Question Bank

Course B.A (Hons)Business economics III Sem

(2018 – 2019) Odd semester

Paper C5 Macro Economics and applications - I

1. Give reasons in support of your argument & explain briefly
    a. An increase in marginal propensity to save results in higher value of multiplier in a closed economy. True/ False
    b. Bond Prices and Interest rate are inversely related. True/ False
    c. An increase in consumer confidence, in short run, leads to an increase in equilibrium output of closed economy IS-LM model. True/False
    d. Expansionary open market operations are, one in which the central bank decreases the money supply by buying bonds leading to an increase in the price of bonds and a decrease in the interest rate. True/ False.
    e. The natural rate of unemployment is unaffected by policy changes. True/ False
    f. Bond prices and Interest rates are positively related.
    g. Winning of a lottery price is not included in national income.
    h. If individuals decide to increase their private saving rates, it can lead to a fall in general consumption and lower output.
    i. The production of an economy car contributes more to GDP than the production of luxury car
    j. The Wholesale Price Index is used more widely than the Consumer Price Index.
2. Can Gross Domestic Product be used as an index of welfare of the people? Why is it desirable for a country to have a large GDP? Give an example that would raise GDP and yet be undesirable.
3. What is CPI? Does an increase in the CPI always indicate an increase in the consumer's cost of living?
4. Explain the relationship between real demand for money, real income and real rate of interest. Using these relationships, derive LM curve
5. Explain that an initial shift in demand causes an increase in output that is larger by a factor equal to the multiplier. Illustrate your answer with suitable diagram and equations.
6. GDP only counts the production of goods in their final form during a given period of time. What are the various components of the final demand for goods?
7. Distinguish between GDP deflator and consumer price index (CPI). Also explain the significance of GDP deflator.

a) The following equations describe a three-sector economy:

Demand for money is M^D=0.20Y

Real Money supply is 200

C=90+0.80Yd,

T=50

$I=140-5i$

$G=50$

(i) Derive the IS and LM equations

(ii) Find equilibrium output, the rate of interest and investment.

(iii) Derive the IS equation when Government spending increases 20, ceteris paribus.

(iv) Find Equilibrium output, the rate of interest and investment when Government spending is 70

8. Given $C= 20+0.8Yd$

   $I = 60$

   $TA = 40$

   $TR = 10$

   $G = 30$

   Compute equilibrium level of income. Find the new equilibrium level of income when (G) increases from 30 to 40 and taxes (TA) increases from 40 to 50.

   ($Y = 430$, $Y = 440$)

9. $C= 40 + 0.75\ Y$

   $I = 60$

   Determine equilibrium income, consumption, and savings. Show that at equilibrium level, output is equal to spending and savings equal to investment.

   ($Y= 400$, $C= 340$, $S = 60$)

10. Assume the following model of the economy for closed economy IS-LM :
    i. $C = 0.8(Y^d)$
    ii. $T = 1{,}000$ $I = 800 – 20r$
    iii. $G = 1{,}000$
    iv. $M^d = 0.4Y – 40r$
    v. $M^S = 1{,}200$
    vi. $P = 1$

    Where C=Consumption, Y^d= Disposable Income T=Tax Revenue I= Investment, r=rate of interest, G=Government Expenditure, $M^{d=}$Demand for money, M^s=Money Supply P=Price level

    a. Derive formula for the IS curve, showing Y as a function of r alone.
    b. Derive formula for the LM curve, showing Y as a function of r alone.
    c. What are the short-run equilibrium values of Y, r, Y^d, C, I?
    d. Assume that G increases by 200. By how much will Y increase in short run equilibrium?

11. Assume that G is back at its original level of 1,000, but MS (nominal money supply) increases by 200. By how much will Y increase in short-run equilibrium?

12. How the interest rate is determined as being determined by the condition that the supply of central bank money be equal to the demand for central bank money.
13. How does decrease in the government deficit affect the price level, output level and the interest rate in the economy in the short run and the medium run?
14. State the equilibrium in terms of the equality of overall supply and overall demand for money.
15. Explain that the IS – LM model characterizes the implications of equilibrium in both the goods and the financial markets. What is the impact of expansionary fiscal policy on the economy's output and interest rate?
16. "An increase in autonomous spending has more than one for one effect on the equilibrium output" Explain diagrammatically.
17. Show that at the given interest rate, an increase in nominal income shifts the demand for money to the right.
18. How does commodity and money market interact to determine the short run equilibrium values of national income and rate of interest.
19. What are the effects of fiscal consolidation on output and the interest rate. Support your answer with diagrams.
20. Using wage setting and price setting relations explain the labour market equilibrium. Show that the natural rate of unemployment is associated with the natural rate of employment and natural output level.
21. "If wage decisions are staggered, disinflation must be phased in slowly to avoid an increase in unemployment". Explain in relation to Fisher and Taylor argument**.**
22. "Equilibrium in the labour market requires that the real wage chosen in the wage setting be equal to the real wage implied by price setting". Explain
23. What are the factors that determine unemployment and output in the medium run?
24. "Higher the mark up chosen by the firms, the lower the real wage implied by price setting decisions will be" Explain.
25. Show the effect of money growth on output, unemployment and inflation in both short run and medium run.
26. Using both the original and modified phillips curves, explain a relationship between unemployment rate and inflation rate.
27. How the inflation, output and unemployment are linked to each other?
28. "At very low or negative rates of inflation, the Phillips curve appears to become weaker" Comment
29. "Wage indexation increases the effect of unemployment on inflation" Explain the statement.
30. Discuss that the new Keynesian economics provides a better explanation of stickiness of wages and prices in the short run. Using quantity theory of money examine the links between inflation and economic growth.
31. How does Real Business cycle theory explain fluctuations in output and employment?
32. Explain the factors that determine wages in the labor market.
33. 'New Keynesian economics provided a better explanation of why wages and prices are sticky in the short run.' Explain.

34. Elaborate the dynamic effects of decrease in government budget deficit on price level, output and interest rate in an economy both in the short and medium run.
35. “Inflation is a monetary phenomenon” Explain the statement.
36. Write Short notes on
    a) Crowding out
    b) Liquidity trap
    c) Lucas critique
    d) Sacrifice ratio
    e) Paradox of savings
    f) Monetary policy and Transmission mechanism in short run IS-LM model
    g) Impact of policy mix in goods and money market.
    h) Hyperinflation