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KIRIRI WOMENS' UNIVERSITY OF SCIENCE AND TECHNOLOGY
UNIVERSITY EXAMINATION, 2023/2024 ACADEMIC YEAR
SECOND YEAR, SECOND SEMESTER EXAMINATION
FOR THE DEGREE OF BACHELOR OF SCIENCE
(BUSINESS ADMINISTRATION)

Date: 17th August, 2023
Time: 11.30am –1.30pm

KFI 202 - INTERMEDIATE MACRO – ECONOMIC THEORY

INSTRUCTIONS TO CANDIDATES

ANSWER **QUESTION ONE (COMPULSORY)** AND **ANY OTHER TWO** QUESTIONS

QUESTION ONE (30 MARKS)

a) University management has invited you to clarify some economic terms to the board. Distinguish between the following terms to the enable the management understand how they affect economic activities in a country
   i) Depreciation and devaluation   (2 Marks)
   ii) Discretionary and automatic policies   (2 Marks)
   iii) Keynesian and monetarists' view of managing the economy   (2 Marks)
   iv) Private domestic investment and public domestic investment   (2 Marks)
   v) Good market and money market   (2 Marks)

b) The government has aggressively embraced increased taxation to fund its' expenditure. Using the Aggregate demand – Aggregate supply (AD-AS) analysis, illustrate and explain the effect of an increase in taxation on output and employment in the economy.   (8 Marks)

c) Discuss two policies you would propose to the government of Kenya to address the problem in part (b) above   (4 Marks)

d) Assume the LM-curve is perfectly elastic, elastic and perfectly inelastic. Demonstrate the effect of an expansionary fiscal policy on the sections of LM curve   (8 Marks)

QUESTION TWO (20 MARKS)

a) The unemployment problem could be solved by workers taking cuts in their money wages. But suppose workers would not take reduction in their money wages, what other policy would be applied to solve the unemployment problem?   (6 Marks)

b)   Basing your arguments on Classical Economists, explain this phenomenon with the help of relevant diagrams   (6 Marks)
c)   Discuss any four merits to a country that engages in multiple exchange regimes.
                                                                                                                    (8 Marks)

QUESTION THREE (20 MARKS)

a)   Kenya is currently faced with Balance of Payment (BOP) problems due to ballooning exchange rate plunging the country into a deficit. Assume Kenya operates a fixed exchange rate regime, illustrate and discuss how the government can solve the problem giving examples where necessary
                                                                                                                    (10 Marks)
b)   Assume the following equations for a developing closed economy in Sub-Saharan Africa. Use the equations to respond to the equations below;

$C = 100 + 0.8Y^d$ (Consumption function)
$I = 10 - 10r$ (Investment function)
$G = 10$ (Government Purchases)
$T = 0.25Y$ (Tax rate)
$L = Y - 100r$ (Real Money Demand)
$M = 295$ (Real Money Supply)

Required;
i)   Derive the equations for the IS and LM curves for the economy   (5 Marks)

ii)   Determine the values of r and y at which the two markets are clearing   (2 Marks)

iii) Compute the values of C and L   (3 Marks)

QUESTION FOUR (20 MARKS)

a)   Households have various motives for holding cash balances at any given time. Discuss according to Keynesian the motives for holding cash balances by households in an economy.
                                                                                                                    (10 Marks)
b)   Illustrate and discuss how life cycle hypothesis affects household consumption in Kenya today
                                                                                                                    (10 Marks)

QUESTION FIVE(20 MARKS)

a)   Suppose that everyone in the economy at every interest rate decided to save more, would this lead to unemployment? In other words, would the total output change? Explain this statement with the help of a well labelled diagram.
                                                                                                                    (8 Marks)
b)   Using an example explain why macroeconomic policy measures implemented by Kenyan government commonly appear contradictory
                                                                                                                    (6 Marks)

c)   Households demand money for various motives in the economy. Discuss these motives according to Keynesian school of thought   (6 Marks)