

**UNIVERSITY OF COLOMBO, SRI LANKA**  
**FACULTY OF ARTS**

**First Year Examination in Arts - 2018**

**First Semester Final Examination**

**ECN 1103 – Principles of Economics**

***Time Allowed: Two Hours (02) Only***

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Question (1). Answer any 5 questions of the following.

- i. Explain the reasons for a downward sloping demand curve an upward sloping supply curve and outline the underlying assumption in drawing these curves.
- ii. Distinguish between entrepreneurship and labor and describe the specific functions of an entrepreneur.
- iii. Examine the welfare impact of a unit tax imposed on a consumer good using an appropriate demand and supply diagram.
- iv. Discuss the major macroeconomic issues faced by countries and explain the policies to address them
- v. What is meant by economic growth? How it is measured? what are the basic issues in comparing growth rates of a large economy and a small economy?
- vi. Distinguish between potential output and actual output and explain how the actual output behave during the four phases of a business cycle

(10 marks each part)

Part I. Select one question from this section

Question (2)

(a) The market demand and supply functions are given below

$$QD = 725 - 2.5P$$

$$QS = 100 + 10P$$

Find the equilibrium price and quantity

(5 marks)

(b) Calculate the price elasticity of demand and supply at equilibrium and comment on them.

(5 marks)

(c) If the government implements a minimum price on this product at Rs.60, what would be the impact on the market? Explain with calculations.

(5 marks)

(d) Explain what is meant by "change in quantity demanded" and "change in demand" in an appropriate diagram. What causes these changes?

(5 marks)

(e) How do you decide whether a good is a normal good or an inferior good and a substitute or complementary good using income and cross elasticity of demand? (5 marks)

**Question (3)**

- (a) Define the following costs concepts
- (i) Fixed cost and variable costs
  - (ii) Average fixed cost and average variable costs
  - (iii) Average cost and marginal cost (5 marks)
- (b) Explain the reasons for the "U" shape of the average cost curve (5 marks)
- (c) Outline the profit maximizing condition of a firm and explain the meaning of it (5 marks)
- (d) What is meant by "short run" and "long run" equilibrium of a firm? (5 marks)
- (e) "A perfectly competitive firm in the short run can continue production even if it makes a loss" Explain why. (5 marks)

**Question (4)**

- (a) How do you explain the differences between monopolistic competition and oligopoly market structures? (5 marks)
- (b) A perfectly competitive firm can earn a super normal profit or makes a loss only in the short run. Explain why. (5 marks)
- (c) Why is a monopoly firm can influence the price or quantity of the product it produces but not both at a time. (5 marks)
- (d) Explain why are the prices charged by oligopoly firms stable than the firms in the other markets. (5 marks)
- (e) Explain the ways in which monopolies can occur. (5 marks)

Part II Select one question from this section

**Question (5)**

- (a) What is circular flow of income model? Explain the importance of circular flow of income model in explaining economic activities in a three-sector economy (7 Marks)
- (b) Discuss the three approaches of measuring national income? Show that these three approaches give identical result. (6 Marks)
- (c) Explain why we cannot calculate the national product simply by adding up the production of all firms. (5 Marks)
- (d) What is meant by withdrawal and injections? How do they affect the size of circular flow of income and expenditure in an economy? (7 Marks)

**Question (6)**

- (a) Why is the national income measured at factor prices and not at market prices? (3 Marks)
- (b) What is the difference between GDP and GNP? (3 Marks)
- (c) What is the difference between Gross and Net National product? (3 Marks)
- (d) How do you eliminate double and multiple counting? (4 Marks)
- (e) What are the measurement errors of the GDP figures? (6 Marks)
- (f) What are the uses and weaknesses of computing national accounts? (6 Marks)

**Question (7)**

Suppose the consumption function is given by  $C = 110 + 0.7Y$ , while investment  $I = 50$ , government purchases  $G = 200$ , exports  $X = 100$  and imports  $M = 110$

- (a) What is the equilibrium level of income? (6 Marks)
- (b) What is the level of saving in equilibrium? (5 Marks)
- (c) What is the value of the multiplier? (4 Marks)
- (d) Draw a diagram indicating the equilibrium? (5 Marks)
- (e) Starting from  $S=I$  and the saving function, derive the equilibrium level of income? (5 Marks)

**Question (8)**

- (a) Explain the short run and long run aggregate supply curves. What are the reasons for the difference in their shapes. (5 marks)
- (b) What is a production function? Explain the components of a typical production function. (5 mark -)
- (c) What is meant by total factor productivity? How it is measured? (5 marks)
- (d) Explain the concept of Gross Domestic Capital Formation (GDCF). How it is measured? (5 marks)
- (e) Explain the role of interest rate in the "Money Market" and the "Loanable Funds market" (5 marks)