1. How would each of the following affect the operation of a regulated taxi market and the price of a medallion?
   a. A reduction in the maximum fare cabs can charge.
   b. An increase in the fares on subways and buses.
   c. An increase in parking fees in the downtown area.
   d. A police crackdown on the operation of illegal taxis.
   e. Announcement that the market will be deregulated in five years.

   a. The return to driving a cab decreases, reducing the number of people who drive cabs. The demand for and the price of medallions would fall.
   b. The demand for cabs rises, so the price of cabs will increase and the price of medallions will rise. This raises the cost of driving one’s own car downtown so the demand for cabs increases, causing fares to increase and the price of medallions to increase.
   c. Same as c.
   d. Same as c. Impact on the market will not be very great because new entry cannot occur until deregulation. The price of medallions will fall though, because the expected time period over which the higher prices can be collected has fallen.

2. a. "Because a monopoly is the only source of supply, consumers are entirely at its mercy. There is no limit to the price the monopoly can charge." Evaluate this statement.
   b. Why will Disneyland never set its admission price at a level where its demand curve is inelastic? Use the total revenue and total cost curves to illustrate your answer.

   a. The statement is incorrect. People always have the option to buy other products. The extent of market power the monopolist has depends on how close some other goods can be as a substitute for the monopolized good. If the statement were correct, why wouldn’t monopolies charge even higher prices than they do?
   b. A monopolist will never set a price at which the demand curve is inelastic because it is not the profit-maximizing price. Profit is maximized at the output where marginal revenue equals marginal cost. Since marginal cost will be positive, the profit maximizing output will be associated with the elastic portion of the demand curve.

3. In the market for organs for transplant, such as kidneys and hearts, the price is constrained to equal zero. Opposition to any type of remuneration for donating organs has been all but absolute from physicians and legislators. Reliance on altruism, however, does not appear to be working. The number of people waiting for organ transplants (and dying if they do not receive them) is double the number of willing donors. Relying on graphs,
explain the effect of the proscription of financial incentives for organ donations on the producer surplus and consumer surplus in this market.

Under the current system, the quantity supplied of organs is $Q$. Under unrestricted markets, the quantity would be $Q^*$ and price would be $P^*$. The total surplus at this equilibrium would be $ABQO$. Under the current system, the surplus is $ACQO$, which is less by the area of triangle $CBQ$.

![Graph showing the effect of proscription of financial incentives for organ donations on producer and consumer surplus.]

4.a. Explain why magazine publishers sometimes offer a lower per-unit price to consumers who take a longer time to renew their subscription. Also explain why this is a profit-enhancing strategy as long as not too many customers realize that they can get a better deal by holding out.

b. In 1996, the State University of New York's various colleges began setting lower tuition rates for courses offered at night, on weekends, during the summer, and at sites with vacant seats. From an economic perspective does such a policy make sense? Explain why or why not.

a. This is a form of third-degree price discrimination or market segmentation. Presumably, customers who take longer to renew are more price sensitive. Thus, if resale can be prevented, it makes sense to charge a lower price to offer customers who are more recalcitrant about confirming their interest in renewing a subscription.

b. This inter-temporal price discrimination or peak-load pricing makes sense. The policy reflects inter-temporal price discrimination if there is no difference in cost in offering classes at night or on the weekends versus the daytime. The practice reflects peak-load pricing if there is a cost difference. For the record, the State University of New York's facilities were used only 10 percent of the time in the evening and on weekends when the policy was implemented.
5. Suppose that there is a single seller of gasoline in a particular town. Suppose that policymakers, outraged by the prices charged by this monopoly seller, impose a price ceiling. Will the seller's output increase? Explain your answer.

Under unregulated monopoly, output is QM and price is PM. With a price ceiling of P, the demand curve the monopolist faces becomes PED, and the marginal revenue curve becomes PEGMR. The new profit-maximizing rate of output is Q and price is P, so output increases and price falls. Output need not always increase with a price ceiling, however. If the price ceiling is set below X the seller’s output will fall.

6. In 1995, President Bill Clinton unveiled sweeping proposals to regulate cigarette advertising. In response, the largest cigarette manufacturer, Philip Morris, whose leading brand, Marlboro, accounted for 30 percent of all cigarette sales in the United States, lambasted the proposals and filed suit against the federal government. Notwithstanding its actions, why do you think some tobacco industry analysts and even Philip Morris executives believed that the proposed regulations would end up benefiting the world's biggest cigarette supplier?

As detailed in Section 14.7, restrictions on advertising may serve to make an existing supplier's demand curve less price elastic and give the firm greater monopoly power. Alternatively, advertising bans limit the ability of new firms to announce that they have entered the market, meaning that an advertising ban is an entry restriction.

Merry Christmahanukwanzaakah!