

**ARE 201 Spring 2009 Exam #3**

**Topics: Chapters 7—9**

**Date: 04/07/2008**

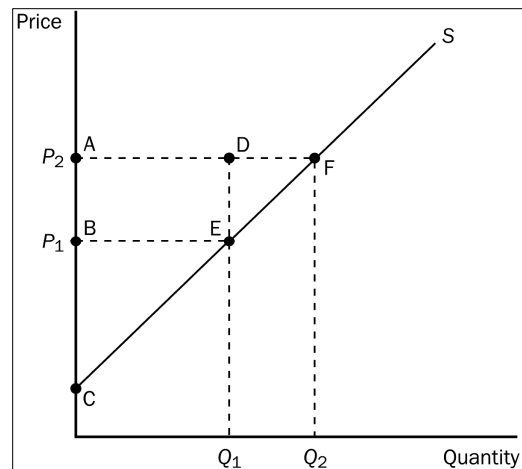
**Time: 1:30pm—2:45pm**

**Instructor: Prof. Zheng**

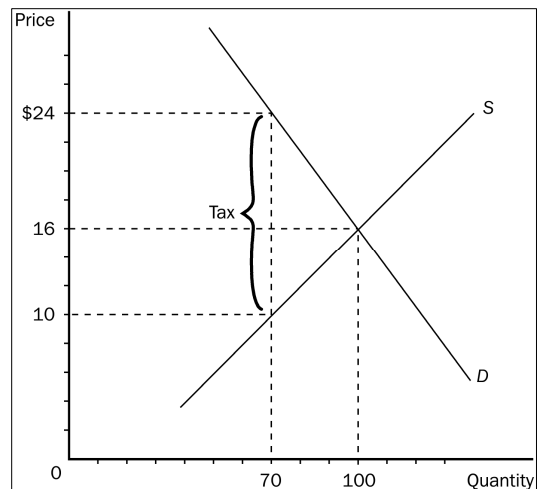
**Format: Closed-book**

**MULTIPLE CHOICE (3 points each)**

1. With respect to welfare economics, the equilibrium price of a product is considered to be the best price because it
  - a. maximizes total revenue to firms and total utility to buyers.
  - b. maximizes the total welfare of buyers and sellers.
  - c. minimizes costs and maximizes profits of sellers.
  - d. minimizes the level of welfare payments to those who no longer live below the poverty line.
2. Suppose that Larry, Moe and Curly are bidding in an auction for a mint-condition video of Charlie Chaplin's first movie. Each has in mind a maximum amount that he will bid. This maximum is called
  - a. a resistance price.
  - b. willingness to pay.
  - c. consumer surplus.
  - d. producer surplus.
3. Cost is a measure of the
  - a. seller's willingness to sell.
  - b. seller's producer surplus.
  - c. producer shortage.
  - d. seller's willingness to buy.
4. According to the graph, which area represents producer surplus at a price of  $P_2$ ?
  - a. BCE
  - b. ACF
  - c. ABED
  - d. DEF
  - e. AFEB
5. Which of the following is NOT correct?
  - a. consumer surplus = value to buyers – amount paid by buyers
  - b. producer surplus = amount received by sellers – cost of sellers
  - c. total surplus = value to buyers – amount paid by buyers + amount received by sellers – costs of sellers
  - d. total surplus = value to sellers – costs of sellers

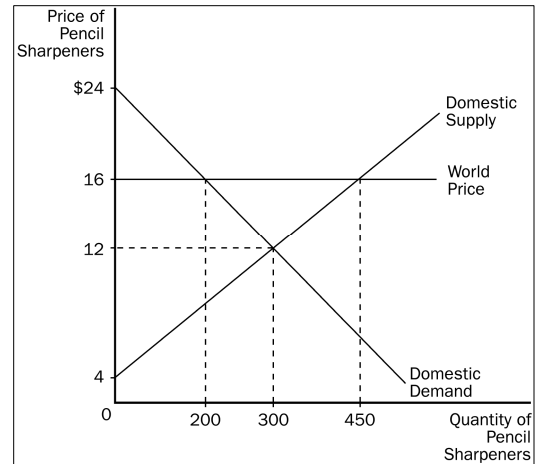


6. When a market is in equilibrium, which of the following would not be correct?
  - a. The price determines which buyers and sellers participate in the market.
  - b. Those buyers who value the good more than the price choose to buy the good.
  - c. Those sellers whose costs are less than the price choose to produce and sell the good.
  - d. Consumer surplus will be equal to producer surplus.
7. A tax placed on chocolate will
  - a. reduce the equilibrium price of chocolate and increase the equilibrium quantity.
  - b. increase the equilibrium price of chocolate and reduce the equilibrium quantity.
  - c. increase the equilibrium price of chocolate and increase the equilibrium quantity.
  - d. reduce the equilibrium price of chocolate and reduce the equilibrium quantity.
8. Deadweight loss measures the
  - a. loss in a market to buyers and sellers that is not offset by an increase in government revenue.
  - b. loss in revenue to the government when buyers choose to buy less of the product.
  - c. loss of efficiency in a market as a result of government intervention.
  - d. lost revenue to businesses because of higher prices to consumers from the tax.
9. The size of the tax and the deadweight loss of a tax are
  - a. positively related.
  - b. negatively related.
  - c. independent of each other.
  - d. equal to each other.
10. According to the graph, the amount of tax revenue received by the government is equal to
  - a. \$210.
  - b. \$420.
  - c. \$560.
  - d. \$980.
11. If the government quadrupled the tax on gasoline, the deadweight loss from the gasoline tax would
  - a. more than quadruple.
  - b. quadruple.
  - c. increase, but it would not quadruple.
  - d. not change.



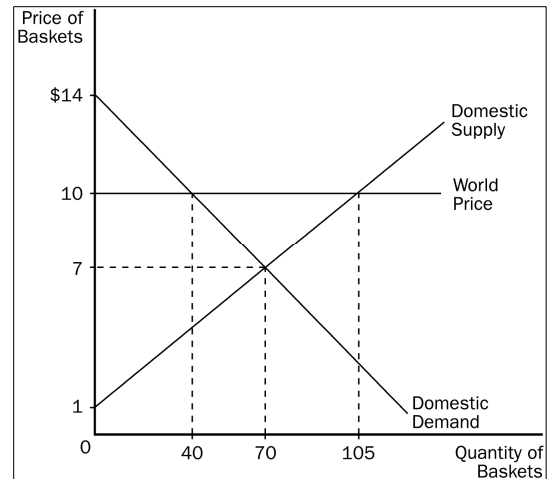
12. The Laffer curve
- relates income tax rates to total income taxes collected.
  - was so ridiculous that economists took it as a joke, hence the name, Laffer Curve.
  - relates tax rates to deadweight welfare losses.
  - relates government welfare payments to the birth rate.

13. According to the graph for this country, at the world price,



- the domestic quantity demanded is greater than the domestic quantity supplied.
- the domestic quantity demanded is less than the domestic quantity supplied.
- the domestic quantity demanded equals the domestic quantity supplied.
- this country should raise the domestic price of baskets.

14. According to the graph, with free trade, consumer surplus would be



- \$45.
- \$80.
- \$210.
- \$245.

15. A tariff is

- a tax on imported goods.
- a tax on exported goods.
- a limit on imported goods.
- a tax on luxuries.

16. Turkey is an importer of goose down pillows. The world price of these pillows is \$50. Turkey imposes a \$7 tariff on pillows. Turkey is a price-taker in the pillow market. As a result of the tariff Turkey's price of pillows will be

- \$50 and the quantity of pillows purchased will decrease.
- \$57 and the quantity of pillows purchased will decrease.
- \$50 and the quantity of pillows purchased will increase.
- \$57 and the quantity of pillows purchased will increase.

17. Workers displaced by trade will eventually find jobs in

- another country.
- the government sector.
- the industries in which the country has a comparative advantage.
- a different company in the same industry.

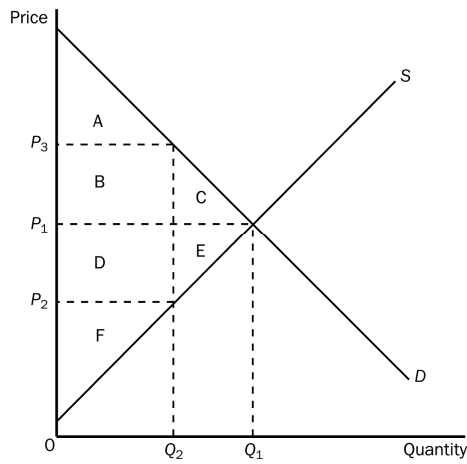
18. Critics of free trade sometimes argue that allowing imports from foreign countries costs jobs domestically. An economist would not argue that
- a. foreign competition may cause unemployment in import-competing industries, but the effect is temporary because other industries, especially exporting industries, will be expanding.
  - b. foreign competition may cause unemployment in import-competing industries, but the increase in consumer surplus due to free trade is more valuable than the lost jobs.
  - c. the critics are correct, so countries must protect their industries with tariffs or quotas.
  - d. foreign competition may cause unemployment in import-competing industries, but the increase in the variety of goods consumers can choose from is more valuable than the lost jobs.

**TRUE/FALSE (2 points each)**

1. Consumer surplus is the amount a buyer actually has to pay for a good minus the amount the buyer is willing to pay for it.
2. Connie can clean windows in large office buildings at a cost of \$1 per window. The market price for window cleaning is \$3 per window. If Connie cleans 100 windows, her producer surplus is \$100.
3. When markets fail, public policy can potentially remedy the problem and increase economic efficiency.
4. A tax on a good causes the size of the market to increase.
5. If a tax did not induce buyers or sellers to change their behavior, it would not cause a deadweight loss.
6. As the size of a tax increases, the government's tax revenue rises, then falls.
7. Without free trade, the domestic price of a good must be equal to the world price of a good.
8. If a tariff is placed on watches, the price of both domestic and imported watches will rise by the amount of the tariff.
9. If Honduras were to subsidize the production of wool blankets and sell them in Sweden at artificially low prices, the Swedish economy would be worse off.

**SHORT ANSWER**  
**APPLICATION/SCENARIO (9 points each)**

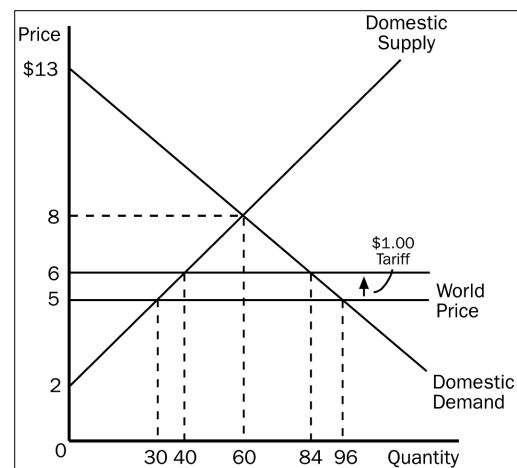
1.



Use the graph shown to fill in the following table.

	WITHOUT TAX	WITH TAX	CHANGE
Consumer surplus			
Producer surplus			
Tax revenue			
Total surplus			

2. Using the graph shown, assume that the government imposes a \$1 tariff on hammers. Answer the following questions given this information. (**Express the answers in terms of dollars**)
- What is the domestic price and quantity demanded of hammers after the tariff is imposed?
  - What is the quantity of hammers imported before the tariff?
  - What is the quantity of hammers imported after the tariff?
  - What would be the amount of consumer surplus before the tariff?
  - What would be the amount of consumer surplus after the tariff?
  - What would be the amount of producer surplus before the tariff?
  - What would be the amount of producer surplus after the tariff?
  - What would be the amount of government revenue because of the tariff?
  - What would be the total amount of deadweight loss due to the tariff?



MULTIPLE CHOICE (3 points each)

1	2	3	4	5	6	7	8	9	10
11	12	13	14	15	16	17	18		

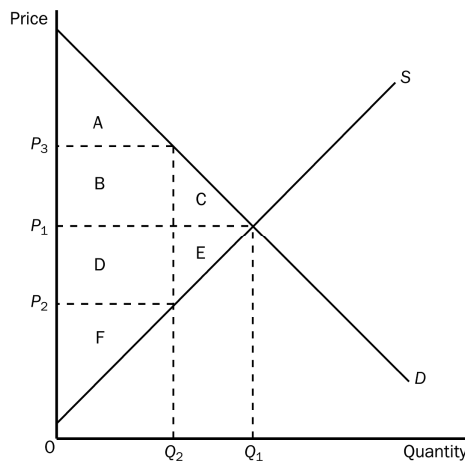
TRUE/FALSE (2 points each)

1	2	3	4	5	6	7	8	9

SHORT ANSWER

APPLICATION/SCENARIO (9 points each)

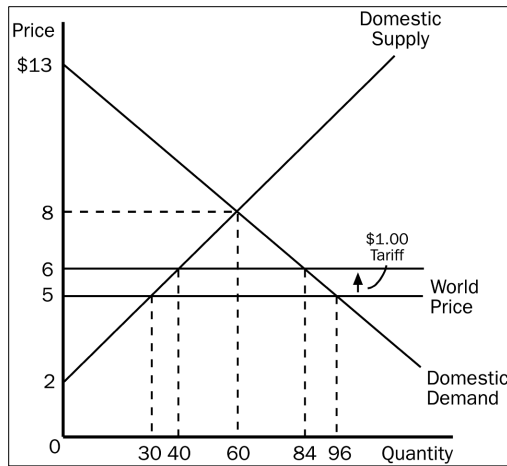
1.



Use the graph shown to fill in the following table.

	WITHOUT TAX	WITH TAX	CHANGE
Consumer surplus			
Producer surplus			
Tax revenue			
Total surplus			

2. Using the graph shown, assume that the government imposes a \$1 tariff on hammers. Answer the following questions given this information. (**Express the answers in terms of dollars**)



- What is the domestic price and quantity demanded of hammers after the tariff is imposed?
- What is the quantity of hammers imported before the tariff?
- What is the quantity of hammers imported after the tariff?
- What would be the amount of consumer surplus before the tariff?
- What would be the amount of consumer surplus after the tariff?
- What would be the amount of producer surplus before the tariff?
- What would be the amount of producer surplus after the tariff?
- What would be the amount of government revenue because of the tariff?
- What would be the total amount of deadweight loss due to the tariff?