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UNIVERSITY EXAMINATIONS

2012/ 2013 ACADEMIC YEAR

FOR THE DIPLOMA OF
BUSINESS MANAGEMENT

COURSE CODE: ECO205(ECO 311) **COURSE TITLE:** INTERMEDIATE MACRO ECONOMIS

DATE: 19th August 2013. **TIME:** 2.00pm – 5.00pm

Instructions to Candidates

- Answer any four questions

QUESTION ONE

(a) Define implicit GOP deflator (2 marks)

(b) Distinguish between the following terms as used in macroeconomics

(i) Real GDP and nominal GDP (2 marks)

(ii) Aggregate income and per capital income

(iii) Gross domestic product (GDP) and Gross National product (GDP) (2 marks)

(c) Suppose the goods K and L are the only goods product in the economy and that economy and that they are sold in the quantities and at the prices indicated the following.

Table :

Year	Quantity	Price	Quantity	Price
		Kshs		Kshs
2004	5	6	10	8
2005	6	6	12	15
2006	6	10	12	20

(i) Computer nominal GDP IN EACH YEAR

(ii) Compute real GDP using 2004 as the base year in each year for the three years (2 marks)

(iii) In which year was there growth and by what percentage

(iv) Calculate the GDP deflator for 2005 and 2006 (2 marks)

(d) Using a well labeled diagram, with price on vertical axis and real output on horizontal axis, what would happen an aggregate demand when the government increases taxes (9 marks)

QUESTION TWO

(a) Assume the business firms become pessimistic and expect a recession, inventories and also want to buy less new plant and equipment. With the help of a well, lableled diagram, explain what would happen to the income, planned savings and investment when there is a shift(decrease) in the investment function (12 marks)

(b) Using your knowledge gained in macroeconomics course, explain three positive effects of tax cuts (reduction in taxes) an economic performance of a developing country (10 marks)

(c) What do you understand by balance of payment (3 marks)

QUESTION THREE

(a) State thre functions of money (3 marks)

(b) When the economy of a country is experience unemployment or a recessionary gap, the government can institute an expansionary monetary policy with an aim of increasing money supply. To achieve this, the central bank can take one or both of the following actions.

i) Buy government securities/bonds from commercial banks and the public in the open market

ii) Switch government deposits to the commercial banks or both

iii) Explain in detail the effect of the above government actions (14 marks)

(c) State and explain the objective of monetary policy (8 marks)

QUESTION FOUR

a) Explain the functions of central monetary authorities (10 marks)

b) Foreign exchange marked intervention occurs when government buys or sells foreign exchange in an attempt to influence the exchange rate. State the reasons why government through central banks intervene (5 marks)

c) Using a relevance illustration , explain how is LM curves are derived indicating the level of general equilibrium (10 marks)

QUESTION FIVE

a) Differentiate between marginal propensity to consumer (MPC) and marginal prosperity to save (mps)

b) Derive the relation between output and the components of demand, government and net exports (5 marks)

c) The table below gives some hypothetical consumption and saving schedules

INCOME	CONSUMPTION	SAVINGS
0	60	-60
100	140	-40
200	220	-20
300	300	0
400	380	20
500	460	40
600	540	60

Graph the above information of consumption saving on the vertical axis and real output (income) on the horizontal axis

a) Determine the level of consumption when income is zero (5 marks)

b) Determine the marginal propensity to consume (slope) (5 marks)

c) Determine the marginal propensity to save (5 marks)

QUESTION SIX

a) Write short notes on the following

i) Consumer price index
ii) Transfer payments
iii) Frictional unemployment
iv) Crowding out effect
v) Liquidity (15 marks)

b) Monetary policy is one of the tools used by the government to try to keep the economy growing at a reasonable rate, with low inflation. If the economy is in liquidity trap. Explain the effect of monetary policy carried out through open market operation and the changes in the quality of money on the interest rate and level of income (10 marks)