

MAASAI MARA UNIVERSITY

**REGULAR UNIVERSITY EXAMINATIONS**

**2017/2018 ACADEMIC YEAR**

***THIRD* YEAR *SECOND* SEMESTER**

**SCHOOL OF BUSINESS AND ECONOMICS**

**BACHELOR OF ARTS (ECONOMICS)**

**COURSE CODE: ECO 323**

**COURSE TITLE:** **PUBLIC FINANCE AND FISCAL POLICY**

**DATE: 23rd AUGUST 2018 TIME: 8.30 – 10.30**

**INSTRUCTIONS TO CANDIDATES**

1. Answer Question **ONE** and any other **THREE** questions

*This paper consists of* ***3*** *printed pages. Please turn over.*

# QUESTION ONE

1. The County Government of Garissa intends to undertake the following two mutually exclusive projects (PA and PB). The table below gives their cash flows and initial costs. Use the Net Present Value technique and the Internal rate of return techniques to decide which project should be undertaken. (Use a required rate of return of 11 per cent) **(10 Marks)**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| Project | Yearly Cash Flows (USD Millions) | | | | | |
| 0 | 1 | 2 | 3 | 4 | 5 |
| P1 | (1,555) | 450 | 590 | 510 | 250 | 205 |
| P2 | (1,861) | 500 | 1,150 | 650 | 520 | 280 |

|  |  |
| --- | --- |
| 1. Discuss 5 rationales for government intervention in private sector activities | **10 Marks)** |
| 1. State five constraints to the government expenditure through debt financing . | **(5 marks)** |

# QUESTION TWO

|  |  |
| --- | --- |
| 1. Discuss five cannons of a good tax system. (**10 marks)** |  |
| 1. Give five (5) differences between social goods and private goods. | **(5 marks)** |

# QUESTION THREE

|  |  |
| --- | --- |
| 1. Discuss four (4) instruments of fiscal policy. | **(8 marks)** |
| 1. Using a well-labelled diagram, demonstrate how market failure would result if the agents engage in uncompetitive practices. | **(7 marks)** |

# QUESTION FOUR

|  |  |
| --- | --- |
| 1. Differentiate between negative externality and externality | **(2 marks)** |
| 1. Discuss how the government can use the following approaches to correct negative externalities: 2. Property rights; 3. Actionable pollution permits; 4. Social conventions. | **(6 marks)** |
| 1. Give two critiques to the Pigouvian tax system as a way forcing producers to produce socially optimal output levels. | **(3 marks)** |
| 1. Define the following terms as used in the public sector economics: 2. Information asymmetry; 3. Moral hazards; 4. Market failure; 5. Institutional rigidities; | **(4 marks)** |

# QUESTION FIVE

1. Differentiate between the following terms:

|  |  |  |
| --- | --- | --- |
| 1. In-rem taxes and personal taxes; 2. Callable public debt and redeemable public debts; 3. Benefit principal to tax equity and Ability-to-Pay principal to tax equity. | **(6marks)** | |
| 1. Use a well-labeled diagram to illustrate the consequence on tax incidence of imposing a unit tax on a commodity. | | **(7 marks )** |

|  |  |
| --- | --- |
| 1. Explain any two factors that would affect the incidence of a tax. | **(2 marks)** |