



Eastern University, Sri Lanka
Faculty of Commerce and Management

First Year Second Semester Examination in BBA /B.Com 2007/08 (September 2009)

(Proper and Repeat)

ECN 1214 Economic Theory

Answer all Question

Time: 03 hours

1. a. What are the basic problems of an economic system? How do they arise due to the scarcity of resources?
(07 Marks)
- c. Explain how the basic economic problems of an economy are solved in a free market economy
(06 Marks)
- d. What is increasing opportunity cost of a commodity? Explain the Reasons for increasing opportunity cost with a diagram
(07 Marks)
2. a. Distinguish between Total Utility and Marginal Utility
(05 Marks)
- b. Explain the Law of Diminishing Marginal Utility
(05 Marks)
- c. You are given the following utility function
$$U = \frac{1}{2} XY$$

U = utility
X, Y = commodities
The price of the commodity X is P_x and the price of the commodity Y is P_y
Consumer income is M
Derive the demand function for commodity X and Y
(10 Marks)
3. a. Explain the three stages of short-run production function with a diagram
(08 Marks)
- b. Explain the relationship between Average cost and Marginal cost in short run with a diagram
(06 Marks)
- c. Explain the Long run equilibrium of a perfect competitive firm with a diagram
(06 Marks)

4. a. Explain the circular flow of income in a simple economy with diagram (05 marks)

b. Consider the following consumption function of an economy

$$C = 100 + 0.75Y_d$$

Where, Y is National Income.

If the planned level of investment in a year equals 90 million, what will be the equilibrium level of national income?

c. Briefly explain the main functions of money (05 Marks)

d. Distinguish between a central Bank and a Commercial Bank (05 marks)

5. Briefly explain the following

- a. Inflation
- b. Comparative advantage
- c. World financial crisis
- d. Floating exchange rate

(20marks)
