KIBABII UNIVERSITY

UNIVERSITY EXAMINATIONS
2021/2022 ACADEMIC YEAR

SPECIAL/SUPPLEMENTARY EXAMS

SECOND YEAR SECOND SEMESTER EXAMINATIONS

FOR
BACHELOR OF COMMERCE

COURSE CODE: ECO 221/ECO311/ECO205

COURSE TITLE: INTERMEDIATE MACROECONOMICS

DATE: 20TH JANUARY,2022 **TIME:** 11.00AM – 1.00PM

INSTRUCTIONS TO CANDIDATES

1. Answer a total of **three** questions; question **one** and any other **two** questions.
2. Question **one** carries **30 marks** and each of the other two questions carry **20** marks each.

QUESTION ONE

. a) Define the LM curve   (2 marks)

b) Define the aggregate supply curve   (2 marks)

c) Explain the two theories of aggregate supply   (6 marks)

d) Explain the permanent income hypothesis   (5 marks)

e) Explain the reasons for firms holding inventory   (5 marks)

f) Explain the various categories of investment   (5 marks)

g) What is the difference between the classical and Keynesian supply curve   (5 marks)

QUESTION TWO

a)A hypothetical closed economy has a national income model of the form $Y = C + I + G$ where $C = 60 + 0.8Y$ and I and G and private investment and government expenditure are exogenously determined at 100 and 160 units respectively.

Compute the national equilibrium level of income for this economy using aggregate income equals aggregate expenditure and withdrawals and equal injection methods   (10 marks)

b) Briefly explains the Keynesian Theory of Consumption   (5 marks)

c) Use the theory of liquidity preference to explain why an increase in the supply of money lowers the interest rate   (5 marks)

QUESTION THREE

In the Keynesian cross model, assume that the consumption function is given by $C=200+0.75(Y-T)$ and planned investment=100, government purchases and taxes are ach of them100

a) Draw a graph of planed expenditure as a function of income   (5 marks)

b) What is equilibrium level of income? (5 marks)

c) If government purchases increase to 125 what is the new equilibrium income(5 marks)

d) What level of government purchases is needed to achieve the income of 1600? (5 marks)

QUESTION FOUR

Suppose the money demand function is M d= 1000- 100r and the price level is 2 .

a)Graph the supply and demand for real money balances(5 marks)

b). What is equilibrium interest rate? (5 marks)

c). Assume the price level is fixed .what happens to equilibrium interest rate if the supply of money is raised from 100 to 1200
(5 marks)

d). If the central bank was to raise the interest rate to 7%,what money supply should it set? (5 marks)

QUESTION FIVE

a) According to Mundell Fleming model, when the exchange rates are fixed and capital is perfectly mobile will fiscal and monetary policy be more successful? Explain   (10 Marks)

b) What are the advantages of floating exchange rates and fixed exchange rates? (5 marks)

c) Discuss the Keynesian consumption function   (5 marks)