Practice Exam 3 Questions

1. Monopolies may be able to earn economic profits in the long run because there are:
   a) inelastic consumers.
   b) free entry and exit.
   c) numerous close substitutes for the firm’s product.
   d) barriers to entry.

2. The demand curve facing the monopolist is
   a) the same as the market demand curve.
   b) more elastic than the market demand curve.
   c) less elastic than the market demand curve.
   d) upward sloping.

3. Assume that at the current output level, a monopolist is earning positive economic profit, has a marginal revenue of $7, and a marginal cost of $4. Which of the following is an accurate conclusion with regard to the monopolist's profit?
   a) the firm is producing the profit maximizing output.
   b) the firm could increase its profit by increasing its price.
   c) the firm could increase its profit by decreasing its output.
   d) the firm could increase its profit by decreasing its price.
   e) none of the above

4. Which of the following is NOT necessary for a monopoly to increase its economic profit by discriminating among groups of buyers?
   a) The firm must be able to separate different buyer types.
   b) The firm must be able to identify each individual consumer’s precise willingness to pay.
   c) Each group of buyers must have a different average willingness to pay.
   d) Resale of the product is difficult or unlikely.

5. In the case of a perfectly price-discriminating monopolist, there is no:
   a) transfer of consumer surplus to the producer.
   b) deadweight loss.
   c) short-run economic profit.
   d) long-run economic profit.

6. A monopolist has divided its market into two segments according to gender. The elasticity of demand for the product by men is equal to 3. The elasticity of demand for the product by women is equal to 5. If the marginal cost of selling the product to each segment is a constant $20 per unit, what price should the monopolist charge each segment?
   a) Price for men = $30; Price for women = $25
   b) Price for men = $25; Price for women = $30
   c) Price for men = $20; Price for women = $20
   d) Price for men = $60; Price for women = $4
   e) Impossible to determine from the information provided.
7. Compared to a single-price monopoly, a competitive industry produces:
a) less output at a lower price.
b) less output at a higher price.
c) more output at a lower price.
d) more output at a higher price.

8. A monopolist maximizes profit by:
a) charging the highest price that anyone will pay for the good.
b) producing the level of output associated with maximum total revenue.
c) producing as much as people will buy at a price equal to average cost.
d) producing where marginal revenue intersects marginal cost.
e) producing the level of output associated with unitary price elasticity of demand.

Question 9 and 10 refer to the table below:

<table>
<thead>
<tr>
<th>Quantity</th>
<th>Per unit price</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>10</td>
</tr>
<tr>
<td>2</td>
<td>9</td>
</tr>
<tr>
<td>3</td>
<td>8</td>
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<tr>
<td>4</td>
<td>7</td>
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<tr>
<td>5</td>
<td>6</td>
</tr>
<tr>
<td>6</td>
<td>5</td>
</tr>
<tr>
<td>7</td>
<td>4</td>
</tr>
</tbody>
</table>

9. The table above shows Nuts R Us' demand curve. If the marginal cost is a constant $3 per unit, the firm should produce ____ units of output and sell them at a price of ____ each.
a) 6; $5  
b) 5; $6  
c) 4; $7  
d) 3; $8  
e) 2; $9

10. An increase in the cost of leasing office space (a fixed cost) will:
a) cause Nuts to increase their price to cover the rent increase.
b) cause Nuts to reduce price since demand must be price-elastic. The additional revenue will pay for the increase in lease costs.
c) result in an increase of Nuts' price, reduce the quantity of nuts sold, and reduce profits.
d) have no effect on Nuts' price; however, profits will be reduced.

11. A Texas firm sells lead pipe in Saudi Arabia and in Britain. The price elasticity of demand is higher in Britain than in Saudi Arabia. Thus:
a) the price is likely to be higher in Britain.
b) the price is likely to be higher in Saudi Arabia.
c) the price is likely to be the same in each country.
d) we do not have enough information to determine what the price will be in either country.
12. Which of the following is true? A profit-maximizing monopolist:
   a) should be regulated to prevent price discrimination.
   b) has positive short-run profits.
   c) with long-run economic losses will leave the market.
   d) has no potential competitors.
   e) can always prevent entry.

13. A clothing store can sell 2 shirts for $20 each or 3 shirts for $18 each. At a quantity of 3 shirts sold, marginal revenue:
   a) is $14
   b) is $18
   c) is $20
   d) is $54
   e) cannot be determined from the information given

14. Public goods are those for which
   a) individuals who do not pay can be excluded from consuming.
   b) individuals who do not pay cannot be excluded from consuming.
   c) external costs exist.
   d) no external costs exist.

15. Of those listed below, the best example of a public good is:
   a) a state lottery
   b) a book
   c) a rock concert held in a small auditorium
   d) a radio broadcast

<table>
<thead>
<tr>
<th>Levee Height (feet)</th>
<th>Total benefit (millions of dollars)</th>
<th>Total cost (millions of dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>100</td>
<td>20</td>
</tr>
<tr>
<td>2</td>
<td>155</td>
<td>40</td>
</tr>
<tr>
<td>3</td>
<td>200</td>
<td>70</td>
</tr>
<tr>
<td>4</td>
<td>235</td>
<td>110</td>
</tr>
<tr>
<td>5</td>
<td>260</td>
<td>160</td>
</tr>
</tbody>
</table>

16. Valley City is considering building a levee to protect its residents from flooding. The total costs and benefits are in the table above. The levee height that achieves the maximum net benefit is
   a) 2 feet.
   b) 3 feet.
   c) 4 feet.
   d) 5 feet.

17. The free rider problem implies that public goods:
   a) must be paid for through government and produced by the government.
   b) must be paid for through government and can be produced by private firms.
   c) must be produced by the government but can be sold to consumers by private firms.
   d) will be overprovided by government.
18. An example of a good produced by the government that does NOT have features of a public good is:
   a) national defense
   b) postal delivery
   c) police protection
   d) the judicial and legal system
   e) highways

19. The Coase theorem applies when property rights are given
   a) to the victim of pollution but not to the polluter.
   b) to the polluter but not to the victim.
   c) to either the polluter or the victim.
   d) neither to the polluter nor to the victim.

20. An example of an activity that generates an external cost is
   a) dumping soapsuds into a trout stream.
   b) national defense services.
   c) planting flowers along an interstate highway.
   d) eating an apple.

The following table refers to Questions 21 and 22.

<table>
<thead>
<tr>
<th>Quantity (tons)</th>
<th>Marginal private benefit (dollars per ton)</th>
<th>Marginal private cost (dollars per ton)</th>
<th>Marginal social cost (dollars per ton)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1,000</td>
<td>140</td>
<td>50</td>
<td>80</td>
</tr>
<tr>
<td>2,000</td>
<td>120</td>
<td>60</td>
<td>90</td>
</tr>
<tr>
<td>3,000</td>
<td>100</td>
<td>70</td>
<td>100</td>
</tr>
<tr>
<td>4,000</td>
<td>80</td>
<td>80</td>
<td>110</td>
</tr>
<tr>
<td>5,000</td>
<td>60</td>
<td>90</td>
<td>120</td>
</tr>
<tr>
<td>6,000</td>
<td>40</td>
<td>100</td>
<td>130</td>
</tr>
</tbody>
</table>

21. The above table shows the marginal benefits and costs from production of fertilizer. If the market is perfectly competitive and unregulated, the equilibrium output will be
   a) 2,000 tons.
   b) 3,000 tons.
   c) 4,000 tons.
   d) 5,000 tons.

22. The above table shows the marginal benefits and costs from production of fertilizer. If the market is perfectly competitive and unregulated, the socially efficient level of output could be achieved by setting a per ton tax of
   a) $30.
   b) $70.
   c) $100.
   d) $110.
23. The efficient level of pollution in the environment is
   a) zero.
   b) the level at which the average social cost of cleanup equals the average benefit of cleanup.
   c) the level at which the marginal social cost of cleanup equals the marginal benefit of cleanup.
   d) the level that minimizes the total cost of cleanup.

24. Taxes can yield the efficient level of pollution if the tax is set equal to the:
   a) marginal benefit of pollution.
   b) marginal external cost of the activity.
   c) marginal social cost of the activity.
   d) equilibrium price of the activity.

25. Tradable permits give a firm an incentive to:
   a) find more costly forms of pollution control.
   b) increase its emissions.
   c) lower its emissions because the firm can sell a permit if it does not use it.
   d) hold a permit for the long term if it does not use the permit.
   e) shift costs of pollution on somebody else.

26. One reason that education has external benefits is that:
   a) knowledge has diminishing marginal productivity.
   b) education creates job opportunities for teachers.
   c) education creates better citizens.
   d) property owners pay taxes to support the school system.

27. In a market with external benefits, social efficiency can be achieved by:
   a) leaving the market alone.
   b) monopolizing the market.
   c) offering a subsidy equal to the external benefit
   d) imposing a tax equal to the external cost.