MACHAKOS UNIVERSITY

University Examinations for 2017/2018

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF ECONOMICS

FOURTH YEAR SECOND SEMESTER EXAMINATION FOR

BACHELOR OF ECONOMICS AND FINANCE

BACHELOR OF ECONOMICS

EET 401: MACROECONOMIC THEORY IV

DATE: 18/12/2017 **TIME: 8:30 – 10:30 AM**

INSTRUCTIONS TO CANDIDATES

Answer Question ONE and any other TWO questions

QUESTION ONE (COMPULSORY 30MARKS

(a) (i) State Keynes's three conjectures. (3 marks)

(ii) Suppose you are given interest rate, r, consumer discount rate, δ, while utility function is stated as $u = \sum_0^T \frac{lnc}{(1+\delta)^t}$ and the multi-periods intertemporal budget constraint is written as $\sum_0^T \frac{C_t}{(1+r)^t} = \sum_0^T \frac{y_t}{(1+r)^t}$ .Where C_t and $y_t$are real consumption and income respectively at time t. Derive the intertemporal optimizing model of consumption and represent consumption path in a diagram. (12 marks)

(b) Briefly explain the following concepts

i) Permanent income hypothesis (3 marks)
ii) Hall's random-Walk Hypothesis (3 marks)
iii) Tobin's Q (3marrks)
iv) The Present Value Creterion for Investment (3 marks)
v) The Life-Cycle Hypothesis (3 marks)

QUESTION TWO (20 MARKS)

(a) Discuss Liquidity Preference Theory (8 marks)

(b) Distinguish between the Friedman and Keynesian Theories for money demand framework. (8 marks)

(c) Explain quantity theory of money and starting with Irving Fisher's equation of exchange derive the velocity of money equation. (6 marks)

QUESTION THREE (20 MARKS)

(a) Distinguish between fiscal and monetary policy. (4marks)

(b) Explain four policy instruments for monetary policy. (12 marks)

(c) Explain how Kenyan government can invoke fiscal policy to create more employment opportunities. (4 marks)

QUESTION FOUR (20 MARKS)

Discuss the relevance of Endogenous Growth Theory within the context of Kenya and explain how endogenous growth theory can be used to spur economic growth in Kenya

(20 marks)

QUESTION FIVE (20 MARKS)

Citing relevant examples discuss the causes of wage rigidity in Kenya. (20 marks)