

# THE PUBLIC ACCOUNTANTS EXAMINATIONS BOARD

*A Committee of the Council of ICPAU*

## CPA(U) EXAMINATIONS

### LEVEL ONE

#### ECONOMIC ENVIRONMENT – PAPER 2

**WEDNESDAY, 15 DECEMBER 2004**

#### INSTRUCTIONS TO CANDIDATES:

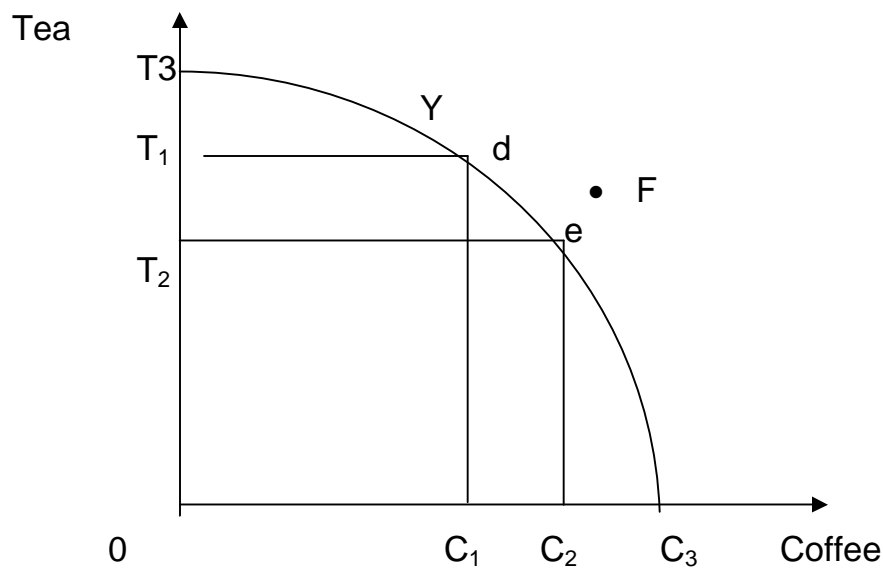
1. Time allowed: **3 hours**
2. Attempt **all** questions in Section A and any **four** questions from Section B.
3. Section **A** has twenty compulsory questions each carrying 2 marks.
4. Section **B** has **six** questions and only **four** are to be attempted. Each question carries 15 marks.
5. Please, read further instructions on the answer book.

## SECTION A

### Question 1

- (i) In a planned economy, resources are allocated by:
- Demand and supply.
  - Consumers and producers.
  - Consumer sovereignty.
  - Central authority.
- (ii) In buying goods and services, consumers aim at:
- Buying fashionable goods.
  - Equating demand and supply.
  - Paying lower prices.
  - Maximising utility.

Use the graph below to answer questions (iii) – (v)



- (iii) The above curve, labeled Y is:
- A transformation curve.
  - A marginal productivity curve.
  - A diminishing returns curve.
  - An indifference curve.
- (iv) According to the graph, points d and e:
- Cannot be attained using the available resources.
  - ImPLY efficient utilization of resources.
  - ImPLY underutilisation of resources.
  - ImPLY increase in production of tea and coffee.

- (v) Point F on the graph:
- (a) Suggests overutilisation of resources.
  - (b) Suggests economic growth.
  - (c) Cannot be attained using the available resources.
  - (d) Suggests optimal utilization of resources
- (vi) The fraction of total Income that is spent is known as:
- (a) Marginal propensity of income.
  - (b) Marginal propensity of import.
  - (c) Average propensity of spending.
  - (d) Average propensity to consume.
- (vii) Mukasa, a sole trader has been involving his wife in business activities without paying her, such a cost is:
- (a) Implicit.
  - (b) Private.
  - (c) Social
  - (d) Explicit.
- (viii) A firm's long run average cost curve is U-shaped because of:
- (a) Improvement in technology.
  - (b) Economies and diseconomies of scale.
  - (c) Employing more factors of production.
  - (d) The law of variable proportions.

**Use the table below to answer questions (ix) and (x):**

Commodity	Base Year Price	Current Year Price
A	200	300
B	250	500
C	400	200

- (ix) What is the average simple price index for commodities A, B and C?
- (a) 333.3
  - (b) 283.3
  - (c) 133.3
  - (d) 45.4
- (x) What is the likely interpretation of the answer obtained in question (ix) above?
- (a) Prices are relatively lower.
  - (b) Cost of living is low.
  - (c) Money value is high.
  - (d) There is an inflationary situation.

- (xi) Which of the following is not a feature of monopolistic competition?
- (a) No advertising.
  - (b) Elastic demand curve.
  - (c) Firm is a price maker.
  - (d) Brand loyalty.
- (xii) Balance of trade refers to the difference between:
- (a) Invisible exports and imports.
  - (b) Value of goods exported and imported.
  - (c) Total receipts and payments.
  - (d) Price index of exports and imports.
- (xiii) Which of the following enables trade unions to demand for a wage increment?
- (a) Low cost of living.
  - (b) Elastic demand for labour.
  - (c) Low unemployment.
  - (d) Elastic supply of labour.
- (xiv) If a government wants to maximize tax revenue; taxes should be levied on goods with:
- (a) Price elastic demand.
  - (b) Income inelastic demand.
  - (c) Income elastic demand.
  - (d) Price inelastic demand.
- (xv) Devaluation of the currency will have a positive effect on the economy, when:
- (a) Demand for exports is inelastic.
  - (b) Demand for imports is inelastic.
  - (c) Demand for imports is elastic.
  - (d) Supply of exports is inelastic.
- (xvi) Which of the following is not included in public finance?
- (a) Taxation.
  - (b) Borrowing.
  - (c) Buying and selling government securities.
  - (d) Government expenditure.

- (xvii) Under economic integration, free factor mobility is a feature of:
- (a) Preferential trade area.
  - (b) Free trade area.
  - (c) Customs Union.
  - (d) Common market.
- (xviii) Which of the following cannot reduce seasonal unemployment?
- (a) Acquisition of multiple skills.
  - (b) Diversification of the economy.
  - (c) Investing in small-scale firms.
  - (d) Specialization strategy.
- (xix) Bank A received an initial deposit of Shs. 200,000 and had a cash ratio of 10%. Calculate the credit multiplier.
- (a) 10.
  - (b) 5.
  - (c) 20.
  - (d) 0.1.
- (xx) What is the total credit that Bank A in question (xix) above can create?
- (a) Shs 1,000,000.
  - (b) Shs 2,000,000.
  - (c) Shs 100,000.
  - (d) Shs 500,000.

## SECTION B

### Question 2

- (a) State the laws of demand. (2 marks)
- (b) Give reasons to explain the downward slope of the demand curve. (8 marks)
- (c) Account for an increase in quantity demanded of a commodity when price of that commodity has not reduced.
- (Total 15 marks)**

**Question 3**

- (a) Distinguish between perfect competition and monopolistic competition. (4 marks)
  - (b) Give any four characteristics of a perfectly competitive market. (4 marks)
  - (c) Demonstrate how a firm under perfect competition determines output, price and profits in the short run. (7 marks)
- (Total 15 marks)**

**Question 4**

- (a) Define the term “fixed costs”. (1 mark)
  - (b) Differentiate between marginal cost and average cost. (4 marks)
  - (c) Why do small scale firms exist along side large scale firms? (10 marks)
- (Total 15 marks)**

**Question 5**

- (a) What is a “development goal”? (1 mark)
  - (b) Outline any four development goals in your country. (4 marks)
  - (c) Give any ten features of underdevelopment in third world countries. (10 marks)
- (Total 15 marks)**

**Question 6**

- (a) Give five methods that can be used to limit imports. (5 marks)
  - (b) Examine the merits and demerits of protectionism as a trade policy. (10 marks)
- (Total 15 marks)**

**Question 7**

- (a) Distinguish between public revenue and public expenditure. (4 marks)
  - (b) Give six non-tax sources of government revenue. (3 marks)
  - (c) Account for the recent increase in government expenditure in your country. (8 marks)
- (Total 15 marks)**