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ATD LEVEL III

PRINCIPLES OF ECONOMICS

MONDAY: 21 May 2018. **Time Allowed: 3 hours.**

Answer any FIVE questions. **ALL questions carry equal marks.**

QUESTION ONE

(a) Summarise four uses of a production possibility curve. (4 marks)

(b) Differentiate between "stable market equilibrium" and "unstable market equilibrium". (4 marks)

(c) Outline four conditions that must be fulfilled for consumer rationality to exist. (4 marks)

(d) Discuss four applications of the concept of elasticity of demand in an economy. (8 marks)

(Total: 20 marks)

QUESTION TWO

(a) Highlight four functions of money. (4 marks)

(b) Explain three reasons why the elasticity of supply of agricultural goods is ever low. (6 marks)

(c) A rational firm in a competitive market has the demand structure and total cost function represented by:

Demand, $P = 50$

Total cost, $TC = 10 + 5Q^2$

Where: P = Price
TC = Total cost
Q = Quantity

Required:

(i) Average fixed cost function. (2 marks)

(ii) Average variable cost function. (2 marks)

(iii) Marginal cost function. (2 marks)

(iv) The profit maximising level of output. (2 marks)

(v) Maximum profit. (2 marks)

(Total: 20 marks)

QUESTION THREE

(a) (i) Define the term "capital" as a factor of production. (2 marks)

(ii) Summarise four roles of capital in economic development. (4 marks)

(b) Highlight four factors that might lead to increasing return to scale in the production process. (4 marks)

(c) Differentiate between "marginal cost" and "marginal revenue". (4 marks)

(d) Describe three circumstances under which the concept of opportunity cost is applicable in an economy. (6 marks)

(Total: 20 marks)

QUESTION FOUR

(a) (i) Define the term "fiscal policy". (2 marks)

(ii) List four instruments of fiscal policy. (4 marks)

(b) Outline six objectives of fiscal policies in an economy. (6 marks)

(c) The following data relate to a hypothetical economy of country Zed:

	Sh. "million"
Imports	3,000
Exports	5,000
Autonomous consumption	30,000
Government spending	24,000
Investment	6,000

Required:
The equilibrium national income of country Zed, given that the country's marginal propensity to save is 0.4. (8 marks)

(Total: 20 marks)

QUESTION FIVE

(a) Summarise five benefits of economic growth and development to an economy. (5 marks)

(b) Enumerate five factors that could limit credit creation by commercial banks. (5 marks)

(c) Explain the effects of high interest rates on:

(i) Investments. (2 marks)

(ii) Inflation. (2 marks)

(iii) Employment. (2 marks)

(iv) Exchange rate. (2 marks)

(v) National income. (2 marks)

(Total: 20 marks)

QUESTION SIX

(a) With the help of a well labelled diagram, using indifference curve analysis, derive the demand curve for a normal good. (8 marks)

(b) Outline six salient features of a firm operating under oligopoly market. (6 marks)

(c) (i) Explain the term per capita income. (2 marks)

(ii) Highlight four uses of per capita income. (4 marks)

(Total: 20 marks)

QUESTION SEVEN

(a) Explain the term "money illusion". (2 marks)

(b) With the help of a diagram, explain inelastic supply. (4 marks)

(c) (i) Define the term "economic planning". (2 marks)

(ii) Suggest six policy measures that could be implemented to combat poverty in developing countries. (6 marks)

(d) The market demand and supply functions of commodity **X** are given below:

$Q_d = 50 - 2P$

$Q_s = -40 + 3P$

Where: Q_d is the quantity demanded
Q_s is the quantity supplied
P is the price

Required:
The equilibrium price and quantity of commodity **X**. (6 marks)

(Total: 20 marks)

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