

University of Toronto at Mississauga

Date: 2nd May, 2005

Course: Economics 380

Instructor: Simon Board

Duration: 2 hours

Aids: books, notes, calculators.

Total marks: 100

It is an academic offence for students to possess the following items at their examination desks: cell phones, pagers, wild orangutans, personal digital assistants or wristwatch computers. If any of these items are in your possession, put them with your belongings at the front of the room before the examination begins. No penalty will be imposed. Please note, students are not allowed to petition to rewrite a final examination. Good luck!

1. [20] Two Bertrand competitors face demand curve $p = a - q$ and have costs 0. The firms agree to price at $p^* \in (0, a/2)$, split the profits and to sustain it using Nash-reversion (i.e. returning to price 0) if either firm defects. What condition on the common discount factor, δ , is required to sustain cooperation?
2. [10] When you get admitted into Harvard this sends a positive signal to the job market. If education is unproductive, what use would there be to actually completing the degree?
3. [15] In Toronto, a taxi licence is currently worth around \$100,000. Suppose the government is profit-maximising and cannot commit to not to issue more plates. Argue that we would eventually expect to see the market flooded with plates and their value fall to zero. What would happen to the quantity sold if the profit-maximising government rented plates? Do you think the government's profits would be larger under selling or renting?
4. [15] Alcohol prices should be higher in the UK (where the government taxes alcohol and supermarket sells it) than Toronto (where the government sells alcohol via the LCBO). In the UK, the government and the supermarkets take a slice of the pie; in Toronto, there's only the government to worry about. Discuss.
5. [10] Name three (or more) examples of price discrimination in the airline industry.
6. [15] Holdup is due to lack of commitment. Holdup is due to incomplete contracts. Holdup is due to asset specificity. Which view is correct?
7. [15] Profits should be higher in markets without product differentiation since no one will ever enter. Discuss.