Multiple Choice

1. Mr. Hudson notes that if he produces ten pairs of shoes per day, his average fixed cost (AFC) is $14 and his marginal cost is $8; if he produces twenty pairs of shoes per day, his MC is $15. What is his AFC when output is twenty pairs of shoes per day?
   a. $5
   b. $7
   c. $8
   d. $15

2. When a product is produced with a fixed factor and a variable factor, the marginal product of the variable resource will eventually diminish as the output of the firm expands. This diminishing return to the variable factor explains why
   a. average fixed costs eventually diminish.
   b. average fixed costs eventually increase.
   c. marginal costs eventually increase.
   d. marginal costs eventually decrease.

3. When the conditions in a competitive price-taker market are such that the firms are consistently unable to cover their production costs,
   a. the firms will suffer short-run economic losses that will be exactly offset by long-run economic profits.
   b. all firms will go out of business since consumers will not pay prices that enable firms to cover their production costs.
   c. some firms will exit from the industry, and market price will rise until the remaining firms can earn the normal rate of return.
   d. resource prices will increase, competition will decline, and eventually the firms in the industry will earn monopoly profit.

4. Which of the following best characterizes the short-run market supply in an industry when the firms are price takers?
   a. It is the sum of the maximum outputs of the individual firms.
   b. It is the horizontal sum of the average total cost curves of the firms.
   c. It is the horizontal sum of the marginal cost curves, above average variable cost, of the individual firms.
   d. It is the sum of the upward-sloping portions of the average variable cost curves of the individual firms.

5. The only way a firm can avoid fixed costs is by
   a. laying off employees.
   b. shutting down.
   c. reorganizing its production methods.
   d. going out of business.
6. If firms in a competitive price-searcher market are currently experiencing economic profits, then over time,
   a. new firms will enter the market, and the current firms will experience a decrease in demand for their products until zero economic profit is again restored.
   b. new firms will enter the market, and the current firms will experience an increase in demand for their products until zero economic profit is again restored.
   c. some existing firms will exit the market, and the remaining firms will experience an increase in demand for their products until zero economic profit is again restored.
   d. some existing firms will exit the market, and the remaining firms will experience a decrease in demand for their products until zero economic profit is again restored.

7. When long run equilibrium is present in competitive price taker and competitive price searcher markets,
   a. price will exceed average total cost in price searcher markets, but not price taker markets.
   b. price will exceed average total cost in price taker markets, but not price searcher markets.
   c. price will equal average total cost in both price taker and price searcher markets.
   d. price will exceed average total cost in both price taker and price searcher markets.
   e. price will be less than average total cost in both price taker and price searcher markets.

8. In a market that is contestable, but has only a few sellers,
   a. the threat of new entrants will prevent the current producers from producing inefficiently and charging prices above the competitive level.
   b. the producers will be able to charge prices that are high enough to produce long-run economic profits.
   c. the producers will not face new competition because the barriers to entry are high.
   d. the market will never be expected to come close to the competitive result.

9. Which of the following most clearly illustrates the concept of "derived demand"?
   a. An increase in the price of steak causes the demand for poultry to increase.
   b. As the price of coffee increases, the quantity demanded of coffee declines.
   c. A boom in the housing market leads to an increase in the demand for lumber and electricians.
   d. An increase in beer advertising on television leads to an increase in per capita beer consumption.

10. Consider the following:
    I. The Marginal Product (MP) of a resource will fall as employment of the resource expands.
    II. The Marginal Revenue Product (MRP) of a resource will rise as employment expands.
    a. Both are true
    b. I is true; II is false
    c. I is false, II is true
    d. Both are false
11. Which one of the following labor resources will likely have the most inelastic supply schedule in the short run?
   a. truck drivers
   b. physicians
   c. unskilled laborers
   d. lawn service employees

12. Which of the following is true of America's millionaires?
   a. Most millionaires inherited the bulk of their wealth.
   b. Millionaires are far more likely than others to be self-employed entrepreneurs.
   c. It is virtually impossible to achieve this status by saving and investing over a lengthy period of time.
   d. Only about 20 percent of the millionaires in the United States have a college degree.

13. Which of the following is the primary source of rapid growth in the real earnings of workers?
   a. strong unions
   b. government regulation of labor markets
   c. high worker productivity
   d. increases in the minimum wage

14. The linkage between high productivity and high earnings is vitally important because
   a. it provides individuals with a strong incentive to develop skills and engage in activities that others value highly.
   b. high productivity (a large output per hour worked) is the key to high living standards.
   c. it brings the self interest of individuals into harmony with economic progress.
   d. All of the above are true.
   e. None of the above are true.

15. Additional investments in machines that enhance the ability to produce goods and services, imply that
   a. the owners of the investments will necessarily have to borrow funds.
   b. the owners of the investments will necessarily have to reduce their current consumption.
   c. someone will have to reduce current consumption.
   d. future consumption will have to be reduced.

16. If Microsoft stock has a constant net return each year, then value of Microsoft stock is determined by
   a. subtracting Microsoft's total costs from its total revenue.
   b. multiplying the annual net income by the number of shares
   c. dividing the annual net income from the asset by the interest rate
   d. both a and b above
17. Consider the following:
   I. There can never be economic profit in a competitive market
   II. Uncertainty and entrepreneurship can be two sources of economic profit.

   a. Both are true
   b. I is true; II is false
   c. I is false; II is true
   d. Both are false

18. Consider the following:
   I. Your spouse cleans your house every Thursday.
   II. You sell an old bicycle for $100.
   III. Your economics textbook is stolen.

   a. All three events increase GDP.
   b. I and II increase GDP; III reduces GDP.
   c. Only II increases GDP; I and III leave GDP unchanged.
   d. None of the events affect GDP.

19. Which one of the following would count as investment in the national income accounts?
   a. buying a U.S. government bond
   b. buying 100 shares of ExxonMobil stock
   c. buying an existing house
   d. a freight-hauling firm buying a new domestically produced truck

   Use the table below to choose the correct answer.

<table>
<thead>
<tr>
<th>Source</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate profits</td>
<td>$1,000</td>
</tr>
<tr>
<td>Interest income</td>
<td>200</td>
</tr>
<tr>
<td>Indirect business taxes</td>
<td>400</td>
</tr>
<tr>
<td>Depreciation</td>
<td>300</td>
</tr>
<tr>
<td>Employee compensation</td>
<td>3,200</td>
</tr>
<tr>
<td>Proprietor's income</td>
<td>600</td>
</tr>
<tr>
<td>Rents</td>
<td>100</td>
</tr>
<tr>
<td>Personal consumption</td>
<td>2,950</td>
</tr>
<tr>
<td>Government consumption and gross investment</td>
<td>1,200</td>
</tr>
<tr>
<td>Net exports</td>
<td>100</td>
</tr>
<tr>
<td>Income received by citizens for factors of production supplied abroad</td>
<td>300</td>
</tr>
<tr>
<td>Income paid to foreigners for their contribution to domestic output</td>
<td>150</td>
</tr>
</tbody>
</table>

20. Refer to the table. Gross domestic product equals
   a. $5,500.
   b. $5,650.
   c. $5,800.
   d. $6,650.
ANSWER SHEET

1. ___________
2. ___________
3. ___________
4. ___________
5. ___________
6. ___________
7. ___________
8. ___________
9. ___________
10. ___________
11. ___________
12. ___________
13. ___________
14. ___________
15. ___________
16. ___________
17. ___________
18. ___________
19. ___________
20. ___________
1. a) Analyze and advise this price taker who desires to maximize his profit. The info: marginal cost is $4.00 and, at this dollar value, cuts average variable cost from below at AVC’s minimum. Total cost is $12,000. Total fixed cost is $4,000. Total revenue is $10,000.

b) Analyze and advise a price searcher who desires to maximize profit and is in the same initial position as described in part a).
2. True or false and WHY? Labor saving innovations always reduce jobs in the industry in which they are applied. Analyze with words and graphs.

3. How is it that a price taker who faces a situation of marginal revenue product not equal to marginal factor cost can adjust to the profit maximizing point? She can't change the price of what she sells, and she can't change the price per unit of input she hires. Analyze with words and graphs.
4. "We should produce for people, not for profit." Discuss.

5. True or false and WHY? A price searcher, seeking maximum profit, will attempt to locate on the inelastic portion of her demand curve.
6. I sell the same service in two markets, and I have higher profit than if the markets were merged with a uniform price. Explain in words and pictures how this is possible.

Please sign the following: I have neither given nor received unauthorized aid on this piece of work, nor have I knowingly tolerated any violation of the Honor Code.