



MACHAKOS UNIVERSITY

University Examinations for 2019/2020 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF ECONOMICS

FOURTH YEAR FIRST SEMESTER EXAMINATION FOR

BACHELOR OF SCIENCE (AGRIBUSINESS MANAGEMENT AND TRADE)

AGB 411: MACROECONOMICS THEORY II

DATE: 10/12/2019

TIME: 11.00-1.00 PM

INSTRUCTIONS:

- i) Answer question ONE and any other TWO questions. Question one carries 30 marks and the other questions carry 20 marks each.
- ii) Do not write on the question paper

QUESTION ONE (30 MARKS)

- a) Explain any five differences between the classical theory of output, income and employment and Keynesian theory. (10 marks)
- b) You are provided with the following information about the commodity and money markets of a closed economy without government intervention.

Commodity market

$$C = 50 + \frac{2}{5}(Y)$$

$$I = 790 - 21r$$

Money market

$$M_{DT} = \frac{1}{6}(Y) \text{ -transaction demand for money}$$

$$M_{DS} = 1200 - 18r \text{ -speculative demand for money}$$

$$MS = 1250 \text{ -Money supply}$$

Required:

- i) Determine equilibrium levels of income and interest rate for this economy. (6 marks)
 - ii) Using a well labelled diagram, illustrate equilibrium conditions in part (i) (4 marks)
 - iii) If money supply increases by 50, what would be the effect on the equilibrium level of income and rate of interest? (2 marks)
- c) What is the cost of inflation to an economy? (8 marks)

QUESTION TWO (20 MARKS)

- a) With the aid of well labelled diagrams, describe how a country using a fixed exchange rate system eliminates a deficit in the balance of payment. (8 marks)
- b) Briefly explain how monetary policy affects inflation and output when the economy is at;
- Full employment
 - Not at full employment (8 marks)
- c) Explain the difference between the devaluation of a currency and the depreciation of a currency. (8 marks)

QUESTION THREE (20 MARKS)

- a) In what ways is knowledge of consumption theories helpful in the economic decision making and management? (10 marks)
- b) Discuss the main macroeconomic policy objectives that any responsible government would strive to achieve. (10 marks)

QUESTION FOUR (20 MARKS)

- a) On what grounds did Keynesian criticize Says Law? (10 marks)
- b) Explain the likely effects of expansionary monetary policy in the Kenyan economy. (10 marks)

QUESTION FIVE (20 MARKS)

- a) A country's national income model is expressed as follows:

$$Y = C + I + G$$

$$C = C_0 + C_1 Y$$

$$I = I_0$$

$$G = G_0$$

Required:

- Solve the equilibrium values of \bar{Y} and \bar{C} . (4 marks)
 - Derive:
 - Government expenditure multiplier. (2 marks)
 - Investment multiplier. (2 marks)
 - Autonomous consumption multiplier. (2 marks)
- b) In your view, why has an unemployment become an issue of concern in developing countries? (10 marks)