

## EC201: Principles of Macroeconomics

## In-class Worksheet 3

Fall 2021

1. Find out what is wrong with these following statements. Then show the correct impact by drawing appropriate graphs. Hint: mixing up a movement along vs a shift.

1. “A technological innovation that lowers the cost of producing a good might seem at first to result in a reduction in the price of the good to consumers. But a fall in price will increase demand for the good, and higher demand will send the price up again. It is not certain, therefore, that an innovation will really reduce price in the end.”
2. “A study shows that eating a clove of garlic a day can help prevent heart disease, causing many consumers to demand more garlic. This increase in demand results in a rise in the price of garlic. Consumers, seeing that the price of garlic has gone up, reduce their demand for garlic. This causes the demand for garlic to decrease and the price of garlic to fall. Therefore, the ultimate effect of the study on the price of garlic is uncertain.”

**2. The following table shows a demand schedule for a normal good.**

Price	Quantity demanded
\$23	70
21	90
19	110
17	130

1. Do you think that the increase in quantity demanded (say, from 90 to 110 in the table) when price decreases (from \$21 to \$19) is due to a rise in consumers' income? Why or why not?
2. Now suppose that the good is an inferior good. Would the demand schedule still be valid for an inferior good? Why or why not?
3. Lastly, assume you do not know whether the good is normal or inferior. Devise an experiment that would allow you to determine which one it was. Explain.

**3. Use a diagram to illustrate how each of the following events affects the equilibrium price and quantity of pizza.**

1. The price of mozzarella cheese rises.
2. The health hazards of hamburgers are widely publicized.

3. The price of tomato sauce falls.

4. The incomes of consumers rise, and pizza is an inferior good.

5. Consumers expect the price of pizza to fall next week.

**4. A study conducted by Yahoo! revealed that chocolate is the most popular flavor of ice cream in America. For each of the following, indicate the possible effects on demand, supply, or both as well as equilibrium price and quantity of chocolate ice cream.**

1. A severe drought in the Midwest causes dairy farmers to reduce the number of milk-producing cattle in their herds by a third. These dairy farmers supply cream that is used to manufacture chocolate ice cream.

2. A new report by the American Medical Association reveals that chocolate does, in fact, have significant health benefits.

3. The discovery of cheaper synthetic vanilla flavoring lowers the price of vanilla ice cream.

4. New technology for mixing and freezing ice cream lowers manufacturers' costs of producing chocolate ice cream.