Wilfrid W. Csaplar Jr. Principles of Microeconomics Review Sheet for Exam 2

This review sheet is intended to cover everything that could be on the exam; however, it is possible that I will have accidentally left something off. You are still responsible for everything in the chapters covered except anything that I explicitly say you are not responsible for. Therefore, if I left something off of this sheet, it can still be on the exam. There will be no multiple-choice questions. Most of the questions will be like the ones in the homework assignments, and possibly a few definition questions, but I am more likely to ask questions that make you use the definitions rather than recite them. I will probably ask one of the questions from the book at the end of the chapters.

The review session will be at a time to be determined in class, probably Sunday, 10/05 in the normal room.

Chapter 5: What are negative externalities and positive externalities? How are they seen on the graph? What is the best way to offset them? Show that on the supply and demand diagram. Know the economic reasons for *providing a legal system, promoting competition, providing public goods, merit goods, demerit goods,* and *income redistribution.* What is the difference between voting and spending?

Chapter 6: How do we calculate *marginal tax rate, average tax rate,* and *total taxes paid*? What is meant by proportional, progressive, and regressive taxes? What is the tax base? How can increasing a tax result in less revenue? What are sales, excise, ad valorem, specific (unit) taxes? What is the Laffer Curve? The book actually draws it in Chapter 13. What are Medicare and Social Security? What are their effects on the economy? What is the problem with Social Security? What are some of the proposals for solving the problem? What are the pluses and minus of using each "solution"? I am most likely to give you a proposal for a solution and ask you how it would work, and whether or not you would implement my proposal.

Chapter 20: What is meant by "utility"? Be able to fill in a table like the one we did in class for quantity, total utility, average utility, and marginal utility. Be able to plot them. What is meant by diminishing marginal utility? Understand the economic reason why $MU_X/P_X = MU_Y/P_Y$ is utility maximizing. What are the income and substitution effects? How do they relate to the demand curve?

Chapter 21, up through page 538: How do you calculate the price elasticity of demand? Note that if you average the prices and quantities, then you are using "arc elasticity" otherwise you are using "point elasticity." What do the different elasticities of demand look like on a demand curve? I.e., which elasticities yield flat curves and which yield steep curves? Note that because the elasticity of demand is different at every point on a straight-line demand curve, you can only use the slope to compare two demand curves at the one point where they cross. How does the elasticity relate to marginal revenue (MR)? What determines if the price elasticity of demand is elastic, inelastic, or unitary elastic? The main determinant is the number, price, and quality of substitutes. However, the percentage of budget and the amount of time also make a difference. Page 539 (cross price elasticity of demand) and on will be on test #3.

This is the non-graded Assignment #4A that will be reviewed with Assignment #4.

1) (20 points) Fill in the table to the right. Show all work.

Q	Total Utility	Marginal Utility	Average Utility
0			
2	20		
4	32		
6	36		
8	36		

2) (10 points) Explain the reason why $MU_X/P_X = MU_Y/P_Y$ will result in utility maximization.

3) (15 points) Suppose that at a price of \$5/gallon, you buy 10 gallons of milk, but at a price of \$4/gallon, you buy 14 gallons of milk. What is the elasticity of demand? Use both arc and point elasticity methods. Is that elastic, inelastic, or unitarily elastic?

4) (10 points each) For each of the following goods, what number would you estimate to be the elasticity of demand? Explain your logic.

A) Bananas

B) Food

C) Housing

D) A house on Logan Court in Bethany, WV.

5) (15 points) Do elastic or inelastic goods have a larger marginal revenue? Explain your logic.