

UNIVERSITY OF FORT HARE
ALICE AND EAST LONDON CAMPUS

ECO121F & ECO121L

BACHELOR OF COMMERCE MAIN EXAM

NOV/DEC 2019
MAIN EXAMINATION

Time: 3 Hours

Subject: Introduction to Economics (Micro-Economics)

Marks: 100

This paper consists of 15 pages including the cover page

Internal Examiners

Ms N. Ndlovu

Ms A. Jiza

Internal Moderator

Ms P Makhetha-Kosi

Instructions

Answer ALL questions in section A and section B

Answer only one question in section C, both questions carry equal marks

Answer ALL sections in answer books provided

SECTION A (50marks)

1. As more and more units of a good are consumed by a household, the total utility gained from that good will:
 - A. diminish.
 - B. increase, but by successively smaller amounts.
 - C. rise steeply.
 - D. remain unchanged.

2. Which one of the following statements is correct?
 - ~~A. A consumer is in equilibrium when his or her average utility is at a maximum.~~
 - B. A consumer is in equilibrium when his or her marginal utility is at a maximum.
 - C. A consumer is in equilibrium when his or her weighted marginal utility is at a maximum.
 - D. A consumer is in equilibrium when the marginal utilities per rand spent are equal for all goods purchased.
 - E. It is possible to compare the utility derived by two individual consumers from the consumption of a particular good (eg ice cream).

3. Utility from consuming a good is understood by economists to mean:
 - A. how often we consume the good.
 - B. how much satisfaction or benefit we get from consuming the good.
 - C. how much it costs to buy the good.
 - D. how we best use the good.
 - E. none of the above.

4. Suppose the weighted marginal utility for two goods, x and y, at a position of consumer equilibrium is 70. If the price of good x is R10 and the relevant marginal utility for y is 140, what is the price of good y and the relevant marginal utility for good x?
 - A. The price of y = R140; the marginal utility for x = 70
 - B. The price of y = R10; the marginal utility for x = 700
 - C. The price of y = R70; the marginal utility for x = 70

- D. The price of $y = R2$; the marginal utility for $x = 700$
 - E. The price of $y = R2$; the marginal utility for $x = 140$
5. What does it mean when you experience indifference between two products?
- A. You feel that one product is inferior to the other product.
 - B. You have no preference for any combination of the two products.
 - C. You prefer to have equal amounts of the two products.
 - D. You prefer to have only one of the two products, but it does not matter which one.
6. Why is an indifference curve convex to the origin?
-
- A. Marginal utility of goods decreases as consumption increases.
 - B. Marginal utility of goods increases as consumption increases.
 - C. It represents a higher level of satisfaction at the origin of the curve.
 - D. It represents a lower level of satisfaction at the origin of the curve.
7. The more convex the indifference curve of two goods is:
- A. The more indifferent you are between the two goods
 - B. The more substitutable the goods are
 - C. The more complementary the goods are
 - D. The smaller the slope becomes
8. The closer the indifference curve is to the origin:
- A. The lower the level of satisfaction
 - B. The higher the level of satisfaction
 - C. The lower the level of indifference
 - D. The higher the level of indifference
9. Which one of the following statements about indifference curves is **false**?
- A. They connect points of equal utility to the consumer.
 - B. The indifference curve that lies furthest from the origin indicates the greatest level of consumer satisfaction.
 - C. When two indifference curves cross, the one that ends on the right hand side indicates the greatest level of consumer satisfaction.

D. Indifference curve analysis can be used to derive predictions about the impact on quantity demanded of changes in consumer incomes.

10. The assumption that the indifference curve approach is ordinal:

- A. allows individuals to compare their exact marginal utilities associated with the consumption of a commodity.
- B. means that one can establish how much more satisfaction is derived from a cup of tea than from a cup of hot chocolate.
- C. means that the satisfaction from consuming different products can be ranked or ordered.
- D. allows for two indifference curves to intersect at a common point.

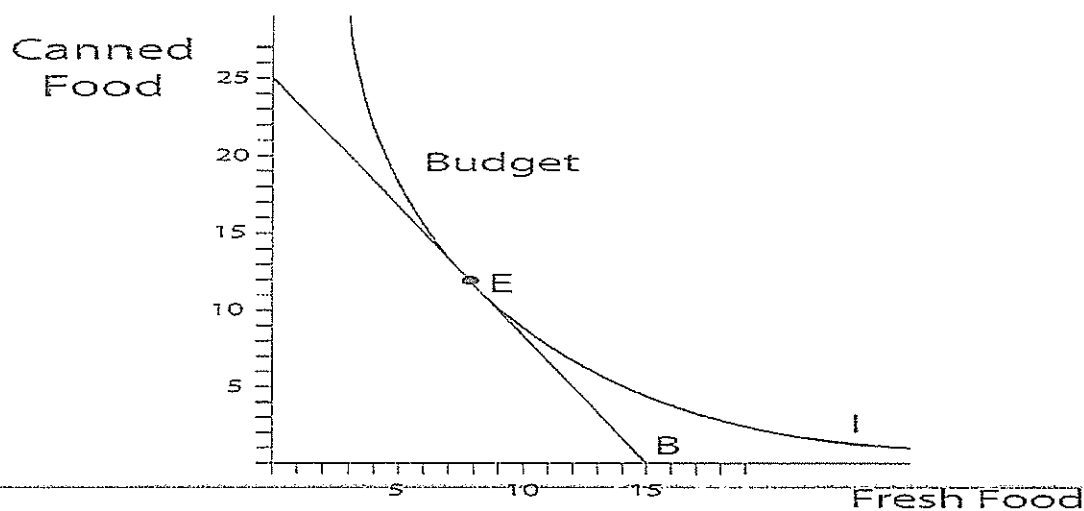
11. Indifference curves are convex to the origin because of:

- A. the transitivity of consumer preferences.
- B. The law of substitution.
- C. the assumption of non-satiation.
- D. the assumption of completeness.
- E. the assumption of consistency.

12. An indifference curve:

- A. indicates how many units of satisfaction the consumption of different quantities of a good provides to the consumer.
- B. indicates the different combinations of two products that will provide the consumer with equal levels of satisfaction.
- C. is based on cardinal utility.
- D. indicates the different combinations of two goods that a consumer can afford to buy.
- E. indicates the different quantities of a good that will be demanded at different prices.

Study the indifference curve (I) below and answer questions 13–14.



13. What does the equilibrium point (E) on the indifference curve represent?
- A. The intersection with another indifference curve
 - B. The point of maximum satisfaction
 - C. What the consumer decides to do *given his income*
 - D. What the consumer can afford
14. How many units of canned food is Tim willing to give up if he wants to increase his consumption of fresh foods from 5 units a week to 10 units a week?
- A. 5
 - B. 9
 - C. 18
 - D. 25
15. Which one of the following is **not** an assumption on which the indifference approach is based?
- A. A consumer can rank all possible combinations of two goods or services in order of preference.
 - B. Consumers act consistently.
 - C. Consumers prefer more to less.
 - D. Consumers assign numerical values (utils) to the utility derived from each good or service.

16. What will happen to the budget line if the price of canned food increases?

- A. It will become steeper
- B. It will become less steep
- C. It will move upwards
- D. It will move downwards

17. In economics, the short run is a period of time:

- A. of one year or less.
- B. in which all inputs are variable.
- C. in which all inputs are fixed.
- D. in which the quantity of at least one input is fixed and the quantities of the other inputs can be varied.
- E. in which all inputs are variable but technology is fixed.

18. When economists talk about 'costs' what do they refer to?

- A. All sacrifices that can be measured in monetary terms
- B. Explicit costs
- C. Opportunity and explicit costs
- D. Implicit costs

19. The law of diminishing returns states that, given a certain capacity:

- a. As more variable factors of production are employed, returns will decrease
- b. As more variable factors of production are employed, returns will decrease at first, reach a minimum, and eventually increase
- c. As more variable factors of production are employed, returns will increase
- d. As more variable factors of production are employed, returns will increase at first, reach a maximum, and eventually decrease

20. Which one of the following statements is correct?

- A. The short run is a time period of one year or less.
- B. The short run is a period of time during which the quantities of all inputs can be varied, but technology is held constant.

- C. The short run is a period of time during which the quantity of at least one input is fixed and the quantities of the other inputs can be varied.
 - D. The long run is a period of time during which the quantities of all factor inputs are fixed.
 - E. The time period separating the short run from the long run is at least 3 months.
21. One of the characteristics of a perfectly competitive market is that:
- A. Suppliers can sell as much as they choose to sell at a specific market price
 - B. Suppliers can control the price of the goods they sell
 - C. Large capital investments are necessary for entry into the market
 - D. Individual suppliers face downward-sloping demand curves
22. Someone who has to accept the price determined by the market is known as a:
- A. Consumer
 - B. Competitor
 - C. Price taker
 - D. Monopoly
23. The market price in a perfectly competitive market:
- A. Is the price where an economic profit will be realised
 - B. Will stay constant regardless of changes in the market supply and/or demand
 - C. Is where no surplus or shortage of goods will be present in the market
 - D. Will depend on the number of competitors in the market
24. What will happen if a supplier in a perfectly competitive market decides to increase the price of his goods?
- A. The supplier's higher price will become the new market price.
 - B. Consumers will still buy the product despite the higher price as the product is unique
 - C. The supplier's demand curve will become downward-sloping

D. No-one would buy from this supplier anymore and would rather choose to buy from a competitor

25. How can an individual supplier in a perfectly competitive market maximise his profit?

- A. By choosing the price to be where supply and demand is equal to each other
- B. By producing at the output level where marginal cost is equal to marginal revenue.
- C. By selling their goods at a price slightly higher than the market price
- D. By selling their goods at a price slightly lower than the market price

26. When a supplier in a perfectly competitive market supplies more than the optimal output, what will the result be?

- A. Marginal revenue will exceed marginal cost
- B. Profits will increase
- C. He overshoots his equilibrium meaning his marginal cost exceeds his marginal revenue hence he incurs a loss per unit beyond optimal output.
- D. Potential profit will be sacrificed

27. Which of the following statements will be true in the scenario where an individual supplier in a perfectly competitive market suffers a loss?

- A. The market price is lower than average total cost
- B. Average total cost is equal to market price
- C. Marginal costs exceed average variable costs
- D. The market price is below average variable costs and above average total cost

28. In a perfectly competitive market, profit will be at its maximum when:

- A. Marginal cost is equal to total cost
- B. Marginal cost is equal to average revenue
- C. Total cost is equal to demand
- D. Marginal cost is equal to average total cost

29. Which of the following is/are features of a perfectly competitive market?

- i. Each produces a slightly differentiated product in order to compete better.
- ii. Buyers are better informed than sellers on special bargains due to easy access to information.
- iii. Established firms have no advantage over new entrants.

- A. i
- B. ii
- C. iii
- D. All of the above.

30. The goal of the firm is to ____.

- A. maximise income
- B. maximise economic profit
- C. break even over the long run
- D. maximise normal profit

31. The market demand curve for a firm in a perfectly competitive market is horizontal.

This indicates that:

- A. its product has perfect substitutes.
- B. the demand for its product is perfectly elastic.
- C. it can sell its full production at market price.
- D. All of the above.

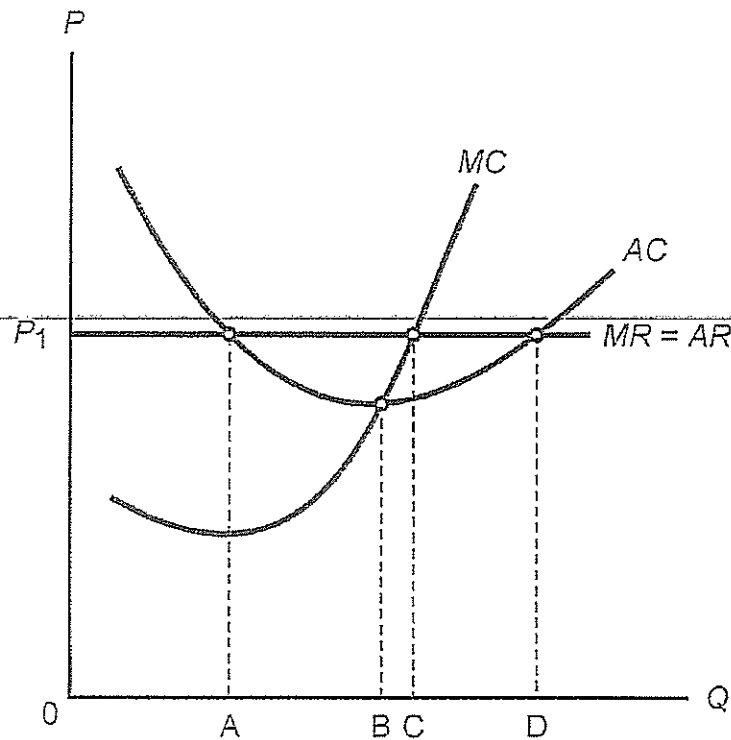
32. Which of the following statements is/are true?

- i. Profit is maximised when average total cost is at a minimum.
- ii. Marginal revenue is the price received for selling one extra item.
- iii. In the short run, the market supply curve sums the quantities supplied by individual firms at certain prices.

- A. i and ii
- B. i and iii

- C. ii and iii
 - D. None of the above combinations.
33. External economies are factors that the firm cannot control that lower the ___ cost of production as the market output increases. In the long run this will result in ___.
- A. firm's; an increase in price
 - B. firm's; a decrease in price
 - C. market's; a decrease in price
 - D. market's; an increase in price
34. Which one of the following statements is correct? The demand for the product of a perfectly competitive firm:
- A. slopes downward from left to right.
 - B. slopes upward from left to right.
 - C. is perfectly elastic.
 - D. is perfectly inelastic.
35. Which one of the following is NOT a requirement for or characteristic of perfect competition?
- A. The good must be homogeneous (standardised).
 - B. All market participants should have perfect knowledge of market conditions.
 - C. Every firm must have the power to set its own price.
 - D. There must be a large number of sellers.
 - E. There should be no government intervention.
36. A small farmer is more likely to operate in a perfectly competitive market than a company like SABMiller because:
- A. a small business is more likely to keep close control on costs than a large firm.
 - B. SABMiller employs many people, whereas perfectly competitive firms are owner-managed.
 - C. the demand for beer is less elastic than the demand for food.
 - D. a small farmer supplies a small share of market supply.
 - E. farming is more risky than beer production.

37. The following graph illustrates the cost and revenue conditions of a firm that operates in a perfectly competitive market. Which one of the following indicates the profit maximising output of the firm?



- A. A
- B. B
- C. C
- D. D

38. A perfectly competitive firm is in equilibrium where marginal cost is equal to marginal revenue because:

- A. this is where the optimum factor combination occurs.
- B. it is not possible to expand production in the short run.
- C. at this point average cost is always at its lowest.
- D. no other quantity yields higher profits.
- E. at this point the final unit produced yields the highest profit (per unit).

39. In what way is monopolistic and perfect competition the same?

- A. Both market structures consist of only one supplier.
- B. In both market structures the suppliers are price takers.
- C. In both market structures suppliers supply identical goods.
- D. In both market structures maximum profit is earned by suppliers where marginal revenue equals marginal costs.

40. Which of the following statements regarding a monopolistic competition market is true?

- A. The market outcome is inefficient.
- B. Suppliers are price takers.
- C. Entry into the market is expensive.
- D. The suppliers' demand curve is inelastic.

41. In what way does a monopolistic competitive market and a monopolistic market differ?

- A. In a monopolistic competitive market, suppliers have a horizontal demand curve, where monopolists have a downward-sloping demand curve.
- B. In a monopolistic competitive market, suppliers have a downward-sloping demand curve, where monopolists have a horizontal demand curve.
- C. In the long run, suppliers in a monopolistic competitive market can earn only normal economic profits, whereas it is possible to earn positive economic profits in a monopolistic market in the long run.
- D. The marginal revenue curve of a supplier in the monopolistic market is downward-sloping and below the demand curve, whereas the marginal revenue curve of a supplier in the monopolistic competitive market is downward-sloping and above the demand curve.

42. In a monopolistic competitive market, the equilibrium price for the product in the short-run:

- A. Is equal to the marginal cost.
- B. Exceeds the marginal cost.
- C. Is equal to the marginal revenue.

D. Is read off the y-axis at the point where marginal revenue equals marginal cost.

43. In the long run, in the monopolistic competitive market:

- A. Economic profits can be earned.
- B. No profits can be earned.
- C. Only normal profits can be earned.
- D. Economic profit, normal profits, or losses can be made.

44. Which of the following is a characteristic of an oligopoly market?

- A. There is only one supplier in the market.
- B. Goods supplied are always differentiated.
- C. The suppliers are all interdependent.
- D. It is ruled by cartels determining the market price.

45. In the kinked demand curve model:

- A. A price higher than the initial price will follow an elastic demand curve.
- B. The flexibility of prices is illustrated.
- C. There will be a vertical part present on the demand curve.
- D. A price lower than the initial price will follow an elastic demand curve.

46. In an oligopolistic market:

- A. Maximum efficiency is reached.
- B. Prices are stable.
- C. Suppliers have an inelastic demand curve.
- D. Profits are not always maximised.

47. One way in which oligopolists can bring about maximum profit maximisation is by:

- A. Formal agreements between suppliers.
- B. Informal cooperation in ways such as price leadership.

- C. Forming cartels.
- D. Increasing prices.

48. In an oligopolistic market, what does the term 'price leader' refer to?
- A. The supplier that sets the price, which its competitors then follow.
 - B. The largest firm in the market that determines the market price.
 - C. The suppliers with the biggest market share and therefore the biggest influence on the price.
 - D. The supplier asking the highest price, and earning the largest revenue.

49. Which one of the following statements about a monopoly is true?

- A. The monopolist has a flat demand curve because of high barriers to entry.
- B. For a monopolistic firm, profit will be maximised where $P = MR$.
- C. In the long run, a monopolist can earn only normal profits.
- D. Price in the long run is not usually equal to minimum average total cost.
- E. A monopolist will always make economic profit in the long run.

50. If a monopoly market were to be replaced with a perfectly competitive market for the same product and with the same cost structure, we would expect:

- A. prices to increase, output to increase and efficiency to increase.
- B. prices to increase, output to decrease and efficiency to decrease.
- C. prices to decrease, output to increase and efficiency to increase.
- D. prices to decrease, output to decrease and efficiency to decrease.
- E. prices to remain unchanged, output to decrease and efficiency to increase.

SECTION B (Answer ALL questions in this section)

1. Anne is a big fashion enthusiast and likes buying shoes and jackets. Suppose that a pair of shoes costs R350 and the number of utils of satisfaction she will gain from the pair of shoes is 15. If she will gain 20 utils of satisfaction when she buys another jacket, what is *the* most that she is willing to pay for the jacket if she wishes to maximise her utility?

2. John Scott has R200 per week available to spend on beer and cigarettes. Beer costs R10 per bottle and cigarettes cost R40 per packet. Suppose John buys 8 bottles of beer and 3 packets of cigarettes and that his marginal utility from beer is then 20 utils and that from cigarettes 35 utils. Is he in equilibrium? If not, should he buy more beer or more cigarettes? Explain. (7)
3. When will the profit made by a supplier in the monopolistic competitive market be maximised in the short run? (5)
4. In a perfectly competitive market, when will the best option for the supplier be to shut-down, rather than to continue doing business? (6)
-
5. Explain the difference between nominal wages and real wages. (2)

SECTION C (Choose only one question)

Question 3

- a) State and explain the 3 different assumptions and four characteristics of an indifference curve. Use graphs where applicable (15)
- b) Use a diagram to explain the relationship between average product and marginal product. (10)

OR

Question 4

- a) What are the main differences between:
- i. Monopoly and perfect competition?
 - ii. Monopoly and monopolistic competition?
 - iii. Monopolistic competition and perfect competition?
 - iv. Oligopoly and perfect competition?
 - v. Monopoly and Oligopoly

(15)

b) Use a diagram to explain the relationship between average product and marginal product. (10)

.....END.....