

**McMaster University Department of Economics
ECON 1B03
Fall 2011**

Test 1 ANSWERS

**Saturday October 15, 2011
90 minutes
Instructor: H Holmes**

MULTIPLE CHOICE

Answer all questions on the scan sheet using HB pencil.
Calculators are permitted.
Hand in the scan and this sheet separately.

TOTAL MC MARKS AVAILABLE: 40

NAME: _____

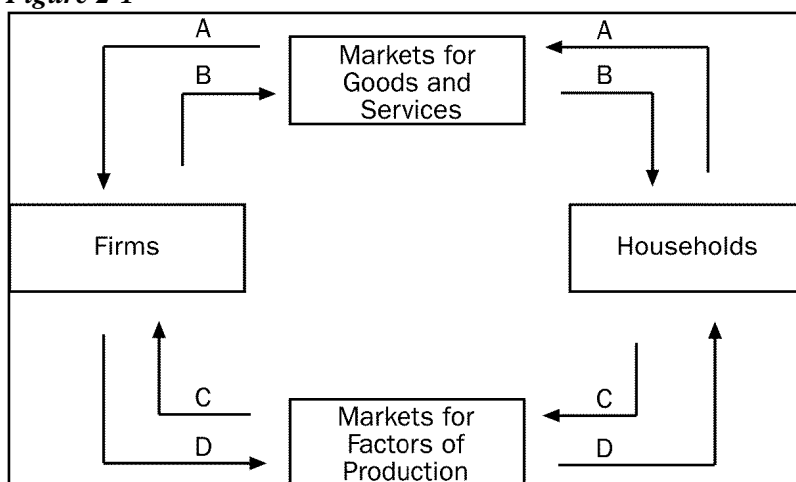
STUDENT #: _____

Multiple Choice

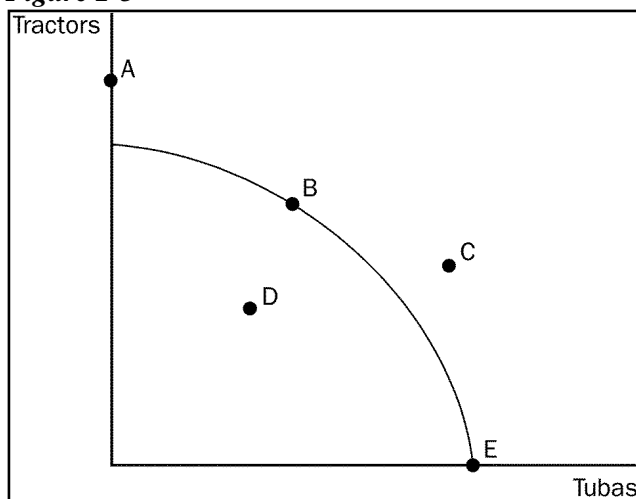
Identify the choice that **best** completes the statement or answers the question.

- _____ 1. Which of the following is the best example of a marginal change?
- After graduating college, Audrey's income increases from \$500 per month to \$3,000 per month.
 - Morgan gets a raise at her part-time job and is now paid \$7.25 per hour instead of \$7.00.**
 - Housing prices in an area increase by 40% when a new highway is built in a small town.
 - A hard freeze wipes out half of the tobacco crop in Ontario and the price of orange juice doubles.
- _____ 2. According to Adam Smith, the success of decentralized market economies is primarily due to
- the basic benevolence of society.
 - society's justice (legal) system.
 - individuals' self-interest.**
 - basic human survival instincts.
- _____ 3. If a copper refinery does NOT bear the entire cost of the smoke it emits, it will
- not emit any smoke so as to avoid the entire cost of the smoke.
 - emit lower levels of smoke.
 - emit an acceptable level of smoke.
 - emit too much smoke.**
- _____ 4. The two loops in the circular-flow diagram represent the flow of
- goods and the flow of services.
 - dollars and the flow of financial assets.
 - inputs and outputs and the flow of dollars.**
 - capital goods and the flow of consumer goods.

Figure 2-1



5. Refer to Figure 2-1 on the previous page. Which arrow shows the flow of goods and services?
- A
 - B**
 - C
 - D
6. Production possibilities frontiers are usually bowed outward. This is due to
- constant opportunity cost.
 - increasing opportunity cost.**
 - decreasing opportunity cost.
 - None of the above are correct.
7. Suppose an economy produces two goods, food and machines. This economy always operates on its production possibilities frontier. Last year, it produced 72 units of food and 28 machines. This year, it is producing 75 units of food and 30 machines. Which of the following would *not* explain the increase in output?
- a reduction in unemployment**
 - an increase in the labour force
 - an improvement in technology
 - All of the above are correct.
8. If an economy is producing efficiently
- there is no way to produce more of one good without producing less of the other.**
 - it is possible to produce more of both goods.
 - it is possible to produce more of one good without producing less of the other.
 - it is not possible to produce more of one good at any cost.

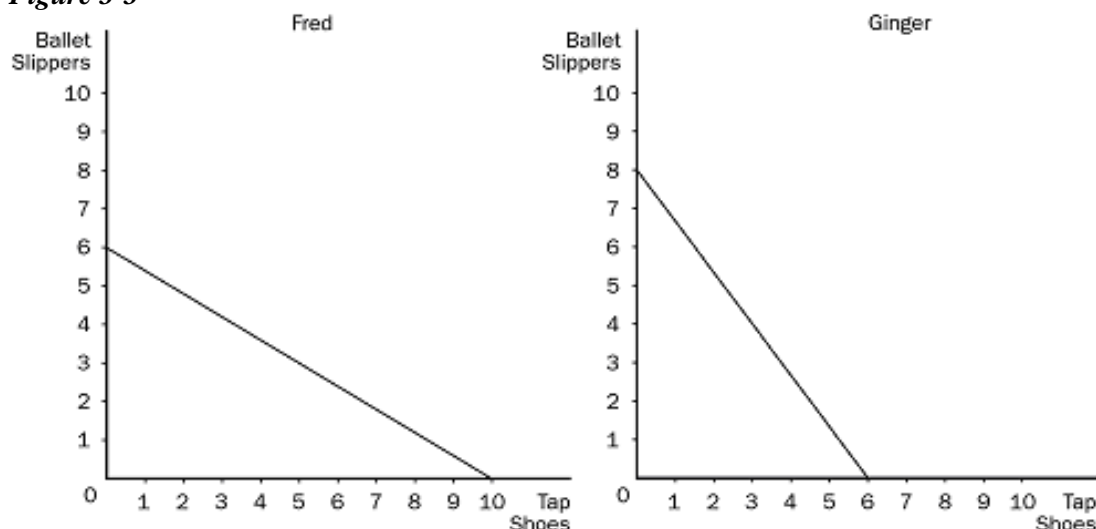
Figure 2-3

9. Refer to Figure 2-3. The economy can produce at which point or points?
- B, D, E**
 - A, B, D, E
 - D, C
 - D
 - D, E

10. Refer to Figure 2-3. Which point or points are inefficient?
- A, C
 - D, C
 - C
 - D
11. Without trade
- a country is better off because it will become self-sufficient.
 - a country's production possibilities frontier is also its consumption possibilities frontier.
 - a country can still benefit from international specialization.
 - more product variety is available in a country.
12. A country's consumption possibilities frontier can be outside its production possibilities frontier if
- additional resources become available.
 - there is an increase in the level of technology.
 - the country engages in trade.
 - All of the above are correct.
 - Both a and b are correct.
13. The difference between production possibilities frontiers that are bowed out and those that are linear is that
- bowed out production possibilities frontiers illustrate tradeoffs where linear production possibilities frontiers do not.
 - bowed out production possibilities frontiers show increasing opportunity cost where linear ones show constant opportunity cost.
 - bowed out production possibilities frontiers are the result of perfectly shiftable resources where linear production possibilities frontiers are not.
 - linear production possibilities frontiers illustrate real world conditions more than bowed out production possibilities frontiers.
 - bowed out production possibilities frontiers show decreasing opportunity cost where linear ones show constant opportunity cost.

These graphs illustrate the production possibilities available for dancing shoes to Fred and Ginger with 40 hours of labour.

Figure 3-3



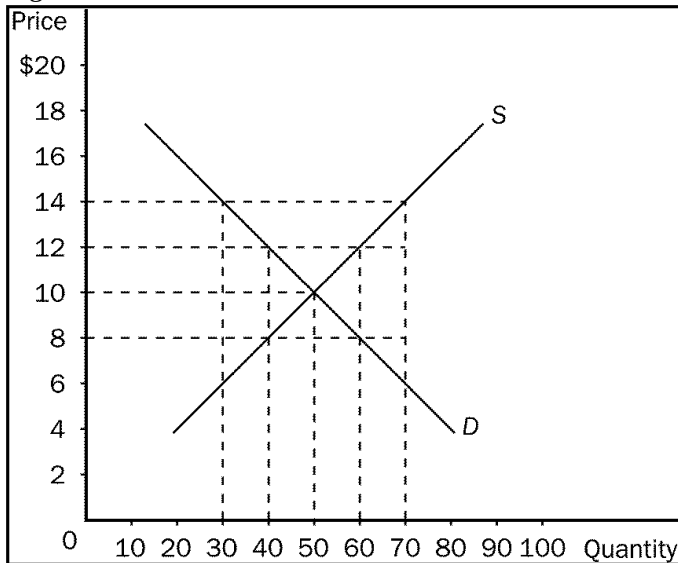
- _____ 14. **Refer to Figure 3-3.** The opportunity cost of 1 pair of tap shoes for Fred is
- 1/3 pair of ballet slippers.
 - 1/5 pair of ballet slippers.
 - 3/5 pair of ballet slippers.**
 - 5/3 pairs of ballet slippers.
- _____ 15. **Refer to Figure 3-3.** The opportunity cost of 1 pair of ballet slippers for Ginger is
- 1/4 pair of tap shoes.
 - 1/3 pair of tap shoes.
 - 3/4 pair of tap shoes.**
 - 4/3 pairs of tap shoes.
- _____ 16. **Refer to Figure 3-3.** Ginger has an absolute advantage in
- ballet slippers and Fred has an absolute advantage in tap shoes.**
 - tap shoes and Fred has an absolute advantage in ballet slippers.
 - neither good and Fred has an absolute advantage in both goods.
 - both goods and Fred has an absolute advantage in neither good.
- _____ 17. **Refer to Figure 3-3.** Ginger has a comparative advantage in
- tap shoes and Fred has a comparative advantage in ballet slippers.
 - both goods and Fred has a comparative advantage in neither good.
 - ballet slippers and Fred has a comparative advantage in tap shoes.**
 - neither good and Fred has a comparative advantage in both goods.
- _____ 18. **Refer to Figure 3-3.** If Fred and Ginger devote 1/2 of their time (20 hours) to the production of each good, total production of ballet slippers would be
- 7 and total production of tap shoes would be 8.**
 - 8 and total production of tap shoes would be 8.
 - 9 and total production of tap shoes would be 6.
 - 10 and total production of tap shoes would be 8.
- _____ 19. **Refer to Figure 3-3.** If Fred and Ginger both specialize in the good in which they have a comparative advantage, total production of ballet slippers would be
- 6 and total production of tap shoes would be 6.
 - 8 and total production of tap shoes would be 6.
 - 8 and total production of tap shoes would be 8.
 - 8 and total production of tap shoes would be 10.**

Table 3-3

	Labour Hours Needed to Make One Unit of:		Amount Produced in 24 Hours:	
	Baskets	Birdhouses	Baskets	Birdhouses
Alberta	6	2	4	12
Manitoba	3	4	8	6

- _____ 20. **Refer to Table 3-3 on the previous page.** Alberta has an absolute advantage in
- a. **birdhouses and Manitoba has an absolute advantage in baskets.**
 - b. baskets and Manitoba has an absolute advantage in birdhouses.
 - c. neither good and Manitoba has an absolute advantage in both goods.
 - d. both goods and Manitoba has an absolute advantage in neither good.
- _____ 21. **Refer to Table 3-3.** Alberta has a comparative advantage in
- a. baskets and Manitoba has a comparative advantage in birdhouses.
 - b. **birdhouses and Manitoba has a comparative advantage in baskets.**
 - c. neither good and Manitoba has a comparative advantage in both goods.
 - d. both goods and Manitoba has a comparative advantage in neither good.
- _____ 22. Which of the following demonstrates the law of demand?
- a. Jon buys more pretzels at \$1.50 each since he got a \$1 raise at work.
 - b. Melissa buys fewer muffins at \$0.75 each than at \$1 each.
 - c. **Dave buys more donuts at \$0.25 each than at \$0.50 each.**
 - d. Kendra buys fewer Snickers at \$0.60 each since the price of Milky Ways fell to \$0.50 each.
- _____ 23. If Francis receives a decrease in his pay, we would expect
- a. Francis's demand for each good he purchases to remain unchanged.
 - b. Francis's demand for normal goods to increase.
 - c. Francis's demand for luxury goods to increase.
 - d. **Francis's demand for inferior goods to increase.**
- _____ 24. If the price of a substitute to good X increases, then the
- a. demand for good X will decrease.
 - b. market price of good X will decrease.
 - c. **demand for good X will increase.**
 - d. quantity demanded for good X will increase.
- _____ 25. Two goods are complements if a decrease in the price of one good
- a. increases the quantity demanded of the other good.
 - b. reduces the demand for the other good.
 - c. reduces the quantity demanded of the other good.
 - d. **raises the demand for the other good.**
- _____ 26. You love peanut butter. You hear on the news that 50 % of the peanut crop in the South has been wiped out, which will cause the price to double by the end of the year. As a result,
- a. your demand for peanut butter will increase by the end of the year.
 - b. **your demand for peanut butter increases today.**
 - c. your demand for peanut butter falls as you look for a substitute good.
 - d. you decide to give up peanut butter completely.
- _____ 27. Which of the following cause and effect events is in order for a seller?
- a. Technology improves, profit falls, the supply curve shifts left.
 - b. **An input price falls, profit increases, the supply curve shifts right.**
 - c. An input price rises, profit falls, the supply curve shifts right.
 - d. An input price rises, profit rises, the supply curve shifts left.

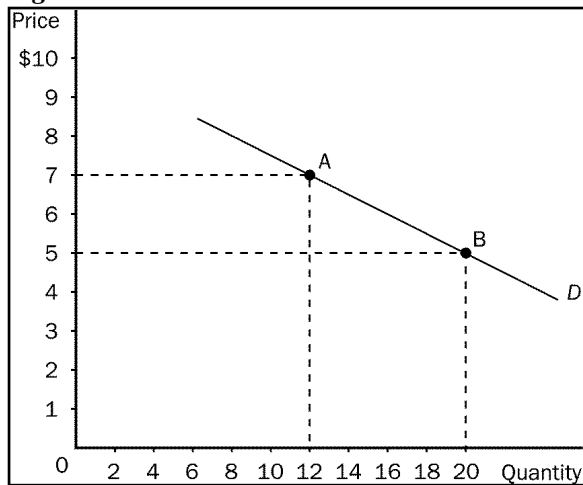
Figure 4-8



28. Refer to Figure 4-8 on the previous page. If price in this market is currently \$14, there would be a
- shortage of 20 units and price would tend to rise.
 - surplus of 20 units and price would tend to fall.
 - shortage of 40 units and price would tend to rise.
 - surplus of 40 units and price would tend to fall.
29. A decrease in resource costs to firms in a market will result in
- a decrease in equilibrium price and an increase in equilibrium quantity.
 - a decrease in equilibrium price and a decrease in equilibrium quantity.
 - an increase in equilibrium price and no change in equilibrium quantity.
 - an increase in equilibrium price and an increase in equilibrium quantity.
30. Suppose that the incomes of buyers in a particular market for a normal good decrease and there is also a reduction in input prices. What would we expect to occur in this market?
- The equilibrium price would increase, but the impact on the amount sold in the market would be ambiguous.
 - The equilibrium price would decrease, but the impact on the amount sold in the market would be ambiguous.
 - Both equilibrium price and equilibrium quantity would increase.
 - Equilibrium quantity would increase, but the impact on equilibrium price would be ambiguous.
 - None of the above is correct.
31. Barb's Bakery made \$200 last month selling 100 loaves of bread. This month it made \$300 selling 60 loaves of bread. The price elasticity of demand for Barb's bread is
- 0.266.
 - 0.583.
 - 0.642
 - 1.11.
 - 1.25.

32. When demand is inelastic, a decrease in price will cause
- an increase in total revenue.
 - a decrease in total revenue.
 - no change in total revenue.
 - There is insufficient information to answer this question.
33. Moving up a linear demand curve, we know that total revenue
- increases, then decreases.
 - decreases, then increases.
 - increases.
 - decreases.
34. When demand is elastic in the current price range,
- an increase in price would increase total revenue because the decrease in quantity demanded is less than the increase in price.
 - an increase in price would decrease total revenue because the decrease in quantity demanded is greater than the increase in price.
 - a decrease in price would decrease total revenue because the increase in quantity demanded is smaller than the decrease in price.
 - a decrease in price would not affect the total revenue.

Figure 5-8



35. Refer to Figure 5-8. Between point A and point B we know that
- the slope is equal to $1/4$ and elasticity is equal to $2/3$.
 - the slope is equal to $1/4$ and elasticity is equal to $3/2$.
 - the slope is equal to $3/2$ and elasticity is equal to $1/4$.
 - the slope is equal to $2/3$ and elasticity is equal to $1/4$.
 - the slope is equal to 4 and elasticity is equal to $3/2$.
36. Market demand is $Q_d = 400 - 4P$ and market supply is $Q_s = 2P - 14$. In equilibrium,
- $P = \$69, Q = 124$
 - $P = \$124, Q = 69$
 - $P = \$64, Q = 143$
 - $P = \$143, Q = 64$

- _____ 37. Market demand is $Q_d = 400 - 4P$ and market supply is $Q_s = 2P - 14$. A market analyst is investigating what happens if market price was \$50 and increased to \$55. The analyst concludes that in this price range, the elasticity of demand is
- a. .9
b. 1.1
c. 4.0
d. .25
- _____ 38. Market demand is $Q_d = 400 - 4P$ and market supply is $Q_s = 2P - 14$. Suppose the market price is currently \$70. What is producer surplus?
- a. \$4340
b. \$4020
c. \$3960
d. \$3780
- _____ 39. Market demand is $Q_d = 400 - 4P$ and market supply is $Q_s = 2P - 14$. Suppose the market price is currently \$50. What is the deadweight loss in total surplus?
- a. \$541.50
b. \$1083.00
c. \$361.00
d. \$180.50
- _____ 40. Market demand is $Q_d = 400 - 4P$ and market supply is $Q_s = 2P - 14$. If the price was \$50, what should sellers do if they want to increase total revenue?
- a. Increase the price
b. Decrease the price
c. Leave the price alone. TR is at a maximum.
d. Not enough information to decide.
- _____ 41. BONUS: Which of these people is one of the TAs for this course?
- a. Robert
b. Rebecca
c. Renata
d. Rudy