

## Precept 11/16/20005

1. Explain the economics of happy hour.
2. Last fall your preceptor decided to spend a few days in Florida. Martin went online and found a package on hotels.com for \$999. Since he was unsure whether to take it or not he kept on surfing the site, and the next day went back to that exact same offer in order to book it. Now the price was at \$1099, so your preceptor tried to change the dates or details. Nothing lowered the price, so he said to himself fine, demand seems to be strong, let's book it at \$1099. He went back to the original offer whose price had now increased to \$1149. Martin was now tempted to book immediately, since he thought there must be strong demand and the company's website probably updated prices all the time. Suddenly, however, his economic instincts kicked in and he deleted the cookies, and tried again: There was the trip for \$999. Discuss what is going on and why. You can also go to hotels.com and see if they do it to you.
3. If you book an airline flight and you do not show up for your first flight segment, the airline usually invalidates reservations on all your later segments. Suppose you went the first segment by train, now you call the airline to get reservations again for your further segments. The operator tells you that his computer cannot do that, even if he tried to. Why doesn't the airline update its computers so he can do that? Shouldn't the airline be happy about customers who use only part of their multi-city itinerary, since they pay full price but use only part of it?
4. Airbus and Boeing are the only firms in the market for large civilian aircraft. Suppose the inverse demand function on the market is

$$p = 12 - \frac{1}{3}Q$$

Their total cost functions are:

$$\begin{aligned} C_A &= \frac{1}{2}Q_A^2 \\ C_B &= Q_B^2 \end{aligned}$$

(i) Suppose that the firms fail to see that there is only two of them and behave competitively. What is the industry supply curve ?

(ii) Now suppose Airbus and Boeing collude and maximize total profit. Calculate the total industry production now and each company's production! Can you give a supply curve?

(iii) Why is it that in (ii) both firms produce, even though Boeing has higher costs than Airbus at any level of output ? Would they make more total profit if they shut down Boeing's production and let Airbus produce all the large airplanes?

(iv) The United States and the European Union are involved in a bitter trade dispute over subsidies for large civilian aircraft. The US has filed suit against the EU with the WTO in Geneva. The popular press, for example Newsweek, often portrays this as a battle between US and European national interests. Often they ask for the elimination of subsidies on both sides, and claim that this is in US national interest. What would the policy be that best serves American and European interests ? Whose interests does the current policy of large subsidies (launch aid in Europe, government subsidies for Boeing's Japanese suppliers and indirect subsidies via defence contracting to Boeing) serve?

5. What explains the price difference between a hardback and a paperback version of a book?
6. Some software programs offer student versions. These versions are more costly to produce than the standard version since they require costly tricks to disable certain features and a lot of thinking what should and what should not be disabled. How come that student versions are cheaper ?
7. Harvard University owns a hotel, The Inn at Harvard, very close to Harvard Square. When a university department or institute invites a speaker or holds a conference, they are charged a very low rate; the rates for other visitors are much higher. Similarly companies usually use marginal cost for transfer pricing, but charge a higher price to outside buyers. What is going on?