Economics 1
Quiz 3
May 21, 2008

Each correct answer is worth 5 points. Answers left blank are worth 2 points. Wrong answers are worth 0 points.

**True-False Questions:** Fill in Bubble A for True, Bubble B for False.

1. A profit-maximizing firm will hire the number of workers that maximizes the difference between the average value product of labor and the wage it pays to workers.

2. If the demand curve for labor is elastic, a minimum wage that is set higher than the equilibrium wage will decrease total labor income.

3. If an industry with free entry and exit is in long run equilibrium, any firm that is not currently producing in the industry could not make a profit by entering the industry.

4. As a firm increases the number of units it sells, its fixed costs increase proportionately.

5. If a small increase in a firm’s output would decrease its average variable cost, the firm’s marginal cost is less than its average variable cost.

**Multiple Choice Questions**

6. In the rental housing market in the town of Enchilada Grande, the price elasticity of demand is −1 and the price elasticity of supply is 3. The market is currently in competitive equilibrium. A rent-control ordinance is proposed which would set the maximum rent at a rate 30% lower than the current rate. If this proposal is adopted, then the quantity of rental housing that is demanded at the new legal maximum price will be

(a) 30% greater than the amount that was demanded before the ordinance went into effect.

(b) 90% greater than the amount that was demanded before the ordinance went into effect.

(c) 30% smaller than the amount that was demanded before the ordinance went into effect.

(d) 90% smaller than the amount that was demanded before the ordinance went into effect.

(e) the same as the quantity that was demanded before the ordinance went into effect.
7. If the rent-control ordinance is adopted in Enchilada Grande, then the number of housing units that are actually rented will

(a) increase by 30%.
(b) increase by 90%.
(c) decrease by 90%.
(d) decrease by 30%.
(e) not change.

8. A profit-maximizing firm producing black boxes has fixed costs of $1,600 and variable costs of $80 per unit sold. It has a capacity of 40 units of output. In the short run it can not avoid its fixed costs. In the short run, this firm

(a) will supply no output at prices below $80 and will supply 40 units at prices above $80.
(b) will supply no output at prices below $120 and will supply 40 units at prices above $120.
(c) will supply no output at prices below $80, will supply 20 units at prices between $80 and $120, and will supply 40 units at prices above $120.
(d) will supply 40 units at any price above 0.
(e) will have a supply curve that is an upward-sloping straight line passing through the origin, with slope 8.

9. In the long run, the profit-maximizing firm described in the previous question would be able to avoid its fixed costs by shutting down and producing zero output. In the long run, this firm

(a) will supply no output at prices below $80 and will supply 40 units at prices above $80.
(b) will supply no output at prices below $120 and will supply 40 units at prices above $120.
(c) will supply 40 units of output at any price above 0.
(d) will supply no output at prices below $80, will supply 20 units at prices between $80 and $120, and will supply 40 units at prices above $120.
(e) will have a supply curve that is an upward-sloping straight line passing through the origin, with slope 8.
10. All firms in the black box industry have the same costs as the firm described in the previous two problems. Suppose 150 buyers are willing to pay as much as $200 for a black box and 100 more buyers are willing to pay as much as $100 for a black box. In long-run competitive equilibrium, how many firms will be in the black box industry?

(a) 2
(b) 3
(c) 4
(d) 5
(e) 6

11. Courts often require criminal defendants to post bail bonds (a monetary payment), which the defendants forfeit if they fail to appear for a hearing. To meet those requirements, defendants may turn to bail bond firms. The firms post bonds for defendants and charge the defendants a fee for doing so. The state of California has set the fee at 10 percent of the bond. According to the Los Angeles Times article, "It’s Brutal in the Bail Business,"

(a) the fee is so low that most bail bond firms are leaving the industry.
(b) the fee is so high that new firms are entering the industry.
(c) the fee is so high that few defendants use the services of bail bond firms.
(d) defendants are likely to vanish after bonds are posted for them, so profits in the bail bond industry are low.
(e) the bail bond industry is dominated by one large firm.

12. Any number of whifflegongs can be made at a cost of $1 each, so with no tax, the supply curve is horizontal at a price of $1. There are 5000 people with Buyer Values of $10 for a whifflegong and there are 5000 people with Buyer Values of $3. Nobody else wants one at all. In the absence of a tax, whifflegongs sold at a competitive equilibrium price of $1. The government introduced a sales tax of $14 per whifflegong. What was the excess burden caused by this tax?

(a) 0
(b) $55,000
(c) $45,000
(d) $10,000
(e) $27,500
13. In 2010, Californians bought 100,000 pounds of tangerines, spending $150,000 on tangerines in total. Early in 2011, space aliens landed in Coalinga, hijacked a Southern Pacific freight train, and took all the tangerines on board back with them to the red planet. Tangerine prices increased, and Californians bought only 50,000 pounds of tangerines in 2011, spending $100,000 on tangerines in total. Assuming the demand curve for tangerines in California didn’t change between 2010 and 2011, from the information above it appears that
  
  (a) the price elasticity of supply for tangerines is less than 1.
  (b) the price elasticity of demand for tangerines is less than $-1$.
  (c) the price elasticity of demand for tangerines is between $-1$ and 0.
  (d) the price elasticity of supply for tangerines is greater than 1.
  (e) the supply curve for tangerines slopes downward.

14. The Bergstrom Box Company (BBC) makes cute Swedish boxes to sell to gullible American tourists. If it employs one worker, it can make and sell 6 boxes per day. If it employs two workers, it can make and sell 10 boxes per day; and if it employs 3 workers, it can make and sell 12 boxes per day. Each box sells for $10. If the wage of a worker is $30 per day, how many workers should BBC hire?

  (a) 0 workers per day
  (b) 1 worker per day
  (c) 2 workers per day
  (d) 3 workers per day
  (e) 5 goats and no workers

15. There are five other box companies in Sweden (6 in total). Each company has the same relationship between labor employed and output as BBC has. Each company can also sell its boxes for a price of $10 per box. There are 5 workers in Sweden willing to work in a box company for $25 per day or more, and there are 6 workers willing to work in a box company for $35 per day. What is the competitive equilibrium wage for box company workers in Sweden?

  (a) $25 per day
  (b) $30 per day
  (c) $35 per day
  (d) $40 per day
  (e) $60 per day

Bonus Question. A correct answer to the following question will increase your score by 5 points. It does not change the maximum score for the exam, however. The maximum is still 75.
16. In the Kaye Lecture on Monday, May 19, Josh Berman discussed the initial advantage MySpace had over Friendster, the first social networking site. According to Berman, the main advantage was

(a) Friendster charged users a higher fee for their personal web page.
(b) Friendster removed websites if they did not conform to its rules.
(c) Friendster had too much advertising.
(d) Friendster was owned by Microsoft.
Each correct answer is worth 5 points. Answers left blank are worth 2 points. Wrong answers are worth 0 points.

**True-False Questions:** Fill in Bubble A for True, Bubble B for False.

1. If the demand curve for labor is elastic, a minimum wage that is set higher than the equilibrium wage will decrease total labor income.

2. If an industry with free entry and exit is in long run equilibrium, any firm that is not currently producing in the industry could not make a profit by entering the industry.

3. If a small increase in a firm’s output would decrease its average variable cost, the firm’s marginal cost is less than its average variable cost.

4. As a firm increases the number of units it sells, its fixed costs increase proportionately.

5. A profit-maximizing firm will hire the number of workers that maximizes the difference between the average value product of labor and the wage it pays to workers.

**Multiple Choice Questions**

6. In the rental housing market in the town of Enchilada Grande, the price elasticity of demand is $-1$ and the price elasticity of supply is 3. The market is currently in competitive equilibrium. A rent-control ordinance is proposed which would set the maximum rent at a rate 30% lower than the current rate. If this proposal is adopted, then the quantity of rental housing that is demanded at the new legal maximum price will be

   (a) 30% smaller than the amount that was demanded before the ordinance went into effect.
   (b) 90% smaller than the amount that was demanded before the ordinance went into effect.
   (c) 90% greater than the amount that was demanded before the ordinance went into effect.
   (d) 30% greater than the amount that was demanded before the ordinance went into effect.
   (e) the same as the quantity that was demanded before the ordinance went into effect.
7. If the rent-control ordinance is adopted in Enchilada Grande, then the number of housing units that are actually rented will

(a) decrease by 30%.
(b) increase by 90%.
(c) decrease by 90%.
(d) increase by 30%.
(e) not change.

8. A profit-maximizing firm producing black boxes has fixed costs of $1,600 and variable costs of $80 per unit sold. It has a capacity of 40 units of output. In the short run it can not avoid its fixed costs. In the short run, this firm

(a) will supply 40 units at any price above 0.
(b) will supply no output at prices below $80, will supply 20 units at prices between $80 and $120, and will supply 40 units at prices above $120.
(c) will supply no output at prices below $120 and will supply 40 units at prices above $120.
(d) will supply no output at prices below $80 and will supply 40 units at prices above $80.
(e) will have a supply curve that is an upward-sloping straight line passing through the origin, with slope 8.

9. In the long run, the profit-maximizing firm described in the previous question would be able to avoid its fixed costs by shutting down and producing zero output. In the long run, this firm

(a) will supply no output at prices below $80 and will supply 40 units at prices above $80.
(b) will supply no output at prices below $120 and will supply 40 units at prices above $120.
(c) will supply 40 units of output at any price above 0.
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10. All firms in the black box industry have the same costs as the firm described in the previous two problems. Suppose 150 buyers are willing to pay as much as $200 for a black box and 100 more buyers are willing to pay as much as $100 for a black box. In long-run competitive equilibrium, how many firms will be in the black box industry?

(a) 2
(b) 4
(c) 5
(d) 3
(e) 6

11. Courts often require criminal defendants to post bail bonds (a monetary payment), which the defendants forfeit if they fail to appear for a hearing. To meet those requirements, defendants may turn to bail bond firms. The firms post bonds for defendants and charge the defendants a fee for doing so. The state of California has set the fee at 10 percent of the bond. According to the Los Angeles Times article, "It’s Brutal in the Bail Business,"

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12. Any number of whifflegongs can be made at a cost of $1 each, so with no tax, the supply curve is horizontal at a price of $1. There are 5000 people with Buyer Values of $10 for a whifflegong and there are 5000 people with Buyer Values of $3. Nobody else wants one at all. In the absence of a tax, whifflegongs sold at a competitive equilibrium price of $1. The government introduced a sales tax of $14 per whifflegong. What was the excess burden caused by this tax?

(a) $45,000
(b) 0
(c) $10,000
(d) $55,000
(e) $27,500
13. In 2010, Californians bought 100,000 pounds of tangerines, spending $150,000 on tangerines in total. Early in 2011, space aliens landed in Coalinga, hijacked a Southern Pacific freight train, and took all the tangerines on board back with them to the red planet. Tangerine prices increased, and Californians bought only 50,000 pounds of tangerines in 2011, spending $100,000 on tangerines in total. Assuming the demand curve for tangerines in California didn’t change between 2010 and 2011, from the information above it appears that

(a) the price elasticity of supply for tangerines is greater than 1.
(b) the price elasticity of demand for tangerines is between −1 and 0.
(c) the price elasticity of demand for tangerines is less than −1.
(d) the price elasticity of supply for tangerines is less than 1.
(e) the supply curve for tangerines slopes downward.

14. The Bergstrom Box Company (BBC) makes cute Swedish boxes to sell to gullible American tourists. If it employs one worker, it can make and sell 6 boxes per day. If it employs two workers, it can make and sell 10 boxes per day; and if it employs 3 workers, it can make and sell 12 boxes per day. Each box sells for $10. If the wage of a worker is $30 per day, how many workers should BBC hire?

(a) 2 workers per day
(b) 1 worker per day
(c) 0 workers per day
(d) 3 workers per day
(e) 5 goats and no workers

15. There are five other box companies in Sweden (6 in total). Each company has the same relationship between labor employed and output as BBC has. Each company can also sell its boxes for a price of $10 per box. There are 5 workers in Sweden willing to work in a box company for $25 per day or more, and there are 6 workers will to work in a box company for $35 per day. What is the competitive equilibrium wage for box company workers in Sweden?

(a) $30 per day
(b) $25 per day
(c) $35 per day
(d) $40 per day
(e) $60 per day

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16. In the Kaye Lecture on Monday, May 19, Josh Berman discussed the initial advantage MySpace had over Friendster, the first social networking site. According to Berman, the main advantage was

(a) Friendster was owned by Microsoft.
(b) Friendster removed websites if they did not conform to its rules.
(c) Friendster charged users a higher fee for their personal web page.
(d) Friendster had too much advertising.
Each correct answer is worth 5 points. Answers left blank are worth 2 points. Wrong answers are worth 0 points.

**True-False Questions:** Fill in Bubble A for True, Bubble B for False.

1. As a firm increases the number of units it sells, its fixed costs increase proportionately.
2. If an industry with free entry and exit is in long run equilibrium, any firm that is not currently producing in the industry could not make a profit by entering the industry.
3. A profit-maximizing firm will hire the number of workers that maximizes the difference between the average value product of labor and the wage it pays to workers.
4. If the demand curve for labor is elastic, a minimum wage that is set higher than the equilibrium wage will decrease total labor income.
5. If a small increase in a firm’s output would decrease its average variable cost, the firm’s marginal cost is less than its average variable cost.

**Multiple Choice Questions**

6. In the rental housing market in the town of Enchilada Grande, the price elasticity of demand is \( -1 \) and the price elasticity of supply is 3. The market is currently in competitive equilibrium. A rent-control ordinance is proposed which would set the maximum rent at a rate 30% lower than the current rate. If this proposal is adopted, then the quantity of rental housing that is demanded at the new legal maximum price will be

   (a) 30% smaller than the amount that was demanded before the ordinance went into effect.
   (b) 90% smaller than the amount that was demanded before the ordinance went into effect.
   (c) 90% greater than the amount that was demanded before the ordinance went into effect.
   (d) 30% greater than the amount that was demanded before the ordinance went into effect.
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(b) increase by 90%.
(c) decrease by 90%.
(d) increase by 30%.
(e) not change.

8. A profit-maximizing firm producing black boxes has fixed costs of $1,600 and variable costs of $80 per unit sold. It has a capacity of 40 units of output. In the short run it can not avoid its fixed costs. In the long run it could avoid its fixed costs by shutting down. In the short run, this firm

(a) will supply 40 units at any price above 0.
(b) will supply no output at prices below $80 and will supply 40 units at prices above $80.
(c) will supply no output at prices below $80, will supply 20 units at prices between $80 and $120, and will supply 40 units at prices above $120.
(d) will supply no output at prices below $120 and will supply 40 units at prices above $120.
(e) will have a supply curve that is an upward-sloping straight line passing through the origin, with slope 8.

9. In the long run, the profit-maximizing firm described in the previous question would be able to avoid its fixed costs by shutting down and producing zero output. In the long run, this firm

(a) will supply no output at prices below $120 and will supply 40 units at prices above $120.
(b) will supply 40 units of output at any price above 0.
(c) will supply no output at prices below $80 and will supply 40 units at prices above $80.
(d) will supply no output at prices below $80, will supply 20 units at prices between $80 and $120, and will supply 40 units at prices above $120.
(e) will have a supply curve that is an upward-sloping straight line passing through the origin, with slope 8.
10. All firms in the black box industry have the same costs as the firm described in the previous two problems. Suppose 150 buyers are willing to pay as much as $200 for a black box and 100 more buyers are willing to pay as much as $100 for a black box. In long-run competitive equilibrium, how many firms will be in the black box industry?

(a) 4
(b) 2
(c) 5
(d) 3
(e) 6

11. Courts often require criminal defendants to post bail bonds (a monetary payment), which the defendants forfeit if they fail to appear for a hearing. To meet those requirements, defendants may turn to bail bond firms. The firms post bonds for defendants and charge the defendants a fee for doing so. The state of California has set the fee at 10 percent of the bond. According to the Los Angeles Times article, "It’s Brutal in the Bail Business,"

(a) the fee is so high that few defendants use the services of bail bond firms.
(b) the fee is so high that new firms are entering the industry.
(c) defendants are likely to vanish after bonds are posted for them, so profits in the bail bond industry are low.
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12. Any number of whifflegongs can be made at a cost of $1 each, so with no tax, the supply curve is horizontal at a price of $1. There are 5000 people with Buyer Values of $10 for a whifflegong and there are 5000 people with Buyer Values of $3. Nobody else wants one at all. In the absence of a tax, whifflegongs sold at a competitive equilibrium price of $1. The government introduced a sales tax of $14 per whifflegong. What was the excess burden caused by this tax?

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(e) the supply curve for tangerines slopes downward.

14. The Bergstrom Box Company (BBC) makes cute Swedish boxes to sell to gullible American tourists. If it employs one worker, it can make and sell 6 boxes per day. If it employs two workers, it can make and sell 10 boxes per day; and if it employs 3 workers, it can make and sell 12 boxes per day. Each box sells for $10. If the wage of a worker is $30 per day, how many workers should BBC hire?

(a) 2 workers per day
(b) 3 workers per day
(c) 1 worker per day
(d) 0 workers per day
(e) 5 goats and no workers

15. There are five other box companies in Sweden (6 in total). Each company has the same relationship between labor employed and output as BBC has. Each company can also sell its boxes for a price of $10 per box. There are 5 workers in Sweden willing to work in a box company for $25 per day or more, and there are 6 workers willing to work in a box company for $35 per day. What is the competitive equilibrium wage for box company workers in Sweden?

(a) $40 per day
(b) $30 per day
(c) $25 per day
(d) $35 per day
(e) $60 per day

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16. In the Kaye Lecture on Monday, May 19, Josh Berman discussed the initial advantage MySpace had over Friendster, the first social networking site. According to Berman, the main advantage was

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(b) Friendster removed websites if they did not conform to its rules.
(c) Friendster was owned by Microsoft.
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**True-False Questions:** Fill in Bubble A for True, Bubble B for False.

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(c) decrease by 30%.
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8. A profit-maximizing firm producing black boxes has fixed costs of $1,600 and variable costs of $80 per unit sold. It has a capacity of 40 units of output. In the short run it can not avoid its fixed costs. In the short run, this firm

(a) will supply 40 units at any price above 0.
(b) will supply no output at prices below $120 and will supply 40 units at prices above $120.
(c) will supply no output at prices below $80, will supply 20 units at prices between $80 and $120, and will supply 40 units at prices above $120.
(d) will supply no output at prices below $80 and will supply 40 units at prices above $80.
(e) will have a supply curve that is an upward-sloping straight line passing through the origin, with slope 8.

9. In the long run, the profit-maximizing firm described in the previous question would be able to avoid its fixed costs by shutting down and producing zero output. In the long run, this firm

(a) will supply no output at prices below $80, will supply 20 units at prices between $80 and $120, and will supply 40 units at prices above $120.
(b) will supply 40 units of output at any price above 0.
(c) will supply no output at prices below $120 and will supply 40 units at prices above $120.
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10. All firms in the black box industry have the same costs as the firm described in the previous two problems. Suppose 150 buyers are willing to pay as much as $200 for a black box and 100 more buyers are willing to pay as much as $100 for a black box. In long-run competitive equilibrium, how many firms will be in the black box industry?
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   (b) 2  
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   (d) 5  
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(a) 0 workers per day
(b) 2 workers per day
(c) 3 workers per day
(d) 1 worker per day
(e) 5 goats and no workers

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