



S3EBHQ3

MACRO-ECONOMICS

FINAL EXAM 2019

EXAMINER:
INTERNAL MODERATOR
DURATION:

DR M BIYASE MARKS: 100
PROF R BAUR
3HRS

INSTRUCTIONS TO CANDIDATES:

1. Answer ALL questions.
2. In your own interest, please write legibly.

Surname:	Initials:	Student number:	cell no
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Question	Marks	Total
1	30	
2	20	
3	20	
4	30	
TOTAL		<div style="display: flex; justify-content: space-between; align-items: center;"> /100 %= </div>

QUESTION 1

[30]

Consider a closed economy which can be characterized by the following equations:

$$C = 200 + 0.25(Y - T)$$

$$I = 140 + 0.25Y - 3000i$$

$$G = 300$$

$$T = 120$$

$$M_d = 2Y - 30000i$$

$$M_s = 1600$$

(a) Derive an equation for the IS-curve. (4)

(b) Derive an equation for the LM-curve. (2)

(c) Determine the equilibrium income and interest rate in the two markets (5)

(d) Calculate the equilibrium level of consumption (2)

(e) Calculate the equilibrium level of capital formation. (2)

(f) Assume that the Reserve Bank increases the money supply by R1000. What happens to the equilibrium level of interest rate and income? (6)

(g) Using the appropriate graph, check if the above answer make economic sense. (6)

Draw a graph/s in the space below

(h) Consider the following model:

$$Y = C + G + I$$

$$C = \bar{C} + cY_d$$

$$T = 50, G = 150, I = 100$$

$$\text{with } \bar{C} = 10 \text{ and } c = 0.25.$$

Compute equilibrium income (3)

QUESTION 2

[20]

The International Monetary Fund reported on Monday that Venezuela's crippling inflation could top 1 million percent by the end of the year, as its economy continues to worsen. The South American nation finds itself in a political and economic crisis that has led to more than a million fleeing the country since 2015.

a) If you were advising the president of Venezuela, what kind of policy action would you recommend? Explain briefly the reasons for your choice. (5)

- b) Make use of the IS-LM-BP model to illustrate and explain carefully the macroeconomic impact of the policy which you recommended above.

Draw a graph/s in the space below

(6)

The primary effect is:

(2)

The secondary effect is:

(2)

Net Effect

(1)

The initial BoP effect is: (2)

The concluding BoP effect is: (2)

QUESTION 3 [20]

According to the IMF, Venezuela's real GDP is projected to fall by about 18 percent this year. The decline is being driven by a significant drop in oil production, widespread micro-level distortions and large macroeconomic imbalances.

- 3.1) If you were advising the president of Venezuela, what kind of policy action would you recommend? Explain briefly the reasons for your choice. (5)

- 3.2) Make use of the IS-LM-BP model to illustrate and explain carefully the macroeconomic impact of the policy which you recommended above.

Draw a graph/s in the space below (6)

The primary effect is: (2)

The secondary effect is: (2)

Net Effect (1)

The initial BoP effect is: (2)

The concluding BoP effect is: (2)

QUESTION 4 [30]

Suppose that the economy starts at the natural level of output. Now suppose there is a decline in business confidence, so that investment demand falls for a given interest rate. a) In an AD-AS diagram, show what happens to output and the price level in the short run and the medium run.

Graph here

b) What happens to the unemployment rate in the short run? In the medium run?

Suppose that the Federal Reserve decides to respond immediately to the decline in business confidence in the short run. In particular, suppose that the Fed wants to prevent the unemployment rate from changing in the short run after the decline in business confidence. c.

c) What should the Fed do? Show how the Fed's action, combined with decline in business confidence, affects the AD-AS diagram in the short and medium run

d) How do short-run output and the short-run price level compare to your answers from part (a)?

END
