AMERICAN UNIVERSITY OF BEIRUT

Suliman S. Olayan School of Business

Dr-shill

BUSS 305
FINAL EXAM

Time: 1:45   January, 2004

Answer Questions I, II and III then choose <u>two</u> of the following <u>three</u> questions.

I.   Multiple choice (30 points) – Circle the right answer

1. Which of the following statements is (are) true concerning a pure competition situation?
            a) Its demand curve is represented by a vertical line
            b) Firms must sell at or below market price
            c) Marginal revenue is equal to price
            d) Both b and c
            e) Both a and b

2. If a price ceiling is set below the market clearing price.
     a) supply will exceed demand
     b) rationing is likely
     c) consumers will face a situation of surpluses
     d) supply will exactly equal demand at that price

3. Governance mechanisms are designed
     a) to increase contracting costs
     b) to resolve post-contractual opportunism
     c) to enhance the flexibility of restrictive covenants
     d) to replace insurance
     e) none of the above

4. All of the following are mechanisms which reduce the adverse selection problem except _____
     a) warranties from established enterprises with non-redeployable assets
     b) high interest rates
     c) large collateral requirements
     d) brand names and product-specific promotions and retail displays
     e) higher prices in repeat customer transactions

5. Of the following, which is <u>not</u> an economic rationale for public utility regulation ?
     a) production process exhibiting increasing returns to scale
     b) constant cost industry
     c) avoidance of duplication of facilities
     d) protection of consumers from price discrimination
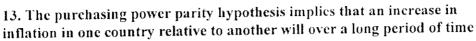   e) none of the above

6. A barometric price leader is:
   a) any firm in an industry
   b) always the largest firm
   c) always the smallest firm
   d) always the second largest firm
   e) always the oldest firm

7. Al oligopoly is characterized by:
   a) a relatively small number of firms
   b) either differentiated or undifferentiated products
   c) actions of any individual firm will affect sales of other firms in the industry
   d) a and b
   e) a,b, and c

8. If a cartel seeks to maximize profits, the market share (or quota) for each firm should be set at a level such that the _____ of all firms is identical
   a) average total cost
   b) average profit
   c) marginal profit
   d) marginal cost
   e) marginal revenue

9. The segmenting of customers into several small groups such as household, institutional, commercial, and industrial users, and establishing a different rate schedule for each group is known as:
   a) first-degree price discrimination
   b) market penetration
   c) third-degree price discrimination
   d) second-degree price discrimination
   e) none of the above

10. Transfer prices in a multiproduct divisionalized firm:
   a) serve as a measure of the marginal value of resources employed when making price output decisions that will maximize profits
   b) cannot be determined whenever one division sells its products both internally to another division and externally in a perfectly competitive market
   c) serves as a measure of the overall value of the resources employed in the division when analyzing the performance of the division
   d) a and c only
   e) a,b, and c

11. Joint products are:
   a) products which are technically independent in the production process
   b) exemplified by beef and hide from cattle
   c) products whose production processes are interdependent
   d) a and b
   e) b and c

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12. If the value of the U.S. dollar rises from DM 1.4 per dollar to DM 1.8 per dollar,

a) imports of automobiles from Germany will decline
b) American inflation will increase
c) German exports of all traded goods will decline
d) American exports to Germany will decrease
e) Sales by American manufacturers for the export markets will increase

13. The purchasing power parity hypothesis implies that an increase in inflation in one country relative to another will over a long period of time

a) increase exports
b) reduce the competitive pressure on prices
c) lower the value of the currency
d) increase foreign aid
e) increase the speculative demand for the currency

14. Trading partners should specialize production in accordance with comparative advantage, then trade and diversify in consumption because

a) out-of-pocket costs of production decline
b) free trade areas protect infant industries
c) economies of scale are present
d) manufacturers face diminishing returns
e) more goods are available for consumption

15. Companies that reduce their margins on export products in the face of appreciation of their home currency may be motivated by a desire to

a) sacrifice market share abroad but build market share at home
b) increase production volume to realize learning curve advantages
c) sell foreign plants and equipment to lower their debt
d) reduce the costs of transportation
e) all of the above

II.   (20 points) Explain the concept of _market failure_ in project evaluation. What are the different _reasons_ for its emergence.

III.   (20 points) A monopolist is selling its product in _two_ different markets. Demand in first market is $Q_1 = 1000 - 20 P_1$ while in the second market it is $Q_2 = 500 - 5 P_2$. Total cost fits the equation
$TC = 80 + 4 (Q_1 + Q_2)$
A. Calculate Q_1 and Q_2 in the two markets
B. Calculate P_1 and P_2 in the two markets
C. Calculate _total_ profit in two markets

IV.   (15 points) Compare with the help of _diagrams_ _monopolistic competition_ model with _monopoly_ model. In what respects they are _similar_ and in what respects they are _different?_ Give example about products that fit both models.

V. (15 points) From the following payoff matrix where payoffs refer to profits or losses that firms A&B earn by producing large cars or small cars. Determine (a) whether <u>firm</u> A has dominant strategy

Firm B

		Large Cars	Small Cars
Firm A	Large	(4,4)	(-2, -2)
	Small	(2, – 2)	(4, 4)

(b) whether firm B has dominant strategy (c) optimal strategy of each (d) the Nash equilibrium.

VI- (15 points)   Given the following data on the Balance of Payments for country Z.

- Service Exports	$ 600 million
- Net Unilateral Transfer	- 80 million
- Statistical Error	80 million
- Merchandise exports	800 million
- Capital inflow in short-run	980 million
- Merchandise imports	4000 million
- Capital outflow in long-run	1800 million
- Capital outflow in short-run	500 million
- Capital inflow in long run	3000 million
- Change in country's international reserves	1120 million
- Service imports	200 million

a) Tabulate the data in a standard way which shows major components of the Balance of Payment.
b) What is the <u>deficit</u> or <u>surplus</u> in country's Z Balance of payments?
c) How a certain country can correct a <u>deficit</u> in its <u>Balance</u> of <u>Payment</u>?