MUEO

MOI UNIVERSITY

OFFICE OF THE DEPUTY VICE CHANCELLOR, ACADEMIC AFFAIRS, RESEARCH & EXTENSION

UNIVERSITY EXAMINATIONS

2014/2015 ACADEMIC YEAR

4TH SEMESTER EXAMINATIONS

FOR THE DEGREE OF MASTER OF BUSINESS ADMINISTRATION

EXAM CODE:- **ECO 110**

COURSE TITLE:- **INTRODUCTION TO MICROECONOMICS**

DATE:-28TH SEPTEMBER, 2015 **TIME:-9.00A.M. – 12.00NOON.**

INSTRUCTION TO CANDIDATES

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ECO 110: INTRODUCTION TO MICROECONOMICS

ANSWER ANY THREE QUESTIONS

QUESTION ONE

(a) Describe the law of diminishing marginal utility and explain how this law can be used in making decisions on contemporary economic issues. (10 marks)

(b) You are given the following market model for commodity X

$Qd = 20 - 1/3P$

$Qs = -20 + 3P$

Where Qd is demand function of commodity X

Qs is supply function of commodity X

P is price in shilling

Required:

(i) Compute the equilibrium price and quantity of commodity X (5 marks)

(ii) What is the effect of a decrease in price of commodity Y which is a close substitute to commodity X on the equilibrium quantity and price? Use diagram(s) to illustrate (5 marks)

QUESTION TWO

Define the terms 'substitution effect' and 'income effect' of a price change. Use appropriate diagrams to show substitution and income effects of a price change in a two goods market (X and Y) when price of X changes if:

(i) Both goods X and Y are normal goods

(ii) Good X is an inferior good but good Y is a normal good

(20 marks)

QUESTION THREE

(a) Describe the characteristics of a perfectly competitive market and show how equilibrium price and output are achieved in the long – run (10 marks)

(b) A farm wants to increase output by increasing the input of labour while capital remains fixed/unchanged. The human resource manager argues that this strategy is viable and the firm can continuously hire more labour for the next twelve months. Do you agree with this strategy? Support your answer (10 marks)

QUESTION FOUR

Distinguish between the following pairs of concepts:

(i) Cross elasticity and income elasticity of demand (4 marks)

(ii) Oligopoly and monopoly markets (4 marks)

(iii) Long – run and short – run periods of production (4 marks)

(iv) Engel curve and demand curve (4 marks)

(v) Marginal rate of technical substitution and marginal rate of substitution (4 marks)

QUESTION FIVE

(a) Derive individual consumer's demand curve using:

(i) Indifference curve analysis (6 marks)

(ii) Cardinalist approach (4 marks)

(b) Using appropriate diagrams, clearly explain how optimal combination of factor inputs is achieved by a profit maximizing firm (10 marks)