

Homework 2 – KEY

Average: 96.28 + Opts GI bonus

Due on 27/1/2026, by 23:00

The tasks in this assignment were designed for the average student to solve independently after mastering the material. The answers provided here are written in an instructional manner to help you understand the problem-solving process for each task. If you continue to struggle with a task after reviewing this key, the difficulty may stem not from the task itself, but from having missed or overlooked some parts of the required material.

1. ✓ Which of the following examples best describes the Law of Demand?

- A. When a good is advertised, its consumption increases.
- B. When the price of a good increases, firms produce more of that good.

97% C. When the price of a good increases, consumption of this good decreases.

- D. When consumer income increases, consumption tends to increase.
- E. All of the above.

[The law of demand states that as the price of a good increases, its quantity demanded tends to decrease. A, B and D do not indicate such a relationship]

2. ✓ Which of the following best describes the measure of elasticity?

- A. It is the ratio of the changes in two variables.

97% B. It is the ratio of the percentage changes in two variables.

- C. It is the product of the changes in two variables.
- D. It is the product of the percentage changes in two variables.

[Elasticity measures how much one variable changes in percentage terms, when another variable changes]

3. ✓ Which of the following is most likely to shift the demand curve for a good toward the left?

- A. A decrease in the price of its complements. *[This would make people consume more of the good in question regardless of its price]*

92% B. A decrease in the price of its substitutes. *[This would make people consume less of the good in question regardless of its price]*

- C. An increase in the price of the good. *[This would decrease the quantity demanded, but it doesn't affect the demand as a whole]*
- D. An increase in the production cost of the good. *[Production cost does not affect the demand]*

4. ✓ The demand for a good is price inelastic. Which of the following is most likely to happen if there is a 10% increase in its price?

- A. The quantity demanded for the good will increase more than 10%.
- B. The quantity demanded for the good will increase less than 10%.
- C. The quantity demanded for the good will decrease more than 10%.

96% D. The quantity demanded for the good will decrease less than 10%.

- E. The quantity demanded for the good will not change at all.

[The price increase will result in a decrease in quantity demanded. Moreover, since the good is price inelastic we have: $|\epsilon_d| < 1$ or $|\frac{\Delta Q\%}{\Delta P\%}| < 1$ or $|\Delta Q\%| < |\Delta P\%|$ or $|\Delta Q\%| < 10\%$]

5. ✓ The price of a good is measured in Singapore dollars and its quantity demanded is measured in liters. Which of the following would affect the value of its elasticity of demand?
- A. If we convert the price to another currency.
 - B. If we measure the quantity in ounces.
 - C. Both A and B.
 - 98%D. **None of the above.**
[The units of price (currency) and quantity will not make a difference to the elasticity because elasticity is a pure number with no units. When we divide $\Delta P/P$ and $\Delta Q/Q$ the units of price and quantity cancel out]
6. ✓ Which of the following goods should the government choose to increase the GST on, if it wishes to increase its tax revenue?
- 97%A. **Wireless service, whose price elasticity of demand is -0.5.** *[The increase in wireless service's price due to the excise tax would lead to a relatively smaller decrease in its quantity demanded, finally resulting in an increase in government's revenue from taxation]*
 - B. Wine, whose price elasticity of demand is -1. *[The increase in wine's price would lead to an equal decrease in its quantity demanded, leading to unchanged tax revenue]*
 - C. Designer belts, whose price elasticity of demand is -2. *[The increase in belts' price would lead to a relatively bigger decrease in their quantity demanded, resulting in lower tax revenue]*
 - D. All of the above would bring about the same tax revenue.
7. ✓ Which of the following is most likely to be an inferior good?
- A. A good that its demand increases when it is advertised.
 - 97%B. **A good that its demand increases when the household becomes poorer.**
 - C. A good that its quantity demanded increases when its price decreases.
 - D. A good for which its cross-price elasticity is negative.
[A good is inferior if consumers buy more (or less) of it as their income falls (or rises)]
8. ✓ The cross-price elasticity between two goods is -1. Which of the following is most likely to be true?
- A. They are substitutes.
 - 99%B. **They are complements.**
 - C. They are normal goods. *[We need information for income changes for this]*
 - D. They are inferior goods. *[We need information for income changes for this]*
[Since the increase in the price of one good leads to a decrease in the quantity demanded for the other good, these goods must be complements]
9. ✓ Which of the following goods is most likely to have the lowest income elasticity?
- A. Books.
 - 95%B. **Toilet paper.**
 - C. Air tickets.
 - D. Coffee.
[Toilet paper is a basic necessity that consumers tend to buy in roughly the same amount regardless of income, so its income elasticity must be very low, whereas books, air tickets and coffee are non-essential goods]

10. ✓ Suppose that the government completely bans the consumption of good A. How will this possibly affect good B, which is good A's complement?

- A. The quantity demanded for good B will increase but its demand will remain constant.
- B. The quantity demanded for good B will decrease but its demand will remain constant.
- C. The demand for good B will increase.

93% **D. The demand for good B will decrease.**

[The prohibition of good A will reduce consumers' desire to buy good B no matter what the price of B is. That is, the prohibition decreases the demand for B]