Chapter 16: Review

Readings  Chapter 16: all

Outline: See class handout

Text and Study Guide Questions

Questions for Review (from the text)
1 – 7

Problems and Applications (from the text)
1, 2, 5 – 11

Practice Problems from the Study Guide
1 (except c), 2 (a bit complicated but quite a bit like the collusion game we did in class)

Short Answer Questions from the Study Guide
1 – 7

True False Questions from the Study Guide
1 – 12, 14, 15

Multiple Choice Questions from the Study Guide
1 – 12, 14 – 17, 20

Advanced Critical Thinking Questions from the Study Guide
none

Other Problems

1. You and your friend “Conspiracy Conrad” are out to breakfast. He is reading an article about two firms, COX and YINC, which are bidding for a government contract to build the next generation optical space telescope. The two firms are both new to the satellite business. This is their first time competing for a satellite contract and competing against each other.

Conrad states; “I bet the two firms will get into a price fixing agreement. They will get together and each will agree to raise its bid. The two firms, in my opinion, will not act competitively. There is a lot of precedent here. Let me tell you another story of firms fixing prices when bidding for government contracts.”

Conrad precedes to tell you the story of price fixing by several firms bidding to supply the Tennessee Valley Authority generators. These firms repeatedly fixed (i.e. raised through collusion) their prices over a period of many years before they were caught.

Do you think Conrad is right? Is price fixing (i.e. collusion) likely in the case of COX and YINC? Why or why not?
2. Anthony is an anthropologist studying the Elpoep, a small tribal society in the Amazon. He is amazed at how cooperative members of the Elpoep are. "I grew up in New York" he states. "There, no one would help anyone else unless they got an immediate reward for it. Among the Elpoep, however, there is an amazing amount of sharing and cooperation. They are really willing to go out on a limb for each other." From an economic perspective, which of the following best explains the high levels of cooperation among the Elpoep?

a. Direct observation makes people less likely to maximize their scarce resources  
b. cooperation is (in terms of income elasticity) an inferior good  
c. a lack of money  
d. many repeated interactions between members of the Elpoep tribe  
e. b & c

Answer questions 3 – 5 based on the payoff matrix at right.

The payoff matrix models 2 firms and their decision on which size of railroad gauge (the distance between the rails) to adopt. Compatibility, is a major issue.

3. What is Bessie System’s dominant strategy?
   a. narrow gauge  
b. wide gauge  
c. Bessie System does not have a dominant strategy.  
d. More information is needed to answer this.

4. What is Burley Northern’s dominant strategy?
   a. narrow gauge  
b. wide gauge  
c. Burley Northern’s does not have a dominant strategy.  
d. More information is needed to answer this.

5. Does the game have exactly one Nash Equilibrium?
   a. Yes, both choose the narrow gauge.  
b. Yes, Bessie chooses narrow and B.N. chooses wide.  
c. Yes, both choose the wide gauge.  
d. Yes, Bessie chooses wide and B.N. chooses narrow.  
e. No the game has no Nash Equilibria, or multiple Nash Equilibria.
Answer questions 6 – 8 based on the payoff matrix at right. The payoff matrix models 2 firms, the only burger joints in town, and their decision on what price to charge for their combo meal.

6. What is Krusty Burger’s dominant strategy?
   a. Choose $4.00 as the price.
   b. Choose $5.00 as the price.
   c. Krusty Burger does not have a dominant strategy.
   d. More information is needed to answer this.

7. What is Sideshow Bob’s dominant strategy?
   a. Choose $4.00 as the price.
   b. Choose $5.00 as the price.
   c. Sideshow Bob does not have a dominant strategy.
   d. More information is needed to answer this.

8. Does the game have exactly one Nash Equilibrium?
   a. Yes, both choose $4.00.
   b. Yes, Krusty chooses $4.00 and Bob chooses $5.00.
   c. Yes, both choose $5.00.
   d. Yes, Krusty chooses $5.00 and Bob chooses $4.00.
   e. No the game has no Nash Equilibria, or multiple Nash Equilibria.