JARAMOGI OGINGA ODINGA UNIVERSITY OF SCIENCE AND TECHNOLOGY

SIAYA CAMPUS

UNIVERSITY EXAMINATIONS 2019/2020

YEAR 4 SEMESTER 2 EXAMINATION FOR THE DEGREE OF BACHELOR OF AGRIBUSINESS MANAGEMENT

SCHOOL OF AGRICULTURE AND FOOD SECURITY

BEN 3426: INTERMEDIATE MACROECONOMICS

(SPECIAL /SUPPLEMENTARY EXAMS)

Date: Time: 3 HOURS

DATE-11/11/20 EXAM SESSION:7-10AM

INSTRUCTIONS:

1.Attempt question ONE and any other TWO questions.

Question one carries 30 marks.

2. Candidates are advised to write on the text editor provided, or to write on a foolscap, scan and upload alongside the question

3. Candidates must ensure they submit their work by clicking "finish and submit attempt" button at the end.

QUESTION ONE (COMPULSORY)

(a) Define the following terms;

- Lending margins with respect to direct control as a monetary policy tool (1mk)
- Induced consumption (1mk)
- Exogenously determined variables (1mk)
- Marginal propensity to import (MPM) (1mk)
- Consumption expenditure (1mk)
- Deposit mobilization effect (1mk)

(b) Illustrate with a diagram and explain the concept of the circular flow of income. (8mks)

(c) Briefly discuss theories of consumption behaviour in short and long run (8mks)

(d) Explain the concept of liquidity trap (8mks)

QUESTION TWO

a) The commodity and money market for an economy are defined by the following equations:

<u>The Commodity Market</u>

$$Y = C + I$$

$$C = 200 + \frac{2}{5}Y$$

$$I = 1900 - 12r$$

Where Y, C and I are national income function, consumption function and investment function respectively

<u>Money Market</u>

$$M_{DT} = \frac{1}{2}Y$$

$$M_{DS} = 100 - 10r$$

$$M_S = 1500$$

Where;

M_{DT}, M_{DS} and M_S are Precautionary &Transactions demand for money, Speculative demand for money and Money supply respectively

Required:

i) Derive the IS and the LM functions for the economy (4mks)

ii) What is the equilibrium income and the rate of interest rate? (4mks)

b) Explain the various motives of holding money. (6mks)

c) How can Central Bank of Kenya (CBK) impose direct control as a monetary policy instrument in order to achieve expansionary effect in the economy? (6mks)

QUESTION THREE

a) Briefly discuss some of the importance of circular flow of income with regard to government's decision on policy matters. (5mks)

b) Briefly discuss some of the variables that have strong influence on consumption. (5mks)

c) Highlight the factors that influence the decision to invest. (10mks)

QUESTION FOUR

a) Assume the following information represents the National Income Model of a 'Utopian' Economy.

$$Y = C + I + G$$
$$C = a + b(Y - T)$$
$$T = d + tY$$
$$I = I_O$$
$$G = G_O$$

Where $a > O; O < b < 1$
$d > O; O < t < 1$

T = Taxes
I = Investment
G = Government Expenditure

i) Explain the economic interpretation of the parameters a, b, d and t. (4mks)
ii) Find the equilibrium values of income, consumption and taxes. (8mks)

b) Highlight ANY FOUR concepts the CBK uses to distinguish money supply on the basis of their liquidity. (8mks)

QUESTION FIVE

a) Briefly explain the multiplier and accelerator principles. (3mks)

b) In a certain economy the marginal propensity to save is 0.2 and the autonomous consumption equals 400.

i. Formulate the consumption function. (3mks)
ii. If the Government's expenditures were to increase by 50% what would be the resultant change in National income. (3mks)

c) (i) Based on the circular flow of income analysis, explain why marginal propensity to consumer plus marginal propensity to save equals one. (4mks)

(ii) What is the relationship between the simple multiplier and marginal propensity to consume? (3mks)

(d) State some of the limitations posed by monetary policies employed by central banks in developing countries. (4mks)