

Place your name on the back of this sheet of paper and nowhere else. Staple your answers on the front of this sheet of paper. Failure to follow these directions will cost you 1 point. Your assignment will be typed, except graphs can be drawn by hand and mathematical equations can be done by hand. Failure to type it will cost you 10 points. If you use double-sided printing or print on the back of scrap paper, I will give you one additional point.

- 1) (20 points) Draw the supply and demand for milk. Milk used to have a price floor. Draw the price floor. Explain the problem which it causes. What happens if the government does nothing about the problem?
- 2) (20 points) Draw the supply and demand for rental housing. Some places have rent controls, i.e., price ceilings. Show how this hurts the consumer.
- 3) (30 points) Draw the supply and demand for a product which creates air pollution like a coal burning power plant. Prove that the socially optimal consumption of electricity is not achieved and the price of electricity is too low. What do economists say is the best solution to fighting the pollution? Illustrate that on your diagram. Explain why the line(s) moved as drawn and prove that the socially optimal price and quantity are achieved. Who pays the costs of the government action?
- 4) (20 points) Draw the supply and demand for a good like a garden which creates a positive externality. Prove that the socially optimal price and quantity of that good is not achieved by the market. Do NOT worry about correcting it.
- 5) (10 points) The book says that income redistribution is a non-economic argument for having a government. I say it is also an economic reason for having a government. Explain my logic.