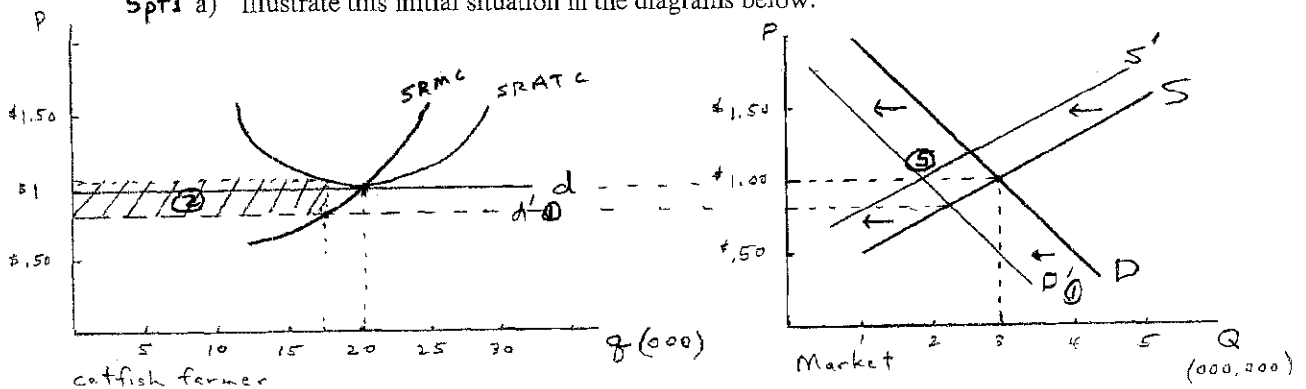


Problem Set #7 **KEY** The year is 1989. Catfish farming has been a thriving industry for several decades in the southeastern United States. The industry is currently in long-run equilibrium. The market price of catfish is \$1.00 per pound. 3 million pounds of catfish are produced each year. A typical catfish farmer produces 20,000 pounds of catfish per year.

5pts a) Illustrate this initial situation in the diagrams below:



10pts b) The removal of alligators from the endangered species list causes many individuals to start raising alligators. A glut of alligator meat on the market causes the market demand for catfish to decline, since many recipes in southern cookbooks call for the use of either catfish or alligator meat. Now for your analysis:

- What will happen to the price of catfish in the short run?

① Market price will fall after market demand shifts to the left.

- What will the short-run profit outlook be for catfish farmers?

② Catfish farmers will suffer short-run economic losses.

- Five years from now, will there be more, the same number, or fewer catfish farmers?

Losses will cause some farmers to exit the industry, so fewer.

- What will the profit outlook be for catfish farmers who are in the industry five years from now?

As firms exit, market supply will shift left and price will rise. Long-run outlook is zero economic profit.

- Will the price of catfish be equal to, higher than, or lower than \$1.00 per pound five years from now?

Price is expected to return to its original level - high enough so that farmers who stuck it out are earning a normal return, i.e. zero economic profit.