

Exam 3 Sample 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.
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. A men's tie store sold an average of 30 ties per day when the price was \$5 per tie but sold 50 of the same ties per day when the price was \$3 per tie. The absolute value of the price elasticity of demand, using the midpoint method, is:

- a) greater than zero but less than 1
- b) equal to 1
- c) greater than 1 but less than 3
- d) greater than 3

13. A major state university in the South recently raised tuition by 12%. An economics professor at this university asked his students, "Due to the increase in tuition, how many of you will transfer to another university?" One student out of about 300 said that he or she would transfer. Based on this information, the price elasticity of demand for education at this university is:

- a) 1.
- b) highly elastic
- c) highly inelastic
- d) 0

14. If the estimated price elasticity of demand for foreign travel is 4, then:

- a) a 20% decrease in the price of foreign travel will increase quantity demanded by 80%.
- b) demand for foreign travel is inelastic.
- c) a 10% increase in the price of foreign travel will increase quantity demanded by 40%
- d) a 20% increase in the price of foreign travel will increase quantity demanded by 80%.

15. The price elasticity of demand for gasoline in the short run has been estimated to be 0.4. If a war in the Middle East causes the price of oil (from which gasoline is made) to increase, how will that affect total revenue from gasoline in the short run, all other things unchanged?
- Quantity demanded will stay the same; total revenue will fall
 - Quantity demanded will decrease; total revenue will rise.
 - Total revenue will remain unchanged.
 - Demand will not change; total revenue will rise.
16. A newspaper typically consumes a smaller fraction of a consumer's budget than a home entertainment system. Therefore, you would expect the demand for:
- a home entertainment system to be more price-elastic.
 - a home entertainment system to be more price-inelastic.
 - newspapers to be more price-elastic.
 - both to be equally price-elastic.
17. Suppose the cross-price elasticity between demand for Burger King burgers and the price of McDonald's burgers is 0.8. If McDonald's increases the price of its burgers by 10%, then:
- Burger King will sell 10% more burgers.
 - Burger King will sell 8% more burgers.
 - Burger King will sell 8% fewer burgers.
 - We cannot tell what will happen to Burger King, but McDonald's will sell 8% fewer burgers.
18. Suppose you manage a convenience mart and are in charge of ordering products but do not set the price. The home office provides the prices. In your area, the income elasticity of demand for peanut butter is -0.5 . Due to local factory closings, you expect local incomes to decrease by 20%, on average, in the next month. As a result, you should stock:
- 20% more peanut butter on the shelves.
 - 5% more peanut butter on the shelves.
 - 10% more peanut butter on the shelves.
 - 10% less peanut butter on the shelves.
19. Eric's income increased from \$40,000 to \$50,000 per year. Eric's consumption of tickets to pro football games increased from 2 to 4 per year. Using the midpoint formula, his income elasticity of demand for pro football game tickets is equal to _____ and football game tickets are _____ goods.
- $-\frac{1}{3}$; inferior
 - $+\frac{2}{3}$; normal
 - 3; inferior
 - +3; normal
20. The pair of items that is most likely to have a negative cross-price elasticity of demand is:
- aspirin and hamburgers.
 - hot dogs and mustard
 - margarine and butter.
 - ketchup and coffee.
21. Suppose the government decides to fight obesity in America by imposing an excise tax on the saturated fat content of food. The effect of this tax would be to:
- lower the profits of ice cream suppliers.
 - decrease revenue for the government.
 - decrease black market activity.
 - raise the profits of ice cream suppliers.

22. An excise tax collected from the producers of a good:
- shifts the supply curve upward.
 - creates a loss of revenue for the government.
 - has a similar effect as a tax subsidy.
 - shifts the supply curve downward.
23. By law, FICA (the Federal Insurance Contributions Act), a payroll tax, is collected equally from the employers and the employees. In reality:
- the law works—both the employers and the employees bear half the burden of the tax.
 - the employees bear almost all the burden of the tax
 - the employers bear almost all the burden of the tax.
 - it's impossible to determine who bears the burden of the tax.

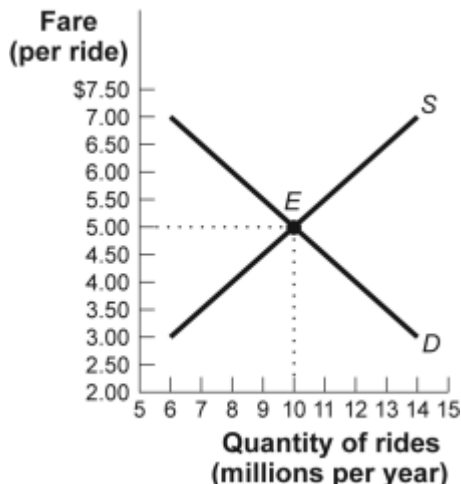
Table: Market for Fried Twinkies

Market for Fried Twinkies		
Price (unit)	Quantity Demanded (units)	Quantity Supplied (units)
\$1.10	9,000	3,000
1.20	8,000	5,000
1.30	7,000	7,000
1.40	6,000	9,000
1.50	5,000	11,000

24. The government decides to tax fried Twinkies at a rate of \$0.30 per Twinkie and collect that tax from the producers. Using the table above, the consumers will pay _____ per Twinkie and buy _____ Twinkies after the tax.
- \$1.20; 8,000
 - \$1.30; 7,000
 - \$1.40; 6,000
 - \$1.50; 5,000
25. From the table above, of the \$0.30 tax per fried Twinkie, consumers actually pay _____, while producers actually pay _____.
- \$0.30; \$0.00
 - \$0.15; \$0.15
 - \$0.20; \$0.10
 - \$0.00; \$0.30
26. From the table above, as a result of the \$0.30 tax per fried Twinkie, the government will receive total tax revenue of:
- \$500
 - \$1,000
 - \$1,500.
 - The total is impossible to calculate.
27. Suppose the government imposes a \$4 excise tax on Good X. If the demand for Good X is perfectly elastic and the supply curve is elastic, then the price of Good X will:
- increase by more than \$4.
 - increase by exactly \$4
 - increase, but by less than \$4
 - remain constant.

28. Suppose the government imposes a \$4 excise tax on Good Y. If the demand for Good Y is perfectly inelastic and the supply curve is elastic, then the price of Good Y will:

- a) increase by more than \$4.
- b) increase by exactly
- c) increase, but by less than \$4.
- d) remain constant.



29. The figure above represents a competitive market for taxi rides. If the government now imposes an excise tax of \$4 per ride (causing the supply curve to shift upward by that amount), then the government will collect tax revenues of _____, which might be used for worthwhile purposes. However, there will be an excess burden (or deadweight loss) to society of _____ caused by this tax.

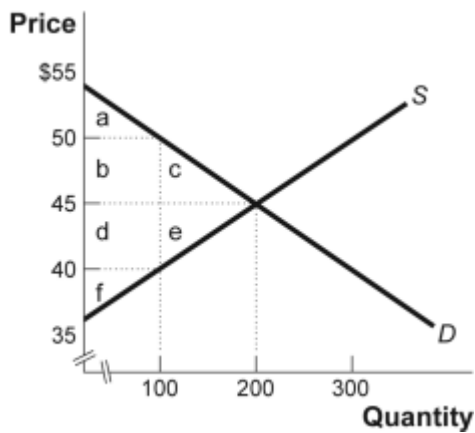
- a) \$9 million; \$1 million
- b) \$16 million; \$2 million
- c) \$21 million; \$6 million
- d) \$24 million; \$8 million

30. The number of seats in a football stadium is fixed at 70,000. The city decides to impose a ticket tax of \$10 per ticket. In response, the team management raises the ticket price from \$30 to \$40 and still sells all 70,000 tickets. The tax caused a change in the consumer surplus of _____, a change in the producer surplus of _____, and a deadweight loss of _____.

- a) -\$10; \$0; \$10
- b) -\$700,000; \$0; \$700,000
- c) -\$10; \$0; \$0
- d) -\$700,000; \$0; \$0

31. The 1990 “yacht tax” caused a large deadweight loss, because demand for luxury yachts made in the United States is:

- a) very elastic.
- b) very inelastic.
- c) perfectly inelastic since “rich” people will pay whatever is necessary.
- d) perfectly elastic.



32. The government recently levied a \$10 tax on the producers of blue jeans. Using the graph above, identify the area(s) that represent the loss of consumer surplus due to the tax.

- a) c
- b) b+c
- c) b
- d) a+b+c

33. If tax efficiency is the only goal, a tax system should be designed to minimize its:

- a) deadweight loss
- b) administrative costs
- c) impact on the poor
- d) deadweight loss and its administrative costs

34. A lump-sum tax, such as the fee for a driver's license, does not take into consideration:

- a) efficiency.
- b) the benefits principle.
- c) the ability-to-pay principle.
- d) the tax base.

35. Which of the following situations provides an example of the benefits principle?

- a) Employed workers pay taxes that are used to fund technical training programs.
- b) Revenue from the federal tax on gasoline is used to maintain and improve the interstate highway system.
- c) Most of the revenue from property taxes is used to fund public schools. The taxes are paid by all homeowners.
- d) Taxes on cigarettes are used to pay state employees' salaries.

36. The richest 20% of families in the United States pay a much _____ share of total income taxes collected and a _____ share of total payroll taxes than their share of total income.

- a) higher; lower
- b) lower; higher
- c) higher; higher
- d) lower; lower

37. The two most important sources of federal tax revenue are the:

- a) payroll and income taxes.
- b) corporate income and payroll taxes.
- c) excise and income taxes.
- d) Social Security and excise taxes.

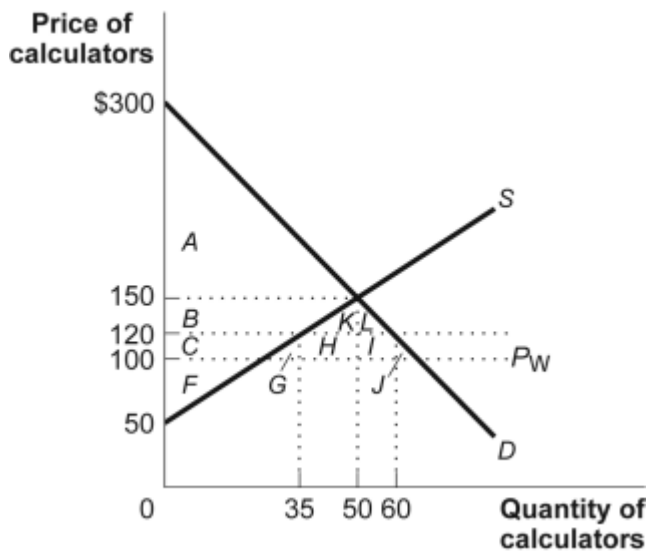
38. State and local taxes tend to be _____ and federal taxes tend to be _____
- a) regressive; regressive
 - b) progressive; regressive
 - c) progressive; progressive
 - d) regressive; progressive
39. Paying a tax of \$10 on an income of \$100, a tax of \$25 on an income of \$200, and a tax of \$60 on an income of \$300 is an example of a:
- a) progressive tax.
 - b) proportional tax.
 - c) regressive tax.
 - d) flat tax.
40. In Eastlandia, personal income up to and including \$25,000 is not taxed, income greater than \$25,000 and less than or equal to \$50,000 is taxed at a rate of 10%, and income over \$50,000 is taxed at a rate of 20%. A family earning income equal to \$75,000 in Eastlandia will pay _____ in personal taxes.
- a) \$6,000
 - b) \$7,500
 - c) \$11,250
 - d) \$15,000
41. In Westlandia, personal income up to and including \$30,000 is not taxed, income greater than \$30,000 and less than or equal to \$60,000 is taxed at a rate of 10%, and income over \$60,000 is taxed at a rate of 25%. A family earning income equal to \$100,000 in Westlandia will pay an average tax rate of:
- a) 5%.
 - b) 10%.
 - c) 13%.
 - d) 25%.
42. In the United States, over the last 40 years, as a percentage of gross domestic product:
- a) exports have grown.
 - b) imports have grown.
 - c) exports have decreased.
 - d) exports and imports have grown.
43. In a single growing season, the country of Pastoral can raise 100 tons of beef or produce 1,000 boxes of tulips. In the same growing season, the country of Bucolic can raise 50 tons of beef or produce 750 boxes of tulips. In autarky the price of beef:
- a) is higher in Pastoral than in Bucolic.
 - b) is lower in Pastoral than in Bucolic.
 - c) is the same in Pastoral as in Bucolic.
 - d) cannot be determined in either country.
44. In a single growing season, the country of Pastoral can raise 100 tons of beef or produce 1,000 boxes of tulips. In the same growing season, the country of Bucolic can raise 50 tons of beef or produce 750 boxes of tulips. At which of the prices below will trade occur between the two countries?
- a) One ton of beef costs 20 boxes of tulips.
 - b) One ton of beef costs 5 boxes of tulips
 - c) One ton of beef costs 12 boxes of tulips.
 - d) One ton of beef costs 8 boxes of tulips.

Table: Production Possibilities for Machinery and Petroleum

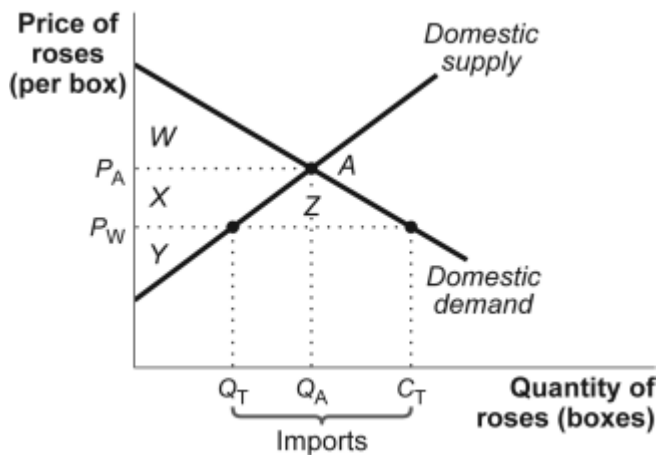
The table shows the maximum amounts of machinery and petroleum that the United States and Mexico can produce if they only produce one good. Both nations face constant costs of production.

Countries	Machinery (units)	Petroleum (units)
United States	80	40
Mexico	60	180

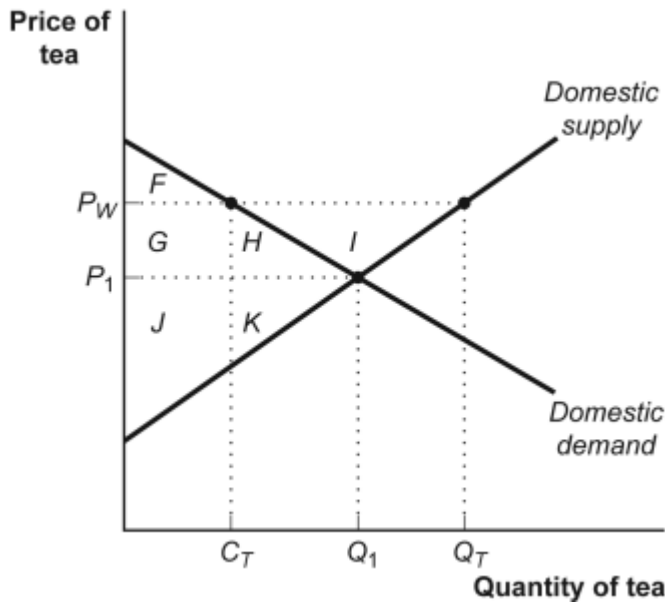
45. Consider the table above. Which of the following is true?
- a) The opportunity cost of petroleum is less in the United States than in Mexico.
 - b) The opportunity cost of petroleum is more in the United States than in Mexico.
 - c) Petroleum costs are the same in the United States and in Mexico.
 - d) Machinery costs are the same in the United States and in Mexico.
46. Consider the table above. The opportunity cost in the United States of producing 30 units of petroleum is _____ units of machinery.
- a) 60
 - b) 80
 - c) 100
 - d) 120
47. Consider the table above. Both the United States and Mexico will gain from trade if one unit of machinery trades for _____ of petroleum.
- a) 2 units
 - b) 4 units
 - c) 6 units
 - d) 8 units
48. In the market for wooden furniture, if a country's price in the absence of trade is lower than the price with trade, the country must:
- a) import wooden furniture.
 - b) export wooden furniture.
 - c) have absolute advantage in wooden furniture production.
 - d) have a surplus of wooden furniture.
49. The main difference between a tariff and a quota is:
- a) a quota reduces imports more sharply than a tariff.
 - b) a tariff will cause higher prices than a quota.
 - c) a tariff generates tax revenue for the government, while a quota generates rents to the license-holders.
 - d) a tariff will cause lower prices than a quota.
50. If a country removes a tariff on imported shoes, we expect the domestic price of shoes to _____ and the quantity of shoes consumed in the domestic market to _____ .
- a) fall; fall
 - b) fall; rise
 - c) rise; fall
 - d) rise; rise



51. The figure above shows the domestic supply and demand curves for calculators. The world price, P_W , equals \$100. The government imposes a quota restricting imports to 25 calculators. The domestic price rises to _____ and the quota rent is equal to area _____.
- \$120; $K + L$
 - \$150; $K + H + I + L$
 - \$120; $H + I$
 - \$150; $G + H + I + J$



52. In the figure above, consumer surplus without international trade would be area(s):
- $W + X + Y$.
 - Z .
 - $W + X + Z$.
 - W .
53. In the figure above, consumer surplus with international trade would be area(s):
- $W + X + Y$.
 - Z .
 - $W + X + Z$.
 - W .



54. In autarky, the price of tea in Northlandia is P_1 . Consumer surplus equals _____ and producer surplus equals _____.

- a) $F + G + H + I; J + K$
- b) $F; G + H + I + J + K$
- c) $F + I; J + K$
- d) $F + G + H; J + K$

55. Many countries engage in trade protection by imposing import tariffs or quotas for at least some goods. This is because:

- a) economists have established that such restrictions are welfare-improving for certain categories of goods (such as raw materials).
- b) such restrictions tend to benefit consumers without harming producers.
- c) while such restrictions harm consumers, they benefit producers who are usually a more cohesive and politically influential group.
- d) while such restrictions harm consumers and benefit producers, the losses to consumers are outweighed by the gains to producers

56. Which statement is *not* true about the World Trade Organization (WTO)?

- a) The WTO provides the framework for complex negotiations involved in major international trade agreements.
- b) The WTO resolves disputes between member countries.
- c) The WTO is an international organization.
- d) The WTO is a direct enforcer of trade agreements.

57. If the executives of the U.S. silicon-chip industry lobby Congress for protection from imports on the grounds that theirs is a new industry that needs time to develop technological efficiency, they are using the:

- a) environmental standards argument.
- b) infant industry argument.
- c) cheap foreign labor argument.
- d) national security argument.