

University of Fort Hare

Department of Economics

Introduction to Micro Economics – ECO111F/L

Test 3/EMA

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Hours: 2 Hours

Marks: 50

This paper consists of 9 pages including the cover page

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Instructions

Answer ALL questions in Section A & B.

Answer ONE question in section C

Section A: Multiple Choice Questions (Answer ALL)

- 1) Consider the demand and supply of labour in the sugar industry. If there is a minimum wage in this industry (above equilibrium wage/price), then the effect of removing this minimum wage would be to
- A. increase the equilibrium price (wage) and increase the quantity of labour demanded.
 - B. decrease the equilibrium price (wage) and remove the shortage of labour.
 - C. decrease the equilibrium price (wage) and remove the surplus of labour.
 - D. increase the equilibrium price (wage) and cause a shortage of labour.
 - E. none of the above.

- 2) Which one of the following statements is incorrect?

An increase in the supply of plastic bags:

- A. may be illustrated by a rightward shift of the supply curve.
- B. may be caused by an increase in labour productivity.
- C. could be the result of lower wages in the plastic industry.
- D. could be the result of a decrease in the cost of producing plastic bags.
- E. may be illustrated by an upward movement along the supply curve.

- 3) Which one of the following statements is incorrect?

- A. An increase in supply tends to result in a lower price.
- B. An increase in demand tends to result in a higher price.
- C. A simultaneous increase in demand and supply has an uncertain impact on price.
- D. A simultaneous increase in demand and supply tends to result in a higher equilibrium quantity in the market.
- E. The impact of a simultaneous decrease in demand and supply on the equilibrium quantity is impossible to predict.

- 4) If government sets a maximum price above the equilibrium price:

- A. a surplus will develop.

- B. a shortage will develop.
- C. excess supply will develop.
- D. excess demand will develop.
- E. the market will be unaffected.

5) If government sets a maximum price below the equilibrium price:

- A. the market will be unaffected.
- B. the quantity supplied will be greater than the quantity demanded.
- C. a market shortage will develop.
- D. the market will still be able to fulfil its rationing function.
- E. there will be an excess supply.

6) Which one of the following statements is incorrect?

If government sets a price ceiling below the equilibrium price:

- A. the market cannot fulfil its rationing function.
- B. a black market may develop.
- C. consumers who are able to obtain the product may resell it to other consumers at higher prices.
- D. the government would have to devise plans about how to get rid of the surplus.
- E. the market forces of supply and demand are prevented from eliminating excess demand.

7) Which one of the following statements is incorrect?

A minimum price:

- A. is effective only if it is set above the equilibrium price.
- B. below the equilibrium price has no impact on the market.
- C. above the equilibrium price results in a market surplus (excess supply).
- D. below the equilibrium price results in an excess demand (market shortage).
- E. above the equilibrium price requires further measures to deal with the market surplus.

8) Which one of the following statements is incorrect?

- A. Fixing a maximum price for diesel above the equilibrium price will result in an excess supply of diesel.
- B. Fixing a maximum price for rugby tickets below the equilibrium price will result in an excess demand for rugby tickets.
- C. Fixing a maximum price for soccer tickets below the equilibrium price may lead to black market activity.
- D. Black market activity will occur only if there is a market shortage of the good or service.
- E. Fixing a maximum price below the equilibrium price results in a welfare loss to society (ie a deadweight loss).

11. Price elasticity of demand refers to:

- A. How easy it is to adjust a good's market price
- B. The product of a good's price and the quantity of the good sold
- C. How the price of a good will change as the quantity demanded of the good changes
- D. How much the quantity demanded of a good will change with a change in the good's price

Study the information about the sales of cow's milk at a local supermarket in the table below and answer questions 12–16.

7	231
8	217
9	199
10	178
11	154

12. If the supermarket decides to increase the price of milk from R8 per liter to R9 per litre, which of the following statements will be true?
- A. The supermarket is operating on the elastic part of the demand curve and the total revenue will increase.
 - B. The supermarket is operating on the inelastic part of the demand curve and the total revenue will increase.
 - C. The supermarket is operating on the inelastic part of the demand curve and the total revenue will decrease.
 - D. The supermarket is operating on the elastic part of the demand curve and the total revenue will decrease.
13. On which portion of the demand curve of milk will the curve be most elastic?
- A. When between 199 and 231 litres are sold per day
 - B. When exactly 199 liters of milk are sold per day
 - C. When the price of milk is R7
 - D. When the price of milk is between R10 and R12
14. What is the arc elasticity of milk?
- A. 1.010
 - B. 0.664
 - C. -0.529
 - D. 0.859
15. One can say that overall the demand for milk is:
- A. Price elastic, because it is a necessity
 - B. Price elastic, because there exists a close substitute product for milk

- C. Unit elastic, because the percentage change in price will be more or less equal to the percentage change in the quantity of milk demanded
 - D. Price elastic, because a change in income will have a significant impact on the quantity of milk demanded
16. The supermarket also sells goat's milk. As the price of cow's milk increases, the demand for goat's milk seems to remain unchanged. What does this say about the two types of milk?
- A. The cross-price elasticity of demand is large and positive and the two types of milk are substitutes of each other.
 - B. The cross-price elasticity of demand is large and negative and the two types of milk are not substitutes for each other.
 - C. The cross-price elasticity of demand is low and positive and the two types of milk are substitutes for each other.
 - D. The cross-price elasticity is low and the two types of milk do not compete on the same market.
17. As more and more units of a good are consumed by a household, the total utility gained from that good will:
- A. diminish.
 - B. increase, but by successively smaller amounts.
 - C. rise steeply.
 - D. remain unchanged.
18. Utility from consuming a good is understood by economists to mean:
- A. how often we consume the good.
 - B. how much satisfaction or benefit we get from consuming the good.
 - C. how much it costs to buy the good.
 - D. how we best use the good.
 - E. none of the above.

The table below shows a hypothetical total utility schedule for a consumer of traditional beer. Use the table to answer Questions 19 to 20.

Traditional beer consumed	Total utility
0	0
1	90
2	190
3	270
4	350
5	420
6	420
7	400

19. The consumer begins to experience diminishing marginal utility when she consumes the:

- A. first traditional beer.
- B. second traditional beer.
- C. third traditional beer.
- D. fourth traditional beer.
- E. seventh traditional beer.

20. Marginal utility becomes negative with the consumption of the:

- A. fourth traditional beer.
- B. fifth traditional beer.
- C. sixth traditional beer.
- D. seventh traditional beer.
- E. third traditional beer.

SECTION B (Answer ALL)

- 1) Suppose that you are the manager of a soccer stadium where all the tickets always have to be sold at the same price. Two matches are scheduled to be played during the next fortnight, the first between Sundowns and Pirates and the second between two First Division sides.
- (a) Market research indicates that you can sell 40 000 tickets for the Sundowns-Pirates clash at R10 each, or 30 000 tickets at R20 each. Which option would you choose? What is the price elasticity of the demand for tickets for this particular game? (4)
- (b) Likewise, market research indicates that you can sell 15 000 tickets for the First Division fixture at R10 each, or 5 000 tickets at R20 each. Which option would you choose? What is the price elasticity of the demand for tickets for this game? (4)
- 2) Use diagrams to illustrate what will happen to the equilibrium price and quantity of a product if an increase in demand is associated with a decrease in supply. Clearly indicate instances where the impact cannot be predicted. (7)

SECTION C (Choose One)

Question 2

- a) Explain, with the aid of a diagram, what happens in the market for (say) electricity if the government fixes a maximum price below the equilibrium price. (4)
- b) Describe in words what each of the following means:
- I. perfectly inelastic demand.
 - II. unitary elastic demand.
 - III. elastic demand. (6)
- c) What is meant by the term 'utility' and how do marginal and total utility differ? (5)

OR

Question 3

- a) Suppose you are the supplier of Thingamabobs and that you are in a position to decide at which price you will offer these products for sale. What would your pricing strategy tend to be if you have determined that the price elasticity of the demand for Thingamabobs is:
- I. greater than one.

II. equal to one.

III. smaller than one.

Explain your decision in each case.

(6)

b. John Scott has R200 per week available to spend on beer and cigarettes. Beer costs R10 per bottle and cigarettes cost R40 per packet. Suppose John buys 8 bottles of beer and 3 packets of cigarettes and that his marginal utility from beer is then 20 utils and that from cigarettes 35 utils. Is he in equilibrium? If not, should he buy more beer or more cigarettes? Explain.

(6)

c. In your own words briefly explain what is meant by the law of equalising the weighted marginal utilities.

(3)

.....**END**.....