අධ්‍යයන පොදු සහතික පත්‍ර (උසස් පෙළ) විභාගය, 2026
கல்விப் பொதுத் தராதரப் பத்திர (உயர் தர)ப் பரீட்சை, 2026
General Certificate of Education (Adv. Level) Examination, 2026

ආර්ථික විද්‍යාව I
பொருளியல் I
Economics I

21 E I

පැය දෙකයි
இரண்டு மணித்தியாலம்
Two hours

Instructions:

* *Answer **all** the questions.*
* *Write your **Index Number** in the space provided in the answer sheet.*
* *Instructions are given on the back of the answer sheet. Follow them carefully.*
* *In each of the questions from **1** to **50**, pick one of the alternatives from (1), (2), (3), (4), (5) which is **correct or most appropriate** and **mark your response on the answer sheet with a cross** (×) in accordance with the instructions given on the back of the answer sheet.*

1. Among the following topics, the topics related to microeconomics is the
(1) effect of government regulation on railway transport service.
(2) causes of rapid increase in the general price level.
(3) obstacles to achieve a sustained economic growth.
(4) effect of government budget deficit on inflation.
(5) determination of equilibrium level of national income.

2. Which of the following is a consequence of the scarcity of resources relative to unlimited human wants?
(1) There is no excess supply in markets for goods and services.
(2) Markets are unable to allocate resources efficiently.
(3) All goods and services have a market price.
(4) The employment of factors of production has an opportunity cost.
(5) The quantities available of some resources exceed the demand for them.

3. Consider a country that produces tea and tyres. If resources are fully employed and there is technological progress only in the production of tyres, in which of the following ways will the opportunity cost of producing tea and tyres change?

	Opportunity Cost of Tea Production	Opportunity Cost of Tyre Production
(1)	Increase	Increase
(2)	Increase	Decrease
(3)	No change	Increase
(4)	Decrease	Increase
(5)	Decrease	Decrease

4. Why might the motivation to innovate be weaker in a centrally planned economic system compared to a market economic system?
(1) Encouragement of imitation due to excessive competition among firms
(2) Existence of strong intellectual property rights
(3) Lack of profit motives
(4) Frequent changes in consumer preferences
(5) Investment decisions are fully decentralized

[see page two

5. One reason consumers typically increase the quantity of a good they purchase when the price of the good decreases, while other things remain constant, is that
   (1) as income increases, willingness to pay for an additional unit increases.
   (2) consumers' purchasing power increases.
   (3) consumers increase their purchases of substitute goods.
   (4) consumers increase their purchases of complementary goods.
   (5) consumers expect future prices to fall.

6. The Table shows the price of a good and total outlay on the good during specific periods when the market is in equilibrium.
   What can be deduced from this data?
   (1) The good is an inferior good.
   (2) The good has constant opportunity cost in production.
   (3) Price elasticity of demand is equal to one.
   (4) Price elasticity of supply is equal to zero.
   (5) This is a luxury good.

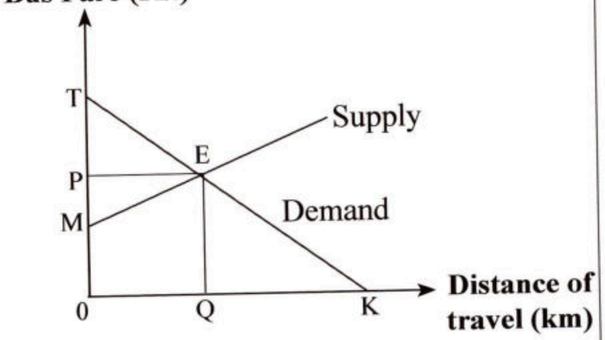
Period	Price (Rs.)	Total Outlay (Rs.)
1	15	750
2	8	400
3	5	250
4	10	500
5	6	300

7. In a particular year, 5 000 units of a commodity are sold at a price of Rs. 100 per unit. In a later year, 8 000 units are sold at a price of Rs. 125 per unit. If consumer tastes remain unchanged, which of the following could explain the change between the two years?
   (1) A decrease in the price of raw materials used for production
   (2) A technological improvement in the production process
   (3) The formation of a monopoly in the production of the good
   (4) An increase in the price of a complementary good
   (5) An increase in the price of a substitute good

8. The relationship between increase in price and decrease in quantity demanded for five internet services is given below. Which service has the lowest price elasticity of demand?

	Internet Service	Increase in price by (%)	Decrease in quantity demanded by (%)
(1)	A	10	8
(2)	B	6	6
(3)	C	10	4
(4)	D	3	7
(5)	E	10	0

9. The diagram shows the demand curve and the supply curve for bus travel within a major city. In order to reduce environmental pollution and traffic congestion, the Municipal Council has decided to pay bus companies to provide bus transport free of charge for general public.
   As a result of this policy the consumer surplus will increase by
   (1) PTE. (2) OPEK.
   (3) QEK. (4) OTK.
   (5) OMEK.



10. Suppose the initial market demand and supply equations are given below.
$$Q_D = 200 - 3P \qquad Q_S = -20 + 2P$$
   If demand decreases by 20 units at every price and supply increases by 20 units at every price, the new equilibrium price is
   (1) Rs. 20. (2) Rs. 30. (3) Rs. 36. (4) Rs. 44. (5) Rs. 72.

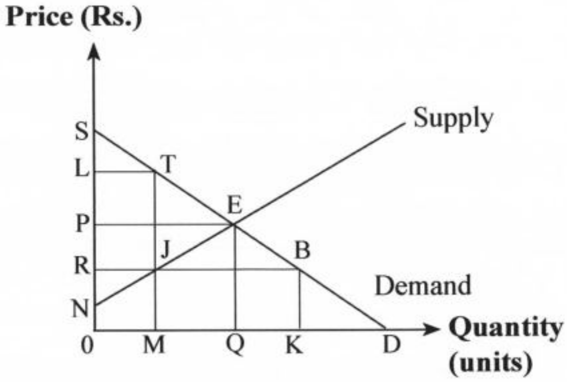
[see page three

11. Consider the market described by the following demand and supply functions.

$P = 140 - Q_D$ (Demand) $P = 40 + Q_S$ (Supply)

The economic surplus at equilibrium in this market is
(1) 1 250. (2) 2 500. (3) 3 250. (4) 4 500. (5) 5 750.

12. If there is price ceiling set at R, in the market shown by this diagram, the consumer surplus is represented by the area
(1) PEDO.
(2) PSE.
(3) RSTJ.
(4) RSB.
(5) RJMO.



13. Suppose the market for good X is in equilibrium with 1 000 units sold at a price of Rs. 50 per unit. The government pays a subsidy of Rs. 5 per unit for the producers of good X. Under which conditions the total expenditure by the government on the subsidy be minimum?

	Price elasticity of demand for good X	Price elasticity of supply for good X
(1)	Less than 1	Less than 1
(2)	Less than 1	More than 1
(3)	More than 1	Less than 1
(4)	More than 1	More than 1
(5)	More than 1	Equal to one

14. Which of the following statements best explains why government introduces minimum price for agricultural crops?
(1) To reduce consumer expenditure
(2) To stabilize consumer prices by reducing demand fluctuations
(3) To benefit poorer consumers
(4) To increase market competition
(5) To guarantee producers a higher and stable income

15. The Table below shows the total variable cost for different levels of output sold by a firm in a competitive market.

Output (units)	Total Variable Cost (Rs.)
1	60
2	90
3	110
4	125
5	130

Assume that total fixed cost is Rs. 100. Based on the cost and output data, calculate the marginal cost when the firm increases its output from 3 to 4 units and the average total cost of producing 5 units.

	Marginal Cost (Rs.)	Average Total Cost (Rs.)
(1)	15	26
(2)	30	70
(3)	20	80
(4)	15	46
(5)	60	56

[see page four

16. If the price of the firm's variable input increases while other things remain unchanged, which of the following will occur?
(1) The firm will increase its level of production.
(2) The firm will decrease its level of production.
(3) The firm's average total cost will decrease.
(4) The price of the good will decrease in the short run.
(5) The firm's marginal cost will decrease at every level of output.

17. Assume that a perfectly competitive firm is incurring economic losses in the short run. If the firm continues to produce and sell its goods, then which of the following is true?
(1) The firm is covering all of its fixed and variable costs.
(2) The firm is covering all of it fixed costs but not all of its variable costs.
(3) The firm is covering all of its variable costs but not all of its fixed costs.
(4) The firm is covering all of its explicit costs but not all of its implicit costs.
(5) The firm must have raised the price of its goods in order to minimize its losses.

18. A profit-maximizing firm will shut down in the short run when the firm's total revenue is less than the
(1) total cost.
(2) total opportunity cost.
(3) total variable cost.
(4) total explicit cost.
(5) total implicit cost.

19. What is most likely to increase a country's circular flow of income?
(1) Increase in budget deficit
(2) Increase in imports
(3) Increase in the rate of interest
(4) Increase in households' marginal propensity to save
(5) Increase in indirect taxes

20. Which of the following is treated as a non-produced non-financial asset?
(1) Machinery
(2) Computer software
(3) Stocks of finished goods
(4) Radio frequencies
(5) Residential buildings

21. If gross value added at basic price is Rs. 2 000 million, other taxes less subsidies on production are Rs. 100 million, taxes on products are Rs. 450 million, and subsidies on products are Rs. 50 million, the value of GDP is
(1) Rs. 1 600 million.
(2) Rs. 1 900 million.
(3) Rs. 2 400 million.
(4) Rs. 2 500 million.
(5) Rs. 2 600 million.

22. The table shows some selected macroeconomic data of a hypothetical economy.

	Nominal Gross Domestic Product (Rs. Billion)	**Index of General Price Level**
Year 1	200	100
Year 2	300	125
Year 3	450	150

What is the real economic growth rate for this economy in Year 3?
(1) 5%
(2) 10%
(3) 15%
(4) 20%
(5) 25%

23. Which of the following reduces the size of the national income multiplier the most?
(1) Increase in marginal propensity to consume
(2) Decrease in tax rate
(3) Increase in marginal propensity to save
(4) Increase in autonomous consumption
(5) Increase in investment

[*see page five*

24. In the Keynesian Cross diagram, the 45^0 line represents
(1) all points where saving equals investment.
(2) all points where aggregate income equals aggregate expenditure.
(3) all full employment levels of income.
(4) the relationship between the aggregate demand and the price level.
(5) all points where consumption expenditure equals disposable income.

25. In a closed economy model, consumption (C), taxes (T), investment (I) and government purchases (G) are given below.

$C = 200 + 0.75$ Yd (Yd is disposable income), $T = 400$, $I = 500$ and $G = 600$

Estimate the level of national income (Y), consumption (C) and savings (S) at equilibrium.

	Y	C	S
(1)	3 600	1 200	600
(2)	4 000	2 900	700
(3)	4 000	2 700	1 100
(4)	3 200	2 000	600
(5)	6 400	4 700	1 700

26. In which year did Sri Lanka record its highest inflation as measured by the Colombo Consumers' Price Index?
(1) 2021 (2) 2022 (3) 2023 (4) 2024 (5) 2025

27. Which of the following situations would most likely cause headline inflation to exceed core inflation?
(1) Stable food and fuel prices
(2) Falling import prices
(3) Temporary increase in international oil prices
(4) Tight monetary policy reducing aggregate demand
(5) Decline in indirect taxes

28. Suppose that the Central Bank purchases Rs. 200 million worth of securities from the open market. Assume that the required reserve ratio is 10%, banks keep no excess reserves, and there are no cash leakages. By which of the following the reserves, demand deposits and loans of the banking system will increase after banks have made all adjustments?

	Reserves (Rs. Million)	**Demand Deposits (Rs. Million)**	**Loans (Rs. Million)**
(1)	200	2 000	2 000
(2)	2 000	1 800	2 000
(3)	1 800	2 000	1 800
(4)	200	1 800	2 000
(5)	200	2 000	1 800

29. A housewife has Rs. 10 000 in cash that she has been keeping at home for emergencies. She deposits this money into her current account at a commercial bank. How will this deposit affect money aggregates?
(1) M_1 decreases, while M_2 increases.
(2) M_1 remains unchanged, while M_2 increases.
(3) M_1 increases, while M_2 remains unchanged.
(4) M_1 and M_2 increase.
(5) M_1 and M_2 remain unchanged.

[see page six

30. Which of the following best explains the main rationale for strengthening central bank independence under the new Central Bank Act in Sri Lanka?
(1) To enable the central bank to directly finance government budget deficits without restriction.
(2) To reduce political interference in monetary policy decision-making and enhance policy credibility.
(3) To delegate monetary policy implementation entirely to commercial banks in the financial system.
(4) To ensure that interest rates are kept low even when inflationary pressures are rising.
(5) To remove the central bank's involvement in any form of commercial banking activities.

31. Which of the following best explains why market failure occurs in the presence of negative externalities?
(1) Marginal social benefit exceeds marginal private benefit.
(2) Marginal private cost exceeds marginal social cost.
(3) Marginal social cost exceeds marginal private cost.
(4) Consumers lack rational expectations.
(5) The government imposes excessive taxation.

32. In a progressive tax system,
(1) tax rate decline as income rises. (2) everyone pays the same amount of taxes.
(3) tax rates rise as income rises. (4) indirect taxes dominate direct taxes.
(5) government expenditure exceeds revenue.

33. Which principle of taxation emphasizes minimizing distortions in resource allocation?
(1) Neutrality (2) Certainty (3) Equity (4) Simplicity (5) Productivity

34. Which statement correctly distinguishes between public goods and common resources?
(1) Public goods are rival, while common resources are non-rival.
(2) Public goods are non-excludable and non-rival, whereas common resources are non-excludable but rival.
(3) Common resources are excludable while public goods are rival.
(4) Public goods always generate negative externalities and common resources always generate positive externalities.
(5) Common resources are always privately owned and public goods are always provided by the government.

35. The balanced budget multiplier suggests that
(1) equal increases in taxes and government purchases can increase national income.
(2) tax reductions always reduce inflation.
(3) budget deficits automatically reduce unemployment and increases economic growth.
(4) government expenditure has no multiplier effect.
(5) equal increase in taxes and the government expenditure can definitely reduce the poverty.

36. The main distinction between absolute advantage and comparative advantage is that comparative advantage is based on
(1) labour productivity. (2) resource ownership.
(3) opportunity cost differences. (4) population size.
(5) export volume.

37. Suppose a tariff on imported final goods is 20%, while tariffs on imported raw materials are 5%. This is likely to
(1) lower effective protection for domestic producers.
(2) increase effective protection for domestic industries.
(3) eliminate domestic value addition.
(4) reduce domestic production incentives.
(5) discourage foreign direct investment flows.

[*see page seven*

38. Which of the following is **not** a function of the World Trade Organization?
(1) Administrating multi-lateral trade agreements
(2) Providing a platform for trade negotiations
(3) Settling trade disputes among member countries
(4) Providing long term loans to member countries
(5) Monitoring trade policies of member countries

39. The secondary income account of the Balance of Payments differs from the primary income account because it
(1) records only factor income payments.
(2) excludes all transfers, including remittances and foreign aid.
(3) includes unilateral transfers such as remittances.
(4) records only investment income from government securities.
(5) records only interests payments on external debt.

40. Which of the following helps to explain why, in a freely floating exchange rate system, market forces are likely to automatically reduce a deficit or surplus on a country's balance of trade?
(1) A deficit leads to excess demand for the country's currency and a depreciating exchange rate.
(2) A deficit leads to excess supply for the country's currency and an appreciating exchange rate.
(3) A surplus leads to excess demand for the country's currency and a depreciating exchange rate.
(4) A surplus leads to excess supply for the country's currency and a depreciating exchange rate.
(5) A deficit leads to excess supply for the country's currency and a depreciating exchange rate.

41. A foreign investor buys a 5% share in a Sri Lankan plantation company. This transaction is recorded in Sri Lanka's balance of payments statement as
(1) debit to direct investment in financial account.
(2) credit to direct investment in financial account.
(3) debit to portfolio investment in financial account.
(4) credit to portfolio investment in financial account.
(5) credit to capital transfers in capital account.

42. Which of the following is most likely to help a country move from a current account deficit of the balance of payments to a current account surplus?
(1) Higher interest rates attracting foreign investors
(2) Increased domestic spending and a stronger currency
(3) Higher worker remittances from abroad and a weaker currency
(4) Higher export prices and larger interest payments on external debt
(5) Higher business investment and lower portfolio investment

43. A major criticism of Gross Domestic Product (GDP) as a measure of welfare is that GDP
(1) ignores non-market economic activities and environmental costs.
(2) measures only nominal output and never measures real output.
(3) includes transfer payments as a part of current production.
(4) records production of goods and excludes services.
(5) excludes all government expenditure on public services.

44. Which of the following statements best explains the multidimensional nature of economic development?
(1) Economic development means an increase in real GDP per capita.
(2) Economic development involves higher income, better living standards and social progress.
(3) Economic development occurs when agricultural sector becomes less important.
(4) Economic development depends mainly on investment in capital.
(5) Economic development is achieved when unemployment, poverty and inflation are low.

[*see page eight*

45. The income Gini coefficient of a country rises from 0.39 in Year 1 to 0.44 in Year 2. What combination of changes in government social protection and tax policy is likely to have caused the increase in the Gini coefficient?

	Transfers to Low-income households	**Marginal Personal Income Tax rate**
(1)	Decrease	Decrease
(2)	Increase	Unchanged
(3)	Increase	Increase
(4)	Unchanged	Increase
(5)	Increase	Unchanged

46. Which of the following statements correctly distinguishes income poverty from multidimensional poverty?
(1) Income poverty focuses only on food expenditure, while multidimensional poverty focuses only on education.
(2) Income poverty measures lack of sufficient income, while multidimensional poverty measures deprivations in several dimensions of life.
(3) Income poverty is calculated only by the World Bank, while multidimensional poverty is calculated only by the United Nations Development Programme.
(4) Income poverty excludes health and education, while multidimensional poverty excludes health and living standards.
(5) Income poverty focuses only on consumption, while multidimensional poverty focuses only on inflation adjusted wage rate.

47. Which of the following statements best describes the current demographic change in Sri Lanka according to the Census of Population and Housing 2024?
(1) Population growth driven mainly by high natural increase and high fertility.
(2) A rapid increase in the share of children due to higher fertility rates.
(3) A growing percentage of elderly people due to lower birth rates and longer life expectancy.
(4) A declining dependency ratio caused by a sharp increase in the working-age population.
(5) A reduction in the median age due to rising birth rates.

48. According to the latest official data, Sri Lanka's Gross Domestic Product per capita in 2025 was US dollars
(1) 4 428. (2) 4 546. (3) 4 910. (4) 5 003. (5) 5 010.

49. A major risk to Sri Lanka's future economic growth prospects is
(1) declining competitiveness in export-oriented industries and related sectors.
(2) increasing pressure from an aging population on public finance.
(3) weak productivity growth in the industrial sector and associated services.
(4) persistent weakness in private investment confidence across the economy.
(5) global trade uncertainties, external shocks and delayed implementation of structural reforms.

50. Which policy measure would most effectively strengthen Sri Lanka's resilience against external shocks?
(1) Providing extensive subsidies to import-dependent industries to maintain production levels.
(2) Maintaining a fixed exchange rate through continuous interventions in the foreign exchange market.
(3) Building foreign exchange reserves while diversifying export products and export destinations.
(4) Increasing reliance on short-term external borrowing to finance development expenditure.
(5) Raising tariffs on all imported goods to reduce exposure to global market fluctuations.

* * *

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අධ්‍යයන පොදු සහතික පත්‍ර (උසස් පෙළ) විභාගය, 2026
கல்விப் பொதுத் தராதரப் பத்திர (உயர் தர)ப் பரீட்சை, 2026
General Certificate of Education (Adv. Level) Examination, 2026

ආර්ථික විද්‍යාව II
பொருளியல் II
Economics II

21 E II

පැය තුනයි
மூன்று மணித்தியாலம்
Three hours

අමතර කියවීම් කාලය - මිනිත්තු 10 යි
மேலதிக வாசிப்பு நேரம் - 10 நிமிடங்கள்
Additional Reading Time - 10 minutes

Use additional reading time to go through the question paper, select the questions you will answer and decide which of them you will prioritise.

Instructions:
* *Answer **five** questions only, selecting minimum of **two** questions from Sub section '**A**' and **two** questions from Sub section '**B**'.*
* *Graph papers will be provided.*

Sub section 'A'
(*Select minimum of **two** questions from this section.*)

1. (i) Explain how scarcity transforms natural resources into economic goods. Use water or air as an example to explain your answer. (03 marks)

(ii) Should digital goods (e.g. software, e-books) be classified as economic goods or quasi-free goods? Explain your answer. (04 marks)

(iii) State **four** major functions performed by the entrepreneurs in the production process. (04 marks)

(iv) Explain how the price mechanism allocates scarce resources in a market economic system. (04 marks)

(v) Mention **five** key characteristics of Sri Lanka's economy that demonstrate its nature as a mixed economic system. (05 marks)

2. (i) Suppose the supply function of a firm is given as $Q_s = -40 + 10P$.

(a) Determine the quantity supplied when price equals Rs. 10 per unit. (01 mark)

(b) What would be the minimum price required for quantity supplied to become positive? (02 marks)

(ii) (a) State the underlying assumptions of the Law of Demand. (02 marks)

(b) Mention the circumstances under which the Law of Demand may not hold. (02 marks)

(iii) Name **three** factors that determine whether consumers will significantly reduce quantity purchases following the price increase of a commodity. (03 marks)

(iv) Analyse why the supply of agricultural goods is generally less price elastic than software supply. (04 marks)

(v) Suppose the price of bread rises from Rs. 140 to Rs. 180 per loaf, while all other factors affecting demand, including consumers' income remain constant.

(a) Using a diagram, explain the substitution effect and the income effect associated with the price change, assuming that bread is a Giffen good. (03 marks)

(b) Mention **three** conditions necessary for Giffen-type consumer behaviour to occur. (03 marks)

[See page two

3. (i) (a) Define a 'black market'. (02 marks)

(b) Using **two** examples, explain how government interventions in markets may create black markets. (04 marks)

(ii) Analyse the following impact of a unit subsidy to the producer of a consumer good using a diagram.

(a) Economic surplus

(b) Cost to the government

(c) Deadweight loss (DWL) (02 × 3 = 06 marks)

(iii) Suppose the government imposes a minimum price of Rs. 50 per unit of a commodity sold in a competitive market where demand and supply functions are represented by the following equations.

$Q_D = 200 - 2P$ $Q_S = -40 + 4P$

(a) Calculate the consumer surplus before and after the imposition of minimum price in the market. (04 marks)

(b) Calculate the producer surplus before and after the imposition of minimum price assuming that there is no excess supply in the market. (04 marks)

4. (i) Using a diagram, illustrate the **three** main stages of the short run production function. (03 marks)

(ii) (a) What is meant by economies of scale? (01 mark)

(b) Distinguish between internal and external economies of scale. (02 marks)

(iii) A perfectly competitive firm operating in the short run has the following information on its current cost and revenue levels:

Average Variable Cost (AVC) = Rs 90
Average Total Cost (ATC) = Rs. 115
Market price per unit = Rs. 100.

(a) Should the firm continue production in the short run? Explain your answer. (02 marks)

(b) Is the firm earning profit or loss? Explain your answer. (02 marks)

(iv) A garment manufacturing firm sells garments worth of Rs. 16 million annually. The following annual costs are incurred by the firm.

Item	Value (Rs.)	Item	Value (Rs.)
Raw materials	3 500 000	Interest paid to banks	1 000 000
Wages	3 000 000	Owner's capital invested in the firm	10 000 000
Rent paid	120 000	Market interest rate	12%
Insurance	500 000	Annual salary forgone by owner	1 800 000
Utilities	880 000		

Using the above information calculate the following:

(a) Total explicit cost

(b) Total implicit cost

(c) Total economic cost

(d) Accounting profit

(e) Economic profit (02 × 5 = 10 marks)

[See page three

5. (i) (a) Define the concept of 'production boundary' used in the preparation of national accounts. (02 marks)

(b) Explain why household cooking is excluded, while food served by restaurants is included, in the calculation of Gross Domestic Product. (03 marks)

(ii) The Table below presents some data pertaining to national accounts of a hypothetical economy.

Item	Value (Rs. Million)
Gross Value of Output at basic price (GVO)	30 000
Intermediate consumption	5 000
Compensation of employees	6 000
Gross Mixed Income	8 500
Other Taxes less subsidies on production	500
Taxes less subsidies on products	1 000

(a) Calculate the Gross Domestic Product. (02 marks)

(b) Calculate the Gross Operating Surplus. (02 marks)

(iii) The following are some macroeconomic data for a hypothetical economy:

$C = 300 + 0.8\ Yd$; $I = 250$; $G = 150$; $T = 100$;

Full employment income level = 3 500 (All values are in Rs. million).

(a) Calculate equilibrium national income level. (02 marks)

(b) Determine the magnitude of economy's inflationary gap or deflationary gap. (02 marks)

(c) Estimate the required change in government taxes to achieve full employment. (02 marks)

(iv) (a) What is meant by inventories? (02 marks)

(b) Briefly explain the difference between aggregate expenditure and aggregate demand. (03 marks)

Sub section 'B'

(*Select minimum of **two** questions from this section.*)

6. (i) An economy records the following annual inflation rates for the last four years:

Year 1 = 16%; Year 2 = 10%;

Year 3 = 4%; Year 4 = −3%;

State the periods of inflation, disinflation, and deflation according to this data. (03 marks)

(ii) (a) Define demand-pull inflation and cost-push inflation. (02 marks)

(b) Using aggregate demand and aggregate supply analysis, explain how each type of inflation occurs. (04 marks)

(iii) The Table below presents items in the Balance Sheet of a commercial bank:

Item	Value (Rs. Million)	Item	Value (Rs. Million)
Cash reserves	100	Fixed assets	50
Time deposits	200	Savings deposits	250
Capital	50	Loans and advances	800
Government securities	150	Demand deposits	600

(a) Prepare the Balance Sheet of this commercial bank. (02 marks)

(b) Calculate the total liquid assets of this commercial bank. (01 mark)

(c) Calculate the total deposits of the commercial bank. (01 mark)

(iv) (a) What are the components of reserve money in Sri Lanka? (03 marks)

(b) Explain how the Central Bank can contract reserve money. (04 marks)

[See page four

7. (i) (a) Define merit goods and demerit goods. (02 marks)
(b) Explain why merit goods are under-consumed in a free market. (02 marks)
(ii) State **three** major sources of government tax revenue in Sri Lanka. (03 marks)
(iii) Examine the economic justification for state-owned enterprises. (03 marks)
(iv) Some annual data pertaining to public finance of a hypothetical economy is given below.

Item	Value (Rs. Billion)
Total Revenue	5 400
Grants	100
Gross financing needs	2 400
Interest Payments	2 500
Capital and Net Lending	1 200
Amortization Payments	1 600

Using above data calculate the following:
(a) Overall fiscal balance (b) Total recurrent expenditure
(c) Primary expenditure (d) Primary balance
(e) Recurrent account balance (02 × 5 = 10 marks)

8. (i) (a) Distinguish between static comparative advantage and dynamic comparative advantage. (02 marks)
(b) Name **four** ways a government can develop dynamic comparative advantages of a country. (04 marks)
(ii) (a) State **three** reasons why developing countries adopt protectionist policies. (03 marks)
(b) Distinguish between nominal protection and effective protection. (02 marks)
(iii) Explain how Sri Lanka's export concentration and import dependence increase its vulnerability to global shocks. (04 marks)
(iv) (a) Name **three** important factors that contributed to the depreciation of Sri Lankan rupee against the US dollar during the first half of 2026. (03 marks)
(b) State **two** measures taken by the Central Bank and the government of Sri Lanka to reduce the pressure on the exchange rate during this period. (02 marks)

9. (i) Define economic development. (03 marks)
(ii) Describe why development cannot be measured only through increases in national income. (04 marks)
(iii) Examine why multidimensional poverty is higher in the estate and rural sectors of Sri Lanka. (04 marks)
(iv) Explain whether Sri Lanka is currently experiencing a 'middle-income trap' or not. (04 marks)
(v) Analyse the long term implications of low birth rate for labour supply and economic growth in Sri Lanka. (05 marks)

10. (i) "The Western Province contributes a disproportionately large share of Sri Lanka's Gross Domestic Product, while other provinces contribute relatively smaller shares." State **five** reasons why economic activities are concentrated in the Western Province. (05 marks)
(ii) What are the economic consequences of climate-related disasters on the developing economies such as Sri Lanka? (05 marks)
(iii) Explain the importance of strengthening the agricultural sector as a part of Sri Lanka's long-term development strategy. (05 marks)
(iv) Describe briefly how digitalization can support Sri Lanka's economic growth. (05 marks)

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