Exercise: Unit I

14.5 / 15

Name___

Lab Day/Time 12:00-12:50 Thurs.

Lab Instructor Carlstrom

1. Suppose the bookstore increases the price of pencils by 100%. Will this price increase raise or lower the bookstore's total revenues? Why or why not?

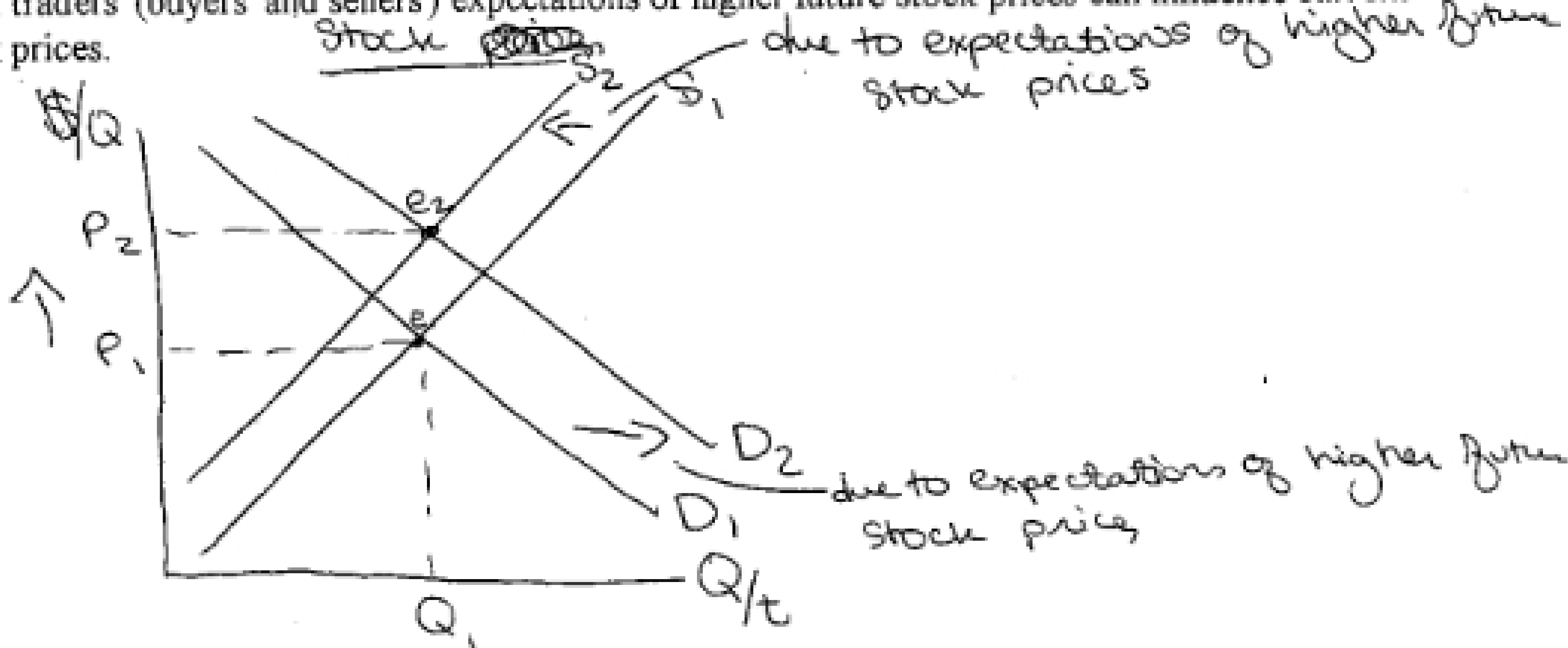
$E_d = \left| \frac{\% \Delta Q_D}{\% \Delta P} \right| = \Rightarrow E_d < 1$, inelastic, P↑, TR↑

$\Rightarrow E_d > 1$, elastic, P↑, TR↓

Because the $\% \Delta Q_D$ is unknown, the E_d can either be greater than one which means an increase in price and increase in total revenue thereby making it inelast or $E_d > 1$ which means the price increase + total revenue decrease thereby making it elastic.

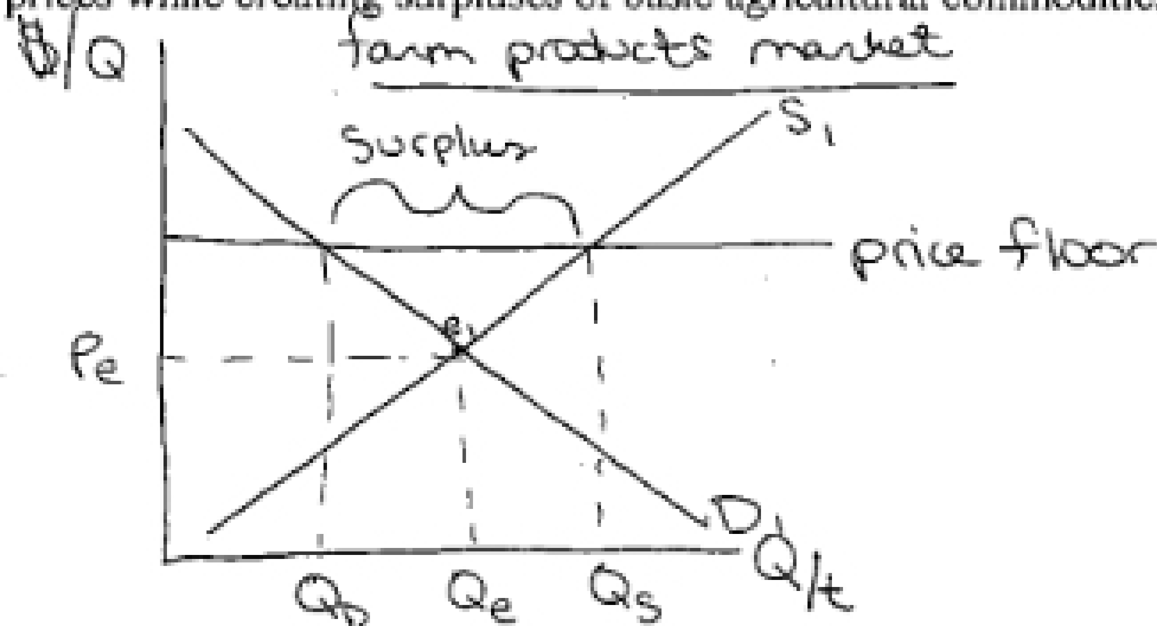
−1/2

2. Use a competitive market supply/demand diagram and brief verbal descriptions to explain how stock traders' (buyers' and sellers') expectations of higher future stock prices can influence *current* stock prices.



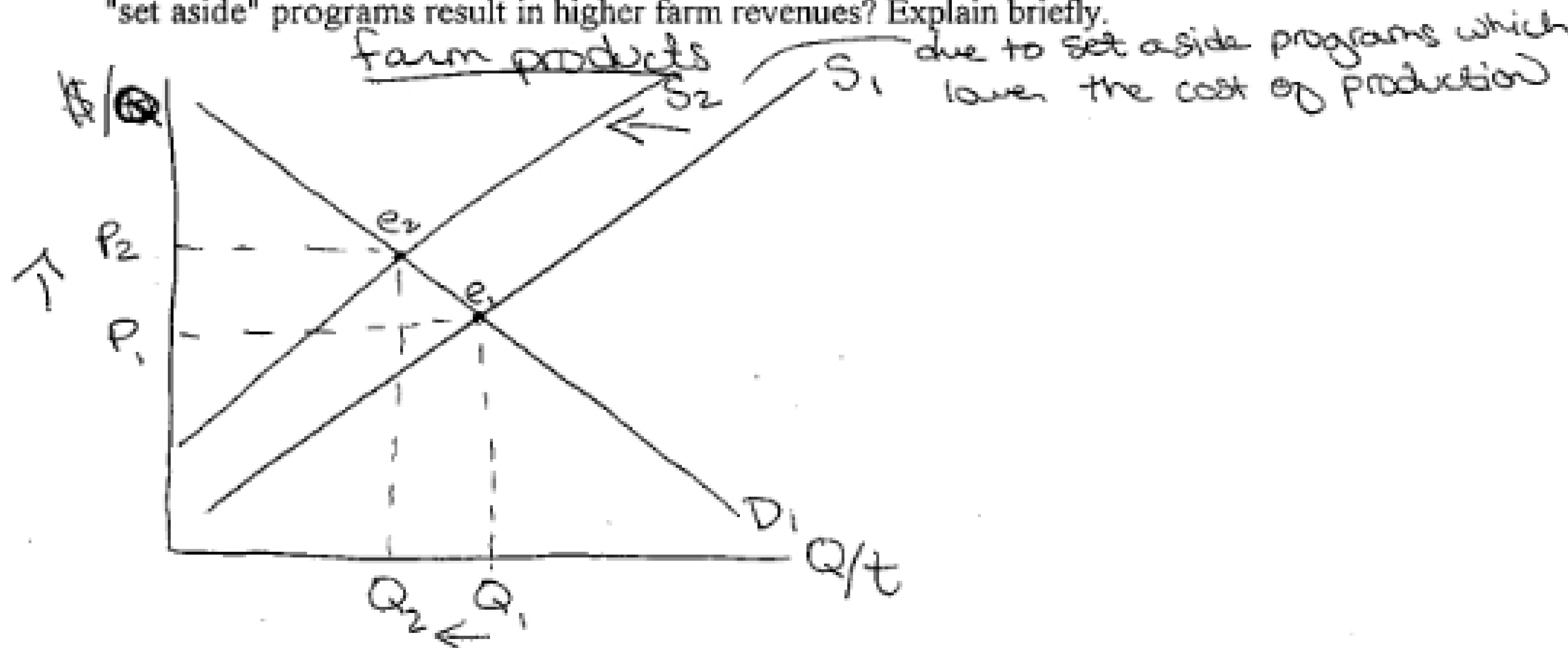
With the expectations of higher future stock price, demand increase and supply decreases. This causes the price to increase + the Quantity is ambiguous

3. Use a competitive supply/demand diagram of the farm products market and brief verbal descriptions to explain the following: "Agricultural price supports (legal price floors) raise food prices while creating surpluses of basic agricultural commodities."



when the price floor is enacted the price is raised above equilibrium. ~~too low~~ This ~~creates~~ means that the Quantity supplied is greater than the Quantity demanded and this creates a surplus of basic agricultural commodities

4. Acreage "set aside" programs are designed to reduce the supply of farm products *and* increase the total revenues of farmers. (1) Use a competitive supply/demand diagram to illustrate a decrease in the supply of farm products. (2) Under what conditions of demand elasticity will the "set aside" programs result in higher farm revenues? Explain briefly.



$\left|\frac{\%\Delta Q_d}{\%\Delta P}\right| = E_d < 1$, this diagram shows that the market is relatively inelastic. The increase in Price, decrease in Quantity from the reduction of supply results in higher total revenues. The % change in Q_D was less than % change in price showing that it is more inelastic

Exercise: Unit II

14/15

Name

Lab Day/Time Thurs. 12:00-12:50

Lab Instructor Adam Carlstrom

1. Define average propensity to consume (APC) and marginal propensity to consume (MPC). Briefly discuss Keynes' views concerning the APC and MPC.

APC = the fraction of disposable (or after tax) income devoted to consumer spending

MPC = the change in consumer spending due to an increase in disposable (or after tax) income

Keynes = • MPC is always between 0 and one
• APC declines when disposable income increas

At some level of Y_d, consumer spending = Y_d

2. Consider the following consumption function: $C = 5000 + .75\ Y_d$

a. How much would consumer spending amount to for a family with after-tax income of $20,000? (Show your calculations). Is this family "breaking even"? Why or why not?

$C = 5000 + .75(20000)$
$C = 5000 + 15{,}000$
$C = 20000$

The family is breaking ev b/c the amount of consump is the same as the amoun of disposable income, zero savings

savings = $Y_d - C$
= 20000 − 20000 = 0 = savings = break even

b. What is the APC and level of savings (S) of a family with disposable income of $100,000? (Show your calculations).

$C = 5000 + .75(100000)$
$C = 5000 + 75000$
$C = 80000$

APC = $\frac{80{,}000}{100000} = \frac{C}{Y_d} = .8$ (APC)

savings = $Y_d - C$
= 100000 − 80000 = 20,000.00 = savings (S)