

KABARAK



UNIVERSITY

EXAMINATIONS

2008/2009 ACADEMIC YEAR

**FOR THE DEGREE OF BACHELOR OF ECONOMICS AND
MATHEMATICS**

COURSE CODE: ECON 220

COURSE TITLE: INTERMEDIATE MACROECONOMICS

STREAM: Y2S2

DAY: WEDNESDAY

TIME: 2.00-4.00 P.M.

DATE: 10/12/2008

INSTRUCTIONS:

1. Answer questions ONE and any other TWO questions.
2. Question ONE carries 30 marks and the rest 20 marks each
3. Show all your workings clearly

PLEASE TURN OVER

1. Given the following information

$$\begin{aligned} C &= 1000 + 0.85Y^d && \text{(Consumption Function)} \\ I &= 200 + 0.2Y^d - 10r && \text{(Investment Function)} \\ G &= 400 && \text{(Government Spending)} \\ T &= -20 + 0.15Y && \text{(Tax Function)} \\ M^d &= 10 + 0.25Y - 10r && \text{(Money Demand)} \\ M^s &= 500 && \text{(Money Supply)} \end{aligned}$$

- (a) (i) Define and derive algebraically the IS and LM curves **(8 marks)**
(ii) Calculate equilibrium income and interest rate **(4 marks)**
(iii) Calculate government expenditure multiplier and interpret your results **(3 marks)**
(iv) Explain the main uses of income calculated in a (ii) above **(5 marks)**
- (b) Explain the various ways that can be used to correct unfavorable balance of payment (BOP) of a country. **(6 marks)**
- (c) Explain the objectives of fiscal policy in developing countries **(4 marks)**
- 2 (a) A country's X economic growth was 4.8% in 2006 and 5.2% in 2007, therefore, the standard of living of its citizens improved. Discuss. **(10 marks)**
- (b) (i) Explain the motives of holding money **(4 marks)**
(ii) Which motive of holding money is associated with the theory of liquidity preference and explain how this theory works? **(6 marks)**
3. (a) With reference to money market, show that a rise in money supply will shift the LM curve to the right by an amount equal to $\frac{I}{K} \Delta \left[\frac{M_o^s}{P_o} \right]$ **(10 marks)**
- (b) Define the term money and explain its main function. **(6 marks)**
- (c) Explain the factors that determine the level of investment in a country **(4 marks)**
4. The following information relates to country A

$C = 100 + 0.8Y^d$	(Consumption Function)
$I = 400$	(Investment)
$G = 600$	(Government Expenditure)
$X = 300$	(Exports)
$M = 50 + 0.2Y$	(Import expenditure function)
$T = 100 + 0.5Y$	(Tax Function)
$Y^d = \text{Disposable Income}$	

- (a) (i) Calculate equilibrium levels of income, tax, consumption and imports
(8 marks)
- (ii) State with reasons the position on the government expenditure so as to attain external and internal balance.
(3 marks)
- (iii) What changes are required in export and government expenditure so as to attain external and internal balance?
(3 Marks)
- (b) Explain the main limitations of national income accounting. **(6 marks)**
- 5 (a) Compare and contrast the life cycle and permanent income theories of consumption
(8 marks)
- (b) Using the life cycle hypothesis of consumption explain Kuznet's (1946) findings on consumption functions.
(6 marks)
- (c) Explain in detail the main factors that influence consumption in a country
(6 marks)