

CHUKA



UNIVERSITY

UNIVERSITY EXAMINATIONS

EXAMINATIONS FOR THE AWARD OF DEGREE OF BACHELOR OF

ECON 222: INTERMEDIATE MACROECONOMICS

STREAMS:

TIME: 2 HOURS

DAY/DATE: WEDNESDAY 08/8/2018

2.30 P.M. – 4.30 P.M.

INSTRUCTIONS: Answer question ONE and any other TWO questions

1. Distinguish between the following concepts [10 marks]

- (i) Tax evasion and tax avoidance
- (ii) Expansionary and contractionary fiscal policy
- (iii) Marginal propensity to save and average propensity to save
- (iv) Structural and frictional unemployment
- (v) Rational and irrational expectations

2. Suppose you are given the following information about an economy

$$C = 80 + 0.8Y^d - i \quad \text{Consumption function}$$

$$T = 60 - i \quad \text{Tax function}$$

$$I = 200 - 10i - i \quad \text{Investment function}$$

$$G = 200 - i \quad \text{Government expenditure}$$

$$M_d = 0.4Y + 300 - 29i - i \quad \text{Money demand}$$

$$M_s = 470 - i \quad \text{Money supply}$$

- (a) Derive the IS and LM schedules [4 marks]
- (b) Calculate equilibrium consumption, tax, investment and money demand [4 marks]

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- (c) Suppose the government increases in expenditure by 200, what is the effect on equilibrium income? [2 marks]
- (d) Find out if the country has a balanced budget [4 marks]
3. Discuss the instruments of monetary policy [6 marks]

QUESTION TWO

1. “An expansionary monetary policy may only accelerate the rate of inflation and cause a higher level of unemployment in the long run”. Explain [8 marks]
2. Discuss the principles of a good tax system [6 marks]
3. Clearly explain the life cycle income theory of consumption [6 marks]

QUESTION THREE

1. Briefly explain the major contributions of the rational expectation theory [6 marks]
2. Discuss and illustrate the inflationary and deflationary gaps and explain how they can be removed [10 marks]
3. Discuss the Keynesian criticisms of classical macroeconomics pillars [4 marks]

QUESTION FOUR

1. With the help of diagrams, explain the effect of the following disturbances on variables in the classical macroeconomic model;
- (i) Increase in money supply [5 marks]
- (ii) Increase in demand for labor [5 marks]
- (iii) Increase in labor supply [5 marks]
2. Discuss the reasons why there’s need for a public sector in a country [5 marks]
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