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Economics paper 1 set 11 and marking guide

1. (a) (i) Given that an increase in the price of commodity **X** from Shs. 1500 to Shs. 1800 resulted into a change in quantity demanded for commodity **Y** from 600 units to 570 units; calculate the cross elasticity of demand. (2marks)

$$\text{C.E.D} = \frac{\% \text{change in Qty demanded of } Y}{\% \text{ change in price of } X} = \left(\frac{570-600}{570} \times 100 \right) \div \left(\frac{180-150}{150} \times 100 \right) = -0.25$$

- (ii) State the relationship between commodities **X** and **Y**. (02 marks)

X and y are complimentary goods, **OR** Jointly demanded goods

- (b) (i) What is meant by a mixed economy? (01 mark)

A mixed economy is one where the resources are owned and controlled by both the state (central Authority/Public) and the private sector (market forces of demand and supply).

- (ii) Give any three merits of a mixed economy. (03 marks)

- Limited resource wastage due to regulated competition.
- Better quality products are produced because of competition between the private and public sectors.
- Production of a wide variety of products by both the private and public sector.
- Reduced income inequalities due to state control.
- Individuals self-interests are regulated e.g. Over exploitation of resources.
- It increases employment opportunities in both the private and public sectors.
- The public sector provides essential services that the private sector would not provide.
- There is economic stability due to government intervention.

- (c) (i) Distinguish between average product and marginal product. (02 marks)

Average product is the output produced per unit of a variable factor employed e.g. Labour.

While

Marginal product is the change in total output resulting from employing an additional unit of a factor input e.g. Labour.

OR

Marginal product is the additional/extra output produced by an additional unit of a factor employed e.g. Labour.

- (ii) State any two factors that may lead to an increase in marginal product of labour.

Factors that may lead to increase in marginal product of labour;

- Increase in wage rate
- Improvement in technology
- Increase in the level of education /training/skills
- Improvement in the quality of management and supervision
- Increase in the availability and quality of co-operant factors
- Improvement in the working conditions
- Improvement in attitude of labour towards work.
- Increase in the level of specialization and division of labour.
- Improvement in political climate.
- Improvement in health conditions of the workers.

(d) (i) State Irving Fisher's equation of exchange. (02 marks)

$$MV = PT \text{ or } P = \frac{MV}{T}$$

Where M = amount of money in circulation /money supply

V= velocity of circulation money

T = level of transaction/volume of product/level of output

P = general price level/average price

(ii) How is the value of money determined in Fisher's equation of exchange? (02 marks)

- The quantity of money in circulation/money supply.
- The velocity of circulation of money
- The level of transactions/volume of production/level of output
- The price level/General price level/Average price

(e) (i) Define the term regressive tax. (01 mark)

A regressive tax is one whose rate falls/reduces as income (spending power) increases i.e. it takes a higher proportion of income of the low income earner than high income earners.

(ii) State any three effects of regressive taxes in an economy. (03 marks)

- They encourage hard work among the poor.
- They widen the income gap between the poor and the rich.
- They limit consumption of consumer goods/reduce standards of living among the poor.
- Low revenue realized by the government.
- They discourage savings and investment among low income earners.
- They lead to social unrest/political discontent.
- Resentment among the low income earners/the poor.
- They encourage tax evasion and avoidance among the poor
- They promote saving among the rich

SECTION B

2. (a) State the Malthusian population theory.

Malthusian population theory states that whereas **population grows at a geometric rate**, food production tends to grow at **an arithmetic rate**.

Malthus stated that due to the above trend, **population growth after a time would outstrip food production (population trap)** and after such a time, there was a need for control of population growth through preventive (negative) checks like moral restraint, celibacy etc. otherwise positive checks like pestilence, wars, and diseases would serve to reduce the population.

(b) Explain five ways in which the Malthusian population theory is relevant to developing countries. (10 marks)

Ways in which the theory is relevant to LDCs;

- Land supply being fixed and subject to the law of diminishing returns is what is being experienced and he envisaged this situation.
- Natural family planning methods/control measures like celibacy are being used; these control measures are his initiation (Negative checks).
- The positive checks on the population exist in LDCs to day e.g. epidemic, wars, etc.
- Some areas of LDCs are facing food shortage/famine
- Existence of a subsistence sector which is still large in LDCs.

(c) State six limitations of the theory (06 marks)

- It assumes constant technology which is unrealistic since technology is ever changing/technological progress occurs.
- It assumes a closed economy, yet economies of most LDCs are open economies. He ignored the roles of international trade
- Agricultural modernization is not foreseen by the theory yet this takes place in most LDCs.
- Failure of the theory to visualize labour mobility
- Population growth does not depend on food alone.
- The theory is based on the subsistence economy yet LDCs economies are not predominantly subsistence any longer.
- The theory did not foresee great improvement in transport.
- It did not foresee the possibility of getting foreign aid/Resource from other countries.
- There is no mathematical relation regards growth in food and population.
- The theory ignored the deliberate and scientific methods of birth control/modern family planning methods.
- It did not realize that rising living standards can cause a fall in birth rates and population.
- It ignored the possibility emigration to ease pressure on resources.
- Malthus was influenced by the law of diminishing returns which is not always true/which only operates in the short run.
- Negative checks suggested by him are unrealistic due to human behaviour.

Note: Giving of assumptions is irrelevant.

3. (a) Why do prices of agricultural products fluctuate? (10 marks)

- Long gestation period
- Heavy dependence on nature/natural factors
- Perishability of agricultural products/storage problems.
- Low price elasticity of demand (inelastic demand) for agriculture products.
- Bulkiness of agricultural products, thus transport problems.
- Low income elasticity of demand for agricultural products.
- Weak bargaining position of LDCs on the world market/External determination of prices.
- Poor Surplus disposal system/machinery e.g. poor infrastructure.
- Divergence between planned and actual output levels.
- Agricultural products forming minor inputs in industrial sector.
- High competition from synthetic fibre
- Raw material saving technology by major consumers.
- High competition among agricultural producers/many producers i.e. making planning difficult/flooding of market
- Lack of co-operant factors among producers of agricultural products
- Change in the cost of production

(b) What are the effects of agricultural price fluctuations in an economy? (0 marks)

- unstable/fluctuating terms of trade

- Unstable export earning
- Balance of payment instabilities
- Planning is made difficult
- Fluctuation of government revenue
- Unstable farmers income
- Fluctuations of employment level
- Worsens income inequality
- Discourages investment in agriculture
- Leads to rural-urban migration
- Cause exchange rate instabilities

4.(a) Explain the differences and similarities between pure monopoly and monopolistic competitive markets

Differences

- In pure monopoly there is only one producer/seller/firm while in competitive monopolistic competitive markets there are many producers i.e. no completion exist in pure monopoly while competition exists in monopolistic competitive markets
- In pure monopoly entry to the market is blocked while in monopolistic competitive market, there is free entry and exit
- In pure monopoly there is no persuasive advertisement while in competitive monopolistic market there is persuasive advertisement
- The demand/average revenue curve in pure monopoly is inelastic while that of competitive monopolistic market is elastic
- In pure monopoly one product without close substitute is produces while in monopolistic competitive market firms produce differentiated products
- In the long run, pure monopoly firms earn abnormal profits while monopolistic competitive markets earn normal profits
- In **pure** monopoly a form practices price discrimination which is not the case in competitive monopolistic market.

Similarities between pure monopoly and monopolistic competitions

- Existence of excessive capacity /produce less than installed capacity.
- The producer/seller/firms in both are price markers
- The demand//AR curves in both are down sloping from left to right
- In firms in both situations earn abnormal profits
- Both market attains equilibrium output at a point where $P = AR$ but greater than $MR = MC$
- In both market situations, there are many byers/customers.

(b) How does existence of monopolistic competitive markets affect producers in Uganda? (06 marks)

- It lead to wastage of resource due to duplication of services/activities.
- They carryout competitive advertisement which leads to high operational costs.
- Production of excess capacity, thus underutilization of resources/produce less than the installed capacity.
- The firms/producers earn normal profits in the long run, which limits expansion of operation.
- Existence of stiff competition leads to collapse of small/inefficient firms.
- Firms earn abnormal profits in the short run which can tie ploughed back/used for expansion.
- Existence of competition leads to production of high quality products i.e. improved innovation and invention.
- The firms are price makers because of having monopoly over their brands.
- Persuasive advertisement enables firms to expand markets for their products.

5.(a) What is the feature of an economic union? (06 marks)

- Strong regional institutions.

- Use of a common currency.
- Sharing of common services.
- Joint economic planning.
- Free movement of goods and services/free trade within the union.
- Free movement of factors of production
- Common external tariff structure
- Harmonized economic policies/joint economic planning.

(b) Explain the factors that limit regional economic integration among the developing countries. (14 marks)

- They tend to produce similar goods and services which limits market
- Failure/fear to share benefits equally
- Fear to lose customs revenue
- Existence of political instabilities in some of the states
- Differences in the levels of development.
- Differences in social factors e.g. culture, religion, language etc.
- Conflicts among leaders.
- Differences in currencies.
- Differences in political ideologies.
- External interference /sabotage.
- Poor infrastructure among the countries in LDCs.
- Differences in economic policies.
- Lack of political support/will/ignorance of the people.
- Limited geographical proximity between countries.
- Difference in the size of market/population.
- Ignorance of the people about the benefits of integration.

Note: State and explain your points in order to get maximum marks for each point

6. (a) What is meant by centralized planning? (04 marks)

Centralized planning is one where the central authority/government/state plans/allocates resources in the whole economy and it directs implementation of plans in line with set targets/objectives.

Or is planning where the central authority plans for the whole economy and it directs implementation of plans in line with set targets.

(b) Explain the rationale for centralized planning in an economy. (16 marks)

- To minimize wastage of resources/efficient allocation of resources
- To ensure proper co-ordination in sectoral development since the private sector is still weak.
- To ensure equitable distribution of resources/to fight income inequality.
- For proper sequencing of operations in the economy
- To solve the problem of shortage of manpower of local/lower levels/district levels.
- To protect national interests.
- To ensure consistency of plans since centralized planning is done in line with the available resources.
- To ensure proportionality and compatibility of plans.
- For easy mobilization of resources.
- To allow regional specialization and thus avoid duplication of development projects.
- For political support.
- To ensure economic stability e.g. price stability.
- To solve unemployment problem.
- To promote self-reliance.

- To achieve a pre-determined rate of economic growth.
- To identify areas suitable for public and private investment.
- To relate present and future trends and targets
- To reduce strain on the local people in terms of mobilization of resource
- To correct deficiencies of price mechanism especially during situations of rapid structural changes.

7. (a) Define the term nationalization of enterprises. (04 marks)

Nationalization of enterprises is where the government deliberately takes over **control and ownership** of privately owned enterprises with or without compensation.

Or refers to the selling of privately owned enterprises to the government/state.

Or refers to the buying of privately owned enterprises by the government/state.

(b) Examine the merits and demerits of nationalization of enterprises in an economy. (16 marks)

Merits of nationalization of enterprises

- Reduces wasteful competition/duplication of activities.
- Encourages large scale production/increased output/economies of scale/economic growth.
- Reduces consumer exploitation by charging affordable prices/provision of public utilities/makes goods available to low income earners.
- Makes it easy to respond to structural changes when need arises.
- Nationalization of private enterprises enables the country get rid of foreign domination with all its associated evils.
- It promotes/ensures/encourages economic stability e.g. price control.
- Promotes equitable distribution of resources/wealth and income.
- It minimizes profit and income repatriation by foreign investors.
- It encourages government to manage vital investment/strategic enterprises.
- Reduces social costs
- It controls private monopoly and its negative effects
- It generates revenue for the government i.e. nationalized industries generate revenue for the government.
- Protects consumers against consumption of undesirable products.
- It increases employment opportunities.

Demerits of nationalization of enterprises

- It leads to inefficiency and therefore production of low quality output.
- Encourages corruption and thus misuse of funds.
- Consumer choice is restricted due to limited variety of goods and services/reduces consumer sovereignty.
- It is associated with bureaucracy and thus slows decision making/Red Tape
- High Government Expenditure on running nationalized enterprises may subject nationals to high taxation.
- Political interference in running of nationalized enterprises e.g. political appointment of managers.
- Leads to low tax revenue.
- Leads to resource misallocation since it interferes with price mechanism .
- Discourages private investment

Thank you

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