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Addis Ababa University
College of Business and Economics
Department of Economics
Introduction to Economics Mid-term Exam (25%)
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Instructions:

- ✓ **Cheating is strictly forbidden**
- ✓ **Switch off your cell phone**
- ✓ **Time allowed: 1:00 hour**

Part I: Choose the best answer from the given alternatives (1.5 points each)

1. Which of the following statement is false concerning the subject matter of economics, currently?
   A. It studies about scarce resources
   B. It gives concerns for efficient allocation of resources
   C. It studies how to save and grow rich at the expense of reducing consumption
   D. It studies how to satisfy unlimited human wants up to the possible degree from scarce resources
   E. None of the above
2. Identify the ***wrong*** statement regarding the method of analysis in economics.
   A. Normative economics deals with analysis of facts, and any disagreement in it is resolved through voting mechanism
   B. Positive economics is a pure science, and it tries to describe the world as it is
   C. Inductive method of analysis derives a general theory by using specific independent facts
   D. Deductive method of analysis derives specific correct statement from general statement
   E. None of the above
3. Which of the following statement is correct about scarcity?
   A. It is a short run and specific phenomena
   B. It arises if the amount available is less than the amount people wish to have at prevailing price
   C. It arises because of the rapid increase in population growth relative to the fixed economic resources
   D. It refers to the finite availability of resources used for producing goods and services in relation to unlimited human wants
   E. All of the above except A
4. Which of the following statement is true about the concept of production possibility curve (PPC)?
   A. Any movement along the PPC curve shows a change in resource quality and quantity
   B. The downward sloping nature of the PPC curve indicates trade off in production between two goods (say X and Y)

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C. The concavity of PPC curve indicates that the opportunity cost per unit of producing additional output diminishes.

D. Points on the PPF curve indicates that the economy has efficiently utilized its resources so that it can have unlimited amount of output

E. All of the above

5. Which of the following statement is ***wrong*** about the economic activities of economic agents in closed economy setting?

A. Government collects tax from households and firms

B. Firms produce goods and services

C. Government provides public goods

D. Households supply goods and services to the goods and service markets

E. None

6. Which of the following factor may not be regarded as determinant of demand?

A. Change in the taste of the consumers B. Change in the price of inputs

C. Change in the income of the consumers D. Increase in number of buyers in the market

7. Michael's income has just risen from $940 per week to $1,060 per week. As a result, he decides to increase his demand for tomato from 12 units to 14 units per week. The income elasticity of Michel's demand for tomato is

A) 1.00 B) 0.90 C) 1.30 D) 0.75 E) 1.93

8. Identify the correct statement from the following alternatives.

A. Basic necessity goods have higher price elasticity than luxury goods

B. Cross-elasticity of demand for complementary goods is positive

C. Price elasticity of demand is more elastic for goods which have more substitutes

D. The larger the proportion of income spent on a good, the lesser price elasticity will be

E. All of the above

9. When both demand and supply decline simultaneously

A. Price definitely decreases, but quantity increases if the fall in demand is lower than the fall in supply

B. Price definitely decreases, but quantity increases if the fall in demand is higher than the fall in supply

C. Quantity definitely decreases, but price increases if the fall in demand is more than the fall in supply

D. Quantity definitely decreases, but price increases if the fall in supply is more than the fall in demand

E. None of the above

10. Given market demand $Q_d = 50 - P$, and market supply $P = Q_s + 5$. Where, P denotes price. Then the market equilibrium price and quantity, respectively, are

A) 27.5 and 23.5 B) 27.5 and 10.5 C) 27.5 and 22.5 D) 29.5 and 21.5 E) 22.5 and 27.5

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Part II: Workout

1. Consider a simple economy producing two goods: computer and Oil. The following table gives several points on this economy's production possibility frontier.

computers (1000's/year)	Oil (1000's of gallons/year)
0	70
1	60
2	40
3	0

A) Graph this economy's production possibility frontier (1 point)

B) Why is the production possibility frontier downward sloping? Be sure to explain the economic intuition behind it (1 point)

C) Why is the production possibility frontier concave? Be sure to explain the economic intuition behind it. (1 point)

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D) Suppose the economy is currently producing 2000 computers and 40,000 gallons of oil. What is the opportunity cost of producing additional 30,000 gallons of oil? (1 point)

E) The introduction of new oil refining technology allows oil producer firms to get twice as much Oil daily than before the introduction of the new technology. In terms of this production possibility frontier, this means that this economy can now produce twice as much Oil at each level of computer output. With the economy currently producing 3,000 computers, John claims that the development of new technology allows the economy to produce more Oil and more Computers. Do you agree? Explain carefully, using an appropriate diagram to illustrate your answer. (1 point)

2. Assume that good X and good Y are related goods and the demand functrion of good X is given as: $Q_x = 1691 - P_x + 6P_y - 6M$. Suppose $P_x = 0.1$ birr, $P_y = 0.3$ birr, and M (income) = 10 birr. Compute:

A) Price elasticity of demand for good X. (1 point)

B) Income elasticity of demand for good X and explain nature of the good. (2 points)

C) Cross-elasticity of demand ($\varepsilon_{x,y}$). Are the goods substitute or complements? (2 points)

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