

CLEP Principles of Microeconomics

AT A GLANCE

Description of the Examination

The Principles of Microeconomics examination covers material that is usually taught in a one-semester undergraduate course in introductory microeconomics. This aspect of economics deals with the principles of economics that apply to the analysis of the behavior of individual consumers and businesses in the economy. Questions on this exam require test-takers to apply analytical techniques to hypothetical as well as real-world situations and to analyze and evaluate economic decisions. Candidates are expected to demonstrate an understanding of how free markets work and allocate resources efficiently. They should understand how individual consumers make economic decisions to maximize utility, and how individual firms make decisions to maximize profits. Test-takers must be able to identify the characteristics of the different market structures and analyze the behavior of firms in terms of price and output decisions. They should also be able to evaluate the outcome in each market structure with respect to economic efficiency, identify cases in which private markets fail to allocate resources efficiently, and explain how government intervention fixes or fails to fix the resource allocation problem. It is also important to understand the determination of wages and other input prices in factor markets and analyze and evaluate the distribution of income.

The examination contains approximately 80 questions to be answered in 90 minutes. Some of these are pretest questions that will not be scored. Any time candidates spend on tutorials and providing personal information is in addition to the actual testing time.

Knowledge and Skills Required

Questions on the Principles of Microeconomics examination require candidates to demonstrate one or more of the following abilities:

- Understanding of important economic terms and concepts
- Interpretation and manipulation of economic graphs
- Interpretation and evaluation of economic data
- Application of simple economic models

The subject matter of the Principles of Microeconomics examination is drawn from the following topics. The percentages next to the main topics indicate the approximate percentage of exam questions on that topic.

I. BASIC ECONOMIC CONCEPTS (10%–16%)

- A. Scarcity, choice, and opportunity cost
- B. Production possibilities curve
- C. Comparative advantage, specialization, and trade
- D. Economic systems
- E. Property rights and the role of incentives
- F. Marginal analysis

II. THE NATURE AND FUNCTIONS OF PRODUCT MARKETS (55–70%)

- A. Supply and Demand (15–20%)
 1. Market equilibrium
 2. Determinants of supply and demand
 3. Price and quantity controls

4. Elasticity
 - a. Price, income, and cross-price elasticities of demand
 - b. Price elasticity of demand and total revenue
 - c. Price elasticity of supply
5. Consumer surplus, producer surplus, and market efficiency
6. Tax incidence and deadweight loss
- B. Theory of consumer choice (5–10%)
 1. Total utility and marginal utility
 2. Utility maximization: equalizing marginal utility per dollar
 3. Individual and market demand curves
 4. Income and substitution effects
- C. Production and costs (10–15%)
 1. Production functions: short and long run
 2. Marginal product and diminishing returns
 3. Short-run costs
 - a. Fixed cost, variable cost, average cost, marginal cost, and total cost
 - b. The relationship between productivity and marginal cost
 4. Long-run costs and economies of scale
 5. Long-run cost-minimizing input combination
- D. Firm behavior and market structure (23–33%)
 1. Profit:
 - a. Accounting versus economic profits
 - b. Normal profit
 - c. Profit maximization: $MR=MC$ rule
 2. Characteristics of different market structures
 3. Perfect competition
 - a. Profit maximization
 - b. Short-run supply and shut-down decision
 - c. Firm and market behaviors in short-run and long-run equilibria
 - d. Efficiency and perfect competition
 4. Monopoly:
 - a. Sources of market power
 - b. Profit maximization
 - c. Inefficiency of monopoly
 - d. Price discrimination
 - e. Natural monopoly
 5. Oligopoly:
 - a. Interdependence, collusion, and cartels
 - b. Game theory and strategic behavior with payoff matrix
 - c. Dominant strategies and Nash equilibrium

6. Monopolistic competition:
 - a. Product differentiation and role of advertising
 - b. Profit maximization
 - c. Short-run and long-run equilibrium
 - d. Excess capacity and inefficiency

III. FACTOR MARKETS (6–12%)

- A. Derived factor demand
- B. Marginal revenue product
- C. Labor market and firms' hiring of labor

IV. MARKET FAILURE AND THE ROLE OF GOVERNMENT (8–14%)

- A. Externalities
 1. Marginal social benefit and marginal social cost
 2. Positive externalities
 3. Negative externalities
 4. Remedies
- B. Public and private goods
 1. Excludability, rivalry, and free-rider problem
 2. Provision of public goods
- C. Public policy to promote competition
 1. Antitrust policy
 2. Regulation
- D. Income distribution
 1. Income inequality
 2. Lorenz curve and Gini coefficient
 3. Sources of income inequality

Study Resources

Most textbooks used in college-level introductory microeconomics courses cover the topics in the outline above, but the approach to certain topics and the emphasis given to them may differ. To prepare for the Principles of Microeconomics exam, it is advisable to study one or more college textbooks, which can be found in most college bookstores. There are many introductory economics textbooks that vary greatly in difficulty. Most books are published in one-volume editions, which cover both microeconomics and macroeconomics; some are published in two-volume editions, with one volume covering macroeconomics and the other microeconomics. A companion study guide/workbook is available for most textbooks. The study guides typically include brief reviews, definitions of key concepts, problem sets, and multiple-choice test questions with answers. Many publishers also make available companion websites, links to other online resources, or computer-assisted learning packages.

To broaden your knowledge of economic issues, you may read relevant articles published in the economics periodicals that are available in most college libraries. *The Economist*, *The Wall Street Journal*, and *The New York Times*, along with local papers, may also enhance your understanding of economic issues.

A recent survey conducted by CLEP® found that the following textbooks are among those used by college faculty who teach the equivalent course. You might find one or more of these for sale online or at your local college bookstore. HINT: Look at the table of contents first to make sure it matches the knowledge and skills required for this exam.

Arnold, <i>Microeconomics</i> , Concise Edition (South-Western)
Bade and Parkin, <i>Foundations of Microeconomics</i> (Addison Wesley)
Baumol and Blinder, <i>Microeconomics: Principles and Policy</i> (South-Western)
Case and Fair, <i>Principles of Microeconomics</i> (Prentice Hall)
Colander, <i>Microeconomics</i> (McGraw-Hill)
Frank and Bernanke, <i>Principles of Microeconomics</i> , Brief Edition (McGraw-Hill)
Krugman and Wells, <i>Microeconomics</i> (Worth)
Lipsey, Ragan, and Storer, <i>Microeconomics</i> (Addison Wesley)
Mankiw, <i>Brief Principles of Microeconomics</i> (South-Western)

McConnell and Brue, <i>Microeconomics</i> (McGraw-Hill)
McEachern, <i>ECON for Microeconomics</i> (South-Western)
Salvatore, <i>Schaum's Outline of Microeconomics</i> (McGraw-Hill)
Samuelson and Nordhaus, <i>Microeconomics</i> (McGraw-Hill)
Schiller, <i>The Micro Economy Today</i> (McGraw-Hill)
Stiglitz and Walsh, <i>Principles of Microeconomics</i> (W. W. Norton)
Taylor and Weerapana, <i>Principles of Microeconomics</i> (South-Western)

These resources, compiled by the CLEP test development committee and staff members, may help you study for your exam. However, none of these sources are designed specifically to provide preparation for a CLEP exam. The College Board has no control over their content and cannot vouch for accuracy.

Modern States: Free CLEP Principles of Microeconomics Course

modernstates.org/course/principles-of-microeconomics/

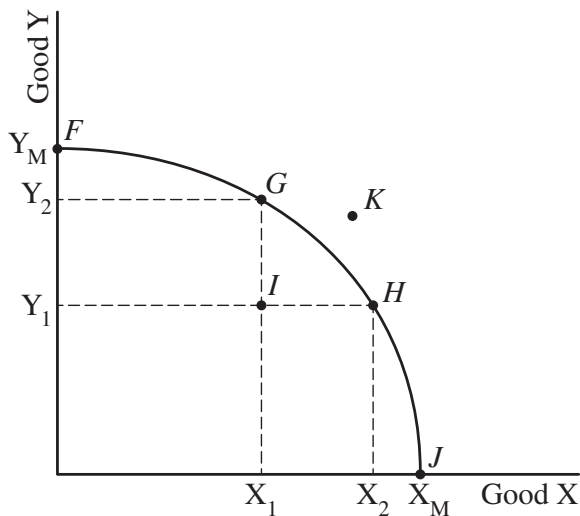
Berkeley Webcast and Legacy Course Capture webcast.berkeley.edu

(search for free Berkeley economics webcast courses)

Visit clep.collegeboard.org/clep-exams/principles-microeconomics for additional economics resources. You can also find suggestions for exam preparation in Chapter IV of the *CLEP Principles of Microeconomics Examination Guide*. In addition, many college faculty post their course materials on their schools' websites.

Sample Test Questions

The following sample questions do not appear on an actual CLEP examination. They are intended to give potential test-takers an indication of the format and difficulty level of the examination and to provide content for practice and review. For more sample questions and info about the test, see the *CLEP Official Study Guide*.



- Which of the following is true if the country is producing at point I?
 - The country can increase the production of Good X only by decreasing the production of Good Y.
 - The country is producing the efficient combination using all its available resources.
 - The country can produce more of both goods with its existing resources.
 - The country cannot increase the production of either good.
 - The country's level of unemployment will not change by moving from point I to point H.
- Suppose that oranges and apples are close substitutes. If the price of apples decreases, the equilibrium price and quantity of oranges are expected to change in which of the following ways?

Price of Oranges	Quantity of Oranges
A. Increase	Increase
B. Increase	Decrease
C. No change	Decrease
D. Decrease	Increase
E. Decrease	Decrease
- When the price of a product increases, a consumer's real income decreases, causing the consumer to decrease the quantity of the product demanded. This is known as
 - the substitution effect
 - the income effect
 - income elasticity
 - cross-price elasticity
 - diminishing marginal utility
- Assume that a firm is producing 1,000 units of output using both labor and capital. The last unit of labor used has a marginal product of 80 units of output; the last unit of capital used has a marginal product of 50 units of output. If the unit price of labor is \$16 and the unit price of capital is \$5; which of the following statements is true?
 - The firm should be able to produce more than 1000 units with the labor and capital currently being used.
 - The firm is minimizing the total cost of producing the 1000 units of output.
 - The firm should use more capital and less labor to reduce the total cost of producing 1000 units.
 - The firm should use less capital and more labor to reduce the total cost of producing 1000 units.
 - Since the price of capital is less than the price of labor, the firm should produce using all capital and no labor.
- A profit-maximizing firm will shut down in the short run if
 - marginal cost is greater than average total cost
 - marginal cost is equal to average total cost
 - price is less than average total cost
 - price is less than average variable cost
 - average variable cost is greater than average fixed cost
- Which of the following is true of the marginal factor cost for a firm hiring labor in a perfectly competitive labor market?
 - It is constant and equal to the market wage rate.
 - It is greater than the market wage rate.
 - It is less than the market wage rate.
 - It increases as the number of workers hired increases.
 - It decreases as the number of workers hired increases.

7. In a competitive market, when a negative externality exists, the private market produces
- more than the socially optimum level because the marginal social cost is less than the marginal private cost
 - more than the socially optimum level because the marginal social cost is greater than the marginal private cost
 - less than the socially optimum level because the marginal social benefit is less than the marginal private benefit
 - less than the socially optimum level because the marginal private benefit is greater than the marginal external cost
 - the optimal level of output because marginal private benefits equal marginal social costs

Bushels of Corn	Total Cost
0	\$20
1	\$25
2	\$32
3	\$41
4	\$52
5	\$65

8. The table above shows ABC Farming's total cost of producing various quantities of corn. The market for corn is perfectly competitive, and the market price for corn is \$10 per bushel. What is ABC Farming's profit-maximizing quantity?
- 1 bushel
 - 2 bushels
 - 3 bushels
 - 4 bushels
 - 5 bushels

Credit Recommendations

The American Council on Education has recommended that colleges grant three credits for a score of 50, which is equivalent to a course grade of C, on the CLEP Principles of Microeconomics exam. Each college, however, is responsible for setting its own policy. For candidates with satisfactory scores on the Principles of Microeconomics examination, colleges may grant credit toward fulfillment of a distribution requirement, or for a particular course that matches the exam in content. Check with your school to find out the score it requires for granting credit, the number of credit hours granted, and the course that can be bypassed with a passing score.

Answers to Sample Questions:

1-C; 2-E; 3-B; 4-C; 5-D; 6-A; 7-B; 8-C.