

EASTERN UNIVERSITY, SRI LANKA
FACULTY OF COMMERCE AND MANAGEMENT
First year/ Second Semester Examination in Bachelor of Business Administration /
Bachelor of Commerce
Repeat 2002/03

ECN. 1014 - Economic Theory



Answer all Questions

Time : 3 Hours

Part I

1. The problem of choice between the various uses of resources arises because
 - a. Resources are scarce
 - b. Resources have alternative use
 - c. Productivity of scarce resources various in their alternative use and producers want to maximize their profit

2. Which of the following statement is true?
 - a. The desire for a commodity backed by ability and willingness to pay is demand
 - b. The demand for a commodity is inversely related to the price of its substitutes
 - c. Demand for car and price of petrol are inversely related.

3. When total utility increases, marginal utility is
 - a. Negative and increasing.
 - b. Negative and declining.
 - c. Positive and declining.

4. At the equilibrium, the slope of the indifference curve is
 - a. Greater than the slope of the budget line.
 - b. Equal to the slope of the budget line.
 - c. Smaller than the slope of the budget line.

5. The law of diminishing returns implies that
 - a. Quantity of an input is increasing.
 - b. Quantity of an input is decreasing.
 - c. Quantity of an output is decreasing

6. Consider the cost function $C = 10 + 2Q + Q^2$ and $P = 22$, the profit is maximum when the output is
 - a. 20 Units.
 - b. 10 Units.
 - c. 8 Units.

7. The MC curve intersects the AVC curve and the AC curve at their minimum point. The above statement is true.
- Always.
 - Never.
 - Sometime.
8. Which of the following statements is correct?
- A firm is a price – maker under perfect competition.
 - Under perfect competition a firm fixed its price where its $AR = MR$.
 - Free entry and free exit is a major characteristic under monopoly.
9. Which of the following is not an important use for national income accounting
- it makes possible an estimate of the output of final goods and services in the economy.
 - it permits measurement of the economic efficiency of the economy.
 - It enables the economists to chart the growth or decline of the economy over a period of time.
10. GDP in an economy is \$ 3,452 billion. Consumer expenditure are \$ 2,343 billion, government purchases are \$ 865 billion, and gross investment is \$378 billion. Net export are
- \$ 135 billion
 - \$ 93 billion
 - \$ 123 billion

(2x10 Marks)

Part II

2. i. What constraints does the consumer face in seeking to maximize the total utility from personal expenditure? (5 Marks)
- ii. Express and explain mathematically the conditions for consumer equilibrium. (5 Marks)
- iii. The following Table shows an individual marginal utility for commodity X and Y. Suppose the price of commodity X and commodity Y are 10 rupees and the consumer's income is 80 rupees per week. He/she spent entire income on the two commodities.

Q	1	2	3	4	5	6	7	8
MU _x	11	10	9	8	7	6	5	4
MU _y	19	17	15	13	12	10	8	6

- Calculate how the consumer spend the income in order maximize the total utility.
- What is the total utility received by the consumer

(10 Marks)

3. i. Explain the various type of business organizations.
- ii. Explain why AC curve and AVC curve come closer when output increases.
- iii. What do you understand by iso-quant and marginal rate of substitution?
- iv. Consider the following Cobb – Dauglus production function

$$Q = K^{0.25} \cdot L^{0.5}$$

Determine the function exhibits increasing, constant and decreasing return to scale.

(4x5 Marks)

4. i. Briefly state the basic difference between the monopololy and perfect competitive firm?
- ii. Distinguish between monopolist excess profit equilibrium and competitive firm's excess profit equilibrium in short run.
- iii. What are the sources that might create various types of monopoly?
- iv. Do you agree that perfect competition leads to optimum level of output in the Short run.

(4x5 Marks)

5. i. Explain the circular flow of income.

(5 Marks)

- ii. Explain three sector model of circular flow of income and the assumptions of the model

(10 Marks)

- iii. How you can overcome the disequilibriam situation in the circular flow of income model

(5 Marks)

