

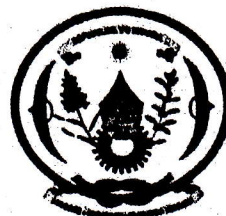
Economics II

018

16 Nov.2012

2 pm - 5 pm

REPUBLIC OF RWANDA



RWANDA EDUCATION BOARD (REB)

ADVANCED LEVEL NATIONAL EXAMINATIONS 2012

SUBJECT : ECONOMICS

PAPER 2 : APPLICATION OF BASIC PRINCIPLES OF ECONOMICS

COMBINATION(S): HISTORY- ECONOMICS-GEOGRAPHY : HEG

HISTORY- ECONOMICS-LITERATURE : HEL

LITERATURE- ECONOMICS-GEOGRAPHY : LEG

MATHEMATICS-ECONOMICS-GEOGRAPHY: MEG

MATHEMATICS-COMPUTER SCIENCE-ECONOMICS: MCE

PHYSICS-ECONOMICS-MATHEMATICS: PEM

DURATION: 3 HOURS

INSTRUCTIONS:

This paper consists of **TWO** sections **A** and **B**.

Section A: Answer **ALL** questions.

(55 marks)

Section B: Answer **any THREE** questions of your choice. **(45 marks)**

SECTION A - ATTEMPT ALL QUESTION (55 marks)

1. i. Distinguish between "need" and want". (2 marks)
ii. Show the relationship between opportunity cost and choice. (2 marks)
2. a) Explain the effect of the following on price : (3 marks)
i. Demand
ii. Supply
iii. Competition
b) How are decisions made in a market economy? (1 mark)
3. a) i. Define an entrepreneur. (1 mark)
ii. Describe any three functions of an entrepreneur. (3 marks)
b) i. Distinguish between a partnership and a public limited company. (2 marks)
ii. Mention any two advantages of a sole proprietor. (2 marks)
4. a) i. What is National income? (1 mark)
ii. Give any three reasons to explain why National income compilation is important in any Economy. (3 marks)
b) Discuss any three problems faced by developing countries while compiling National income statistics. (3 marks)
5. a) Describe any three factors which determine money supply in an economy. (3 marks)
b) Discuss any four positive effects which an increase in money supply has on an economy. (4 marks)
6. a) Differentiate between Creeping inflation and run-away inflation. (2 marks)
b) Give any three policy instruments for controlling inflation in your country. (3 marks)
7. a) i. What is the meaning of a Government budget? (1 mark)
ii. Mention any three objectives of a Government budget. (3 marks)
b) Differentiate between income tax and consumption tax. (2 marks)

8. a) Distinguish between favorable terms of trade and favorable balance of trade. (2 marks)
- ✓ b) Give three reasons to explain whether favorable terms of trade imply favorable balance of trade. (3 marks)
9. a) i. What is meant by the term underdevelopment? (2 marks)
- ii. Outline any three characteristics of underdevelopment. (3 marks)
10. a) What is optimum population? (1 mark)
- b) Give and explain three policies which can be used to reduce population growth in your country. (3 marks)

SECTION B: ATTEMPT ANY THREE QUESTIONS/45 MARKS

11. a) i. What is monetary policy? (2 marks)
- ✓ ii. What are the main objectives of monetary policy? (2 marks)
- ✓ b) Explain how monetary policy can influence interest rate. (2 marks)
- c) Explain the monetary policy tools used in your country. (9 marks)
12. a) i. What is export promotion? (1 mark)
- ii. Explain why developing countries adopt an export promotion industrial development strategy. (10 marks)
- b) Outline any four disadvantages of infant industries. (4 marks)
- ✗ 13. a) What are trade unions? (1 mark)
- b) Explain any four functions of trade unions. (4 marks)
- c) Under what conditions may trade unions demand for higher wages? (10 marks)
- Group 1 → 14. a) Describe ^{the general} two characteristics of developing countries. (2 marks)
- Group 2 → b) Discuss any eight obstacles to rapid economic growth in developing countries. (8 marks)
- Group 2 → c) Suggest any five policy measures which can be adopted in order to reduce poverty in developing countries. (5 marks)

- ✓
15. a) What five contributions has the private sector made to the economic development of your country? **(5 marks)**
- b) Account for the weakness of the private sector in Rwanda. **(5 marks)**
- c) i. Give three reasons to explain why education is an investment. **(3 marks)**
- ii. Explain why education is considered as an infrastructure in the economy. **(2 marks)**

b. i) An ordinary partnership is a partnership in which all members have unlimited liability i.e. all members are answerable to all debts of the business up to extent of selling their personal property. While a limited partnership on the other hand is one in which the liability of the members is restricted to the amount of capital contributed to the business.

ii) A sole proprietor has the following advantages:

- **Setting up this kind of business does not require a lot of capital**
- **All assets belong to the owner**
- **He does not require long formal proceedings of registration in order to start business.**
- **Since the business is usually, it makes easy for him/her to run and manage it**
- **The cost of organization is low**
- **The owner is independent and can initiate his/her own plans.**
- **He enjoys all profits alone**
- **This type of business can be located anyway to serve various categories of customers.**
- **Decisions made are immediately put into action, since he does not have to consult anyone.**
- **Since the business is his own, his personal interest in it makes him put more effort in its success, than a person working for some body else.**
- **He can stop his business at his own wish**
- **Since the business is small, it does not require a lot in terms of space**

4. a. i) National income is defined as the measure in money value of Goods and services which arise from all productive activities of a nation in any one year.

ii) Compilation of national income statistics is very important in economy because of the following reasons:

- **To measure the size of the national cake**
- **To identify the relative importance of the productive capacity of different sectors.**
- **To analyze income distribution – among factors of production, regions social groups etc.**
- **To measure changes in the level of economic activity**
- **To measure the rate of economic growth and development overtime**
- **To measure the size of availability of goods and services.**
- **To indicate standards of living and people's welfare**
- **To compare standards of living between countries**
- **It necessary for the development planning by the government**

- Governments use information obtained from National income statistics to determine policy measures needed for the development of their economies
- To analyze the partners of expenditure – both private and public expenditures
- National income figures are very important in estimating the level of international transaction and the extent to which countries are interdependent. This can be based on import and export figures.

b) Encountered problems by LDCs while compiling national income statistics :

- **Boundary of production :** i.e. which goods and services should be included or excluded when compiling national income.
 - **Double counting :** This mainly due to failure to distinguish between final and intermediate goods.
 - **Inadequate information :** Developing countries lack information regarding the size of population, price of goods and services , the income earned by the self-employed, etc.
 - **Government services :** It difficult to estimate the monetary value of services provided by the government e.g. medical care, roads, security, etc.
 - **Subsistence sector :** Output from this sector is either over valued or under valued.
 - **Services by the people themselves :** e.g. huts build by owners, collection of fire wood, water,.... May be overlooked. These are non market activities.
 - **Change in money value :** With change in money value due to inflation, it becomes difficult for National income statisticians to come up with an appropriate value of the current stock.
 - **Lack of facilities** required in the compilation exercise e.g. computers stationary, transport,
 - **Net Income earned abroad** is difficult to come by
 - **Lack of qualified people** to compile the statistics.
 - **Illegal activities :** which in some countries are excluded while compiling national income statistics ?

5. a) Factors determining money supply :

- Credit creation
- Level of interest rate
- Volume of foreign reserves
- Capital outflow and inflow
- Size of the subsistence sector

- Printing money by the Government
- Open market operations
- Size of balance of payment surplus
- Demand for money – liquidity preference
- Monetary sector preference
- Level of total output of goods and services.

b) Positive effects of the increase in money supply on an economy :

- Increased purchasing power
- Increased consumption
- Increased output
- There is trade boom in the economy
- High rate of economic growth
- Employment level increases
- Tax revenue of the government increase.

6. a) Creeping inflation is whereby persistent increase in the general price level proceeds at a slow rate, usually not exceeding 10%. Where as Run-away inflation is where the general price level increases at every high rate, the increase taking place within hours, days or weeks.

b) Policy instruments for controlling inflation in Rwanda:

- High direct taxes
- Controlled government expenditures
- Selling of securities
- Currency reforms
- Price control
- Control wage rate
- Liberalization of the economy
- Privatization drive
- Improved infrastructures
- Controlling issuing of currency
- Encourage imports
- Encourage production

7. a. i) Government budget is an estimate of revenue the government intends expects to raise and how it plans to spend it in a financial year.

ii) Objectives of government budget :

- **To reduce unemployment and creating job opportunities**
- **To raise the rate of economic growth / investment**
- **To control inflation, recession, and depression**
- **To improve the position of balance of payments**
- **Raise revenue for providing social services**
- **To protect infant industries / controlling dumping**
- **Discourage consumption of harmful products by increasing taxation on them.**

b) Income tax is a levy or a charge on individual household's or firms earnings while consumption tax is an outlay i.e. a levy or charge on consumption expenditure of an individual consumption unit.

8. a) Favorable term of trade refers to the situation where the price of exports are greater than price of imports. That is to say that one unit of export buy more than one unit of imports and there is an increase in the purchasing power of exports while favorable balance of trade refers to the situation where the value of goods exported is greater than the value of goods imported in a given year.

b) Favorable terms of trade do not necessary means that the country could enjoy favorable balance of trade because :

- **Favorable terms of trade may be as a result of low price of important but if quantities of imported goods are high, the country can have unfavorable balance of trade. Balance of trade depends on quantity and prices of goods exported and imported while terms of trade are about prices of exports and imports.**
- **Favorable terms of trade may come as a result of high prices of exports, however if the quantities exported are low, the country can have unfavorable balance of trade.**
- **Terms of trade consider both prices of goods and services whereas balances of trade consider only the value of goods. A country can enjoy favorable terms of trade because of low prices of imported services which outweigh the high prices of imported goods and low prices of exported goods.**

However by having favorable terms of trade a country can get a favorable balance of trade if the volume of export is greater than the volume of imports.

/3mks

9. a. i) - The term underdevelopment refers to countries which industrially, technologically, scientifically and economically less developed.

- **It is a situation whereby countries have lower level of development resources, low levels of exploitation of the potential resources, low levels of exploitation of the potential resources, low level of structural development, and have little or no up-date techniques of production.**

ii) Characteristics of underdevelopment:

- **Vicious circle of poverty**
- **Dualism**
- **Existence of an agriculture based export sector**
- **Abundant supply of unskilled labour**
- **High level of unemployment and underemployment**
- **Misallocation of resources by both the private and the state sectors**
- **Higher infant mortality rates**
- **Low levels of corruption**
- **Less developed infrastructure e.g. roads, hospital, etc.**
- **Low level of education**
- **High population growth rates**
- **Traditionalism**
- **Prevalent malnutrition**
- **Low standards of living because of low purchasing power**
- **Backward agricultural sector due to lack of mechanization, skills, research, etc.**
- **Low life expectancy**
- **Low level of industrialization**
- **Low level of specialization**
- **Inflation**
- **Uneven distribution of incomes**
- **Frequent political upheavals**
- **High rates of rural urban migration**
- **High proportion of the population engaged in agricultural sector**
- **Brain drain**
- **Limited domestic consumer market**
- **Balance of payment problem**

10. a) What is optimum population
b) Give any six policies which can be used to reduce population growth in your country. / 3mrks

11. a) Optimum populations is a situation where population in an area matches with the available resources./1mrk

iii) **Control of credits** : In order to control money in circulation central bank instructs commercial banks to reduce the amount of credits (loans). The decrease in money in circulation cause the fall in price and inflation./1.5 mark

iv) **Is the minimum balance** which commercial banks are required to maintain as reserves. It means they are no required to give more than the reserve requirements.

During inflation the central bank instructs commercial bank to provide credit is lowered and therefore the amount of money in circulation is reduced leading to fall in price and inflation./1.5 marks

v) **Special deposits** : These are special accounts which are opened by commercial banks at the central bank. During inflation the central bank instructs commercial banks to make special deposits at the central bank apart from the usual deposit they make, in order to reduce ability of commercial banks to provide credits. In this way the central bank is able to control amount of money which commercial banks can provide as credits and inflation. / 1.5 marks

vi) **Special credit** : In this method the central bank instructs commercial banks to provide credits to special projects only such as Agricultural projects and industrial projects. The aim is boost an control amount of credits. During inflation the central bank instructs commercial banks to provide credits to productive sectors of the economy in order to increase production. Therefore make supply meet the demand.

/ 1.5 marks

vii) **Moral situation**. In this instrument the central bank persuades or advise commercial banks to reduce the amount of credit during inflation.

12. a. i) **Export promotion is an industrial strategy of development which is aimed at producing for the outside market. It is a deliberate policy to expand the volume of exports./ 1mrk**

ii) Argument supporting why developing countries adopt an export promotion industrial strategy of development :

- It increases foreign exchange earnings and, therefore, improves on the balance of payments position of the country.
- Establishment of such industries creates employment opportunities (especially if they are labor intensive)
- Increased production under this strategy, promotes economic growth
- Developing countries need to diversify their export sector. Export promotion industries help a country to diversify her exports.
- There is limited domestic consumer market in poor countries.
- Exports promotion leads to market expansion by creating outside market for the products.
- Maximum use of domestic raw materials in production
- It promotes the manufacturing industries in general.
- Development of domestic skills will be encouraged. This reduces dependence on foreign manpower.
- It leads to the production of high quality goods e.g. export of high value added agricultural products like vegetable oil.
- It leads to improve co-operation among countries through international trade.
- Development of infrastructure at home may result due to the need to facilitate production activities for the export market.
- Export promotion industries can be spread all over country side, to achieve regional balanced growth. This is because such industries are not, often, attracted by market pull factors.
- It improves entrepreneurial ability in the country.
- It provides higher revenue through taxation.

b) Costs of infant industries.

- Production of poor quality goods
- May require subsidies from government
- Tendencies of siphoning capital from others industries (efficient)
- They seem not to mature

- They lead to income inequality
- They sometime require imported inputs
- They are high cost producers
- They are high cost producers
- In absence of delocalization programmes, regional inequality may be promoted
- Underutilization of resources
- Limited employment

13. a) Trade unions are workers' associations to work as mediators between employees and employers so as to maintain and improve on the workers' pay and working conditions. / 1mk

b) Trade unions are formed purposely to : / 4mks

- Improve workers' skills e.g. through seminars
- Improve workers' working conditions e.g. uniforms
- maintain employment for the employees.
- Co-operate with government in the implementation of government policies
- Improve workers' fringe benefits e.g. health, transport, and accommodation.
- Advise the government in the economic planning process.

c) Normally trade unions may demand for increase in wages under the following conditions : / 10mks

- Increase the cost of living trade unions' demand for high wages are justified, if the cost of living has increased.
- If the employer is in position to meet their wage demands.
- If the cost of production has reduced.
- When other workers in similar production processes are earning higher wages
- When the prices of production are gone up.
- Under a situation of full employment, trade unions can demand for higher pay, since there is little fear of replacing them.
- If the productivity of workers has increased
- When the employer has failed to pay the previous wage increments
- Where political policies in the country favors their demands
- If the goods produced by the workers experience inelastic demand, such as the employer can easily meet their wage demands by increasing the prices.

- When the wage demands do not contract with government policy e.g. on minimum wage.
 - If the wage bill makes only a small percentage of the total cost of production of the firm.
 - During an inflation period, when the real wage is falling.
 - During boom, when the demand is high, entrepreneurs are able to pay high wages
14. a) LDC's are characterized by low income, low savings, poverty, low investment /2mks

b) Rapid economic growth in developing countries is hindered by :

- High population growth in rates. This limits economic growth, as most of the resources which could be used for investment diverted to sustaining the ever increasing population e.g. in form of provision of foods, social services etc.
- Frequent political turmoil (e.g. civil wars, social unrest, etc) in many developing countries has always created an unfavorable atmosphere for both domestic and foreign investors.
- Lack of entrepreneurs i.e. risk bears and qualified people, has limited the level of investment and production.
- Dependence on agricultural sector by most developing countries, which has led to deteriorating terms of trade. In addition, the sector has many risks and uncertainties.
- Dualism-absence of integrated society
- Poor management in the public sector enterprise has reduced efficiency, leading to low production.
- Inadequate supply of rich natural resources e.g. minerals, etc
- Inadequate incentives for the rural population to increase output e.g. low price for agricultural products
- Frequent devaluations, which have not often, been successful
- Brain drain and therefore lack of skilled manpower to increase productivity
- Excessive government intervention discouraging small private investment
- Bureaucratic tendencies, causing delays in implementation of plans.
- Lack of capital.
- Low level of industrialization and specialization
- Unfavorable policies or agreements with International Monetary Fund, World Bank, etc. Leading to unpredictable funding.
- Limited domestic consumer market due to low purchasing power, this affects production levels.

- **Income drains and profit repatriation by foreign investors contributing to capital outflow.**
- **Sabotage by rich industrialized states e.g. as a result of continued colonial domination**
- **Poor planning.**

/Smks

c) To reduce poverty, developing country need to :

- **Break the vicious circle of poverty by supplement their capital resources with foreign investment and foreign aid, giving adequate incentives to stimulate production, increasing domestic savings, etc.**
- **Increase the supply of raw materials to make high value added final goods for both the domestic and foreign markets.**
- **Encourage self-help programmes so as to mobilize people's efforts towards development.**
- **Formulate policies which are aimed at functional income distribution so that the factors of production such as land, labor and capital are adequately rewarded.**
- **Emphasize progressive taxation of the rich, so as to increase government revenue which can be used to provide the poor with subsidized goods and services.**
- **Create more job opportunities by using labor intensive techniques of production so as to create income for the people.**
- **Control population through adequately publicized population policies e.g. family planning.**
- **Encourage agro-based industries to extend the agricultural sector.**
- **Encourage formation of regional co-operation or grouping like common market for East and southern Africa (COMESA) so as to provide joint investments in industry, agriculture, infrastructures, etc. Mobilize domestic resources properly in order to reduce over reliance on foreign capital.**
- **Provide a conducive political atmosphere so as to facilitate economic development**
- **Introduce education reforms which are in line with the man power requirements of developing countries. People should also be equipped with knowledge and skills which can help them to tackle practical problems.**
- **Improve the export sector by diversifying exports, creating wider market for products through trade zones and organizations like COMESA, etc.**

15. a) The private sector have contributed the following : /5mks

- **It provides several employment opportunities for the people**
- **It pays taxes to the government**
- **Provides output for domestic sale and exports.**
- **Uses idle resources specifically raw materials**
- **Foreign private investors bring capital (foreign exchange and machinery) in the country.**
- **Provides services like banking, transport, insurance, entertainment, education, health, etc.**
- **Its contributes to charity organizations to public works like roads, tax collection, licensing, etc.**
- **Sometimes develops infrastructures like storage facilities, telephones, electricity transmission.**

b) The weakness of private sector in our country :

- **Inadequate capital to expand operations**
- **Inadequate skilled manpower and limited entrepreneurial capabilities.**
- **Limited market for inputs and commodities.**
- **Poor infrastructures especially roads, refrigerated vans and aero planes**
- **Affected by high taxes**
- **High interest on commercial loans limits investment**
- **Limited capital markets and this makes it hard to get long loans**
- **Risks and uncertainty affect agricultural firms where insurance companies hardly cover risks like pests, drought, etc.**
- **Some firms are irresponsible and earn profit at the expense of environment deteriorating. E.g. pollution**

c) Education refers to learning while accumulating knowledge, ability and skills; it is among the major ways of increasing human capital accumulation.

Education is an investment because:

- **It has a cost.** Private costs in terms of school fees and work foregone by the student while studying.
- **Education has a benefit:** private benefits in forms of skills gained by an educated person and the income he/she earns after acquiring education.
- **Social benefits** in terms of services rendered to society by educated people e.g. doctors, teachers, policemen etc.
- **It has profits and losses:** Net return of education is calculated by subtracting the total costs of education from total benefit of education. Such returns are both private (if they accrue to the educated person) and social (if they accrue to the whole society). If net returns are positive, education is profitable, if are negative, then it is a loss.
- **Opportunity cost**
- **It is a way of accumulating human capital within labour in the same way as other investment lead to capital accumulation.**

ii) Education can be looked at as an infrastructure.

As an economic infrastructure, it facilitates development of the country by training labour which produces commodities and therefore contributes much to economic growth/1mk

As a social infrastructure, education is a social service which improves the welfare of human beings by increasing awareness on nutrition, public health and modern ways of living, and by providing psychological satisfaction to an educated person. /1mk