



MACHAKOS UNIVERSITY

University Examinations for 2019/2020 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF ECONOMICS

FOURTH YEAR SPECIAL/SUPPLEMENTARY EXAMINATION FOR

BACHELOR OF ECONOMICS AND STATISTICS

BACHELOR OF SCIENCE IN AGRIBUSINESS MANAGEMENT

AGB 411: INTERMEDIATE MACROECONOMICS

DATE: 22/1/2021

TIME: 11.00-1.00PM

INSTRUCTIONS:

- (i) Answer question one (Compulsory) and any other two questions
- (ii) Do not write on the question paper
- (iii) Show your working clearly

QUESTION ONE (COMPULSORY) (30 MARKS)

- a) Explain the following concepts:
 - i. Fiscal Policy and Monetary Policy (2 marks)
 - ii. Discretionary and Automatic Stabilization (2 marks)
 - iii. Demand side and Supply side of the economy (2 marks)
- b) Using a well labeled diagram explain why the total output will not change assuming that everyone decides to save more at every interest rate (10 marks)
- c) Using a well labeled diagram explain adjustment to balance of payment deficit under flexible exchange rate (10 marks)
- d) Why do the public desire to keep a portion of its wealth in money form yet money earn no interest? (4 marks)

QUESTION TWO (20 MARKS)

- a) Discuss the main features of the permanent income hypothesis and its application in African context (10 marks)

- b) Using economic tools of analysis, demonstrate and explain the shape of IS curve under closed economy and open economy (10 marks)

QUESTION THREE (20 MARKS)

- a) The following equations relate to a certain economy:

$$T = 0.75Y \text{ (Tax rate)}$$

$$L = Y - 100r \text{ (Real money demand)}$$

$$M = 300 \text{ (Real money supply)}$$

$$I = 20 - 10r \text{ (Investment function)}$$

$$G = 30 \text{ (Government purchases)}$$

$$C = 200 + 0.25Y^d \text{ (Consumption function)}$$

Required

- i. Derive equations for IS and LM curves (6 marks)
 - ii. Determine the r and y pair at which the two markets are clearing (4 marks)
 - iii. Compute the values of C , I and L (6 marks)
- b) Explain the difference between devaluation and appreciation of currency (4 marks)

QUESTION FOUR (20 MARKS)

- a) Explain the effects of monetary policy in the three ranges of LM curve (10 marks)
- b) What do you understand by Balance of Payments (2 marks)
- c) In case of a balance of payment surplus, illustrate and explain how the IS-LM-BP functions adjust to restore an economy to equilibrium under flexible exchange rate regime (8 marks)

QUESTION FIVE (20 MARKS)

- a) Using a well labeled diagram, show the equilibrium market rate of interest when speculative demand curve and speculative money supply intersect. Explain what happens when speculative money supply and speculative demand for money are not equal. (10 marks)
- b) Using well labeled diagrams and concept of aggregate demand and aggregate supply, illustrate how price is stabilized when the economy is at full employment and when it is not at full employment level. (10 marks)