

ECON 102: Microeconomics

Your Name: (15 points) _____

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Exam 3

1. Manufacturing plants in lesser-developed countries argue that production in these countries benefits not only the manufacturing plant, but it also benefits local businesses in related industries that are also under-developed. For example, having a number of manufacturing plants increases opportunities for raw material suppliers, businesses in the transportation industry, and the financial industry. The manufacturing plants therefore argue that investment in their industry leads to higher economic growth throughout the country.

(a) (5 points) If the manufacturing plants claims are true, how do social costs relate to private costs, and how do social benefits relate to private benefits.

(b) (5 points) Is this an example of a positive or negative externality? Explain why this is considered a market failure.

(c) (5 points) Given your answer in part (a), show with an appropriate graph what would be the socially optimal level of investment in the manufacturing industry.

(d) (5 points) In the graph in your answer to part (c), show also the level of production that would occur without any government intervention.

(e) (5 points) Suggest a government policy that would result in a socially optimal outcome. Show with a graph how your works.

2. Suppose carbon emissions resulting from burning gasoline in automobiles results in global warming, which imposes costs on all individuals in a society. For example, global warming has been suggested to cause more volatile, dangerous, weather, losses of plant life make it more difficult and costly to produce agricultural products, and losses of wildlife reduce gaming and environmental tourism opportunities.
- (a) (5 points) Is this an example of a positive or negative externality? Explain why this is considered a market failure.
- (b) (5 points) According to the Coase Theorem, a private market can result in a socially optimal outcome without government intervention. What assumption(s) of the Coase Theorem is violated, preventing people in society to use a socially optimal level of gasoline?
- (c) (5 points) Suggest a government policy that would result in a socially optimal outcome. Show with a graph how your works.

3. For each type of market, answer the following questions:

- Does this market result in the most efficient level of production in the long-run?
- How does the price consumers pay compare to the average total cost of production in the long-run?
- What are the long-run profits in this industry? What characteristic of this industry caused profits to be this way?

Use graphs where appropriate.

(a) (15 points) Perfect competition

(b) (15 points) Monopolistic competition

(c) (15 points) Monopoly