

Exam 3 Practice Questions

1. The price elasticity of demand is a measure of:
 - a) how quickly a particular market reaches equilibrium.
 - b) the change in supply associated with lower prices.
 - c) the percent change in sales associated with the percent change in price.
 - d) the effect of an increase in the number of consumers in a particular market.
 - e) the fat that is removed during a liposuction operation.
2. If each 5 percent increase in the price of gasoline reduces by 2 percent the quantity purchased, the price elasticity of demand for gasoline is:
 - a) - 0.4
 - b) - 2.0
 - c) - 2.5
 - d) - 5.0
3. If at a price of \$10 the quantity demanded of azuzapops is 400 per day, and at \$20 the quantity demanded is 300 per day, then the mid-point price elasticity of demand for azuzapops is approximately:
 - a) -0.28
 - b) -0.42
 - c) -0.67
 - d) -2.40
4. The demand for salt is probably more inelastic than the demand for potatoes because:
 - a) potatoes require salt but salt does not require potatoes.
 - b) salt will keep longer than potatoes before spoiling.
 - c) there is so much potential salt in the ocean.
 - d) salt is cheap relative to most users' incomes and has few good substitutes.
5. The Illinois Central Railroad once asked the Illinois Commerce Commission for permission to increase its consumer rates by 20%. The RR argued that declining revenues made this rate increase essential. Opponents of the rate increase contended that the RR's revenue would fall because of the rate hike. It can be concluded that:
 - a) both groups felt that the demand was elastic.
 - b) both groups felt that the demand was inelastic.
 - c) the RR felt demand for passenger service was inelastic and opponents of the rate increase felt it was elastic.
 - d) the RR felt that demand for passenger service was elastic and opponents of the rate increase felt it was inelastic.
 - e) come on, Dr. D, do you really expect me to know this?
6. Which of the following goods would be expected to have the highest price elasticity of demand?
 - a) liquids.
 - b) soft drinks.
 - c) Mountain Dew.
 - d) sodas (pop)
7. Which of the following characteristics of a product tend to make the elasticity of demand greater?
 - a) the product is a necessity.
 - b) the time period is relatively short.
 - c) the product is relatively expensive.
 - d) there are no good substitutes for the product.
 - e) (a), (b), and (c).

8. Suppose you are in charge of pricing at Apple Computer and you wish to increase revenues from your Macintosh line. Apple's chief economist informs you that the price elasticity of demand for Macintoshes is estimated to be $E = -1.17$.

Based on this information, you would:

- a) increase price.
- b) decrease price.
- c) not change price.
- d) not enough information to make a rational decision.

9. If Marietta College theatre department increases ticket prices for its performances and we observe that total ticket revenue decreases, we can conclude that:

- a) performances are price elastic.
- b) performances are price inelastic.
- c) performances are unitary price elastic.
- d) performances are an inferior good.
- e) performances are a normal good.

10. When the price of milk rose 50% the quantity of milk sold fell 25% and the sale of breakfast cereal also fell 25%. This set of facts indicates that:

- a) the demand for milk is price elastic.
- b) the demand for breakfast cereals is price elastic.
- c) the cross price elasticity between milk and cereal is negative so the two are complements.
- d) the cross price elasticity between milk and cereal is positive so the two are complements.

11. A price floor will cause a larger surplus when demand is _____ and supply is _____.

- a) elastic; inelastic
- b) inelastic; inelastic
- c) elastic; elastic
- d) perfectly inelastic; elastic

12. In calculating the marginal productivity of a factor of production:

- a. that factor and all other factors must be held constant.
- b. that factor must be held constant and the other factors varied.
- c. the other factors may, but need not be varied.
- d. the other factors must be held constant.
- e. none of the above.

13. Marginal costs:

- a. rises for a time, but then begins to decline when the point of diminishing returns is reached.
- b. is defined as the difference between total total and average variable costs.
- c. increases so long as output falls.
- d. cuts both the average variable cost and the average total cost curves at their minimum point.
- e. cuts both the average total cost and the average variable cost curves at their maximum point.

14. The law of diminishing returns states that if increasing quantities of a variable input are applied to a given quantity of fixed inputs,

- a. the marginal product will eventually decrease with average product remaining constant.
- b. the marginal product becomes negative.
- c. the total product cannot be increased.
- d. the marginal product of the variable factor will eventually decrease.

15. Diseconomies of scale to a firm are shown graphically by:
- a downward-sloping long-run average cost curve.
 - a horizontal long-run average cost curve.
 - a downward-sloping marginal cost curve.
 - an upward-sloping long-run average cost curve.
 - an upward-sloping short-run average cost curve.
16. Which of the following statements about the relationship between marginal product and average product is correct?
- When MP is falling, AP is falling.
 - AP equals MP at MP's maximum point.
 - When MP exceeds AP, AP must be rising.
 - When AP exceeds MP, MP must be rising.
 - AP equals MP at AP's minimum point.
17. Fixed costs:
- are the variable costs of the firm.
 - are sunk into unprofitable investments.
 - are the difference between profits and losses.
 - should not affect short-run decision making.
 - none of the above.
18. A firm has chosen its profit maximizing level of output. At this level of output, its price is \$20 and its ATC is \$25. The firm:
- has made a mistake; it should have shut down.
 - is making a loss of \$20 per unit of output.
 - is making a profit of \$5 per unit of output.
 - has not made a mistake as long as AVC is less than \$20.
 - none of the above.
19. In the short-run, the profit-maximizing behavior for a price-taking firm requires it to operate where:
- $P = \text{minimum ATC} = \text{AVC}$
 - $P = \text{ATC and AVC} = \text{MC}$
 - $P > \text{ATC and } P = \text{MC}$
 - $P > \text{AVC and } P = \text{MC}$
 - $P = \text{MR} = \text{MC} = \text{AVC}$
20. The long-run result of producing where $P = \text{MC}$ in an industry where there is free entry and exit is:
- inefficient production.
 - zero economic profit.
 - negative economic profit.
 - positive economic profit.
 - not enough information to tell.
21. In a perfectly competitive industry, the market price of the product is \$12. Firm A is producing the output at which average total cost equals marginal cost, both of which are \$10. To maximize its profits, Firm A should:
- increase output
 - reduce output
 - leave output unchanged
 - increase its selling price
 - decrease its selling price

22. When a representative firm in a competitive industry is making economic profits:
- accounting profits may be zero.
 - new firms will enter and drive the equilibrium price down.
 - old firms will exit and drive the equilibrium price up.
 - new firms will enter and drive the equilibrium price up.
 - the government will tax the firm and redistribute the revenues to the upper and middle classes.
23. The short run supply curve for a firm in a perfectly competitive market:
- depends on the industry's supply curve.
 - is the marginal cost curve above minimum average total cost.
 - is the marginal cost curve above minimum average variable cost.
 - depends on the industry's demand curve.
 - is non-existent.

For the following question use the data below.

Output	Total Cost
0	\$40
1	48
2	57
3	70
4	88
5	110
6	140
7	200

24. If the product's price is \$10, the firm:
- should not shut down.
 - should leave the business permanently.
 - should shut down.
 - can make a profit.
 - not enough information to tell.

For the following question use the data below.

Output	VC	AVC
1	\$5	\$5
2	8	4
3	12	4
4	20	5
5	30	6
6	48	8

25. If this firm could sell all it wanted to at a price of \$8 per unit, it should produce:
- no output.
 - 3 units.
 - 4 units.
 - 5 units.
 - 6 units.

Questions 26 - 27 refer to the table below:

Fixed Input	Variable Input	Output
2	0	0
2	1	10
2	2	22
2	3	33
2	4	40
2	5	45
2	6	48

26. What is the average product of two units of the variable input?
- a) 3.67
 - b) 11
 - c) 12
 - d) 16
 - e) 22
27. What is the marginal product of the fifth unit of variable input?
- a) 45
 - b) 9
 - c) 5
 - d) 22.5
 - e) 3
28. Assume that 1 worker produces 6 units of output, 2 workers produce 14 units, 3 produce 20 units, and 4 produce 24 units. If the cost is \$20 per unit of labor and fixed costs are \$100, the average fixed costs at 24 units of output is:
- a) \$100
 - b) \$4.17
 - c) \$5
 - d) \$3.33
 - e) \$180
29. From the information in #17, what is the total cost of 20 units of output?
- a) \$100
 - b) \$60
 - c) \$160
 - d) \$40
 - e) not enough information to determine.
30. To say that a firm is a price taker means that:
- a) the government dictates the price.
 - b) the firm cannot influence the price.
 - c) only the firm can determine the price.
 - d) the firm must advertise in order to sell more of its output.
 - e) the only real decision that the firm makes is whether or not to advertise.
31. In a purely competitive situation, the demand curve facing the firm is:
- a) identical to the market demand curve.
 - b) perfectly inelastic even though the market demand is not.
 - c) negatively sloped regardless of the market demand curve.
 - d) perfectly elastic even though the market demand is not.