

THE OPEN UNIVERSITY OF SRI LANKA
DEPARTMENT OF SOCIAL STUDIES
BA DEGREE IN SOCIAL SCIENCES – LEVEL III
FINAL EXAMINATION – 2018/2019
DSU3531 – PRINCIPLES OF ECONOMICS I



DURATION: THREE (03) HOURS ONLY

Date: 02nd February 2019

Time: 09.30 a.m. – 12.30 p.m.

Answer five (05) questions selecting at least two questions from each part.

Show all your workings clearly.

Part I

1. (a) Explain how the problem of scarcity affects the choices people make and the opportunity costs they face? (10 marks)
- (b) Explain briefly how each economic system answer the three basic economic questions. (10 marks)
2. (a) Define a production possibilities curve and explain how it is used to illustrate the following concepts: opportunity cost, economic efficiency and economic growth. (10 marks)
- (b) Why is the production possibilities curve bowed-out in shape? (10 marks)
3. Below is a schedule of demand and supply for strawberries during one week in the December of 2017

Price (Rs.)	Quantity demanded	Quantity supplied
5	140,000	30,000
8	120,000	50,000
10	80,000	80,000
12	60,000	90,000
14	30,000	110,000

- (a) Construct a demand and supply curve diagram using the data in the table. Ensure all aspects of the graph are labelled appropriately. (04 marks)
- (b) Assuming the market for strawberries is a perfectly competitive market, identify the equilibrium price and quantity traded, and explain what is meant by 'equilibrium' (04 marks)
- (c) Assume that during December there was a period of unseasonably cold weather and the output of strawberries was negatively affected. Draw this scenario on the graph in part a., clearly showing the adjustment to the market conditions. (04 marks)
- (d) Identify the new the equilibrium price and quantity. (2 marks)

- (e) Calculate the price elasticity of demand from Rs. 12.00 to Rs. 14.00. (04 marks)
- (f) For this price change, is demand for strawberries elastic or inelastic? Explain your answer. (02 marks)

4.

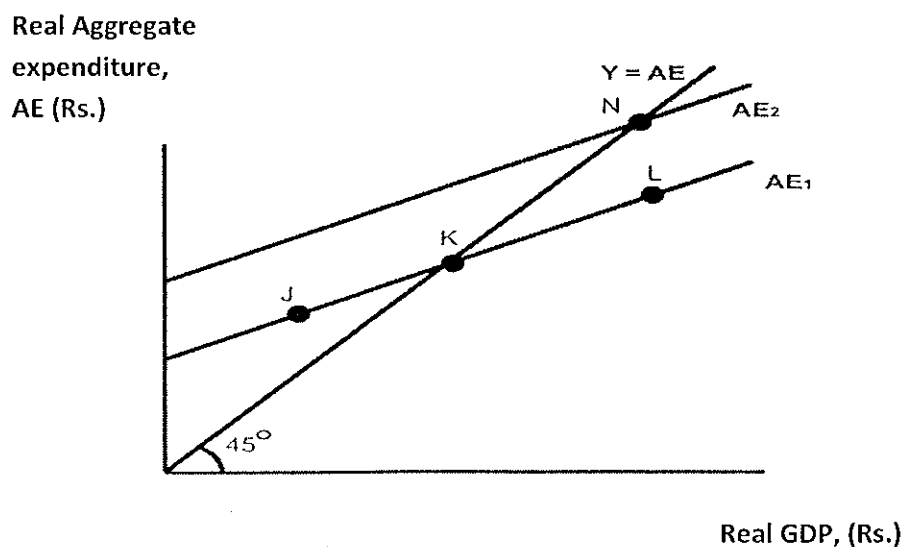
- (a) What is the difference between total utility and marginal utility? (03 marks)
- (b) What is the key assumption about marginal utility? (02 marks)
- (c) Explain the law of diminishing marginal utility with a diagram. (05 marks)
- (d) Explain the conditions that are met when a consumer has found the best affordable combination of goods to buy. Use the indifference curves analysis to answer this question. (10 marks)

Part II

5.

- (a) "The circular flow model illustrates how the economy functions". Explain this statement with a four-sector model. (05 marks)
- (b) Explain the following equation with an example for each concept.
 $GDP = C + I + G + NX$ (05 marks)
- (c) Briefly, explain the injections and leakages in the economy in Sri Lanka. How do they affect national income? (10 marks)

6.



- I. Answer the following questions using the above diagram.
- (a) "Suppose that the level of GDP associated with point N is potential GDP. If the Sri Lankan economy is currently at point K, the economy is in recession" Explain. (03 marks)
- (b) What are the possible causes in shifting Aggregate expenditure, from AE₁ to AE₂? (04 marks)

- II. Consider the consumption function: $C = 600 + 0.6Y_D$ where C represents consumption and Y_D represents disposable income (i.e., $Y - T$). To begin, assume there is no government, investment, or foreign spending. Further, assume taxes are originally set to zero so Y_D and Y are equal.

- (a) What is the Marginal Propensity of Consumption (MPC) in this economy. (02 marks)
- (b) What is the savings function in this economy? (03 marks)

- III. Assume the following in a hypothetical economy

$$C = 200 + 0.6Y_D$$

$$I = 150,$$

$$G = 200,$$

$$X = -250,$$

$$T = 180$$

Where Y_D represents disposable income ($Y - T$).

- (a) What is the value of the multiplier? (02 marks)
- (b) What is the equation for aggregate expenditures in this economy? (06 marks)

7.

- (a) Define inflation (02 marks)
- (b) What problems does inflation bring? (04 marks)
- (c) Explain and draw the three features of Aggregate supply curve. (04marks)
- (d) Show the determination of equilibrium price and real output using AD/AS graph in the short run and in the long run. (10 marks)

8.

- (a) Define how Labour force participation rate is measured. (04 marks)
- (b) The composition of employment in Sri Lanka has changed over the years in line with the structural changes in the economy" Explain. (08 marks)
- (c) What are the factors that led to the increase in female labour force participation rates since the 1980s in Sri Lanka? (08 marks)

9. Write short notes on **four (04)** of the following.

- (a) Economic growth and production possibilities curve
- (b) Taxes and subsidies
- (c) Price ceilings and Price floors
- (d) Income and substitution effects
- (e) Economically active population and economically inactive population
- (f) GDP share of agriculture in Sri Lanka

(04x05=20 marks)

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