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**SCHOOL OF ACCOUNTING AND BUSINESS
BSc. (APPLIED ACCOUNTING) GENERAL / SPECIAL DEGREE
PROGRAMME**

**YEAR I SEMESTER I (Group A)
END SEMESTER EXAMINATION – JULY 2015**

BEC 10125 Microeconomics

Date : 20th July 2015
Time : 9.00 a.m. - 11.30 a.m.
Duration : Two and half (02 ½) hours

Instructions to Candidates:

- This paper consists of three sections (A, B and C).
- Section A – Answer **ALL** the questions in the sheet provided.
Section B – Answer **FOUR** questions out of the five questions given.
Section C – Answer **ONE** question out of the two questions given.
- The total marks for the paper is 100.
- The marks for each question are shown in brackets.
- Answers should be written neatly and legibly.

Section A

Answer **ALL** questions in this section.

Select the most appropriate answer.

1. Assume you bought a laptop for Rs. 100,000/=. A similar laptop would now cost Rs. 120,000/= but yours would only obtain Rs.75,000/=. The present opportunity cost of owning the laptop is;
 - a. Rs 120,000/=
 - b. Rs 100,000/=
 - c. Rs 75,000/=
 - d. Rs 25,000/=
 - e. Rs 20,000/=
2. As the price of coal used in the production of electricity decreases, ceteris paribus:
 - a. The demand for electricity will increase
 - b. The demand for electricity will decrease
 - c. The supply of electricity will increase
 - d. The supply of electricity will decrease
 - e. There will be no change in demand and supply of electricity
3. In which way does monopolistic competition differ from perfect competition?
 - a. Products are differentiated
 - b. Average revenue exceeds average cost in long-run equilibrium
 - c. The market has one firm
 - d. Marginal revenue exceeds marginal cost in long-run equilibrium
 - e. There are significant barriers to enter and exit
4. If deregulation of telecommunication charges, other things being equal, led to lower prices and higher revenues, it could be concluded that
 - a. The demand for telecommunication is elastic
 - b. The demand for telecommunication is inelastic
 - c. The demand for telecommunication is unitary elastic
 - d. The supply for telecommunication is elastic
 - e. The supply for telecommunication is inelastic

5. A decrease in a consumer's money income is most likely to
- Pivot the budget line only from one axis as the consumer can purchase less of one good.
 - Shift the indifference curve inwards as the consumer can now satisfy fewer wants
 - Shift the budget line outwards as the consumer can now purchase more of both goods.
 - Shift the budget line inwards as the consumer can now purchase less of both goods.
 - Shift both the indifference curve and budget line inwards as the consumer can now satisfy fewer wants as well as purchase less of both goods.
6. Economic rent will be greater, the more
- Elastic the demand curve of labour
 - Inelastic the demand curve of labour
 - Elastic the supply curve of labour
 - Inelastic the supply curve of labour
 - This does not depend on the elasticity of either supply or demand
7. In the short run, when the marginal product is less than the average product:
- The average product is decreasing
 - The average product is increasing
 - The marginal product is increasing
 - The marginal product is decreasing
 - The total product is increasing at an increasing rate
8. A strategy that gives higher payoffs no matter what the rival does is best known as;
- Mutual strategy
 - Dominated strategy
 - Dominant strategy
 - Nash strategy
 - Rational strategy

9. Zero economic profits means

- a. The firm is making neither profit nor losses.
- b. The firm needs to increase its advertising expenditures.
- c. The firm will exit the industry in the long run.
- d. The firm is covering all of its opportunity costs and will remain in the industry.
- e. The firm is charging a lower price.

10. The three firm concentration ratio for five industries are given as follows;

<i>Industry</i>	<i>Three firm concentration ratio</i>
A	34
B	65
C	78
D	12
E	26

Based on the above information the industry which is highly concentrated is;

- a. Industry A
- b. Industry B
- c. Industry C
- d. Industry D
- e. Industry E

(10 marks)

Section B

Answer **only Four (04)** questions

Question No. 01

1. Explain the following concepts using appropriate examples;
 - a. Microeconomics and Macroeconomics
 - b. Positive economics and Normative economics

(4 marks)

2. Differentiate between 'income elasticity of demand' and 'cross price elasticity of demand'.

(4 marks)

3. Analyse how each of the following market conditions would affect the equilibrium price and quantity of tea market using diagrams.
 - a. Increase in prices of coffee
 - b. Increase in prices of milk powder
 - c. Increase in wage rate of tea estate workers

(6 marks)

4. 'Though the effects are similar, imposing indirect taxes are more effective than price controls'.

Evaluate this statement using diagrams.

(6 marks)

(Total 20 marks)

Question No 02

1. Differentiate between 'income consumption curve' and 'price consumption curve'.
(4 marks)
 2. 'Indifference curves are always convex to the origin'.
Do you agree? Justify your answer using appropriate diagrams.
(5 marks)
 3. Using indifference curve and budget constraint, graphically illustrate the substitution effect and income effect that would result from a decrease in price of an inferior good.
(5 marks)
 4. Explain four (4) axioms of ordinal utility approach
(6 marks)
- (Total 20 marks)**

Question No. 03

1. The total cost function of a firm is given by the equation;
$$TC = 800 + Q + 2Q^2$$

If the firm produces 10 units in terms of quantity (Q) calculate;
 - a. Average total cost
 - b. Marginal cost
(4 marks)
 2. Outline the relationship between average and marginal product curves using a diagram.
(5 marks)
 3. Graphically illustrate the conditions associated with a producer optimum.
(5 marks)
 4. Illustrate the three (3) types of returns to scale that could be experienced by a firm in the long run.
(6 marks)
- (Total 20 marks)**

Question No. 04

1. List four (4) distinguishing characteristics of oligopoly market structure.
(4 marks)
2. Distinguish between ‘cartel’ and ‘contestable market’ models of oligopoly.
(4 marks)
3. Monopolistic market structures are characterized by excess capacity and mark up over marginal costs. Discuss using a diagram.
(5 marks)
4. Coca-cola and Pepsi two oligopoly firms have to decide on their promotional strategy. The following payoff table shows their annual payoffs in terms of profits from the decisions they make.

Coca-cola's price

		<i>High</i>		<i>Low</i>	
Pepsi's price	High	10	14	08	09
	Low	09	11	12	12

- a. Identify the likely outcome of this promotional decision problem.
(03 Marks)
- b. Analyse whether the answer to 4 (a) above will differ if Coca-cola becomes the first mover in making the decision.
(Hint: Use a game tree to explain your answer).

(04 Marks)

(Total 20 marks)

Question No. 05

1. 'In a perfect competition; $P = MR = AR$ always'.

Do you agree? Justify your answer.

(4 marks)

2. 'A perfectly competitive firm will earn economic profits only in the long run'.

Comment on this statement using diagrams.

(5 marks)

3. It is often said that essential industries such as water and electricity are subsidized by the government to ensure that the services are available to all at an affordable price.

Comment on this statement using a diagram.

(5 marks)

4. Explain the three (3) types of price discrimination using appropriate diagrams.

(6 marks)

(Total 20 marks)

SECTION C

Answer **only one** question

Question No. 01

‘The pricing strategies of oligopoly firms are often referred to as a prisoner’s dilemma game’.

Discuss by using your own example.

(Total 10 marks)

Question No. 02

‘A rational producer is always said to operate in the stage of diminishing returns’.

Critically evaluate this statement by focusing on the three stages of law of diminishing returns.

(Total 10 marks)