



(Knowledge for Development)

**KIBABII UNIVERSITY
UNIVERSITY EXAMINATIONS**

2021 / 2022 ACADEMIC YEAR

**SECOND YEAR SECOND SEMESTER
MAIN EXAMINATION**

FOR THE DEGREE OF BACHELOR OF COMMERCE

COURSE CODE: ECO221

COURSE TITLE: INTERMEDIATE MACROECONOMICS

DATE: 31ST AUGUST, 2022 TIME: 9.00AM - 11.00AM

INSTRUCTIONS TO CANDIDATES

1. Answer Question One in Section A and Any other TWO (2) Questions in Section B
2. Question **one** carries **30** marks and each of the other two questions carry **20** marks each.

TIME: 2 Hours

KIBU observes ZERO tolerance to examination cheating

This Paper Consists of 6 Printed Pages. Please Turn Over.

QUESTION ONE [30 MARKS]

- a) Define the term 'Price control' (2 Marks)
- b) With reference to the four sector economy, describe the circular flow of income and expenditure indicating the direction of money and products(4 marks)
- c) Let the following variables represent the structure of a small theoretical open economy with perfect capital mobility and flexible exchange rates

Consumption(C) $C = 80 + 0.6Y^d$, Government expenditure (G) = 84
Autonomous tax(T) $T = 60$ Autonomous investment (I) = $70 - 10r$
Net Exports (NX)= $100 - 0.1Y$, Money demand (M/P) $d = 0.2Y - 4r$
Money Supply(MS) = 60

Required:

- i) Assume that initially foreign and domestic interest rates be equal. Formulate the IS and LM equations [4 marks]
- ii) Determine the equilibrium income (Y), interest rate (r) and net exports [5 marks]
- iii) Suppose that the central bank thinks that income(Y) is too high and reduces the money supply from 60 to 56 in order to reduce GDP. Find the new equilibrium values of (Y), (r) and NX) [5 marks]
- iv) After the central bank's intervention of (C), the government thinks that as a result of the intervention NX is too low. In order to increase NX, the government reduces spending by 10. Find the ne equilibrium values of (Y), (r) and NX) after the reduction in G [5 marks]
- v) You are a chief economic advisor in the hypothetical economy. Do you believe that fiscal policy is more potent than the monetary policy? Justify the statement [5 marks]

QUESTION TWO (20 MARKS)

- a) Describe the process of building an economic model [4 marks]
- b) Assume an economy has the following models with figures measured in billions of shillings
 $C=50 + 0.8Y_d$
 $T = 0.25Y$

$$M=5 + 0.1Y$$

$$I_0 = 100$$

$$G_0 = 50$$

$$X_0 = 10$$

$$TR_0 = 25$$

- i) Compute the national income at equilibrium, consumption at equilibrium, imports and taxes at equilibrium [7 marks]
- ii) Compute the imports multiplier [3 marks]
- iii) How much additional government expenditure will be required to increase equilibrium income by 50 billion shillings? [3 marks]
- iv) At equilibrium, does the economy have a trade deficit or trade surplus and by how much. [3 marks]

QUESTION THREE (20 MARKS)

- a) Justify why money wages are supposed to be rigid downward and not upward [8 marks]
- b) Define the following;
- i. Stock and Flow Variables [4 marks]
 - ii. Absolute-Income Hypothesis [4 marks]
 - iii. Static, Comparative Static and Dynamic Analysis [4 marks]

QUESTION FOUR (20 MARKS)

- a) Examine the concept of consumer sovereignty as applied in economic analysis [2 marks]
- b) Assess 5 factors that limit consumer sovereignty [10 marks]
- c) Analyse the four main goals of macroeconomic policy in developing countries [8 marks]

QUESTION FIVE (20 MARKS)

- a) Examine five factors that limit the effectiveness of the monetary policies in developing countries [10 marks]
- b) Outline the main causes for rise in the unemployment levels in developing countries

[4 marks]

- c) Suggest the possible remedy measures to contain unemployment crisis in developing countries [6 marks]