EXAMINATIONS: MAY 2016
ELEMENTARY MICRO ECONOMICS – ECON 1C0

INTERNAL EXAMINERS:  MR. S. GUMEDE
                         MR. A. MEYIWA
                         MS. K. MUTULA

EXTERNAL EXAMINER:    DR. P. NYATANGA

Marks: 320
Duration: 3 hours

THE PAPER CONSISTS OF:

80 MCQ QUESTIONS.

COMPLETE ON THE MCQ ANSWER SHEET PROVIDED IN PENCIL. PLEASE ENSURE YOUR STUDENT NUMBER IS CORRECTLY FILLED IN. IF YOU CHANGE YOUR MIND ASK FOR A FRESH SHEET IF YOU HAVE DIFFICULTIES WITH ERASING THE INCORRECT ANSWER.

MARK ALLOCATION IS AS FOLLOWS: CORRECT ANSWER (+4), INCORRECT (0) AND NO ANSWER IS VALUED AT (0) MARKS.

TOTAL MARK ALLOCATION 320.
1. The word "economy" comes from the Greek word aikonomas, which means:
   a. "environment."
   b. "production."
   c. "one who manages a household."
   d. "one who makes decisions."

2. Which of the following statements best represents the principle represented by the adage, "There is no such thing as a free lunch"?
   a. Melissa can attend the concert only if she takes her sister with her.
   b. Greg is hungry and homeless.
   c. Brian must repair the tire on his bike before he can ride it to class.
   d. Kendra must decide between going to Colorado or Cancun for spring break.

3. When the government implements programs such as progressive income tax rates, which of the following is likely to occur?
   a. Equity is increased and efficiency is increased.
   b. Equity is increased and efficiency is decreased.
   c. Equity is decreased and efficiency is increased.
   d. Equity is decreased and efficiency is decreased.

4. A tradeoff exists between a clean environment and a higher level of income in that:
   a. studies show that individuals with higher levels of income actually pollute less than low-income individuals.
   b. efforts to reduce pollution typically are not completely successful.
   c. laws that reduce pollution raise costs of production and reduce incomes.
   d. by employing individuals to clean up pollution, employment and income both rise.

5. Maurice receives $100 as a birthday gift. In deciding how to spend the money, he narrows his options down to four choices: Option A, Option B, Option C, and Option D. Each option costs $100. Finally he decides on Option B. The opportunity cost of this decision is:
   a. the value to Maurice of the option he would have chosen had Option B not been available.
   b. the value to Maurice of Options A, C and D combined.
   c. $100.
   d. $300.
6. Sarah buys and sells real estate. Two weeks ago, she paid R140,000 for a house on Oak Street, intending to spend R20,000 on repairs and then sell the house for R175,000. Last week, the city government announced a plan to build a "halfway house" for convicted criminals on Oak Street. As a result of the city's announced plan, Sarah is weighing two alternatives: She can go ahead with the R20,000 in repairs and then sell the house for R135,000, or she can forgo the repairs and sell the house as is for R120,000. Sarah should:

   a. keep the house and live in it.
   b. go ahead with the R20,000 in repairs and sell the house for R135,000.
   c. forgo the repairs and sell the house as it is for R120,000.
   d. move the house from Oak Street to a more desirable location, irrespective of the cost of doing so.

7. After much consideration, you have chosen Cancun over Ft. Lauderdale as your Spring Break destination this year. However, Spring Break is still months away, and you may reverse this decision. Which of the following events would prompt you to reverse this decision?

   a. The marginal benefit of going to Cancun increases.
   b. The marginal cost of going to Cancun decreases.
   c. The marginal benefit of going to Ft. Lauderdale decreases.
   d. The marginal cost of going to Ft. Lauderdale decreases.

8. In the former Soviet Union, producers were paid for meeting output targets, not for selling products. Under those circumstances, what were the economic incentives for producers?

   a. To produce good quality products so that society would benefit from the resources used.
   b. To conserve on costs, so as to maintain efficiency in the economy.
   c. To produce enough to meet the output target, without regard for quality or cost.
   d. To produce those products that society desires most.

9. Which of the following statements about trade is false?

   a. Trade increases competition.
   b. With trade, one country wins and one country loses.
   c. Bulgaria can benefit, potentially, from trade with any other country.
   d. Trade allows people to buy a greater variety of goods and services at lower cost.
10. The invisible hand’s ability to coordinate the decisions of the firms and households in the economy can be hindered by:

   a. government actions that distort prices.
   b. increased competition in markets.
   c. too much attention paid to efficiency.
   d. None of the above.

11. In an economy in which decisions are guided by prices and individual self-interest, there is:

   a. a strong need for government intervention in the market.
   b. less efficiency than would be observed in a centrally-planned economy.
   c. more need for a strong legal system to control individual greed than would be needed in a centrally-planned economy.
   d. the potential to achieve efficiency in production.

12. In a particular country in 1995, the average worker needed to work 30 hours to produce 40 units of output. In that same country in 2005, the average worker needed to work 20 hours to produce 29 units of output. In that country, the productivity of the average worker:

   a. decreased between 1995 and 2005, so we would expect the standard of living to have decreased accordingly.
   b. increased between 1995 and 2005, so we would expect the standard of living to have increased accordingly.
   c. decreased between 1995 and 2005, so we would expect inflation to have decreased accordingly.
   d. increased between 1995 and 2005, so we would expect inflation to have increased accordingly.

13. The short-run tradeoff between inflation and unemployment implies that, in the short run,

   a. a decrease in the growth rate of the quantity of money will be accompanied by an increase in the unemployment rate.
   b. an increase in the growth rate of the quantity of money will be accompanied by an increase in the unemployment rate.
   c. policymakers are able to reduce the inflation rate and, at the same time, reduce the unemployment rate.
   d. policymakers can influence the inflation rate, but not the unemployment rate.
14. Just like models constructed in other areas of science, economic models:
   a. incorporate assumptions that contradict reality.
   b. incorporate all details about the real world.
   c. complicate reality.
   d. All of the above are correct.

15. Economists regard events from the past as:
   a. irrelevant, since history is unlikely to repeat itself.
   b. of limited interest, since those events seldom provide any useful economic data.
   c. interesting but not particularly valuable, since those events cannot be used to evaluate present-day economic theories.
   d. interesting and valuable, because those events are capable of helping us to understand the past, the present, and the future.

16. What would be the best statement about a theory based on assumptions that are not true?
   a. If the assumptions underlying the theory are not true, the theory must be false.
   b. The ideas may be good in theory, but not in practice.
   c. The theory is a good one if it helps us to understand how the world works.
   d. The theory is a good one if no logical mistakes were made in developing it.

17. Good economic models:
   a. often leave out important variables, causing serious errors.
   b. omit many details to allow us to see what is truly important.
   c. are designed to give a complete picture of a given relationship.
   d. cause economics to be misunderstood by the general public.

18. In the circular-flow diagram,
   a. factors of production flow from government to firms.
   b. goods and services flow from households to firms.
   c. income paid to the factors of production flows from firms to households.
   d. spending on goods and services flows from firms to households.

19. In the markets for the factors of production,
a. households are sellers and firms are buyers.
b. households are buyers and firms are sellers.
c. households and firms are both buyers.
d. households and firms are both sellers.

Refer to the figure below to answer questions 20.

20. Juan fills out an application to work at McDonald's and McDonald's hires him. To which of the arrows does this action directly contribute?

   a. A only.
   b. A and B.
   c. C only.
   d. C and D.

21. When an economy is operating at a point on (rather than inside) its production possibilities frontier, then:

   a. consumers are content with the mix of goods and services that is being produced.
   b. there is no way to produce more of one good without producing less of the other.
   c. equal amounts of the two goods (measured along the two axes) are being produced.
   d. All of the above are correct.
22. It is possible for an economy to increase its production of computers and, at the same time, to increase its production of cars if the economy:

a. moves downward and to the right along its production possibilities frontier and the frontier is bowed outward.
b. moves upward and to the left along its production possibilities frontier and the frontier is bowed outward.
c. moves in either direction along its production possibilities frontier and the frontier is a straight line.
d. moves from a situation of inefficient production to a situation of efficient production.

Use the figure below to answer Question 23.

23. The movement from point C to point D was most likely caused by:

a. unemployment.
b. a decrease in society's preference for bananas.
c. fewer resources available for production.
d. All of the above are correct.

24. Production possibilities frontiers can shift outward if:

a. government increases the amount of money in the economy.
b. there is an increase in technology.
c. resources can be moved from the production of one good to another.
d. Both b and c are correct.
25. In a certain economy, peanuts and books are produced, and the economy currently operates on its production possibilities frontier. Which of the following events would allow the economy to produce more peanuts and more books, relative to the quantities of those goods that are being produced now?

a. Unemployed labor is put to work producing peanuts and books.
b. The economy puts its idle capital to work producing peanuts and books.
c. The economy experiences economic growth.
d. All of the above are correct.

26. In a competitive market, each seller has limited control over the price of his product because:

a. other sellers are offering similar products.
b. in competitive markets, buyers have more influence over price than sellers.
c. the products sold in competitive markets are generally in abundant supply.
d. sellers in competitive markets prefer to meet and set a price that each will profit from.

27. A good is considered either a normal good or an inferior good based on:

a. quality of the good.
b. price of the good.
c. personal preference toward the good.
d. the amount of a person's income.

28. Ryan tells you that he thinks the price of potato chips, his favourite food, will decrease in the near future. He will probably respond by:

a. decreasing his current demand for chips.
b. not changing his current demand for chips.
c. increasing his current demand for chips.
d. currently refusing to buy anymore chips.
Use the figure below to answer Question 29.

29. The movement from point A to point B on the graph would be caused by:

a. an increase in price.
b. a decrease in price.
c. a decrease in the price of a substitute good.
d. an increase in income.

30. Lead is an important input in the production of crystal. If the price of lead increases, all else equal, we would expect the supply of:

a. crystal to be unaffected.
b. crystal to decrease.
c. crystal to increase.
d. lead to increase.

31. Suppose Spencer and Kate are the only two demanders of lemonade. Each month, Spencer buys six glasses of lemonade when the price is R1.00 per glass, and he buys four glasses when the price is R1.50 per glass. Each month, Kate buys four glasses of lemonade when the price is R1.00 per glass, and she buys two glasses when the price is R1.50 per glass. Which of the following points is on the market demand curve?

a. Quantity demanded = 4, price = $2.50.
b. Quantity demanded = 16, price = $2.50.
c. Quantity demanded = 3, price = $1.50.
d. Quantity demanded = 10, price = $1.00.
32. Which of the following would NOT affect an individual's demand curve?
   a. Expectations.
   b. Income.
   c. Price of related goods.
   d. The number of buyers.

33. The market supply curve shows:
   a. the total quantity supplied for the market at any price.
   b. the average quantity supplied for the market at any price.
   c. a ratio between price and quantity supplied for the market.
   d. a supply curve representing the 10 largest firms in the market.

Use the figure below to answer Question 34.

34. At a price of $20, which of the following statements is not correct?
   a. The market is in equilibrium.
   b. Equilibrium price is equal to equilibrium quantity.
   c. There is no pressure for price to change.
   d. The quantity of the good that is bought and sold is 600.
Use the table below to answer Question 35.

<table>
<thead>
<tr>
<th>PRICE</th>
<th>QUANTITY DEMANDED</th>
<th>QUANTITY SUPPLIED</th>
</tr>
</thead>
<tbody>
<tr>
<td>R10</td>
<td>10</td>
<td>60</td>
</tr>
<tr>
<td>R8</td>
<td>20</td>
<td>45</td>
</tr>
<tr>
<td>R6</td>
<td>30</td>
<td>30</td>
</tr>
<tr>
<td>R4</td>
<td>40</td>
<td>15</td>
</tr>
<tr>
<td>R2</td>
<td>50</td>
<td>0</td>
</tr>
</tbody>
</table>

35. In the table shown above, if the price were R8, a

a. surplus of 50 units would exist and price would tend to fall.
   b. surplus of 10 units would exist and price would tend to fall.
   c. surplus of 25 units would exist and price would tend to fall.
   d. shortage of 25 units would exist and price would tend to rise.

Use the figure below to answer Question 36.

36. Graph A shows which of the following?

a. An increase in demand.
   b. An increase in quantity demanded.
   c. An increase in quantity supplied.
   d. Both a and c are correct.
37. An increase in the number of scholarships issued for college education would:
   a. increase the supply of education.
   b. decrease the supply of education.
   c. increase the demand for education.
   d. decrease the demand for education.

38. What will happen to the equilibrium price and quantity of new cars if the price of gasoline rises, the price of steel rises, public transportation becomes cheaper and more comfortable, and auto-workers negotiate higher wages?
   a. Price will fall and the effect on quantity is ambiguous.
   b. Price will rise and the effect on quantity is ambiguous.
   c. Quantity will fall and the effect on price is ambiguous.
   d. Quantity will rise and the effect on price is ambiguous.

39. Which of the following would unambiguously cause a decrease in the equilibrium price of cotton shirts?
   a. An increase in the price of wool shirts and a decrease in the price of raw cotton.
   b. A decrease in the price of wool shirts and a decrease in the price of raw cotton.
   c. An increase in the price of wool shirts and an increase in the price of raw cotton.
   d. A decrease in the price of wool shirts and an increase in the price of raw cotton.

40. There are very few, if any, good substitutes for motor oil. Therefore,
   a. the supply of motor oil would tend to be price elastic.
   b. the demand for motor oil would tend to be price elastic.
   c. the demand for motor oil would tend to be price inelastic.
   d. the demand for motor oil would tend to be income elastic.

41. A perfectly inelastic demand curve will be:
   a. negatively sloped, because buyers decrease their purchases when the price rises.
   b. vertical, because buyers purchase the same amount whether the price rises or falls.
   c. positively sloped, because buyers respond by increasing their purchases when price rises.
   d. horizontal, because buyers increase their purchases by huge amounts with slight changes in price.

School of Accounting, Economics and Finance, UKZN, Westville and Pietermaritzburg Campus.
42. Cross-price elasticity of demand is calculated as the:
   a. percentage change in quantity demanded of good 1 divided by the
      percentage change in the price of good 2.
   b. total percentage change in quantity demanded divided by the total percentage
      change in price.
   c. percentage change in quantity demanded divided by the percentage change
      in income.
   d. percentage change in the price of good 1 divided by the percentage change
      in the price of good 2.

43. An increase in the price of pure chocolate morsels from $2.25 to $2.45 causes Nestle
    to increase production from 125 bags per minute to 145 bags per minute. We know
    that the elasticity of supply is:
    a. elastic and equal to 1.74.
    b. elastic and equal to 0.57.
    c. inelastic and equal to 0.57.
    d. inelastic and equal to 1.74.

44. If the price elasticity of demand for a good is 4.0, then a 10 percent increase in price
    would result in a:
    a. 4.0 percent decrease in the quantity demanded.
    b. 10 percent decrease in the quantity demanded.
    c. 40 percent decrease in the quantity demanded.
    d. 40 percent increase in the quantity demanded.

45. On a downward-sloping linear demand curve, total revenue would be at a maximum
    at the
    a. midpoint of the demand curve.
    b. lower end of the demand curve.
    c. upper end of the demand curve.
    d. It is impossible to tell without knowing prices and quantities demanded.

46. Because the demand for wheat tends to be inelastic, the development of a new, more
    productive hybrid wheat would tend to:
    a. increase the total revenue of wheat farmers.
    b. decrease the total revenue of wheat farmers.
    c. weaken the demand for wheat.
    d. weaken the supply of wheat.
47. Binding price ceilings result in each of the following except:

a. market inefficiency.
b. shortages.
c. seller bias.
d. surpluses.

Use the figure below to answer Question 48.

48. Which panel(s) best represent(s) a binding rent control in the long run?

a. Panel (a).
b. Panel (b).
c. Neither panels.
d. Both panels.

49. Under rent control, bribery is a mechanism to:

a. bring the total price of an apartment (including the bribe) closer to the equilibrium price.
b. allocate housing to the poorest individuals in the market.
c. force the total price of an apartment (including the bribe) to be less than the market price.
d. allocate housing to the most deserving tenants.
50. In general, advocates of the minimum wage:

   a. believe that there are no adverse effects of minimum-wage laws.
   b. believe that adverse effects are small, and generally a higher minimum wage makes the poor better off.
   c. believe that the minimum wage is the answer to society's economic problems.
   d. are socialists who want to replace the market system with central economic planning.

51. Unlike minimum wage laws, wage subsidies:

   a. discourage firms from hiring the working poor.
   b. cause unemployment.
   c. help only wealthy workers.
   d. raise living standards of the working poor without creating unemployment.

52. A burden of tax on yachts will:

   a. be borne by the rich and by the poor equally.
   b. fall more heavily on the rich consumers rather than the producers because the demand for yachts is relatively more elastic.
   c. fall more heavily on the producers because supply of yachts is relatively inelastic.
   d. fall more heavily on producers of yachts because the supply of yachts is relatively more elastic compared to the demand for yachts.
Use the figure below to answer Questions 53 and 54.

53. The price buyers pay after the tax is imposed is:
   a. $18.00.
   b. $14.00.
   c. $12.00.
   d. $8.00.

54. The amount of the tax imposed in this market is:
   a. $10.00.
   b. $6.00.
   c. $4.00.
   d. $2.00.

55. Buyers of a product will pay the majority of a tax placed on a product when:
   a. supply is more elastic than demand.
   b. the demand is more elastic than supply.
   c. the tax is placed on the seller of the product.
   d. the tax is placed on the buyer of the product.

56. The amount of money that a firm pays for all its inputs is called:
   a. total cost.
   b. variable cost.
   c. marginal cost.
   d. fixed cost.
57. Which of the following can be added to profit to obtain total revenue?
   a. Net profit.
   b. Capital profit.
   c. Operational profit.
   d. Total cost.

58. Those things that must be forgone to acquire a good are called:
   a. substitutes.
   b. opportunity costs.
   c. explicit costs.
   d. competitors.

59. Explicit costs:
   a. require an outlay of money by the firm.
   b. include all of the firm’s opportunity costs.
   c. include income that is forgone by the firm’s owners.
   d. Both b and c are correct.

60. Economic costs:
   a. will always be less than accounting costs.
   b. are always equal to accounting costs.
   c. are always greater than accounting costs because they include implicit costs.
   d. are less than or greater than accounting costs depending on output produced.

61. Which of the following expressions is correct?
   a. Accounting profit = economic profit + implicit costs.
   b. Accounting profit = total revenue - implicit costs.
   c. Economic profit = accounting profit + explicit costs.
   d. Economic profit = total revenue - implicit costs.

Refer to the following scenario to answer Questions 62 and 63.

Zach took R400,000 out of the bank and used it to start his new cookie business. The bank account pays 3 percent interest per year. During the first year of his business, Zach sold 6,000 boxes of cookies for R2.50 per box. Also, during the first year, the cookie business incurred costs that required outlays of money amounting to R9,000.
62. Zach's accounting profit for the year was:
   a. $-494,000.
   b. $-6,000.
   c. $6,000.
   d. $12,000.

63. Zach's economic profit for the year was:
   a. $-506,000.
   b. $-6,000.
   c. $3,000.
   d. $6,000.

64. Marginal cost is at its lowest when:
   a. average total cost is at its minimum.
   b. average variable cost is at its maximum.
   c. marginal productivity of labour is at its peak.
   d. None of the above.

65. Marginal product of labour is equal to the:
   a. incremental cost associated with a one unit increase in labour.
   b. incremental profit associated with a one unit increase in labour.
   c. increase in labour necessary to generate a one unit increase in output.
   d. increase in output obtained from a one unit increase in labour.

66. When adding another unit of labour leads to an increase in output that is smaller than the increases in output that resulted from adding previous units of labour, we have the property of:
   a. diminishing labour.
   b. diminishing output.
   c. diminishing marginal product.
   d. negative marginal product.
Refer to the figure below concerning cookie production to answer Questions 67 and 68.

67. As the number of workers increases:
   a. total output increases, but at a decreasing rate.
   b. marginal product increases, but at a decreasing rate.
   c. marginal product increases at an increasing rate.
   d. total output decreases.

68. With regard to cookie production, the figure implies:
   a. diminishing marginal cost of cookie production.
   b. decreasing cost of cookie production.
   c. diminishing marginal product of workers.
   d. increasing marginal product of workers.

69. Average fixed costs continually decline precisely because:
   a. the average total costs are constantly decreasing.
   b. output keeps increasing and the fixed cost component is spread across increasing production.
   c. marginal cost is also declining.
   d. Both a and b are correct.

70. The profit maximizing rule:
   a. is the equality of marginal cost and marginal revenue.
   b. depends on the firm’s ability to charge the highest price possible.
   c. is the equality of average total cost with marginal cost.
   d. is dependent on achieving highest attainable output.
71. Which of the following is not a characteristic of a perfectly competitive firm?

(i) free entry and exit  
(ii) no control over the market price  
(iii) normal profits for all firms in the long run

a. (i) only.  
b. (ii) only.  
c. none of the above.  
d. (i) and (iii).

Refer to the Table below to answer Questions 72 to 75.

<table>
<thead>
<tr>
<th>Quantity</th>
<th>Price</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>13</td>
</tr>
<tr>
<td>2</td>
<td>13</td>
</tr>
<tr>
<td>3</td>
<td>13</td>
</tr>
<tr>
<td>4</td>
<td>13</td>
</tr>
<tr>
<td>5</td>
<td>13</td>
</tr>
<tr>
<td>6</td>
<td>13</td>
</tr>
<tr>
<td>7</td>
<td>13</td>
</tr>
<tr>
<td>8</td>
<td>13</td>
</tr>
<tr>
<td>9</td>
<td>13</td>
</tr>
</tbody>
</table>

72. The price and quantity relationship in the table is most likely that faced by a firm in a:

a. monopoly.  
b. concentrated market.  
c. perfectly competitive market.  
d. strategic market.

73. Over which range of output is average revenue equal to price?

a. 1 to 5.  
b. 3 to 7.  
c. 5 to 9.  
d. Average revenue is equal to price over the whole range of output.

74. Over which range is marginal revenue declining?

a. None; marginal revenue is constant over the whole range of output.  
b. 1 to 6.  
c. 3 to 7.  
d. 7 to 9.

75. If the firm doubles its output from 3 to 6 units, total revenue will:

a. increase by less than $39.  
b. increase by exactly $39.  
c. increase by more than $39.  
d. It cannot be determined from the information provided.
76. In a competitive market, no single producer can influence the market price because:

a. many other sellers are offering a product that is essentially identical.
b. consumers have more influence over the market price than producers do.
c. government intervention prevents firms from influencing price.
d. producers agree not to change the price.

Refer to the figure below to answer Questions 77 and 78.

77. When the price rises from $P_2$ to $P_3$, the firm finds that:

a. marginal cost exceeds marginal revenue at a production level of $Q_2$.
b. if it produces at output level $Q_3$ it will earn a positive profit.
c. expanding output to $Q_4$ would leave the firm with losses.
d. it could increase profits by lowering output from $Q_3$ to $Q_2$.

78. When the price falls from $P_3$ to $P_1$, the firm finds that:

a. fixed cost is higher at a production level of $Q_1$ than it is at $Q_3$.
b. it should produce $Q_1$ units of output.
c. it should produce $Q_3$ units of output.
d. it should shut down immediately.
Refer to the figure below to answer Question 79.

79. When market price is \( P_5 \), a profit-maximizing firm's profits can be represented by the area:

a. \( P_5 \) \( Q_3 \).
b. \( (P_5 - P_3) \) \( Q_2 \).
c. \( (P_5 - P_4) \) \( Q_3 \).
d. When market price is \( P_5 \) there are no profits.

80. Suppose a competitive market is comprised of firms that face identical cost curves. The firms experience an increase in demand that results in positive profits for the firms. Which of the following events are then most likely to occur?

(i) New firms will enter the market.
(ii) In the short run, price will rise; in the long run, price will rise further.
(iii) In the long run, all firms will be producing at their efficient scale.

a. (i) and (ii) only.
b. (i) and (iii) only.
c. (ii) and (iii) only.
d. (i), (ii) and (iii).