



**ASSOCIATION OF ACCOUNTING TECHNICIANS
OF SRI LANKA**

curriculum 2020

PILOT PAPER

Level I

103 - ECONOMICS (ECN)

A publication of the Education and Training Division

Association of Accounting Technicians of Sri Lanka

103 - Economics [ECN]

Instructions to Candidates (Please Read Carefully)

Time Allowed:

Writing: 03 hours

Structure of Question Paper:

- This paper consists of three Sections: Section A, Section B and Section C.
- All the questions of Section A, Section B and Section C are compulsory.

Marks:

- Allocation of marks for each section:

Section	Marks
Section A	40
Section B	40
Section C	20
Total	<u>100</u>

- Marks for each question are shown with the question.
- The pass mark for this paper is 50%.

Answers:

- All answers should be written in the booklet provided, answers written on the question paper will not be considered for marking.
- Begin your answer of each question on a new page.
- All workings should be clearly shown.
- Do not write on the Margins.

Answer Booklets:

- Instructions are shown on the front cover of each answer booklet.

Calculators:

- Candidates may use any calculator except those with the facility for symbolic algebra and differentiation. No programmable calculators are allowed.

Attached:

- Action verb checklist – Each question will begin with an action verb (excluding OTQ's). Students should answer the questions based on the definition of the verb given in the checklist.

Objective Test Question (OTQs)

SECTION A

Twenty (20) Compulsory Questions

(Total 40 marks)

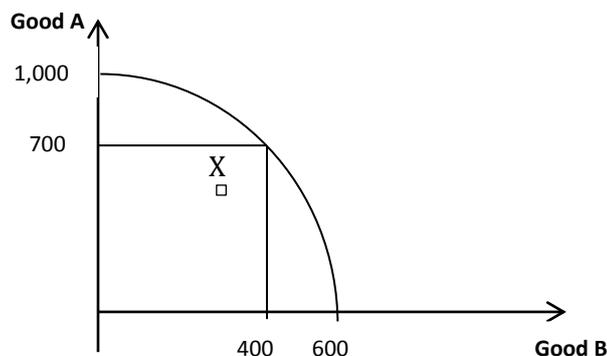
Question 01

Select the most correct answer for question No. 1.1 to 1.10.

1.1 Select from the following the sentence which describes scarcity of resources:

- (1) It exists when demand and supply are in the market.
- (2) It exists only in developing countries.
- (3) It exists when availability of resources is insufficient to fulfill human needs and wants.
- (4) It exists when resources are not allocated properly.

1.2 The diagram below shows production possibility frontier for an economy.



According to the above diagram, point X shows:

- (1) Full employment.
 - (2) Under Employment.
 - (2) Economic Recession.
 - (4) Economic Growth.
- 1.3 The law of diminishing marginal utility states:
- (1) When more and more units of a good are consumed the satisfaction obtained from each additional unit will fall.
 - (2) When more and more goods are consumed total satisfaction diminishes.
 - (3) When more and more goods are produced the price will fall.
 - (4) When more and more goods are consumed, total satisfaction increases.

1.4 Market demand and supply curves for a particular product in a competitive market are given by the following equations:

$$Q_D = 150 - 10P \quad Q_S = -50 + 10P$$

Price elasticity of demand at the market equilibrium is:

- (1) -1.0 (2) -0.8 (3) -1.8 (4) -2.0

1.5 Which one of the following reasons affects to shift the demand curve of a commodity to the left?

- (1) Decrease in price of that commodity. (2) Increase in price of that commodity.
(3) Increase in consumer income. (4) Decrease in consumer income.

1.6 You are given following national income account information for a particular economy:

	Rs. (Million)
Private Consumption	24,000
Gross domestic capital formation	36,000
Government's consumption	14,000
Changes in inventories	2,500
Net tax on products	5,000
Net exports	-4,000

Gross domestic expenditure (Rs.million) at market price of this economy is:

- (1) 70,000. (2) 74,000. (3) 79,000. (4) 76,500.

1.7 The aggregate of narrow money supply and time and savings deposits held by the public at commercial bank is known as :

- (1) Monetary Base (2) Broad Money Multiplier.
(3) Consolidated Broad Money Supply. (4) Broad Money Supply.

1.8 You are given the following information:

Country	Garments per labor hour	Tea per labour hour
Sri Lanka	8	20
Indonesia	10	15

Based on the above, select the correct statement from the following:

- (1) Sri Lanka has comparative advantage in production of tea.
- (2) Both Sri Lanka and Indonesia have comparative advantage in production of garment.
- (3) Sri Lanka has an absolute advantage in production of garments.
- (4) Indonesia has an absolute advantage in production of tea.

1.9 Which one of the following is included in the financial account of a country's Balance of Payment account:

- (1) Interest payment on foreign loans.
- (2) Interest earned on investment.
- (3) Trade in goods.
- (4) Direct foreign investment.

1.10 What is the goal of sustainable development agreed by all nations as a part of the 2030 agenda for sustainable development?

- (1) Zero hunger.
- (2) No poverty.
- (3) Gender equality.
- (4) All of the above.

Select the correct word/words from those given within brackets to fill in the blanks of question No. 1.11 to 1.12:

1.11 Economic as a social science studies (*individual behavior/ economic behavior*) of the people and economic problems of the society.

1.12 If the cross price of elasticity of demand for two goods is positive, the goods are (*complements / substitutes*).

State whether each of the following statements in question No. 1.13 to 1.14 is True or False:

- 1.13 Economic cost consists of both direct and indirect costs of production.
- 1.14 Marginal Cost (MC) curve intersect the Average Cost (AC) curve at the maximum point of the AC curve.

Write the correct answer for question No 1.15 to 1.20:

- 1.15 State four (04) assumption of the production possibilities curve.
- 1.16 List four (04) characteristics of the market economic system.
- 1.17 Briefly explain two (02) reasons for negative relationship between price and quantity demanded.
- 1.18 State two (02) determinants of price elasticity of demand.
- 1.19 Briefly explain the difference between consumer surplus and producer surplus.
- 1.20 State two (02) reasons for shifting the supply curve of a commodity to the right.

(02 marks each - 40 marks)

End of Section A

Four (04) Compulsory Questions

SECTION B

Total 40 marks

Question 02

- (a) (i) **Explain** economic resources of an economy? (02 marks)
- (ii) **Identify** the type of economic system in Sri Lanka and explain reasons for your identification. (03 marks)
- (b) The demand and supply equations of commodity X are given below:
- $$Q_D = 300 - 5p \qquad Q_S = -50 + 5p$$
- Calculate** the market equilibrium price and quantity. (03 marks)
- (c) Suppose that government decided to impose a minimum price of Rs. 40 for commodity X. **Explain** how much of commodity is supplied by producer as a result of minimum price to the market now. (02 marks)
- (Total 10 marks)**

Question 03

- (a) **Explain** the behavior of short run production process (03 marks)
- (b) **Explain** the long run equilibrium of a firm under perfect competition using a graph. (04 marks)
- (c) **State** three (03) differences between a perfectly competitive market and a monopoly market. (03 marks)
- (Total 10 marks)**

Question 04

- (a) **Explain** differences between transaction demand for money and speculative demand for money. (04 marks)
- (b) “Money plays a very important role in a market”
Explain three (03) reasons for validity of this statement. (03 marks)
- (c) **Explain** the difference between demand pull inflation and cost push inflation. (03 marks)
- (Total 10 marks)**

Question 05

- (a) (i) **Explain** what is meant by the business cycle. (02 marks)
- (ii) **Explain** two (02) stages of business cycle. (02 marks)
- (b) **Explain** the difference between absolute advantage and comparative advantage. (02 marks)
- (c) **Explain** consequences of devaluation of the Sri Lankan Rupee against US dollar. (04 marks)
- (Total 10 marks)**

End of Section B

A Compulsory question**SECTION C**(Total 20 marks)

Question 06

- (a) (i) **Explain** what is meant by market failure. (01 mark)
- (ii) **State** three (03) reasons for market failure. (03 marks)
- (b) **Explain** four (04) macro-economic objectives of a country. (04 marks)
- (c) You have given the following hypothetical data relating to national accounts of an economy for a period of one year:

Item	Value (Rs. million)
Compensation of employees	4,500
Gross Operating surplus	8,200
Consumption of fixed capital	700
Other tax less subsidies on production	100
Net tax on products	1,200
Net primary income from the rest of the world	-800

Calculate the following:

- (i) Gross Value Added (GVA) - at basic price (02 marks)
- (ii) Gross Domestic Product (GDP) - at market price (02 marks)
- (iii) Gross National Income (GNI) (02 marks)
- (d) **Explain** the relationship between liquidity and profitability of commercial banks. (03 marks)
- (e) **Identify** three (03) new global economy trends. (03 marks)
- (Total 20 marks)

End of Section C

Action Verbs Check List

Analysis (4)	Draws Connections Among Ideas and Solve Problems	Analyze	Examine in details to find the solution or outcome
		Differentiate	Constitute a difference that distinguishes something
		Discuss	Examine in detail by arguments
		Compare	Examine to discover similarities
		Contrast	Examine to show differences
		Outline	Make a summary of significant features
		Communicate	Share or exchange information
Application (3)	Uses and Adapts Knowledge in New Situations	Apply	Put to practical use
		Calculate	Ascertain or reckon with mathematical computation
		Demonstrate	Prove or exhibit with examples
		Prepare	Make or get ready for particular purpose
		Solve	Find solutions through calculations and/or explanation
		Assess	Determine the value, nature, ability or quality
		Graph	Represent by graphs
Comprehension (2)	Explains Ideas and Information	Reconcile	Make consistent/compatible with another
		Define	Give the exact nature, scope or meaning
		Explain	Make a clear description in detail using relevant facts
		Describe	Write and communicate the key features
		Interpret	Translate in to understandable or familiar terms
Knowledge (1)	Recalls Facts and Basic Concepts	Recognize	Show validity or otherwise using knowledge or contextual experience
		List	Write the connected items
		Identify	Recognize, establish or select after consideration
		State	Express details definitely or clearly
		Relate	Establish logical or causal connections
Draw	Produce a picture or diagram		
Level of competency	Description	Action Verbs	Verb Definitions



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CURRICULUM 2020

SUGGESTED ANSWERS

Level I

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Answers to Question No 1

1.1	(3)	1.6	(2)	1.11	Economic behavior
1.2	(2)	1.7	(4)	1.12	Substitutes
1.3	(1)	1.8	(1)	1.13	True
1.4	(4)	1.9	(4)	1.14	False
1.5	(4)	1.10	(4)		

- 1.15 - Full employment of resources.
- The best available technology is used and it remains constant.
- Only two types of goods are produced.
- It is prepared for a given period of time.
- 1.16 - All the resources are directly or indirectly owned by private sector.
- Consumers have the sovereignty (freedom).
- Producers have sovereignty (freedom).
- Limited role for the government.
- Operations of price mechanism.
- Private sector is motivated by profits.
- Prices of commodities are determined through the demand and supply market forces.
- 1.17 (1) Income Effect:
When the prices of a product changed, the real income (the purchasing power) of the consumers is changed. Therefore, the number of units that can be purchased from his money income will be changed. For example, when a commodity's price falls, the purchasing power of an individual increases. It allows to purchase more number of units. This is known as income effect.

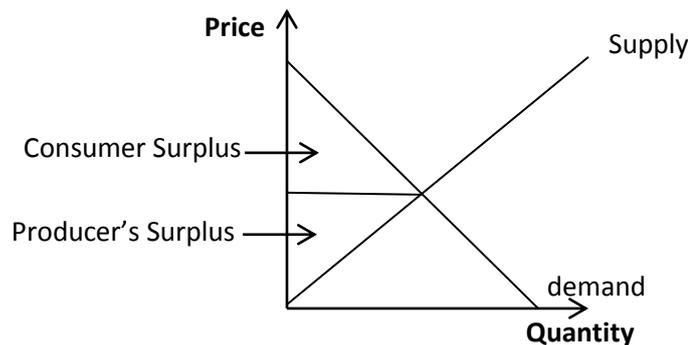
(2) Substitution Effect:

When a commodity's price falls, it is cheaper in the market with related to the other substitute products. Thus, an individual normally purchases more of this good than substitute goods. For example, when price of tea falls and the price of coffee is unchanged, more tea and less coffee will be purchased. This is called as substitution effect.

1.18

- Availability of close substitute.
- Nature of the goods.
- Share of consumer's budget.
- Passage of time.
- Habit forming goods.

1.19 Consumer surplus is the difference between the total amount that consumers are willing and able to pay for a good or service and the total amount that they actually pay. Producer surplus is the difference between what producers are willing and able to supply a good and the price they actually receive.



- 1.20
- Decrease in the price of related goods.
 - Decrease in the prices of inputs
 - Development technology.
 - Cut off government taxes and supply of subsidies.
 - Expectation that the price will reduce in the future

(02 mark each - 40 marks)

End of Section A

Four (04) Compulsory Questions

(Total 40 marks)

SECTION B**Answers to Question 2**

Unit 1 – Economic concepts and systems related to business environment.

Unit 2 – Demands, Supply, Equilibrium and ways of government intervention.

Learning outcomes - Explain economic resources and non-economic resources.

- Explain different types of economic systems.

- Analyze the theory of demand and supply.

(a) (i) Land

Land includes all resources that are gift of mother nature available for production activities. Rent is the payment or reward for the use of land.

Ex: - rivers, minerals

Labor

Labor is defined as the physical and mental abilities of the human being used in the production activities. Wage or salary is the payment for labor.

Capital

Capital is the man made resources used in production activities. It includes physical plant, machinery, factory buildings etc. Interest is the reward for capital.

Entrepreneurship

Entrepreneurship is a special category of labor which enriched in creative ability. This is a scarce resource because a very few people are willing to take business risk. Profit is the reward for Entrepreneurship. **(02 marks)**

- (ii) Sri Lankan economy is a mixed economy. The features of market economy and socialist economy are visible in the Sri Lankan economy. Government provides services such as education, health, etc. while private sector is operating in the economy. **(03 marks)**

(b)

$$300 - 5P = -50 + 5p$$

$$10P = 350$$

$$P = 35$$

$$Q_D = 300 - 5(35)$$

$$Q = 125$$

(03 mark)

(c)

$$Q = -50 + 5(40)$$

$$= -50 + 200$$

$$= 150$$

(02 marks)
(Total 10 marks)

Answers to Question 3

Unit 3 – Behavior of production process and different market structure.

Learning outcomes – Explain the behavior of production cost in the production process.

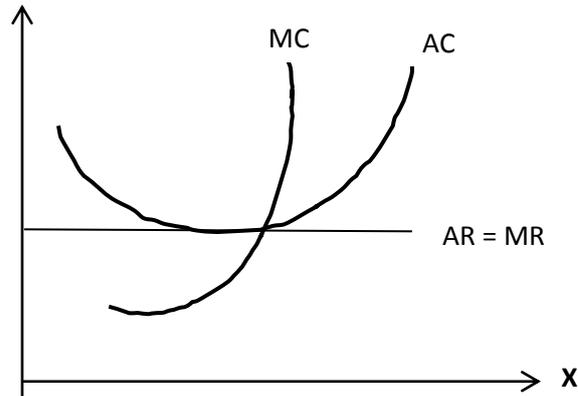
- Discuss the different market structures and their characteristics.

(a) In the short run production process, the law of diminishing marginal return determines behavior of the output in short run. If more and more of a variable factor of production is used in a combination with a fixed factor of production, marginal product then the average product will eventually decline. In short run production is increased only by changing the variable inputs keeping the fixed inputs constant.

(03 marks)

(b) In the long run new firms can enter to the market to compete the existing firms. Under the perfect competition, equilibrium of the firm occurs where the demand curve (price) intersects the marginal cost (MC) curve and minimum point of average cost (AC) curve.

Y



(04 marks)

(c)

	Perfectly Competitive Market	Monopoly Market
1.	Large number of sellers.	Single seller.
2.	Homogeneous products.	Specific products.
3.	Free entry and exit.	Barriers to entry.
4.	Firms are price takers.	Firm is price maker.
5.	Firms face with perfectly elastic demand curve.	Firm faces with downward sloping demand curve.

(03 differences, 03 marks)

(Total 10 marks)

Answers to Question 4

Unit 5 – Financial system, Money and General Price level

Learning outcomes – Explain functions of money, demand for money and money supply.

- Explain the fundamentals of money supply & demand, interest rates, price level and inflation.

(a)

- (1) Transaction demand for money is related to the function of money as a medium of exchange and the speculative demand for money is related to the function of money as a store of wealth.
- (2) Since households and firms payments and receipts are not perfectly synchronized, they have to hold some amount of their income in the form of money to fill the gap between receipts and payments. The amount of money that people will be hold for this purpose is called transaction demand for money. People would like to hold certain amount of their income in the form of money to invest in bonds. The amount of money that people wish to hold for this purpose is called speculative demand for money.
- (3) While transaction demand for money depends on the level of income, speculative demand for money depends on interest rate. **(04 marks)**

(b) Medium of exchange

The most significant function of money is as a medium of exchange in order to facilitate transactions. If there is no money, all business transactions would have to be carried through barter system.

Store of value

Individual can choose to forgo consumption in the current period and save to increase their spending power in the future. Inflation has the effect of reducing the internal purchasing power of money.

Unit of account

Money as common unit of account enables us to compare the relative prices and goods and services in rupees.

Standard of deferred payment

It allows payment for goods and services consumed today in a future time period.

Eg: - mortgage on a house.

(03 marks)

(c) Demand full inflation occurs when total demand for goods and services is greater than total supply. This type of inflation happens when there has been excessive growth in aggregate demand and there is an inflationary gap.

Cost push inflation occurs from the supply side and it is usually the result of increase in the cost of production. It happens when firms increase price to maintain or protect profit margin after experiencing a rise their costs of production.

(03 marks)

(Total - 10 marks)

Answers to Question 5

Unit 4 – National accounting and role of the government.

Unit 6 – International trade and foreign exchange market.

Learning outcomes - Explain trade cycle and its impact on business.

- Explain theories of international trade.

- Explain the foreign exchange market and determination of exchange rates.

(a) (i) Business cycle is the rise and fall in production output of goods and services in an economy.

(02 marks)

(ii) Expansion / boom

This is characterized by increasing employment. This will continue till there is 100% utilization of available resources.

Peak

This is the highest point of the business cycle. At this period the output is maximized. This leads to increase in the price of consumer goods.

Contraction (Recession)

At the peak of economy demand is stagnant. Then very soon demand starts falling in certain of the economy. This is the start of the contraction phase of the trade cycle which is the opposite of the expansion phase.

Trough

This is the lowest phase of the business cycle. It is a severe form of recession and we can see negative growth in the economy.

(Any two stages – 02 marks)

(b) When one nation is more efficient than the other nation in the production of a commodity that nation has absolute advantage in the production of that commodity.

The ability of a nation to produce a particular good or service at a lower opportunity cost over another nation is known as comparative advantage.

(02 marks)

(C)

- Devaluation of rupee causes inflation because:
 - Imports will be more expensive (any imported good or raw material will increase in price)
 - Cost of production will increase and it results to increase in prices of goods and services.
 - Due to inflation it affects standard of living of people.
 - It affects to increase in deficit of balance of payment account

- Reduces the purchasing power of citizens due to increase in prices of goods and services.
- Reduces real wages. With the increase in prices of goods and services real wage of employees will reduce.
- A large and rapid devaluation affects to foreign investments. It causes that investors do not willing to invest in the country.
- Due to devaluation of rupee, repayment of foreign loan and interest will be high. It affects to increase in deficit balance of balance of payment account.

(04 marks)

Answer to Question 6

Unit 4 – National Accounting and role of the government.

Unit 5 – Financial system, Money and General Price level.

Unit 7 – Economic growth, development and new trends in the economy.

Learning outcomes - Explain the role of government to achieve macro-economic objectives.

- Identify macro-economic objectives.
- Calculate the national income on three main approaches.
- Explain the relationship between liquidity and profitability of commercial banks.
- Explain new trends in the economy.

(a) (i) Inefficiency in distribution of resources are known as market failure. **(01 mark)**

(ii)

- Lack of Public goods/ Semi-public goods.
- Externalities.
- Imperfect information.
- Absence of certain markets.
- Imperfect factor mobility.
- Unequal distribution resources.
- Macroeconomic instability.

(03 marks)

(b) Price Stability

To achieve price stability it is necessary to manage the economy without inflation or deflationary pressures. Average price level in the economy is considered as stable when economy experiences very lower rate of inflation.

(ii) Gross Domestic Product - at market price

Gross value at basic price	12,800	
<u>Add</u>		
Net tax on products	<u>1,200</u>	
GDP at market price	Rs. <u>14,000 billion</u>	(02 marks)

(iii) Gross National Income

Gross domestic product (MP)	14,000	
<u>Add</u>		
Net primary income from the rest of the world	<u>(800)</u>	
Gross National Income	Rs. <u>13,200 billion</u>	(02 marks)

(d) Commercial banks do their business with funds collected from other. The value of deposits that a bank can generate is depending on the confidence on that people have about the financial soundness of such banks. To maintain that requirement banks have to maintain liquidity. That is banks have to keep sufficient funds with them to maintain liquidity. On the other hand banks have to generate profit through lending. **(03 marks)**

(e)

- Advanced Technology. Eg: AI, block chain.
- Natural disaster will affect to economy.
- Financial crises of some countries.
- Introduction new law specially in IT related matters.
- Economic of UK, Japan and China began to weaken.
- Global economy is declining due to corona virus.

(Any 3 points - 03 marks)

(Total 20 marks)

End of Section C