Question Bank

Course Name: B.A. (Hons) Business Economics

Paper Name: Macro Economics and Application-II

Paper Number: C-8

Semester: 4th

1. Discuss the behaviour of income, consumption, saving and wealth over the life cycle of consumer according to the Life Cycle Hypothesis of consumption. Suppose an 80 year old and a 30 year old each received a lottery winning rupees one crore. Which one will increase their consumption more? Explain why.
2. Why is current consumption more responsive to current changes in income than what is suggested by Life Cycle – Permanent income hypothesis?
3. Explain flexible accelerator model of investment. Give 2 reasons why firms may respond to the difference between the desired and the already existing stock of capital and not related rental cost of capital.
4. What is the random walk hypothesis of consumption? What are its implications for economic policy?
5. Explain using diagrams, fisher's model of intertemporal choice.
6. The Life Cycle Hypothesis is a micro economic theory about an individual's lifetime consumption and saving patterns. Explain. How does the theory relate to aggregate consumption?
7. Explain the process of determination of equilibrium in the housing market in the short run. What are the factors that determine the position of demand curve?
8. Discuss the behaviour of income, consumption, saving and wealth over the life cycle of consumer according to the Life Cycle Hypothesis of consumption. Suppose an 80 year old and a 30 year old each received a lottery winning rupees one crore. Which one will increase their consumption more? Explain why.
9. Examine the effects a small open economy of Mundell – Fleming model of a fiscal expansion on income and the trade balance under fixed and floating rate regime.
10. What are the pros and cons of fixed exchange rate and floating exchange rate.
11. Consider the following statements. Give reasons in support of your answer

    1) The Solow growth model is based on production function which exhibits increasing returns to scale. True/False

2) The steady state level in Solow growth exists where stock of capital goods grows as investment is greater than rate of depreciation.
3) In the Solow growth model if an economy has more capital than in the golden rule steady state, then reducing saving will increase consumption at all points in time

12. In the process of population growth, using Solow model, explain the impact of increase in population growth on steady state level of capital. How does it explain why some countries are rich and others are poor? Discuss.
13. Use fisher model of consumption to analyse an increase in second period income. Compare the case in which consumer faces a binding constraint and the case in which he does not.
14. Explain that the cost of owning capital by a rental firm depends on relative price of capital goods, real interest rate and depreciation rate.
15. Do you agree with the following? Give reasons for your answers
    a) Investment tends to be higher when the nominal interest rate is lower.
    b) Investment tax credit reduces rental cost of capital
    c) A booming stock market is good for investment.
18. Explain Accelerator model of Inventories.
19. State Friedman theory of consumption hypothesis and its implications.
20. How do an expansionary (1) Fiscal policy and (2) Monetary policy affect the aggregate income, exchange rate and trade balance of a small open economy under the fixed exchange rate.
21. Discuss the equilibrium condition in a small open economy according to Mundell Fleming model, using the IS-LM framework.
22. "More elastic imports and exports are, the more likely is that real exchange depreciation or devaluation will improve the trade balance". Explain the above statement.
23. In real world, why do domestic interest rates differ from world interest rate? Are there any economic repercussions of their difference?
24. Assuming floating exchange rate and perfect capital mobility analyse the impact of expansionary monetary and fiscal policies both in the long run and short run.
25. What is the optimal inflation rate? Briefly explain the costs and benefits of inflation in the range of zero to four percent?
26. Derive an expression for a change in government debt between two periods and show that if government achieves a primary deficit of zero and maintain it then the ratio of debt to GDP increases at a rate equal to real interest rate minus growth rate of output.
27. Consider given statements below and give reasons in support of your arguments.

1) According to Mundell Fleming model, the demand for real balances depends negatively on interest rate (r), which is equal to the world interest rate (r*). True/ False
2) The vertical LM curve in Mundell Fleming model implies that exchange rate does not enter in to the LM equation at a given interest rate. True/ False
3) In the small open economy under floating exchange rate regime, expansionary fiscal policy results in an increase in level of income through depreciation of exchange rate. True/ False
4) The Mundell - Fleming model with a changing price level implies that a given money stock decline in price level shift inwards LM curve therefore lower level of income and appreciation of real exchange rate.

28. Explain how is population related to the steady state of capital? How does a change in population affect this steady state?
29. What role is played by technology in explaining differences in the growth rate of different countries? Explain.
30. List and explain the various sources of growth