



## Introduction to Economics & Finance

Foundation Examination  
Spring 2013  
Module B

6 March 2013  
100 marks - 3 hours  
Additional reading time - 15 minutes

### Instructions to candidates:

- (i) All the Questions from Section A are compulsory.  
(ii) Attempt any TWO out of THREE Questions from Section B.

### Section A

- Q.1 (a) What is “Market mechanism”? Explain how it resolves the basic economic problems. (07)  
(b) Draw a production possibility curve from combinations of consumer goods and capital goods as set out below:

Possibilities	A	B	C	D	E
Consumer Goods	120	100	80	50	0
Capital Goods	0	30	60	80	100

(03)

- Q.2 (a) Describe and differentiate between the concepts of “Change in quantity demanded” and “Change in demand”. Draw diagrams in support of your answer. (10)  
(b) Briefly explain the following:  
(i) Income elasticity of demand (05)  
(ii) Cross price elasticity of demand (05)

- Q.3 (a) What is “Marginal Efficiency of Capital”? Briefly state the level of interest up to which firms are willing to borrow capital. Support your answer with the help of a diagram. (10)  
(b) What do you understand by the term “Oligopoly”? Briefly explain the economic effects of oligopolistic markets. (05)

- Q.4 Select appropriate answer from the options available for each of the following Multiple Choice Questions (MCQs). Each MCQ carries ONE mark.

- (i) The short-run average cost curve is:  
(a) Upward sloping (b) Downward sloping  
(c) U shaped (d) A straight line
- (ii) Which of the following has a relatively flat supply curve?  
(a) Raw material (b) Land (c) Labour (d) Capital
- (iii) Rapid increases in price level during recession or high unemployment is referred to as:  
(a) Stagnation (b) Inflation (c) Stagflation (d) Slump
- (iv) Increasing long-run average costs are associated with:  
(a) Law of diminishing return (b) Constant returns to scale  
(c) Increasing returns to scale (d) Decreasing returns to scale
- (v) A profit maximising firm will produce output where:  
(a) Total sales are maximised (b) Average total costs are minimised  
(c) Marginal cost equals marginal revenue (d) Average revenue is maximized

- (vi) Which of the following is **NOT** a motive for holding money?  
 (a) Inflationary motive (b) Precautionary motive  
 (c) Transactions motive (d) Asset motive
- (vii) The sum of frictional and structural unemployment is considered as the:  
 (a) Demand deficient unemployment (b) Natural rate of unemployment  
 (c) Seasonal rate of unemployment (d) Cyclical rate of unemployment
- (viii) The productivity of an input is **NOT** affected by:  
 (a) Technological change (b) Economies of scale  
 (c) Advances in knowledge (d) Diminishing returns
- (ix) The ratio of change in consumption to change in income is called:  
 (a) Marginal propensity to consume (b) Average propensity to consume  
 (c) Aggregate consumption (d) Consumption function
- (x) If planned injections are less than planned withdrawals:  
 (a) Unemployment will tend to reduce (b) Inflation will tend to rise  
 (c) Balance of trade will tend to improve (d) National income will tend to rise
- (xi) International trade encourages the formation of:  
 (a) Perfect competition (b) Imperfect competition  
 (c) Monopolistic competition (d) Oligopoly
- (xii) To transform GDP from market prices to basic prices it is necessary to:  
 (a) Exclude imports (b) Subtract taxes and subsidies  
 (c) Subtract taxes and add subsidies (d) Add income from abroad
- (xiii) A movement along an indifference curve from left to right means that the consumer's:  
 (a) Marginal utility has risen (b) Total utility is unchanged  
 (c) Marginal utility has fallen (d) Money income is unchanged
- (xiv) Which of the following is a direct tax?  
 (a) Federal excise duty (b) Value added tax  
 (c) Sales tax (d) Capital gains tax
- (xv) Firms can benefit through specialisation and international trade due to:  
 (a) Absolute advantage (b) Comparative advantage  
 (c) Unilateral advantage (d) All of the above

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### Section B

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- Q.5 (a) What do the terms Demand-pull inflation and Cost-push inflation mean? **(04)**  
 (b) Explain the concept of cost-push inflation with the help of demand and supply curves. **(08)**  
 (c) What is meant by Price Index? Explain any three commonly used price indices. **(08)**
- Q.6 (a) Briefly describe the main factors on which general rate of interest depends. **(08)**  
 (b) Differentiate between fiscal deficit and the national debt. What relationship exists between the two over a period of time? Also discuss the direct effect of rise in interest rates on the fiscal deficit and the national debt. **(08)**  
 (c) Briefly explain the economic problems which a country may face on account of high national debt in relation to its Gross Domestic Product. **(04)**
- Q.7 (a) Briefly explain the "Flows" in a Circular Flow of Income. Draw a diagram of the Circular Flow of Income and identify **three** types of 'Withdrawals' and 'Injections' into the Circular Flow. **(10)**  
 (b) What is "Free Trade"? Briefly describe its main advantages. **(10)**

**(THE END)**