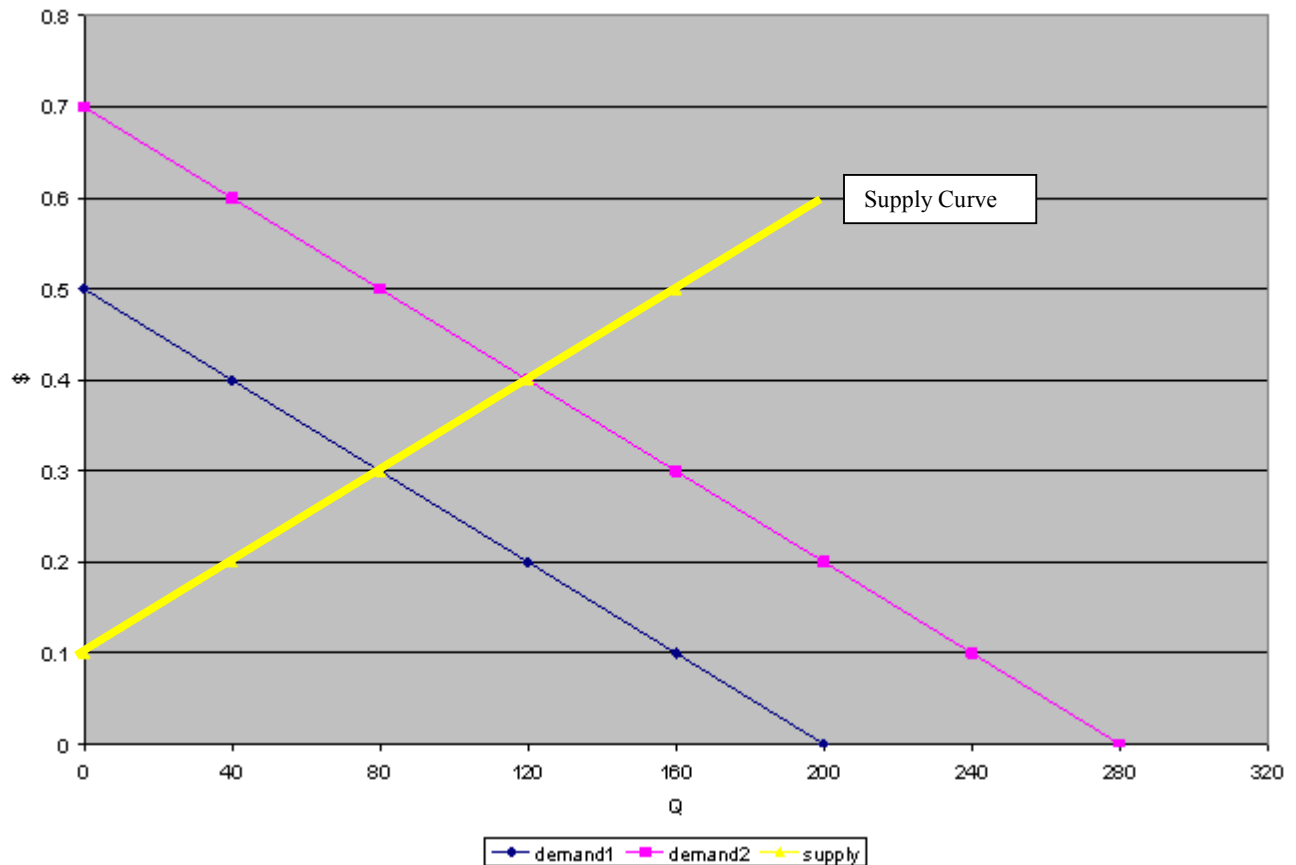


This guide to the answers is based on Version 1 of the Midterm Exam. Version 2 is the same questions in a different order

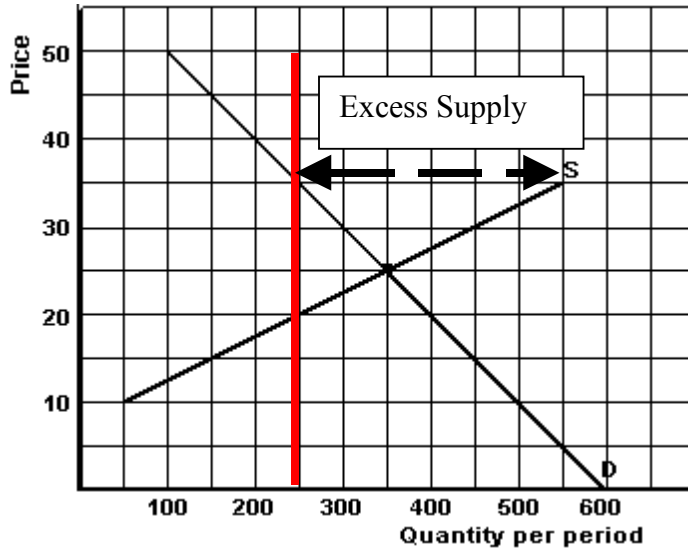
1. The market demand is obtained by:
  - A) adding the difference between supply and demand at each price for each individual.
  - B) taking the vertical sum of individual demands.
  - C) taking the horizontal sum of individual demands. At each price how much will each buyer wish to buy...add those up at that price
  - D) none of the above.
  
2. All of the following statements are **false** except:
  - A) In positive economics, personal values do not enter the analysis and description of economic events. True, positive statements are value neutral.
  - B) "The Canadian unemployment rate for September, 2008 was 6.1 percent" is a normative statement. No, statements based on statistical information are "positive"
  - C) "The government should provide a minimum income to every citizen" is a positive statement. No. Normative "value based" use of the term "should"
  - D) Normative economic statements are statements of fact. No. Reverse is true.

Use the following to answer question 3:



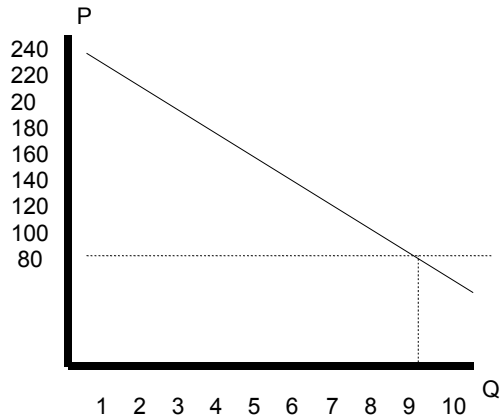
3. In figure 3.2, it is **not** the case (not true) that:
- A) the new equilibrium price is \$0.40. <True
  - B) quantity supplied increased. <True
  - C) supply has not changed. <True
  - D) supply has increased. <Not True

Use the following to answer question 4:

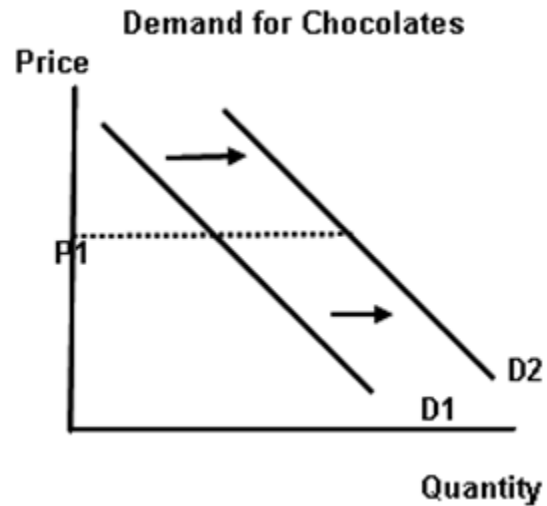
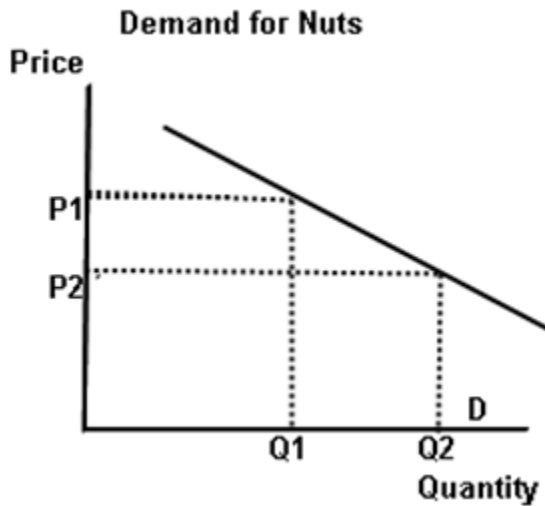


4. In figure 3.9, what would be the result if the government imposes a quota of 250 units in this market? (*Hard question!*)
- A) There would be a shortage of 150 units.
  - B) There would be no shortage. Price rises to \$35 and there would be excess supply
  - C) There would be a shortage of 100 units.
  - D) There would be a shortage of 200 units.
5. Suppose that Veronica is prepared to pay a maximum of \$2.40 for her first glass of fruit juice, but for each subsequent glass she is only prepared to pay 20 cents less than the previous one. If the price of juice is 80 cents per glass, how many glasses will she purchase? (*Draw a diagram to help answer this*)
- A) 10 glasses.
  - B) 3 glasses.
  - C) 8 glasses.
  - D) 9 glasses.

Following figure has Q going up by 1 unit at every 20 cent drop in price. So, at \$0.80  $Q = 9$



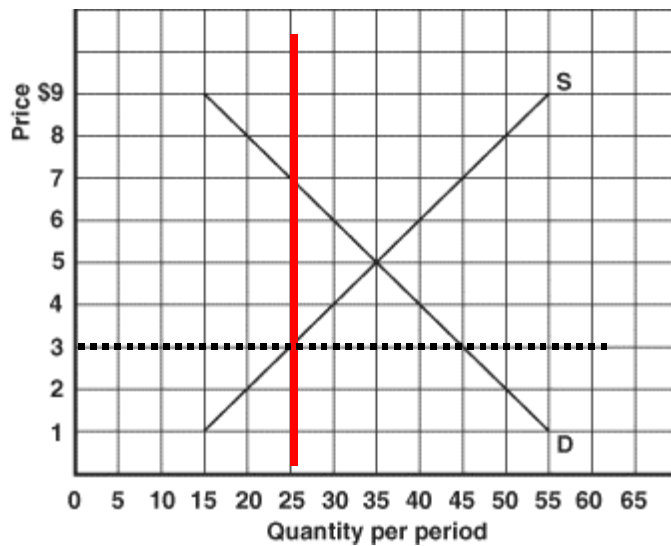
Use the following to answer question 6:



6. Referring to figure 4.4, suppose that the price of nuts *decreases* from  $P_1$  to  $P_2$  and the demand curve for chocolates *shifts to the right* from  $D_1$  to  $D_2$ . What can be said about these products?
- A) The cross-price elasticity of demand between nuts and chocolates is positive and nuts and chocolates are complements.
  - B) The cross-price elasticity of demand between nuts and chocolates is positive and nuts and chocolates are substitutes.
  - C) The cross-price elasticity of demand between nuts and chocolates is negative and nuts and chocolates are complements. Cheaper nuts, buy more of both**
  - D) The cross-price elasticity of demand between nuts and chocolates is negative and nuts and chocolates are substitutes.

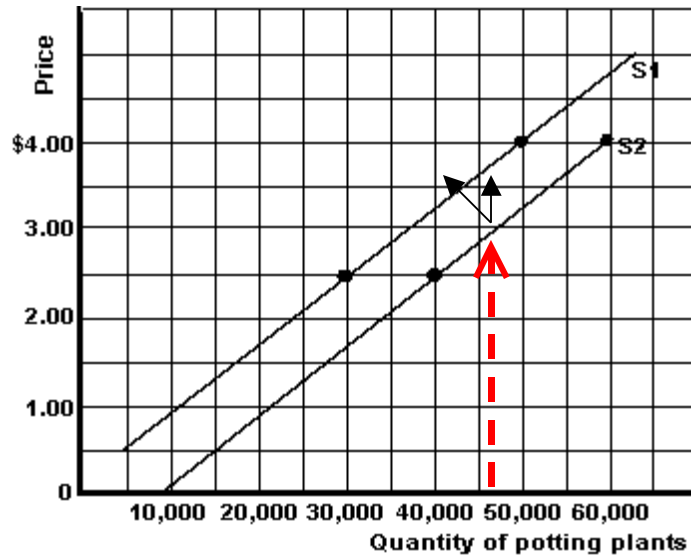
7. If you produce Dollar Store food produces, and you know that Dollar Store food produces are inferior goods (*with respect to income elasticity of demand*), and you expect the current financial crisis to be followed by an economic recession you should:
- A) increase your output because the demand for your product will likely increase. Falling income would result in increased demand for inferior good (Note: “inferior” is an income elasticity of demand economic concept here. It doesn’t refer to the quality of the good.)
  - B) keep your output of widgets the same but raise price in order to increase revenue.
  - C) reduce the price of widgets to increase your total revenue.
  - D) reduce your output because you likely will be left with a large inventory.

Use the following to answer question 8:



8. In figure 3.7, what must be true if the quantity currently being purchased is 25?
- A) There is a price floor of \$3.
  - B) Equilibrium price is \$3.
  - C) Consumers would like to buy 10 more units at a price of \$3.
  - D) There is a price ceiling of \$3. At price ceiling of \$3 suppliers only offer  $Q = 25$
9. A proposed market model has two equations  $P = 2 + 3Q$  and  $P = 6 + 3Q$ . The model yields a solution for  $Q$  of: (*easy!*)
- A) -100.
  - B) No solution.  $2 + 3Q = P = 6 + 3Q \Rightarrow 2 = 6 \leq$  i.e., no solution – parallel lines!
  - C) 100.
  - D) 0.

Use the following to answer question 10:



10. Graphically, what is the effect of imposing an excise tax on a product? (*Use the graph to help formulate your answer*)

- A) It will shift the supply curve for the product to the left/up. Tax adds to supply price and market demand determines how incidence of tax is split between buyers and sellers
- B) It will shift the supply curve for the product to the right/down.
- C) It will shift both the supply and the demand curve for the product to the right/down.
- D) It will shift both the supply and the demand curve for the product to the left/up.

Use the following to answer question 11:

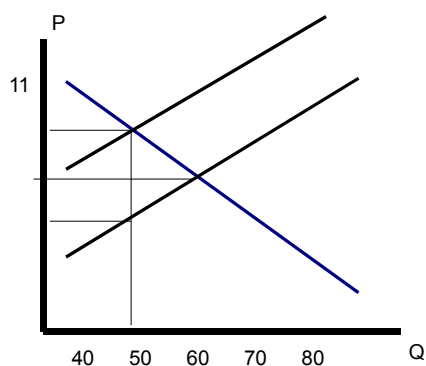
Good	Q purchased	Price/unit 2005 (\$)	Price/unit 2007 (\$)
Bread	100	2	10
Meat	75	10	14
Vegetables	50	4	2
Milk/Soya	25	40	50

11. Table 2.1 shows the prices and quantities of four different goods purchased by the typical household in 2005 and 2007. Using 2005 as the base year, the value of the consumer price index in 2005 was:

- A) 175.
- B) Cannot calculate, need more information.
- C) 200.
- D) 100. The value of an index in its base year is always 100 ! <= EASY

Use the following to answer question 12:

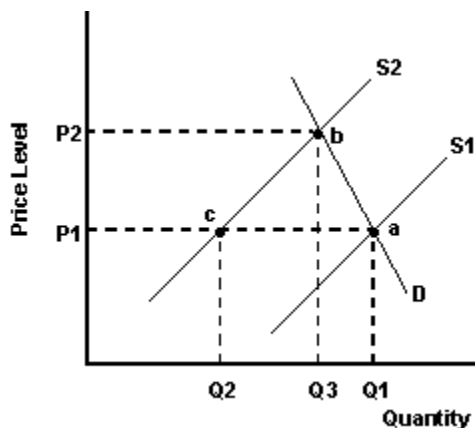
Price	Quantity demanded	Quantity supplied
7	80	40
8	70	50
9	60	60
10	50	70
11	40	80



12. Refer to table 4.2, if the government imposes a \$2 per unit sales tax on this product, how much of that tax will consumers pay and how much will sellers pay? (*Draw a graph to help answer this question. Don't just stare at the table of numbers!*)
- A) Consumers will pay \$1.50 and sellers \$.50.
  - B) Consumers will pay \$.50 and seller \$1.50.
  - C) Consumers will pay all \$2 of the tax.
  - D) Consumers and sellers will each pay \$1. See diagram**
13. Using a supply and demand diagram of your own (*draw it on your exam booklet*), if a per unit tax is imposed, the *more inelastic demand* is, the:
- A) smaller the deadweight loss to consumers.
  - B) smaller the deadweight loss. The more inelastic the smaller the fall in Q and hence the smaller the deadweight loss.**
  - C) larger the deadweight loss.
  - D) larger the deadweight loss to producers.
14. Other things equal, when the market price of a good increases, we would expect:
- A) quantity supplied to increase. YES, implies movement along supply curve.**
  - B) supply to increase. *<= No, that implies an outward shift in the supply curve*
  - C) quantity demanded to increase. *<= No, implies an outward shift in demand curve*
  - D) demand to decrease. *<= No, implies an inward shift in demand curve*

15. When two goods are complementary, *for example: university courses and textbooks*, the cross-price elasticity of demand:
- A) equals zero.
  - B) may be either positive or negative.
  - C) is positive.
  - D) is negative. Tuition up.....fewer courses...less demand for textbooks.**
16. If the income of the *Bare Naked Ladies* singing group falls and they increase their demand for *macaroni&cheese* dinners, then this suggests that *macaroni&cheese* dinners are a(n):
- A) substitute good.
  - B) inferior good. Buy less as income rises, buy more as income falls.**
  - C) complementary good.
  - D) normal good.
17. In a market economy, the ideal/preferred economic solution to the problem of externalities is to:
- A) allow producers to produce the output level where both the marginal private benefit and the marginal private cost equal the price. **No, doesn't equate marginal costs and benefits.**
  - B) prohibit all production involving spillover costs or negative externalities **No, marginal costs of drastic action outweigh the marginal benefits given loss of output**
  - C) regulate both the amount people may consume and the price they pay for goods whose production involves spillover costs or externalities. **No efficiencies here**
  - D) internalize costs by charging/taxing producers the marginal cost of the externality generated in production. Builds costs into the supply curve.**

Use the following to answer question 18:

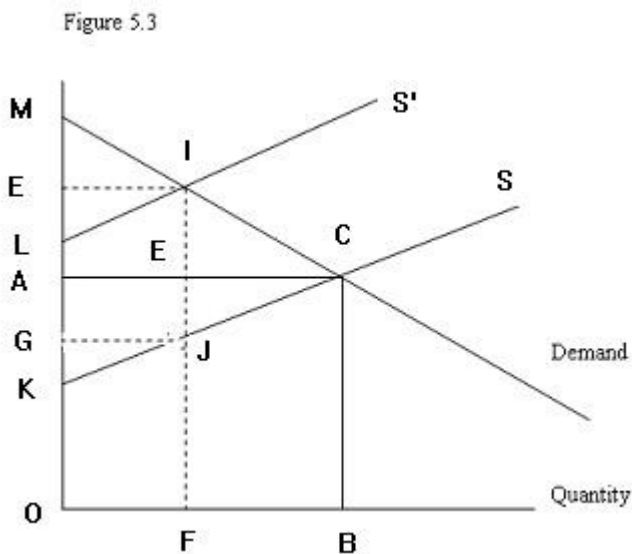


18. In figure 3.5, which of the following statement is correct?
- A) While ac represents a decrease in supply, ab represents a decrease in the quantity demanded. Remember, “decrease in supply” means shift in supply curve.
  - B) Both ab and ac represent a decrease in supply.
  - C) Both ab and ac represent a decrease in the quantity supplied.
  - D) While ac represents a decrease in supply, ab represents a decrease in demand.
19. Which one of the following statements is **false**?
- A) To examine the effect of intellectual ability upon earnings, cross-section data could be used. True, look at “intellectual ability” & “earnings” for cross section of people
  - B) If an economist wants to forecast gross national product based upon observations from previous years, he should use time-series data. True
  - C) To examine the relationship between advertising expenditures and sales during 2007, cross-section data is used. True
  - D) If an economist wants to examine the distribution of income in 2007, she should use time-series data. False, need cross section data
20. In a free market, goods with negative externalities will:
- A) be overproduced at the market equilibrium. Costs are under valued in the supply curve, so production would be excessive since buyers paid less than real cost.
  - B) be under-produced in the market place.
  - C) have the marginal valuation of the externality reflected in their price.
  - D) be produced to the point at which the marginal social benefit equals the marginal social cost of the last unit produced.
21. To say that markets are “free” means that:
- A) consumers are free to purchase all that they want at prices established by the market power of suppliers.
  - B) production, distribution, and consumption of goods is unregulated, but government sets some prices.
  - C) everyone produces according to his ability and receives goods and services according to his needs.
  - D) within market regulations the *invisible hand* operates, and there is no market management by government. The market has regulations but buyer self interest drives demand and the profit motive drives supply.

22. Why do some academics argue that attempts to reduce much of the crime in Canada by "getting tough" on crime and imposing stiffer punishment will not be successful?
- A) Because much of the crime in our society is drug related and the *demand for illegal drugs* is very inelastic. Buyers will pay whatever price, and incentive to supply will remain no matter what the "costs and risks of being caught" are.
  - B) Because much of the crime in our society is drug related and the *demand for illegal drugs* is very elastic. Second part not true
  - C) Because much of the crime in our society is drug related and the *supply of illegal drugs* is very inelastic. Don't know, but problem is in the demand side of market
  - D) Because much of the crime in our society is drug related and the *supply of illegal drugs* is very elastic. Don't know, but problem is in the demand side of market
23. Suppose that the price of gasoline *increases* by 10 percent and the quantity demanded *falls* by 4 percent. We can conclude that the:
- A) demand is *inelastic* with a coefficient of -4.0, so total revenue of sellers falls.
  - B) demand is *elastic* with a coefficient of -4.0, so total revenue of sellers falls.
  - C) demand is *inelastic* with a coefficient of -0.4, so total revenue of sellers rises.
  - D) demand is *elastic* with a coefficient of -0.4, so total revenue of sellers rises.
24. All social systems face *the problem of economic scarcity*, and this problem arises primarily from the fact that: (*Hint: all 4 are true but only one answers the question*)
- A) every society can produce along its possibilities frontier.
  - B) all resources have alternative uses, and this gives rise to opportunity costs.
  - C) in order to produce more of one good, increasing amounts of other goods must be foregone.
  - D) human wants are essentially unlimited but the means to satisfy these wants are limited.
25. If chicken and lamb are substitute goods, then an increase in the price of chicken, other things constant, causes:
- A) the demand for lamb to decrease. No
  - B) the quantity demanded of lamb to fall. No
  - C) lamb to become relatively more expensive than chicken. No
  - D) lamb to become relatively less expensive than chicken.

26. Which of the following statements is correct for a society that emphasizes the current production of capital goods (real investment) over consumer goods?
- A) The society could support faster growth than a society that emphasizes the production of consumer goods. **Yes, more capital goods raise future production capacity**
  - B) The society could enjoy more capital goods and a larger quantity of consumer goods in the future. **Yes, future production could be of capital or consumer goods**
  - C) The society would have to currently save more now than a society that did not emphasize the production of capital goods. **Yes, to produce capital goods now, must not consume output so must save.**
  - D) All of the above are correct.**
27. The **opportunity cost** of attending York University is likely to be highest for a student:
- A) who has to take leave from a high income job. "Opportunity cost" is the next best option one has to give up...so this student has to forego income while at school.**
  - B) who has to pay foreign student tuition fees.
  - C) who will finance the education with student loans.
  - D) whose family is extremely wealthy.

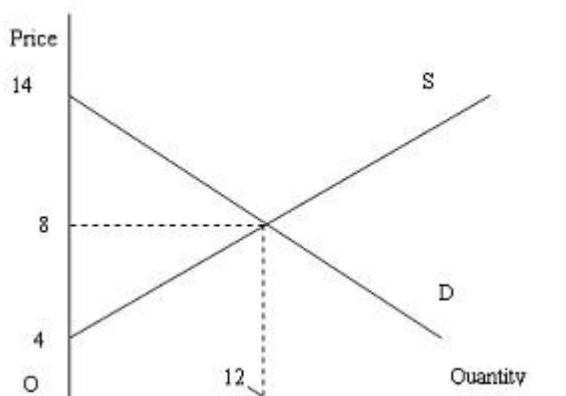
Use the following to answer question 28:



28. Referring to figure 5.3, if  $S'$  represents the *tax-inclusive supply curve*, then *producer surplus* after the tax is imposed is:
- A) EGJCI.
  - B) GJK. At  $Q = F$ , the amount EK is the tax taken from price and GJK is the only producer surplus left to the producer.**
  - C) HJC.
  - D) AKC.

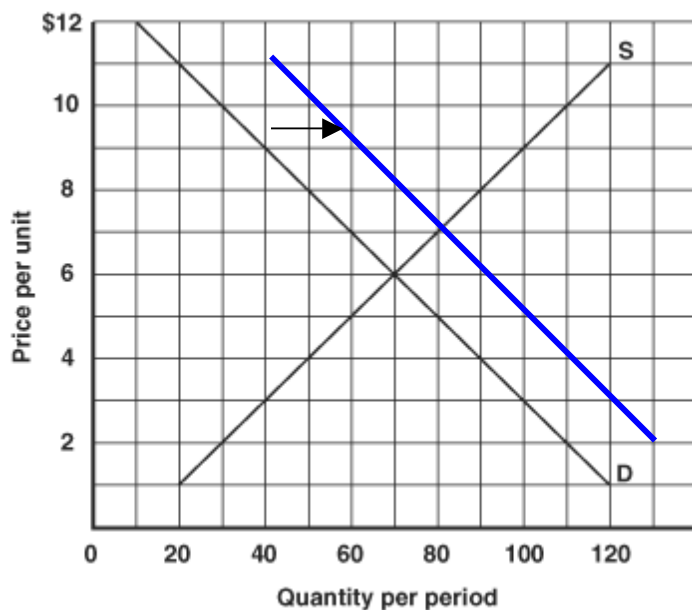
Use the following to answer question 29:

Figure 5.2



29. In figure 5.2, the dollar value of the total economic surplus is:
- A) 36.
  - B) 48.
  - C) 60.  $CS + PS = [(14-8) \times 12]/2 + [(8-4) \times 12]/2 = 60$
  - D) 24.
30. The CPI for 2005 was 284.1. Economists predicted an inflation rate of 3.5 per cent for 2006. The predicted CPI at the end of 2006 was:
- A) 280.6.
  - B) 304.3.
  - C) 294.0.  $284.1 + (.035 \times 284.1) = 294.0$
  - D) 287.6.
31. Suppose that an individual has earned \$400 per week since 2002 and the 2008 CPI is 240 (base year 2002). The purchasing power of this individual's current income in 2002 dollars is:
- A) 160.0
  - B) 360.0
  - C) 166.6  $(400/240) = 166.6$  – or rounded to 166.7 but still best answer
  - D) 240.0
32. When economists say: "*There is no such thing as a free lunch*" they mean:
- A) the more lunch a person eats the more of a weight problem the person will have.
  - B) we must pay money for everything we get.
  - C) every choice we make involves a trade-off.
  - D) it is against the law to receive goods or services without paying for them.

Use the following to answer question 33:



33. In figure 3.3, assume that the market was at equilibrium and that demand increases by 20 units. What will be the new equilibrium price and quantity?
- A) Price will rise by \$1 and quantity traded will rise by 10 units. “demand increases” means that the demand curve shifts. What happens to quantity demanded depends on where supply and demand intercept.
  - B) Price will fall by \$1 and quantity traded will fall by 10 units.
  - C) Price will fall by \$2 and quantity traded will fall by 20 units.
  - D) Price will rise by \$2 and quantity traded will rise by 20 units.
34. Why is there often disagreement amongst the statements of economists?
- A) There may be normative disagreement over what goals society should try to achieve.
  - B) The economy wide and complex, so analysis may start from different assumptions about what is.
  - C) Some economists may be poorly trained in the areas where they speak.
  - D) There is truth in all of the above.

Use the following to answer question 35:

Table 4.3 Here are data for a situation in which several variables change

Year	Income	Price of x	Q <sub>x</sub> demanded	Price of y	Q <sub>y</sub> demanded
1	\$40 000	\$140	50	\$40	200
2	40 000	150	40	40	160
3	40 000	150	30	70	140
4	50 000	150	40	70	160
5	50 000	160	50	90	200

This is a BAD Question since: (1) years 1&2 suggest complements, (2) 2&3 suggest complements, (3) 3&4 suggest normal good, 4&5 –where both P&Q go up for both X&Y- suggests that the demand curve has shifted rightwards. So A is wrong, B is wrong, C is true but not for years 4 & 5, and D is wrong. Most of the scantrons did not select the answer key answer so the 10 point adjustment more than covers this.

35. Referring to table 4.3, between years 4 and 5 both the price and the quantity demanded of X increased. What is the best possible explanation of this?

- A) Product X is a substitute for product Y. Answer Key said A
- B) Graphically, the demand curve for product X must have shifted leftwards.
- C) Product Y is a complement of product X.
- D) Graphically, the demand curve for X must be upward sloping.

36. When economists compute the real value of an economic variable denominated in dollars, they do so by:

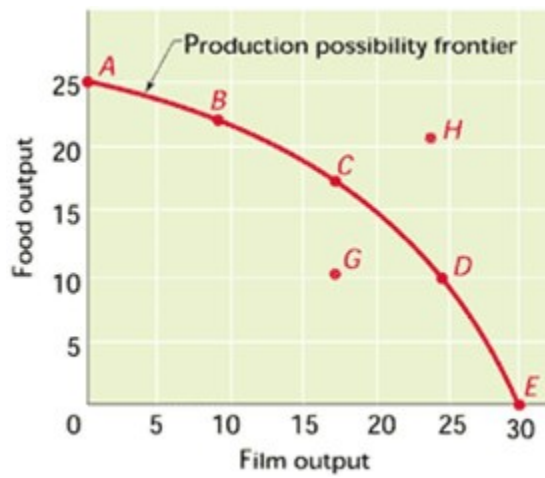
- A) subtracting the price level from the nominal value and multiplying by 100.
- B) dividing the nominal value by 100.
- C) multiplying the nominal value by the price level.
- D) dividing the nominal value by the price index.

37. What do economists mean by the term *consumer surplus*?

- A) It is the difference between the price which consumers pay for a product and the actual costs of production.
- B) It is the difference between the actual price of a product and its real value.
- C) It is the surplus which consumers receive from a product as a result of a drop in its price.
- D) It is the difference between what the consumers are willing to pay and the actual price they pay for the product.

38. The demand curve for a good/commodity slopes downward and to the right because when the price of the good/commodity falls:
- A) suppliers reduce their output of the good/commodity
  - B) in general consumers do not care about the prices of other related goods.
  - C) consumers substitute the now relatively lower-priced good for relatively more expensive other goods.
  - D) consumers' preferences change, so they buy more of the good in question.

Use the following to answer question 39:



39. Referring to figure 1.1, points A, B, C, and D illustrate:
- A) a constant trade-off between food output and film output.
  - B) an inefficient allocation of society's scarce resources.
  - C) society prefers food output to film output.
  - D) possible combinations of food output and film output.
40. A market failure/inefficiency exists when:
- A) resource decisions are optimally allocated in production, but not consumption.
  - B) a competitive markets' clearing price equates both the marginal social cost and marginal social benefits.
  - C) the price established in the market includes all the marginal costs of production.
  - D) the price established in the market does not equate the marginal social benefit of a good and the marginal social cost of production.

41. When specifying economic models, economists often **make assumptions** about the real world. The purpose of assumptions in economics is to:
- A) **simplify the model and provide a focus for the theory or issue under analysis.**
  - B) ensure that the model only covers specific conditions.
  - C) guarantee the accuracy of the model for testing a theory.
  - D) make the model more complete and more realistic.
42. If quantity supplied increases from 1,000 to 1,160 units when prices rise by 8 percent, the elasticity of supply using the initial quantity as base is:
- A) 3.4.
  - B) cannot be determined from the information provided.
  - C) 0.2.
  - D) **2.0 Change in Q = 160/1000 = 16% Change in P = 8% so elasticity = 2.0**
43. Supposing that cigarette smokers demand is more price insensitive than the cigarette manufacturers supply, this means that tax incidence is:
- A) borne more by the manufacturers.
  - B) **borne more by the consumers. Consumers absorb most of the incidence of tax**
  - C) borne entirely by the consumers.
  - D) borne entirely by the manufacturers.
44. Which of the following statements is true about rent ceiling controls?
- A) **It can lead to a long run shortage of apartments. Yes!**
  - B) It leads to a more equitable distribution of apartments. **NO!**
  - C) It makes more apartments available for people. **NO!**
  - D) It can cause a surplus of apartments. **NO!**

Use the following to answer question 45:

Price	Quantity demanded
1	20
2	18
3	16
4	14
5	12
6	10
7	8
8	6
9	4
10	2

45. Referring to table 4.1, what is the elasticity value for the price range \$9 to \$10, respectively (using the mid-point reference value formula)?

- A) 6.35 % Price change = 1/9.5 % Q change = 2/3 => .6.34%
- B) 0.15
- C) 0.22
- D) 2.00

$$\text{Elasticity} = \frac{\frac{(Q_2 - Q_1)}{(Q_2 + Q_1)}}{2} \text{ divided by } \frac{(P_2 - P_1)}{(P_2 + P_1)} \frac{1}{2} \quad \leftarrow \text{Corrected}$$