

Uva Wellassa University
B.Sc. in Export Agriculture



End Semester Examination August/September 2011
Year III Semester II

Macroeconomics EAG 329-2

Instructions

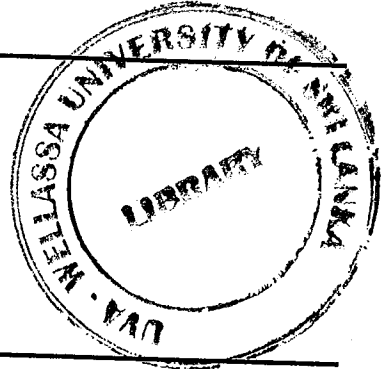
Answer **all** questions. Each question bears equal marks.

No. of questions : Five (05)

No. of pages : Four (04)

Total marks allocated : 100%

Time : Two Hours (02 hrs)



Question 01

Comment on following statements.

- i. The most disadvantage of any recession is a rise in unemployment rate.
- ii. Cutting taxes will have dual impact on economy.
- iii. Money market equilibrium implies that an increase in the interest rate is accompanied by an increase in the level of income.
- iv. Cost push inflation is from the production side rather than consumption side which is the case with demand – pull inflation.

Question 02

a. Given, $GNP = \$ 5000$; $Personal\ disposable\ income = \$ 4100$;

$Government\ budget\ deficit = \200 ; $Consumption = \$3800$; $Trade\ deficit = \$100$

Calculate:

- i. Savings
- ii. Investment
- iii. Government Spending

b. Consider an economy that produces & consumes bread & automobiles. Following table gives the data for two different years.

	Year 2000	Year 2010
Price of an automobile	Rs. 50, 0000	Rs. 60, 000
Price of a loaf of bread	Rs. 10	Rs. 20
Number of automobiles produced	100	120
Number of loaves of bread produced	500,000	400,000

- i. Using the **year 2000** as the base year, compute the following statistics for each year:
 - Nominal GDP
 - Real GDP
 - The implicit price deflator for GDP
- ii. How much have prices risen between **year 2000** and **year 2010**?
- iii. What does the Consumer Price Index measure?
- iv. Do increases in the CPI always indicate an increase in the consumer's cost of living?

Question 03

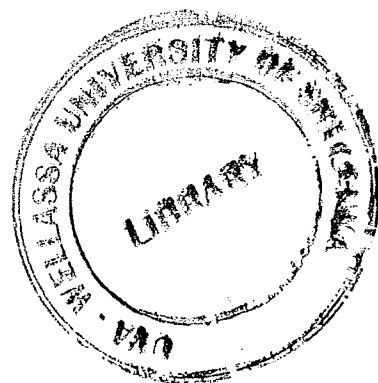
a. According to the IS – LM model, what happens to the interest rate, income, consumption and investment under the following circumstances? Support your answer with suitable diagrams.

- i. The Central Bank increases the money supply.
- ii. The government increases government purchases.
- iii. The government increases taxes.
- iv. The government increases government purchases and taxes by equal amounts.

b. You are given following information on a hypothetical economy. (all values are in million rupees)

- $C = 0.8 Y_d$ (Consumption function)
 $I = 300 - 30i$ (Investment)
 $T = 200 + 0.2 Y$ (Tax)
 $G = 400$ (Government expenditure)
 $TR = 50$ (Transfers)
 $L = 0.3Y - 12i$ (Demand for money)
 $M_s = 150$ (Real money supply)

- i. What is the equation of IS curve?
- ii. What is the equation of LM curve?
- iii. What is the equilibrium level of national income?



Question 04

a.

- i. What is a balance of payments statement?
- ii. Use the data given below to measure a country's **Balance on Merchandize Trade, Balance on Capital Account and Balance of Payment**

The United States exports goods valued at **\$19,650**

The United States imports merchandized valued at **\$ 21, 758**

U.S. citizens receive interest income of **\$3621** from foreign investments

Interest income of **\$1394** is paid on foreign owned assets in the United States

U.S. citizens travel expenditures equal **\$1919**

Foreign travel in the United States is **\$1750**

U.S unilateral transfers are **\$ 2388**

U.S. Capital Outflow is **\$ 4174**

U.S. Capital Inflow is **\$6612**

- b. What is crowding out and when would you expect it to occur? In the case of substantial crowding out which of the policies are more effective.

Question 05

- a. Suppose **Consumption (C) = \$30 + 0.80Y_d**, **Net Tax (NT) = \$50**,

Investment (I) = \$60, **Government Spending (G) = \$50** and

Net Export (X) = \$50 - 0.05Y

- i. Find the equilibrium level of income.
 - ii. Find the net export balance at the equilibrium level of income.
 - iii. What happens to equilibrium income and the net export balance when investment increases from **\$60 to \$70**?
 - iv. What happens to equilibrium income and the net export balance when the net export function changes from **\$50 - 0.05Y** to **\$40 - 0.05Y**?
 - v. Which has the greater effect upon an economy's net export balance: a change in autonomous domestic spending or a change in autonomous net exports?
- b. **Inflation is always and every where a monetary phenomenon**". Do you agree? Give reasons.