~~Q of~~ PPC: Q1, Q9, Q10, Q15, Q18, Q24, Q27, Q30, Q31, Q34.

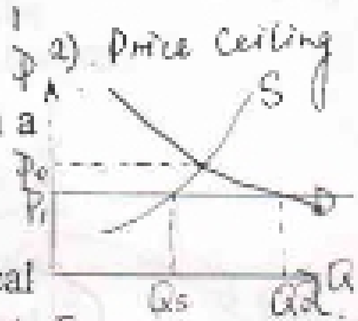
Tax Burden: 3. 5. 7. 13 17 19 (same as 17)

Exam 1 Sample Questions Same

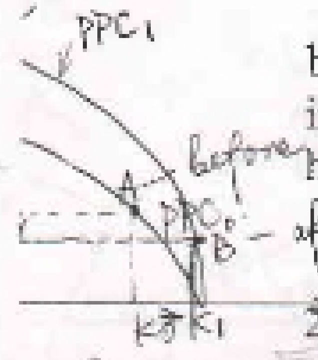
Same as Q18

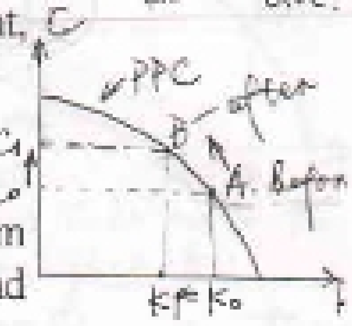
1. Suppose that the economy produces two types of goods: consumer goods (C) and capital goods (K). Use production possibilities curve (PPC) diagrams and brief verbal explanations to explain the following situations:

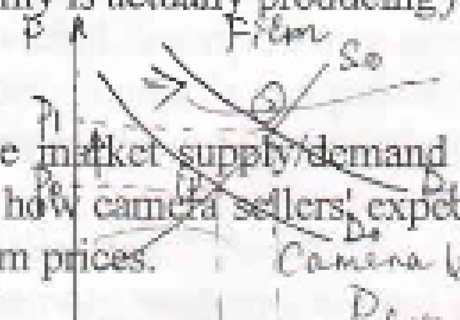
a. The economy is operating at full-employment producing a lot of capital goods when a legal price ceiling is imposed on capital goods. P↓ Qs of K ↓



b. The economy is operating at full-employment both before and after a major technological improvement in the production of consumer goods. After the technological improvement, however, the economy is actually producing *fewer* consumer goods than before.

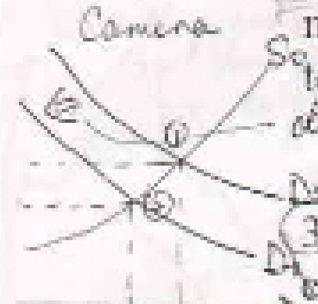




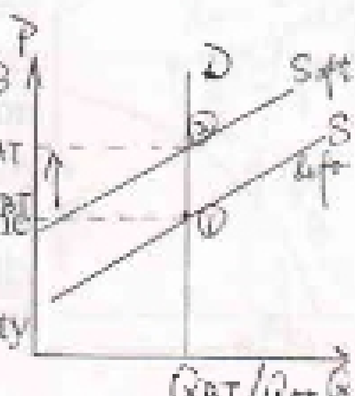


due to P↑

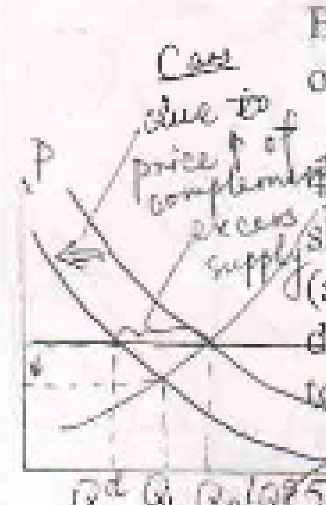
2. Use competitive market supply/demand diagrams of the camera market *and* the film market to illustrate how camera sellers' expectations of lower future camera prices can lead to higher current film prices. Camera & Film are complementary goods P future camera ↓, P↓Q current camera ↓ Q current film ↑



3. Use a competitive market supply/demand diagram and brief verbal descriptions to explain how the entire economic incidence of a per-unit excise tax may fall on gasoline buyers even though the tax is legally imposed exclusively on gasoline sellers. $E_D = 0$.
Briefly explain the determinants of price elasticity of demand (E_d). Why is price elasticity of demand an important concept? ① # of substitutes ② fraction of Income ③ Time period (adjustment) ④ Taste necessities / luxuries
Definition + TR + Tax Burden

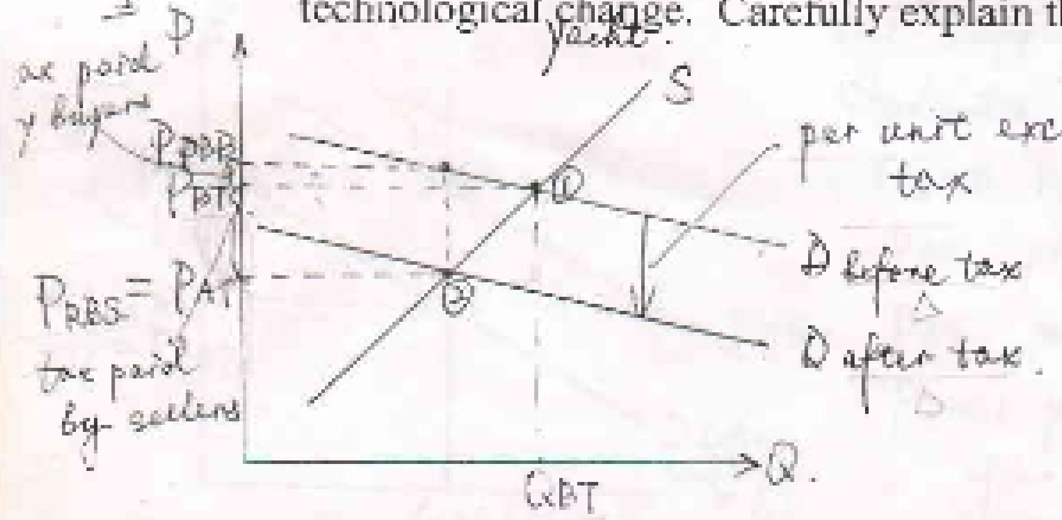


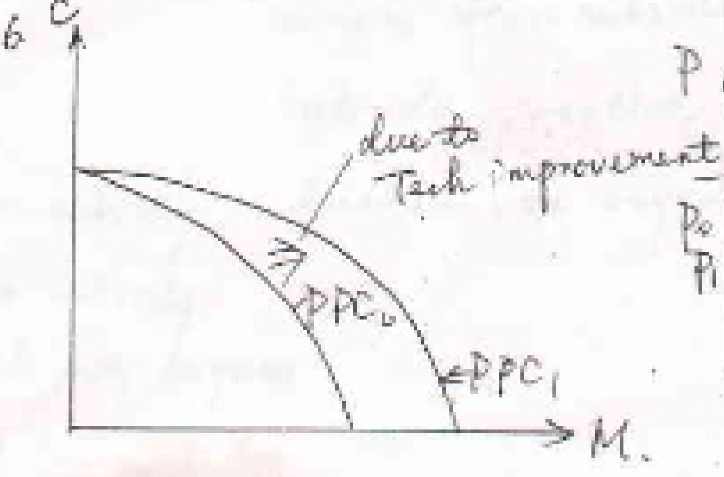
4. Consider the following: "The sharp rise in gasoline prices in the mid 1970's lead to a sharp decline in the demand for 'gas guzzling' cars and large unsold inventories (surpluses) when many dealers refused to cut their sticker prices." Use a supply/demand diagram of the 'fuel inefficient' or 'gas guzzling' car market and brief verbal descriptions to explain this quotation $Q_d < Q^S \Rightarrow$ excess supply.
gas & cars are complementary goods $P_g \uparrow \Rightarrow Q_{car} \downarrow$.

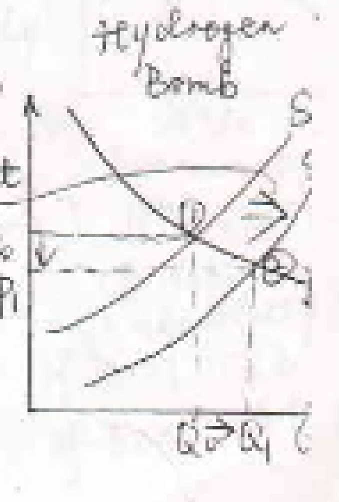


5. In 1990, Congress passed a per-unit excise tax on yachts. The tax was legally imposed on the buyers of these luxury goods. Within a year, a number of New England yacht building firms failed and their unemployed workers protested vigorously. Interestingly, yacht buyers voiced little concern about the tax. Use a supply/demand diagram of the yacht market and your knowledge about the legal and economic incidence of a per-unit excise tax to explain this episode. Luxury good ⇒ high E_D ⇒ economic incidence more fall on sellers.

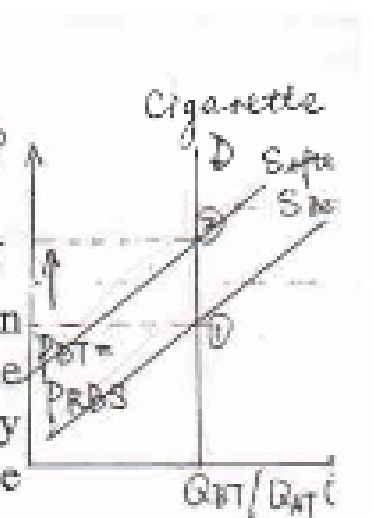
6. Suppose there is a technological advance in the production of hydrogen bombs. Use a supply/demand diagram of the hydrogen bomb market *and* a production possibilities curve (PPC) diagram showing 'military' and 'civilian' goods to illustrate this technological change. Carefully explain the connection between your diagrams.





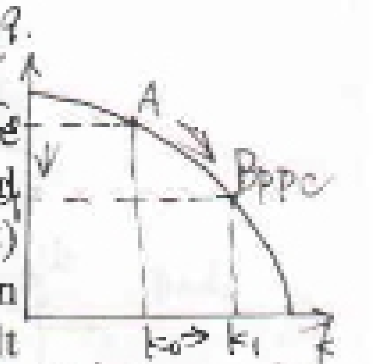


tax → price
excise shift

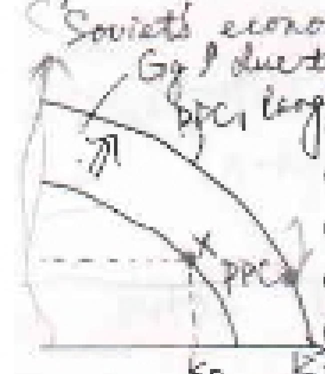


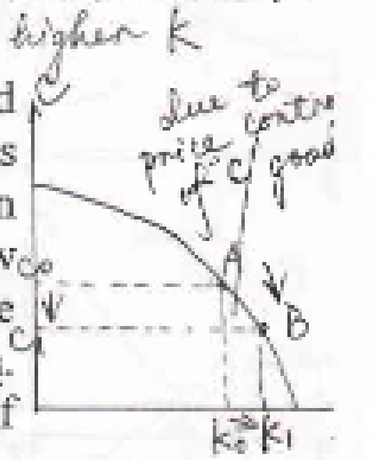
7. Recently, the Clinton administration proposed a $1.00 per-unit (pack) excise tax on cigarettes (which would be imposed *legally or statutorily* on cigarette *sellers*). Some news reports have suggested that the proposed tax would increase cigarette prices by $1.00 per pack and be paid entirely by smokers (cigarette *buyers*). Using a competitive supply/demand diagram of the cigarette market, carefully *show* and *explain* the circumstances under which these new reports would be true. $E_D = 0$ Demand is Inelastic.

8. Why are there so many different nominal interest rates? Explain carefully.

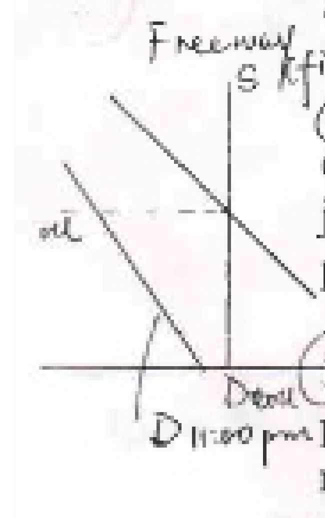


9. Consider an economy that produces consumer goods and capital goods. Suppose the economy is operating at full-employment and all consumer goods are subject to legal price ceilings set below equilibrium prices. Use a production possibilities curve (PPC) diagram and brief verbal descriptions to compare this economy's production combination in the absence of price controls (15 points). In this case, would the price controls result in higher or lower rates of future economic growth? Why? price ceiling on C → less C & more K
higher future Growth → higher K

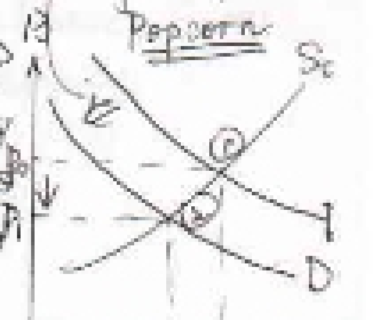




10. Consider the following: "Under the Five Year Plans, the Soviet leadership mandated a production mix heavily weighted toward capital goods. As a consequence, the Soviets enjoyed some years of significant economic growth. Coupled with price controls on consumer goods, however, the Plans also meant that Soviet citizens had very few consumer goods to satisfy their collective wants." Use a production possibilities curve (PPC) diagram and brief verbal descriptions to explain the Soviets' economic growth. Use another PPC diagram and brief verbal description to explain the small number of Soviet consumer goods.



11. Suppose the out-of-pocket price for driving on a freeway is zero. Now, use a competitive supply/demand diagram of the "freeway space" market to explain traffic jams at 8:00 am, but no jams at 11:00 pm. Also, use your diagram to explain the toll price that would eliminate the morning traffic jams. The supply of freeway is inelastic.

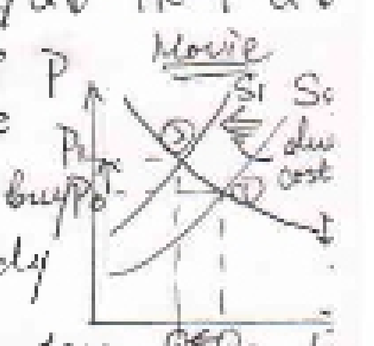


12. Suppose the State legislature passes a $10.00 per credit hour tuition subsidy legally payable to OU students. Use a supply/demand diagram of the OU educational services market to explain the conditions under which the entire economic benefit of the subsidy would flow to the University (not the students).

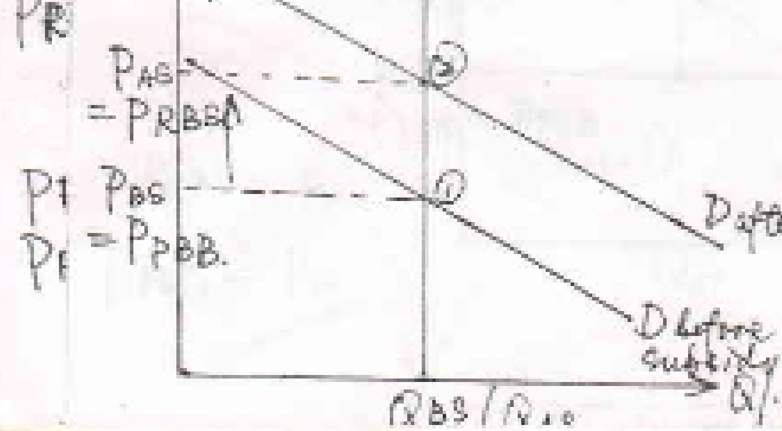
P_m ↑ Q_p ↓

13. Suppose that movies and popcorn are complimentary goods. Further suppose that screenwriters' wages (a major cost of producing movies) increase sharply due to a new union contract. Using *separate* competitive supply/demand diagrams of the movie *and* popcorn markets, illustrate and briefly explain the probable effects of the screenwriters' wage increase on: Equilibrium prices, equilibrium quantities, and total revenues in the movie and popcorn markets.

For popcorn P↓ Q↓ TR = P×Q ↓



For movies P↑ Q↓
TR depends on elasticity
if $E_D > 1$ TR↓
if $E_D < 1$ TR↑



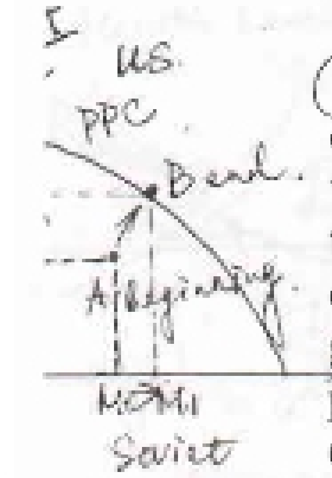
OU: Supply
Students: Demand
$E_D = 0$ Inelastic
P_{BS}: price before subsidy.
P_{AS}: price after subsidy
P_{PBB}: price paid by buyers after subsidy

P_{RBS}: price received by sellers after subsidy

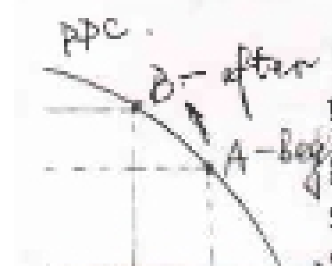
subsidy: negative tax burden (on buyers)

Same as I

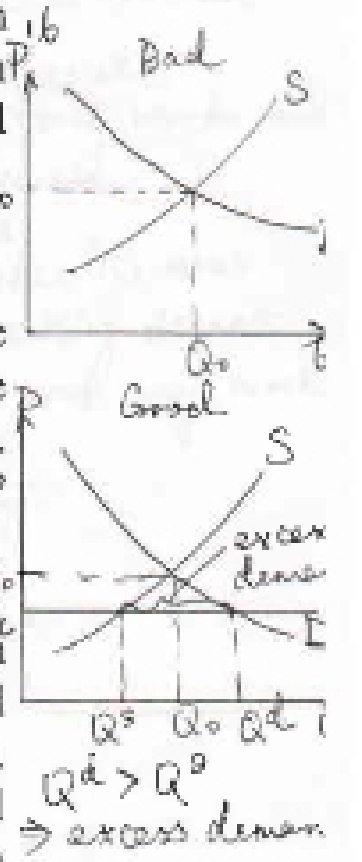
14. In 1992, Congress passed a per-unit excise tax on yachts. Although legally the tax was to be collected from yacht suppliers, the law was intended to make the rich yacht buyers pay more of the tax burden. The tax was repealed in 1993 in response to the vigorous protests of *yacht manufacturers and their workers*. Use a competitive supply/demand diagram of the yacht market and your knowledge of economic tax incidence to these events. Economic Incidence fell on sellers.
yachts ⇒ E_D ↑ ⇒ tax fall on sellers



15. Consider the following: "At the beginning of 1940, the United States economy was characterized by substantial unemployment. The Soviet economy at that time, however, was operating at full-employment. By the end of the year, the U.S. economy had moved to full-employment, increasing its output of *both* civilian and military goods. The Soviet economy was still at full-employment at year's end, but producing many fewer civilian goods and many more military goods than at the beginning of the year." Use production possibilities curve (PPC) diagrams of the U.S. and Soviet economies to illustrate and explain these historical events.



16. Suppose there are two types of OU football tickets: (1) good tickets and (2) bad tickets. Further suppose that the bad ticket market is in equilibrium at $35/ticket, but the good ticket market is not in equilibrium at that price. Draw separate competitive supply/demand diagrams of the good and bad ticket markets to explain this situation. Specifically, what disequilibrium situation do you expect in the good ticket market? Why?



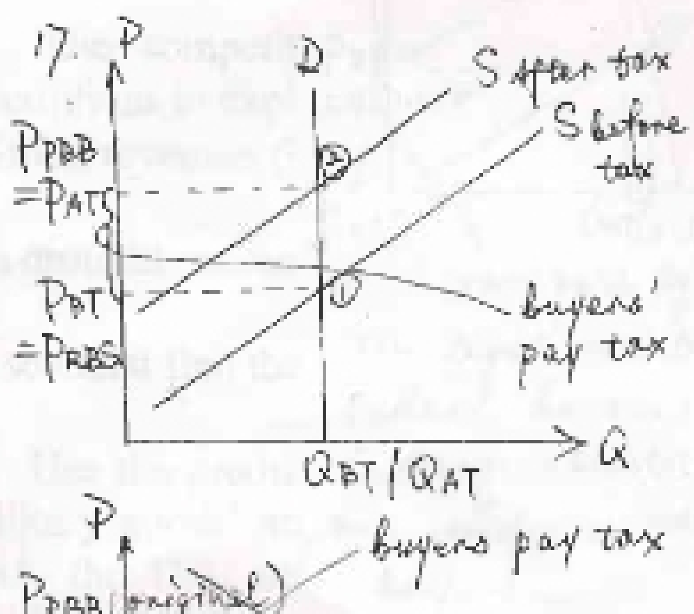
17. Recently, Congressional Republicans wanted to repeal a 4.3 per-gallon excise tax on gasoline (which is statutorily or legally imposed on gasoline sellers). They claimed removing the tax would lower gasoline prices (paid by buyers) by the full 4.3 cents. Using competitive supply/demand diagrams of the gasoline market and brief verbal descriptions, carefully explain two different market conditions under which this claim would be true. gasoline ⇒ $E_D = 0$ inelastic demand or supply is perfect elastic $E_S = 1$
solve as what condition that tax paid by buyers entirely

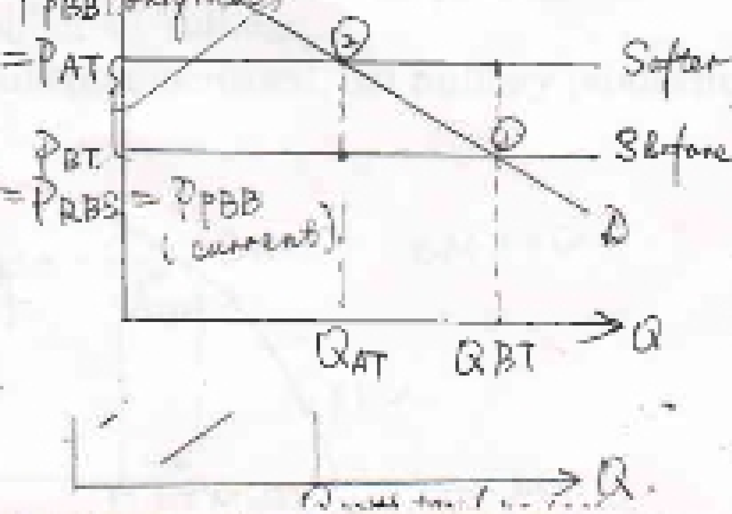
Same as II

18. ... ypes of goods: consumer goods (c) and capital go... es curve (PPC) diagrams and brief verbal de... ions:

a. ... ployment producing a lot of consumer goods wh... nsumer goods.

b. ... mployment both before and after a major tec... ion of capital goods. After the technological im... actually producing fewer capital goods than bef...





P_{RBS} = P_n

P_{PBB} = P_n