



**CPA FOUNDATION LEVEL**

**CIFA FOUNDATION LEVEL**

**ECONOMICS**

**December 2021.**

**Time Allowed: 3 hours.**

**Answer any FIVE questions.**

**ALL questions carry equal marks.**

**QUESTION ONE**

- (a) (i) Explain the concept of “consumer sovereignty” as applied in economic analysis. (2 marks)
- (ii) Highlight five factors that limit consumer sovereignty. (5 marks)
- (iii) ABC limited has been incurring losses over the last few years despite its monopolparastatal status.
- Using a well-illustrated diagram, demonstrate how a monopolist can make losses in the short-run. (5 marks)
- (b) Discuss the four main goals of macroeconomic policy in developing countries. (8 marks)
- (Total: 20 marks)**

**QUESTION TWO**

- (a) Highlight the characteristics of public goods. (5 marks)
- (b) The following economic functions have been derived from the Kenya Coffee Millers Limited:
- $$Q_a = 3p^2 - 4p \text{ and}$$
- $$Q_b = 24 - p^2; \text{ where } p \text{ represents price and } Q \text{ is quantity}$$

**Required:**

- (i) Which of the two functions represents a demand curve and supply curve. Cite relevant economic reasons. (4 marks)
- (ii) Determine the equilibrium price and quantity in the market (6 marks)
- (iii) Explain, with the aid of a diagram, the effect on the demand and supply functions indicated in (a) above of a simultaneous decrease in cost of inputs and a decrease in the price of a substitute good. (5 marks)
- (Total: 20 marks)**

**QUESTION THREE**

- (a) Explain the term ‘Price control’. (4 marks)
- (b) Explain the circumstances under which price control is considered necessary. (5 marks)

The utility total function and other relevant variables related to a consumer are given as follows:

$$U = 20X - 4Z^2 + 40Z - X^2$$

Income  $Y = \text{Kshs. } 48$

Price of  $X (P_x) = \text{Kshs. } 2$

Price of  $Z (P_z) = \text{Kshs. } 4$

**Required:**

- (i) Determine the equilibrium quantities of commodities  $x$  and  $z$  using the cardinalist approach to consumer behavior. (6 marks)
- (ii) Outline the axioms of the cardinalist approach to consumer behavior. (5 marks)
- (Total: 20 marks)**

#### QUESTION FOUR

- (a) Explain the importance of elasticity of supply in decision making. (6 marks)
- (b) Examine five factors that limit the effectiveness of the monetary policies in developing countries. (5 marks)
- (c) You are given the following information about the commodity and Money markets of a closed economy without government intervention:

The commodity market Consumption function:

$$C = 50 + \frac{2}{5}Y$$

Investment function:

$$I = 790 - 21r$$

The Money Market:

Precautionary and Transactions demand for money  $MDT = \frac{1}{6}Y$

Speculative demand for money  $MDS = 1200 - 18r$

Money supply  $MS = 1250$

#### Required:

- (i) Determine the equilibrium levels of income and interest rate for this economy. (6 marks)
- (ii) Using a well labeled diagram, illustrate the equilibrium condition in part (i) above. (3 marks)

**(Total: 20 marks)**

#### QUESTION FIVE

- (a) Explain the meaning of mobility of factors of production and highlight the significance of factor mobility. (6 marks)
- (b) Outline the economic policy recommendations that would reduce regional development imbalances in developing countries. (6 marks)

The table below represents economic transactions for country XYZ in billions of shillings:

|               | Total output | Intermediate purchases |
|---------------|--------------|------------------------|
| Agriculture   | 130          | 110                    |
| Manufacturing | 170          | 145                    |
| Services      | 155          | 125                    |

#### Required:

- (i) Calculate the Gross National Product of this economy using the value added approach. (4 marks)
- (ii) If depreciation and indirect taxes equal 8 billion and 7 billion shillings respectively, find the Net Domestic Product both at Market prices and at factor cost. (4 marks)

**(Total: 20 marks)**

#### QUESTION SIX

- (a) Explain the term 'Oligopoly'? (2 marks)
- (b) Analyse the challenges facing the formation of "cartels" in the oligopoly market structure. (8 marks)
- (c) Citing reasons, suggest why rising inflation is a major cause of concern in developing countries. (10 marks)

**(Total: 20 marks)**

#### QUESTION SEVEN

- (a) Outline the main causes for the rise in the unemployment levels in developing countries. (5 marks)
- (b) Suggest the possible remedy measures to contain unemployment crisis in developing countries. (7 marks)
- (c) Explain the likely challenges facing currency demonetization in your country. (8 marks)

**(Total: 20 marks)**

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