Examination Period 3: 2018/19

ECN301619N

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<th>Module Title</th>
<th>Advanced Economic Theory</th>
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<tr>
<td>Level</td>
<td>Six</td>
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<td>Time Allowed</td>
<td>Two hours</td>
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Instructions to students:

- Enter your student number **not** your name on all answer books.
- Answer **four** out of **six** questions.
- The use of a calculator **is** permitted.
- Show your workings clearly.

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Answer **four** out of **six** questions.

**Question 1**

a. What is a restrictive monetary policy?  
(5 marks)

b. Critically examine the effectiveness of the use of restrictive monetary policy in controlling inflation.  
(20 marks)

**Total:** 25 marks

**Question 2**

Although unemployment in the UK is at record lows, real wages are hardly increasing. The opposition points out that this is just another factor leading to more inequality, next to the cut in welfare benefits. Using the labour market theory characterised by the price setting and wage setting curve, explain why this is the case. Make sure you explain how to derive both curves and labour market equilibrium.

**Total:** 25 marks

**Question 3**

The notion of growth convergence suggests that poorer countries should eventually "catch up" with wealthier countries in terms of per capita income.

a. Examine the notion of growth convergence by distinguishing between (i) absolute convergence and (ii) conditional convergence.  
(20 marks)

b. Use appropriate graphs to support your answer.  
(5 marks)

**Total:** 25 marks
Question 4

Production is an important key to understand economic growth. A country’s production function \( Y = F(A,K,L) \) is specified in the Cobb-Douglas form as \( Y = AK^\alpha L^\beta \); where \( \alpha + \beta = 1 \).

a. Calculate:
   
i. the elasticity of output with respect to \( K \). (6 marks)
   
ii. the elasticity of output with respect to \( L \). (6 marks)
   
iii. explain your answers in i. and ii. above. (6 marks)

b. Explain one feature of the endogenous growth mode. (7 marks)

Total: 25 marks

Question 5

Lancaster’s demand theory lays emphasis on the characteristics or attributes possessed by commodities or their brands. According to this theory, a consumer buys a commodity not for the sake of buying it but because it possesses certain attributes which yield utility to him.

Make a critical appraisal of the Lancaster’s Demand Theory. Your appraisal should include the strengths and weaknesses of the theory.

Total: 25 marks

Question 6

a. In the game that involves tossing a fair coin, if the head turns up, the player wins £100; if the tail turns up, the player loses £50. A player has the chance to toss the coin only once. Calculate the expected value for a player in this game. (6 marks)

b. Risk can be reduced by diversification. Do you agree? Explain your answer (7 marks)

c. Discuss how the following are applied in insurance:
   
i. risk-pooling (6 marks)
   
ii. risk-sharing (6 marks)

Total: 25 marks

End of Paper