Seat No.: _____ Enrolment No._____

GUJARAT TECHNOLOGICAL UNIVERSITY

MBA – SEMESTER 1 – EXAMINATION – WINTER 2015

Subject Code: 2810002 **Date: 19/12/2015**

Subject Name: Economics for Managers

Time:10.30 AM TO 01.30 PM **Total Marks: 70**

Instructions:

1. **Attempt all questions.**
2. **Make suitable assumptions wherever necessary.**
3. **Figures to the right indicate full marks.**

Q.1 (a) Objective Questions **6**

1. The cost of producing an extra unit of output is the _____.
   A. Total Cost B. Marginal Cost
   C. Variable Cost D. Cost of Production
2. _____ is falling when marginal cost is below it and rising when marginal cost is above it.
   A. Average variable cost B. Average Total Cost
   C. Average Fixed Cost D Total Cost
3. For Competitive firm P= _____
   A. MR > AR B. AR > MR
   C. AR = MR D. MR < AR
4. In the long run supply curve becomes _____
   A. Vertical B. Horizontal
   C. Upward Slopping D. Downward Slopping
5. Oligopoly means _____
   A. One seller many buyer B. few seller few buyer
   C. few seller many buyers D. two seller many buyers
6. Real Interest rate is _____ Nominal Interest rate
   A. Greater than B. Less than
   C. Equal to D. not comparable with

Q.1 (b) Define the Terms **04**

1. Monetary Neutrality
2. Monopolistic Competitive Firm
3. Aggregate Demand
4. Economic Profit

Q.1 (c) Discuss the Circular Flow Diagram. **04**

Q.2	**(a)**	What is Economics? Explain any three principles of it.	**07**
	(b)	Explain Price elasticity of Supply with reference to the Petroleum Products.	**07**
		OR	
	(b)	Person A's income declines and as a result, he buys more spinach. Is spinach an inferior or a normal good? What happens to person A's demand curve for spinach?	**07**
Q.3	**(a)**	Define ATC, AVC, AFC, and MC. Discuss relationship among them.	**07**
	(b)	Competitive Firm stays in market even if they make zero economic profit. Explain it.	**07**
		OR	
Q.3	**(a)**	Discuss production and pricing decision for monopoly firm.	**07**
	(b)	What is prisoner's Dilemma and what does it have to do with oligopoly?	**07**
Q.4	**(a)**	What is CPI? How it can be Calculated?	**07**
	(b)	GDP is not ultimate measure of well-being of an economy. Discuss it.	**07**
		OR	
Q.4	**(a)**	Discuss various types of costs of inflation.	**07**
	(b)	RBI uses various tools to control money supply. Discuss it.	**07**

Q.5 Read following case and answer the questions.

THE CASE AGAINST ACTIVE STABILIZATION POLICY

Some economists argue that the government should avoid active use of monetary and fiscal policy to try to stabilize the economy. They claim that these policy instruments should be set to achieve long-run goals, such as rapid economic growth and low inflation, and that the economy should be left to deal with short-run fluctuations on its own. Although these economists may admit that monetary and fiscal policy can stabilize the economy in theory, they doubt whether it can do so in practice.

The primary argument against active monetary and fiscal policy is that these policies affect the economy with a substantial lag. As we have seen, monetary policy works by changing interest rates, which in turn influence investment spending. But many firms make investment plans far in advance. Thus, most economists believe that it takes at least six months for changes in monetary policy to have much effect on output and employment. Moreover, once these effects occur, they can last for several years. Critics of stabilization policy argue that because of this lag, the Fed should not try to fine-tune the economy. They claim that the Fed often reacts too late to changing economic conditions and, as a result, ends up being a cause of rather than a cure for economic fluctuations. These critics advocate a passive monetary policy, such as slow and steady growth in the money supply.

Fiscal policy also works with a lag, but unlike the lag in monetary policy, the lag in fiscal policy is largely attributable to the political process. In the United States, most changes in government spending and taxes must go through congressional committees in both the House and the Senate, be passed by both legislative bodies, and then be signed by the president. Completing this process can take months and, in some cases, years. By the time the change in fiscal policy is passed and ready to implement, the condition of the economy may well have changed.

These lags in monetary and fiscal policy are a problem in part because economic forecasting is so imprecise. If forecasters could accurately predict the condition of the economy a year in advance, then monetary and fiscal policymakers could look ahead when making policy decisions. In practice, however, major recessions and depressions arrive without much advance warning. The best policymakers can do at any time is to respond to economic changes as they occur.

Questions:

1. Give an example of a government policy that acts as an automatic stabilizer. Explain why this policy has this effect..
2. What are the primary arguments against active monetary and fiscal policy?

OR

Q.5 Read following case and answer the questions.

WHY WERE INFLATION AND UNEMPLOYMENT
SO LOW AT THE END OF THE 1990S?

As the twentieth century drew to a close, the U.S. economy was experiencing some of the lowest rates of inflation and unemployment in many years. In 1999, for instance, unemployment had fallen to 4.2 percent, while inflation was running a mere 1.3 percent per year. As measured by these two important macroeconomic variables, the United States was enjoying a period of unusual prosperity. Some observers argued that this experience cast doubt on the theory of the Phillips curve. Indeed, the combination of low inflation and low unemployment might seem to suggest that there was no longer a tradeoff between these two variables. Yet most economists took a less radical view of events. As we have discussed throughout this chapter, the short-run tradeoff between inflation and unemployment shifts over time. In the 1990s, this tradeoff shifted leftward, allowing the economy to enjoy low unemployment and low inflation Simultaneously. What caused this favorable shift in the short-run Phillips curve? Part of the answer lies in a fall in expected inflation. Under Paul Volcker and Alan Greenspan, the Fed pursued a policy aimed at reducing inflation and keeping it low. Over time, as this policy succeeded, the Fed gained credibility with the public that it would continue to fight inflation as necessary. The increased credibility lowered inflation expectations, which shifted the short-run Phillips curve to the left. In addition to this shift from reduced expected inflation, many economists believe that the U.S. economy experienced some favorable supply shocks during this period. (Recall that a favorable supply shock shifts the short-run aggregate-supply curve to the right, raising output and reducing prices. It therefore reduces both unemployment and inflation and shifts the short-run Phillips curve to the left.) Here are three events that may get credit for the favorable shift to aggregate supply:

_ *Declining Commodity Prices.* In the late 1990s, the prices of many basic commodities fell on world markets. This fall in commodity prices, in turn, was partly due to a deep recession in Japan and other Asian economies, which reduced the demand for these products. Because commodities are an important input into production, the fall in their prices reduced producers' costs and acted as a favorable supply shock for the U.S. economy.

_ *Labor-Market Changes.* Some economists believe that the aging of the large baby-boom generation born after World War II has caused fundamental changes in the labor market. Because older workers are typically in more stable jobs than younger workers, an increase in the average age of the labor force may reduce the economy's natural rate of unemployment.

_ *Technological Advance.* Some economists think the U.S. economy has entered a period of more rapid technological progress. Advances in information technology, such as the Internet, have been profound and have influenced many parts of the economy. Such technological advance increases productivity and, therefore, is a type of favorable supply shock.

Questions:

1. What are the main events that get credit for the favorable shift to the aggregate supply? Which event is most important?
2. What is the sacrifice ratio? How might the credibility of the Fed's commitment to reduce inflation affect the sacrifice ratio?

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