KASNEB
ATD LEVEL III
PRINCIPLES OF ECONOMICS

MONDAY: 23 May 2016.

Answer any FIVE questions.

Time Allowed: 3 hours.

All questions carry equal marks.

QUESTION ONE
(a) Explain the following terms:

(i) Actual economic growth. (2 marks)
(ii) Potential economic growth. (2 marks)

(b) Highlight six externalities associated with increase in economic growth in a country. (6 marks)

(c) Describe five factors that limit the efficient operation of a free market economy. (10 marks)
(Total: 20 marks)

QUESTION TWO
(a) Define the term “cross elasticity of demand” as used in economics. (2 marks)

(b) The table below shows the quantity supplied of a certain commodity at different price levels:

<table>
<thead>
<tr>
<th>Unit Price (Sh.)</th>
<th>60</th>
<th>50</th>
<th>40</th>
<th>30</th>
<th>20</th>
</tr>
</thead>
<tbody>
<tr>
<td>Quantity supplied (units)</td>
<td>6,000</td>
<td>5,500</td>
<td>4,500</td>
<td>3,000</td>
<td>0</td>
</tr>
</tbody>
</table>

Required:
The elasticity of supply of the commodity when the unit price decreases from Sh.50 to Sh.30. Interpret your result. (5 marks)

(c) Enumerate six factors that determine the own price elasticity of demand. (6 marks)

(d) (i) Using an appropriate diagram, explain the law of diminishing marginal utility. (4 marks)

(ii) Outline three exceptions to the law of diminishing marginal utility. (3 marks)
(Total: 20 marks)

QUESTION THREE
(a) Highlight six factors that determine the level of savings in an economy. (6 marks)

(b) State six problems that are faced by the industrial sector in developing countries. (6 marks)

(c) Summarise eight measures that could be adopted to boost the agricultural sector in developing economies. (8 marks)
(Total: 20 marks)

QUESTION FOUR
(a) With the aid of well labelled diagrams, describe the profit maximising level of output and price for a firm operating under monopolistic competition in the:

(i) Short-run period. (6 marks)
(ii) Long-run period. (6 marks)

(b) The following data relate to a certain commodity in the market:

\[ P = 68 - 4Q_d - Q_d^2 \]
\[ P = 12 + 2Q_s + Q_s^2 \]
Where: 
P is the price of the commodity.
Qd is the quantity demanded.
Qs is the quantity supplied.

Required:
The equilibrium price and quantity of the commodity.

**QUESTION FIVE**
(a) Examine six functions of money in an economy. (6 marks)
(b) Discuss three roles of the central bank of a country. (6 marks)
(c) Analyse four factors that could limit the effective application of the accelerator in an economy. (8 marks)

(Total: 20 marks)

**QUESTION SIX**
(a) The data below relate to the demand and total cost functions of a firm operating under perfect competition:

\[
P = 150 \\
TC = 30 - 15Q^2
\]

Where: 
P = Price 
Q = Output 
TC = Total Cost

Required:
(i) Average fixed cost function. (2 marks)
(ii) Average variable cost function. (2 marks)
(iii) Marginal revenue function. (2 marks)
(iv) The profit maximising level of output. (4 marks)

(b) Discuss five criticisms levelled against the use of national income statistics. (10 marks)

(Total: 20 marks)

**QUESTION SEVEN**
(a) Describe four types of mobility of labour that could be experienced in an economy. (8 marks)
(b) Using appropriate diagrams, analyse the profit maximising level of output for a firm operating in a perfectly competitive market structure:

(i) In the short-run period. (6 marks)
(ii) In the long-run period. (6 marks)

(Total: 20 marks)