

Economics 3600
Labour Economics
Fall 2008
Dr. R. E. Mueller
Midterm Examination
October 17, 2008

Answer any three of the following questions in the examination booklet provided. Take a few minutes to think about your answers before you begin writing.

1. Assume that the wage rate for an individual increases. Use a labour-leisure diagram to explain what happens to labour supply. Do you expect the amount of time devoted to leisure to increase or decrease? Explain your answer.
2. Assume that the person in Question 1 has won the lottery. Show and explain what happens to the amount of leisure consumed. Does this differ from your response in Question 1. Explain your answer.
3. Assume that children are considered to be an inferior good (i.e., NOT a normal good). Explain what would happen to the demand for children as women's wages increase in the economy.
4. Assume that salaries increase for regular, full-time university professors. The university has a fixed amount of money to spend for wages. Using the appropriate diagram, show and explain what you would expect to happen to the employment of part-time faculty as regular faculty salaries increase.

Answer Key

1. This should show the income and substitution effects of a wage increase. We do not know, a priori, if the wage increase will result in more or less leisure be consumed. It depends on the size of the income and substitution effects, which depend on the individual's preferences for income and leisure.
2. This is pure income effect, so more leisure will be taken. This is unambiguous.
3. Both income and substitution effects would point away from having children. This is unambiguous.
4. We are not sure. There are both substitution and scale effects working in opposite directions. See notes for a diagram.