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## Economics paper 2 set 13 and marking guide

### SECTION A

*Answer all parts of this question.*

1. (a) (i) Differentiate between transfer earnings and transfer payments. (02 marks)  
(ii) Give any two examples of transfer payments in your country. (02 marks)
- (b) (i) What is meant by the balanced growth strategy of economic development? (01mark)  
(ii) State any three factors that limit the application of the balanced growth strategy in developing countries (03marks)
- (c) State any four features of the agricultural sector in your country. (04 marks)
- (d) (i) Distinguish between a customs union and a common market. (02 marks)  
(ii) State any two benefits of economic integration to your country. (02 marks)
- (e) (i) Differentiate between liquidity ratio and liquidity preference. (02 marks)  
(ii) Mention any two reasons for the high liquidity preference in developing countries. (02 marks)

### SECTION B

*Answer any four questions*

2. (a) Differentiate between location and localization of an industry. (04marks)  
(b) Assess the impact of localization of industries in your country. (16marks)
3. (a) Explain the role of capital in the development of your country. (08marks)  
(b) Discuss the factors that influence capital accumulation in your country. (12 marks)
4. (a) What is meant by a Trade Union? (04marks)  
(b) Explain the challenges faced by Trade Unions in your country. (16 marks)
5. (a) Account for the persistent balance of payments deficits in your Country. (10marks)  
(b) Suggest measures that should be taken to reduce balance of payments deficits in your country (10marks)
6. (a) Explain the causes of unemployment in your country. (10marks)  
(b) Suggest measures that should be taken by the government to reduce unemployment in your country (10marks)
7. (a) Explain importance of taxes in your country. (08marks)  
(b) Discuss the demerits of imposing taxes in your country (12marks)

Guides

Guide

### SECTION A

*Answer all parts of this question.*

1. (a) (i) Differentiate between transfer earnings and transfer payments. (02 marks)

**Transfer earnings** refer to the minimum/lowest payment to a factor of production to keep it in its current employment (use and prevent it from shifting/transferring to the next best /an alternative use).

## Whereas

**Transfer payments** refer to income received by an economic entity without anything given in return. Or payment made to individuals without corresponding goods/services rendered (i.e. they are non- quid pro quo payments).

(ii) Give any two examples of transfer payments in your country. (02 marks)

- Grants/ donations
- Pension
- Sick relief / benefits / allowances and other forms of relief
- Gifts
- Pocket/ upkeep money given to students / relatives/ spouses

(b) (i) What is meant by the balanced growth strategy of economic development? (01mark)

**Balanced growth strategy of economic development** (According to Ragner Nurkes) advocates for harmonious and simultaneous development of investment in all sectors of the economy so that they complement each other and grow in unison/ grow more or less at the same place.

(ii) State any three factors that limit the application of the balanced growth strategy in developing countries (03marks)

- Limited labour skills
- Poor entrepreneurial ability | skills
- Low level of infrastructural development.
- Poor production techniques /low levels of technology
- Small market size
- Conservation
- Poor land tenure system
- Poor political atmosphere
- Low level of accountability / corruption
- Weak planning machinery
- Limited capital
- Unfavourable government policy on investment/ insufficient investment incentives
- Weak inter-sectoral linkages

(c) State any four features of the agricultural sector in your country. (04 marks)

- Highly dependent on family labour
- Mainly small scale
- Mainly rural based
- Mainly uses labour intensive technology
- uses mainly unskilled and semi-skilled labour
- mainly dependent on nature dominated by subsistence production
- mainly low quality of output produced.
- quantity of output produced is generally low
- production is mainly for the local market
- Mainly food stuffs | narrow range of cash crops produced narrow range of production for export

(d) (i) Distinguish between a customs union and a common market. (02 marks)

**Customs Union** is a form of economic integration in which member countries have free trade among themselves and common external barriers / tariffs.

While:

**Common market** is a form of economic integration in which member states have free trade among themselves, common external trade barriers, free mobility of factors of production among themselves.

(ii) State any two benefits of economic integration to your country. (02 marks)

- Trade creation effect
- Leads to specialization and its benefits
- Stimulates industrial development
- Avoids duplication of resources/ goods
- Leads to low average cost of joint research Attracts foreign resources
- Increased resource(s) utilization hence avoiding wastage.
- Improves the bargaining position and understanding among member states
- Creation of employment opportunities
- Production of variety of goods hence widening consumer choices Leads to increased output hence economic growth
- Economies of scale are enjoyed by firms.
- Production of quality output due to competition
- Increased provision of infrastructure at relatively low average cost to each member country.
- Leads to creation of a wide market.

(e) (i) Differentiate between liquidity ratio and liquidity preference. (02 marks)

**Liquidity ratio** is the proportion i percentage of commercial bank (total) deposit that is / must be kept in cash and or near cash form.

While

**Liquidity preference** is the desire by individuals to hold assets/ wealth in cash or near cash form (rather than investing it).

(ii) Mention any two reasons for the high liquidity preference in developing countries. (02 marks)

- Low level of income
- High level of speculation
- High rates of inflation / high price level
- High level of cash transactions
- High degree of uncertainty
- Low level of development of commercial banks and other financial institutions/ poor distribution of banks
- Low interest rates on financial assets
- Limited knowledge of services provided by commercial banks
- Stringent requirement for opening and running accounts
- High level of illiteracy

## SECTION B

Answer any four questions

2. (a) Differentiate between location and localization of an industry. (04marks)

**Location of an industry** - refers to a place or site or point at which an industry/ firms producing related products is/are found / situated / established / set up.

While

**Localization of an industry** is the concentration of firms producing related products/ an industry in an area (in order to reap /enjoy external economies scale / reap advantages of the location).

(b) Assess the impact of localization of industries in your country. (16marks)

**Positive impact of localization in my country.**

- Facilitates infrastructural development in the area
- Creation of more employment opportunities in the area
- Leads to cooperation of the industries in solving common problems
- Development of a pool of skilled labour
- Development of organized markets / expansion of market for products A wide variety of goods produced in the area
- Encourages (forward and backward) linkages.
- Promotes specialization and its advantages Leads to low prices of final products increased revenue to government Increased reputation popularity of an area
- Increased security of the area (in the national interest).
- increased quality of output due to competition Increased output hence economic growth

**Negative impacts of localization:**

- Leads to regional imbalance in development
- Results into rural urban migration and its negative consequences.
- Over strains infrastructures in the area.
- Rise in cost of inputs
- Leads to problem of income inequality
- Quick depletion of resources in an area
- Increased cost of land / high rent rates
- Leads to environmental degradation / pollution (in the area).
- The economy becomes dependent on particular area which is risky /heavy loses to the economy in the event of a catastrophe in the area
- Displacement of people, making many landless.
- Increased cost of labour
- Leads to rising cost of living in the area

3. (a) Explain the role of capital in the development of your country. (08marks)

- **It leads to technological development in form of inventions and innovations.** This leads to the production of goods and services in large quantities and of high quality hence economic growth and development.
- **It increases the standards of living.** This is due to increased incomes of individuals and production of a variety and better quality goods and services which are consumed at lower prices.
- **It facilitates resource exploitation.** This increases production and investments in the industrial, agricultural and service sectors hence economic growth and development.
- **It helps to create employment opportunities in the economy.** This is due to increased investments and production activities in the economy.
- **It facilitates the construction social overheads** in form of roads, railways etc. This increases mobility of factors of production
- **It helps to reduce on the level of inflation in the economy.** The increased production of goods and services helps to meet the high aggregate demand for goods and services. In addition, capital accumulation reduces the supply rigidities associated with the production of goods especially in the agricultural sector. This increases supply in the long run hence economic stability.
- **It helps to solve the balance of payment problems.** This is as a result of increased production of high quality goods and services for export which helps the government to earn more foreign exchange. In addition, capital accumulation leads to establishment of import substituting industries and this reduces on the importation of high valued manufactured goods. Therefore, the gap between export earnings and import expenditure is reduced hence favorable balance of payments.
- **It brings about market expansion** through establishment of social and economic infrastructure. This facilitates trade and economic development.
- **It increases the national income of the country.** This is as a result of increased production and economic activities resulting from capital accumulation.
- **It helps to relieve the country from the burden of the foreign debt.** This is because capital accumulation increases resource exploitation and mobilization which increases the country's capacity to be self-sufficient and reliant.
- **Capital facilitates production of quality goods and service.**
- **Capital facilitates specialization.**

(b) Discuss the factors that influence capital accumulation in your country. (12 marks)

- The level of income
- The rate of inflation
- The level of infrastructural development
- The entrepreneurial ability
- The existing capital stock / .the availability of capital.
- The political atmosphere/ politic I climate
- The techniques of production
- The population growth rate
- The government policy on investment
- The level of monetization of the economy

- The land tenure system
- The market size
- The degree of accountability
- The interest rate on capital/ loans
- Cultural factors / conservatism
- Level of capital inflow and outflow/capital flow
- consumption habits / time preference
- The level of savings

4. (a) What is meant by a Trade Union? (04marks)

Trade unions are labour organizations formed to maximize the well-being of their members by negotiating for better wages and improved working conditions through collective bargaining with employers.

(b) Explain the challenges faced by Trade Unions in your country. (16 marks)

- Disunity of workers
- Poor leadership ability
- Political interference
- Limited fund
- Limited skill of members
- High levels of unemployment.
- Limited membership/low level of unionization.
- Low demand for products produced by members to employ a tool of boycott in their bargaining for salary increase.
- Poor economic performance / low profitability of firms.
- Low demand for labour/High degree of substitutability of labour
- Low level of accountability/ corruption
- Poorly developed infrastructure(s)/ poor communication
- High proportion of wage bill to total costs.
- Apathy / ignorance of workers of their rights.
- Having no other sources of income.

5. (a) Account for the persistent balance of payments deficits in your Country. (10marks)

- **High levels of inflation in developing countries.** Inflation increases production costs and discourages exports by making them expensive. This leads to low demand for exports hence low foreign exchange earnings.
- **Low export prices.** Since developing countries mainly export primary products where prices are low on the world market, they get less foreign exchange earnings hence balance of payment.
- **Excessive reliance on imports in form of consumer and capital goods.** Developing countries import expensive manufactured products leading to high foreign exchange expenditure hence balance of payment deficits.
- **Low productive capacities in developing countries.** This is due to limited co-operant factors used in the production process like limited capital, use of poor technology, unskilled man power etc. This leads to low output for export purposes hence balance of payment deficits.
- **Excessive capital out flow in forms of profit repatriation,** public debt servicing and capital flight by the nationals.

- **Wide spread political instabilities in developing countries.** Political instabilities discourage investments and production which leads to a decline in exports. In addition political instabilities increase expenditure on military equipments which leads to borrowing hence balance of payment deficits.
- **Poor and inadequate social and economic infrastructures .**The existing infrastructure is in a bad state. For example, there exists poor transport, storage and communication facilities which greatly discourage the production and distribution of commodities for export purposes hence balance of payment deficits.
- **Use of poor technology.** This results into inefficiency in resource use and the production of low quantity and poor quality exports which fetch low prices on the world market.
- **Protectionism by developed countries.** The high tariff and non-tariff barriers imposed by developed countries against exports from developing countries lead to a reduction in exports and foreign exchange earnings hence balance of payment deficits.
- **Discovery of synthetic fibers by developed countries.** Synthetic fibers like Nylon, Rayon, silk and the use of raw material saving technology by developed countries have led to a decline in demand for agricultural raw materials from developing countries hence a decline in foreign exchange earnings.
- **11. High population growth rates and dependence burdens.** These force developing countries to import more foodstuffs and medical services in order to support the rapidly growing population. In addition, a rapidly growing population has led to an increase in consumption of commodities which would otherwise be exported hence balance of payment deficits.
- **Existence of natural disasters.** These include floods, drought, pests and diseases which adversely affect the agricultural sector hence a decline in agriculture export and export earnings.
- **High levels of corruption and embezzlement of scarce economic resources.** Resources meant for domestic and export production and embezzled for personal gain. This increases government expenditure on unproductive public enterprises forcing the government to keep on importing hence balance of payment deficits.
- **Limited economic diversification by developing countries.** Developing countries tend to concentrate on the production and exportation of a few traditional cash crops which face unfavorable terms of trade on the world market hence balance of payment deficits.

(b) Suggest measures that should be taken to reduce balance of payments deficits in your country (10marks)

- Adaptation to import substitutes to reduce import loss of foreign exchange
- Trade restrictions to reduce dumping
- Reduce corruption and swindling of government revenues
- Devaluation policy to promote consumption of local products as the imports become expensive
- Manpower planning to reduce expenditure on expatriates
- Barter trade arrangement to minimize use of foreign exchange in international trade
- Substituting foreign trips with teleconferencing.

- Debt rescheduling
- Restriction on profit and income repatriation
- Increasing government efficiency causing reduction in extravagant expenditures on foreign expensive goods.
- Export promotion to increase foreign exchange revenue.
- Diversification of exports to increase the range of exports

6. (a) Explain the causes of unemployment in your country. ( 10marks)

- **Rapid growth of population.** The fact that population grows faster the rate at which employment is created; many people remain unemployed.
- **Existence of the defective (poor) education system.** The system is theoretical in nature therefore prepares job seekers instead of job creators. The white-collar jobs are in short supply yet the turnover of the education system is high, leaving many school graduates unemployed.
- **Rural urban migration.** Due to rural-urban wage gap and other push and pull factors, most people migrate from rural areas to urban centers primarily in search of better wage employment opportunities which are not always available in urban centers. Since the rate of rural to urban migration is higher than the rate of urban employment creation, many migrants from rural areas become unemployed in urban centers.
- **Use of inappropriate technology:** Use of capital intensive production technique by some industries reduces the demand for labour hence unemployment.
- Discrimination and sectarianism in labour market. This is based on tribes, gender, religion, political ideologies and many other socio-economic factors. This leaves some members of the society unemployed due to lack of connections.
- **Seasonal variations in economic activity.** This is brought about by climatic changes especially in the agricultural sector leading to seasonal unemployment,
- **The IMF structural adjustment programs.** Policies like privatization, retrenchment of civil servants and demobilization of soldiers aimed at reducing the number of government employees as a way of reducing government expenditure. This leads to short run unemployment,
- **Lack of information regarding the presence of jobs in the labour market.** This leads to frictional unemployment.
- **Existence of political instabilities in developing countries.** Political insecurity destroys productive infrastructures and distorts production activities. This greatly discourages both domestic and foreign investment hence unemployment.
- **Lack of serious manpower planning by the government.** Governments do not effectively relate training in higher institutions of learning with the available employment opportunities. Consequently, more labour force is produced for certain professions than the country's ability to absorb the trainees. This results into surplus labour supply for certain professions hence unemployment.
- **Excessive use of foreign expatriates at the expense of the local labour.** This is common in foreign funded projects, NGO's and in businesses owned by foreigners. This leads to unemployment of the local labour force.
- **Deficiencies in demand for some products.** This forces some industries to layoff some workers hence unemployment. For example the coffee industry.
- Poor infrastructural facilities. This is in form of poor road network, poor communication facilities etc. which lead to low levels of investments hence unemployment.

- **High levels of inflation in the economy.** This increases the costs of production which discourages both domestic and foreign investment hence unemployment.
- **Existence of natural disabilities in form of physical and mental handicaps leading to residual unemployment.**
- **The poor land tenure system.** Land tenure system refers to the rights regarding ownership and use of land in the economy. Some people have plenty of land which is under-utilized while others do not have land at all and therefore they remain unemployed.
- **High levels of poverty.** Most people earn low incomes and therefore this leads to low aggregate demand. This discourages investments hence low levels of economic growth and employment.

(b) Suggest measures that should be taken by the government to reduce unemployment in your country(10marks)

- **Educational reforms.** The education system is being revised to suit the manpower requirements of the country. More emphasis is being put on vocational education in order to make graduates job makers instead of job seekers. Science based subjects are also being emphasized by the government.
- **Economic diversification.** The government is diversifying the economy in order to reduce dependence on one sector. This is being done by encouraging the growth on number of sectors like small scale industries, fisheries, tourism etc. in order to increase the rate of job creation in the economy.
- **Control of population growth rate.** Measures are being taken to control population growth rate through family planning, emphasizing girl child education etc. This is aimed at ensuring that the population growth rate matches the rate of resource exploitation hence controlling unemployment.
- **Modernization and commercialization of agriculture.** This is being done through the application of modern techniques of production, use of resistant crops and animals, agricultural research etc. aimed at increasing production and reducing unemployment.
- **Encouraging the use of appropriate technology.** Use of labour intensive technology is being emphasized so as to absorb the surplus labour and reduce on unemployment.
- **Rural development and transformation.** The government is transforming rural areas through infrastructure development, rural electrification, health, rural water and sanitation etc. This is aimed at increasing economic activities and employment opportunities in rural areas as a way of reducing rural urban migration.
- **Political Stability.** The government is promoting political stability through democratic governance and the use of the amnesty laws. This is helping to create a conducive investment climate both for local and foreign investors hence creating more employment opportunities.
- **Promoting investment.** The government is attracting foreign investments by providing investment incentives to foreign investors in form of tax holidays and tax exemptions. This is helping to increase investment and creation of employment opportunities in various sectors of the economy.
- **Infrastructural development.** The government is setting up and improving on the infrastructure for example construction roads, transport and

communication facilities, as well as banks and educational facilities in the country. This is aimed at creating more employment opportunities.

- **Economic integration.** This is aimed at expanding the market for goods and services in the economy as a way of stimulating investment hence creating more employment opportunities.
- **Privatization policy.** The government is expanding the private sector as a way of creating efficiency in production hence creating more employment opportunities.
- **Economic liberalization.** The government is removing unnecessary controls from economic activities to allow private individuals to freely participate in business activities. This helps to create more employment opportunities as many people are involved in trade.
- **Advertising of the existing jobs.** The government is guiding jobs seekers on the availability of jobs by advertising them in mass media. This is helping to reduce on frictional unemployment.
- **Providing credit to the local investors.** The government is providing soft loans to people to enable them invest and create employment opportunities. This is being done through schemes like poverty eradication programs, prosperity for all funds etc.
- **Control of inflation.** The government is controlling inflation by using restrictive fiscal and monetary policies. This has encouraged investment hence creating more employment opportunities.
- **Land reforms.** The government is reforming the land tenure system in order to enable the landless to have access and ownership over land. This is being done by introducing the land act which stops the eviction of squatters by landlords.

7. (a) Explain importance of taxes in your country. (08marks)

- To **raise revenue** by exploiting all potential taxable avenues base
- To **protect domestic industries** for cheap imports
- To **reduce income inequality** by taxing the rich more than the poor.
- To **protect peoples health by charging heavily harmful products** such as tobacco to reduce consumption.
- To **improve on the country's balance of payments position** by discouraging imports and encouraging exports
- To **discourage dumping into the country** and promote local production through lower taxes on domestic firms
- To **encourage growth of major sector** like education and health by imposing low taxes.
- To **break monopoly powers** especially land monopoly to encourage land sale to landless.
- To **protect the scarce resource**; like forest and mineral from over exploitation.
- To **reduce inflation** through direct taxes on income
- To **control economic variables like employment**, saving, investment, saving, etc.
- To **redistribute wealth** from the rich to the poor.
- To **solve environmental problems** created by consumption of some goods such pollution from gasoline.

(b) Discuss the demerits of imposing taxes in your country (12marks)

- Discourages saving;
- Encourages malpractices for example smuggling corruption, etc.

- Discourages effort and initiatives.
- It is inflationary - (the case with indirect taxes).
- Causes resentment of government that may erode her popularity/ leads to unrest by tax payers / traders.
- Limit the volume and benefit of trade / leads to retaliation in trade.
- Leads to diversification of resources from highly taxed to at times nonproductive activities that are less taxed leads to misallocation of resources.
- Reduces consumer welfare due to reduced consumption/Reduces consumption hence reduced welfare
- Leads to inefficiency of domestic (infant) firms which are shielded from external competition.
- Increases production costs leading to closure of some firms; reduced producer profits / unemployment due to closure of loss making firms.
- Discourages investment
- Leads to income inequality

Thank you

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