Examination Period 3: 2016/17

Module Title: The Economic Environment
Level: Four
Time Allowed: Two Hours

Instructions to students:

- Enter your student number not your name on all answer books.
- **Section A**: Answer all questions. Questions are worth 3 marks each.
- **Section B**: Answer one out of three questions. Questions are worth 35 marks each.
- **Section C**: Answer one out of three questions. Questions are worth 35 marks each.

No. of Pages: 5
No. of Questions: 16
Section A

Answer all Questions.

Questions are worth 3 marks each.

1. The following factors can cause a shift in the demand curve for tea except:
   a. the price of tea
   b. the price of coffee
   c. a change in consumer’s income
   d. a change in consumer’s preference for tea

2. If the income elasticity of demand for a product is equal to -0.5, then an increase in income of 10%:
   a. will lead to a decrease in demand of 5% and the product is a normal good
   b. will lead to an increase in demand of 5% and the product is a normal good
   c. will lead to an increase in demand of 5% and the product is an inferior good
   d. will lead to a decrease in demand of 5% and the product is an inferior good

3. The marginal product is equal to the average product when the average product:
   a. is at its maximum
   b. is at its minimum
   c. is equal to zero
   d. all of the above

4. Strategic behaviour is one of the main features of the oligopoly market. This means that an oligopoly firm:
   a. takes into account its rival when making pricing and output decisions
   b. does not take into account its rival when making pricing and output decisions
   c. considers the existence of barriers to entry before operation
   d. none of the above

5. Which of the following can cause market failure?
   a. presence of monopoly power
   b. positive externalities
   c. public goods
   d. all of the above

Section A continues overleaf
6. In measuring the value of Gross Domestic Product in an economy, the expenditure approach:

a. adds up all the incomes from factors of production  
b. adds up the value added by each firm in the economy  
c. adds up consumption expenditure, investment expenditure, government expenditure and net exports  
d. none of the above

7. The demand for money as an insurance against unforeseen circumstances is the:

a. transaction motive for holding money  
b. precautionary motive for holding money  
c. speculative motive for holding money  
d. all of the above

8. An increase in government expenditure, will increase aggregate demand, which will cause prices to:

a. rise  
b. fall  
c. remain unchanged  
d. none of the above

9. Which of the following does not imply cyclical unemployment?

a. demand-deficient unemployment  
b. unemployment that typically occurs when there is a recession  
c. unemployment caused by insufficient aggregate demand  
d. natural rate of unemployment

10. The vote to leave the EU has resulted in a depreciation of the British Pound. This implies that:

a. the value of the British currency has fallen  
b. British Exports have become cheaper  
c. British Import have become more expensive  
d. all of the above
Section B

Answer one out of three questions.

Questions are worth 35 marks each.

11.  
a. Define the term **income elasticity of demand** and show how this concept can be applied to explain normal and inferior goods.  
   (10 marks)

   b. Define **price elasticity of demand** and explain the main factors that influence the price elasticity of demand of a good.  
   (10 marks)

   c. Explain, using appropriate diagrams, what happens to the total revenue of a grocery store if the price of basic food items such as bread and milk increase.  
   (15 marks)

12.  
a. Discuss the main characteristics of a perfectly competitive market?  
   (15 marks)

   b. Explain (with appropriate diagrams) what happens in the long run to a perfectly competitive firm that is making supernormal profits.  
   (20 marks)

13. 
   a. Monopolies arise due to **barriers to entry**. Explain, (with examples) the concept of “barriers to entry”.  
      (10 marks)

   b. Using appropriate diagrams, show how abnormal profit is made in a monopoly market structure. Will the monopoly continue to make abnormal profit in the long-run?  
      (25 marks)

End of Section B
Section C follows overleaf
Section C

Answer one out of three questions.

Questions are worth 35 marks each.

14.  
   a. How do economists measure unemployment in an economy such as the UK? 
      (10 marks)

   b. Distinguish between frictional and structural unemployment and explain how you would advise the government of a country to deal with these two types of unemployment? 
      (25 marks)

15.  
   a. What is aggregate demand and explain its main components? 
      (10 marks)

   b. The Russian government decides to invest an additional $300 million in preparation for the 2018 World Cup. Explain, using aggregate demand and aggregate supply diagrams, how this additional government expenditure will affect equilibrium price level and equilibrium national output. 
      (25 marks)

16.  
   a. What is Money and how is money supply determined? 
      (10 marks)

   b. Explain the different motives for holding money. 
      (10 marks)

   c. Explain how the interest rates adjust to bring about equilibrium in the money and bonds market. 
      (15 marks)

End of Section C
End of Paper