

Economics 3550
Intermediate Microeconomics
Professor Rous
Mid-Term Exam 1
October 2, 2002

Name _____

Clearly label all graphs for full credit and please write legibly; I cannot grade what I cannot read.

1. (6) “One of the most problematic aspects of the science of economics is the strong belief that everyone is rational. I don’t know about you, but I know plenty of people who do irrational things, and therefore, economics is based on a false premise.”

Do you agree or not with the above quote, please comment.

2. (6) Which of the following reasons does Landsburg believe accounts for the phenomenon of celebrity endorsements?
- a. Firms think that consumers believe celebrities would only endorse high quality products.
 - b. Firms believe that consumers want to own the same goods that celebrities do.
 - c. Firms that intend to be around for a long time want to signal their intention by spending a lot of money on a celebrity.
 - d. Firms assume that consumers will be more likely to pay attention to a commercial if a celebrity appears in it.
3. (7) When Supply decreases, ceteris paribus:
- a. price increases, demand decreases.
 - b. price increases, quantity demanded decreases.
 - c. price decreases, demand decreases.
 - d. price decreases, quantity demanded decreases.

4. Assume the supply and demand for microwaves follows the following equations:

$$\text{Demand: } P = 220 - .5Q_d$$

$$\text{Supply: } P = 40 + .3 Q_s$$

- (8) What is the equilibrium Price and Quantity in the microwave market?

(6) Now suppose a \$10 excise tax is placed on producers of microwaves. What will be the new equilibrium price and quantity, the price that consumers will pay (price to demanders), and the price to suppliers?

5. (8) Workers in France can produce 3 DVD players or 6 radios in one day. Workers in Italy can produce 6 DVD players or 9 radios in one day. Which country has a comparative advantage in producing DVD players? How do you know?

6. (7) A budget constraint shows us:
- how income can be used to buy one bundle of goods at different prices
 - an individual's consumption possibilities.
 - how increases in the price of a good affect an individual's income.
 - which bundle of goods maximizes utility.
7. (6) That indifference curves bow away from the origin follows from which preference assumption?
- the transitivity assumption of consumer preferences.
 - the nonsatiation assumption of consumer preferences.
 - the completeness assumption of consumer preferences.
 - the convexity assumption of consumer preferences.
8. (5) A Giffen Good is one...
- for which an increase in price causes an increase in the quantity demanded.
 - for which the Engel curve is negatively sloped.
 - for which there are perfect substitutes.
 - for which the income elasticity is exactly 0.0.
9. (5) The Substitution Effect...
- is the part of a change in the quantity demanded caused by an increase in the price of a substitute.
 - is the part of a change in purchasing power caused by a change in price.
 - is the part of a change in the quantity demanded caused by a change in the price ratio while purchasing power is held constant.
 - is the part of a shift in demand caused by a change in price.
10. (8) The price of going to a movie is \$5 per person (\$10 for a couple). The price of going to the ballet is \$30 per person (\$60 for a couple). Say a babysitter costs \$20.

Assuming people with or without children have similar incomes and preferences, where would you expect to find a larger percentage of childless couples, at the movie or ballet? Please explain.

Answer **ONE** of the following two questions. **Do NOT answer both.**

- 12.(10) After September 11, 2001, some said that while they hated to say there was a silver lining in such a tragedy, the rebuilding was sure to stimulate the economy and make us better off.

One reason the Spring 2002 GDP growth figures looked so good was because the new Federal Agency that is responsible for airport security hired lots of new security guards and bought lots of new x-ray and bomb detecting machines, illustrating the point that new safety measures will increase employment and be good for the American standard of living.

Based on your reading of Hazlitt, please comment on the above statements.

13. (10) According to DeLong, there are several reasons that private property is important. Among the reasons is efficiency. Describe two different market failures that result from insufficient or absent property rights (make sure you explain why property rights are important). Cite examples of each.