INSTITUTE AND FACULTY OF ACTUARIES

EXAMINATION

30 September 2013 (pm)

Subject CT7 – Business Economics
Core Technical

PART B

Total exam time allowed: Three hours

INSTRUCTIONS TO THE CANDIDATE

1. *Enter all the candidate and examination details as requested on the front of your answer booklet.*

2. *You must not start writing your answers in the booklet until instructed to do so by the supervisor.*

3. *Mark allocations are shown in brackets.*

4. *See front of answer booklet for further instructions.*

5. *Candidates should show calculations where this is appropriate.*

Graph paper is NOT required for this paper.

AT THE END OF THE EXAMINATION

Hand in ALL answer booklets and this question paper.

In addition to this paper you should have available the 2002 edition of the Formulae and Tables and your own electronic calculator from the approved list.

27 The owner of an orchard can choose to grow apples or pears on their land. Apples sell for £200 per tonne. Pears sell for £350 per tonne. The costs of seed, fertiliser, labour and storage costs are £140 per tonne for both goods. Calculate the owner's cost and profit per tonne if the orchard owner decides to grow pears instead of apples on their land. [2]

28 Describe how a firm that manufactures cars may experience economies of scale. [4]

29 (i) Draw a diagram to show a typical monopolistically competitive firm, such as a coffee shop, which is wishing to operate but is making a loss. Your diagram should show all the relevant cost and revenue curves and the area corresponding to the firm's losses. [3]

(ii) Now assume that consumer demand for hot drinks increases. Show, with the use of a new diagram, the effect this will have on the market price and quantity traded in the short run, assuming that the firm now makes a profit. [2]

[Total 5]

30 List four factors which favour collusion amongst oligopolistic firms. [2]

31 Describe two reasons why firms might wish to form strategic alliances. [2]

32 (i) Discuss, with the use of examples, two factors that influence the price elasticity of demand for a good. [2]

(ii) Demonstrate, with the use of two separate diagrams, the effect of an increase in labour productivity on the price and quantity traded when demand is:

(a) elastic.
(b) inelastic.

[2]

[Total 4]

33 Outline two possible drawbacks of government intervention in the market. [4]

34 For a given amount of resources, the table below shows weekly production of either socks or shoes in Country A and Country B.

Country	*Socks*	*Shoes*
A	20	20
B	18	9

(i) State:

(a) which country has an absolute advantage in the production of each of the two goods.

(b) which country should specialise in the production of socks.

(c) which country should specialise in the production of shoes.

[3]

(ii) Now assume that each country wishes to produce equal amounts of socks and shoes.

(a) Determine the production of each good in Country A.

(b) Determine the production of each good in Country B.

[2]

(iii) Determine the total gain in production of each good when countries specialise using all of the available resources in comparison to the case (ii) above. [1]

[Total 6]

35 Use the aggregate demand and supply model to illustrate and explain the difference between demand pull and cost push inflation. [6]

36 Describe the main types of policies that governments can use to encourage competition. [6]

37 (i) Explain, using a diagram, the Phillips curve relationship. [3]

(ii) Explain, with reference to a diagram, the expectations-augmented Phillips curve and the accelerationist theory of money and discuss the implications this has for government policy. [7]
[Total 10]

38 (i) Explain, using a diagram, the impact on aggregate expenditure and GDP in an economy with no public sector and no international trade, following each of the events below (treat the two events separately):

(a) An increase in business confidence
(b) An increase in the marginal propensity to consume

[8]

(ii) Show on your diagram from part (i)(b), an inflationary gap and a deflationary gap at the new level of aggregate expenditure. [2]
[Total 10]

END OF PAPER