

CHUKA



UNIVERSITY

**UNIVERSITY EXAMINATIONS**

**FIRST YEAR EXAMINATION FOR THE AWARD OF DEGREE  
OF BACHELOR OF COMMERCE**

**ECON 121: PRINCIPLES OF MACROECONOMICS**

**STREAMS: BCOM (Y1S2)**

**TIME: 2 HOURS**

**DAY/DATE: WEDNESDAY 07/8/2019**

**8.30 A.M. – 10.30 A.M.**

**INSTRUCTIONS: ANSWER QUESTION ONE AND ANY OTHER TWO QUESTIONS**

**QUESTION ONE (30 MARKS)**

- (a) Distinguish between the following pair of terms as used in macroeconomics [10 marks]
- (i) Injections and withdrawals
  - (ii) Autonomous consumption and marginal propensity to consume
  - (iii) Consumer price index and producer price index
  - (iv) Frictional unemployment and structural unemployment
  - (v) Depreciation and devaluation of currency
- (b) According to Keynes, people hold money for transactions, precautionary and speculative purposes. Discuss 3 factors that determine the amount of money held for transaction purposes. [6 marks]
- (c) The commodity and money markets for an economy are defined by the following equations:
- $$C = 200 + 0.4Y$$
- $$I = 1900 - 12r$$

## ECON 121

Money market

$M_{Dr} = 0.5Y$  (Transactions and precautionary money demand)

$M_{DS} = 100 - 10r$  (Speculative money demand)

$MS = 1500$  (Money supply)

- (i) Derive the IS and LM functions for the economy. [2 marks]
- (ii) What is the equilibrium income, rate of interest and consumption for the economy? [6 marks]
- (d) Discuss 3 measures used to correct a trade deficit [6 marks]

### QUESTION TWO (20 MARKS)

- (a) Discuss the major goals of macroeconomic policy [8 marks]
- (b) With the aid of diagram, discuss the circular flow of income in a four sector economy [8 marks]
- (c) Given the savings function as  $S = -A + Y$  (I-b), derive the corresponding consumption function and prove that  $MPC + MPS = 1$  [4 marks]

### QUESTION THREE (20 MARKS)

- (a) Although national income is a measure of economic growth of a country, higher per capita income does not necessarily imply better living standards for citizens of a country. Discuss this statement and give illustrations. [8 marks]
- (b) Outline the difficulties encountered in measuring national income. [6 marks]
- (c) National income accounting and statistics are important to a number of people in an economy. What are some of the uses of national income accounting? [4 marks]

### QUESTION FOUR (20 MARKS)

- (a) Discuss the disadvantages of a high rate of inflation on a country. [6 marks]
- (b) What are some of the policies that can be implemented to curb high inflation rates [6 marks]
- (c) Distinguish between a fixed and flexible exchange rate regimes. [4 marks]
- (d) Devaluation of currency can have both positive and negative implications on an economy. Discuss this statement and give clear examples. [4 marks]