

**Multiple Choice:**

1. Section 8.1 presents a discussion of fixed and variable costs, sunk costs and avoidable costs. The take-home message of this section is:
  - a. It is not possible to classify any cost (such as the purchase price of a license to operate a taxi cab) unless you know the context of the decision and the terms of the sale. If you buy a one-year license, the purchase price is fixed for one year after you buy the license. It is only a sunk cost if you cannot legally sell the license to another party (to recover your money). It was avoidable prior to moment at which you actually committed to purchase it.
  - b. All fixed costs are sunk.
  - c. Fixed costs cannot be avoidable.
  - d. None of the above.
2. JetBlue has several different types of contracts for leasing gates at airports. At some airports, JetBlue must rent each gate for an entire day, regardless of the number of flights per day. At these airports, the gate rental expense is a:
  - a. variable cost.
  - b. fixed cost.
  - c. avoidable cost.
  - d. sunk cost.
3. Coors uses rice to brew beer, and it grows its own rice. Coors could have chosen to purchase this rice in the rice market at market prices, but – instead – Coors prefers to grow it's own rice. Does this strategy reduce the cost of obtaining this input?
  - a. yes, if the cost of growing the rice is lower than the cost to purchase the rice in the market
  - b. no, because the opportunity cost of using the rice it grows is equal to the market price
  - c. none of the above
4. If a long-lived asset is “expensed”,
  - a. the asset is very costly.
  - b. the firm records the full cost of the asset in the year the expenditure occurs.
  - c. the expense records the true cost of the asset.
  - d. all of the above
5. Calpine's average cost function slopes up because:
  - a. Producing more electricity requires more natural gas. As Calpine increases output, it must use more natural gas, so the cost increases.
  - b. Calpine has diseconomies of scale.
  - c. Calpine uses its most efficient generators first. If that does not provide sufficient capacity, it adds generators that are less efficient. (Less efficient generators produce electricity at higher cost).
  - d. None of the above
6. Budget lines are one specific type of isocost line. The difference between the indifference curve/ budget line graphs used to analyze consumer decisions and the isoquant/isocost graphs used to analyze firm input purchase decisions is:
  - a. The household is more careful about how it spends its money.
  - b. A household has one budget line because the household has a specific income at any point in time. In contrast, a firm looks at the entire family of isocost lines because the firm chooses the

production quantity, buys inputs, and then sells the output to generate revenue. The firm is not restricted to one specific level of expenditure.

c. None of the above

7. When the firm is using the least-cost combination of inputs,

a. the ratio of the marginal products of the two inputs is equal to the ratio of the prices of the two inputs.

b. the marginal product of the last dollar spent on input A is equal to the marginal product of the last dollar spent on input B.

c. the ratio of the prices of the two inputs is equal to MRTS.

d. all of the above

8. Dell noticed that computer manufacturers produced their products long before consumers bought them. This delay between producing the product and selling the product generates two types of costs in the computer industry. Identify the two that are noted in Application 8.4.

a. The money spent to purchase the inputs and produce the product is not sitting in a bank. The opportunity cost of this capital is one of these costs.

b. The cost of computer parts was falling rapidly at that time. If input purchases could be delayed, the unit price would be lower.

c. Warehouses must be rented or purchased to store the assembled computers prior to sale.

9. Economies of scale occur when

a. total cost falls as output increases.

b. average cost falls as output increases.

c. the cost curve shifts as output increases

d. all of the above.

10. Frederick Smith founded Federal Express in 1973. This company is successful because Frederick Smith identified a segment of consumers that were not well-served by existing firms. He developed this insight when he was:

a. a high school student

b. an undergraduate student

c. a graduate student

d. an employee of one of the existing firms

## **Essay Questions**

### **A: Chapter 8 In-Text Questions**

8.5 (BW p.277)

8.6 (BW p.287)

### **B: End-of-Chapter 8 Questions (BW p.292)**

8.4 8.6 8.7 8.9 8.12 8.13 8.14 8.15 8.16