	UNIVERSITY OF RUHUNA **FACULTY OF MANAGEMENT AND FINANCE**	No. of Pages : 04 No. of Questions: 05 Total Marks : 70
1000 LEVEL FIRST SEMESTER END EXAMINATION – AUG/SEP 2022		
BACHELOR OF BUSINESS ADMINISTRATION HONOURS DEGREE		*Three Hours*
BBA 11033 – Microeconomics	Academic year 2021/2022	

Instructions
Answer all questions
Calculators are allowed

Question 01

Mention the correct answer for each MCQ in your answer script

A. Which of the following theories explain the conflict between agent and principal?

i. Transaction Theory
ii. Agency Theory
iii. Motivation theory
iv. Information theory

B. Suppose the cross elasticity of demand for products X and Y is 3.6. What can you conclude from this?

i. X and Y are complements
ii. X and Y are substitutes
iii. X and Y are luxury goods
iv. X and Y are inferior goods

Answer questions C and D based on the below information

In 2020, Amal opened a book shop at Matara. He left his job as the Assistant Librarian at the Matara public library to open this store. During the year the bookstore earned Rs. 1,000,000 from book sales. The costs for the year in the profit and loss statement showed Rs. 630,000. As an assistant librarian, Amal earned an annual salary of Rs. 250,000. Further, he invested Rs. 50,000 to open the bookstore from his personal funds which earned him a guaranteed 10% annual rate of return.

C. What is the total implicit cost of the owner supplied resources?

i. Rs.250,000
ii. Rs.5,000
iii. Rs.255,000
iv. None of the above

D. What is the economic profit of Amal?

i. Rs.115,000
ii. Rs.370,000
iii. Rs.118,000
iv. Rs.255,000

E. Why is there an inverse relationship between price and quantity demanded?

i. Price is an obstacle for consumer purchases
ii. Substitution effect
iii. Income effect
iv. All of the above

F. Suppose an increase in the price of a good from $4 to $6 increases the quantity supplied from 10 units to 14 units. Calculate the price elasticity of supply and the level of elasticity

i. PES = 0.7 and level of elasticity: inelastic
ii. PES = 0.4 and level of elasticity: inelastic
iii. PES = 0.8 and level of elasticity: inelastic
iv. PES = 8 and level of elasticity: elastic

G. Suppose the cross elasticity of demand for products X and Y is -1.2 What can you conclude from this?

i. X and Y are weak complements
ii. X and Y are weak substitutes
iii. X and Y are strong complements
iv. X and Y are strong substitutes

H. A firm that sells luxury wristwatches has found out that the price elasticity of demand is elastic for their products. Which of the following would be a good pricing strategy if this firm wants to maximize its revenue?

i. Have a premium price for watches
ii. Provide discounts to customers
iii. No specific pricing strategy
iv. Increase the price of watches with inflation

I. What are the practical application/s of the concept of price elasticity of demand?

i. Pricing decisions
ii. Deciding the quantity of production
iii. Deciding goods to impose taxes
iv. All of the above

J. Which one of the below statements is a normative economic statement?

i. "The unemployment rate of the country is increasing rapidly"
ii. "The distribution of wealth among citizens is unequal"
iii. "There is a relationship between money printing and inflation"
iv. "The per capita income should be maintained at an average level to avoid poverty"

(1 Mark x 10 = 10 Marks)

Question 02

A. Explain the difference between the short run and long run of production (02 Marks)

B. Draw the short run production curves and mark the three production stages in your diagram (04 Marks)

C. Suppose the total cost (TC) function of a firm is given as $TC = 1000 + 10Q^2$

i. Determine the output level that minimizes average total cost (ATC) (02 Marks)

ii. Verify that at this output level marginal cost = average total cost (MC=ATC)

(02 Marks)

D. A company is facing the below total revenue (TR) function and the total cost (TC) function. This company can add or remove workers as they wish. However, they are unable to change the capacity of their factory during this period. Determine the optimal level of workers this company can employ to maximize profit.

$$TR = 1125L + 10L^2 - \frac{10}{3}L^3$$

$$TC = 1500 + 1095L$$ (05 Marks)

(Total Marks = 15)

Question 03

A. Explain why a firm in a perfectly competitive market is a price taker. (03 Marks)

B. Explain about collusions in an oligopolistic market with examples (03 Marks)

C. Laktex company is operating in an oligopolistic industry. It faces a kinked demand curve for its product as characterized by the below equations. Prices/costs are in rupees.

$$Q_1 = 720 - 7P$$

$$Q_2 = 420 - 4P$$

The total cost equation of the firm is represented by $TC = 1000 + Q + 0.5Q^2$

i. Give the price and output level of Laktex's product (02 Marks)

ii. Based on your answer to part i, calculate the profit of Laktex? (02 Marks)

D. Hide and seek are two companies that own 70% of the market share. Both firms are currently trying to decide whether to give a discount on their product or maintain the price. If both maintain their price, both will earn Rs. 50 million in profits. If both firms give discounts, both will earn Rs. 10 million in profits. If one firm gives a discount while the other firm maintains the price, profit will be Rs. 70 million for the firm giving the discount and Rs. 5 million for the firm maintaining the price. Determine the optimal strategy and dominant strategy of Hide and Seek by using a payoff matrix. Assume that Hide and Seek are not aware of each other's actions in advance. (05 Marks)

(Total Marks = 15)

Question 04

A. Compare and contrast perfect competition and monopolistic competition. (03 Marks)

B. Suppose that the existing firms in a market based on monopolistic competition are earning profits in the short run and this has encouraged new firms to enter into the market.

Briefly explain the market situation and profit levels of existing firms after new firms enter into the market. Graphically illustrate your answer. (05 Marks)

C. Aqua Motors (Pvt) Limited is a company that provides electricity as a monopolist in the market. The market demand curve faced by Aqua Motors (Pvt) Limited and its total cost (TC) function is given below.

$$Q=300-2P$$

$$TC = 500 + 10Q + 2Q^2$$

i. Determine Aqua Motors (Pvt) Limited's inverse demand function, marginal revenue (MR) function and marginal cost (MC) function. (03 Marks)

ii. Compute the level of output and price at which Aqua Motors (Pvt) Limited is maximizing its profits in the market and the amount of profit they have earned.

(04 Marks)

(Total Marks = 15)

Question 05

A. State four (04) properties of an indifference curve. (03 Marks)

B. Briefly explain how a consumer will maximize their utility according to the utility maximizing rule. (04 Marks)

C. Kamal's income is Rs.1,000 which he is expecting to spend on buying bread and bananas. The price of bread is Rs. 100 and a banana is Rs. 50.

i. Draw the budget constraint line by plotting bread on the Y axis and bananas on the X axis.

ii. Mark the below points on your graph (show the calculations related to the points on the answer script)

a. If Kamal spends all of his income on bread how much bread he will buy?

b. If Kamal spends all of his income on bananas how many bananas he will buy?

c. If Kamal buys 10 bananas how many units of bread can he buy?

(02 Marks)

D. Briefly explain any three (03) of the following topics.

I. Relationship between productivity curves and cost curves

II. Marginal Rate of Substitution

III. Economies of Scale

IV. Barriers to Entry

V. Excess Capacity

VI. Productive Efficiency

(02 Marks each = 06 Marks)

(Total Marks = 15)

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