THE UNITED REPUBLIC OF TANZANIA

NATIONAL EXAMINATIONS COUNCIL OF TANZANIA

ADVANCED CERTIFICATE OF SECONDARY EDUCATION EXAMINATION

151/2 **ECONOMICS 2**

ECONOMIC DEVELOPMENT

(For Both School and Private Candidates)

Time : 2 Hours 30 Minutes **ANSWERS** **2006 February, 17 Friday, a.m**

Instructions

1. This paper consists of sections A and B.
2. Answer **five (5)** questions, choosing at least **two (2)** questions from each section.
3. All questions carry equal weight.
4. Communication devices and any unauthorised materials are **not** allowed in the examination room.
5. Write your **Examination Number** on every page of your answer booklet(s).

1. The per capita income in country A is shs 860,000 while the per capita income in country Z is shs 1,000,000. However, the standard of living in country A is higher than that in country Z. Explain the factors which may be in play in the two countries.

The cost of living may be lower in country A than in country Z. Even though incomes are lower, people in country A can buy more goods and services with the same amount of money compared to those in country Z, giving them a higher standard of living.

Income distribution may be more equal in country A than in country Z. If wealth in country Z is concentrated in the hands of a few, the majority of the population may live in poverty despite the higher average income. In contrast, fairer distribution in country A improves general welfare.

The provision of social services such as health, education, water, and housing may be better in country A. If government policies ensure wide access to these services, the standard of living is improved even if per capita income is lower.

Country A may also have better infrastructure and governance. Reliable transport, communication, and electricity improve quality of life and economic opportunities, which may not be the case in country Z.

Cultural and social stability could also be a factor. If country A enjoys peace, security, and strong social support systems, people live more comfortably compared to country Z, where instability or insecurity may undermine living standards.

2. Figure 1 above shows two countries' Lorenz curves of income distribution (A and Z). Other things being equal: (a) Which of the two countries do you think has a fair income distribution than the other, and why?

Country A has a fairer income distribution compared to country Z. This is because its Lorenz curve lies closer to the line of absolute equality, meaning that income is distributed more evenly among the population. In contrast, country Z's curve is further from the equality line, showing higher inequality.

(b) In which of the two countries do you think it is easier to alleviate (reduce) poverty, and why?

It is easier to alleviate poverty in country A. Since income is more fairly distributed, government policies to support the poor will have broader impact. Additionally, fewer extreme inequalities exist, so redistributing resources through taxes and welfare programs is more effective. In country Z, poverty reduction is harder because of deep inequality where the rich control most resources, leaving the majority with very little.

3. In the context of Tanzania, account for the existence of structural and casual unemployment.

Structural unemployment in Tanzania exists because of mismatches between workers' skills and the demands of the labor market. Many people are trained in fields where there are few job opportunities, while industries that need workers lack qualified people. For example, graduates in arts may find it hard to secure employment while technical jobs remain vacant.

Another reason for structural unemployment is the slow pace of industrial development. The Tanzanian economy is still largely dependent on agriculture and informal activities, so formal job opportunities are limited compared to the growing population.

Casual unemployment arises because of the seasonal nature of agriculture, which is the main employer. During planting and harvesting seasons, demand for labor is high, but during off-seasons, workers lose their jobs and remain idle.

Casual unemployment is also common in the construction and informal sectors. Workers are hired on short contracts or daily wages, and when projects are completed, they are dismissed without long-term security.

Poor investment in manufacturing and services further contributes to both structural and casual unemployment, as there are insufficient industries to absorb the growing labor force.

4. Study figure 2 below which represents economic recession as demonstrated by a decline in aggregate demand. Explain the factors which generally cause such aggregate demand curves to shift e.g. from AD_0, AD_1 to AD_2, AD_3.

One factor is a fall in consumer spending. If households reduce consumption due to lower income, higher taxes, or pessimism about the future, aggregate demand shifts leftward, leading to recession.

A decline in investment spending by firms is another factor. High interest rates, weak business confidence, or unfavorable policies may discourage investment, reducing aggregate demand.

Government spending cuts also shift aggregate demand leftward. When governments reduce expenditure on public projects, total demand in the economy decreases.

Falling exports can also reduce aggregate demand. If international markets contract or global prices of exports fall, countries like Tanzania experience reduced foreign earnings, decreasing aggregate demand.

Finally, monetary and fiscal policies that reduce liquidity, such as higher taxes or tight credit policies, reduce people’s purchasing power and shift aggregate demand downwards.

5. How can money supply in an economy be controlled by the Central Bank?

The Central Bank controls money supply through open market operations. It buys or sells government securities to regulate the amount of money circulating in the economy. Selling securities reduces money supply, while buying increases it.

It also uses the reserve requirement ratio. By increasing the percentage of deposits that commercial banks must hold as reserves, the Central Bank reduces their lending capacity, which lowers money supply.

The Central Bank adjusts interest rates through its discount rate policy. Raising rates makes borrowing more expensive, reducing credit creation and money supply, while lowering rates has the opposite effect.

Foreign exchange control is another method. By managing currency reserves and exchange rates, the Central Bank can influence liquidity in the economy.

Finally, the Central Bank can apply credit control measures such as limiting or encouraging bank lending to certain sectors, directly influencing how much money flows into the economy.

6. Explain why in a developing country like Tanzania much of government revenue is collected from indirect taxes.

In Tanzania, much government revenue comes from indirect taxes because they are easier to administer. Taxes such as Value Added Tax (VAT), excise duties, and customs duties are collected at points of sale or import, reducing the chances of tax evasion compared to direct taxes on income.

A large proportion of the population in Tanzania works in the informal sector, where incomes are difficult to track. Since many workers are not formally registered, it is easier for the government to tax consumption through indirect taxes rather than income.

Indirect taxes provide a steady flow of revenue because people consume goods and services daily. This ensures a constant source of income for the government to finance its expenditure.

Another reason is that indirect taxes are less visible to consumers compared to direct taxes. People often pay them unknowingly as part of the price of goods, which makes them politically easier for the government to implement.

Finally, indirect taxes also help the government control imports and encourage local industries. By imposing tariffs on imported goods, the government not only raises revenue but also protects domestic production.

7. (a) Distinguish between balance of trade and balance of payments.

Balance of trade refers to the difference between the value of a country's exports and imports of goods in a given period. If exports exceed imports, there is a trade surplus, but if imports exceed exports, there is a trade deficit.

Balance of payments is a broader concept. It records all financial transactions between residents of a country and the rest of the world, including trade in goods and services, investment flows, foreign aid, and capital transfers. It gives a full picture of a country's economic relations with the outside world.

(b) Argue why it is always safer to have a favourable balance of trade than to have a favourable balance on the capital account.

A favourable balance of trade is safer because it reflects real productive capacity. When a country exports more than it imports, it earns foreign exchange from goods and services, which is sustainable and based on economic strength.

By contrast, a favourable balance on the capital account often depends on foreign loans, investments, or aid. These flows can be unstable, as they may stop suddenly if investors lose confidence or if donor policies change.

Trade surpluses create jobs and stimulate domestic industries, while capital account surpluses may lead to debt accumulation and dependence on external financing.

Moreover, a favourable balance of trade strengthens a country's currency by increasing demand for its goods abroad, while reliance on capital inflows can cause instability in exchange rates.

Therefore, a trade surplus is safer because it is built on production and competitiveness, making it more sustainable than capital inflows.

6. **(a) What are the advantages of international economic integration?**

International economic integration increases trade opportunities among member countries. By reducing tariffs and barriers, countries can access larger markets for their goods and services.

It allows for specialization and efficiency. Countries focus on producing goods where they have comparative advantage, leading to better use of resources and higher productivity.

Integration attracts foreign direct investment, since investors prefer large, unified markets with reduced trade restrictions. This brings capital, technology, and employment.

It strengthens political and economic cooperation, reducing conflicts and fostering regional stability. Shared economic interests encourage peace and development.

Finally, consumers benefit from lower prices and more variety of goods due to competition and free movement of products within integrated regions.

(b) Explain two (2) forms of international economic integration.

One form is a **free trade area**, where member countries agree to remove tariffs and trade barriers among themselves, but each country maintains its own external trade policies. An example is the African Continental Free Trade Area (AfCFTA).

Another form is a **customs union**, where member states not only remove internal trade barriers but also adopt a common external tariff policy towards non-members. This creates uniformity in trade relations with outside countries.

9. What are the main features of an economic plan?

An economic plan has clearly defined objectives such as reducing unemployment, achieving growth, and improving living standards. These goals guide resource allocation.

It is time-bound, usually covering a specific period such as five years, within which targets must be achieved.

It involves resource allocation. Scarce resources like capital, labor, and land are directed towards prioritized sectors to maximize benefits.

It relies on government coordination. Plans are often prepared and supervised by central authorities to ensure consistency.

Finally, an economic plan is flexible. It can be revised in response to changing economic conditions such as inflation, drought, or global crises.

10. Why is the tertiary sector, especially finance and banking, still small compared to the primary and secondary sectors in Tanzania in terms of employment?

The tertiary sector is small in employment because Tanzania is still a developing country with a large share of its population engaged in agriculture. The majority of people rely on farming for survival, leaving fewer employed in services like finance and banking.

Industrialization in Tanzania is still limited, so the secondary sector also provides fewer jobs compared to agriculture. Since the tertiary sector depends on growth in industry and commerce, its employment base remains narrow.

Another factor is the low level of financial inclusion. Many people in rural areas do not use banking services due to lack of access, awareness, or income. This reduces the expansion of finance and related services.

The skills required for tertiary sector jobs are more advanced. Since education and training levels are still developing, fewer people qualify for employment in banking, insurance, and modern services.

Finally, infrastructure and technology limitations restrict the growth of services. Without widespread internet, electricity, and transport, modern service industries cannot expand as quickly as primary activities.