

Economics 160, Midterm 1, answer keys.

If your first question's possible answers were in this order:

1. The phenomenon of scarcity stems from the fact that
 - a. most economies' production methods are not very good.
 - b. in most economies, wealthy people consume disproportionate quantities of goods and services.
 - c. governments restrict production of too many goods and services.
 - d. resources are limited.
 - e. None of the above

answers are:

- 1.d
- 2.d
- 3.b
- 4.a
- 5.b
- 6.d
- 7.e
- 8.c
- 9.a
- 10.a
- 11.d
- 12.c
- 13.b
- 14.c
- 15.d
- 16.c
- 17.a
- 18.a
- 19.d
- 20.e
- 21.a
- 22.e
- 23.c
- 24.a
- 25.d

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 - c. resources are limited.
 - d. most economies' production methods are not very good.
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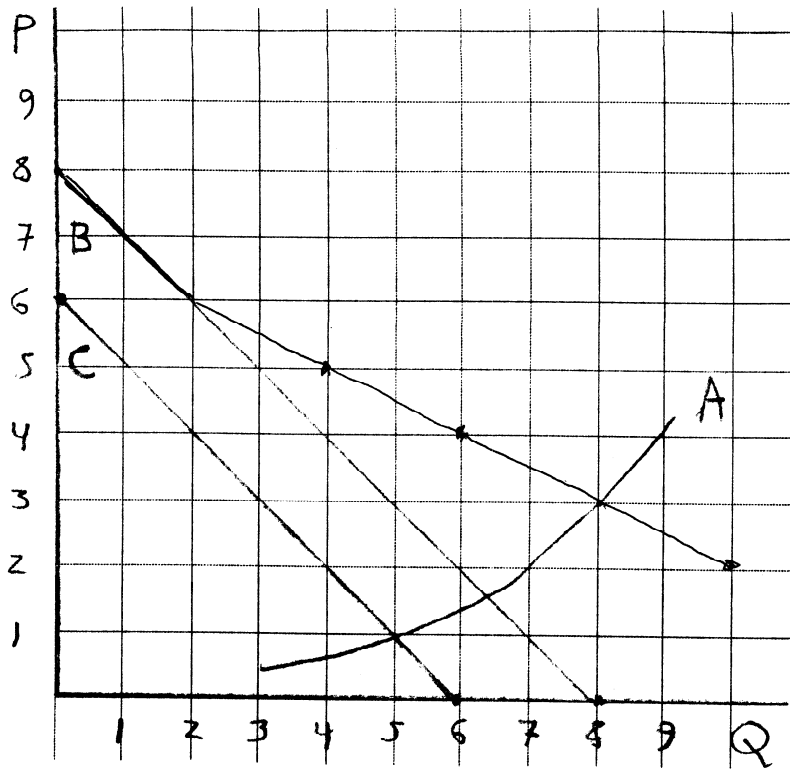
- 1.c
- 2.c

3.c
4.b
5.a
6.e
7.e
8.d
9.a
10.d
11.a
12.d
13.a
14.d
15.c
16.b
17.b
18.c
19.b
20.a
21.e
22.e
23.c
24.a
25.c

Written questions.

1) 20 pts. The graph below describes supply and demand in a perfectly competitive market for bananas. A is the supply of bananas. B is demand for bananas of left-handed people. C is demand for bananas of right-handed people.

a) Add a line that represents *total* demand for bananas.



b) The equilibrium price of bananas is 3

The equilibrium quantity of bananas is 8

2) 20 pts. Consider two countries, Narnia and Archenland. Each country can produce two goods, gin and tonic, with productivities as given below. Narnia has 100 workers. Archenland has 200 workers.

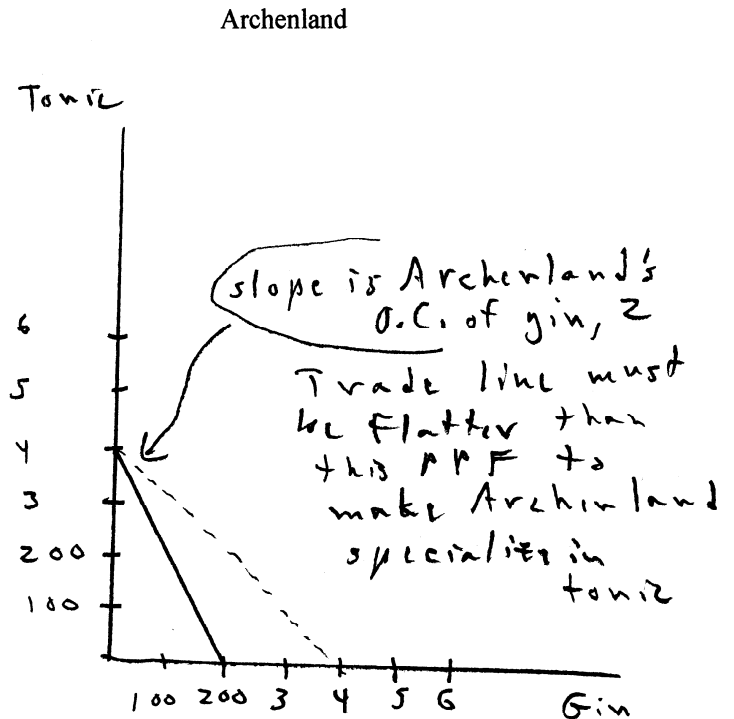
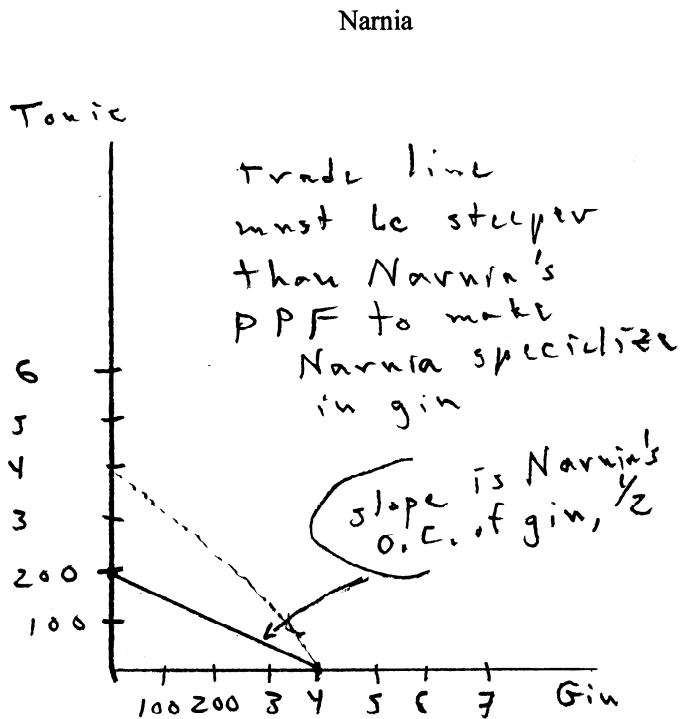
	Output from one worker		Opportunity costs	
	Gin	Tonic	Gin	Tonic
Narnia	4	2	1/2	2
Archenland	1	2	2	1/2

a) Think about gains from trade. In order to make both countries, better off, a trade deal must cause

Narnia to specialize in production of gin

Archenland to specialize in production of tonic

b) On the two graphs below, draw the PPFs for Narnia and Archenland, with *solid* (not dotted or dashed) lines.



c) Think up a particular trade deal that will make both Narnia and Archenland better off than under autarchy. On the graphs above, depict this trade deal with a dotted line on each graph. These dotted lines show the possible combinations of gin and tonic that each country can get if it specializes and trades.

d) What is this trade deal you have depicted with the dotted lines?

In order to get one unit of gin, the tonic-producer must hand over one unit(s) of tonic.

In order to get one unit of tonic, the gin-producer must hand over one unit(s) of gin.

Slope of trade line is number of tonics you get in return for giving up one gin.

Or, number of tonics you must give up in order to get one gin.

Any trade line with slope bigger than $\frac{1}{2}$ (absolute value), smaller than 2 will work.