Micro, Spring 2016 with P. Stankov, TA Session on Perfect Competition
Source: Case/Fair (Principles of Economics) + Farnham (Economics for managers)

MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.

Refer to the information provided in the Figure 12.4 below to answer the questions that follow.

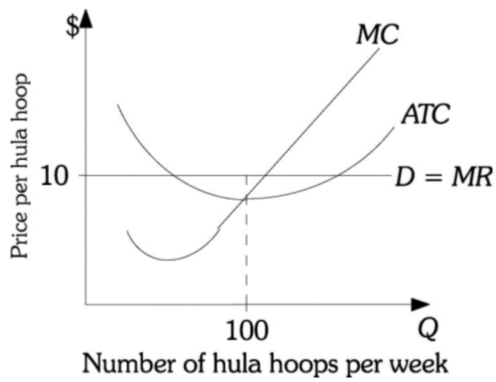

Figure 12.4

1) Refer to Figure 12.4. Hula hoops are produced in a perfectly competitive market. This hula hoop firm is currently producing and selling 100 hula hoops per week. Which of the following is TRUE? 1) ________
   A) Hula hoop production is at the efficient level because *ATC* is minimized.
   B) Society would be better off if fewer hula hoops were produced because if this firm reduced its production, its profits would increase.
   C) Society would be better off if more hula hoops were produced because at the current level of production price is greater than marginal cost.
   D) Fewer resources should be devoted to hula hoop production because *ATC* is less than price.

2) All of the following are characteristics of a perfectly competitive market *except*: 2) ________
   A) perfectly elastic demand.
   B) barriers to entry.
   C) a homogeneous product.
   D) a large number of sellers.

3) Which of the following is *not* a characteristic of perfect competition? 3) ________
   A) Large number of firms in the industry.
   B) Outputs of the firms are perfect substitutes for one another.
   C) No barriers to entry or exit.
   D) Firms face downward-sloping demand functions.

4) The fact that the outputs of the firms in a perfectly competitive market are undifferentiated means that: 4) ________
   A) consumers don't care which supplier they buy from.
   B) purchase decisions are based only on price.
   C) the quality of each producer's output is the same.
   D) all of the above.

5) The manager of a perfectly competitive firm has to decide: 5) ________
A) the quantity of output the firm should produce and the price it should charge.
B) the quantity of output the firm should produce.
C) the price the firm should charge for its output.
D) neither the quantity of output the firm should produce nor the price it should charge because the market makes both of these decisions.

6) The demand curve faced by the individual perfectly competitive firm is: 6) ________
A) vertical.
B) horizontal.
C) downward sloping.
D) upward sloping.

7) Which of the following statements is *false*? 7) ________
A) Economic profit is the difference between total revenue and explicit costs.
B) Economic profit is generally less than accounting profit.
C) Economic profit is the difference between total revenue and the full opportunity cost of all the resources used in production.
D) The owners of a firm must be compensated for the use of their funds, because those funds have alternative uses.

8) In order to maximize its profits, a price-taking firm should produce the level of output at which: 8) ________
A) marginal revenue = marginal cost.
B) variable revenue = variable cost.
C) total revenue = total cost.
D) average revenue = average cost.

9) Marginal revenue is equal to: 9) ________
A) price, but only if the firm is a price searcher.
B) the change in P x Q due to a one unit change in output.
C) the change in price divided by the change in output.
D) the change in quantity divided by the change in price.

10) In the case of the perfectly competitive firm: 10) ______
A) marginal revenue is greater than the market price.
B) marginal revenue is less than the market price.
C) marginal revenue equals the market price.
D) marginal revenue is equal to, less than, or greater than market price depending on the level of output.

11) Assume a perfectly competitive firm is producing a level of output at which MR > MC. What should the firm do to maximize its profits? 11) ______
A) The firm should increase price.
B) The firm should do nothing — it wants to maximize the difference between MR and MC in order to maximize its profits.
C) The firm should increase output.
D) The firm should hire less labor.

12) A firm will earn zero economic profit when, at the firm's profit-maximizing level of output: 12) ______
A) P = ATC.
B) P = AVC.
C) MR = MC > ATC.
D) P = AFC.

13) When a firm is earning positive economic profit: 13) ______

A) price is greater than average total cost.
B) price is greater than or less than average total cost depending on the level of output.
C) price equals average total cost.
D) price is less than average total cost.

14) When price is greater than average variable cost but less than average total cost at the profit-maximizing level of output, a firm should: 14) ______

A) reduce output to the level at which price equals average variable cost to minimize its losses.
B) shutdown to minimize its losses.
C) continue to produce the level of output at which marginal revenue equals marginal cost.
D) increase output to minimize its losses.

15) Assume a perfectly competitive firm is producing the profit-maximizing level of output and price is less than average total cost, but greater than average variable cost. Which of the following statements is correct? 15) ______

A) The firm should continue to produce in the short run in order to minimize its losses.
B) The firm should move its resources to another industry.
C) The firm should raise its price enough to cover its losses.
D) The firm should shutdown in order to minimize its losses.

16) Assume a perfectly competitive firm is producing 300 units of output, P = \$10, ATC of the 300th unit is \$8, marginal cost of the 300th unit = \$10, and AVC of the 300th unit = \$6. Based on this information, the firm is: 16) ______

A) earning an economic profit of \$600.
B) incurring a loss of \$1,200.
C) incurring a loss of \$600.
D) earning an economic profit of \$1,200.

17) Assume a perfectly competitive firm is producing 500 units of output, P = \$7, ATC of the 500th unit is \$6, marginal cost of the 500th unit = \$7, and AVC of the 500th unit = \$5. Based on this information, the firm is: 17) ______

A) earning an economic profit of \$1,000.
B) incurring a loss of \$500.
C) earning an economic profit of \$500.
D) incurring a loss of \$1,000.

18) Assume that as the firms in a perfectly competitive industry expand output, the prices of productive inputs increase. All else constant, this would cause the individual firms' marginal cost curves to ________ and the market supply curve to become ________. 18) ______

A) shift up; flatter
B) shift up; steeper
C) shift down; steeper
D) shift down; flatter

19) When a perfectly competitive firm is earning zero economic profit: 19) ______

A) the firm is earning what it could earn in its next best alternative.
B) its total revenues equal its total implicit costs.
C) the firm's implicit costs equal \$0.
D) its total revenues equal its total explicit costs.

20) Assume there is an increase in the number of consumers in the market for a good sold by perfectly competitive firms that are initially producing the profit-maximizing level of output. For the individual firm, this would result in: 20) _______

A) a decrease in both price and the profit-maximizing quantity of output.
B) an increase in price and decrease in profit-maximizing quantity of output.
C) an increase in both price and the profit-maximizing quantity of output.
D) a decrease in price and increase in the profit-maximizing quantity of output.

21) Assume there is an increase in demand in a perfectly competitive market that was initially in long-run equilibrium. Which of the following statements is *false*? 21) _______

A) Consumers have shown that they now consider the good to be more valuable.
B) In the short run, profits will be lower than normal.
C) Over time, the market supply curve will shift right.
D) Resources from other industries will be attracted into the market.

22) Assume a perfectly competitive firm is producing 300 units of output, P = $10, ATC of the 300th unit is $8, marginal cost of the 300th unit = $10, and AVC of the 300th unit = $6. Based on this information, the firm is: 22) _______

A) incurring a loss of $1,200.
B) earning an economic profit of $1,200.
C) incurring a loss of $600.
D) earning an economic profit of $600.

23) Assume a perfectly competitive firm is producing 500 units of output, P = $7, ATC of the 500th unit is $6, marginal cost of the 500th unit = $7, and AVC of the 500th unit = $5. Based on this information, the firm is: 23) _______

A) incurring a loss of $500.
B) earning an economic profit of $1,000.
C) earning an economic profit of $500.
D) incurring a loss of $1,000.

24) Assume that as the firms in a perfectly competitive industry expand output, the prices of productive inputs increase. All else constant, this would cause the individual firms' marginal cost curves to ________ and the market supply curve to become ________. 24) _______

A) shift up; steeper
B) shift up; flatter
C) shift down; flatter
D) shift down; steeper

25) When a perfectly competitive firm is earning zero economic profit: 25) _______

A) its total revenues equal its total implicit costs.
B) its total revenues equal its total explicit costs.
C) the firm's implicit costs equal $0.
D) the firm is earning what it could earn in its next best alternative.

26) Assume there is an increase in the number of consumers in the market for a good sold by perfectly competitive firms that are initially producing the profit-maximizing level of output. For the individual firm, this would result in: 26) _______

A) a decrease in price and increase in the profit-maximizing quantity of output.
B) an increase in both price and the profit-maximizing quantity of output.
C) a decrease in both price and the profit-maximizing quantity of output.
D) an increase in price and decrease in profit-maximizing quantity of output.

27) Assume there is an increase in demand in a perfectly competitive market that was initially in long-run equilibrium. Which of the following statements is *false*? 27) _______

A) Consumers have shown that they now consider the good to be more valuable.
B) Over time, the market supply curve will shift right.
C) Resources from other industries will be attracted into the market.
D) In the short run, profits will be lower than normal.

28) Assume perfectly competitive firm Z is in long-run equilibrium and consumers' tastes and preferences for the type of good produced by Z increase. Which of the following will *not* happen in the long run? 28) _______

A) New firms will enter, causing market price to fall.
B) The firms that were already in the industry will return to a situation in which they earn zero economic profit.
C) Price will be lower at the new long-run equilibrium as a result of entry into the market.
D) The market will return to long-run equilibrium when profits return to their normal level.

29) Industry X, which is perfectly competitive, is in long-run equilibrium. Assume a new law is passed that requires employers in industry X to provide health insurance to previously uninsured employees. As a result of this new requirement we would expect to observe: 29) _______

A) a decrease in price and total output in industry X.
B) an increase in price and total output in industry X.
C) a decrease in price and an increase in total output in industry X.
D) an increase in price and a decrease in total output in industry X.

30) Assume that there is an improvement in the technology used by firms in a perfectly competitive industry. After all adjustments have taken place, we would expect to see: 30) _______

A) a decrease in equilibrium price and quantity.
B) an increase in equilibrium price and a decrease in quantity.
C) an increase in equilibrium price and quantity.
D) a decrease in equilibrium price and an increase in quantity.