Homework 9 Pricing Microeconomics

1. When transaction costs are positive, buying at a low price in one market and reselling at a higher price in another market
a) will not generate any profit because of transactions costs.
b) will eventually eliminate all of the price differences.
c) will eventually eliminate most, but not necessarily all, of the price differences.

2. The best example of demand-based price discrimination among the following is:
   a. A bald person's haircut costs less than yours.
   b. Dry cleaner charges lower price for cleaning men's cotton shirts than women's silk blouses.
   c. A similar pair of flip-flops costs less at Walmart than at Macy's.
   d. *New York Times* paper costs $1 and *Daily News* costs $2.
   e. "Early-bird specials" at restaurants.

3. Bubba's Hula Shack bar and bistro has begun giving customers who can show proof that they arrived at the establishment by public transportation a 10% discount on their total bill. All else equal, customers who arrive by public transportation to take advantage of Bubba's Hula Shack discount have a ________ for the services of the establishment than customers who drive to the establishment.

A) higher price elasticity of demand
B) lower price elasticity of demand
C) higher price elasticity of supply
D) lower price elasticity of supply

4. Are grocery store coupons a form of price discrimination? Why or why not?

5. Which is NOT required for a firm to price discriminate successfully?
   a. It must have some market power.
   b. It must be able to differentiate the buyers into different groups.
   c. Its product must be expensive.
   d. Consumers unable to resell the product.

6. The Paramount movie theatre has a seating capacity of 270. On any given night, there are 180 people who would potentially attend a movie at the Paramount. There are 80 people who are willing to pay up to $15 to attend a movie at the Paramount, and there are an additional 100 people who are willing to pay up to $5 to attend a movie at the Paramount. The total cost (including movie rental, labor, and rent on the theatre) to the theatre owners of showing a movie at the Paramount is fixed at $800 per night no matter how many people watch the movie. If they must charge the same price to all buyers, what price should the owners of the Paramount charge for movie tickets in order to maximize their profits? *(show work)*

a) $15 b) $5 c) $4.44 d) $10 e) $8.89

7. In the problem above, suppose all those people who are willing to pay no more than $5 are students. The theatre decides to offer a $10 discount to anyone with a student ID. What will the total profit of the theatre be? *(show work)*

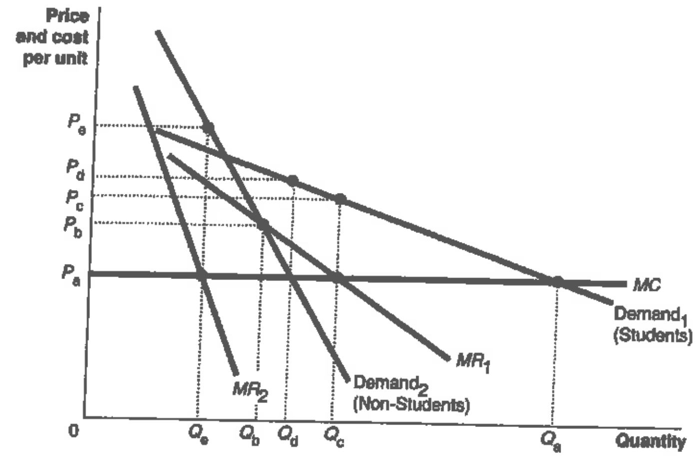
a) $100 b) $400 c) $900 d) $1200 e) $1700

8. If a firm could practice perfect price discrimination, it would

A) allow resale of its product.
B) charge every buyer a different price.
C) charge a price based on the quantity of a product bought.
D) use odd pricing.

9. Give your own example of price discrimination.

10. What is the price charged in the two markets? How do you explain the difference?



11. If the selling price of a firm's product is $500 and the estimated average cost of producing this product is $400, what is the firm's markup?

12. Which of the following firms is most likely to use cost-plus pricing?
- A) A firm that makes one product.
- B) A firm that sells one product and has a sizable research and development budget.
- C) A firm that makes several products and has a sizable research and development budget, the cost of which cannot be easily assigned to each product.
- D) A firm that makes many products but has a small research and development budget, the cost of which can be easily assigned to the different product lines.

13. Some firms require consumers to pay an initial fee for the right to buy their product and an additional fee for each unit of the product they purchase. This practice is referred to as
- A) odd pricing.
- B) dual pricing.
- C) a two-part tariff.
- D) perfect price discrimination.

14. Argue with the following statement. Monopolies overcharge and underproduce. This imposes costs on the society. Therefore all monopoly businesses should be banned by the government. Give 2 arguments in defense of monopolies.

15. Products produced for mass consumption are often criticized as being of poor quality. We know, however, that markets create many assurance mechanisms to help consumers monitor product quality. "Piece of Crap" by Neil Young discusses several of these mechanisms. In reference to the song, what market mechanisms help to alleviate problems arising from the lack of information about the quality of goods? Does Neil Young think these mechanisms work well?

Tried to save the trees *Bought a platsic bag* *The bottom fell out* *It was a piece of crap* *Saw it on the tube* *Bought it on the phone* *Now you're home alone* *It's a piece of crap*	*I tried to plug in it* *I tried to turn it on* *When I got it home* *It was a piece of crap* *Got it from a friend* *On him you can depend* *I found out in the end* *It was a piece of crap*	*I'm trying to save the trees* *I saw it on TV* *They cut the forest down* *To build a piece of crap* *I went back to the store* *They gave me four more* *The guy told me at the door*

Microeconomics [redacted] 10 Oligopoly

1. The characteristic most closely associated with oligopoly is:
   a. easy entry into the industry.
   b. a few large producers.
   c. product standardization.
   d. no control over price.
   e. zero profits

2. Which of the following is the poorest example of an oligopoly market?
   a. breakfast cereals in the US
   b. domestic cars in the US
   c. OPEC
   d. bars/night clubs in NYC
   e. universities in Manhattan

3. OPEC as a cartel will, in comparison to a competitive industry:
   a. Produce less output and charge a higher price
   b. Produce greater output and charge a higher price
   c. Produce greater output and charge a lower price
   d. Produce less output and charge a lower price

4. When the player of a game chooses a dominant strategy,
   a. it is the best strategy only if other players are cooperative
   b. it is always leads to a Nash equilibrium that makes all players equally well off
   c. the game can never reach a Nash equilibrium
   d. it is the best strategy, regardless of choices made by other players

5. Each cell in the strategic chart above shows (payoff to Firm A, payoff to Firm B) given two different price strategies. Mark each firm's dominant strategy and answer the following question. Find Nash equilibrium of this game.

		Firm B	
		price high	price low
Firm A	price high	(15,15)^{A}	(2,25)^{B}
	price low	(25,2)^{C}	(5,5)^{D}

6. The incentive to cheat is strong in a cartel because:
   a. the marginal revenue is greater than marginal cost at the profit-maximizing price set by the cartel.
   b. there is a significant lack of government regulation of cartels, especially those in worldwide production.
   c. the costs of production are the same for each firm, but the product demand differs.
   d. each firm can increase its output and thus its profits by cutting price.

7. Collusion
A) is rampant in perfect competition as all firms charge the same price.
B) reduces market concentration in an industry.
C) among firms is difficult to maintain because it eliminates long run economic profit.
D) is more difficult when there are many firms producing differentiated products in an industry.

8. Boeing an Airbus are considering whether to build a new factory. What is the Nash equilibrium of this game?

		Air Bus	
		Build	Don't Build
Boeing	Build	(-10, -10)^{A}	(-5, -15)^{B}
	Don't build	(-5, 5)^{C}	(10, 0)^{D}

9. Give examples of industries that are highly concentrated.

Next 3 questions are based on the following table. The table shows the payoff [redacted]x for Walmart and Target from every combination of pricing strategies for the popular PlayStation 3. At the start of the game each firm charges a low price and each earns a profit of $7,000.

		Walmart	
		High price	Low price
Target	High price	(10, 10)	(5, 14)
	Low price	(14, 5)	(7, 7)

10. Is the current strategy in which each firm charges the low price and earns a profit of $7,000 a Nash equilibrium? If not, why and what is the Nash equilibrium?

11. For each firm, is there a better outcome than the current situation in which each firm charges the low price and earns a profit of $7,000?

12. Suppose Walmart and Target both advertise that they will match the lowest price offered by any competitor. What is the purpose of such a strategy?

13. Suppose pricing PlayStations is a repeated game in which Wal-Mart and Target will be selling the game system in competition over a long period of time. In this case, what is the most likely outcome?

1. If violent crime rates rise in hot weather, the growth of air conditioning generates
   a. A negative externality
   b. A positive externality
   c. Negative private net benefits
   d. No link to the crime rate
   e. Public goods

2. Dioxin emission that results from the production of paper is a good example of a negative externality because
   A) self-interested paper firms are generally unaware of environmental regulations, and information is costly.
   B) self-interested paper producers will not consider the full cost of the dioxin pollution they create.
   C) there are fines and taxes for producing too much dioxin.
   D) toxic emissions are public goods.

3. If producing plastic toys generates acid rain that damages wildlife habitat in a region downwind from a factory, from a social perspective, the price of toys will be _____ but the quantity produced will be _____
a. too low; correct b. too low; too high c. correct; too low d. too high; too low e. too high; too high

4. Dick owns a dog whose barking annoys Dick's neighbor Jane. Suppose that the benefit of owning the dog is worth $500 to Dick and that Jane bears a cost of $700 from the barking. A possible private solution to this problem is that
   A) Jane pays Dick $450 to get rid of the dog.
   B) Jane pays Dick $650 to get rid of the dog.
   C) Dick pays Jane $650 for her inconvenience.
   D) Dick pays Jane $450 for her inconvenience.
   E) There is no private solution that would improve this situation.

5. If a community is assigned property rights over air quality and the environment, a steel mill in the community that generates air pollution:
   A) will sue damages and for the right to produce steel.
   B) will cease to pollute.
   C) can contract to pay the community to allow some level of air pollution.
   D) must shut down.
   E) will outsource production to a "pollution heaven" country, such as China.

6. Externalities weaken the efficiency of the market system because they:
   A) increase prices and restrict competition
   B) are a major source of inflation
   C) mean that certain essential goods and services do not get produced at all
   D) are a major source of unemployment
   E) cause certain goods to be overproduced or underproduced relative to socially optimal level

7. When dealing with externalities, the free-market equilibrium can be moved closer to the optimum by:
   a. taxing positive externalities and subsidizing negative externalities.
   b. taxing negative externalities and subsidizing positive externalities.
   c. taxing both positive and negative externalities.
   d. subsidizing both positive and negative externalities.
   e. None of the above is correct, because government has no corrective policy with regards to externalities.

8. Some policymakers have argue that products like cigarettes, alcohol, and sweetened soda generate negative externalities in consumption. All else equal, if the government decided to impose a tax on soda, the equilibrium quantity of soda would ________ and the equilibrium price of soda would ________.
   A) increase; increase B) increase; decrease C) decrease; increase D) decrease; decrease

9. An ice cream cone is
A) excludable and rival in consumption.
B) excludable and not rival in consumption.
C) not excludable and rival in consumption.
D) not excludable and not rival in consumption.
E) a good breakfast

10. Which of the following is the best example of a public good (nonexcludable and nonrival)?
   a. an iPod. b. a bottle of soda. c. clean air. c. an economics lecture. e. a highway.

11. Which one of the following is the LEAST likely to be considered a public [redacted]
   a. A golf course   b. A national park   c. An interstate highway   d. Wildlife   e. A river

12. The Great Lakes are
   a. natural monopolies.   b. private goods.   c. public goods.   d. common resources.

13. Private firms will not provide such goods as flood-control projects, research in basic sciences, space exploration and wildlife preservation because:
   A) such projects generate harmful spillover effects
   B) marginal benefits invariably fall short of marginal costs in such projects
   C) these are major sources of revenue for government
   D) there is no way of denying benefits to those who are unwilling to pay
   E) these projects do not benefit the society

14. The free-rider problem is that:
   A) free education is not free for the tax payers.
   B) free public transportation is overcrowded.
   C) government supplies goods at no charge to people who could otherwise afford them.
   D) people will not voluntarily pay for a good when they can obtain the benefits of the good without paying
   E) public goods often create external costs.

15. Why has the value of ivory threatened the extinction of the elephant, whereas the value of beef has enhanced the survival of the cow?
   A) Elephants are larger than cows, requiring more economic resources.
   B) Cows are a common resource, whereas elephants are owned by governments.
   C) Elephants live in Africa, where economic resources are scarce.
   D) Elephants are a common resource, whereas cows are privately owned.

16. The Ogallala aquifer is a large underground pool of fresh water under several western states in the United States. Any farmer with land above the aquifer can at present pump water out of it. Which of the following statements about the aquifer is correct?
   A) The aquifer is a artificially scarce good which should be left as it is.
   B) The aquifer is a private good which must be privately owned to be used efficiently.
   C) The aquifer is a public good which must be publicly owned to be used efficiently.
   D) The aquifer is a common property resource which will be overused if no one owns it.

17. Which of the following quotations illustrates the Tragedy of the Commons?
   A) A bird in the hand is worth two in the bush.
   B) You can't always get what you want.
   C) Anyone who is not a socialist before he is 30 has no heart; anyone who is still a socialist after he is 30 has no head.
   D) What is common to many is taken least care of, for all men have greater regard for what is their own than for what they possess in common with others.
   E) The only difference between the rich and other people is that the rich have more money.

18. Give one example of a positive externality. Suggest a policy that could encourage this activity.

19. Give one example of a negative externality. Suggest a policy that could discourage this activity.