

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 170 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) (12 points) Answer EITHER Part A OR Part B.

A) For *technical efficiency*, state the condition which determines if it is being done efficiently. Explain why that condition should hold.

B) Explain how market power prevents one of the three efficiencies from holding. Make sure you state that efficiency condition.

2) (12 points) Give EITHER an example of *adverse selection* OR *moral hazard* in the insurance markets. Explain how that is an example. Do not worry about reducing the problem.

3) (12 points) Answer EITHER Part A OR Part B.

A) Prove the *Law of Comparative Advantage* using general variables rather than specific numbers.

B) Suppose in China it takes 9 hours to make a chair and 3 hours to make a hat. In the USA, it takes 50 hours to make a chair and 10 hours to make a hat. What is one possible ratio of hats per chair which the two countries could trade at and make both better off? How did you find that ratio? **Do not** worry about proving that trade helps both countries.

4) (12 points) Answer EITHER Part A OR Part B.

A) Economists generally use the *utilitarian* measure of equity. What is that and what is a problem with using it?

B) Without using a graph, explain why yard sales rarely have high quality merchandise.

5) (14 points) Answer EITHER Part A OR Part B.

A) Recently the Department of Economics and Business hired somebody. If you had been one of the over 340 candidates, what could you have done to signal you were serious about wanting to work at Bethany College and/or you are a hard worker? Explain how that action would send that signal.

B) Some people have proposed that the CEO of a company should get shares of stock which cannot be sold for at least 10 years. What is the problem they are trying to reduce? How would it reduce the problem?

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

A) Draw the MCA diagram for two firms with different costs of abatement. Use it to prove that fees are better than regulations.

B) Draw the S/D diagram for a product like gasoline which causes a negative externality. Prove that we do not get the efficient level of production. Explain how you found the dead-weight loss

7) (22 points) Answer EITHER Part OR Part B.

A) Draw a Edgeworth box for Sleepy and Dopey consuming apples and pears. Choose three points on the contract curve. Use them to find three points on the utility possibilities frontier. Briefly explain how you did it.

B) Draw a PPF and indifference curve diagram for computers and doors. Draw the diagram such that we export the good on the horizontal axis. Prove that we are better off trading than at autarky and that we export the good on the horizontal axis.