KASNEB
CPA
Economics

26th May 2014

QUESTION ONE

a)
   i. Briefly explain the term "credit creation" (2 marks)
   ii. Explain four factors that limit the effectiveness of credit creation by commercial banks. (8 marks)

b) Outline seven limitations of the quantity theory of money. (7 marks)

c) The demand function of a certain product is given as follows:

$Q=100-5P$

Where: Q is the level of output
P is the unit price

Required:
The point elasticity of demand when unit price is Sh. 10. Interpret your result (3 marks)

(Total 20 marks)

QUESTION TWO

a) Differentiate between "partial equilibrium analysis" and "general equilibrium analysis" as used in economics. (2 marks)

b) Explain three exceptions to the law of demand. (6 marks)

c) With the aid of well labeled diagrams, analyze the effects of each of the following situations on the market equilibrium price and quantity of orange fruit.
   i. Where there is a fall in the price of mango fruit which is a substitute of orange fruit. (4 marks)
   ii. Where the government initiates an effective promotional campaign aimed at boosting the sales of orange fruit. (4 marks)
   iii. Where there is a severe drought that has led to poor yield of orange fruit. (4 marks)

(Total 20 marks)

QUESTION THREE

a) Highlight four causes of cost-push inflation in an economy. (4 marks)

b) Suggest eight non-monetary measures that could be used to curb unemployment in developing countries. (8 marks)

c) The demand and average cost functions of a certain firm are given by

$Q-90+2P=0$
And
$AC=Q^2-8Q+57+2Q^{-1}$

Where: Q is the level of output
P is the unit price

Required:

The level of output that will maximize profit. (8 marks)

(Total 20 marks)

QUESTION FOUR

a)

i. Explain the law of variable proportions. (2 marks)

ii. Enumerate four assumptions underlying the law of variable proportions. (4 marks)

b) "A government might intervene in a free market economic system". Discuss five reasons that might drive a government to intervene. (5 marks)

c) With the aid of appropriate diagrams, describe three properties of indifference curves. (9 marks)

(Total 20 marks)

QUESTION FIVE

a)

i. Briefly describe a deflationary gap. (2 marks)

ii. Illustrate how fiscal policy might be used to control a deflationary gap in an economy. (4 marks)

b) Outline four limitations of the theory of comparative advantage. (4 marks)

c) Discuss five cannons of a good taxation system. (10 marks)

(Total 20 marks)

QUESTION SIX

a) Analyze five measures that could be adopted by developing countries to promote exports of goods and services. (10 marks)

b) Discuss the role played by the International Monetary Fund (IMF) in developing countries. (10 marks)

(Total 20 marks)

QUESTION SEVEN

a) Enumerate five sources of external economies of scale. (5 marks)

b) Describe four ways in which a government could influence the allocation of economic resources in a country. (8 marks)

c) The data provided below represents the national income model of a hypothetical country in trillions of shillings:

C=50+0.6(Y-T)

1=35

G=25

T=20

X=30

M=8+0.1Y

Where: C=Consumption expenditure

Y=National Income

T=Taxes

I=Investments
G=Government expenditure
X=Exports
M=Imports

Required:

i. The equilibrium level of national income. (3 marks)

ii. The multiplier (2 marks)

iii. The equilibrium level of consumption expenditure (2 marks)

(Total 20 marks)