

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) Answer EITHER Part A OR Part B.

- A) In the song “It’s Still Rock and Roll To Me,” Billy Joel sang, “Should I try to be a straight A student? If you are, then you think too much.” Use terminology from economics to explain what he means.
- B) Use terminology from economics to explain why business professors are paid more than professors of art.

2) (12 points) Answer EITHER Part A OR Part B.

- A) If the consumption function is $C = 200 + .7(Y-T)$ and a person’s disposable income is \$20,000.00, then what are the values for the MPC, APC, MPS, and APS? Show all work. If there is no work, then state how you found it.
- B) What is meant by *adverse selection*? Use it to explain why we use financial intermediaries like banks rather than dealing directly with others?

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

- A) Draw a PPF for apples and oranges. Illustrate the effects of an improved fertilizer. Explain why the curve moved as drawn.
- B) State and prove the *law of comparative advantage*.

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

- A) What are *public goods*? Why are they an economic reason for government?
- B) What is *creative destruction*? How does that help a country to develop?

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

- A) Draw the supply and demand for **dresses**. Illustrate the effects of an increase in the price of curtains. Explain why the curve(s) moved as drawn. What happens to the price of **dresses** and the quantity of **dresses** sold?
- B) Draw the supply and demand for cars. Illustrate the effects of an increase in the prices of both aluminum and steel. Explain why the curve(s) moved as drawn. What happens to the price and quantity sold?

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

- A) Suppose you were given the data below. You have already calculated NNP and found it to be \$5350. Now you are to calculate NI. Write the equation you will use and show the calculation. Most of this data is unnecessary. If some data you need is missing, then assume it is zero. Consumers buy \$3000 worth of goods. Firms build \$500 worth of factories. The government pays \$2000 worth of salaries. We export \$50 worth of goods and import \$60 worth of goods. The machines lost \$40 worth of value from wearing down. The government gave firms \$100 in subsidies and the firms paid \$200 worth of sales tax. The corporations paid \$800 in corporate taxes and retained \$20 worth of profits. The government paid \$600 in Social Security. Individuals paid \$2300 in income tax.

B) Suppose the CPI at the beginning of the year was 800 and at the end of the year it was 816. What was the inflation rate? Show all work. If people had expected 5% inflation, then who is hurt? Name one group of people who are hurt and explain why they are hurt.

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

A) What is the long-term problem Social Security is facing? What are the two long-term trends which are contributing to it? One proposed solution to the problem is to do means testing on benefits; therefore, if you are rich when you retire, you do not get all that is promised to you and you may get nothing. How would that reduce the problem? Would you do that as part of a big plan to fix Social Security? Explain your logic

B) Both the supply and demand curves show the effects of opportunity costs. Explain how opportunity costs can be seen in both graphs.