

Economics 2  
Winter 2005

your name \_\_\_\_\_  
your TA's name \_\_\_\_\_  
day and time of your discussion section \_\_\_\_\_

PRACTICE FIRST EXAM

**DIRECTIONS:** No calculators, books, or notes of any kind are allowed. All papers and notebooks must remain closed and on the floor at all times throughout the exam, and students are not allowed to leave the examination room until finished. Answer all questions in the space provided with the exam. 115 points are possible on this exam.

**HINTS:** Feel free to use either of the following formulas if you find them useful.

Area of a triangle =  $(1/2)$  (base) (height)

Area of a trapezoid =  $(1/2)$  (base1 + base2) (height)

**PART I: MULTIPLE CHOICE**—circle the correct answer (4 points each, 80 points total)

- 1.) A subsidy on an item tends to result in
  - a.) an increase in the price paid by buyers and an increase in the price received by sellers
  - b.) a decrease in the price paid by buyers and a decrease in the price received by sellers
  - c.) a decrease in the price paid by buyers and an increase in the price received by sellers
  - d.) an increase in the price paid by buyers and a decrease in the price received by sellers
  
- 2.) Which of the following is not an example of the economic waste caused by a price ceiling?
  - a.) there are some consumers who are willing to pay more than the marginal cost of producing the good but are unable to receive it
  - b.) some of the consumers who receive the good may value it less than some of the consumers who do not receive the good
  - c.) the marginal benefit of giving the good to another consumer is less than the marginal cost of producing the good
  - d.) shortages will prompt buyers to take costly actions to increase their chances of receiving the good
  
- 3.) Which of the following characterizes the choice made by a price-taking, profit-maximizing firm operating in an environment of perfect competition?
  - a.) average revenue = marginal cost
  - b.) average revenue = average cost
  - c.) marginal cost = average cost
  - d.) average cost = marginal revenue
  
- 4.) Let  $Q_n$  be the level of output that would be produced if we wanted to maximize the sum of consumer plus producer surplus. Let  $Q_m$  be the level of output that will be produced by a perfectly price-discriminating monopolist. Then
  - a.)  $Q_n$  is larger than  $Q_m$
  - b.)  $Q_n$  is equal to  $Q_m$
  - c.)  $Q_n$  is smaller than  $Q_m$
  - d.)  $Q_n$  could be larger or smaller than  $Q_m$ , depending on the elasticities

- 5.) The incentive for a firm to “cheat” on a cartel arises from
- a.) the firm’s desire to produce at a point where its average cost is below the cartel price
  - b.) the fact that the firm’s marginal revenue from producing one more unit exceeds the marginal revenue of the cartel as a whole
  - c.) the firm’s desire to lower the price the cartel has agreed to charge
  - d.) the firm’s desire to raise the price the cartel has agreed to charge
- 6.) Which of the following could not be an explanation of where monopoly power comes from?
- a.) network externalities
  - b.) the existence of high fixed costs
  - c.) government restrictions on the ability of new producers to enter the market
  - d.) a government-imposed price ceiling
- 7.) Production is said to exhibit increasing returns to scale if
- a.) doubling the scale of production more than doubles the average cost per unit
  - b.) doubling the scale of production exactly doubles the average cost per unit
  - c.) doubling the scale of production produces no change in the average cost per unit
  - d.) doubling the scale of production leads to a decrease in the average cost per unit

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PART II: FILL IN THE BLANK (33 points total)—credit for correct answer only (no partial credit)  
For sample problems see problem sets 1 and 2.

ANSWERS:

1c, 2c, 3a, 4b, 5b, 6d, 7d