

Quiz 3 – Microeconomics – ECON 1B
Summer Semester – Cabrillo College
Dr. Robert McNab

Name: _____

Score: _____

INSTRUCTIONS: Read each question carefully. Use the back of the quiz for extended answers.

Assumption 1: Assume that gasoline is a normal good and that the market for gasoline in San Francisco is in equilibrium and that the average price of gasoline in Atlanta is \$2.00 a gallon with a quantity of 25 million gallons demanded weekly.

1. Using Assumption 1, illustrate the potential impact on market price and quantity, assuming all else remained equal, if the new technology reduced the cost of refining crude oil into gasoline and the price of methanol, a substitute fuel, increased? 2 points

Assumption 2: Assume that Frank's video store operates in a perfectly competitive market. Frank can rent 50 videos a day at \$2 a video. On average, it costs Frank \$1.75 to rent a video, of which \$1.25 is variable costs and \$0.50 is fixed costs.

2. Calculate Total Revenue, Total Costs, and Total Profit (or Loss) for Frank's video store. Based upon your answer, will firms enter the market, exit the market, or is the market in equilibrium? 3 points
3. Illustrate, using Assumption 2, the market and Frank's firm. Assume that 5000 videos are rented daily in the market. Ensure that you label all the cost and market curves. 3 points

1. the student should graph an increase in supply resulting from a decrease in refining costs and an increase in demand as the price of a substitute has increased...without specific information on the shifts of the demand and supply curves, we only know that market quantity has increased but are uncertain as to whether price has increased or decreased

2. Total revenue = $p * q = 2 * 50 = 100$

Total cost = $atc * q = 1.75 * 50 = 87.5$

Profit = $TR - TC = 12.50$

Due to positive short-run profits, firms would enter the industry

3. Using the methodology developed in class, the student would graph a perfectly competitive firm making short-run economic profits