

**Economics 321 Test 1 Fall 2004**  
**Chappell**  
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**Name** \_\_\_\_\_

**Student Number** \_\_\_\_\_

**True/False**

*Indicate whether the sentence or statement is true or false.*

- \_\_\_ 1. An increase in the price of compact discs would shift the demand curve for CD players to the left.
- \_\_\_ 2. If the demand for a good is high, then there will be a shortage of that good.
- \_\_\_ 3. The most efficient typist is the one who can type the greatest number of words per minute.
- \_\_\_ 4. The most efficient house cleaner is the person who has the lowest cost of cleaning houses.
- \_\_\_ 5. A doubling of all prices has the same effect on the budget line as reducing income by half.
- \_\_\_ 6. If the consumer's income doubles, then his optimal purchases of all goods will double.
- \_\_\_ 7. If the Consumer Price Index (CPI) reports an inflation rate of 0%, then a person with a fixed income will be neither better off or worse off.
- \_\_\_ 8. Normal goods have upward-sloping Engel curves.
- \_\_\_ 9. In a two-good world, one good-but not both-can be inferior.
- \_\_\_ 10. The (ordinary) demand curve for a normal good must be downward sloping.
- \_\_\_ 11. Estimates of the price elasticity of demand depend, in part, on the units used to measure price and quantity.

## Multiple Choice

Identify the letter of the choice that best completes the statement or answers the question.

- \_\_\_ 12. If the supply of oil falls and all other relevant factors remain unchanged, then,
- the demand for oil will fall.
  - the quantity demanded of oil will fall.
  - the demand for oil will rise.
  - the quantity demanded of oil will rise.
- \_\_\_ 13. Which of the following would cause the demand curve for peanuts to shift to the left?
- A rise in the price of peanuts.
  - A blight that destroyed 75% of the peanut harvest.
  - A report claiming that the high fat content of peanuts causes heart disease.
  - A tariff that doubles the price of imported pistachio nuts.
- \_\_\_ 14. Suppose the price of a commodity is \$15 per unit. At that price, consumers wish to purchase 6,000 units weekly and producers wish to sell 4,000 units weekly. In this situation,
- unsatisfied consumers will bid up the market price.
  - the market price will fall because producers are unsatisfied.
  - the price will rise and the demand will fall to bring the market to equilibrium.
  - supply will increase by 2,000 units in order to satisfy consumers.
- \_\_\_ 15. Suppose we observe that the price of gasoline has been rising, even though the quantity of gasoline sold has been falling. We can conclude that
- the law of supply does not hold for gasoline.
  - the law of demand does not hold for gasoline.
  - the demand for gasoline must have fallen.
  - the supply of gasoline must have fallen.
- \_\_\_ 16. In 1 hour, Robinson Crusoe can either shoot 4 birds or catch 4 fish. A typical native on a nearby island can either shoot 5 birds or catch 10 fish in an hour's time. Which of the following is true according to the doctrine of comparative advantage?
- Crusoe will be better off if he specializes in either activity and then trades with the natives.
  - The natives have a comparative advantage in both shooting birds and catching fish, so Crusoe cannot make himself better off by trading with the natives.
  - Crusoe should concentrate on shooting birds and then trade with the natives to obtain fish.
  - Crusoe should spend his time catching fish, and he should trade with the natives to obtain birds.
- \_\_\_ 17. An indifference curve shows the bundles of goods which
- have the same marginal values.
  - the consumer can purchase, given his income and the prices he faces.
  - are the most preferred of the baskets within his budget.
  - are all equally desirable, providing the consumer with some fixed level of satisfaction.
- \_\_\_ 18. Under standard assumptions, which of the following is *not* a property of indifference curves?
- They are downward sloping and convex.
  - They fill the plane and never cross.
  - Their slope is equal, in magnitude, to the relative price of the goods.
  - Baskets on indifference curves further away from the origin provide more satisfaction than those which are closer to the origin.

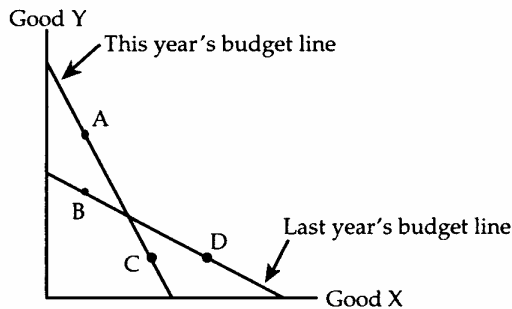
## Goods X and Y

For the following questions, assume that good X is on the horizontal axis and good Y is on the vertical axis in the consumer-choice diagram.  $P_X$  denotes the price of good X,  $P_Y$  is the price of good Y, and  $I$  is the consumer's income. Unless otherwise stated, the consumer's preferences are assumed to satisfy the standard assumptions.

- \_\_\_ 19. Refer to Goods X and Y. If the marginal rate of good X in terms of good Y is large, then the indifference curve will be
- convex.
  - concave.
  - steep.
  - flat.
- \_\_\_ 20. Refer to Goods X and Y. The relative price of good X in terms of good Y is always equal to
- the magnitude of the slope of the budget line.
  - the marginal value of X in terms of Y.
  - the horizontal intercept of the budget line.
  - the vertical intercept of the budget line.
- \_\_\_ 21. Refer to Goods X and Y. Which of the following can cause a parallel, outward shift in the budget line?
- A rise in the consumer's income.
  - A rise in the marginal value of X in terms of Y.
  - A fall in the price of good X.
  - A fall in the price of good Y.

## Budget Lines

The following questions refer to the following diagram, which shows the budget lines faced by a consumer last year and this year.



- \_\_\_ 22. Refer to Budget Lines. Which of the following changes is consistent with the situation shown in the diagram?
- The consumer's income fell.
  - The relative price of good X in terms of good Y fell.
  - The absolute price of good X rose, and the absolute price of good Y fell.
  - The absolute price of both goods rose, with the price of good X rising by the higher percentage.

- \_\_\_\_\_ 23. Consider an income tax and a head tax, the sizes of which have been set so that the government collects the same amount of money under each tax. Which tax does the consumer prefer?
- The consumer is indifferent between the two taxes, since he pays the same amount of money under each tax.
  - The consumer prefers the head tax, because it does not lower the relative wage as does the income tax.
  - The consumer prefers the income tax, because it can be avoided by increasing the amount of leisure time consumed.
  - The consumer may prefer either tax, depending on whether the income tax increases or decreases the number of hours of work at the optimum.
- \_\_\_\_\_ 24. Suppose the price of a good rises. When will the resulting substitution effect reduce the quantity demanded of the good?
- Always.
  - Whenever the good is a non-Giffen good.
  - Only when the good is normal.
  - Only when the good is inferior.
- \_\_\_\_\_ 25. Elasticity measures are preferred by economists to measures of slope when analyzing changes in the quantity of a good consumers purchase because
- they are harder to calculate.
  - the measure of slope is dependent upon the units of measurement, elasticity is not.
  - the measure of slope does not have any units of measurement, elasticity does.
  - elasticity measures depend upon the type of currency, slope does not.

### Analytical Questions

1. Suppose the marginal value of bread in terms of wine is  $\frac{1}{2}$  bottle of wine per loaf of bread, while the relative price of bread in terms of wine is  $\frac{1}{4}$  bottle of wine per loaf of bread. Explain how the consumer can adjust his purchases to raise his level of satisfaction.

2. Suppose the demand curve for bus travel is downward sloping, and the income elasticity of demand for bus travel is negative.
  - (i) Draw an indifference curve-budget line diagram showing the substitution and income effects created when the price of bus travel falls. In your diagram, place bus travel on the horizontal axis and all other goods on the vertical axis.
  - (ii) Explain how your diagram shows that the income elasticity of demand for bus travel is negative.