Economic Detective
Hy Feshn Neckties

Problem
Hy Feshn owns and operates a necktie boutique in one of New York City's trendy neighborhoods. The spring weather is mild, his clientele is loyal, and overall, his business prospers. A friend in the garment district tells him, however, that the coming fall's new fad will be the starched turtleneck shirt worn without a tie. Hy knows that fads fade quickly, but he still worries about keeping his business going during the down season sure to come.

Investigation 1
Hy's first line of defense is to cut expenses.
He calls Cap Hill, his congressional representative, to see if he is eligible for any government help. Cap says no, but his mother would let him have her nearby rent-controlled apartment for a fee of $500 in addition to the usual rent. Hy decides to pay the $500 and convert the cheaper second-story quarters into a boutique. Hy takes inventory before he moves and finds he has no more $30 Speckle ties but nearly his full shipment of $50 Spott ties in stock. He plans to make some adjustments after he moves.

1. In what way does Hy benefit from government price ceilings?

2. How does Hy's experience illustrate some of the problems connected with government price intervention?

3. What part of Hy's inventory illustrates excess supply?

Investigation 2
Settled in his new location, Hy stocks a new shipment of Speckle ties and raises the price to $32.50. At the same time, he lowers the price of the Spott ties to $4.5. The Speckle ties continue to sell so well that Hy runs out of them before his next shipment arrives. This time he raises their price to $37 and does not run out until another shipment comes in. The Spott ties still sit on the shelf, however. Hy puts them on sale for $39, at which price he just meets demand and is able to sell them steadily until he runs out of stock. He does not reorder, however, because he learns that waste dyes used in their manufacture are discoloring the waters of his favorite lake.

1. (a) What problem of excess demand does Hy face?

   (b) How does he remedy it?

2. In what way is Hy's market for Spott ties in disequilibrium?

3. (a) What is the equilibrium price for Hy's Speckle ties?

   (b) For his Spott ties?

4. To what spillover cost does Hy object?

Investigation 3
As the dreaded fall season approaches, a new designer offersHy an innovative "Soopt" tie suitable for the turtleneck collar. Hy orders 500 Soopt ties, which he prices at $75. The Soopt ties sell out in less than a week, with customers asking for more. Seeing the success of her ties, the designer offers her employees more than minimum wage to attract more workers. Before long her output rises, but she still cannot keep up with orders. Her problem eases when she starts charging Hy more for his orders, but Hy does not mind. His customers will pay up to $100 for a Soopt tie, even though other designers and stores have also started offering them.

1. What price floor appears in the Soopt tie story?

2. How does price flexibility serve the market for Soopt ties?

3. What role do profit incentives play in the success of Soopt ties?
Economic Detective

Elmo Entrepreneur

Problem:
Elmo Entrepreneur has a basement wood shop where he enjoys making model cars. He sells his cars to hobby shops, but lately orders have been falling off and Elmo's income is suffering. Reluctantly, Elmo decides he must look for a new business.

Investigation 1:
While delivering an order of model cars at the mall, Elmo stops to buy a new pair of running shoes. To his surprise, the price of his favorite shoes has increased $15. The next day, Elmo goes to the library and studies the market supply and sales data for the city's running shoes. He soon decides that this is a good time to enter the shoe manufacturing business. He will make his favorite style and sell his shoes directly to customers for $60 a pair, or the price charged by all suppliers.

1. What sort of data did Elmo's library search probably reveal to prompt his decision?
2. How will Elmo's new business affect the market supply for running shoes?
3. What amount of income can Elmo expect in his new business?
4. How does Elmo's decision illustrate the law of supply?

Investigation 2:
Elmo starts small. He uses his garage as a factory, with his property taxes costing $50 a month and his utilities $40 a month. He buys a cutting-and-stitching machine, hires a worker, and finds that he can produce 5 pairs of shoes an hour. Encouraged, Elmo hires another worker, doubling his labor costs but increasing output to 12 pairs per hour. He continues to hire more workers, increasing output to 24 pairs with three workers, 36 pairs with four workers, and 48 pairs with five workers. In the meantime, the cost of leather for shoe tops and soles has risen twice, but the cost of fabric for linings has fallen enough to offset the rising cost of leather.

1. What factors make up Elmo's variable costs?
2. What is Elmo's total revenue per hour after he hires three workers?
3. What is Elmo's marginal product of labor after he hires a second worker?
4. When does Elmo reach a diminishing marginal return of labor?
5. What does Elmo pay in fixed costs?

Investigation 3:
Elmo's shoe business does so well that he adds another room to his garage and buys another cutting-and-stitching machine. Unwelcome news comes in the mail, however. The federal government, deciding that running shoes are harmful to the foot, places a tax on all running-shoe producers. Seeing his profits shrink, Elmo lays off a worker and cuts his output. After further research, the federal government reverses its position and removes the tax, but the running shoe industry remains depressed. To revive it, the city council votes to pay running shoe producers $1 a pair but requires them to insert heel cups in the shoes to ensure foot health.

1. How does Elmo try to increase his production?
2. a. What kind of tax does the federal government impose?
   b. How does it influence quantity supplied?
3. What regulation does Elmo have to follow?
4. a. What subsidy does Elmo receive?
   b. What is the source of the subsidy?