

Economics 380: Midterm 2

16 November, 2005

This test is open book. It is marked out of 100. You have 60 minutes. Good luck.

1. [25] Microsoft is currently considering leasing its Windows operating system. Why would it seek to do this? In your answer you should explain precisely how leasing could increase Microsoft's profits.
2. [25] What is the difference between second-degree and third-degree price discrimination? Name three examples of price discrimination in the airline industry. Include at least one example of second-degree price discrimination and at least one example of third-degree price discrimination.
3. [25] Suppose an airline is using yield management.
 - (a) Intuitively, when would the airline increase its price? When would the airline decrease its price? Explain why.
 - (b) Instead of yield management, the airline could simply use a fixed price. When will there be little loss from using a fixed price? That is, for what kind of flights will the lost profit be small?
4. [25] You are bidding for a used car at an auction.
 - (a) A car is likely to have private-value and common-value components: provide an example of each.
 - (b) Explain how the common value components can lead to a winner's curse.