

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 12-point question should take 6 minutes. I cannot give extra time because some students have a class after your class.

1) (10 points) Answer EITHER Part A OR Part B.

A) A few years back, Ozfest was “free.” Use economic terms and logic to prove the festival was not free even though tickets cost nothing.

B) This semester, an athlete with a B- average in your class, withdrew from the class stating that they were on a team and could not put in the necessary work for this course. Use economic terms and logic to explain that student’s decision to withdraw from the course.

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

A) In 1997, Zimbabwe passed a law which allowed the government to take property from individuals and corporations without compensating the owner. Given our keys to development, did this hurt or help their economic development? Explain your logic.

B) What is meant by *human capital*? How does that help production?

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

A) Draw a PPF for bananas and cars. Illustrate the effect of a new technology which enables car manufacturers to produce cars using less materials. Explain why the curve moved as drawn.

B) Draw the supply and demand for a good which has a positive externality, like a mural on a public building. Use the diagram to find the market level of production & price, and the socially optimal level of production & price. Explain how you found both and why they are not the same. Do **not** explain how we should reduce the problem.

4) (14 points) Answer EITHER Part A OR Part B.

A) What is meant by *moral hazard*? How does FDIC insurance cause it?

B) What is meant by *adverse selection*? Use it to explain why we use financial intermediaries.

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

A) Draw the MS/MD diagram. Illustrate the effects of an increase in the price level. Explain why the curve(s) moved as drawn. What happens to the interest rate and the amount of money?

B) Draw the MS/MD diagram. Use it to explain why the Federal Reserve cannot control both interest rates and the money supply at the same time.

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

A) Draw the supply and demand for school buses. Illustrate the effect of an increase in the price of trucks. Explain why the curve(s) moved as drawn. What happens to the price of buses and the quantity sold?

B) Draw the supply and demand for a college education. Illustrate the effects of an increase in the wages professors get. Explain why the curve(s) moved as drawn. What happens to the price of an education and the quantity sold?

7) (20 points) Answer EITHER Part A OR Part B.

A) What is the long-term problem with Social Security? What are the two main causes of the problem? One possible solution to the problem is to raise the Social Security tax on everybody. Explain how this will reduce the problem. Would you use the method (either with or without other solutions) to reduce the problem? Explain your logic.

B) Suppose the table to the right shows the income tax brackets. If a person earns \$50,000 a year of taxable income, then how much taxes does she pay? What are her marginal and average tax rates? Show all work and briefly explain what you did.

Income	tax rate
\$0 - \$10,000	20%
\$10,000 - \$30,000	30%
\$30,000 - \$90,000	40%
>\$90,000	50%