

UNIVERSITY OF SWAZILAND  
FACULTY OF SOCIAL SCIENCE  
DEPARTMENT OF ECONOMICS  
SUPPLEMENTARY EXAMINATION  
JULY 2010

**TITLE OF PAPER : MACROECONOMICS**

**COURSE CODE : ECON 203/IDE ECON 203-1 & 2**

**TIME ALLOWED : THREE (3) HOURS**

**INSTRUCTIONS:**

- 4) ANSWER ANY TWO (2) QUESTIONS FROM EACH SECTION.**
- 5) ALL QUESTIONS CARRY EQUAL MARKS OF 25 EACH.**
- 6) START EACH QUESTION ON A NEW PAGE.**

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## SECTION A

## QUESTION 1

- Derive the aggregate demand equations in the Simple Keynesian model with and without the government sector. (10 marks)
- Sketch the aggregate demand functions you derived in part (a) above. State the differences between these curves. (5 marks)
- Discuss the main features of the CMA. (10 marks)

## QUESTION 2

- Derive the money demand equation. Why is it downward sloping? Use graphs to illustrate your solution. (10 marks)
- Why are there a precautionary demand for money and a speculative demand for money? (6 marks)
- Elucidate what happens to the level of precautionary money balances when
  - Income payments are made less frequently.
  - Businessmen are certain about the level of spending.
  - When economic activity contracts such that households are not optimistic about the receipt of income. (3 each)

## QUESTION 3

- Graphically derive the IS curve equation. Explain clearly. Why does it slope downwards? (10 marks)
- Assume that the following equations describe the Swazi economy;

$$C = 500 + 0.65 YD$$

$$I = 200 + 0.2Y - 30i$$

$$\bar{G} = 400$$

$$T = -40 + 0.4Y$$

$$M_{ss} = 1000$$

$$M_{dd} = 20 + 0.5Y - 50i$$

- Derive the goods market equilibrium equation. (5 marks)
- Derive the money market equilibrium equation. (5 marks)
- Obtain the equilibrium interest rate. (2 marks)
- Obtain the equilibrium income. (3 marks)

**QUESTION 4**

- a) Discuss **any two** characteristics common to developing countries. (5 marks)
- b) Suppose the Central Bank of Swaziland increases the discount rate. Use the IS-LM model to analyse how this would affect income and interest rates in the economy. (10 marks)
- c) Write concise notes on each of the following:
  - (i) Monetary-fiscal policy mix.
  - (ii) Crowding out
  - (iii) Monetising budget deficits
  - (iv) Adverse supply shock
  - (v) Liquidity trap

(2 marks each)

**SECTION B****QUESTION 5**

- a) Outlining the underlying assumptions, derive the trade balance schedule. Show the deficit and surplus regions. Explain your derivation. (10 marks)
- b) Distinguish between internal and external balance. (5 marks)
- c) Analyze the effect of a fall in exports on equilibrium income, interest rate and the trade balance. Use a graph to illustrate your answer. (10 marks)

**QUESTION 6**

- a) In the Aggregate demand/aggregate supply model both monetary and fiscal policy fail to affect output. Do you agree? Explain using a graph. (10 marks)
- b) Illustrate and explain the three phases along the short run aggregate supply curve. (10 marks)
- c) List any two shift parameters of the aggregate demand and supply curves. (5 marks)

**QUESTION 7**

- a) A progressive income tax is considered as a built-in stabilizer. Why? (5 marks)
- b) Discuss the problems that policy makers face as they implement stabilisation policies. (10 marks)
- c) Define the following:
  - (i) Producer price index,

- (ii) Hyperinflation,
- (iii) Stagflation,
- (iv) Disguised unemployment
- (v) Technological unemployment. (2 marks each)

**QUESTION 8**

- a) In the General theory Keynes stressed the role played by effective demand in the economy. Do you agree? Explain. (5 marks).
- b) Outline the three building blocks of modern macroeconomics introduced by Keynes when deriving effective demand. (6 marks)
- c) Name two of the mathematical formalizations of Keynes General theory carried out by Economists. (4 marks)
- d) Write brief explanatory notes on each of the following;
  - (i) Lucas critique
  - (ii) New Keynesian economics
  - (iii) New Classical school of thought
  - (iv) Random walk of consumption
  - (v) Staggering of wage and price decisions (by Fischer and Taylor)

(2 marks each)