
CERTIFIED ACCOUNTING TECHNICIAN

LEVEL 1 EXAMINATION

L1.5: ECONOMICS AND THE BUSINESS ENVIRONMENT

FRIDAY: 14 JUNE 2013

INSTRUCTIONS:

- 1. Time Allowed: 3 hours 15 minutes** (15 minutes reading and 3 hours writing).
- This examination has **seven** questions and only **five** questions are to be attempted.
- Marks allocated to each question are shown at the end of the question.
- Show all your workings

QUESTION ONE

- a) Distinguish between the following terms as used in Economics
- i) Economic goods and free goods. (3 Marks)
 - ii) Real Capital and financial Capital. (3 Marks)
 - iii) Fixed and variable factors of production. (3 marks)
 - iv) Production Possibility Frontier and production function. (3 Marks)
- b) Distinguish between the objectives of consumers and producers. (4 marks)
- c) What is the meaning of the term consumer sovereignty and how does it relate to the concepts of demand and supply. (4 Marks)

(Total 20 Marks)

QUESTION TWO

- a) Discuss the concept of price discrimination. (8marks)
- b) Why is it difficult to use national income as a measure of international living standards
- c) Distinguish between **free float** and **managed float**. (4marks)
- d) Outline the differences between **trade creation** and **trade diversion**. (4 Marks)

(Total 20 Marks)

QUESTION THREE

- a) With the help of a diagram, discuss the circular flow of income. (6marks)
- b) Briefly explain three methods used in the computation of National Income statistics. (6marks)
- c) A statistics office in a hypothetical country XYZ gave the information as regards the economy of that country for the year 2011. The figures are in billions of Frw.

Details	Frw
Gross National product (GNP)	5,100
Net factor income from abroad	198
Capital consumption allowance	564
Indirect business taxes	564
Social security contribution	393
Corporate income taxes	219
Undistributed profits	78
Transfer payment	720
Personal income tax	603

Required:

- i) Net National Product (N.N.P) (2marks)
 - ii) National Income (N.I) (2marks)
 - iii) Personal income (P.I) (2marks)
 - iv) Disposal income (D.I) (2marks)
- (Total: 20 marks)**

QUESTION FOUR

- a) Define Money and outline its major functions. (6marks)
 - b) Explain the various motives of holding money. (6marks)
 - c) What are the likely effects of an expansionary monetary policy in an economy? (8marks)
- (Total: 20 marks)**

QUESTION FIVE

You have been hired as a consultant by a firm producing bread to advise on a pricing strategy that would enable the firm to maximize profits. This firm is a monopolist which sells in two distinct markets, one of which is completely sealed off from the other.

As part of the analysis, you establish that the total demand for the firm's output is given by the following equation:

$Q = 50 - 0.5P$ and the demand for the firm's output in the two markets is given by the following equations:

$$Q_1 = 32 - 0.4P_1$$

and

$$Q_2 = 18 - 0.1P_2$$

Where:

Q = total output

P = Price

Q₁ = Output sold in Market 1

Q₂ = Output sold in Market 2

P₁ = Price charged in Market 1

P₂ = Price charged in Market 2

The cost of production is given by:

$$C = 50 + 40Q$$

Where:

C = total cost of producing bread.

Required:

- The total output that the firm must produce in order to maximize profits. **(4 marks)**
- (a) What price must be charged in each market in order to maximize profits? **(2 marks)**
- c) How much profit would the firm earn if it sold the output at a single price, and if it discriminates? **(5 marks)**
- d) The price elasticity of demand for the two markets at the equilibrium price and quantity. **(4 marks)**
- f) Comment on how the price elasticity of demand may be used in making economic decisions. **(3 marks)**
- g) Under what conditions is price discrimination possible? **(2 marks)**

(Total: 20 marks)

QUESTION SIX

- a Define the term inflation **(2marks)**
- b Explain the major causes of inflation **(10marks)**
- c What are the economic effects of a high rate of inflation **(8marks)**

(Total: 20 marks)

QUESTION SEVEN

- a) Define marginal Utility and clearly explain the concept of diminishing marginal utility **(6marks)**
- b) Explain Consumer equilibrium under the cardinalist and ordinalist approach. **(14 marks)**

(Total: 20 marks)

End of question paper