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TOPICALLY ARRANGED

Updated With
December 2025
Past Paper with Answers

TOPICS **PAGE NUMBERS**

PAST PAPERS QUESTIONS

PAST PAPERS ANSWERS

.

TOPIC 2

DEMAND, SUPPLY AND DETERMINATION OF EQUILIBRIUM

QUESTION 1

December 2025 Question One B and C

(b) Explain **THREE** differences between "individual demand" and "market demand" as applied in economics. (5 marks)

(c) Discuss **THREE** applications of elasticity of supply in business decision-making process. (6 marks)

QUESTION 2

December 2025 Question Two A

State **SIX** effects of subsidies on market equilibrium. (6 marks)

QUESTION 3

December 2025 Question Seven A

The demand for a commodity is 20 units when the prevailing market price is Sh.80 per unit. However, when the price per unit rises to Sh.100 the quantity demanded rises to 30 units.

Required:

(i) Arc elasticity of this commodity. (2 marks)

(ii) Point elasticity of this commodity. (2 marks)

QUESTION 4

August 2025 Question Two B and D

(b) Outline FOUR determinants of elasticity of supply of labour. (4 marks)

(d) Using a well labelled diagram, illustrate the price ceiling for a good or service. (6 marks)

QUESTION 5

August 2025 Question Three A and B

(a) The demand and supply functions of a certain product are given as follows:

Qd = 110 – 2P

Qs = – 40 + 3P

The government imposes a tax of Sh.5 per unit.

PART B

SUGGESTED ANSWERS

TOPIC 2

DEMAND, SUPPLY AND DETERMINATION OF EQUILIBRIUM

QUESTION 1

December 2025 Question One B and C

(b) Differences between "individual demand" and "market demand" as applied in economics.

In economics, **individual demand** refers to the quantity of a specific good or service a single consumer is willing and able to purchase at various prices within a given time period. It represents the demand behavior of an individual person.

Market demand, in contrast, is the total quantity of a specific good or service that all consumers in a particular market are willing and able to purchase at various prices within a given time period. Market demand is derived by horizontally summing the individual demand curves of all consumers in the market at each price point.

(c) Applications of elasticity of supply in business decision-making process.

- **Production planning**: Businesses use supply elasticity to determine how quickly and effectively they can scale up or down production in response to price changes or shifts in market demand. Firms with elastic supply (easy to increase production) can quickly capitalize on price spikes.
- **Inventory management**: Understanding supply elasticity helps businesses optimize inventory levels. Firms with inelastic supply may need to hold larger inventories to meet sudden demand increases, as they cannot quickly produce more goods.
- **Pricing strategy**: Businesses can use elasticity to forecast how competitors or the overall market might react to their pricing changes. If the industry supply is elastic, a price increase might attract many new suppliers, potentially driving prices back down.
- **Responsiveness to market shocks**: The ability to adapt to sudden changes, such as raw material shortages or natural disasters, depends on the flexibility of supply chains, which is directly related to supply elasticity.

QUESTION 2

December 2025 Question Two A

Effects of subsidies on market equilibrium.

- **Shift in supply curve**: A production subsidy effectively lowers the producer's cost of production. This results in an outward (rightward) shift of the supply curve, meaning producers are willing to supply more at every given price.
- **New equilibrium price and quantity**: The shift in supply establishes a new market equilibrium. The equilibrium quantity traded in the market increases, and the price paid by consumers' decreases.
- **Division of benefit**: Both producers and consumers benefit from a subsidy. Consumers pay a lower price, and producers receive a higher effective price (the consumer price plus the per-unit subsidy amount). The incidence of the subsidy (who benefits more) depends on the relative elasticities of supply and demand.
- **Welfare effects**: While subsidies benefit the specific market participants, they involve a cost to the government (taxpayers) and can lead to an inefficient allocation of resources in the broader economy, potentially causing a "deadweight loss" if the cost of the subsidy exceeds the gains in consumer and producer surplus.

QUESTION 3

December 2025 Question Seven A

(i) **Arc elasticity of this commodity.**

Initial price $((P_1)$ = Sh. 80

Initial quantity (Q_1) = 20 units

New price (P_2) = Sh. 100

New quantity (Q_2) = 30 units

$$E_a = \frac{Q_2 - Q_1}{Q_2 + Q_1} \times \frac{P_2 + P_1}{P_2 - P_1}$$

$$E_a = \frac{10}{50} \times \frac{180}{20}$$

$$= 0.2 \times 9$$

$$= 1.8$$

(ii) **Point elasticity of this commodity.**

$$\frac{dQ}{dP} \times \frac{P}{Q} = \frac{10}{20} \times \frac{80}{20} \quad = 2.0$$

QUESTION 4

August 2025 Question Two B and D

(b) Determinants of elasticity of supply of labour.

- **Specific skills and educational requirements:** The more complicated the skills and the higher, or longer to achieve, the qualifications required, the more inelastic the supply.

- **The time period under consideration:** In the short run, the supply curve of labour tends to be inelastic as it takes time for people to respond to changes in relative wages.
- **Availability of alternative occupations:** If a worker has highly specialized skills with few alternatives (e.g., a tenured university professor in a niche subject), their supply of labour to that profession is very inelastic. They are less likely to leave their profession even if wages stagnate. Workers with transferrable skills make supply elastic.
- **The mobility of labour:** The easier workers find it to change jobs or to move from one area to another, the easier it will be for an employer to recruit more labour by raising the wage rate. Thus, higher mobility makes the supply elastic.
- **Geographical mobility of labour:** If mobility is low due to factors like family ties, cultural barriers, high cost of moving, immigration restrictions, or language differences, the labour supply will be inelastic and vice versa.

(d) **Using a well labelled diagram, illustrate the price ceiling for a good or service.**
A price ceiling is the maximum amount a seller is permitted to charge for a product or service. It is usually set by law and is typically applied to staples such as food and energy products when they become too expensive for average consumers.
For the measure to be effective, the ceiling price must be below that of the equilibrium price. The ceiling price is binding and causes the equilibrium quantity to change – quantity demanded increases while quantity supplied decreases. It causes a quantity shortage of the amount Qd – Qs. In addition, a deadweight loss is created from the price ceiling.