



Association of Accounting Technicians of Sri Lanka

Level I Examination – January 2026

Question Paper and Suggested Answers

(103) ECONOMICS (ECN)

Association of Accounting Technicians of Sri Lanka

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THE ASSOCIATION OF ACCOUNTING TECHNICIANS OF SRI LANKA

Level I Examination – January 2026

(103) ECONOMICS

SUGGESTED ANSWERS

(Total 40 Marks)

SECTION - A

Suggested Answers to Question One:

Question No **Answer**

1.1 (3)

1.2 (1)

1.3 (1)

1.4 (2)

1.5 (2)

1.6 (3)

1.7 (3)

1.8 (4)

1.9 (1)

1.10 (2)

1.11 Opportunity Cost

1.12 Maximum

1.13 True

1.14 False

1.15 Characteristics of Economic Goods (Section 1.3.3.3)

- Existence of limitation/scarcity in supply.
- Existence of cost of resources.
- Existence of opportunity cost.
- Most of the economic goods are having a price.
- Economic goods are an outcome of a production process.
- Existence of a clear ownership



1.16 Demand Pull Inflation (Section 5.10.2)

Demand Pull Inflation is the type of inflation that results when an economy's aggregate **demand exceeds its aggregate supply**. To put this in simple terms, when production cannot keep up with the aggregate demand, higher prices quickly follow.

1.17 Motives for Demand for Money (Section 5.2)

- Transactions motive
- Precautionary motive
- Speculative motive

1.18 Difference between total utility and marginal utility(Section 2.1.1.2)

Total Utility: The total satisfaction derived from consuming any given quantity of a good or service, over a given period of time.

Marginal Utility: The additional satisfaction gained from consuming one additional unit of a good or service, over a given period of time.

1.19 Elements in the profile of Human Development (Section 7.3.1)

- Income
- Education
- Health Conditions
- Political Freedom
- Economic freedom
- Healthy social relations
- working environment
- Empowerment
- Equality

1.20 Recent economic trends in Sri Lankan Economy (Section 7.6)

- Inflation remains low and stable and some deflationary pressures in certain months
- Government working toward debt sustainability targets and the budget deficit reduction efforts continuing
- Return to positive GDP growth.
- Foreign reserves continued to improve
- Continuing strong performance in tourism sector
- Tax performance has dramatically improved.
- Sri Lanka is diversifying beyond traditional sectors like tea, rubber, spices, and tourism. Key emerging industries include: Information and Communication Technology (ICT), Healthcare, Real Estate, Education
- Innovation in agriculture through technology and AI, alongside rising demand for organic and healthy foods, supporting growth in food processing and related ventures

- Gross domestic production and the importance of agricultural sector has diminished.
- Manufacturing and service sectors have increased.
- Percentage of employment in agriculture sector has declined while the percentage of employment in industrial and service sectors has increased.
- There has been a decline in the working age population of the labour force in Sri Lanka while the labour force participation rate has gone up.
- Upward trend in the female participation recently.
- Upward trend in Sri Lankan workers seeking foreign employment and as a result there has been a surge in foreign remittances.
- Increase in Digitalization.

(02 marks each, Total 40 marks)



End of Section A

Suggested Answers to Question Two:**Chapter 01 and 02**

(a) Four factors of Production (Economic Recourses) (Section 1.2.1)

(i) Land, Labor, Capital, Entrepreneurship

(02 marks)

(ii) Instances where opportunity cost is zero (Section 1.3.3.1)

- When there is no scarcity of resources.
- When resources have no alternative uses.
- When unemployed resources are used in economic activities

(02 marks)

(b)

Market equilibrium price and quantity (Section 2.4)

At equilibrium: $Q_d = Q_s$

$$200 - 10p = 40 + 30p$$

$$200 - 40 = 30p + 10p$$

$$160 = 40p$$

P = 4 (equilibrium price)

Substituting $p = 4$ into either equation:

$$Q_d = 200 - 10(4) = 200 - 40 = \mathbf{160}$$

$$\text{Or: } Q_s = 40 + 30(4) = 40 + 120 = \mathbf{160}$$

(03 marks)

(c) Determinants of Price Elasticity of Supply (Section 2.7.3)

- The level of mobility of factors of production.
- Nature of the good.
- Ability to maintain stocks and shares.
- The time required to change supply in response to the change in price of the given good.
- Cost of Production

(03 marks)

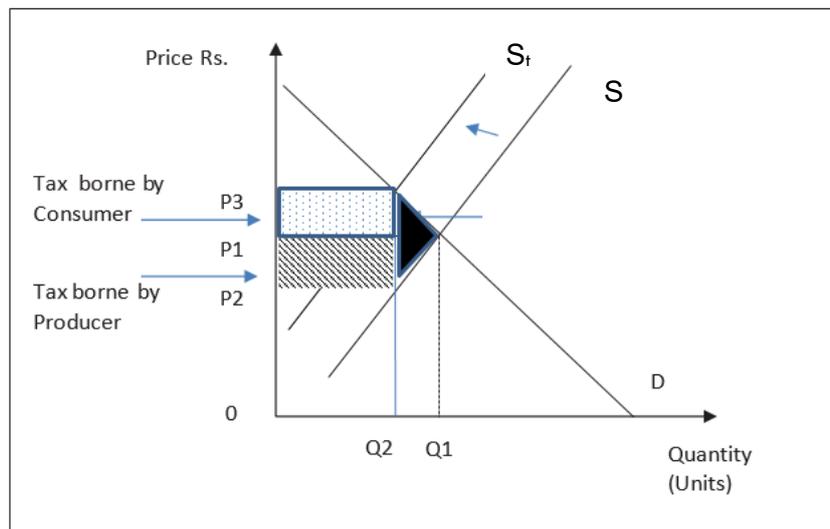
(Total 10 marks)

Suggested Answers to Question Three:

Chapter 02 and 03

(a)

(i)



When a unit tax is imposed, the supply curve shifts to the left from S to S_t . The market equilibrium moves from Q_1 to Q_2 . Consumers pay price P_3 , while producers receive P_2 . As there is no change in the quantities consumers intend to purchase at different prices, before and after the imposition of taxes, there is no change in the position of demand. The difference $(P_3 - P_2)$ represents the tax per unit. The dotted rectangle shows tax revenue collected, while the black triangle illustrates deadweight loss, the economic efficiency loss from reduced market activity.

(ii) Characteristics of the long run in a production process (Section 3.3.9)

- All Factors are Variable
- Returns to Scale / Economic of Scale
- Firms can adopt new production methods and technologies

(05 marks)

(b) Characteristics of an Oligopoly Market (Section 3.6.4)

- Only a few firms operate in the entire market.
- Existence of entry/exit barriers.
- Existence of interdependence among the firms in the industry.
- Firms producing identical or differentiated products.
- The firms in Oligopoly market face relatively a kinked demand curve
- Non-price competition (advertising, branding, product differentiation)
- Price rigidity

(02 marks)

(03 marks)

(Total 10 Marks)

Suggested Answers to Question Four:

Chapter 05

(a) Functions of a commercial bank (Section 5.6.1)

- Accepting Deposits
- Lending Money
- Collection of cheques and bills
- Issuing letters of credit
- Issuing Letters of references
- Issuing travellers cheques
- Safety locker facility
- Modern Facilities (Electronic Fund Transfer (EFT), Automated Teller Machines (ATM))
- Issuing Debit Cards and Credit Cards
- Leasing facilities
- Debt factoring services

(03 marks)

(b) Relationship between price level and rate of interest (Section 5.11)

When the general price level rises, nominal interest rates rise too. There is a negative relationship between price level and the real interest rate.

$$\text{Real interest rate} = \text{Nominal rate} - \text{Inflation rate.}$$

It represents the actual purchasing power return on savings after accounting for inflation's erosion of money value.

When interest rates rise, borrowing becomes expensive, reducing consumption and investment. This decreases aggregate demand, leading to lower price levels. Conversely, lower interest rates stimulate spending, increasing aggregate demand and pushing price levels up.

(03 marks)

(c) Qualitative monetary policy instruments used by the Central Bank of Sri Lanka (Section 5.5.1.2)

- Setting a maximum maturity period for loans
By reducing the maximum loan repayment period, it will reduce the flow of loan quantity. When the repayment period is increased, it will increase the loan for some sector. Therefore, when there is a need to encourage some sector of the economy then the repayment period of loan has to be increased
- Setting preferential rates of interest
If there is a need to reduce the flow of loans to one section, then the rate of interest is increased and vice versa.
- Setting Limits for loan guarantees
If there is a need to increase the flow of loan to one section the guarantees needed to secure loans are reduced for that sector and vice versa.

- Setting limits for investments and loans
This implies setting limits for the loans supplied to a particular sector. If this limit is decreased, then the flow of loans to that sector is increased and vice versa.
Setting limits for Letter of Credit and cash a balance business for profit and involve in financial intermediation.
- Indirect Control (ex:Moral Suasion) Control of loan flow from commercial banks by getting their cooperation instead of direct control.

(04 marks)
(Total 10 marks)

Suggested Answers to Question Five:

Chapter 06

(a) Comparative advantage in the production (Section 6.1.2.2)

Opportunity Costs by Commodity:

Commodity	Australia	Brazil	Comparative Advantage
Sugar	$6/12 = 0.5$	$6/3 = 2$	Australia ($0.5 < 2$)
Wheat	$12/6 = 2$	$3/6 = 0.5$	Brazil ($0.5 < 2$)

Comparative Advantage:

Australia has comparative advantage in sugar as it records the lowest opportunity cost ($0.5 < 2$) (opportunity cost of Australia is 0.5 kg wheat vs Brazil's 2 kg wheat)

Brazil has comparative advantage in wheat as it records the lowest opportunity cost ($0.5 < 2$) (opportunity cost of Brazil is 0.5 kg sugar vs Australia's 2 kg sugar)

Each country should specialize in the good where it has the lower opportunity cost.

(04 marks)

(b) Difference between "Flexible Exchange Rate" and "Fixed Exchange Rate" (Section 6.7.1)

A Fixed Exchange Rate is one, whose value is fixed against the value of another currency or currencies and is maintained by the Central Bank. It is not changed according to the changes in demand and supply of currencies. A Flexible exchange rate is a system that allows the exchange rate to be determined by market forces in the Forex market i.e. Supply and demand forces. As a result the exchange rates may change according to the movements in foreign Exchange Market.

(03 marks)

(c) Steps that can be used to control the depreciation of the Sri Lankan Rupee against US Dollar (\$). (Section 6.8.2)

- **Increase the competitiveness of exports** – Promote and diversify export products to earn more foreign currency (US Dollars), which increases the supply of dollars in the market and strengthens the rupee.
- **Reduce import expenditure** – Implement measures to restrict non-essential imports, encourage import substitution, and promote local production to reduce the demand for US Dollars.
- **Reduce external imbalances** – Address balance of payments deficits by utilizing domestic resources efficiently, attracting foreign direct investment (FDI), and encouraging remittances to increase foreign exchange reserves.
- **Allow monetary policy to operate freely** – Enable the Central Bank to adjust interest rates and money supply without political interference, which helps stabilize the currency through market-based mechanisms.
- **Promote domestic manufacturing** – Reduce import dependence for critical goods through initiatives like make in India and produce locally.
- **Build foreign exchange reserves** – Accumulate adequate reserves through borrowing, tourism revenue, and foreign investments to intervene in the forex market when necessary.
- **Maintain economic and political stability** – Ensure consistent policies and good governance to build investor confidence and prevent capital flight.
- **Promote the Sri Lankan rupees for trade by encouraging the use of rupee for international trade settlement.**

(03 marks)
(Total 10 marks)

End of Section B

Suggested Answers to Question Six:**Chapter 04****(A) Macroeconomic Objectives (Section 4.1)**

- Price stability
- Full employment
- Equilibrium in Balance of Payment
- Equal distribution of income (Reducing income inequalities)
- Sustainable development
- Economic growth and Development

(03 marks)**(B) Different approaches of the National Income Accounting (Section 4.4.6)**

1. Production approach
2. Income Approach
3. Expenditure Approach

(03 marks)**(C)****(a)**

Item	Rs. million
1. Private consumption expenditure	6,000
2. Government consumption expenditure	5,500
3.1 Gross domestic fixed capital formation	2,500
3.2 Changes in stock	500
3.3 Changes in value	200
Gross Domestic Expenditure (GDE) at market price (1+2+3)	14,700

(06 marks)**(b)**

Item	Rs. million
1. Gross Domestic Expenditure (GDE)	14,700
2. Add: Exports of goods and services	6,500
3. Less: Imports of goods and services	(15,000)
Gross Domestic Product (GDP) at market price	6,200

(02 marks)**(c)**

Item	Rs. million
1. Gross Domestic Product (GDP) at market price	6,200
2. Add: Foreign net primary income	1,500
Gross National Income (GNI) at market price	7,700

(02 marks)

(D) Basic price (Section 4.5.2)

When a manufacturer ready to sell the product or service which he/she has manufactured, the price which is relevant for that particular product or service can be identified as basic price. This price should be received from the buyer to the producer.

(02 marks)

(E) Difference between Direct Tax and Indirect Tax (Section 4.10.3)

Direct Tax

The relevant tax, should be paid by the person or entity that is entitled for the direct tax and that cannot be transferred to any other party. In this case the taxable person must bear the burden of the tax.

Examples include income taxes and property taxes.

Indirect Tax

If a person who is legally ordered to pay a tax transfers the tax burden to another person that is referred to as an indirect tax.

Example:VAT

(02 marks)

(Total 20 marks)



End of Section C

Notice:

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These should be understood as Suggested Answers to question set at AAT Examinations and should not be construed as the “Only” answers, or, for that matter even as “Model Answers”. The fundamental objective of this publication is to add completeness to its series of study texts, designs especially for the benefit of those students who are engaged in self-studies. These are intended to assist them with the exploration of the relevant subject matter and further enhance their understanding as well as stay relevant in the art of answering questions at examination level.



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