AFRICA UNIVERSITY

(A United Methodist-Related Institution)

"Investing in Africa's Future"

COURSE TITLE: MEC101 ECONOMIC PRICIPLES 1

SEMESTER: ONE

EXAMINATION: FINAL EXAMINATION- NOV 2014

LECTURER: MR T. MASESE

TIME: 3 HOURS

INSTRUCTIONS

Answer **ALL Questions from this paper**

Total possible mark is 60**.**

Start **each** question on a new page in your answer Booklet.

The marks allocated to **each** question are shown at the end of the section.

Show all your workings.

Credit will be awarded for logical, systematic and neat presentations.

Question One

a. Outline the four main economic resources and their payments, what is the difference between labour and entrepreneurship as factors of production? **(6 marks)**
b. What are the assumptions on which perfect competition is based? **(4 marks)**
c. Suppose you a managing director of a firm which produces 3 goods: X, Y and Z. You are told that the respective price elasticities of demand for the goods are: 2.5, 1.0 and 0.5. The firm is experiencing serious cash flow problems and you have to increase total revenue as soon as possible. If you are in a position to set the prices for these goods, what would be your pricing strategy for each product? Explain **(3 marks)**
d. The following production possibility table shows the production possibilities for the City of Mutare

Possibility	Fish (baskets per day)	Potatoes (kilograms per day)
A	O	100
B	1	95
C	2	85
D	3	70
E	4	40
F	5	0

i. What is a production possibility curve? Sketch/draw the above possibilities on a production possibility curve indicating points U inside the curve and G outside the curve **(4 marks)**
ii. Explain how the above production possibility curve explains the concepts of scarcity; opportunity cost, choice, unemployment and efficiency **(5 marks)**
iii. Illustrate graphically the effect on the PPC of an improvement in the technique for producing potatoes without a change in the technique for producing fish **(2 marks)**
iv. What is the opportunity cost of producing the 2^{nd} basket of fish? **(1 mark)**
v. List the 4 main assumptions made when drawing production possibility frontiers **(4 marks)**

Question Two

a. Suppose you are the owner of an ice-cream shop and you have determined that the price elasticity of demand for ice-cream in your particular market is 1.8. Would you sell the ice-cream for $5 or $4.50 per litre? Explain. **(2marks)**
b. Explain, with the aid of a diagram, explain how each of the following would affect the market for coffee.
   i. A severe frost affects most the coffee crop **(2 marks)**
   ii. Coffee is shown to cause cancer after laboratory tests on mice **(2 marks)**
   iii. The price of tea declines sharply **(2 marks)**
   iv. Coffee prices are expected to rise sharply in the next two months **(2 marks)**
   v. Workers in the coffee industry form a trade union and succeed with claims for higher wages. **(2 marks)**
c. The demand and supply for tomatoes at Sakubva Market on a given day is outlined in the following table.

Price of tomatoes per kg	**Quantity Demanded (kgs)**	**Quantity Supplied (kgs)**	**Excess supply or demand**	**Pressure on price**
1	360	0	Excess demand of 360	Upward
2	320	50	?	?
3	280	100	?	?
4	240	150	?	?
5	200	200	?	?
6	160	250	?	?
7	120	300	?	?
8	80	350	Excess supply of 270	Downward

i. Copy and complete the above table in your answer booklet **(3 marks)**
ii. Sketch the above data on a demand/supply graph clearly indicating the market clearing price and quantity, the consumer surplus and the producer surplus **(5 marks)**
iii. Define the price elasticity of demand and explain any four factors that would influence the price elasticity of demand for a product. Calculate the price elasticity of demand for tomatoes for a price change from $3 to $4. Interpret the elasticity coefficient which you have calculated. **(7 marks)**

iv. What is the effect of government policy setting up a price ceiling at \$3? A price floor at \$7? **(2 marks)**

v. Outline factors that may influence the supply and demand for tomatoes at Sakubva Market **(7 marks)**

vi. Calculate the amount of producer surplus for the above market **(2 marks)**

Question Three

a. Briefly explain the following concepts: **(5 marks)**

   i. Isocost (ii) Isoquant (iii) Economies of scope (iv) Economies of scale (iv) Implicit costs

b. Complete the following table and sketch the graphs for the following costs **(10 marks)**

Units of Output	**TFC**	**TVC**	**TC**	**AFC**	**AVC**	**ATC**	**MC**
0			30				
1							30
2						35.5	
3		79					
4							
5			100				
6							
7							20
8		130					
9							
10						23.1	

c. Briefly explain any 4 sources of economies of scale and 2 sources of diseconomies of scale **(6 marks)**

d. With the aid of graphs draw and explain the graphs for the following

   i. Long run equilibrium for a firm in perfectly competitive **industry (4 marks)**

   ii. A monopolist making abnormal profits **(4 marks)**