MACHAKOS UNIVERSITY

University Examinations for 2017/2018 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF ECONOMICS

THIRD YEAR SECOND SEMESTER EXAMINATION FOR

BACHELOR OF EDUCATION

BACHELOR OF COMMERCE

EAE 313: PUBLIC FINANCE

DATE: 11/12/2017 **TIME: 2:00 – 4:00 PM**

INSTRUCTIONS

Answer Question **ONE** and any other **TWO**questions

QUESTION ONE (COMPULSORY) (30 MARKS)

a) A car manufacturer has decided to make a significant investment into expanding its presence in Africa by setting up a large assembly facility in Kenya. It has estimated its initial set up costs to be in the region of Kenya Shillings 6,398M.

Forecast net income from the project is detailed as follows:

Year 1, Kenya Shilling 1,400M

Year 2, Kenya Shilling 1,450M

Year 3, Kenya Shilling 1,550M

Year 4, Kenya Shilling 1,625M

Year 5, Kenya Shilling 1,480M.

Required;

Calculate the Net Present Value of the project using a discount factor of 5% and comment on the attractiveness of the project. (12 marks)

b) Discuss 5 rationales for government intervention in private sector activities (10 marks)

c) State and explain four constraints to growth of government expenditure. (8 marks)

QUESTION TWO (20 MARKS)

a) Discuss five cannons of a good tax system (10 marks)

b) Give 5 differences between public goods and private goods. (10 marks)

QUESTION THREE (20 MARKS)

a) Discuss 4 instruments of fiscal distribution and stabilization policies. (8 marks)

b) Using a well-labelled diagram, demonstrate the how market failure would result if the agents engage in uncompetitive practices. (7 marks)

c) Explain the two major properties of pure public goods. (5 marks)

QUESTION FOUR (20 MARKS)

a) Define the term externality (2 marks)

b) Discuss any six ways in which externalities can be corrected. (12 marks)

c) State and explain the three main types of budgets (6 marks)

QUESTION FIVE (20 MARKS)

a) Differentiate between the following terms (8 marks)

i) In-rem taxes and personal taxes
ii) Callable public debt and redeemable public debts
iii) Benefit principal to tax equity and Ability-to-Pay principal to tax equity
iv) Bowen model and Efficient allocation model

b) Use a well-labeled diagram to illustrate the consequence on tax incidence of imposing a unit tax on a commodity. (7 marks)

c) Briefly describe 5 ways in which a state corporation can be privatized (5 marks)