic profits?

e) For argument's sake, say that min ATC = $75 (clearly it doesn't). How many firms will there be in the long run?

f) Suppose the government institutes a $20 per unit tax on consumers. The new, after – tax demand curve is Qd = 710 - 2P.

i) What is the deadweight loss due to the tax?

ii) What are the consumer and producer burdens of the tax?

iii) Which is more inelastic – demand or supply?

g) Forget about the tax and return to the original equilibrium. Suppose the government imposes a price floor of $180 in the market.

i) What is producer surplus both before and after the price floor is imposed?

ii) Which is larger – the change in producer surplus or the deadweight loss?