CERTIFIED PUBLIC ACCOUNTANT

FOUNDATION LEVEL 2 EXAMINATIONS

F2.2: ECONOMICS AND THE BUSINESS ENVIRONMENT

DATE: THURSDAY 29, AUGUST 2024

INSTRUCTIONS:

1. **Time Allowed: 3 hours 15 minutes** (15 minutes reading and 3 hours writing).
2. This examination has **Seven** questions and only **Five** questions **should be** attempted.
3. Marks allocated to each question are shown at the end of the question.
4. Show all your workings where necessary.
5. The question paper should not be taken out of the examination room.

QUESTION ONE

Money plays a crucial role in modern economies. Without money, trade would be based on barter. In a barter economy, trade requires a double-coincidence of wants. If you have maize but want a cow you must find somebody who has a cow but wants maize. With barter the activities of selling and buying cannot be separated. In many if not all countries, inflation erodes the real value of money (i.e. the purchasing power of money). The inflation is normally measured in many countries by Consumer Price Index (CPI). It is the responsibility of the central bank to keep the inflation at minimum possible acceptable level through different instruments including monetary policy. In his "General Theory of employment, interest and Money" in 1936, Keynes advanced the three motives of holding cash.

Required:

a) **Explain any FOUR functions of money and explain how inflation prevents money from performing those functions properly**. (8 Marks)

b) **Briefly discuss any THREE tools of monetary policy which can be used by the central bank**. (6 Marks)

c) Using examples, **briefly explain the THREE motives of holding cash as advanced by Keynes.** (6 Marks)

(Total: 20 Marks)

QUESTION TWO

a) After differentiating the income elasticity from cross elasticity of demand, **state FOUR arguments for the concept of elasticity of demand.** (6 Marks)

b) After differentiating minimum price control from maximum price control, **explain any THREE reasons why government and other agencies should ever wish to intervene in price controls.** (8 Marks)

c) In very many cases, unregulated markets and the price system are effective and efficient ways of allocating resources, some forms of well-meaning government intervention can actually make worthy social objectives more difficult to achieve. Nevertheless, this does not mean that unregulated markets are always perfect. The existence of some defects is widely accepted.

Required:

Using a clear example, **support this statement ''*The unregulated markets are not always perfect*".** (6 Marks)

(Total: 20 Marks)

QUESTION THREE

ABC Ltd and XYZ LTD are only two companies operating in Rwanda, specifically in brewery sector. Recently the board of two companies meet to discuss some matters including how these two companies can put together their efforts instead of competing. They have agreed that they merge into one company called ABC_XYZ Ltd. They also discussed about how they will discriminate prices basing on different factors.

Required:

a) **Briefly discuss FIVE arguments for business growth by a means of mergers**
(5 Marks)

b) **Discuss the SIX diversification strategies that ABC_XYZ Ltd would go for**
(6 Marks)

c) After briefly discussing the THREE degrees of price discrimination, **explain the necessary conditions for companies like ABC_XYZ Ltd to operate the price discrimination?** (9 Marks)

(Total: 20 Marks)

QUESTION FOUR

a) **Briefly discuss the three exchange rate regimes.** (6 Marks)

b) Using graphs, **differentiate trade creation and trade diversion as effects of custom union**. (6 Marks)

c) Rwanda imports goods from the USA, those goods include computers, telephones, fabrics etc. with the average prices of FRW 27,384, It also exports coffee and tea. At the weighted average price is FRW18,440.

Required

i) **Calculate and comment on term of trade (TOT).** (4 Marks)

ii) **Discuss Heckscher and Ohlin theory on the international trade.** (4 Marks)

(Total: 20 Marks)

QUESTION FIVE

a) **State FIVE factors that affect the potential size of the National Income** (5 Marks)

b) **Briefly discuss FIVE criticisms of GDP per capita as a measure of economic growth** (5 Marks)

c) The following data were extracted from the national accounts' statistics of Carland country.

	Millions
A National Income	**2024**
Personal consumption	2,130,350
Subsidies	42,975
Statistical discrepancy	25,375
Change in stock	56,600
Public sector current expenditure	712,575
Investment	632,325
Depreciation	566,000
Taxes	8,975
Imports	3,025,925
Net factor incomes from abroad	709,075
Exports	3,647,550

Required:

Using the data from the above table, calculate the following:

i)   **Gross Domestic Product (GDP) at market price.**   (2 Marks)

ii) **Gross National Product (GNP) at market price.**   (2 Marks)

iii) **Gross National Product (GNP) at factor cost.**   (2 Marks)

iv) **Net National Product (NNP) at factor cost**.   (2 Marks)

v)   **If Carland has a population size of 950 million, calculate the GNP per capita.**

(2 Marks)

(Total: 20 Marks)

QUESTION SIX

a) **Referring to the Circular flow of income model, use examples to differentiate leakages from injections**   (4 Marks)

b) **Using relevant diagram, briefly explain how the model of the Circular flow of income works.**   (8 Marks)

c) **Differentiate Marginal Propensity to Consume (MPC) from Average Propensity to Consume (APC).**   (2 Marks)

d) Briefly explain how the following budget position affect the circular flow of income of a given economy:

i)   **Balanced budget**   (2 Marks)

ii) **Budget deficit**   (2 Marks)

iii) **Budget surplus**   (2 Marks)

(Total: 20 Marks)

QUESTION SEVEN

a) **Discuss THREE factors affecting the exchange rate of a given county.** (3 Marks)

b) **Discuss FIVE arguments for international trade protectionism.** (5 Marks)

c) **Define the following terms as used in the international trade finance**
   i. **Real exchange rate.** (2 Marks)
   ii. **Nominal exchange rate.** (2 Marks)
   iii. **Effective exchange rate.** (2 Marks)

d) **Explain THREE reasons why a country may wish to buy currency of another country.** (3 Marks)

e) Assume Rwandan price level is FRW 1,800 while Ugan price level is FRW 2,000. The nominal exchange rate between the countries is 0.3.

Required:
Calculate the real exchange rate of prices in Rwanda over Uganda and comment on your results. (3 Marks)

(Total: 20 Marks)

End of question paper.

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