1. Sugar is produced in a perfectly competitive market using inputs from perfectly competitive factor markets. Frank Sugar Co. is a representative firm in the sugar market.

(b) Assume the demand for sugar increases and sugar is produced in a constant-cost industry.

(i) On your graph in part (a), show the short-run effect of the increased demand for sugar on the market price, labeled P_2, and the quantity sold by Frank Sugar Co., labeled Q_N.

(ii) Compared to the equilibrium identified in part (a)(ii), what will happen to the short-run profit earned by Frank Sugar Co. as a result of the increased demand for sugar?

(iii) When the market adjusts to long-run equilibrium, how will the market price of sugar in the long run compare to P_2 ? Explain.

(d) Assume the government decides to intervene in the market to affect consumers' incentives and to address the negative impact of sugar consumption on public health. Which of the following policies would best achieve that objective in the short run: a lump-sum tax, a per-unit tax, a lump-sum subsidy, or a per-unit subsidy? Explain.

Begin your response to this question at the top of a new page in the separate Free Response booklet and fill in the appropriate circle at the top of each page to indicate the question number.