MATIGO EXAMINATIONS BOARD

P220/1
ECONOMICS
MARKING GUIDE 2023
PAPER 1

Qn	Answer	marks
	SECTION A	
1(a)(i)	**Equilibrium** of an industry is a situation where there is no tendency for firm to enter or leave the industry. (It happens in long run when firms are earning normal profits) While Equilibrium of a firm is a situation where the firm has no tendency to increase or reduce output.	01
(ii)	Condition for a firm to be in equilibrium under perfect competition 1. $MC = MR$ 2. MC curve cuts the MR curve from below OR Where $MC = MR$ at highest level of output	02
(b)		

Output (Q)	***Total revenue***	***Total costs***, TC (Shs)	***Marginal Revenue*** $(M$	***Total Varia*** ***Costs*** (VC)
0	–	900	–	0
1	400	1200	400	300
2	800	1420	400	520
3	1200	1550	400	650
4	1600	1650	400	750
5	2000	1650	400	750
6	2400	1730	400	830
7	2800	1980	400	1,080

(i)	The firm is under perfect competition	01
(ii)	The marginal revenue is $400shs$ for an extra unit produced /sold	01
(iii)	The fixed costs are shs. 900	01

(iv)	The total variable costs for the first two units is shs. 520	01
(c)(i)	Net national product at market price is the money value of all final goods and services produced by nationals of a country both within and abroad in a given year valued at prices paid by final consumers of the products excluding the value of depreciation. While Gross domestic product at factor cost is the money value of all final goods and services produced within the geographical boundaries of a country by both nationals and foreigners in a given year valued at factor prices (it included value of depreciation).	02
(ii)	Adaptation of getting GDP_{fc} from NNP_{mp} NNP_{mp} to GDP_{fc} – Subtract net income from abroad, add depreciation, add subsidies and subtract indirect taxes (outlays) i.e. $NNP_{mp} = GDP_{fc} - (x + m) + D + S - T$	02
(d)(i)	A proportional tax is the one whose rate is constant irrespective of the level of income. *While* A regressive tax is the one whose rate decreases as incomes increases.	02
(ii)	**Two effects of proportional tax;** • It is simple to understand to both tax collectors and tax payers • It has neutrality effect on saving and consumption • Does not lead to social unrests • Raises revenue for the government • It is easy to calculate tax liability • It is inequitable since it heavily affects low income earners • It does not bring insufficient revenue to the government • Lowers the levels of consumption and savings (esp. among low income groups) • Violets the principle of productivity since the rich with enough income pay at the same rate as the poor.	Any $2 \times 1 = 02$marks
(e)	Managed exchange rate is the one where the rate at which a country's currency is exchanged for other currencies (foreign) is determined by market forces of demand and supply but within the limits set by the monetary authority /gov't. *While* A fixed exchange rate is one where the rate at which a country's currency is exchanged for other (foreign) currencies is determined by the monetary authority /fixed by the government.	02

(ii)	**Two demerits of exchange rate control;** • Leads to emergence of smuggling and black markets in foreign exchange. • Reduces the volume of international trade by restricting imports • It leads to bureaucracy in the acquisition of foreign exchange • Involves huge expenses/high operational costs because many people have to be employed to monitor.	*Any* $2 \times 1 = 02marks$
	SECTION B	
2(a)	Cost of living refers to the amount of money required by an individual to sustain the lifestyle he/she is accustomed to. *While* Standards of living is the socio economic welfare of an individual as represented by the basket of goods and services consumed OR Standards of living is the condition of life that people live in or hope to live in.	02
(b)	**Why increase in *GDP* does not necessarily mean better *SOL*** • GDP does not consider income distribution • GDP may increase due to increase in prices/GDP does not consider general price level/rate of inflation. • GDP does not take into account quality of goods produced • GDP ignores the amount of leisure foregone. • GDP does not consider the state of political climate • GDP does not consider the patterns of the gov't expenditure • GDP does not put into account the working conditions of labour force. • GDP ignores the level/size of subsistence sector • GDP ignores the level of environmental pollution/social costs • GDP does not consider the level of taxation • GDP ignores type of goods produces/composition of goods produced • GDP does not consider accuracy in data collection/accuracy of the population figures. *Consider one side of the explanation, one that causes low S.O.L as GDP increases e.g.*	*Any* $8 \times 2 = 16marks$

	GDP does not consider income distribution. It is possible for GDP to increase when the income is concentrated in the lands of very few individuals yet the majority have very low incomes (Long stay in poverty) and are unable to get basic necessities of life leading to low standards of living.	
3(a)	**Circumstances in which price discrimination is successful** • When the producer is a monopolist, the production of a commodity should be undertaken by a monopolist so that he is in position to control the price. • If the cost of transferring a product from one market to another by a consumer is high. • If there is geographical separation of markets. The seller should be able to separate the markets where high prices are charged and where low prices are changed. • When the cost of separating markets by the producer is not too high/if the cost of separating markets by the producer is not too high/if the cost of separating market is relatively low. • In case the consumers are ignorant about other markets where low prices are charged. • If there is no government intervention in price determination • If the elasticity of demand is different in different markets • In case goods are sold on special order • In case of personal services/direct services which cannot be transferred from one person to another. • In case a commodity is made to appear different through product differentiation. • If the marginal revenue in both markets is the same.	*Any* $10 \times 1 = 10marks$
(b)	• Enables the producer to earn more revenue by taking away part of consumer's surplus. • Provides cheap goods for the poor • Reduces income inequality because of charging the rich more than the poor. • The profit earned through price discrimination can be used to improve efficiency if ploughed back. • Price discrimination based on dumping in foreign countries, enables the country to earn more foreign exchange. • Price discrimination can be used to either encourage or discourage consumption of certain goods through charging low prices or high prices respectively. • Helps the producers to dispose off surplus (especially through dumping) • Price discrimination increases consumption which encourages investment and job creation. **Negative effectives of dumping include;** • Causes income inequality (because of excess profits earned by monopolists) • It is exploitative especially for people paying higher prices	*Any* $6 \times 1 = 06marks$

	• Poor quality goods are produced in market where low prices are charged. • It retards the development of domestic industries through dumping • It eliminates consumer surplus hence the welfare of an average consumer. • Leads to diversion of resources from their optimal uses.	*Any* $4 \times 1 = 04marks$
4(a)	Wage legislation is a government policy of fixing wages that is either minimum wage set above the equilibrium wage below which it is illegal for employers to pay their workers or maximum wage set below the equilibrium. *Wage Legislation is a government policy of fixing wages that is either minimum wage set above the equilibrium wage below which it is illegal for employers to pay their workers or a maximum wage set below the equilibrium wage above which it is illegal to pay workers.* Award 4 *marks* to the candidate who indicates the idea of both ma and min wage Award 2mrks to the candidate who leaves the definition flat without indication of max or min wage or one who indicated one form of wages say max or min wage but not both.	04 marks
(b)	**Positive implications of wage legislation;** • It reduces loss of skilled labour to other countries through brain drain • Min wage increases purchasing power of workers/increases aggregate demand • Min wage reduces competition among workers/reduces malpractices such as absenteeism. • Min wage reduces efficiency of workers/labour productivity • Min wage increases government revenue • Min wage protects workers from exploitation by employers • Government gains popularity (min wage) • Min wage enables workers meet the rising cost of living • Min wages ensures equitable distribution of income • Min wage increases saving and investment • Min wage builds a stable workforce/reduces labour turnover. • Wax wages encourages investment as labour expenses reduce • Max wage controls demand pull inflation • Max wage makes labour cheap and affordable • Max price protects employers from exploitation. (Any 10 x 1 = 10mks) • Negative implications of wage legislation • Discourages investment due to high cost of labour (min wage) • It brings about Rum and its associated evils (min wage)	*Any* $6 \times 1 = 06marks$

	• Inflationary tendencies set in (min wage) • Discourages entrepreneurship due to low profit levels (min wage) • Leads to technological unemployment (min wage) • Increases the cost of production due to high labour costs (min wage) • It worsens income inequality • Leads to excess labour supply in relation to its demand (min wage) • Increases gov't expenditure in form of increases wage bill • Leads to loss of skilled labour to other countries through brain drain (in case of max wage) • Causes voluntary unemployment/discourages labour mobility. (max) • Reduces unpopularity of the government (Max wage)	
5(a)	**Causes of persistent increase in the general price level** • Raising cost of production • Desire to make excessive profits by business men • Breakdown of infrastructure and key industries • Excessive inflow of income from abroad • Excessive exportation of essential goods • Natural hazards leading to shortage of food items • Importation from countries experiencing inflation • Uncontrolled credit creation/excessive lending by commercial banks • Political instabilities/unrests • Excessive borrowing of money from the central bank by the government • Depreciation of the local currency. • Hoarding of goals/speculations by traders • Excessive increase in government expenditure • Excessive issuance of currency by the central bank • Reduced direct (income) taxes	Any 10×1 $= 10\ marks$
(b)	**Suggested measures to control persistent increase in prices** • Increase direct taxes • Reduce government expenditure • Use restrictive monetary policy • Liberalize the economy • Further privatize state enterprises	

	• Improve infrastructure • Provide investment incentives • Control printing and issuance currency by the central bank • Import from countries /stop importation from countries from inflation • Ensure political instability • Modernize Agriculture • Restrict exportation of essential goods • Use price wage controls (especially maximum price) • Use wage control measures • Encourage saving through NSSF • Encourage establishment of import substitution industries. *Ensure use of correct language*	*Any* 10×1 $= 10\ marks$
6(a)	**Reasons for development planning!** • To determine the rate of economic growth /to achieve high level /desired level of economic growth. • To properly allocate the scare resources • For equitable distribution of income • To identify areas suitable for public and private investment • To encourage public participation in development prices/to solicit /win public support. • To promote self-reliance / to reduce economic dependence • To correct balance of payment position • To reduce the unemployment problem. • For harmonies and consistent use of resources • To relate the present to future trends and targets • To correct the defects of price mechanism • For resource mobilization • To solicit for foreign aid • To attain price stability.	*Any* 10×1 $= 10marks$
(b)	**Factors that limit effective implementation of economic development plans**. • Limited date • Limited government commitment	

	• Limited funds • High level of corruption/mismanagement of funds • Existence of large private sector • Political instability /unrest/insecurity • Plans drawn are over ambitions • Existence of high level of inflation • Under developed infrastructure • Dependence on external resources which are uncertain tied and inadequate • Failure to identify viable projects • Limited skilled labour/limited qualified planners • Limited support from the public /conservatism of the people • Inefficient administrative machinery • Limited control over natural factors /unfavorable natural factors • Political sabotage /interference by politicians • High population growth rate.	*Any* 10×1 $= 10marks$
7(a)	**The quantity theory of money states that** "The general price level is determined by the amount of money in circulation assuming that the velocity of circulation of money and the level of transactions are held constant. This relationship is given by PT = Mr. where $M = quantity\ of\ money\ in\ circulation$ $V = Velocity\ of\ circulation\ \ of\ money$ $P = General\ price\ level$ $T = Level\ of\ transactions$ *Do not award to candidate who identifies v* as "*velocity of money*"	02 *marks* 01*mark* 01*mark* 01*mark* 01*mark*
(b)	**Limitations of the quantity theory of money in a market economy.** • The theory only attempts to explain changes in value of money but does not indicate/show how value of money is determined. • There is no general price level as the theory assumes but rather a series of price levels. • The theory ignores the influence of interest rate yet interest rate is a major determinant of money supply. • The theory does not consider demand for money which is unrealistic because an increase in money supply at constant money demand may have no influence on prices.	

	• If the marginal propensity to save is high, an increase in money supply results into high saving. This reduces the velocity of circulation of money and prices remain stable or even fall. • If a country has a lot of idle resources, an increase in money leads to increase in exploitation of resources which increases output and supply of goods and services which may make prices not change at all. • The theory does not put into consideration hugging between sellers and buyers to reach an agreeable price. • The theory ignores other causes of price increase other than increase in money supply such as increase in cost of production • The theory ignores other causes of price increase other than increase in money supply such as increase in cost of production • The theory is just a truism which shows the relationship between four variables M, V, P and T but not a true theory. • The theory only considers transactions motives of holding money and ignores the fact that some transactions are carried out through batter trade. • The theory only considers truncation motives of holding money and ignores the fact that some transactions are carried out through batter trade. • The four variables MV and PT are not independent of one another as the theory assumes. V and T are not constant as the theory assumes.	Any $7 \ x \ 2$ $= \ 14 marks$

END

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