MACHAKOS UNIVERSITY COLLEGE

(A Constituent College of Kenyatta University)
University Examinations for 2015/2016

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF ECONOMICS

FIRST SEMESTER EXAMINATIONS FOR DEGREE IN

BACHELOR OF EDUCATION

BACHELOR OF ECONOMICS

EET 201: MACROECONOMIC THEORY II

DATE: 11/8/2016 **TIME: 8:30 – 10:30 AM**

INSTRUCTIONS

Answer question one and any other two questions. Question one carries 30 marks and the other questions carry 20 marks each.

QUESTION ONE(Compulsory)

a) Distinguish between the following set of terms:- (15 marks)

i) Discretionary stabilization and Automatic stabilization.

ii) Aggregate demand analysis and Aggregate supply analysis.

iii) Monetary and fiscal policy

iv) Flexible exchange rate and fixed exchange rate.

v) Deficit and surplus BOP

(b) Demonstrate using the classical model how a decrease in the money supply, a decrease in income velocity and a rise in the transactions demand for money would affect prices, money wages and real variables. (9 marks)

c) Explain the effects of fiscal policy in the three ranges of LM curve. (6 marks)

QUESTION TWO

a) With the aid of well labelled diagrams, describe how a country using a fixed exchange rate system eliminates a deficit in the balance of payment. (8 marks)

b) Briefly explain how monetary policy affects inflation and output when the economy is at; (8 marks)

1) Full employment
2) Not at full employment

c) Explain the difference between the devaluation of a currency and the depreciation of a currency. (4 marks)

QUESTION THREE

a) With the aid of well labelled diagrams distinguish between relative income hypothesis and lifecycle income hypothesis (8 marks)

b) Discuss the fourth pillar of wages and price stability showing clearly how demand for labour and supply for labour curves are derived (6 marks)

c) Explain the monetary policy tools and show how they can be used to combat inflation. (6 marks)

QUESTION FOUR.

a) Clearly distinguish between commodity and money markets. (4 marks)

b) Explain the J - curve phenomena (6 marks)

c) Enumerate the key contributions of the Keynesians economics and the main recommendations advanced by the classics and monetarists in the management of economic of a nation. (10 marks)

QUESTION FIVE

a) According to Keynes, households have three motives for holding money balances. Clearly explain these motives and clearly show the liquidity trap (10 marks)

b) If the money wage is fixed and individuals cannot accept wage cut, use a diagram to explain classical remedy to unemployment arising in this case (10 marks)