Name (please print) ___________________________________

Assigned Seat _______________________

DIRECTIONS: Put all your answers on the attached answer sheet. No credit will be given for answers placed elsewhere. Unless indicated otherwise, each question is worth 1 point.

To answer the next 6 questions, suppose that a small island economy has 10 Iowans and 20 Nebraskans. Each Iowan is capable of making 6 straw hats or 3 rugs in a day. Each Nebraskan is capable of making 5 straw hats or 2 rugs in a day.

1. Who has the comparative advantage in making rugs?

2. (3 points) Draw the PPF for this economy in the space below. Place a numerical value on the vertical intercept, the horizontal intercept, and point at which there is a "kink" in the PPF.

3. If the economy produces 120 straw hats, what is the maximum number of rugs it can produce?

4. If the economy produces 120 straw hats efficiently, _____ hats will be produced by the Iowans and _______ hats will be produced by the Nebraskans.

5. The absolute value of the slope of the PPF is the opportunity cost of _______.
   a. rugs     b. hats
6. In order to achieve the maximum gains from trade, people should specialize according to:
   a. property rights.
   b. absolute advantage.
   c. comparative advantage.
   d. the production possibilities frontier.

7. Suppose that the economy is producing an amount of gasoline where the marginal benefit of gasoline exceeds its marginal cost. On the basis of this information, it would be correct to conclude:
   a. the economy is producing more than the technologically efficient amount of gasoline.
   b. the economy is producing less than the technologically efficient amount of gasoline.
   c. the economy is producing less than the allocatively efficient amount of gasoline.
   d. the economy is producing more than the allocatively efficient amount of gasoline.

8. If the marginal cost of gasoline decreases,
   a. the technologically efficient amount of gasoline increases.
   b. the technologically efficient amount of gasoline decreases.
   c. the allocatively efficient amount of gasoline decreases
   d. the allocatively efficient amount of gasoline increases

To answer the next 3 questions, refer to the supply/demand diagram for gasoline below.

9. If the price of gasoline is $1.10, there is a (shortage, surplus) of _______ million gallons per day.

10. If the price of gasoline is $1.10, quantity supplied is ______ and quantity demanded is ______.

11. A surplus of gasoline would be created by:
   a. a price floor below $1       b. a price ceiling below $1
   c. a price floor above $1      d. a price ceiling above $1
12. Demand would shift right if:
   a. the price of a substitute in production increases.
   b. the price of a substitute in consumption increases.
   c. the price of a complement in consumption increases.
   d. the good is inferior and consumer income increases.

13. Poor weather conditions in California have resulted in a relatively small crop of lettuce this year. As a consequence, we should expect a (higher, lower) equilibrium price and a (higher, lower) equilibrium quantity of lettuce.
   a. higher; higher  b. higher; lower  c. lower; higher  d. lower; lower

14. Given the consequences of the small lettuce crop, we should expect to see that in the market for salad dressing equilibrium prices will (rise, fall) and equilibrium quantities will (rise, fall).
   a. rise; rise  b. rise; fall  c. fall; rise  d. fall; fall

15. Glass manufacturers are capable of using their facilities to produce either glass bottles or glass bowls. An increase in the demand for glass bowls would cause:
   a. a decrease in the supply of glass bottles.
   b. a decrease in the demand for glass bottles.
   c. an increase in the supply of glass bottles.
   d. a decrease in the supply of glass bottles.

16. Which of the following would lead to an increase in the equilibrium price but a decrease in the equilibrium quantity of memory chips for computers?
   a. improved technology which reduces the cost of manufacturing the chips.
   b. an increase in the cost of material used to manufacture the chips.
   c. an increase in consumer income, assuming computer chips are normal goods.
   d. none of the above.
17. Using the demand curve for gasoline above, compute the elasticity of demand between the price of $1.00 and $1.10.

If the elasticity of demand for bus fares is .5, a 20% increase in bus fares would cause
18. ridership to fall by _______ percent.
19. total revenue for the bus company to (rise, fall) by _______ percent.

20. If the demand for bananas is elastic, a decrease in banana prices would cause total revenue from bananas to
a. rise       b. fall.

21. Demand for a product tends to be more inelastic if:
a. there are many substitutes for the product.
b. there are few substitutes for the product.
c. the product represents a large share of the typical consumer’s budget.
d. both b and c
 e. both a and c.

22. If the income elasticity of demand for a product is positive, it is
a. a normal good.
b. an inferior good.
c. a Giffen good.

23. The cross-price elasticity of demand for Pepsi and Coke is likely to be:
a. positive.
b. negative.
c. zero.
24. If the price elasticity of supply for gasoline is .5, a 10 percent increase in the quantity supplied of gasoline would require a ____ percent increase in the price of gasoline.

25. With a linear demand curve, the price elasticity of demand
   a. increases as the price increases.
   b. decreases as the price increases.
   c. does not change as the price increases.

26. Suppose there is an increase in the demand for lettuce. The size of the resulting price increase will be greater if the supply of lettuce is:
   a. elastic
   b. inelastic.

27. If a 10 percent increase in income causes a 5 percent decrease in the demand for Sam’s Cola, the income elasticity of demand is _______ (be sure to indicate whether positive or negative!)

28. According to the article posted on the web, lower income people (or countries) tend to have:
   a. a higher income elasticity of demand for cigarettes.
   b. a lower income elasticity of demand for cigarettes.
   c. a higher price elasticity of demand for cigarettes.
   d. a lower price elasticity of demand for cigarettes.

29. According to the article posted on the web, younger people (or countries) tend to have:
   a. a higher income elasticity of demand for cigarettes.
   b. a lower income elasticity of demand for cigarettes.
   c. a higher price elasticity of demand for cigarettes.
   d. a lower price elasticity of demand for cigarettes.

30. According to the article posted on the web, the demand for a bus ride is
   a. more price elastic during “peak” hours.
   b. more price inelastic during “peak” hours.
   c. more income elastic during peak hours.
   d. more income inelastic during peak hours.
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