Arizona State University (ASU) ECN212 Microeconomic Principles Exam 1 Practice (Sample)

Study Guide

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Questions

1. What is the expectation when demand increases for a good?
   A. The quantity supplied will also decrease
   B. The market will reach a new equilibrium
   C. The price will drop significantly
   D. Consumer surplus will rise indefinitely

2. When the economy experiences an overall decrease in income and coffee is considered an inferior good, what happens to the price and quantity of coffee?
   A. Price of coffee decreases and quantity decreases
   B. Price of coffee increases and quantity increases
   C. Price of coffee is ambiguous and quantity increases
   D. Price of coffee increases and quantity decreases

3. What happens to consumer surplus under efficient rationing?
   A. It remains unchanged
   B. It increases significantly
   C. It decreases
   D. It becomes negligible

4. What is the result of having a price ceiling set below the market equilibrium price?
   A. It creates an optimal market balance
   B. It leads to excess supply
   C. It causes a shortage in the market
   D. It has no impact on the market

5. What does the principle of diminishing marginal utility state?
   A. Utility increases indefinitely with consumption
   B. Each additional unit consumed provides less satisfaction
   C. Demand decreases as quantity increases
   D. Utility is constant regardless of consumption

6. What does 'no shift' in a demand curve mean?

A. No external factor is affecting the market

B. A significant increase in supply

C. The price of the good has increased

D. Market forces are at equilibrium

7. What effect does a decrease in consumer income have on inferior goods?

A. It leads to a decrease in demand for inferior goods

B. It has no effect on demand for inferior goods

C. It leads to an increase in demand for inferior goods

D. It leads to an increase in prices of inferior goods

8. Which of the following is true regarding variable costs during production increases?

A. Variable costs remain constant

B. Variable costs increase

C. Variable costs decrease

D. Variable costs are unaffected by production levels

9. Shortages in a market occur when?

A. Quantity supplied is greater than quantity demanded

B. Quantity demanded is less than quantity supplied

C. Quantity demanded is greater than quantity supplied

D. Prices are above equilibrium

10. What does a leftward shift in a demand curve indicate?

A. An increase in quantity demanded

B. A decrease in demand

C. An improvement in buyer sentiment

D. An increase in supply

Answers

1. B
2. C
3. B
4. C
5. B
6. A
7. C
8. B
9. C
10. B

Explanations

1. What is the expectation when demand increases for a good?

A. The quantity supplied will also decrease

B. The market will reach a new equilibrium

C. The price will drop significantly

D. Consumer surplus will rise indefinitely

When demand for a good increases, the expectation is that the market will reach a new equilibrium. This occurs because an increase in demand typically leads to a higher equilibrium price and quantity. As demand rises, consumers are willing to purchase more of the good at every price level, which puts upward pressure on prices. Suppliers, noticing that consumers are willing to pay more, are incentivized to produce and sell more of that good. As the price rises, the market adjusts until it finds a new equilibrium where the quantity demanded equals the quantity supplied at that new higher price. This adjustment reflects the fundamental principle of supply and demand, which indicates that shifts in demand lead to changes in both price and quantity in the market. Consequently, the new equilibrium represents a temporary balance between buyers and sellers under the new demand conditions. The other choices do not capture the full dynamics of how markets respond to an increase in demand; they do not incorporate how supply adjusts or the resulting changes in equilibrium.

2. When the economy experiences an overall decrease in income and coffee is considered an inferior good, what happens to the price and quantity of coffee?

A. Price of coffee decreases and quantity decreases

B. Price of coffee increases and quantity increases

C. Price of coffee is ambiguous and quantity increases

D. Price of coffee increases and quantity decreases

When analyzing the impact of a decrease in income on the market for an inferior good, the relationship between consumer income and demand must be considered. Inferior goods are characterized by a negative correlation with income: as income decreases, the demand for inferior goods tends to increase, because consumers turn to these less expensive alternatives. In this scenario, when the economy experiences an overall decrease in income, consumers will likely buy more coffee (the inferior good) since they are substituting away from more expensive items. Consequently, this increase in demand for coffee will lead to upward pressure on its price. However, the overall effect on price can depend on the degree to which the supply of coffee can respond to this change in demand. If the supply remains relatively constant in the short term, the increase in demand would generally lead to an increase in the quantity sold and to an increase in price. The quantity of coffee will unambiguously increase due to increased demand as a result of lower incomes. However, the price may either increase or remain stable depending on supply constraints, making it ambiguous. Thus, the conclusion is that the quantity of coffee will definitely increase, while the price could either rise or hold steady, which aligns with the selected answer.

3. What happens to consumer surplus under efficient rationing?

A. It remains unchanged

B. It increases significantly

C. It decreases

D. It becomes negligible

Under efficient rationing, the allocation of resources is optimized to reflect consumers' willingness to pay, ensuring that those who value the resource the most receive it. This process leads to an increase in consumer surplus because efficient rationing promotes higher surplus values for consumers who obtain the goods or services they desire at a price lower than their maximum willingness to pay. In essence, consumer surplus is calculated as the difference between what consumers are willing to pay and what they actually pay. When resources are allocated efficiently, it minimizes deadweight loss, thus enhancing the overall economic welfare and leading to a rise in the total consumer surplus. This impact is particularly notable in markets where prices reflect true supply and demand dynamics, facilitating a situation where consumer benefits are maximized. While other options suggest stability or a reduction in consumer surplus, efficient rationing inherently aims to enhance consumer welfare by ensuring that the distribution of goods aligns closely with consumer preferences and valuations, which is fundamentally why the correct response indicates that consumer surplus increases significantly.

4. What is the result of having a price ceiling set below the market equilibrium price?

A. It creates an optimal market balance

B. It leads to excess supply

C. It causes a shortage in the market

D. It has no impact on the market

The correct response indicates that setting a price ceiling below the market equilibrium price leads to a shortage in the market. A price ceiling is essentially a legal maximum price that can be charged for a good or service. When this ceiling is established below the equilibrium price, the price that sellers can charge is limited, which prevents them from adjusting to the higher demand that exists at the equilibrium level. As a result, at this lower price, more consumers are willing to buy the good because it is more affordable. However, suppliers may be less willing to produce and offer the good at this reduced price, as it may not cover their costs, leading to a decrease in supply. The combination of increased demand and reduced supply creates a situation where the quantity demanded exceeds the quantity supplied, resulting in a shortage of the good. This outcome illustrates the impact of government intervention in markets, where price controls can disrupt the natural balance achieved by supply and demand dynamics. It highlights the repercussions of relying on mechanisms like price ceilings to manage prices without considering their broader market implications.

5. What does the principle of diminishing marginal utility state?

A. Utility increases indefinitely with consumption

B. Each additional unit consumed provides less satisfaction

C. Demand decreases as quantity increases

D. Utility is constant regardless of consumption

The principle of diminishing marginal utility states that as an individual consumes more units of a good or service, the additional satisfaction or utility gained from each additional unit tends to decrease. This means that while the first unit consumed might provide a significant amount of satisfaction, each subsequent unit will likely provide less and less satisfaction. For example, if someone is eating slices of pizza, the first slice may be very enjoyable, but by the fourth or fifth slice, the additional satisfaction from consuming more likely diminishes. This concept is fundamental in microeconomics as it helps explain consumer behavior and demand. It suggests that individuals will only be willing to pay for additional units up to the point where the satisfaction gained equals the price they have to pay for those units. Thus, the principle of diminishing marginal utility is crucial for shaping demand curves and understanding consumer choices in a systematic way.

6. What does 'no shift' in a demand curve mean?

A. No external factor is affecting the market

B. A significant increase in supply

C. The price of the good has increased

D. Market forces are at equilibrium

A 'no shift' in a demand curve indicates that the demand for a good remains the same in response to a change in price, meaning that no external factors are influencing the market dynamics of that good. This scenario typically implies that while the quantity demanded may increase or decrease as the price changes, the overall demand curve—representing the relationship between price and quantity demanded at every price level—stays in its original position. Thus, if there are no external shocks or changes in consumer preferences or income, the demand curve will not shift to the left or right. In contrast, the other options suggest situations that would typically cause changes in demand or market behavior. An increase in supply would shift the supply curve, affecting market equilibrium, while changing prices generally cause movements along the existing demand curve rather than a shift of the curve itself. Lastly, market forces at equilibrium represent a state where supply and demand are balanced, but this doesn't directly relate to the absence of a shift in the demand curve.

7. What effect does a decrease in consumer income have on inferior goods?

A. It leads to a decrease in demand for inferior goods

B. It has no effect on demand for inferior goods

C. It leads to an increase in demand for inferior goods

D. It leads to an increase in prices of inferior goods

A decrease in consumer income leads to an increase in demand for inferior goods because these goods are typically considered lower-quality alternatives to more expensive items. When consumers experience a drop in income, they tend to buy more inferior goods as a way to maintain their consumption levels while economizing. This behavior reflects the very nature of inferior goods, which are defined as goods for which demand rises when consumer incomes fall. As consumers substitute away from more expensive goods they can no longer afford, the demand for inferior goods increases. This is contrary to normal goods, where demand decreases as income decreases. The relationship between income and demand for inferior goods is a fundamental concept in microeconomics, illustrating how changes in consumer income can impact purchasing behavior.

8. Which of the following is true regarding variable costs during production increases?

A. Variable costs remain constant

B. Variable costs increase

C. Variable costs decrease

D. Variable costs are unaffected by production levels

Variable costs are directly associated with the level of production in a business. As production increases, the requirement for inputs such as labor, raw materials, and other resources rises correspondingly, leading to an increase in variable costs. This characteristic of variable costs is crucial for understanding how businesses scale their operations. Unlike fixed costs, which remain unchanged regardless of production levels, variable costs fluctuate as the output increases or decreases. Therefore, the correct answer reflects the fundamental principle that higher production levels necessitate greater expenditure on variable inputs.

9. Shortages in a market occur when?

A. Quantity supplied is greater than quantity demanded

B. Quantity demanded is less than quantity supplied

C. Quantity demanded is greater than quantity supplied

D. Prices are above equilibrium

Shortages in a market occur when the quantity demanded exceeds the quantity supplied. This situation arises when consumers want to purchase more of a good or service than what is available in the market at a given price. When this imbalance occurs, it often leads to upward pressure on prices as consumers compete to secure the limited goods available. Sellers may notice that they can charge a higher price because there are more buyers than goods, incentivizing them to increase production or raise prices. This dynamic helps to signal to the market that more supply is needed to meet consumer demand, eventually moving the market back towards equilibrium where quantity demanded equals quantity supplied. In essence, a shortage reflects a condition where the existing price does not allow for balance between what consumers want to buy and what producers are willing to sell.

10. What does a leftward shift in a demand curve indicate?

A. An increase in quantity demanded

B. A decrease in demand

C. An improvement in buyer sentiment

D. An increase in supply

A leftward shift in a demand curve signifies a decrease in demand for a particular good or service at all price levels. This means that, at any given price, consumers are now willing to buy less of that good than they were before the shift occurred. Factors that can lead to a decrease in demand include a decrease in consumer income, a loss of consumer confidence, an increase in the prices of complementary goods, or a change in consumer preferences away from the good in question. In contrast, an increase in quantity demanded refers to movement along the demand curve to a higher quantity at a lower price, rather than a shift of the curve itself. Improvement in buyer sentiment and an increase in supply would lead to different effects on the demand and supply curves, respectively, without causing the demand curve to shift leftward. Understanding these foundational concepts helps clarify market dynamics and the interplay between consumer behavior and pricing.