

**UNIVERSITY OF FORT HARE**

**ALICE AND EAST LONDON CAMPUS**

**ECO111L & ECO111F**

**BACHELOR OF COMMERCE MAIN EXAMINATION**

**JUNE 2016**

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**Time: 3 Hours**

**Subject: Introduction to Economics (Micro-economics)**

**Marks: 100**

**This paper consists of 24 pages including the cover page**

**Internal Examiners**

**Mr D Hompashe**

**Miss B Mhambi**

**Instructions**

- 1. Answer ALL questions in section A and section B.**
- 2. Answer only one question in section C, both questions carry equal marks.**
- 3. Section A is to be answered on the answer grid provided.**
- 4. Answer Section B and Section C in answer books.**
- 5. The multiple choice answer sheets are to be placed inside the examination book on completion of the examination.**

**Question One**

**Choose the one alternative that best completes the statement or answers the question:**

1. Which one of the following is incorrect? Market capitalism is characterised by:
  - A. Strong government intervention.
  - B. Individualism.
  - C. Private freedom.
  - D. Private property.
  - E. Decentralised decision making.
  
2. When the price of rice rises by 10%, the quantity demanded falls by 18%. This is an example of:
  - A. perfectly elastic demand.
  - B. elastic demand.
  - C. unitary elasticity of demand.
  - D. inelastic demand.
  - E. perfectly inelastic demand.
  
3. The essential problem surrounding the field of economics is that there are:
  - A. virtually unlimited resources to satisfy limited wants.
  - B. virtually unlimited resources to satisfy virtually unlimited wants.
  - C. limited resources to satisfy virtually unlimited wants.
  - D. limited resources to satisfy limited wants.
  - E. limited resources to generate wants.

4. Which of the following is essential to the way in which economists think?
- A. Money
  - B. Wealth
  - C. Opportunity cost
  - D. Poverty
  - E. Balance sheet
5. Researchers established that a 6 per cent increase in the price of maize will result in an 8 per cent increase in the quantity of maize supplied. The supply of maize is thus:
- A. Perfectly price elastic.
  - B. Price elastic.
  - C. Unitarily price elastic.
  - D. Price inelastic.
  - E. Perfectly price inelastic.
6. Microeconomics is a branch of economics that studies:
- A. The determination of the gross domestic product.
  - B. The behaviour of individual decision-making units in the economy.
  - C. The impact of inflation in South Africa.
  - D. The effects and consequences of the aggregate behaviour of all decision-making units.
  - E. Both B and D above.
7. Which one of the following is not a determinant of the quantity of a good that is demanded?
- A. The availability of the good.
  - B. The price of the good.
  - C. The income of consumers.
  - D. The prices of substitutes.
  - E. The prices of complements.

8. Read the following statements and then answer the question below.

- I. Perfectly inelastic demand can be illustrated with the means of a completely horizontal line.
- II. Elastic demand occurs when a percentage change in price leads to a greater percentage change in quantity demanded.
- III. The elasticity co-efficient for inelastic demand is less than one.
- IV. Perfectly inelastic demand is completely unrealistic.

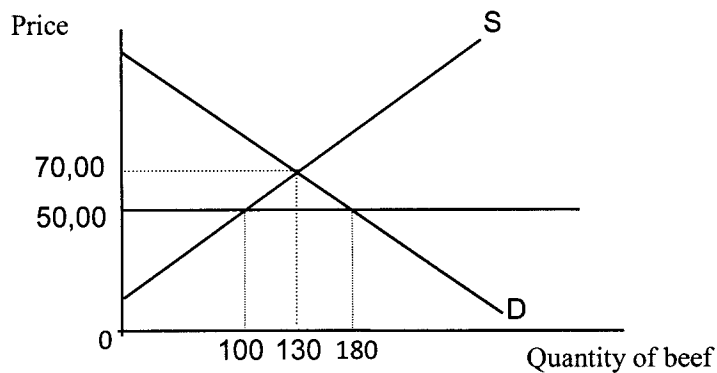
Which of the above statements are true?

- a. I, II and IV.
- b. II, III and IV.
- c. I, III and IV.
- d. III and IV.
- e. II and IV.

9. Which of the following characteristics cannot be associated with a public good?

- A. the benefits of use are widely dispersed in the community.
- B. signs of willingness to pay on the part of consumers are difficult to establish.
- C. it is difficult to exclude non-paying consumers from using the good.
- D. provision by the public sector is usually necessary.
- E. profitable provision by the private sector is relatively easy.

The diagram below shows the market for beef. Use this diagram to answer Questions 10 and 11.



10. The above diagram illustrates a situation whereby:
- A. The government has set a minimum price on beef.
  - B. There is an excess supply of beef.
  - C. There is the potential for black markets to develop.
  - D. The government has set a maximum price on beef.
  - E. Both C and D.
11. If the price of beef is fixed at R50, 00 per kilogram then:
- A. There will be a surplus of 80 kilograms.
  - B. There will be a shortage of 50 kilograms.
  - C. The quantity of beef supplied will fall to zero.
  - D. There will be a shortage of 80 kilograms.
  - E. There will be a surplus of 50 kilograms.

12. Market demand:

- A. shows how much an individual is willing and able to consume at each and every price.
- B. is the horizontal summation of all the individual demand curves in a market.
- C. is the vertical summation of all the individual demand curves in a market.
- D. is a positive slope.
- E. shows how much individuals are willing to supply at each and every price.

13. In a command economy, resource allocation is brought about by

- A. Price signals driven by relative price changes.
- B. The collective preferences of central planners.
- C. The behaviour of self-interested individuals striving to maximise their own well-being.
- D. The principle of consumer sovereignty.
- E. The desire of producers to maximise profits.

14. Which one of the following is correct? The South African economy is a:

- A. Pure market economy.
- B. Pure command economy.
- C. Pure traditional economy.
- D. Mixed economy.
- E. Multilateral economy.

When the price of sausage rolls rises from R5 to R8, the quantity demanded decreases from 200 to 100 sausage rolls per day. Use this information to answer Questions 15 and 16.

15. What is the price elasticity of demand for sausage rolls (using the arc formula)?

- a. (+) 1
- b. (-)  $13/9$
- c. (-)  $9/13$
- d. (+)  $3/5$
- e. (-)  $5/3$

16. How would you classify the demand for sausage rolls, as calculated above?

- A. Price inelastic
- B. Unitary price elastic
- C. Price elastic
- D. Perfectly price elastic
- E. imperfectly price inelastic

17. Opportunity cost is best defined as:

- A. the out-of-pocket money costs incurred when a decision is made.
- B. the value of the best alternative sacrificed when a choice is made.
- C. the value of all the alternatives given up when a choice is made.
- D. the value of time lost when a choice is made.
- E. both b and c above.

18. Which one of the following statements is incorrect?

- A. Money is the most important factor of production. Without money, nothing can be produced.
- B. Natural resources (also called land) are one of the factors of production.
- C. Both the quality and the quantity of factors of production are important.
- D. Capital as a factor of production refers to tangible things that are used to produce other things.
- E. Although the quantity of labour is important, the quality of labour is usually more important.

19. The following statements reflect ways in which an excess supply in the market can be removed. Which one of these statements is incorrect?

- A. Government can purchase the excess and destroy it completely.
- B. Producers themselves can destroy the excess materials.
- C. Government can purchase the excess and export it to foreign countries.
- D. Government can ration the supply using coupons.
- E. Quotas can be introduced by government departments.

20. Which one of the following may result in a decrease in the demand for frozen vegetables?

- A. A rise in consumers' incomes.
- B. An increase in the price of frozen vegetables.
- C. A decrease in the price of freezers.
- D. A decrease in the price of fresh vegetables.
- E. A decrease in the price of frozen vegetables.

21. When an individual's income rises, *ceteris paribus*, his/her demand for half a loaf of bread, an inferior good:

- A. rises.
- B. falls.
- C. remains unchanged.
- D. becomes more positive.
- E. can be affected in different ways – we need additional information to provide an answer.

22. In the South African economy, the problem of “what to produce” is solved primarily by:

- A. the National Planning Commission.
- B. the South African Reserve Bank.
- C. people advertising their wants.
- D. the pattern of consumers' spending.
- E. direction by government.

23. If the income elasticity of demand for a good is  $-0,5$ , then this implies that this good must be a(n)

- A. necessity.
- B. luxury.
- C. inferior good.
- D. substitute.
- E. complement

24. Which one of the following statements is **false**?
- A. The basic economic problem is one of choice.
  - B. Choice is necessary because of limited wants.
  - C. The means available to satisfy wants are limited.
  - D. The wants of human beings are unlimited.
  - E. The opportunity cost of producing a given commodity is the value of the best forgone alternative which could have been produced with the factors of production used in its production.

25. Read the following statements and then answer the question that follows.

- I. An economic system refers to the mechanisms and institutions that resolve the what, how and for whom questions.
- II. Property rights is an important element that is considered in determining the type of economic system on hand.
- III. In traditional economic systems, economic activity is considered highly important.
- IV. Free market economies can also be referred to as socialism.

Which of the above statements are false?

- A. I and II.
- B. II, III and IV.
- C. III and IV.
- D. IV.
- E. All of the above.

26. Privatisation means that:

- A. the private sector sells assets to the government.
- B. the government obtains private assets without compensation.
- C. the government obtains private assets but compensates the owners.
- D. the government sells some of its assets to the private sector.
- E. one private firm sells assets to another private firm, thereby keeping the assets private.

27. Read the following statements and then answer the question that follows.

- i. An item with a wide range of substitutes will most likely have an inelastic demand.
- ii. Products needed for survival are deemed to have a more inelastic demand.
- iii. Products with few substitutions available have an inelastic demand.
- iv. The higher the level of income spent on an item, the greater the level of price elasticity of demand.

Which of the above statements are incorrect?

- A. i and iv.
- B. i, ii and iv.
- C. iii and iv.
- D. Only i.
- E. Only iii.

28. If there is an excess supply of tomatoes on the market, then:

- A. The price of tomatoes will tend to rise.
- B. The government should apply price controls, to prevent an increase in the price of tomatoes.
- C. The price of tomatoes will tend to fall.
- D. The government should set a minimum price to avoid a fall in the price of tomatoes.
- E. The price of tomatoes will remain unchanged.

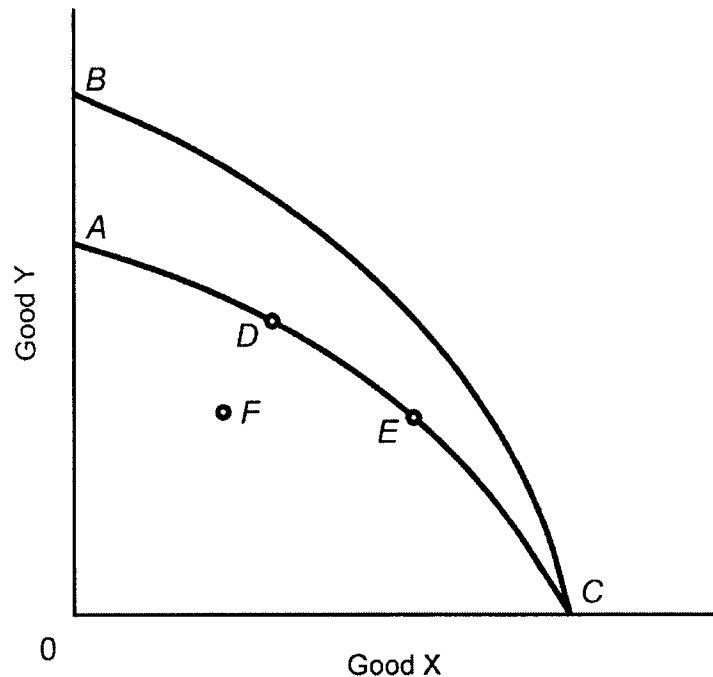
29. A production possibility frontier shows:

- A. the maximum combination of inputs that can be used to produce output in a typical economy.
- B. the maximum revenue that can be generated from the sale of output produced by limited resources in an economy.
- C. the minimum quantities of commodities that can be produced from limited but fully-employed resources in an economy.
- D. the maximum quantities of commodities that can be produced from limited but fully-employed resources in an economy.
- E. the quantities of factors of production available to produce goods and services in an economy.

30. If the cross elasticity of demand between bread rolls and cheese is  $-3,0$ , this implies that these goods are

- A. luxuries.
- B. complements.
- C. necessities.
- D. substitutes.
- E. income inferior goods.

Use the diagram below, which indicates maximum combinations of good X and good Y that can be produced with available resources, to answer questions 31 and 32 below.



31. On production possibility curve AC
- output combinations D and E represent full and efficient use of resources, but A, C and F represent inefficient resource use.
  - output combination D represents the most efficient use of resources.
  - output combinations A, D, E and C all represent full and efficient resource use.
  - output combination A and C represents less efficient resource use than either D or E.
  - the production of goods X and Y require similar factor inputs in similar proportions.
32. The outward shift of the curve from AC to BC could arise from
- a decrease in the level of unemployment
  - technological progress that affects good X production and good Y production equally.
  - an improvement in labour productivity only in the industry producing good X.
  - an improvement in labour productivity only in the industry producing good Y.
  - a reallocation of resources from X production to Y production.

33. Read the following statements and then answer the question below.

- I. Quantity demanded refers to the amount of a good or service that consumers are willing and able to buy.
- II. The law of demand recognises a positive relationship between the price of a product and the quantity demanded of that product.
- III. Market demand refers to the sum of all individual demands for a particular good or service.
- IV. Demand is a summation of events that have already happened, rather than future purchase plans.

Which of the above statements are true?

- A. I and II.
- B. I and III.
- C. I, II and III.
- D. II, III and IV.
- E. IV.

34. Intermediate goods and services can be described as goods and services that are:

- A. Available for immediate consumption by the end user.
- B. Unique and differentiated from other products.
- C. Utilised in the production process as inputs before final consumption.
- D. Unlimited in quantity and have no price attached.
- E. Outputs which are distributed and available for final consumption.

35. An outwards shift of the Production Possibility Frontier (PPF) represents economic growth. Which of these changes can cause such growth?

- A. An increase in the quality of resources available.
- B. Decreases in the amount of scarce resources being utilized.
- C. Improvements in production technology of both goods.
- D. A lower exploitation of resources.
- E. Both A and C.

36. Which one of the following statements is **incorrect**? A minimum price:

- A. is effective only if it is set above the equilibrium price.
- B. below the equilibrium price has no impact on the market.
- C. above the equilibrium price results in a market surplus (excess supply).
- D. below the equilibrium price results in an excess demand (market shortage).
- E. above the equilibrium price requires further measures to deal with the market surplus.

37. For a market to exist, there are a number of requirements. Which of the following does not represent one of these requirements?

- A. The market price must first be determined.
- B. There needs to be a potential buyer and a potential seller.
- C. The agreement has to be guaranteed.
- D. The market has to have a specific location.
- E. The seller must have something to sell.

38. A rise in the price of peanuts from R6 to R10 results in an increase in quantity supplied from 6 000 to 12 000 units. This means that the arc price elasticity of supply for peanuts is:

- A. +1,33.
- B. +0,75.
- C. +1.
- D. +0,5.
- E. +0,75.

39. What happens to the supply of cheese if the prices of various factors of production have suddenly increased?

- A. Supply will increase, shown by a rightwards shift of the supply curve.
- B. Supply will increase, shown by a movement along the supply curve.
- C. Supply will decrease, shown by an upwards movement along the supply curve.
- D. Supply will decrease, shown by a leftwards shift of the supply curve.
- E. The level of supply will remain the same.

40. If there is an increase in the price of corn, a substitute in production for carrots, then:

- A. The supply of carrots will increase.
- B. The demand for carrots will fall.
- C. The supply of carrots will decrease.
- D. There will be a movement along the supply curve for carrots.
- E. None of the above will result.

Use the following information to answer Questions 41 and 42. The demand and supply curves for a small country are represented by the following equations:

$$Q_d = 30 - 2P \quad \text{and} \quad Q_s = 10 + 2P$$

41. The equilibrium price is:

- A. 5
- B. 10
- C. 15
- D. 20
- E. 25

42. The equilibrium quantity is:

- A. 5
- B. 10
- C. 20
- D. 30
- E. 40

43. If government sets a maximum price above the equilibrium price:

- A. a surplus will develop.
- B. a shortage will develop.
- C. excess supply will develop.
- D. excess demand will develop.
- E. the market will be unaffected.

44. The consumer surplus is:

- A. The difference between what consumers pay and the maximum amount that they are willing to pay to obtain the goods in question.
- B. What is left after consumers have bought their monthly groceries.
- C. What consumers have left after all their monthly needs have been satisfied.
- D. The difference between what consumers earn and what they spend.
- E. The positive difference between consumers' income and their expenditure.

45. Which one of the following statements correctly reflects a traditional economy?
- A. Production is determined according to the decisions of a central planning committee.
  - B. The government intervene in certain sectors in order to ensure the fulfilment of individuals' wants.
  - C. Traditional economies mainly pertain to urban areas.
  - D. Economic growth is secondary to cultural values.
  - E. Traditional economies are combinations of both communist and capitalist economic systems.
46. When the price of coke increases from R10 to R15 a bottle, the quantity demanded falls from 1 000 to 800 bottles per week. Using the arc elasticity formula, the price elasticity of demand will be
- A.  $(-) 5/9$ .
  - B.  $(-) 4/9$ .
  - C.  $(+) 9/5$ .
  - D.  $(-) 9/5$ .
  - E.  $(-) 1$ .
47. In the market for diamonds, assuming everything else remains unchanged, the equilibrium price of diamonds will decrease if
- A. there is a shortage of diamonds.
  - B. the price of gold, a complement, decreases.
  - C. the supply of diamonds decreases.
  - D. the price of cubic zirconia's, a substitute, increases.
  - E. there is a technological improvement in mining equipment.

48. Researchers find that a 5 per cent increase in the price of watermelons will result in a 2 per cent increase in the quantity of watermelons supplied. From this we may conclude that the supply of watermelons is:

- A. perfectly price elastic.
- B. price elastic.
- C. unitarily price elastic.
- D. price inelastic.
- E. perfectly price inelastic.

49. Which one of the following statements is **incorrect**?

- A. Demand refers to plans of households, not to actual events.
- B. A change in the price of guavas will result in a change in the quantity of guavas demanded.
- C. The demand for a product depends on the availability of the product.
- D. The market demand is the sum of all the individual demands.
- E. An increase in demand indicates that greater quantities of the good are demanded at the different prices.

50. The producer surplus is:

- A. always greater than the consumer surplus.
- B. the difference between producers' revenue and their cost of production.
- C. the difference between the price that producers receive and the lowest prices at which they are willing to supply the different quantities.
- D. what producers have left after all their expenses have been paid.
- E. simply another term for profit.

**SECTION B: NB Question Two is Compulsory**

**[25 marks]**

**Question Two**

1. Use examples to discuss the concept opportunity cost. [4]
2. Discuss the difference between traditional and command systems. [8]
3. Consider the supply of maize in South Africa. For each of the following scenarios, illustrate and explain how the supply of maize is affected.
  - a. A severe drought impacts maize-producing farmlands. [5]
  - b. Farmers have the choice to produce either maize or sunflowers. For unknown reasons, the price of sunflowers decreases. [5]
4. What are the three central economic questions? [3]

**SECTION C**

**[25 marks]**

**[NB Answer only ONE QUESTION, CHOOSE either Question Three or Question Four]**

**Question Three**

1. Explain, with the aid of a diagram, what will happen if the government fixes a minimum price for maize above the equilibrium price. [7]
2. Using relevant examples where needed, discuss the difference between:
  - a. Intermediate goods and final goods. [4]
  - b. Private goods and public goods. [4]
  - c. Consumer goods and capital goods. [4]
3. Differentiate between income elasticity and cross elasticity of demand. [6]

**OR**

**Question Four**

1. Differentiate between consumer surplus and producer surplus. [4]
2. Use a production possibilities curves to illustrate each of the following (putting goods on the vertical axis and services on the horizontal axis):
  - a. an increase in the potential output of the economy due to a greater availability of factors of production. [3]
  - b. an increase in productivity in the services sector. [3]
  - c. a decrease in productivity in the goods sector. [3]
3. Define price elasticity of demand and briefly discuss the different categories of price elasticity of demand. [12]

## FORMULA SHEET

$$E_p = \frac{(Q_2 - Q_1)/(Q_1 + Q_2)}{(P_2 - P_1)/(P_1 + P_2)}$$

$$E_y = \frac{\% \Delta \text{ in quantity demanded of the product}}{\% \Delta \text{ in consumers income}}$$

$$E_c = \frac{\% \Delta \text{ in quantity demanded of product A}}{\% \Delta \text{ in price of product B}}$$

$$E_s = \frac{\% \Delta \text{ in quantity supplied}}{\% \Delta \text{ in price of the product}}$$

**SECTION A: MULTIPLE CHOICE ANSWER SHEET**

NAME.....STUDENTNO:..... COURSE.....

Indicate your choice by making a **CROSS** in the choice block:

Question number	Options: choose only one				
	USE an 'X' to select your answer				
1	a	b	c	d	e
2	a	b	c	d	e
3	a	b	c	d	e
4	a	b	c	d	e
5	a	b	c	d	e
6	a	b	c	d	e
7	a	b	c	d	e
8	a	b	c	d	e
9	a	b	c	d	e
10	a	b	c	d	e
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12	a	b	c	d	e
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49	a	b	c	d	e
50	a	b	c	d	e