

THE OPEN UNIVERSITY OF SRI LANKA  
 BACHELOR OF MANAGEMENT STUDIES DEGREE PROGRAMME  
 LEVEL - 04  
 ASSIGNMENT TEST - 2017  
 MACRO ECONOMICS – MCU 2207



DURATION : TWO (02) HOURS

DATE : 15.10.2017

TIME : 2.00 p.m. – 4.00 p.m.

Instructions :

Answer any two (02) questions.

All questions carry equal marks (50 Marks).

Use of a non-programmable calculator is allowed.

Question No. 01

- a, “The knowledge in relation to Macro Economics theories and concepts could help a manager to make effective business decisions” Elaborate with examples. (15 Marks)
- b, How economic policy makers alter the policy mix depending on the different macroeconomic goals the government aims at achieving time to time? Explain with examples (23 Marks)
- c, Compare and contrast. (Use illustrations to explain your answer where necessary)
- i. Gross Domestic Product (GDP) and Gross National product (GNP).
  - ii. Three sector and Four sector Circular Flow of Income.
  - iii. Output approach and Expenditure approach in calculating National Income. (12 Marks)

Question No. 02

- a, Considering the below given information derive the Consumption and Savings functions. Explain both using illustrations. (Figures in Rs. Billions)
- Autonomous Consumption = 68                      Marginal Propensity to Save (MPS) = 0.2
- (10 Marks)
- b, Explain whether you “agree” or “Disagree” with the following statements.
- i. The value of the Marginal propensity to Save (MPS), has no impact on the size of the Expenditure Multiplier.
  - ii. As the number of sectors in the economy decreases, the size expenditure Multiplier too decreases. (10 Marks)

c. Details of a three sector economy given as; (Figures in Rs. Billions).

$$\bar{C} = 120 + bY_d \text{ (Consumption Function)}$$

$$MPS = 0.2 \text{ (Marginal Propensity to Save)}$$

$$\bar{I} = 100 \text{ (Autonomous Investments)}$$

$$\bar{T} = 20 \text{ (Autonomous Taxes)}$$

$$\bar{G} = 140 \text{ (Autonomous Government expenditure)}$$

- i. Calculate the equilibrium level of National Income (NI) using the details given above. (03 Marks)
- ii. Derive the savings function from the above consumption function and using the same calculate the equilibrium level of NI. (04 Marks)
- iii. In addition to autonomous taxes, if the government introduces an income tax of 10% and Transfer payments of Rs.10 billion ( $TR = \bar{T}0$ ), find the new equilibrium level of NI. (04 Marks)
- iv. Suppose the economy opens up and following changes take place.

$$\bar{X} = 68 \text{ (Autonomous Exports)}$$

$$M = 64 + 0.1Y \text{ (Import Function)}$$

Find the new equilibrium level of NI.

- v. What makes Exports autonomous and Imports a function? Explain. (05 Marks)
- vi. How could the depreciation of domestic currency against the currencies of its trading partners will affect domestic imports and exports? Explain. (05 Marks)
- vii. Suppose the domestic currency appreciates against the currencies of its trading partners and as a result autonomous exports changes by Rs. 4 billion and autonomous imports changes by Rs. 2 billion, calculate the new equilibrium of NI. (05 Marks)

### Question No. 03

- a, "IS curve highlights the combinations of interest rates and incomes that will bring the money market into equilibrium, and LM curve highlights the combinations of interest rates and incomes that will bring the goods/products market into equilibrium." Do you agree? Explain using illustrations. (06 Marks)
- b, Why is that the "IS" curve positively sloped and "LM" curve negatively sloped? Explain. (06 Marks)

- c. Using IS/Lm framework explain how the following changes influence the rate of interest and level of income in an economy.
- i. The government cuts down expenditure on infrastructure development.
  - ii. In order to increase government revenue, the government increases taxes.
  - iii. Commercial banks introduce strict conditions making it harder for people to obtain loans.
  - iv. The Central Bank reduces the interbank lending rates.
  - v. The Central Bank buys back the government bonds and securities from the public.
  - vi. The Central Bank increases the reserve requirement of commercial banks.
  - vii. The average price level in the economy decreases. **(28 Marks)**
- d. Explain whether you “agree” or “disagree” with the following statements. Provide illustrations to explain your answer.
- i. When demand for money does not depend on rate of interest at all, monetary policies are highly effective.
  - ii In Liquidity trap range fiscal policies are highly effective.

**(10 Marks)**

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