



## Introduction to Economics & Finance

Foundation Examination  
Autumn 2013  
Module B

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

- (i) Which of the following is **NOT** associated with macroeconomics?
  - (a) Study of collective decisions by households or producers.
  - (b) The role of the State Bank in regulating the money supply.
  - (c) The economic behaviour of buyers and sellers in particular markets.
  - (d) Study of issues such as unemployment, inflation, economic growth, etc.
- (ii) Price elasticity of demand depends upon:
  - (a) proportion of income spent on the particular good.
  - (b) income elasticity of demand.
  - (c) substitution elasticity of demand.
  - (d) all of the above.
- (iii) Which of the following is **NOT** a characteristic of monopolistic competition?
  - (a) Existence of many firms
  - (b) Barrier to entry or exit from the market
  - (c) Product differentiation
  - (d) Goods produced are close substitutes of one another
- (iv) Over a long period of time:
  - (a) demand becomes more elastic and supply becomes less elastic.
  - (b) demand becomes less elastic and supply becomes more elastic.
  - (c) both demand and supply becomes more elastic.
  - (d) both demand and supply becomes less elastic.
- (v) If the production possibility curve moves outward to the right, it means that:
  - (a) the economy is capable of producing more goods and services than it could produce previously.
  - (b) the economy is not able to produce goods and services that it could produce previously.
  - (c) it is not possible to produce the optimum combination of goods and services.
  - (d) there is significant decline in population or exhaustion of natural resources.
- (vi) The rate of exchange of the currency of a country will tend to increase, if:
  - (a) the demand for the country's goods and services increases in the foreign markets.
  - (b) the value of the dominant reserve/transaction currency appreciates significantly.
  - (c) the supply of currency of that country in foreign exchange markets increases.
  - (d) citizens of that country increase import of foreign goods and services.

- (vii) According to Keynes, aggregate demand is inherently unstable because:
- (a) a government has limited capability to fine-tune the economy.
  - (b) investment decisions of businessmen are often destabilising.
  - (c) increase in taxes adversely affect investment in new business ventures.
  - (d) measures to control money supply take considerable time to achieve the desired results.
- (viii) Which of the following is **NOT** a determinant factor in the rate of growth of a country's standard of living?
- (a) Lowering of retirement age
  - (b) Capital investment
  - (c) Technological improvements
  - (d) Upgrading of educational standards at the university level
- (ix) Unemployment arising from a long term decline in a particular industry causes an increase in:
- (a) structural unemployment.
  - (b) seasonal unemployment.
  - (c) frictional unemployment.
  - (d) cyclical unemployment.
- (x) Inflation will increase when:
- (a) aggregate demand increases faster than aggregate supply.
  - (b) aggregate supply increases faster than aggregate demand.
  - (c) aggregate demand falls.
  - (d) both b and c.
- (xi) GDP is equal to:
- (a) the market value of all final goods and services produced during the course of the year.
  - (b) the sum of the incomes earned by suppliers of resources in the economy.
  - (c) the sum of value-added at all stages of production.
  - (d) all of the above.
- (xii) Which of the following statement is correct?
- (a) Disposable Income is equal to consumption plus saving.
  - (b) Disposable Income is equal to personal income less personal taxes.
  - (c) Disposable Income is either spent on consumer goods and services or saved.
  - (d) All of the above.
- (xiii) Other things being equal, an increase in the rate of interest leads to:
- (a) an increase in consumer spending.
  - (b) an increase in saving.
  - (c) an increase in business activity.
  - (d) an increase in government spending.
- (xiv) Under the Quantity Theory of Money, changes in price level are:
- (a) inversely related to change in money supply.
  - (b) determined primarily by the Government.
  - (c) directly proportional to changes in money supply.
  - (d) independent of changes in money supply.
- (xv) Which of the following statement is correct?
- (a) A government can help to counter demand-pull inflation by reducing interest rate.
  - (b) A government can help to counter cost-push inflation by linking wage increase to productivity improvement.
  - (c) A government can help to counter cost-push inflation by increasing income tax rate.
  - (d) None of the above.

- Q.2 (a) Explain how the resource allocation choices are made in a market economy and in a planned economy. (04)
- (b) State any **four** disadvantages of a planned economy. (04)
- Q.3 (a) What is 'Price discrimination'? Give **two practical** examples of price discrimination. (03)
- (b) Explain with the help of diagrams how a monopolist finds it profitable to charge discriminating prices when the elasticities of demand in the two markets are different. (09)
- Q.4 (a) Briefly discuss the term 'Returns to scale' and distinguish between the different phases of returns to scale. (04)
- (b) What is the difference between 'Returns to scale' and 'Law of variable proportions'. (02)
- (c) In the context of law of variable proportion, explain with the help of a schedule and a diagram the relationship among total, average and marginal product of labour. (10)
- Q.5 (a) What is an indifference curve? List the properties of an indifference curve. (03)
- (b) Explain the Law of Diminishing Marginal Rate of Substitution with the help of indifference curve analysis. (06)

### Section B

- Q.6 (a) Briefly explain progressive and proportional taxation by giving **one** practical example of each. State any **one** merit and **one** demerit of progressive and proportional taxation. (09)
- (b) What is meant by Direct and Indirect taxes? Briefly discuss the features of a good tax system. (08)
- (c) How does indirect taxation help to promote economic development of a country? (03)
- Q.7 (a) What is 'Multiplier'? Explain the working of the Multiplier with the help of a numerical example. (*for the purpose of working, assume that marginal propensity to consume is equal to 0.6*) (05)
- (b) Briefly state the limitations of Multiplier. (04)
- (c) The difference between increase in income and the increase in consumption represent a leakage from the flow of income stream. These leakages obstruct the growth of national income.
- (i) Discuss the principal leakages in the income stream and their effect on multiplier. (09)
- (ii) What would be the effect on multiplier, marginal propensity to consume, investment and employment if there were no leakages from the flow of income stream? (02)
- Q.8 (a) What is meant by 'Terms of Trade'? Briefly discuss the factors which affect the terms of trade of a country. (09)
- (b) Discuss any **four** advantages of free international trade. Also discuss **four** barriers to free international trade. (11)

(THE END)