

2. The table provided shows the short-run production function for Lowen Feline, a profit-maximizing firm that produces cat food.

Number of Workers	Total Quantity of Cat Food (bags)
0	0
1	5
2	12
3	18
4	23
5	27
6	30
7	32
8	33
9	32

Lowen Feline sells as many bags of cat food as it wants at a market price of \$10 per bag and hires as many workers as it wants at a market wage of \$18.

- (a) Lowen Feline’s fixed cost is \$90. Calculate the average fixed cost if Lowen Feline hires 6 workers. Show your work.
- (b) Assume labor is the only variable input to Lowen Feline. Calculate the marginal cost if Lowen Feline increases output from 27 to 30 units. Show your work.
- (c) With the hiring of which worker do diminishing marginal returns begin? Explain using numbers.
- (d) Determine the profit-maximizing number of workers Lowen Feline will hire. Explain using marginal analysis.
- (e) In the long run, a rival company, Gato Food, increases its production from 40 to 50 units, and its total cost increases from \$600 to \$900. Over the output range of 40 to 50 units, is Gato Food experiencing economies of scale, diseconomies of scale, or constant returns to scale? Explain using numbers.

Begin your response to this question at the top of a new page in the separate Free Response booklet and fill in the appropriate circle at the top of each page to indicate the question number.

2. Keepdry produces and sells rain jackets in a perfectly competitive product market at the price of \$5 per jacket and hires all the workers it needs in a perfectly competitive labor market at the wage rate of \$15. Labor is the only variable input, and the firm’s production schedule is provided in the table.

Number of Workers	Quantity of Output
0	0
1	9
2	20
3	27
4	32
5	34
6	35

- (a) Calculate the marginal revenue product of the second worker. Show your work.
- (b) Diminishing marginal returns will begin with the hiring of which worker?
- (c) Determine the profit-maximizing number of workers the firm should hire. Explain using marginal analysis.
- (d) Assuming Keepdry’s fixed cost is \$40, calculate Keepdry’s economic profit when hiring the profit-maximizing number of workers. Show your work.
- (e) Suppose Keepdry’s fixed cost increases to \$80. Will the profit-maximizing number of workers hired in the short run increase, decrease, or stay the same? Explain.

Begin your response to this question at the top of a new page in the separate Free Response booklet and fill in the appropriate circle at the top of each page to indicate the question number.

2. The table below shows the output a firm produces using different amounts of capital (K) and labor (L). The markets for capital and labor are perfectly competitive. The rental rate of capital is \$75 per unit, and the wage rate is \$200 per unit. In the short run, capital is fixed and labor is variable.

Labor	Output with K=1	Output with K=2
0	0	0
1	10	20
2	25	50
3	38	75

- (a) If the firm uses one unit of capital and one unit of labor, will it be operating with constant, increasing, or decreasing returns to scale? Explain using numbers from the table.
- (b) Assume now that the firm currently has two units of capital and is using three units of labor.
- Calculate the marginal product for the third unit of labor. Show your work.
 - Did the firm experience diminishing marginal returns with the addition of the third unit of labor? Explain using numbers from the table.
 - Calculate the firm's average total cost for its current level of production. Show your work.
 - If the firm's output is sold in a competitive market, what is the lowest output price at which the third unit of labor would be hired?