

**THE OPEN UNIVERSITY OF SRI LANKA
COMMONWEALTH EXECUTIVE MASTER OF BUSINESS/PUBLIC
ADMINISTRATION PROGRAMME
FINAL EXAMINATION – 2025 February
AFP9405 – ECONOMIC ENVIRONMENT OF BUSINESS
DURATION: THREE (03) HOURS**



DATE: 16.02.2025

TIME: 9.30 AM – 12.30 PM

Answer any five (05) questions. All questions carry equal marks (20 marks)

Question No.01

A) “Externalities are one important case of market failure” Providing an example each for economic transactions, one that creates indirect costs and one that brings indirect benefits, explain whether you agree with the given statement.
How can these indirect costs and benefits be internalized? Explain using illustrations.

(08 Marks)

B) Using the knowledge in “Concept of Elasticity” answer the following, where possible use illustrations to explain your answer.

- i. Farm output tends to fluctuate over time and farmers have little or no control over their output. How would these fluctuations in output affect the price of agri products and farmer Income?
- ii. How the recessionary and booming periods of an economy affect the business firms that offer services like travel, leisure and dining?
- iii. Rising the cost of ingredients could tempt the firms to raise the price of the given products, how effective is this move?, Could the price of the given item be continuously increased? Taking the pricing strategy used by local biscuit manufacturers in the recent past as an example, explain.

(12 Marks)

Question No. 02

A) i. Providing appropriate illustrations explain whether the business firms that operate in “Hotel and Catering” industry can make above normal profit and achieve economic efficiency in the long run.

(06 Marks)

ii. If they are unable to make above normal profit, are there any other strategies the given firms can employ that enable them to earn above normal profit? Explain with examples.

(04 Marks)

B) i. Using an appropriate model explain why it could be possible for firms operate in non-collusive oligopolistic industries experience price-quantity stability.

(05 Marks)

ii. How relevant are the findings of the said model under unstable macroeconomic environment? Explain with examples.

(05 Marks)

Question No. 03

- (A) i. "Cost-Push inflation is particularly relevant for businesses, consumers and policymakers"
Elaborate, taking post Covid-19 pandemic developments into consideration. **(06 Marks)**
- ii. How could the policy makers use reserve requirement of commercial banks to dampen the inflationary pressure in a domestic economy? How would this affect the commercial banks? Explain. **(04 Marks)**
- (B) i. Why savings and investments are key factors in enhancing living standards of citizens of a country? Explain. **(05 Marks)**
- ii. "Adjusting the rate of interest itself may not necessarily stimulate productive investment in a country, the actual status of its economic environment too, matters." Do you agree? Explain, taking current status of the economy of Sri Lanka as an example. **(05 Marks)**

Question No. 04

- A) "The governments could deliberately run a budget deficit, especially when domestic economies go through recessionary period. However, running a large and persistent budget deficit could affect economies adversely."
- i. Why running a budget deficit could be desirable at a time of economic recession? **(03 Marks)**
- ii. How does a government budget deficit affect the domestic economy? Do the reasons for budget deficit matter? Explain. **(05 Marks)**
- B) Providing illustrations (AD/AS framework), explain how the following changes affect an economy.
- i. There has been a sharp increase in wages and price of other factor inputs like capital and land.
- ii. Reduction in personal income, increase in government expenditure on infrastructure development at a time when the economy operates well below the full employment level of output.
- iii. There has been a noticeable increase in labour productivity, while nominal wages remain constant.
- iv. Drastic decline in domestic exports due to economic recession in major exporting countries, while there has been a surge in domestic imports at a time when the economy operates closer to full employment level of output. **(12 Marks)**

Question No. 05

- A) i. What is meant by "Voluntary Export Restrictions /Restraints (VER)? Explain using an example. **(03 Marks)**
- ii. Using illustrations explain the economic effects of "Tariffs" and "Quotas" **(06 Marks)**
- iii. What are the disadvantages of trade protectionism? Explain. **(03 Marks)**

- B)** “Economic integration that can take a variety of forms reflecting different degree of closeness allows countries to specialize and freely trade across borders, thus increasing their overall wealth” Elaborate with examples. **(08 Marks)**

Question No. 06

- A)** i. “Allowing the domestic currency to depreciate against the currencies of its trading partners is considered to be an effective way of tackling current account deficit.” Explain the validity of the given statement, by taking economy of Sri Lanka as an example. **(06 Marks)**
- ii. What are the problems associated with depreciation/devaluation of domestic currency? Explain. **(05 Marks)**
- iii. If the depreciation/devaluation of domestic currency to bring desired improvements in net exports, what is the condition that should be met? Explain. **(03 Marks)**
- B)** Using illustrations explain how the Sri Lankan Rupee behave against USA Dollar under floating exchange rate mechanism, when;
- i. The rate of interest in Sri Lanka is lower relative to that of USA.
- ii. Imposition of drastic import controls by the government of Sri Lanka **(06 Marks)**

Question No. 07

- A)** i. What is meant by “Economic Development”? Explain. **(02 Marks)**
- ii. What are the major obstacles encountered, especially by developing countries in the world when achieving economic development? Explain, citing economy of Sri Lanka as an example. **(06 Marks)**
- B)** i. Briefly identifying the types of polices employed by the policy makers in trying to manage the economic crisis faced by Sri Lanka, in early 2020’s, explain how these affected the domestic business and investment. **(06 Marks)**
- ii. “Supply – Side” policies too are a vital tool to be used in achieving major macro goals” While identifying what the Supply-Side policies are explain whether you agree with the given statement. **(06 Marks)**

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