# CENTRAL REGION TEACHERS' ASSOCIATION (CERETA)
## ECONOMICS SEMINAR SOLUTIONS

1. **(a) (i) A free enterprise economy** refers to an economy where allocation of resource is done by the forces of demand and supply without government interference. There is private ownership of resources by firms and households.

   **While/yet/whereas;**

   Mixed economy: Is one where resources are owned, controlled and allocated by both the state (public sector) and private sector (market forces of demand and supply).

   **(ii) Features of a free enterprise economy**

   - Private ownership of resources.
   - Free entry and exit
   - Producers aim at profit motive. -
   - No government intervention in trade/industry.
   - Allocation of resource is done by market forces of demand and supply.
   - High degree of competition in both factor market and commodity market.
   - Self interest.

   **(iii) Demerits of alaissez - faire economy**

   - Leads to economic/price instabilities.
   - Leads to emergence of monopoly and its related evils.
   - Leads to income and wealth inequalities.
   - There is consumer exploitation.
   - Consumer choices are distorted by persuasive advertising.
   - Leads to over utilization of resources/divergence between social costs and private benefits.
   - Inability to cope with rapid structural changes.

- Inability to allocate resources for public goods.
- Leads to unemployment
- Leads to duplication of activities hence resource wastage.

**(b)** **(i) Cross elasticity of demand:** Is the measure of degree of responsiveness of
quantity demanded of one commodity to changes in price of related/other commodity.

**While**

**Elasticity of supply:** Is the measure of degree of responsiveness of quantity supplied of a commodity to changes in factors that affect supply.

**(ii) Uses of price elasticity of demand to government;**

- Helps in devaluing currency.
- Guides in taxation policies.
- Determining the tax incidence.
- Guiding in determining wages of employees of public enterprises.
- Determining subsidization of a product.

**(iii) Causes of price inelastic supply of certain commodities in an economy**

- Unfavourable natural factors.
- Commodity having a long gestation period.
- Perishable nature of the commodity.
- Use of poor or inefficient technology.
- Poor infrastructures.
- High cost of raw materials.
- Unfavorable political atmosphere.
- Unfavourable government policy on production/investments.

**(c)** (i) An operating cost refers to a cost/expense of a firm that varies with the level
of output.

**WHILE**

An over head cost is an expense met by a firm regardless of the level of output produced.

(ii) Two overhead costs in an economy.

- Salaries of the top management.
- Cost on depreciation of machinery.
- Cost on rent.
- Interest on loans
- Cost of machinery.
- Insurance premium.

(iii) Industrial inertia is the tendency of an industry to locate or continue serving in an area where other industries exist even when factors which led to location of the industries are no longer applicable of existing.

(iv) Benefit of industrial localization

- Easy provision of social services.
- External economies of scale.
- Development of specialized/skilled labour.
- Promotes linkages.
- Increased employment.
- Increased government revenue.
- Development of commercial institutions
- Leads to economic growth.
- Promotes competition.
- Encourages market research.
- Reduce average costs of production.
- Optimum utilization of resources.

**(d)** (i) Private capital: Is one owned by an individual and yields income to individual owner.

**While/yet/whereas:-**

**Social capital:** Is one jointly owned by community as a whole for example roads, public hospitals, public schools.

**(ii) Sources of capital accumulation**

- Personal savings
- Inherited income or wealth.
- Retained profits of the business.
- Gifts and donations.
- Borrowing from financial institutions.
- Compulsory savings from NSSF.
- Taxation as a source capital for government.

**(iii) Benefits of capital in development of Uganda:-**

- Increases resources utilization.
- Promotes technological development.
- Monetizes the economy.
- Leads to increased output hence economic growth.
- Improves quality of final output.
- Improves labour skills.
- Facilitates development infrastructures.
- Facilitates industrialization.
- Reduces economic dependence.
- Promotes specialization in production.
- Creation of employment opportunities.
- Capital facilities security for investment as collateral security hence increased investments.

**(iv) Factors limiting capital formation in low developing countries.**

- Low income level.
- High inflation rate.
- Low level of infrastructure development.
- Limited capital stock.
- Unfavourable political climate.
- Poor technology.

- High population growth rate.
- Unfavourable government policy on investments.
- Poor land tenure system.
- Limited market size.
- Corruption.
- High degree of conservatism.

**(e)** (i) Price mechanism is a system in a free enterprise economy where prices are determined by the interplay of market forces of demand and supply and prices allocate resources. There exists consumer sovereignty.

**(ii) Role of price mechanism in the allocation of resources.**

- Promoting efficient allocation of resources.
- Promoting consumer sovereignty.
- Determination of when to produce.
- Determining income distribution.
- Determination for whom to produce.
- Determines how to produce.
- Determining where to produce.

**(iii) Ways of interfering with price mechanism.**

- Use of progressive tax system.
- Offering subsidies to inefficient firs.
- Issuing licences to producers to regulate use of natural resources.
- Enacting laws to regulate the exploitation of a resources e.g. laws to safe guard wetlands,.
- Encouraging the formation of consumer associations to fight for the rights of consumers.
- Price control.
- Rationing scarce commodities.
- Rent control
- Subsidization of consumers.

**(f) (i) Economic dependence:** Is a situation in which an economy relies either mainly on one sector or Relies on other economies for its survival.

**While**

Economic interdependence: Is a situation where two or more countries rely on each other for Survival/growth and development.

(ii) Ways in which Uganda is economically dependent

- Sectoral dependence – Agricultural.
- External resource dependence.
    - Foreign technology.
    - Foreign skills.
    - Foreign capital
- Direct economic dependence – foreign decisions.
- Trade dependence e.g. over reliance on imports, geographical concentration of trade, limited range of exports.

**(iii) Implications of economic dependence**

- Kills local initiatives/encourages laziness.
- Compromises political independence.
- Worsens debt burden.
- Causes capital flight/BOP problems.
- Leads to under utilization of local resources/and domestic industries.
- Worsens economic dominance of the country by foreigners.
- Conditions set by donors are undesirable.
- Gives rise to technological unemployment.

**(g) (i) Balance of Trade (BOT):** Is the difference between the value of the country's
visible exports and value of the visible imports.

(**ii) Terms of Trade (TOT):** Is the ratio of price index of exports to price index of imports.

Or TO T is the relationship between price index of exports and Price Index of imports.

**(iii) Balance of Payment (BOP):** Is the difference between the country's earnings/receipts from Abroad from both visible and invisible exports and expenditure abroad on both visible and invisible imports during a given period of time. It includes capital inflows and capital outflows.

**(iv) Absolute Advantage:** States that given two countries and two commodities, using a given (same) amount of resources, one country produces both commodities more cheaply than the other.

**(v) Comparative Advantage:** Is a principle that encourages a country to specialize in the production of Commodity in which it has/incurs the least opportunity cost in comparison to another country.

**(h) (i) Causes of unfavourable terms of trade in LDCs.**

- Falling prices of exports.
- Low quality of exports.
- Weak bargaining power of LDCs on world market.
- Exportation of semi-processed/primary products.
- Protectionists policies of MDCs.
- Low income elasticity of demand for LDCs exports.
- Invention of raw material savings techniques by MDCs.
- Market flooding of similar agricultural products by LDCs leading to fall in export prices.
- Importation of expensive manufactured goods.
- Rising prices of imports.
- Increased substitution of LDCs exports with synthetic products/materials by MDCS. /

**(i) (i) Employment:** Is the total number of people/labour force gainfully working or an occupation by which a person earns a living i.e. work or business. Employment can be expressed in number of people working/ in total working hours.

OR

Employment is a situation where willing and abled labour force in the country can in actively get involved in a gainful economic activity.

**(ii) Disguised unemployment:** Is a situation whereby labour force is actively involved in a productive activity but the marginal product is either negligible or zero or negative.

**While/yet/ whereas**

**Under employment:** Is the under utilization of labour force, inform of labour working less time than desired or labour engaging in jobs far below his skills.

**(iii) Causes of disguised unemployment in Uganda.**

- Inadequate supply of capital.
- Poor land tenure system.
- Inadequate skills.
- High population growth rates.
- Desire to return work force for future use.
- Poor and uncoordinated man power planning.
- Nepotism in some sectors which results into over-enrolment or over recruitment.

**(j) SAPS of IMF that Uganda has implemented include:**

- Privatization/expanding the role of the private sector.
- Liberalization of trade and foreign exchange.
- Restructuring of the public service/demobilization of workers/soldiers.
- Reduction of government expenditure on non-essential services.
- Devaluation of the currency.
- Tightening monetary and credit policies.
- Restructuring of tax administration.

**(k) (i) Decentralised planning:** Is one whereby economic decision – making and implementation of plan in line with set targets are under taken by local government/local authority.

**(ii) Merits of decentralized planning.**

- Promotes use of local resources.
- Ensures balanced regional development
- Ensure that each area takes full advantage of its priorities.
- Ensures fair distribution of employment opportunities.
- Reduces bureaucratic chain.
- Controls rural urban migration and its evils.
- Promotes the sense of belonging and commitment/encourages public participation in development.
- Ensures efficiency in resource use sine it uses locally available resources.

**(l) (i) Liquidity ratio:** Is the proportion/percentage of commercial bank (total) deposits that is kept in cash or near cash form.

**While**

**Liquidity preference:** is the desire by individuals to hold assets/wealth in cash or near cash form.

(ii) Factors that may lead to increase in liquidity preference in developing countries.

- Rise in inflation rate/increase in price level.
- Decline in income level.
- Increase in level of cash transactions.
- Rise in the level of cash transactions.
- Rise in the level of uncertainty.
- Decline in interest rate on financial assets.
- Break down/decline in the development of commercial banks and other financial institutions.

- Increases stringent requirements for opening and operating bank accounts.

**(iii) Money supply:** Is the total amount of money in circulation in an economy both within the public and deposited in commercial banks.

**(m) (i) Tax base:** Refers to an entity/activity where a tax is levied while taxable capacity is the ability of the tax payer to pay the tax assessed on hi/her and remains with enough disposable income to enjoy the life style he is accustomed to.

(**ii) Tax evasion:** is the deliberate refusal by the tax payer to pay the tax imposed on him or her, it is illegal.

**(iii) Tax avoidance:** Is one where the tax payer exploits the loopholes within the tax law or administration to pay no or less tax, it is legal.

**(iv) Progressive tax:** Is one where the tax payer exploits the loopholes within the tax law or administration to pay no or less tax, it is legal.

(v) Regressive tax: Is one whose rate reduces as income/spending power reduces.

**(n) Ways of improving current tax system of Uganda**

- Reduce or eliminate corruption.
- Sensitize masses on benefits of taxation.
- Develop tax payer friendly system of collection.
- Ensure fair assessment.
- Build up infrastructures.
- Train personnel to assess and collect taxes.
- Ensure proper and effective use of taxes.,
- Improve implementation of tax laws.
- Ensure political stability.

(o) (i) Mild inflation is a type of inflation where prices are rising slowly but steadily and the percentage increase in the general price level is a one digit figure usually less than 10% per year.

**WHEREAS**

Hyper inflation is a type of inflation in which prices are rising at a very fast rate/rapidly and usually exceeding 10% per year.

**(ii) Effects of mild inflation**

- Leads to increased incentives to hard work.
- Encourages optimal utilization of resources.
- Increases production and economic growth.
- Debtors/borrowers gain in real terms.
- Increases employment levels due to increased investment.
- Increases government revenue.
- It promotes savings.
- It encourages labour mobility.
- Promotes entrepreneurship as many people are encouraged to risk in business ventures.
- Helps an economy recover from a depression.
- Commercialization is encouraged in the economy.

2. (a) (i) Price elasticity of demand is the degree of responsiveness of quantity demand

due to change in the commodity's own price.

**While**

Income elasticity of demand is the degree of responsiveness of quantity demanded due to change in the consumer's income

**(ii) Causes of low price elasticity of demand for a good.**

- Absence of substitutes for a good.
- High degree of addictiveness
- High degree of necessity
- Short run period-

- High level of convenience to acquire a good.
- High level of income.
- High level of ignorance of consumers in the market.
- Demand for durable GOODS.
- Small proportion of the consumer's income the commodity takes.
- Demand for a good with few uses.
- High level of advertising.
- Demand for a good in the right season.
-

**(iii) Factors that lead to high price elasticity of demands for a good.**

- Presence of close substitutes
- Low degree of addition.
- Low degree of necessity/demand for luxury goods.
- Long run period.
- Low level of convenience to acquire a good.
- Low level of income of the consumer.
- Demand for perishable goods.
- Big proportion of income the commodity takes.
- Demand for a good with many uses.
- Low level of advertising
- Unfavourable season for a good.
- Consumers being knowledgeable about the market conditions.

(b) (i) Change in demand refers to an increase or decrease in demand for a good at constant price due to change in other factors affecting demand.

**While**

Change in supply refers to an increase or decrease in supply for a good at a constant price due to change in other factors affecting supply.

(ii) Circumstances that may lead to change in supply at a constant price.

- Change in technology.
- Change in cost of production.
- Change in number of producers.
- Change in infrastructure development.

- Change in government policy on taxation of producers.
- Change in objective of the producer.
- Change in supply of factor inputs e.g. raw materials, capital.
- Change in political climate.
- Change in size of market.
- Change in natural factors.
- Change in the price of competitively supplied good.
- Change in the price of a jointly supplied good.

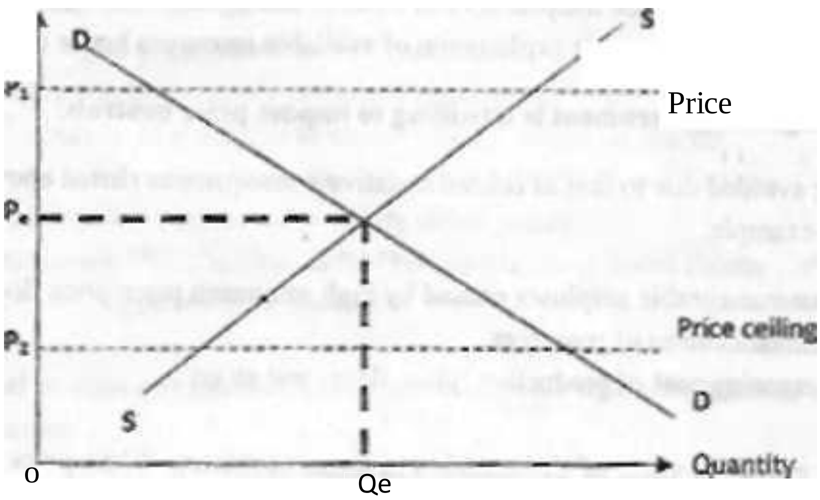
**SECTION B**

3. (a) Price ceiling: refers to the price set by the government below the equilibrium price above which' it is illegal to transact or trade a commodity.

**While**

**Price floor:** Price set by the government above the equilibrium below which it is illegal to trade or sell a commodity. Illustration:

**Illustration:**




DD = Demand curve SS = Supply Curve

**(b) Positive consequences of price legislation in an economy**

- Price floor protects producers/sellers from exploitation by strong buyers
- Price floor enables producers realize stable incomes especially in agricultural sector.
- Price floor leads to increased production of output hence economic growth.
- Price floor pulls the economy out of economic recession/depression.
- Price floor inform minimum wage reduces income inequalities.
- Price floor controls consumption of undesirable commodities such as tobacco, alcohol drinks; etc.
- Minimum wage protects employees from exploitation hence establishing industrial peace.
- Price ceiling protects consumers from being exploited by the producers/sellers.
- Price ceiling controls monopoly power.
- Price ceiling promotes price stability/controls inflation.
- Price ceiling makes it possible to access essential commodities to low income groups.

**(c) Reasons why Uganda government is unwilling to impose price controls;**

**NB:** It is being avoided due to fear of related negative consequences (listed above) of price legislation for example;

- To avoid unmanageable surpluses caused by high minimum price/price floor.
- To avoid misallocation of resources.
- Fear of increasing cost of production (price floor) and so on ….

**4. (a) Geographical mobility of labour:** This refers to the ease with which labour moves from one Area/place to another.

**While/yet/whereas**

**Occupational mobility of labour:** Refers to the ability/ease with which labour moves from one job to another; either vertically or horizontally.

**(b) Factors that affect occupational mobility of labour in an economy**

Note; Neutral answers are expected to show what makes labour either to easily move from one job to the other or what limits it to change jobs. (Balanced explanation needed).

- The level of skills for alternative jobs.
- The level of discrimination in labour market.
- The level of wages/remuneration in alternative jobs.
- Financial requirement required for alternative jobs.
- Prospect of promotion at the current job.
- Degree of awareness about alternative jobs.
- Periods of training and cost of training for alternative jobs.
- Level of esteem attached to alternative jobs.
- Working conditions in alternative jobs.
- The health of workers/labour.
- The age of the worker(s)

**(c) Suggest measures to improve/encourage geographical labour mobility.**

- Improve working conditions in other areas.
- Ensure balanced wage policy in all areas.
- Subsidize workers' transport.
- Improve political atmosphere in the country.
- Develop infrastructures to ease access to alternative areas.
- Advertise available jobs in other areas.
- Increase wages in areas with low incomes.
- Improve workers' health to make them strong to work.

**5. (a) (i) Horizontal merging of firms:** Is the union or combination of two or more firms in the same industry and at the same level or stage of production process.

**ii) Verti cal merging:** Occurs when two or more firms in an industry but at different production stages combine or unit in one production unit

**(iii)Latcral merging: I**s the union of two of more firms dealing in related products that can be conveniently marketed together, for example tooth brush firm combining with tooth paste making firm.

**(iv) Conglomerate merging**: Is the union or combination of two or more firms dealing in completely unrelated products to enjoy economies of diversification.

**(b) Rationale for merging of firms in Uganda**

- To encourage efficiency of firms/reduce cost of production.
- To ensure quality production.
- To attain monopoly and its benefits.
- To effectively exploit available resources.
- To minimize un necessary duplication and wastes.
- Enjoy economies of scale/increase output

**(ii) Factors limiting the integration of firms in Uganda;**

- Fear of high rates of taxation.
- Limited market size/low demand.
- Fear of unemployment.
- Differences in economic objectives of firms.
- Fear of diseconomies of scale (fear of higher risks).
- Shortage of skilled labour.
- Fear of loss of direct contact with customers.
- Reluctancy to share profits/fear to share losses.
- Fear of bureaucratic delays.
- Differences in techniques of production.
- Fear of losing independence.
- Firms dealing in un related products requiring different fields of specialization.
- Government anti-monopoly legislation.

**(iii) Measures that have been taken to support small scale firms in Uganda**

**Note: "has" show how each action has helped the firms to grow.**

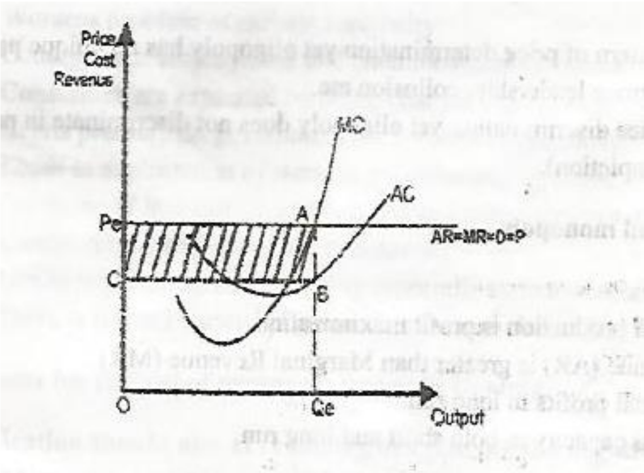
- Infrastructures have been built.
- Provided affordable capital.
- Trained labour to acquire skills.
- Political climate has been stabilized.
- Equipped people with entrepreneurial skills.
- Market size has been widened, through regional integration.
- Encouraged/supported technological development.
- Controlled inflation rates.
- Provided investment incentives such as subsidies, tax holidays.
- Under taken land reforms.
- Further liberalization of the economy has been taken.
- Intensified war against corruption.

**6. (a) Underlying assumptions of a perfectly competitive market**

- Assumes many sellers and buyers.
- Assumes no government interference.
- Assumes no transport costs.
- Assumes perfect knowledge in the market
- Profit **m**aximization is the motive of production.
- Production of homogeneous goods.
- Assumes free entry and exit of firms.
- The demand curve is perfectly elastic.
- No (persuasive) advertising.

**Price, output and profit determination under perfect competition**

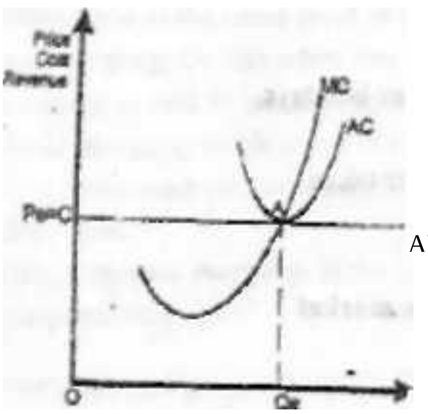
(b) (i) In short run, a firm in a perfect competitive market determines output at a point where marginal cost equal marginal Revenue **(MC=MR)**




- Price is determined where output line meets the AR/DD curve;
- Super normal profit is realized when AR is greater than AC at equilibrium output (the shaded area)

**(ii) Price, output and profit determination under a perfectly competitive market (Long run)**

A perfectly competitive firm/market determines output at a point where Marginal cost equals . Maudnai Revenue (LMCC = LMR).




AR-MR-

- Price is determined where output line meets the LAR/DD curve.
- In long run, the firm earns normal profits (zero profits) since the LAR = LAC at equilibrium output.

**(c) (i) Similarities and differences between oligopoly and monopoly markets.**

- Monopoly there is a single seller while oligopoly there are few sellers.
- Monopoly faces a downward sloping inelastic demand curve yet oligopoly faces a kinked demand curve.
- Monopoly entry of firms is blocked while oligopoly there is limited entry of new firms.
- Monopoly carries out informative advertising while oligopoly (imperfect) carries out intensive persuasive advertising.
- Monopoly has a clear pattern of price determination yet oligopoly has no unique pattern of price determination e.g. price leadership, collusion etc.
- Monopoly carries out price discrimination yet oligopoly does not discriminate in price (but carries out non-price completion).

**Similarities between oligopoly and monopoly**

- Both have many buyers.
- In both the objective of production is profit maximization.
- In both Average Revenue (AR) is greater than Marginal Revenue (MR)
- Both enjoy super normal profits in long run.
- Both produce at excess capacity in both short and long ran.

**(ii) Account for rise/origin/basis of monopoly power in Uganda.**

- Merging of firms.
- Long distance that exists between rival firms.
- Statutory law or acts of parliament causing statutory monopoly.
- Possession of unique talents.
- Exclusive ownership of a strategic natural resource or source of raw material causing natural monopoly.
- Restrictions in international trade causing sheltered monopoly.
- Patent and copy rights privileges given to authors and innovators/inventors.
- Nationalization of firms.
- Huge or high initial capital requirements.

- Product differentiation causing partial monopoly.
- Long period of training required for certain occupations.

**(iii) Effects of monopoly power in an economy**

**Positive implications**

- Limited duplication hence reduces resource wastage.
- Enables firm enjoy economies of scale.
- Price discrimination benefits low income earners.
- Abnormal profits are enjoyed in short and long run.
- Provides employment opportunities especially state monopolies.
- There are low operational costs due to limited advertising.
- Source of revenue to government through taxation.
- Encourages research and innovations.
- Public utilities provide cheaper services.
- Allows growth of infant industries due to patent rights accorded to monopolists.

**Negative implications**

- Causes excess capacity in the industry limiting economic growth.
- Worsens problem of income inequality.
- Causes under employment and unemployment of labour.
- Consumers are exploited by being charged high prices.
- Exerts pressure on government for favourable decisions.
- Leads to exploitation of workers by under paying them.
- Provision of low quality services due to limited/absence of competition.
- Causes shortage in times of breakdown.
- Limits innovations and creativity especially state monopoly.
- There is limited variety of goods thus limited choice for the consumers.

**(iv) Reasons for control of monopoly power in Uganda.**

**Note: Justification should aim at removing or reducing the negative consequences associated with monopoly: Answers should be in objective form.**

- To reduce excess capacity in production.
- To reduce income inequality.
- To enlarge employment opportunities and avoid unemployment of labour.
- To reduce consumer exploitation.
- To reduce exploitation of workers who arc being under paid due to absence of competing firms.
- To ensure production of quality output.
- To avoid shortages in case the firm breakdown.
- To widen varieties hence consumers choice being widened.
- To promote innovations and creativity due to competition being brought about.'
- To reduce pressure on government brought about by monopoly firms especially asking for favourable investment incentives.

**NB: A leaner must also consider how monopoly power can be controlled for wider reading**

**(v) Methods used by oligopoly firms to increase sales of their products**

- Persuasive advertising.
- Sponsoring events such as sports and events.
- Operating one stop shopping centres at fueling stations.
- Use of attractive packaging.
- Organizing ruffle draws.
- Use of trade fares and exhibitions.
- Offering gifts.
- Giving free samples.
- Use of after sales services.
- Opening branches across the country.
- Offering credit facilities.
- Improvement in quality.

- Rebranding.

7. (a) (i) GDP refers to the monetary value of an goods and services produced within the geographical boundaries of a country in a given period of time including depreciation.

**While**

GNP is the monetary value of all goods and services produced by nationals (both Irving abroad and within the country) in a given period of time including depreciation,

(ii) NDP refers to the monetary value of all goods and services produced within the geographical boundaries of a nation in a given period of time excluding the value of depreciation.

**Yet**

NNP is the monetary value of all goods and services produced by nationals in a given period of time excluding the value of depreciation.

**(iii) Real per capita income is income per capita valued at base year prices.**

**While**

Nominal per capital income is income per capita valued at current year prices.

**(b) Weaknesses of using per capita income to compare standard of living in an economy over time.**

- Per capital income ignores change in income distribution overtime.
- It doesn't consider change in price level overtime.
- Ignores change in political atmosphere in the country overtime.
- Per capita income ignores change in employment levels in the country over time.
- Ignores the changes in the nature of government expenditure overtime.
- Ignores changes in the amount of leisure enjoyed overtime.
- Ignores the changes in the consumer's tastes and preferences overtime.