

Write your name on the cover of the test booklet and nowhere else. Enclose this sheet with the booklet. Failure to follow these directions will cost you 1 point. The test has 100 points (to be scaled up to 150 points) and is scheduled to take 50 minutes. Therefore, expect to spend 1 minute for every 2 points. For example, a 14-point question should take 7 minutes. I cannot give extra time because some students have a class after your class.

1) (10 points) Define EITHER *adverse selection* OR *moral hazard*.

2) (10 points) Answer EITHER Part A OR Part B.

A) According to the BBC (<http://news.bbc.co.uk/2/hi/8718696.stm>) citing the South African Public Service Commission, the 2010 World Cup cost South Africa \$3.5 billion. It has been argued that South Africa should not have hosted it. Why do some people feel this?

B) Bethany College costs about \$33,000 per year. That money typically gets you 32 credit hours. So that is about \$1000 per credit hour. This course is three credit hours, so you are paying about \$3000 for this course. This course meets 41 times, so each class is worth just over \$73. Would you consider the opportunity costs of skipping a class to be \$73? Why or why not?

3) (14 points) Answer EITHER Part A OR Part B.

A) What is the law of comparative advantage? Why must it hold?

B) How do we see the opportunity costs of the good on the X-axis of a PPF (PPC)? Explain how you reached that conclusion.

4) (16 points) Answer EITHER Part A OR Part B.

A) Draw the supply and demand for cigarettes. Illustrate the effects of a bad tobacco crop. Explain why the curve(s) moved as drawn. What happens to the price and quantity of cigarettes sold?

B) Draw the supply and demand for wooden chairs. Illustrate the effect of an increase in the price of doors. Explain why the curve(s) moved as drawn. What happens to the price and quantity sold?

5) (16 points) Answer EITHER Part A OR Part B.

A) Draw the supply and demand for a polluting product like gasoline. Prove the socially optimal level of production will not be achieved without government intervention. Do **not** worry about what the government action should be or about illustrating the government action.

B) Use a supply and demand diagram to prove that a price ceiling hurts consumers. Explain the logic.

6) (16 points) Answer EITHER Part A OR Part B.

A) Illustrate the effects of an increase in the marginal propensity to consume on the Keynesian Cross, a.k.a. 45° diagram. Explain why the curve(s) moved as drawn. What happens to GDP?

B) Illustrate the effects of the US\$ getting stronger (appreciating) on the LRAS/SRAS/AD diagram. Explain why the lines moved as drawn.

7) (18 points) Answer EITHER Part A OR Part B.

A) What is the problem with Social Security? What solution is the best solution in your opinion?

Explain why that will reduce the problem. Explain why you think that is a particularly good method of reducing the problem.

B) Explain how *limiting protectionism* and *patents* help an economy to grow.

Remember to fill out course evaluations on-line.