

BACHELOR OF FINANCIAL SERVICES
BFS 1104: INTRODUCTION TO MICROECONOMICS
END OF FIRST SEMESTER EXAMINATION

Date: Wednesday, 5th August, 2020

Time: 3 Hours

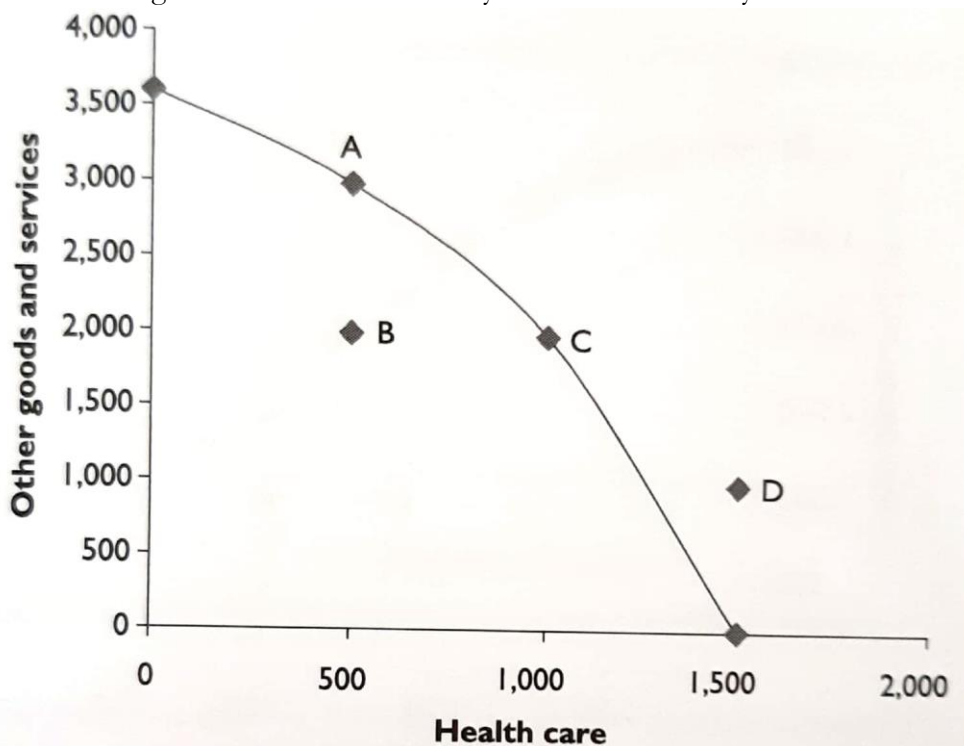
Instructions:

Answer FIVE questions

Answer question 1 and any other four questions

Question 1 (15 Marks)

- a) The following is a Production Possibility Frontier for country X.



Explain which point represents technical efficiency and why?
Explain which point represents technical inefficiency and why?
Explain which point is unattainable and why?

(3 marks)

b) The concepts of Scarcity, Choice and opportunity costs are central to economics. Assuming that you are paying school fees for yourself, discuss how these concepts apply to your decision to enroll for the BFS degree at Strathmore University.

(7 marks)

c) One of the principles of economics is that of trade-offs. Giving an appropriate example, discuss the equity vs efficiency trade-off in an economy

(5 marks)

Question 2 (10 Marks)

a) Giving appropriate examples, define economies and diseconomies of scale and why they might arise?

(3 marks)

b) Using appropriate examples in production, discuss the law of diminishing returns

(2 marks)

c) Discuss the reasons why firms grow in size and outline the ways in which firms can grow

(10 marks)

Question 3 (15 Marks)

a) Why does a demand curve for a normal good have a negative slope?

(1 marks)

b) Using the law of demand, distinguish between a normal good, a Giffen good and a Veblen good

(3 marks)

c) Assuming good beef is a normal good, what would be the effects of the following occurrences on the demand for and prices of beef?

Cause	Effect
A countrywide drought	
A fall in the price of pork	
An increase in national income	
The onset of “mad cow” disease	
A rise in the price of cow feeds	
An expose revealing the use of excessive chemicals in preservation of beef	

(6 marks)

- d) Describe the principle of the invisible hand and its merits and demerits in the allocation of resources

(5 marks)

Question 4 (15 Marks)

- a) Discuss what is meant by the following concepts:
- i. Utility
 - ii. Marginal utility
 - iii. The hypothesis of diminishing marginal utility

(6 marks)

- b) Distinguish between the Cardinalist and Ordinalist approach to utility giving appropriate examples

(5 marks)

- c) In an indifference map why are higher indifference curves preferred?

(2 mark)

- d) Discuss why indifference curves slope downwards from left to right

(2 marks)

Question 5 (15 Marks)

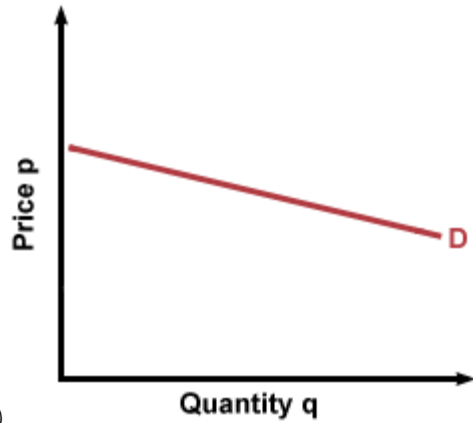
- a) Why is there a positive relationship between quantity supplied and price?

(2 marks)

- b) Suppose the price elasticity of the supply of good X is 1.5. What does this value mean for the relationship between the quantity of X supplied and price?

(2 marks)

- c) Given the following demand curves, which one is price elastic or price inelastic? Justify your answer by giving reasons.



i)



ii)

(6 marks)

d) Consider the market for SUV cars. How will the following events affect the demand and supply of SUV cars.

- People decide to have more children
- A strike by steelworkers raising steel prices
- Engineers develop new automated machinery for the production of SUV cars
- The price of sedan cars (substitutes) rises
- A stock market crash lowers people's wealth

(5 marks)

Question 6 (15 Marks)

- a) Assume that the market for pizza is at equilibrium. Explain what happens to this equilibrium if the price of tomatoes (an ingredient in making pizza) rises?

(2 marks)

- b) The following are the demand and supply functions for good X

$$Q_D = 1000 - 100p$$

$$Q_S = -125 + 125p$$

Calculate the equilibrium price and quantity

(5 marks)

- c) Consider the following events: Scientists reveal that eating oranges decreases the risk of diabetes. At the same time, farmers use a new fertilizer that makes orange trees produce more oranges. Explain the effect of these events on the equilibrium price and quantity of oranges.

(8 marks)

Question 7 (15 Marks)

- a) Firms in a perfectly competitive market are “price takers”. Explain

(4 marks)

- b) Monopolies use price discrimination as a means of maximizing profits.

- i. What is meant by price discrimination? (give an appropriate example)
- ii. What can cause price discrimination to fail?

(3 marks)

- c) “Monopolistic competition provides a wide variety of products for consumers at the cost of some resource misallocation.” Discuss

(4 marks)

- d) The following represents the cost and revenue schedule of a firm

Quantity	Total revenue	Total cost
5	500	350
10	900	550
15	1200	675
20	1400	800
25	1500	1125
30	1500	1800
35	1400	2800

Calculate the following:

- i. Average Revenue (AR)
- ii. Marginal Revenue (MR)
- iii. Average Total Costs (ATC)
- iv. Marginal Costs (MC)

(4 marks)

Question 8 (15 Marks)

- a) “Budget cuts in the education sector can be criticized because education is a public good.”
“Increases in tuition fees can be justified because education is a private good.” Discuss these two statements

(5 marks)

- b) Discuss the role of the public sector in improving equity and equality

(5 marks)

- c) Discuss the effects of setting up a factory which discharges untreated waste into a river taking into account both positive and negative externalities

(5 marks)