KASNEB
CPA
ECONOMICS

25TH MAY 2015

QUESTION ONE

a) Differentiate between "microeconomic theory" and "macroeconomic theory". (2 marks)
b) Explain the three basic economic problems. (6 marks)
c) Outline six limitations of a free market economy. (6 marks)
d) The demand and supply of houses in a certain city are represented by the following function (in thousands):

$$Qd=100-2P$$
$$Qs=50+5P$$

Where: Qd is the quantity demanded
Qs is the quantity supplied P
is the rental price per house

Required:

i. The equilibrium price and quantity. (4 marks)
ii. Evaluate the effect of a renatl price ceiling set by the rental control board at Sh. 6,500 per house. (2 marks)

(Total: 20 marks)

QUESTION TWO

a)
i. Explain the term "elasticity of supply". (1 mark)
ii. Summarise three applications of elasticity of supply in economic decision making. (3 marks)

b) Using a relevant diagram, explain the relationship between the price and quantity demanded of a normal good. (4 marks)
c) Describe three limitations of the cardinal approach of measuring consumer utility. (6 marks)
d) With the aid of a well labeled diagram, discuss the concept of consumer surplus. (6 marks)

(Total: 20 marks)

QUESTION THREE

a) Outline six contributions of industry in the economic development of developing countries (6marks)
b) Highlight six reasons why most developing have failed to realize the benefits of international trade. (6 marks)
c) Examine eight consequences of unemployment. (8 marks)

(Total: 20 marks)

QUESTION FOUR

a) State five criticisms of the marginal productivity theory of wage discrimination. (5 marks)

b) With the aid of well labeled diagrams, analyse the effects of each of the following situations on wage rate and employment level.

i. **Introduction** of a minimum wage rate by the government (5 marks)

i. An increase in the school leaving age coupled with a reduction in the retirement age. (5 marks)

ii. A recession in the economy. (5 marks)

(Total: 20 marks)

QUESTION FIVE

a) Explain three motives of holding money as advanced by the Keynesian liquidity preference theory. (6 marks)

b) With the aid of diagram describe the effect of increase in income to the equilibrium level in the money market. (6 marks)

c) The following information relates to the commodity and money markets of a certain closed in millions of shillings:

$C=300+0.6Y$

$I=1800-10r$

$MDT=0.4Y$

$MDs=20-10r$

$Ms=1200$

Where: C=Consumption function

Y=National **Income**

I=Investments function

r=rate of interest

MDT=Precautionary and transactionary demand for money

MDs=Speculative demand for money

Ms=money supply

Required:

i. The LM Function (2 marks)

ii. The IS Function (2 marks)

iii. The equilibrium level of interest rate (2 marks)

iv. The equilibrium level of national income (2 marks)

(Total: 20 marks)

QUESTION SIX

a) Describe the effect of inflation on each of the following:

i. Exchange rate (2 marks)

ii. Interest rate (2 marks)

iii. Balance of payments (2 marks)

iv. National income (2 marks)

b) Enumerate four causes of a budget deficit in an economy. (4 marks)

c) Discuss four ways in which a country could finance its public sector expenditure. (8 marks)

(Total: 20 marks)

QUESTION SEVEN

a) **Illustrate** the loss making level of output of a firm operating under perfect competition. (5 marks)

b) Outline eight factors that could hinder economic development in developing countries. (8 marks)

c) The following information relates to the national income statistics of a hypothetical economy in billions of shillings:

Personal income taxes	5,000
Price index	250
Undistributed profits	3,000
Business taxes	4,000
Transfer payments	8,000
Social security contributions	11,000
Subsidies	4,000
Consumer expenditure	75,000
Net property income from abroad	1,000
Taxes on expenditure	18,000
Depreciation allowance	15,000
Export of goods and services	36,000
Gross domestic fixed capital formation	24,000
Government expenditure	28,000
Import of goods and services	38,000

Required:

i. Gross national product at market price (2

ii. Disposable income marks)

iii. Real gross national product (2 marks)

(Total: 20 marks)