



MACHAKOS UNIVERSITY

University Examinations for 2021/2022 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS
DEPARTMENT OF ECONOMICS
SECOND YEAR SEMESTER EXAMINATION FOR
BACHELOR OF ECONOMICS AND FINANCE
BACHELOR OF ECONOMICS AND STATISTICS
BACHELOR OF COMMERCE
BACHELOR OF ECONOMICS
BACHELOR OF ARTS

EET 201: MACROECONOMICS THEORY II

DATE:

TIME:

INSTRUCTIONS

1. Answer Question **ONE** and any other **TWO** questions
2. **Do not** write on the question paper.

QUESTION ONE (COMPULSORY) (30 MARKS)

- a) Critically examine whether the following statements are True or False. (5 marks)
- i) Expansionary fiscal policy leads to crowding out of private investors.
 - ii) Equilibrium in labor market is achieved when value of marginal product of labor is equal to labor supply.
 - iii) In his absolute income theory, Keynes assumes that consumption behaviour of individuals is interdependent.
 - iv) Classical macroeconomists argued that the economy is inherently unstable.
 - v) An increase in price leads to decrease in aggregate output.
- b) Classical aggregate supply curve is vertical. Critically examine the validity of this statement. (5 marks)
- c) Using relevant diagram and examples explain the effect of expansionary fiscal policy on the three ranges of LM function. (6 marks)

- d) In the 1930s a major world event occurred that gave rise to a new way of thinking about the operation of the macroeconomy. The rise of orthodox Keynesian macroeconomics
- i. List any four Keynesian macroeconomists that you know. (2 marks)
 - ii. Explain any six views of Keynesian macroeconomics. What makes their arguments different from classical views? (6 marks)
- e) Critically distinguish between permanent income hypothesis and life cycle income hypothesis. Use diagrams where necessary. (6 marks)

QUESTION TWO (20 MARKS)

- a) Using well labelled diagrams explain how a balance of payment deficit would be rectified under flexible exchange rate regime. (6 marks)
- b) Aggregate demand curve is downward sloping. Explain any four possible factors that would make this curve to shift. (8 marks)
- c) Using relevant examples distinguish between Say's law and Keynes Law. (6 marks)

QUESTION THREE (20 MARKS)

- a) Many developing countries have experienced worsening current account over years. Imagine you are a policy adviser in your country, advise the government on what are possible causes and remedies to this BOP disequilibrium. (10 marks)
- b) When income level is zero comrades' autonomous saving is negative. Critically explain the validity of this statement. (4 marks)
- c) Flexible exchange rates follow free market forces. Explain why it would be advisable for any economy to use flexible exchange rate system. (6 marks)

QUESTION FOUR (20 MARKS)

- a) Using Keynesian Cross and investment function explain how IS curve is derived. Use relevant diagrams and examples. (8 marks)
- b) Labour demand is a derived demand. Discuss any six determinants of labour demand in your country. (6 marks)
- c) Unemployment has been a challenge for many developing economies. What policy advice would you give to a government trying to reduce unemployment? (6 marks)

QUESTION FIVE (20 MARKS)

Write short notes on the following macroeconomic concepts

- i. Accelerator theory of investment
- ii. Monetary transmission mechanism
- iii. Long run aggregate supply curve
- iv. Backward bending labor supply curve
- v. Short run Phillips's curve