

Tutorial letter 101/3/2016

Macroeconomics 2

ECS2602


Semesters 1 and 2

Department of Economics

IMPORTANT INFORMATION:

This tutorial letter contains important information
about your module.

BAR CODE



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1 INTRODUCTION AND WELCOME

Dear Student

We are pleased to welcome you to this Macroeconomics module and hope that you will find it both interesting and rewarding. We shall do our best to make your study of this module successful. You will be well on your way to success if you start studying early in the semester and resolve to do the assignments properly.

You will receive a number of tutorial letters during the semester. A tutorial letter is our way of communicating with you about teaching, learning and assessment.

1.1 Tutorial material

The Department of Despatch should supply you with the following study material for this module soon after registration:

- Tutorial Letters 101 and 102
- A study guide (MO001)
- A CDROM entitled *Macroeconomics*. You will also find the information on the CDROM on the website www.econom.co.za

Some of this study material may not have been available when you registered. Study material that was not available when you registered will be posted to you as soon as possible, but is also available on *myUnisa*. Please contact the Despatch Department at despatch@unisa.ac.za if you did not receive your study material, CDROM or a faulty CDROM.

Note that the 200 series tutorial letters (Tutorial Letters 201, 202, 203 and 204) contain the discussions of the assignments and will therefore only be available after the closing date of the specific assignment.

This Tutorial Letter 101 contains important information about the study programme, resources and assignments for this module. We urge you to read it carefully and to keep it at hand when working through the study material, preparing the assignment(s) and for the examination.

You will also find the assignments, assessment criteria as well as instructions on the preparation and submission of the assignments. This tutorial letter also provides all the information you need with regard to the prescribed study material and other resources and how to access it. Please study this information carefully and make sure that you obtain the prescribed material as soon as possible.

We have also included certain general and administrative information about this module. Please study this section of the tutorial letter carefully.

Right from the start we would like to point out that you must read all the tutorial letters you receive during the semester immediately and carefully, as they always contain important and, sometimes, urgent information.

1.2 Module format

1.2.1 Fully online module

Please note that this module is offered fully online.

All study material for this module will be available on *myUnisa*. It is thus very important that you register on *myUnisa* at <https://my.unisa.ac.za> and access the module site on a regular basis. You must be registered on *myUnisa* to be able to access your learning material, submit your assignments, gain access to various learning resources and library functions, “chat” to your lecturer or e tutor and fellow students about your studies and the challenges that you might encounter, and to participate in online discussion forums. Note that *myUnisa* contains the **Learning Units** tool from which you will only be able to access the study guide for this module if you have registered and have access to *myUnisa*.

On the main site = ECS2602-16-S1 (or S2) you can access: – Official study material, – Learning units, – Announcements by module lectures, – Upload your assignments on this site.

1.2.2 Printed materials to support the online module

Because we want you to be successful in this online module, we also provide you with the study materials in printed format. This will allow you to read the study materials, even if you are not online. In addition, to Tutorial Letter 101 you will receive a printed copy of the online study guide available on *myUnisa* (MO001). While the printed material may appear slightly different (the formats differ) from the online study materials, the contents are exactly the same.

Remember, the printed support materials are a back-up to everything that is found online, on *myUnisa*. There is no extra information there. **In other words, you should NOT wait for the printed support materials to arrive before you start studying.**

Please consult the *my Studies @Unisa* publication for more information on the activation of your *myLife* email address as well as obtaining access to the *myUnisa* module site.

2 PURPOSE OF AND OUTCOMES FOR THE MODULE

2.1 Purpose

Macroeconomics will be useful to students who intend to follow a career (academic or otherwise) in economic analysis or wish to understand the functioning of the macroeconomic system.

2.2 Outcomes

The main outcomes of this module are the following:

- To describe the determination of the level of output and income in closed and open macroeconomic models
- To assess the impact of stabilisation policy measures such as fiscal and monetary policy on the economy in terms of the above models

More detailed module outcomes can be found at the beginning of each learning unit in the study guide (MO001).

3 LECTURERS AND CONTACT DETAILS

3.1 Lecturers

You will find the lecturers responsible for this module's contact details on *myUnisa* under the "Learning units" tab. You can also contact us by e-mail via *myUnisa*.

All queries that are not of a purely administrative nature **but are about the content of this module** should be directed to your e-tutor first and if you are not satisfied with their response, then you contact your lecturer.

3.2 Department

The Department of Economics has moved to Hazelwood. The physical address is Club 1 Building, Corner of Dely Road and Pinaster Avenue, Hazelwood, Pretoria.

You can also contact the department's coordinator, Mr Themba Mzangwa at 012 433-4661.

3.3 University

If you need to contact the university about matters not related to the content of this module, please consult the publication: *my Studies @ Unisa* which you received with your study material or visit the Unisa website at <http://www.unisa.ac.za>. The brochure and the website contain information on how to contact the university (e.g. to whom you can write for different queries, important telephone and fax numbers, addresses and details of the times certain facilities are open).

Always have your student number at hand when you contact the university.

4 MODULE RELATED RESOURCES

4.1 Prescribed book

Your prescribed textbook for this module for this year is:

Blanchard & Johnson. 2014. *Macroeconomics: Global and Southern African Perspectives*. First edition. Pearson.

Please refer to the list of official booksellers and their addresses in the *my Studies @ Unisa* brochure.

Prescribed books can be obtained from the University's official booksellers. If you have difficulty locating your book at these booksellers, please contact the Prescribed Book Section at telephone 012 429-4152 or e-mail yospresc@unisa.ac.za

4.2 Recommended books

There are no recommended books for this module.

4.3 Electronic Reserves (e-Reserves)

There are no e-Reserves for this module.

5 STUDENT SUPPORT SERVICES FOR THE MODULE

For information on the various student support systems and services available at Unisa (e.g. student counselling, tutorial support programme and classes, language support), please consult the publication *my Studies @ Unisa* that you received with your study material.

5.1 Contact with fellow students: Study groups

It is advisable to have contact with fellow students. One way to do this is to form study groups. You can get the names of other students in your area for the same modules by contacting the Department of Student Admission and Registration. For further information, please consult the *my Studies @ Unisa* brochure.

5.2 myUnisa

If you have access to a computer that is linked to the internet, you can quickly access resources and information at the university. The *myUnisa* learning management system is Unisa's online campus that will help you to communicate with your lecturers, e-tutor, with other students and with the administrative departments of Unisa – all through the computer and the internet.

To go to the *myUnisa* website, start at the main Unisa website, <http://www.unisa.ac.za>, and then click on the “*myUnisa*” link on the top right-hand side of the screen. This should take you to the *myUnisa* website. You can also go there directly by typing in <https://my.unisa.ac.za>.

Please consult the *my Studies @ Unisa* brochure for more information.

An important resource on the module website on *myUnisa* is the discussion forum (see point 5.4.1 below). Please make use of it.

Additional study material is available at www.econom.co.za. Please note that information on the CDROM is also available under the mentioned website.

5.3 Discussion classes

There are no discussion classes for this module.

5.4 Tutorial support programme

5.4.1 E-tutors

We aware that studying via distance education poses significant challenges to you and you might often feel alone and lost in the sea of content that you are faced with. You might often feel isolated from us and from other students and not knowing where to start when trying to get help from the institution.

The good news is that we have put together a team of subject specialist e-tutors to help you with the content and to empower you as a student to be successful in your studies. They will be your compass and help steer you in the right direction.

Once you have been registered for this module, you will be allocated to a group of students with whom you will be interacting during the tuition period as well as an e-tutor who will be your tutorial facilitator.

Thereafter you will receive a sms informing you about your group, the name of your e-tutor and instructions on how to log onto myUnisa in order to receive further information on the e-tutoring process. All you need to be able to participate in e-tutoring is a computer with an internet connection. If you live close to a Unisa regional Centre or a Telecentre contracted with Unisa, please feel free to visit any of these to access the internet.

Please join and contribute to you e-tutor group as your input is needed to make a success of it.

5.4.1.1 How to find your e-tutor

You will be connected to two sites for ECS2602. The first site is the main site “ECS2602-16-S1” on this site you can access official study material, learning units, announcements by the module lectures as well as upload your assignments. Once you have been linked to an e-tutor you will see a second ECS2602 site, this is your e-tutors site, which will be named “ECS2602-16-S1-#E” (# Can represent any number from 1 to 10 for this module.) On this site you can connect with fellow students and ask your e-tutor questions on the "Discussion Forum"



If you are not sure how to find your e-tutors' site, please see the below graphics which were distributed to students by Unisa to generate awareness about the e-tutor programme.

Click to your e-tutor

Start here

<http://my.unisa.ac.za>

Login

**Go to
the e-tutor
group site**
(e.g. MNM1502-14-S2-3E)

**Go to the
official site for
your module**
(e.g. MNM1502-14-S2)

Learn without limits.

UNISA



How to find your e-tutor

- Go to the Unisa website and login on *myUnisa*.
- Click the "More Sites" tab.
- Select the official module site, for example, MNM1502-14-3E. This site is used to access official study material and previous question papers for this specific module.
- Find your e-tutor site for the specific module. The e-tutor site will have a code like MNM1502-14-S2-3E.



What does the e-tutor module site code mean?

The e-tutor module site code is made up of 4 different parts; let us use MNM1502-14-S2-3E as an example:

- MNM1502 is the module code
- 14 – the year
- S2 – represents the second semester
- 3E is the 3rd e-tutor for this module

You should select the e-tutor group site with the E at the end. Select, for example, MNM1502-14-S2-3E to communicate with your e-tutor and the students in your group.

5.4.2 Face-to-face tutors

For this module there are face-to-face tutors allocated and tutorials for these modules take place at the Unisa regional centres. A tutorial is an organised session where students and tutor(s) meet regularly at a common venue and at scheduled times to discuss course material. The main purpose of the tutorial services is to facilitate student learning by developing the student's independent learning skills and assisting students to become motivated and independent learners. Tutorials help the students to develop and enhance their learning experience and academic performance through interaction with the tutor and fellow students. Tutorials are not compulsory. These tutorials are also offered free of charge, however, it is important for you to register at your nearest Unisa Regional Centre to secure attendance of these classes.

6 MODULE-SPECIFIC STUDY PLAN

6.1 Assignments and learning

Assignments are seen as part of the learning material for this module. As you do the assignment, study the texts, consult other resources, discuss the work with fellow students or tutors or do research, you are actively engaged in learning.

Looking at the assessment criteria given for this module, the five assignments will help you to understand what is required of you more clearly.

If you have access to the internet, you can view and download the study guide (MO001) and tutorial letters for the modules for which you are registered on the university's online campus, *myUnisa*, (under the official study material folder) at <https://my.unisa.ac.za>.

6.2 General remarks

You will find in your *my Studies @ Unisa* brochure contact details regarding enquiries about assignments (e.g. whether or not the university has received your assignment or the date on which an assignment was returned to you). You might also find information on *myUnisa*. Use your *my Studies @ Unisa* brochure for general time management and planning skills.

6.3 Feedback on assignments

Assignments 01, 03 and 04 consist of multiple-choice questions. They are marked automatically – you will receive the correct answers after they have been processed. Assignment 02 (a written assignment) and assignment 05 (a multiple-choice assignment) are self-assessment assignments. Please work thoroughly through the answers we will provide. Compare it with your answers as well. Feedback on assignments **will be sent to all students registered for this module** in follow-up tutorial letters, and not only to those students who submitted the assignments. The tutorial letter numbers will be 201, 202, 203 and 204. These tutorial letters are also available on the module website on *myUnisa*.

As soon as you have received the feedback, please check your answers. The assignments and the feedback on these assignments constitute an important part of your learning and should help you to be better prepared for the next assignment and the examination.

6.4 Learning strategy and proposed study programme

In this module, the emphasis is very much on the development of your understanding of different theories regarding the determination of output and income. Therefore, you will be exposed to a number of different concepts, such as the different assumptions which underlie the theoretical models, the interaction between the various macroeconomic variables, the different analytical tools, and the economic policy implications of each model.

It is important that you have a thorough understanding of the different building blocks of the various models so as to gain a comprehensive picture of how the economy works. Towards the end of the module, this picture will become clearer and logical.

Approach each learning unit in the study guide as follows:

Step 1: First read the learning unit outcomes which will help you to focus on the important aspects and issues in that unit. Work through each section of the study guide together with the relevant chapter in the textbook.

Remember that the study guide serves to assist you to work through the contents of the text book. Make notes or summaries as you go along.

Step 2: Work through all the activities provided in TL 102. You will see that the activities test your understanding of the content and cover a range of the different types of questions that will be examined. You should also check your answers against the solutions provided. If you are not clear on certain concepts or theories, revise them before proceeding to the next learning unit.

To help you to work on this module regularly and systematically, we provide a proposed study programme below and five assignments (see section 8.4 of this tutorial letter). The proposed study programme is based on the assumption that first-semester students will commence their studies before or during the last week of January and second-semester students before or during the third week of July. In each semester the period from the last day of registration to the start of the examination consists of only 15 weeks. Hence, it is critical that you should start working as soon as possible and continue to work regularly and systematically throughout the semester.

PROPOSED STUDY PROGRAMME: FIRST SEMESTER

STUDY WEEK	Week starting	LEARNING UNIT(s) or study instruction
1	1 February	1 and 2
2	8 February	2 and 3
3	15 February	Complete and submit compulsory Assignment 01 <i>Closing date: 29 February</i>
4	22 February	4
5	29 February	4 Complete Assignment 02 It is a self-assessment assignment Do not submit Assignment 02
6	7 March	5 Complete and submit Assignment 03: <i>Closing date: 22 March</i>
7	14 March	5 and 6
8	21 March	6 and 7
9	28 March	7
10	4 April	Complete and submit Assignment 04: <i>Closing date: 11 April</i>
11	11 April	8
12	18 April	9
13	25 April	Complete Assignment 05 It is a self-assessment assignment Do not submit Assignment 05
14	2 May	Prepare for examination
15	9 May	Prepare for examination

ECS2602 is a semester module with a credit value of 12 that must be completed for a BCom degree in Economics. Each credit is equivalent to 10 notional hours. In total it means that to be successful the average student must spend 120 notional hours on this module. The notional hours includes time that is spent studying the learning units, completing the activities in TL102, doing assignments, preparing for the examination, and writing the examination. That boils down to 30 work days (4 hours per day) that must be devoted to this module for the average student to pass it. This is the way in which each module is designed. In other words, you cannot plan your semester on the basis of completing assignments only.

PROPOSED STUDY PROGRAMME: SECOND SEMESTER

STUDY WEEK	Week starting	LEARNING UNIT(s) or study instruction
1	18 July	1 and 2
2	25 July	2 and 3
3	1 August	Complete and submit compulsory Assignment 01 <i>Closing date: 22 August</i>
4	8 August	4
5	15 August	4 Complete Assignment 02 It is a self-assessment assignment Do not submit Assignment 02
6	22 August	5 Complete and submit Assignment 03: <i>Closing date: 5 September</i>
7	29 August	5 and 6
8	5 September	6 and 7
9	12 September	7
10	19 September	Complete and submit Assignment 04: <i>Closing date: 30 September</i>
11	26 September	8
12	3 October	9
13	10 October	Complete Assignment 05 It is a self-assessment assignment Do not submit Assignment 05
14	17 October	Prepare for examination

ECS2602 is a semester module with a credit value of 12 that must be completed for a BCom degree in Economics. Each credit is equivalent to 10 notional hours. In total it means that to be successful the average student must spend 120 notional hours on this module. The notional hours includes time that is spent studying the learning units, completing the activities in TL102, doing assignments, preparing for the examination, and writing the examination. That boils down to 30 work days (4 hours per day) that must be devoted to this module for the average student to pass it. This is the way in which each module is designed. In other words, you cannot plan your semester on the basis of completing assignments only.

7 PRACTICAL WORK AND WORK INTEGRATED LEARNING

There are no practicals for this module.

8 ASSESSMENT

8.1 Assessment plan

Assessment will be done by the module leader and, where applicable, the module team and/or the examiner(s). The name(s) of examiner(s) will also be indicated on examination question papers.

8.1.1 Assessment of assignments

Assessment criteria used for the assignments will be done as follows: the multiple-choice questions in Assignments 01, 03 and 04 will be marked electronically in accordance with mark-reading 'masters' provided to the Assignment section by the module leader. No marks will be deducted for incorrect answers. Assignment 02 is a written self-assessment assignment and Assignment 05 is a multiple-choice self-assessment assignment.

Note that assignment 01 is compulsory. The first assignment will contribute 20% to the semester mark, the third assignment 40% and the fourth assignment 40%.

Please note: Although students may work together when preparing assignments, each student must submit his or her own individual assignment. Any form of plagiarism may lead to penalisation or you may be subjected to disciplinary proceedings by the university.

8.1.2 Assessment of examination

For general information and requirements as far as examinations are concerned, see the brochure *my Studies @ Unisa* which you received with your study material. Please note that the applications for, and the administration of re-marks of examination scripts are handled solely by the Examination department and not academic departments.

Examination admission

Please note that submission of Assignment 01 is compulsory to gain admission to the examination. Three assignments will contribute towards the semester and final marks.

How will this work in practice?

Semester mark

Your semester mark is based on your assignment marks. The three assignments that you submit during the semester contribute towards your semester mark. Different weights are allocated to the assignments. The first assignment contributes 20%, the third assignment 40% and the fourth assignment 40% to your semester mark.

If an assignment is not submitted or submitted late (for whatever reason), zero marks are awarded for such assignments.

The examination mark

The percentage achieved in the examination is used in the calculation of your final mark.

Final mark

The weight of the assignments will be 20% while the examination's weight is 80%.

Your final mark is calculated as follows:

Semester mark (out of 100) x 20% + Examination mark (out of 100) x 80%

For example:

Suppose your semester mark is 46% and you get 60% in the examination. Your final mark will be:

$$\begin{aligned} & (46 \times 20\%) + (60 \times 80\%) \\ &= (46 \times 0.2) + (60 \times 0.8) \\ &= 9.2 + 48 \\ &= 57.2\% \end{aligned}$$

The sub-minimum rule: if you do not achieve a minimum mark of 40% in the summative assessment (the examination), your year mark will not be taken into account for the purpose of calculating the final examination mark.

8.2 General assignment numbers

Assignments are numbered consecutively per module, starting from 01. In this module there are five assignments per semester, namely 01, 02, 03, 04 and 05.

8.2.1 Unique assignment numbers

In addition to the general assignment number (e.g. 01 or 02), each assignment (multiple-choice questions and written assignments) must have its own unique assignment number (e.g. 102717). In this module assignments 01, 03 and 04 consist of only multiple-choice questions and therefore must be completed on a marking-reading sheet with its own unique assignment number. Assignment 02 and 05 are self-assessment assignments that must not be submitted and therefore have no unique assignment numbers.

8.2.2 Due dates of assignments

Please note that the due dates for the submission of assignments to Unisa are indicated in the proposed study programme as well.

SEMESTER 1: ASSIGNMENT SUBMISSION DATES

Assignment number	Unique number	Closing date	Contents of assignments	Type of assignment	Weight
01	806573	2016/02/29	Learning units 1 to 3	Multiple-choice	20
02	No unique number	Self-assessment Please do not submit	Learning units 1 to 4	Written	0
03	863782	2016/03/22	Learning units 1 to 4	Multiple-choice	40
04	884585	2016/04/11	Learning units 5 to 7	Multiple-choice	40
05	No unique number	Self-assessment Please do not submit	Learning units 8 to 9	Multiple-choice	0

SEMESTER 2: ASSIGNMENT SUBMISSION DATES

Assignment number	Unique number	Closing date	Contents of assignments	Type of assignment	Weight
01	850512	2016/08/22	Learning units 1 to 3	Multiple-choice	20
02	No unique number	Self-assessment Please do not submit	Learning units 1 to 4	Written	0
03	707201	2016/09/05	Learning units 1 to 4	Multiple-choice	40
04	705374	2016/09/30	Learning units 5 to 7	Multiple-choice	40
05	No unique number	Self-assessment Please do not submit	Learning units 8 to 9	Multiple-choice	0

8.3 Submission of assignments

You may submit assignments completed on mark-reading sheets either by post or electronically via *myUnisa*. **Assignments may not be submitted by fax or e-mail.**

For detailed information on assignments, please refer to the *my Studies @ Unisa* brochure.

To submit an assignment via *myUnisa*:

- Go to *myUnisa*.
- Log in with your student number and password.
- Select the module.
- Click on "Assignments" in the menu on the left-hand side of the screen.
- Click on the assignment number you wish to submit.
- Follow the instructions.

If you experience any problems submitting your assignment electronically via *myUnisa*, please send an e-mail to myUnisaHelp@unisa.ac.za – with your student number in the subject line.

8.4 Assignments

FIRST SEMESTER ASSIGNMENTS

<p>SEMESTER 1</p> <p>COMPULSORY ASSIGNMENT 01</p> <p>LEARNING UNITS 1 TO 3</p> <p>DUE DATE: 2016/02/29</p> <p>UNIQUE NUMBER: 806573</p>
--

This assignment contributes 20% towards your semester mark.

Please ensure that this assignment reaches the university before the due date.

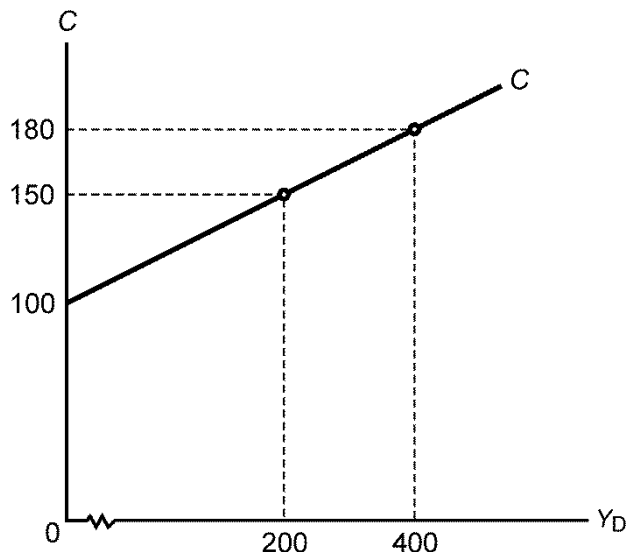
Answer all questions on a mark-reading sheet.

1. The main focus of this macroeconomics module is the study of
 1. the determinants of the short, medium and long-term growth potential of the economy.
 2. only the interaction between the goods market and the financial market.
 3. different theories on the determination of the level of output and income in a closed economy in the short term only.
 4. only the determination of the level of output and income and the impact of fiscal and monetary policy on the financial, labour and foreign exchange markets.
 5. the determination of the level of output and income and the impact of fiscal and monetary policy on the level of output and income.

2. Gross domestic expenditure, which is the total value of spending on final goods and services within the borders of a country ...
 1. includes imports but excludes exports.
 2. excludes imports but includes exports.
 3. includes both imports and exports.
 4. excludes both imports and exports.

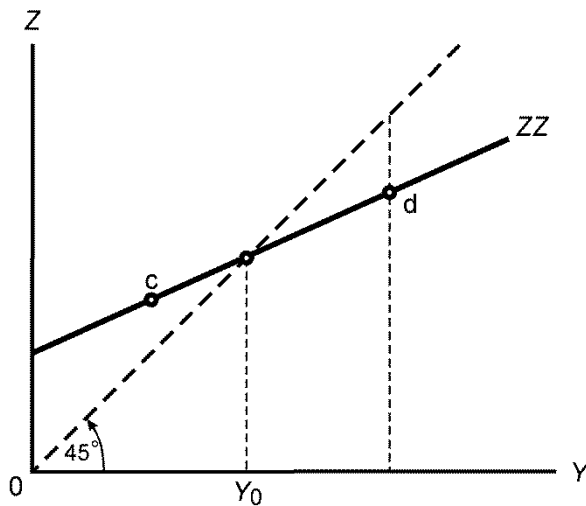
3. Which one of the following statements is **incorrect**?
 1. The four major spenders in the economy are households, government, private firms and the foreign sector.
 2. Final consumption expenditure by households (C) is classified in terms of durable, semi-durable, and nondurable goods and services.
 3. Transfer payments and interest on debt are included in final consumption expenditure by government (G) since they are part of the purchase of final goods and services.
 4. Gross capital formation is the spending by households, private firms and government on residential and non-residential capital goods.

Question 4 is based on the following diagram:



4. Which of the following statements are correct?
- Induced consumption is equal to R100 if disposable income is R200.
 - The marginal propensity to consume is equal to 0.15. It means that if the income of households increases by R100 million, the increase in consumer spending will be R15 million.
 - An increase in autonomous consumption will influence the slope of the consumption curve.
 - If the marginal propensity to save by households increases, the marginal propensity to consume will be lower. In other words, the slope of the C curve will be flatter.
- a, b and c
 - a, b and d
 - Only b and d
 - Only a and d
 - Only b and c
5. Given that $c_0 = R800$, $\bar{I} = R600$, $G = R1\,340$, $c = 0.8$ and $T = R400$ the equilibrium level of output and income is ...
- R12 500
 - R12 100
 - R8 900
 - R2 420
 - R2 740

Question 6 is based on the following diagram below:



6. Given a demand for goods curve ZZ ...
- at point d the demand for goods exceeds the level of output; therefore excess supply occurs and producers will cut back on production to move back to Y_0 .
 - at point d the level of output exceeds the demand for goods; therefore excess supply occurs and producers will cut back on production to move back to Y_0 .
 - at point c the demand for goods exceeds the level of output; therefore excess demand occurs and producers will increase production to move back to Y_0 .
 - at point c the level of output exceeds the demand for goods; therefore excess demand occurs and producers will increase production to move back to Y_0 .
- a and c
 - a and d
 - b and c
 - b and d
7. If the multiplier is 3 and income increased by R72 million, the increase in autonomous spending must have been ...
- R72 million.
 - R24 million.
 - R0.04 million.
 - R216 million.
8. Given that $c_0 = R50$, $\bar{I} = R330$, $G = R300$, $c = \frac{3}{4}$, $T = R100$ and $Y_f = R3\ 000$ the equilibrium level of output and income is _____ and in order to reach the full-employment level of income, government spending must increase by _____ .
- R2 720 million; R280 million
 - R2 420 million; R580 million
 - R2 420 million; R145 million
 - R2 720 million; R70 million

9. Given that an economy is at equilibrium at an income level less than full employment, an increase in the marginal propensity to consume will cause a(n)
1. upward shift of the demand for goods curve.
 2. downward shift of the demand for goods curve.
 3. flatter slope of the demand for goods curve.
 4. steeper slope of the demand for goods curve.
 5. higher vertical intercept of the demand for goods curve.
10. Given a marginal propensity to consume of 0.6 an increase of 200 in government spending and an increase of 240 in taxes will cause the level of output and income to ...
1. decrease by 140.
 2. increase by 140.
 3. decrease by 160.
 4. increase by 240.
 5. increase by 160.
11. Expansionary fiscal policy means that government spending has to be ...
1. increased and/or taxes have to be decreased in order to increase aggregate demand in the economy.
 2. decreased and/or taxes have to be increased in order to increase aggregate demand in the economy.
 3. decreased and/or taxes have to be increased in order to stimulate economic activity by increasing the aggregate demand in the economy.
 4. increased and/or taxes have to be decreased in order to "cool down" economic activity by decreasing aggregate demand in the economy.

Given the following information, answer questions 12 and 13.

Autonomous consumption spending	= R100 million
Investment spending	= R300 million
Government spending	= R200 million
Taxes	= R60 million
Marginal propensity to consume	= $\frac{3}{4}$

12. Which of the following statements are correct?
- a. Autonomous spending = R660 million.
 - b. The multiplier = 4.
 - c. Consumer spending will decrease by R7.5 million if the government increases taxes from R60 to R80 million.
 - d. The marginal propensity to consume of $\frac{3}{4}$ means that if $\Delta Y_D = 100$, $\Delta C = 75$.

1. Only a, b and c
2. Only b, c and d
3. Only a and b
4. Only b and d
5. a, b, c and d

13. The equilibrium level of income and output is ...

1. R138.75 million.
2. R2 640 million.
3. R2 220 million.
4. R416.25 million.
5. R2 580 million.

14. If total production is R500 million and aggregate demand is R550 million ...

1. excess demand occurs and producers will cut back on production until equilibrium is attained.
2. excess supply occurs and producers will cut back on production until equilibrium is attained.
3. excess demand occurs and producers will increase production until equilibrium is attained.
4. excess supply occurs and producers will increase production until equilibrium is attained.

15. If the current level of income (Y_0) is less than the full-employment level of income (Y_F) in a goods market model of a closed economy ...

- a. an increase in investment will move the economy closer to full employment.
- b. an increase in the marginal propensity to consume will move the economy closer to full employment.
- c. an increase in government spending will move the economy closer to full employment.
- d. an increase in taxes will move the economy closer to full employment.
- e. an increase in any of the components of autonomous spending will move the economy closer to full employment.

1. Only a, b, c and e
2. Only b, c and d
3. Only a, c and d
4. Only b, d and e
5. a, b, c, d and e

16. Given a marginal propensity to consume of 0.8, an increase of 100 in government spending and an increase of 80 in taxes will cause the level of output and income to ...

1. increase by 180.
2. be unchanged.
3. increase by 100.
4. increase by 80.
5. decrease by 80.

The questions 17 and 18 are based on the following data for the country Bravos for 2015.

Marginal propensity to consume	= 0.95
Autonomous consumption spending	= R80 million
Government spending	= R29 million
Taxes	= R20 million

17. Which of the following statements is/are correct?

- a. The value of the multiplier is equal to 20.
- b. There is a budget surplus.
- c. The equilibrium level of output and income is R2 000 million.
- d. Total consumption spending is R1 961 million.

- 1. a, b and c
- 2. a, b and d
- 3. b, c and d
- 4. a, c and d
- 5. None of the options 1 to 4

18. Which of the following statements is/are correct?

- a. An increase in government spending of R10 million and a decrease in taxation of R10 million will increase output and income with R10 million and will result in a budget deficit of R9 million.
- b. An increase in government spending of R20 million and a decrease in taxation of R20 million will increase output and income with R20 million and will result in a budget deficit of R9 million.
- c. An increase in government spending of R10 million and a decrease in taxation of R10 million will increase output and income with R390 million and will result in a budget deficit of R29 million.
- d. It is correct to conclude from the above three statements that a balanced budget has an expansionary effect on the output and income level. It can also be concluded that the multiplier's limited effect is due to the low marginal propensity to consume.

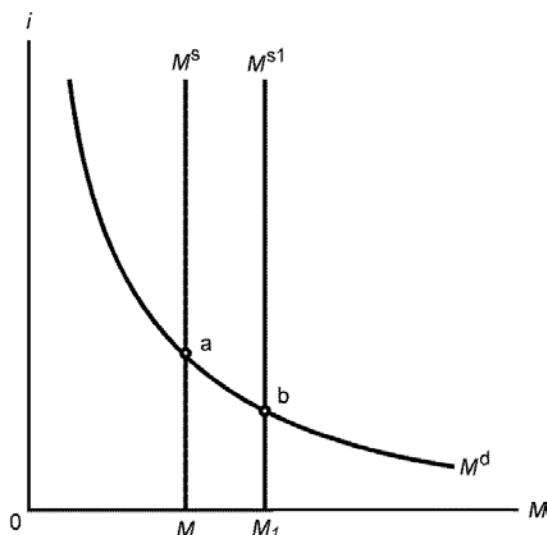
- 1. Only a and b
- 2. a, b and d
- 3. Only c and d
- 4. a, c and d
- 5. None of the options 1 to 4

19. The difference between induced consumption and autonomous consumption is that ...
1. induced consumption is influenced by the level of disposable income while autonomous consumption changes with a change in income.
 2. induced consumption is influenced by the level of disposable income while autonomous consumption is not influenced by the level of income.
 3. induced consumption reflects the influence of non-income determinants of consumer spending while autonomous consumption can be regarded as consumption that is financed from sources other than income.
 4. induced consumption is not influenced by the level of disposable income while autonomous consumption is influenced by the level of income.
20. Which of the following statements is/are correct?
- An autonomous (or exogenous) variable in our model means that the variable ...
- a. is not determined by the level of output and income in the economy.
 - b. is determined by exogenous factors such as business confidence, regulations and political influences.
 - c. is determined by the level of output and income in the economy.
 - d. increases or decreases if income in the economy increases or decreases.
1. Only a
 2. Only b
 3. Only c
 4. Only d
 5. a and b
21. If government spending and taxes increase by the same amount (R100 million), the effect on the ZZ curve will be:
1. The ZZ curve will not shift.
 2. The ZZ curve will shift upwards.
 3. The ZZ curve will swivel downwards.
 4. The ZZ curve will shift downwards.
 5. The ZZ curve will swivel upwards.
22. To calculate an individual's financial wealth, the following different kinds of assets will form part of it:
1. salary, bonds, interest received from bonds and the value of his/her house.
 2. salary, balance on cheque account, bonds and dividends received from shares.
 3. bonds, gold coins, dividends received from shares and the outstanding balance on his/her home loan.
 4. balance on cheque account, cash, bonds, shares, salary, the value of his/her house and paintings.
 5. cash, bonds, shares, the value of his/her paintings and gold coins.

23. If income increases, the demand for money ...

1. will not change.
2. decreases and the money demand curve will shift to the left.
3. increases and the money demand curve will shift to the right.
4. increases and there will be an upward movement along the money demand curve.
5. increases and there will be downward movement along the money demand curve.

Question 24 is based on the diagram below:



24. Which of the following statements is/are correct?

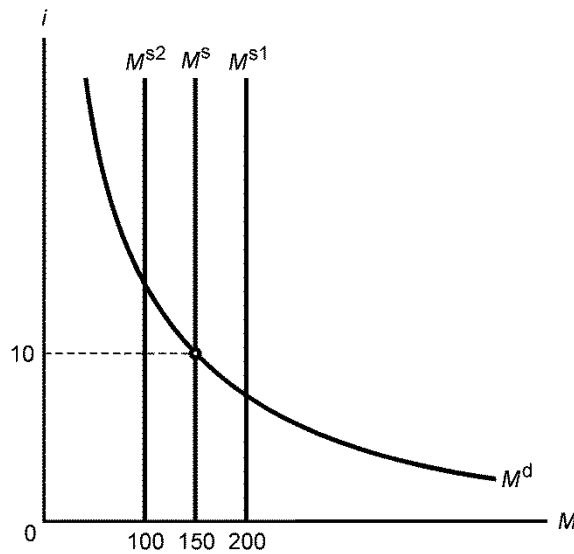
- a. The money supply is a demand-determined money supply that implies that the supply of money depends on the demand for money and the interest rate.
- b. At point a the quantity of money demanded is equal to the quantity of money supplied and it represents an equilibrium position in the financial market.
- c. If money supply increases, a movement from point a to point b implies that the central bank sells treasury bills on the open market in order to decrease the interest rate.
- d. In terms of a chain of events the diagram presented the following:
 $M^s \uparrow: D_B \downarrow \rightarrow P_B \uparrow \rightarrow i \downarrow$

1. Only b and d
2. b, c and d
3. a, b and d
4. a, c and d
5. None of the above options

25. Assuming that the face value of a treasury bill is R150 000, the price paid for the bill is R138 000 and the date to maturity is one year, the rate of return is ...

1. 7.14% and it will decrease if the price paid for it decreases to R135 000.
2. 7.14% and it will increase if the price paid for it decreases to R135 000.
3. 8.70% and it will decrease if the price paid for it increases to R145 000.
4. 8.70% and it will increase if the price paid for it increases to R145 000.

Questions 26 and 27 are based on the diagram below which represents changes in the supply of money:



26. Which of the following statements are correct?

At the initial interest rate of 10% a(n) ...

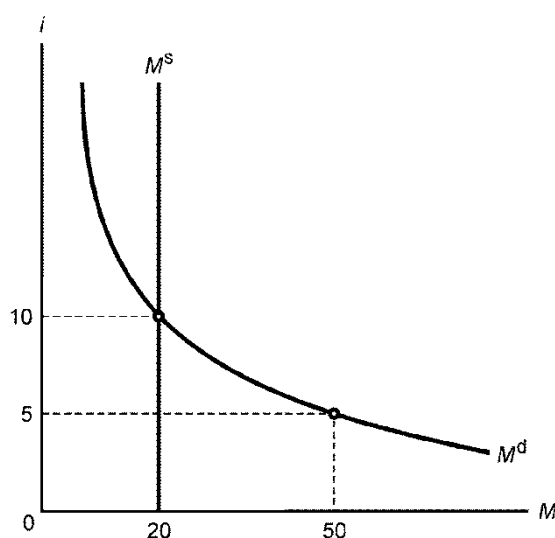
- increase in the supply of money from M^S to M^{S1} results in a surplus of money of R50.
 - increase in the supply of money from M^S to M^{S1} results in a shortage of money of R50.
 - decrease in the supply of money from M^S to M^{S2} results in a surplus of money of R50.
 - decrease in the supply of money from M^S to M^{S2} results in a shortage of money of R50.
- a and d
 - b and d
 - a and c
 - b and c

27. A shift from M^S to M^{S2} represents the impact of a(n) ...

- expansionary monetary policy where the central bank buys treasury bills on the open market and consequently the interest rate increases.
- expansionary monetary policy where the central bank sells treasury bills on the open market and consequently the interest rate increases.
- contractionary monetary policy where the central bank sells treasury bills on the open market and consequently the interest rate increases.
- contractionary monetary policy where the central bank buys treasury bills on the open market and consequently the interest rate increases.

28. A decrease in income with simultaneous contractionary open market operations by the central bank shifts the ...
1. demand for money curve to the left and the money supply curve to the left. The equilibrium interest rate is indeterminate.
 2. demand for money curve to the right and the money supply curve to the left. The equilibrium interest rate is higher.
 3. demand for money curve to the left and the money supply curve to the right. The equilibrium interest rate is indeterminate.
 4. demand for money curve to the right and the money supply curve to the left. The equilibrium interest rate is lower.
29. Money, which can be used for transactions, includes ...
1. income, interest received from bonds, shares and money.
 2. income, bonds, shares, checkable deposits, coins and notes.
 3. money, checkable deposits, income and the interest rate.
 4. financial investment, shares, coins and notes and checkable deposits.
 5. coins and notes and checkable deposits.
30. Exogenously determined money supply implies that ...
1. as the interest rate increases the money supply will also increase.
 2. the supply of money is determined by the demand for money and the interest rate.
 3. money supply is determined by the central bank.
 4. money demand is determined by the central bank.
 5. the money supply curve is perfectly elastic.

Question 31 is based on the diagram below:



31. Which of the following statements are correct?

- a. At an interest rate of 5% the quantity of money supplied is 50 if the money supply is regarded as exogenous.
 - b. At an interest rate of 10% equilibrium occurs in the financial market; the quantity of money supplied (=20) is equal to the quantity of money demanded (=20).
 - c. If the level of income increases, an excess demand for money exists at an interest rate of 10%.
 - d. An increase in the demand for money shifts the M^s curve to the right.
- 1. a, b and c
 - 2. a and d
 - 3. b, c and d
 - 4. Only b and c
 - 5. Only a and b

32. An expansionary monetary policy involves the ...

- 1. selling of bonds by the central bank on the open market to increase the supply of money and the interest rate will decrease.
- 2. buying of bonds on the open market by the central bank to decrease the supply of money and the interest rate will increase.
- 3. selling of bonds on the open market by the central bank to decrease the supply of money and the interest rate will increase.
- 4. buying of bonds on the open market by the central bank to increase the supply of money and the interest rate will decrease.

33. If the face value of a treasury bill is R300 000, the price paid is R280 000 with the maturity date of one year, the rate of return is ...

- 1. R20 000
- 2. 7.14%
- 3. 6.67%
- 4. R280 000
- 5. 2.07%

34. Which one of the following chain of events represents the impact of a decrease in income on the financial market?

- 1. $Y \downarrow \rightarrow I \uparrow$
- 2. $Y \downarrow \rightarrow i \uparrow$
- 3. $Y \downarrow \rightarrow M^d \downarrow \rightarrow P_b \downarrow \rightarrow i \downarrow \rightarrow Y \downarrow$
- 4. $Y \downarrow \rightarrow M^d \uparrow \rightarrow P_b \downarrow \rightarrow i \uparrow \rightarrow Y \uparrow$
- 5. $Y \downarrow \rightarrow M^d \downarrow \rightarrow P_b \uparrow \rightarrow i \downarrow$

35. Which of the following statements is/are correct?

A decrease in income with simultaneous expansionary open market operations by the central bank ...

- a. is represented by a shift of the demand for money curve to the left and the money supply curve to the right.
- b. is represented by a shift of the demand for money curve to the right and the money supply curve to the left.
- c. will result in an increase in the interest rate.
- d. will result in a decrease in the interest rate.
- e. will result in an indeterminate impact on the interest rate.

- 1. Only e
- 2. a and e
- 3. b and c
- 4. a and d
- 5. b and e

SEMESTER 1
WRITTEN ASSIGNMENT 02
LEARNING UNITS 1 TO 4
SELF-ASSESSMENT ASSIGNMENT
DO NOT SUBMIT THIS ASSIGNMENT

HINT: Align the length of your answers to the marks indicated. Do not submit your answers. Assess or mark your answers once you have received Tutorial Letter 202.

Question 1 (5 marks)

The IS-LM model is a simplification of the interrelationship between selected economic variables. The model consists of a number of endogenous variables (those variables whose values are determined inside the model) and a number of exogenous variables (those variables whose values are determined outside the model).

List the various endogenous and exogenous variables in the IS-LM model.

Question 2 (6 marks)

Explain why investment spending is a negative function of the interest rate and a positive function of the level of output and income and name two determinants of autonomous investment in South Africa.

Question 3 (6 marks)

Use the following information to derive an IS curve:

- A decrease in the interest rate from 6% to 4% increases investment spending by 200.
- Autonomous spending before the decrease in the interest rate is 800.
- The multiplier is 5.

Question 4 (6 marks)

Derive the LM curve by assuming that the level of output and income decreases.

Question 5 (6 marks)

Critically discuss the following statement:

The more sensitive investment spending is for a change in the interest rate and the less sensitive it is for a change in the level of output and income the greater the impact of an expansionary fiscal policy on the level of output and income.

Question 6 (8 marks)

Use the IS-LM model to identify the variables that will have an impact on the effectiveness of an expansionary fiscal policy to increase the level of output and income and explain how these variables influence the effectiveness of fiscal policy.

Question 7 (8 marks)

Use the IS-LM model to identify the variables that will have an impact on the effectiveness of an expansionary monetary policy to increase the level of output and income and explain how these variables influence the effectiveness of monetary policy.

Question 8 (10 marks)

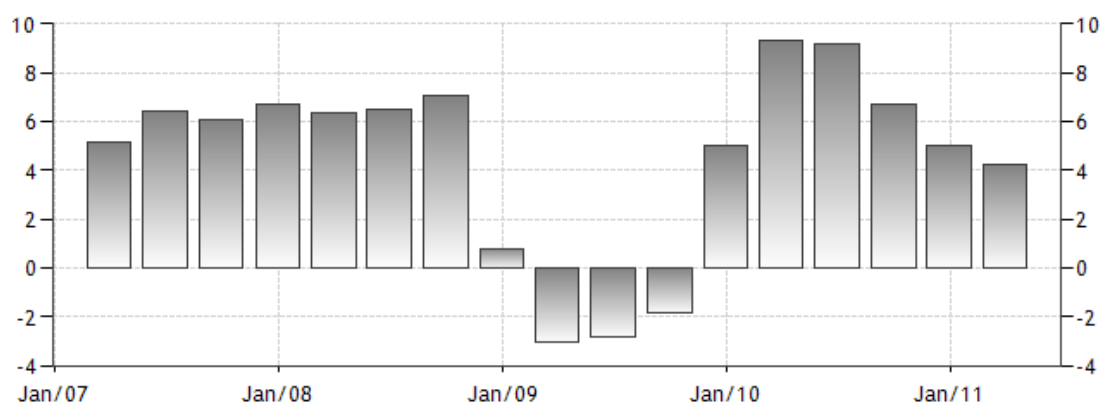
This question is based on the following text and information about the Brazilian economy.

The Great Recession

The Great Recession originated in the financial markets of the United States of America in 2007. It was triggered by falling house prices which led to the so-called “subprime mortgage” crisis. Preceding the crisis there was a rapid increase in mortgages to less creditworthy borrowers. A combination of falling house prices and default mortgage payments led to the failure and near failure of major financial institutions in America. This sent shockwaves across the financial markets of the world and resulted in a loss of confidence in financial markets and institutions, with the result that share prices fell sharply, investor confidence plunged and the availability of credit to firms and households was severely curtailed. This had the result that consumption spending by households and investment spending by firms declined which had a major impact on the level of output and income.

In response to the world wide economic crisis many countries used monetary and fiscal policies in an attempt to deal with the impact of the recession on the level of output and income.

BRAZIL GDP ANNUAL GROWTH RATE



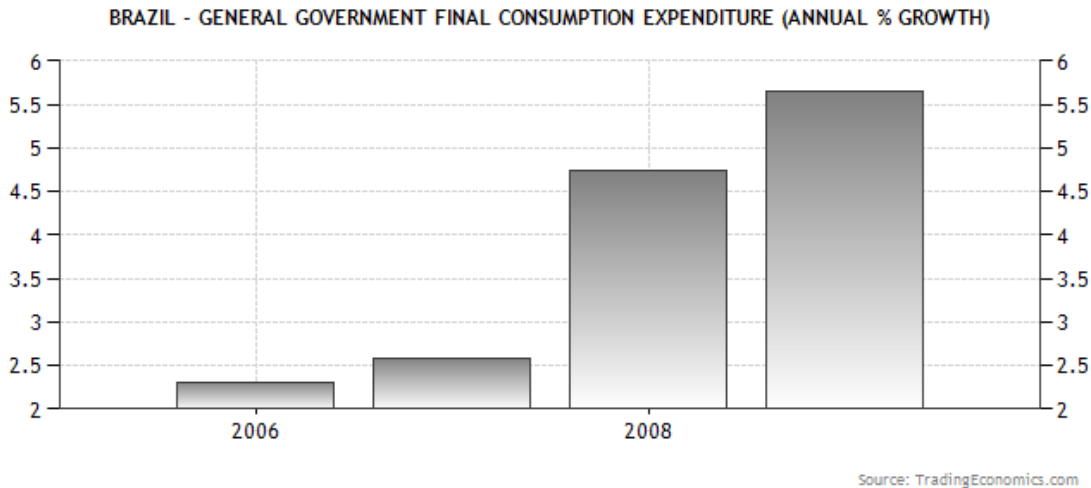
source: TradingEconomics.com; IBGE

BRAZIL INTEREST RATE

Benchmark Interest Rate



source: TradingEconomics.com; Banco Central do Brasil



- a. Given that an economic recession is defined as a decrease in real GDP for two consecutive periods (where a period is 3 months, also known as a quarter because there are four periods of 3 months in a year), during which year did Brazil experience an economic recession?
- b. Based on the above information use the IS-LM model to explain how Brazil made use of monetary and fiscal policies to deal with the economic recession they experienced.

Question 9 (4 marks)

The impact of an expansionary fiscal policy differs in the goods market model compared to the impact in the IS-LM model. What are the similarities and differences between the impact in the goods market model and the IS-LM model?

Question 10 (6 marks)

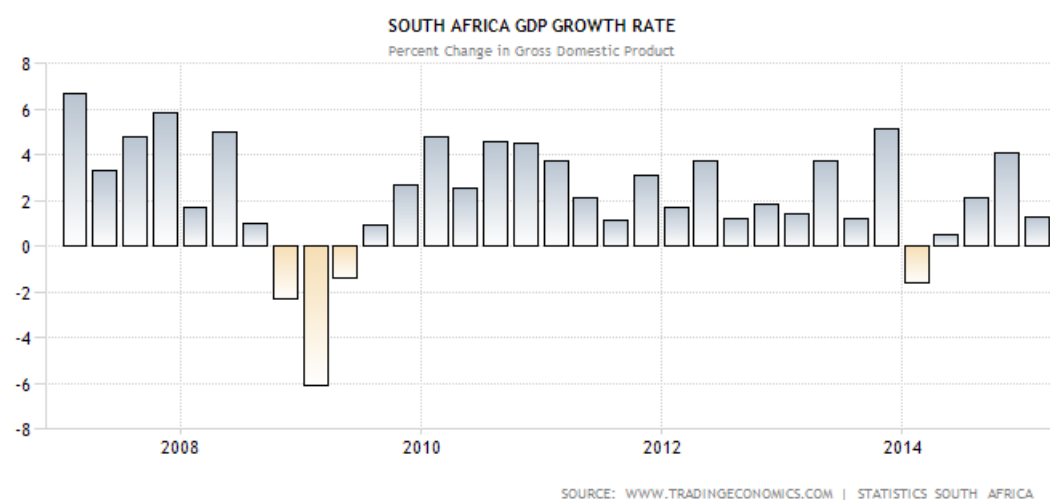
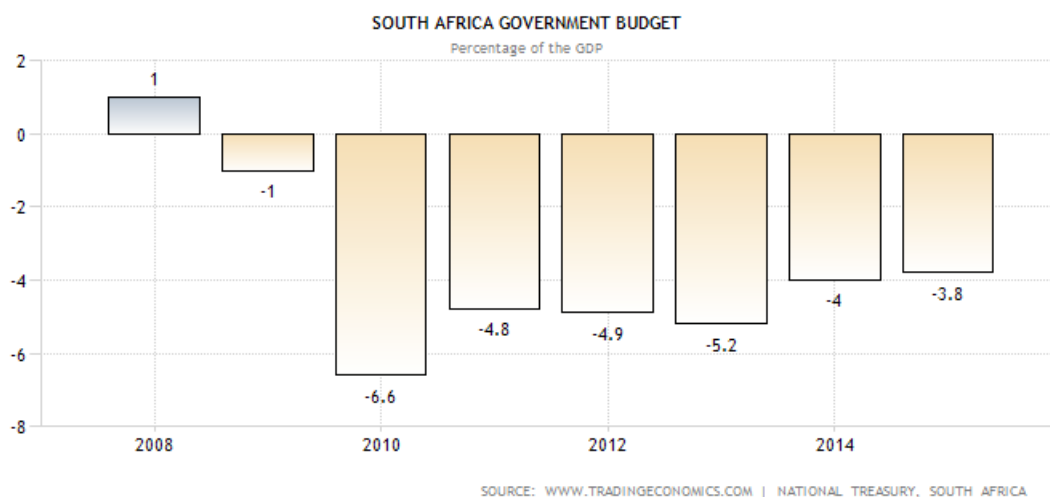
Use the IS-LM model to compare the impact of an expansionary fiscal policy with that of a contractionary monetary policy.

Questions 11 (2.5 marks) and question 12 (8 marks)

Questions 11 and 12 are based on the following graphs:

Question 11 (2.5 marks)





11. Which of the following statements are correct for South Africa?

- Government spending was below R480 000 million in the first quarter of 2007 and reached a high of just under R620 000 million in the fourth quarter of 2014.
- Government has sustained a budget deficit since 2008.
- The economic downturn which began in the last quarter of 2008 was caused by contractionary fiscal policy.
- The country suffered a recession in the beginning of 2014.

- a, b and d
- Only a and b
- Only c and d
- Only a and d

Question 12 (8 marks)

Policy makers in South Africa can use fiscal and monetary policies to deal with the impact of negative economic growth, stemming from an external shock such as a decline in world GDP, on the South African economy.

- a. Identify the period during which a recession took place in the South African economy.
- b. Use the IS-LM model to explain how fiscal and monetary policies were used to deal with this impact in order to boost the economy.

SEMESTER 1

ASSIGNMENT 03

LEARNING UNITS 1 TO 4

DUE DATE: 2016/03/22

UNIQUE NUMBER: 863782

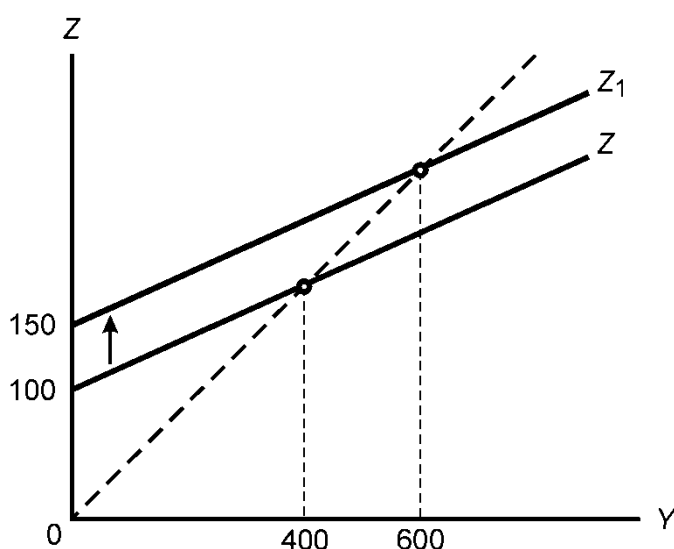
This assignment contributes 40% towards your semester mark.

Please ensure that this assignment reaches the university before the due date.

Answer all questions on a mark-reading sheet.

1. Which of the following would be included in the calculation of gross domestic product (GDP) of South Africa?
 - a. Exports of agricultural products to China.
 - b. Imports of motorcars from Japan to South Africa.
 - c. A citizen from Lesotho (foreign country) earns a wage at a copper mine in South Africa.
 - d. A farmer from Limpopo (South Africa) buys his neighbour's tractor.
 - e. Ford Motor Company of America builds an assembly plant in the Eastern Cape (South Africa).
 1. a, c, d and e
 2. b, c, d and e
 3. a, b and e
 4. Only b, c and d
 5. Only a, c and e

Question 2 is based on the following diagram:

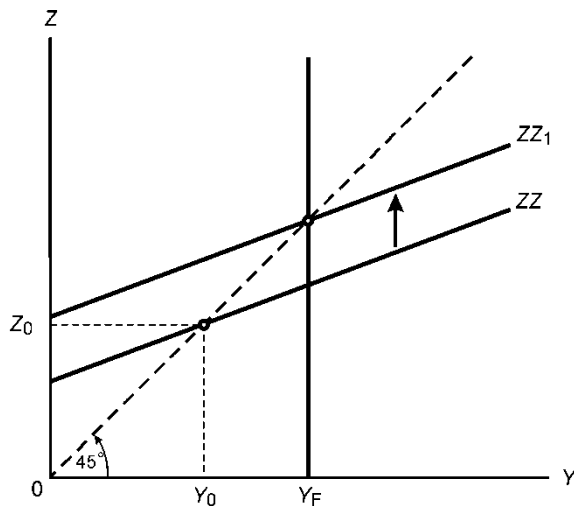


2. Which of the following statements are correct?

- Induced consumption is equal to R100 if income is R400.
- The multiplier is equal to 4.
- If government spending increases with R50, the equilibrium output and income level will increase by 50 times the multiplier.
- If there is a change in the marginal propensity to consume, the Z curve will shift upwards and the equilibrium level of output and income will increase.
- Any change in consumer confidence will have no effect on the above goods market model.

- a, b and c
- b, c and d
- a, c and e
- b, d and e
- Only b and c

Questions 3 and 4 are based on the following diagram.



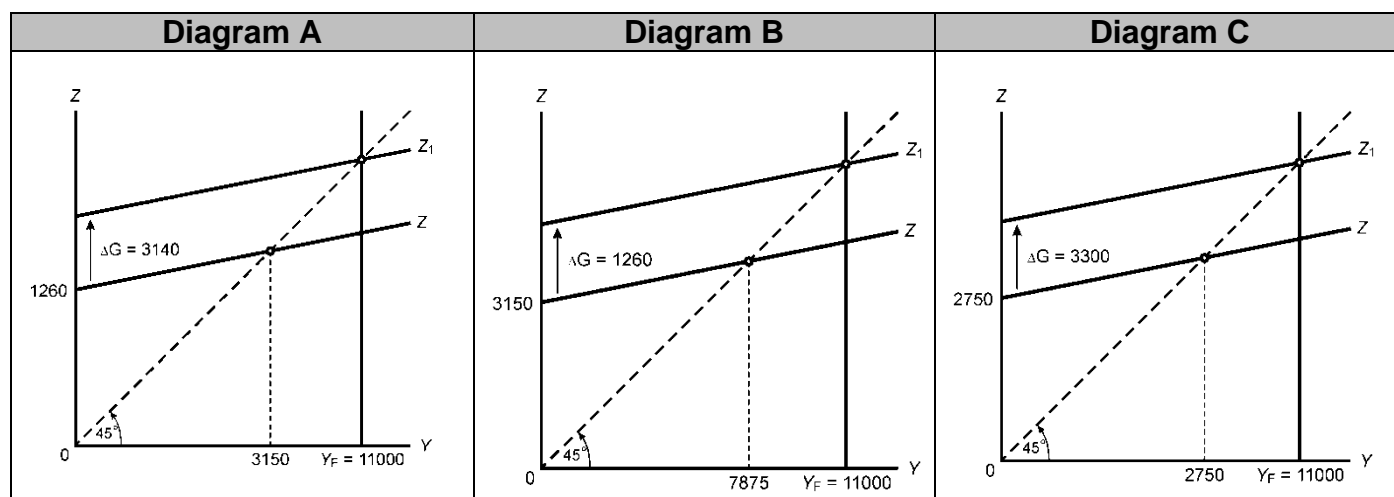
3. Which of the following statements are correct?

The ZZ curve would shift upwards to ZZ_1 if ...

- induced consumption increases.
- the marginal propensity to consume increases.
- investment spending increases.
- government spending increases and/or taxes decrease.
- there is a positive investment confidence and consumer confidence in the economy.

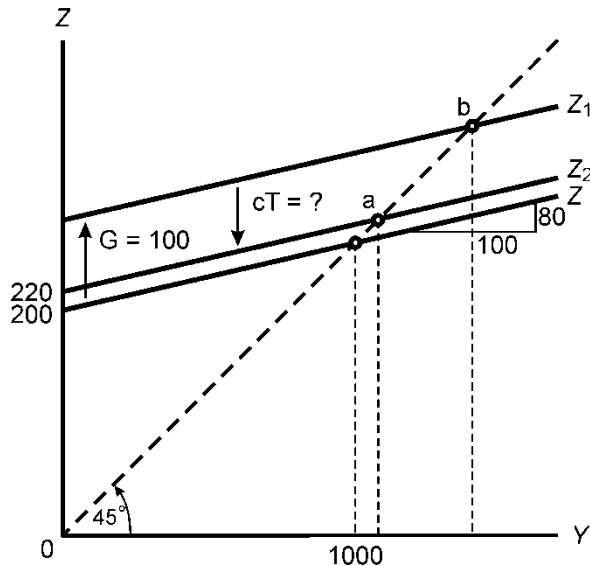
- a, b and c
- Only b, c and d
- b, c, d and e
- Only c, d and e
- a, c, d and e

4. Which of the following statements is/are correct?
To reach the full employment level (Y_f) _____ can be implemented.
- expansionary fiscal policy
 - expansionary monetary policy
 - contractionary fiscal policy
 - contractionary monetary policy
- a and b
 - Only a
 - a and c
 - c and d
 - Only b
5. Given that $c_o = R200$ million, $\bar{T} = R600$ million, $G = R700$ million, $c = 0.6$, $T = R400$ million and $Y_f = R11\ 000$ million the equilibrium level of output and income is _____ and in order to reach the full-employment level of income, government spending must increase by _____.
- R7 250m R2 900m
 - R1 260m R3 896m
 - R3 150m R3 140m
 - R2 750m R3 300m
 - R3 150m R7 850m
6. Which one of the following goods market models represent the data given for question 5 above?



- Diagram A
- Diagram B
- Diagram C
- Not Diagram A, B or C

Question 7 is based on the following diagram. Assume that G and T increase by R100.



7. Which of the following statements is/are correct?

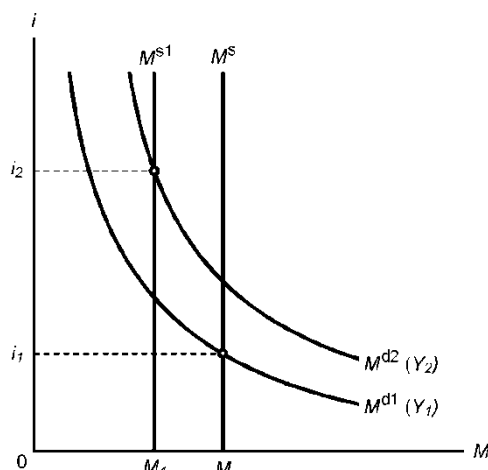
- The multiplier is 4.
- If government spending increases by R100, the equilibrium level of output and income will be R1 500 and the Z curve will shift to Z₁.
- If taxes increase by R100, cT will be R80, the equilibrium level of output and income will be R1 100 and it will be represented by point a in the above diagram.
- The above diagram and questions imply the working of the balanced budget multiplier.
- Although there is an increase of R100 in taxes, there will be still an expansionary net effect of R500 on the equilibrium level of output and income.

- a, b, c and e
- b, c, d and e
- Only a, c and e
- Only b and d
- Not option 1, 2, 3 or 4

8. If income increases, the demand for money ...

- decreases and the money demand curve will shift to the left.
- increases and the money demand curve will shift to the right.
- increases and there will be an upward movement along the money demand curve.
- increases and there will be downward movement along the money demand curve.

Question 9 is based on the following diagram:



9. Which of the following statements is/are correct?

- An increase in the interest rate from i_1 to i_2 will shift the demand for money curve to the right.
- If the money supply curve shifts to the left it implies the implementation of a contractionary fiscal policy.
- If income decreases the M^{d1} curve will shift to M^{d2} and the result is an increase in the interest rate.
- The diagram above represents an increase in income with simultaneous expansionary open market operations by the central bank. The result is that the interest rate will definitely increase.
- The shift from M^S to M^{S1} represents the buying of bonds on the open market by the central bank.

- a, b, c and d
- Only b and c
- d and e
- Only e
- Not option 1, 2, 3 or 4

10. Which of the following statements are correct?

- The demand for money is a function of income and the interest rate.
- The supply of money is a function of income and fiscal policy.
- There is a positive relationship between income and the demand for money.
- If the interest rate increases, the quantity of money demanded decreases.
- If the price of a treasury bill is R9 700 and the rate of return is 3%, the rate of return will be lower than 3% if the price of the treasury bill increases to R9 800.

- a, b, c, d and e
- Only b, d and e
- Only a, d and e
- Only b, c and d
- Only a, c, d and e

11. Which one of the following statements is **incorrect**?

If the financial market is in a liquidity trap it implies that ...

1. monetary policy is ineffective in bringing about a decrease in the interest rate.
2. the return on holding money is zero.
3. there is a high demand for bonds.
4. the return on holding bonds is extremely low.

Questions 12 and 13 are based on the following diagrams:

DIAGRAM 1

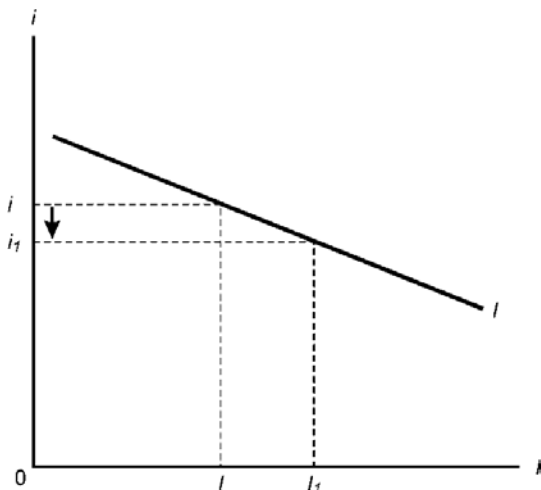
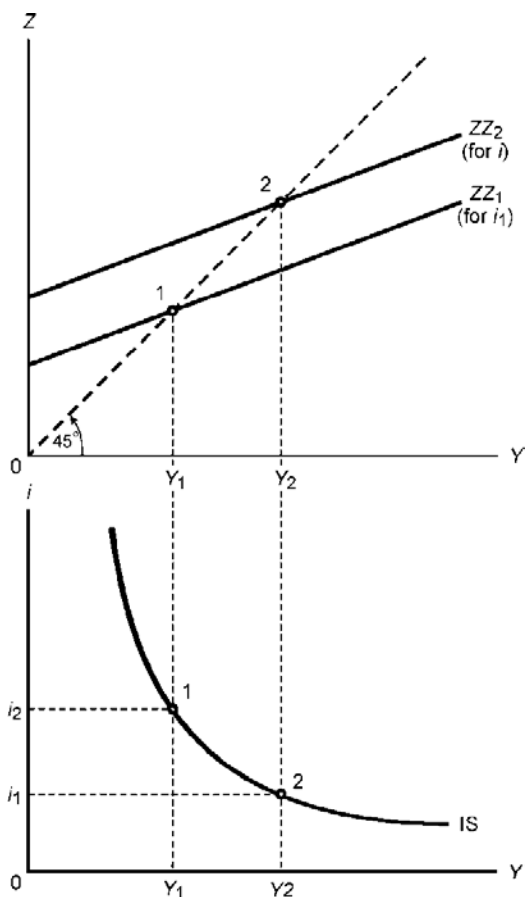


DIAGRAM 2



12. Which of the following statements are correct?

To derive the IS curve ...

- a. the interest rate changes.
- b. the income changes.
- c. a change in the interest rate will have an impact on the goods market.
- d. a change in the income level will have an impact on the goods market.
- e. investment is regarded as autonomous.

- 1. Only a and c
- 2. Only b and d
- 3. b, d and e
- 4. a, c and e
- 5. Only b and e

13. If the interest rate decreases in diagram 1 above ...

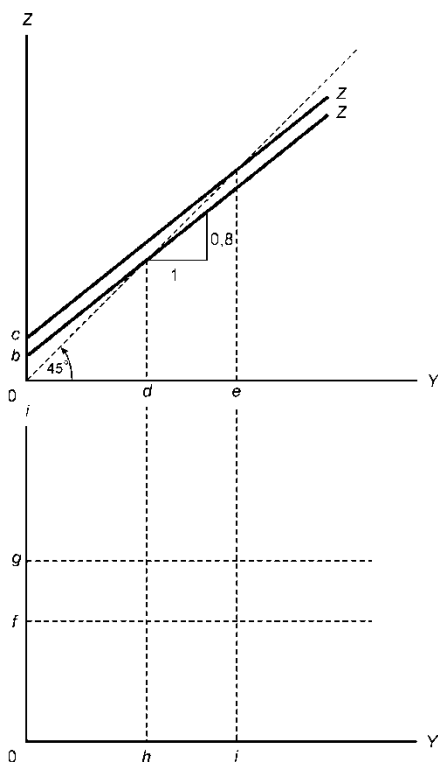
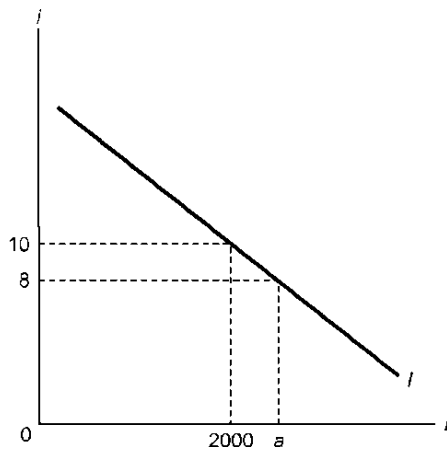
- a. government spending will decrease in the goods market, the demand for goods decreases from ZZ_2 to ZZ_1 and the equilibrium level of output and income falls from Y_2 to Y_1 .
- b. government spending will increase in the goods market, the demand for goods increases from ZZ_1 to ZZ_2 and the equilibrium level of output and income rises from Y_1 to Y_2 .
- c. investment spending will decrease in the goods market, the demand for goods decreases from ZZ_2 to ZZ_1 and the equilibrium level of output and income falls from Y_2 to Y_1 .
- d. investment spending will increase in the goods market, the demand for goods increases from ZZ_1 to ZZ_2 and the equilibrium level of output and income rises from Y_1 to Y_2 .
- e. taxation will decrease in the goods market, disposable income of households decreases which decreases the demand for goods from ZZ_2 to ZZ_1 and the equilibrium level of output and income falls from Y_2 to Y_1 .

- 1. a, c and d
- 2. b, d and e
- 3. Only b and d
- 4. Only c
- 5. Only d

Question 14 deals with the derivation of the IS curve and are based on the following information and diagrams:

The autonomous spending at an interest rate of 10% is 3 000.

A decrease in the interest rate from 10% to 8% increases investment spending by 1 000.

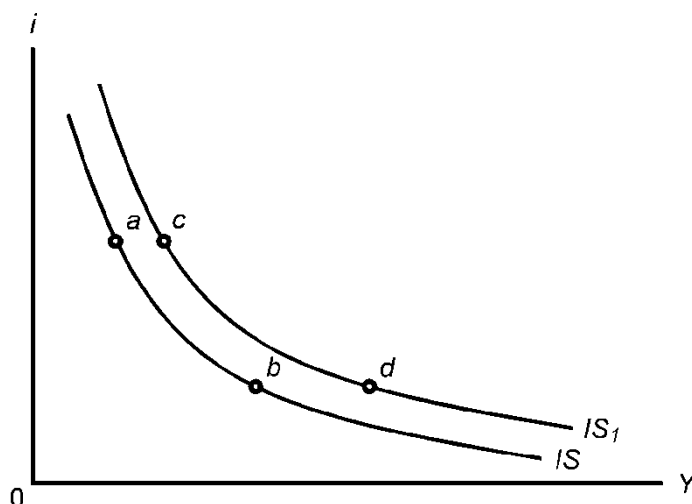


14. Which of the following statements are correct?

- a. The value for a is 3 000.
- b. The values for b and c are: $b = 2\,000$ and $c = 3\,000$
- c. The values for b and c are: $b = 3\,000$ and $c = 4\,000$
- d. The values for d and e are: $d = 15\,000$ and $e = 20\,000$
- e. The values for d and e are: $d = 10\,000$ and $e = 15\,000$
- f. The values for f and g are: $f = 10\%$ and $g = 8\%$
- g. The values for f and g are $f = 8\%$ and $g = 10\%$
- h. The values for h and i are the same as the values for d and e .

1. a, c, e, g and h
2. Only c, d, g and h
3. a, c, d, g and h
4. a, b, d, f and h
5. Not option 1, 2, 3 or 4

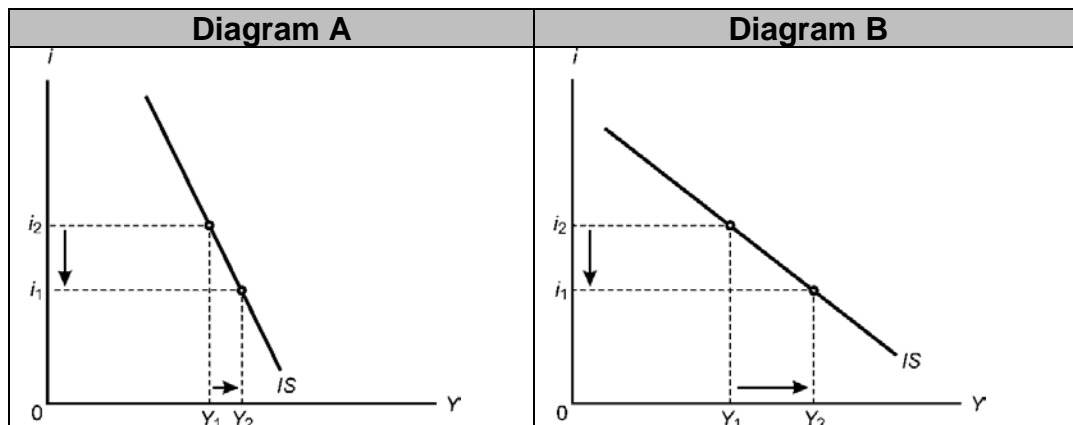
Question 15 is based on the following diagram:



15. Which of the following statements is/are correct?

- a. The movement from point b to point a implies an increase in investment spending.
 - b. The movement from point a to point b implies a decrease in the interest rate which will increase investment spending and the demand for goods.
 - c. A change in investment spending does not always shift the IS curve because an increase in investment spending due to a decrease in the interest rate is represented by a movement along the IS curve.
 - d. An increase in business confidence and a decrease in the interest rate both increase investment spending. The increase in investment spending due to an increase in business confidence shifts the IS curve to IS_1 while an increase in investment due to a decrease in the interest rate causes a downward movement along the IS curve from point a to point d.
 - e. A shift from IS to IS_1 can be the result of a change in government spending, a change in consumer confidence, or a change in any of the autonomous factors that change the demand for goods.
 - f. The movement from point b on IS to point d on IS_1 can be the result of a decrease in taxation.
1. a, c and d
 2. b, c, e and f
 3. Only d and e
 4. c, d and e
 5. None of the options 1 to 4

Question 16 is based on the following diagrams which represent two different slopes of the IS curve:



16. Which of the following statements are correct?

- a. Diagram A indicates that investment spending is very sensitive to a change in the interest rate.
- b. The slope of the IS curve in Diagram B is more inelastic since the impact of a given change in the interest rate will have a greater impact on investment spending and, consequently the impact on the level of output and income is greater.
- c. The output and income sensitivity of investment spending measures how sensitive investment spending is to a change in the interest rate.
- d. The more sensitive investment spending is to a given change of output and income the more elastic the IS curve will be. It is illustrated by Diagram B.
- e. Comparing Diagrams A and B we can conclude that the impact of a change in the interest rate on the level of output and income is greater in Diagram B than in Diagram A.

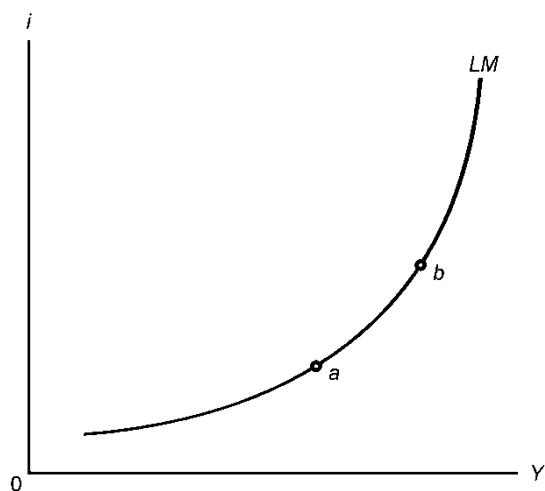
1. a, c and d
2. c, d and e
3. b, d and e
4. a, b and c
5. Only d and e

17. Which of the following statements are correct?

- a. If the nominal money supply is equal to R200 million and the general price level increases from R10 to R20, the real money supply increases from 20 million to 10 million.
- b. For a given nominal money supply, an increase in the general price level will decrease the real money supply while a decrease in the general price level will increase the real money supply.
- c. To derive the LM curve, we can assume an increase or decrease in the level of output and income while deriving the IS curve we assume a change in the interest rate.
- d. The IS curve is derived from the goods market while the LM curve is derived from the financial market.
- e. The LM curve indicates a positive relationship between combinations of interest rates and income levels, where the goods market and the financial market are in equilibrium and the real money supply increased.

1. Only b, c and d
2. a, b, c and d
3. b, c, d and e
4. Only c and d
5. Only a, b and c

Questions 18 and 19 are based on the following LM curve:



18. Given the LM curve the situation at point b compared to point a is described the best by which one of the following?

	Demand for money	Supply of money	Interest rate	Output
1.	Higher	Higher	Higher	Higher
2.	Lower	Lower	Lower	Lower
3.	Higher	The same	Higher	Higher
4.	The same	Higher	Higher	Higher
5.	Lower	The same	Lower	Lower

19. Which of the following factors will shift the LM curve upwards?

- a. An increase in the marginal propensity to consume.
- b. An increase in the nominal money supply.
- c. A decrease in the nominal money supply.
- d. A decrease in investment spending.
- e. A decrease in the interest rate.

1. a and b
2. Only c and e
3. c, d and e
4. Only b
5. Only c

20. Which of the following statements are correct?

- a. Marginal propensity to consume and autonomous consumption are exogenous variables of the consumption function.
- b. Nominal money supply and the part of the demand for money that is influenced by expectations, business confidence, and political and social factors are exogenous variables in the financial market.
- c. Marginal propensity to consume and the level of output and income are endogenous variables in the goods market model.
- d. Investment spending is an exogenous variable in the goods market model but in the IS-LM model the part of investment spending that is dependent on the level of output and income and the interest rate are the endogenous variables.
- e. Level of output and income, interest rate, investment spending, consumption spending are exogenous variables in the IS-LM model.
- f. Taxes, government spending and the nominal supply of money are exogenous variables in the IS-LM model.

- 1. a, b, c and d
- 2. b, c, e and f
- 3. Only a, b and f
- 4. a, b, d and f
- 5. b, d and e

21. Which of the following statements is/are correct?
In the IS-LM model a change in ...

- a. government spending will have an impact on the goods market first where it influences a number of variables which eventually impact on the financial market.
- b. monetary policy will have an impact on the financial market first where it influences a number of variables which eventually impact on the goods market.
- c. the nominal money supply will have an impact on the goods market first where it influences a number of variables which eventually impact on the financial market.
- d. taxes will have an impact on financial market first where it influences a number of variables which eventually impact on the goods market.
- e. fiscal policy will have an impact on the goods market first where it influences a number of variables which eventually impact on the financial market.
- f. monetary policy will have an impact on the goods market first where it influences a number of variables which eventually impact on the financial market.

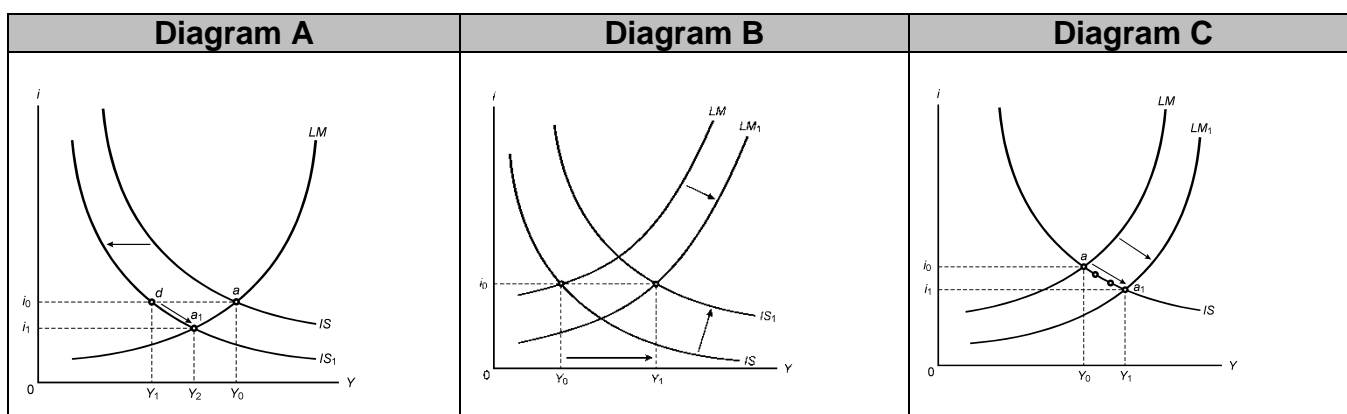
- 1. a, b, d and e
- 2. Only a, b and e
- 3. c, d and f
- 4. b and c
- 5. None of the options 1 to 4

22. Within the IS-LM model, which one of the following policy actions will bring about an increase in the level of output and a decrease in the interest rate?
1. A decrease in government spending.
 2. A decrease in the budget deficit.
 3. An increase in the money supply.
 4. An increase in government spending.
 5. A decrease in the money supply.
23. Within the IS-LM model, which one of the following policy actions will bring about a decrease in the level of output and an increase in the interest rate?
1. A contractionary fiscal policy.
 2. A contractionary monetary policy.
 3. A decrease in the budget deficit.
 4. An expansionary fiscal policy.
 5. An expansionary monetary policy.
24. Within the IS-LM model, which one of the following policy actions is appropriate if the objective is to decrease the budget deficit without decreasing the level of output?
1. An expansionary fiscal policy coupled with a contractionary monetary policy.
 2. An expansionary fiscal policy coupled with an expansionary monetary policy.
 3. A contractionary fiscal policy coupled with an expansionary monetary policy.
 4. A contractionary fiscal policy coupled with a contractionary monetary policy.

Question 25 is based on the following chain of events:

$$\begin{aligned}
 M \uparrow &\rightarrow M/P \uparrow \rightarrow i \downarrow \\
 i \downarrow &\rightarrow I \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow \\
 Y \uparrow &\rightarrow I \uparrow \\
 Y \uparrow &\rightarrow C \uparrow
 \end{aligned}$$

Which one of the following diagrams represents the above chain of events?

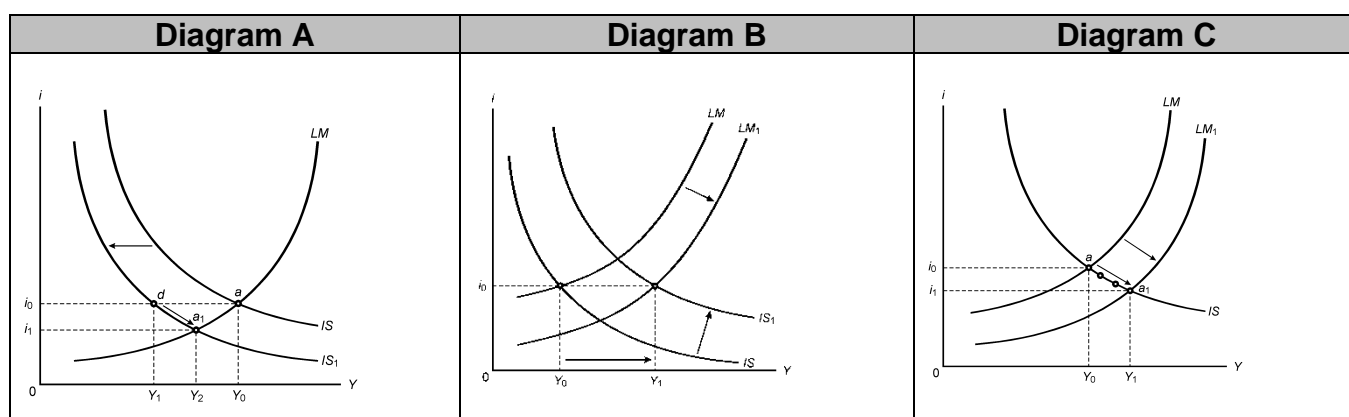


1. Diagram A
2. Diagram B
3. Diagram C
4. Not Diagram A, B or C

Question 26 is based on the following chain of events:

$$\begin{aligned}
 T \uparrow &\rightarrow Y_D \downarrow \rightarrow C \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow \\
 Y \downarrow &\rightarrow C \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow \\
 Y \downarrow &\rightarrow I \downarrow \\
 Y \downarrow &\rightarrow M^d \downarrow \rightarrow i \downarrow \\
 i \downarrow &\rightarrow I \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow
 \end{aligned}$$

26. Which one of the following diagrams represents the above chain of events?



1. Diagram A
2. Diagram B
3. Diagram C
4. Not Diagram A, B or C

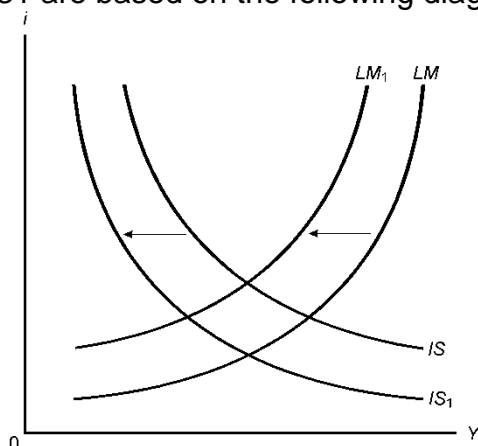
Question 27 refers to the factors that influence the impact or effectiveness of fiscal policy. Assume a decrease in government spending.

27. Which of the following statements are correct?

- a. If the multiplier changes from 2.5 to 5, the greater is the impact on the level of output and income. In the IS-LM model the shift of the IS curve to the left will be greater.
- b. The decrease in government spending will lead to a decrease in the interest rate in the financial market and therefore the decrease in government spending is more effective in influencing the level of output and income.
- c. The greater the interest sensitivity of investment spending the greater the shift of the IS curve.
- d. The output and income sensitivity of investment spending will have no impact on the effectiveness of fiscal policy.

1. Only a, c and d
2. Only a, b and d
3. Only a and b
4. Only b and c
5. a, b, c and d

Questions 28 to 31 are based on the following diagram:



28. The diagram indicates a(n) _____ and a(n) _____.

- | | |
|-------------------------------------|----------------------------------|
| a. contractionary fiscal policy; | contractionary monetary policy |
| b. expansionary fiscal policy; | contractionary monetary policy |
| c. expansionary fiscal policy; | expansionary monetary policy |
| d. decrease in government spending; | decrease in nominal money supply |
| e. increase in taxation; | increase in nominal money supply |

1. a and d
2. b and d
3. c and e
4. Only c
5. Only e

29. The shift from IS to IS₁ and the shift from LM to LM₁ causes a change in the interest rate.

The reason for the lower interest rate in the case of the shift of the IS curve is that the _____ while in the case of the LM curve the interest rate is higher since the _____.

- | | |
|--------------------------------|----------------------------|
| 1. money supply is lower; | money supply is higher |
| 2. demand for money is higher; | money supply is higher |
| 3. money supply is higher; | demand for money is higher |
| 4. demand for money is lower; | money supply is lower |

30. The shift from IS to IS₁ implies investment spending is indeterminate and the shift from LM to LM₁ implies that investment spending is _____ since the _____.

- | | |
|-------------------|--|
| 1. lower; | interest rate is higher |
| 2. higher; | interest rate is lower |
| 3. indeterminate; | interest rate is higher and then lower |
| 4. unchanged; | interest rate is unchanged |

31. The reason investment spending is indeterminate in the case of a shift of the IS curve to the left is because a ...
1. decrease in the interest rate increases investment while the increase in output decreases investment.
 2. decrease in the interest rate decreases investment while the increase in output increases investment.
 3. decrease in the interest rate increases investment while the decrease in output decreases investment.
 4. decrease in the interest rate decreases investment while the decrease in output decreases investment.
32. Comparing the impact in the IS-LM model for a closed economy of an *expansionary monetary policy* with an *expansionary fiscal policy* on investment spending the result is that:
1. In both cases investment spending definitely increases.
 2. In the case of fiscal policy investment spending is indeterminate and in the case of monetary policy investment spending is higher.
 3. In both cases investment spending is indeterminate.
 4. In both cases investment spending is definitely lower.
 5. In the case of fiscal policy investment spending it is higher and in the case of monetary policy investment spending is lower.
33. Comparing the impact in the IS-LM model for a closed economy of an *expansionary monetary policy* with an *expansionary fiscal policy* ...
- a. the real money supply is higher in the case of monetary policy since the nominal money supply is higher while in the case of fiscal policy there is no change in the real money supply.
 - b. the interest rate is higher in the case of monetary policy since the real money supply is higher while in the case of fiscal policy the interest rate is higher since the demand for money is higher.
 - c. the demand for money will increase in the case of monetary policy and in the case of fiscal policy government spending increases and/or taxes decrease.
 - d. In both cases the level of output and income will have a multiplier effect on investment spending.
1. Only a
 2. Only b
 3. Only c
 4. Only d
 5. Only a and d
34. If the objective is to increase the level of output and income without an increase in the interest rate the appropriate policies are _____ and _____.
1. contractionary fiscal policy; contractionary monetary policy
 2. expansionary fiscal policy; contractionary monetary policy
 3. expansionary fiscal policy; expansionary monetary policy
 4. increase in government spending; decrease in nominal money supply
 5. decrease in government spending; increase in nominal money supply

35. If the objective is to decrease the level of output and income as well as the interest rate the appropriate policies are _____ and _____.

- | | |
|-------------------------------------|----------------------------------|
| 1. contractionary fiscal policy; | contractionary monetary policy |
| 2. expansionary fiscal policy; | contractionary monetary policy |
| 3. expansionary fiscal policy; | expansionary monetary policy |
| 4. increase in government spending; | decrease in nominal money supply |
| 5. increase in government spending; | increase in nominal money supply |

SEMESTER 1
ASSIGNMENT 04
STUDY UNITS 5 TO 7
DUE DATE: 2016/04/11
UNIQUE NUMBER: 884585

This assignment contributes 40% towards your semester mark.

Please ensure that this assignment reaches the university before the due date.

Answer all questions on a mark-reading sheet.

1. Which of the following statements are correct?
 - a. Openness in goods markets is the ability of consumers and firms to choose between domestic goods and foreign goods.
 - b. Openness in financial markets is the ability of financial investors to choose between domestic financial assets and foreign financial assets.
 - c. The nominal exchange rate is the relative price of domestic goods in terms of foreign goods.
 - d. The real exchange rate is the price of the domestic currency in terms of the foreign currency.
 - e. The most popular way of measuring the openness of the goods market, is to express the imports and exports as a percentage of GDP.
 1. a, b, c, d and e
 2. Only a and b
 3. Only b, c and d
 4. Only a, b and e
 5. Only c, d and e

2. Which of the following refers to a depreciation of the rand?
 - a. R1 = \$0.40 to R1 = \$0.35
 - b. R1 = \$0.25 to R1 = \$0.35
 - c. R1 = \$0.60 to R1 = \$0.70
 - d. \$1 = R12 to \$1 = R11
 - e. \$1 = R10 to \$1 = R11
 1. a and d
 2. Only b and c
 3. a and e
 4. b, c and d
 5. b and e

3. From the perspective of South Africa, an increase (appreciation) in the nominal exchange rate will cause the following to happen:
 1. The Rand becomes less expensive to foreigners.
 2. Foreign goods are more expensive to South Africans.
 3. Foreign currency is more expensive to South Africans.
 4. South African goods are more expensive to foreigners.
 5. Imports are more expensive.

4. An increase in the nominal exchange rate between RSA and the USA implies that ...
 1. more rands must be paid for a dollar, leading to higher imports and possibly a trade deficit.
 2. fewer rands must be paid for a dollar, leading to lower imports and possibly a trade surplus.
 3. fewer rands must be paid for a dollar, leading to lower exports and possibly a trade deficit.
 4. more rands must be paid for a dollar, leading to lower exports and possibly a trade surplus.

Question 5 is based on the following formula:

The real exchange rate between the rand and the dollar is:

$$\epsilon = \frac{EP}{P^*}$$

Where

P = price of domestic (SA) goods

P* = price of foreign (USA) goods

E = nominal exchange rate

5. Which of the following statements are correct?
 - a. If the increase in the price of domestic goods rises faster than the price of foreign goods and E is unchanged, the real exchange rate increases and a real appreciation takes place.
 - b. If the increase in the price of domestic goods rises faster than the price of foreign goods and E is unchanged, the real exchange rate decreases and a real depreciation takes place.
 - c. If the increase in the price of domestic goods (P) is smaller than the increase in the price of foreign goods (P*) and E is unchanged, the real exchange rate decreases and a real depreciation takes place.
 - d. Assume that the increase in the price of foreign goods (P*) and the increase in the price of domestic goods (P) are the same and the rand depreciates against the dollar. Then, the real exchange rate decreases and a real depreciation take place.
 - e. If the real exchange rate decreases, USA goods are relatively cheaper than SA goods in South Africa.

1. b, c and d
2. c, d and e
3. Only c and d
4. Only a and d
5. a, c and d

6. A trade balance deficit indicates that ...

1. merchandise imports exceed merchandise exports.
2. government spending exceeds tax revenue.
3. merchandise exports exceed merchandise imports.
4. tax revenue exceeds government spending.
5. imports of services exceed exports of services.

7. Given the following information:

Interest rate on RSA bonds: 8%

Interest rate on USA bonds: 11%

Which one of the following statements is correct?

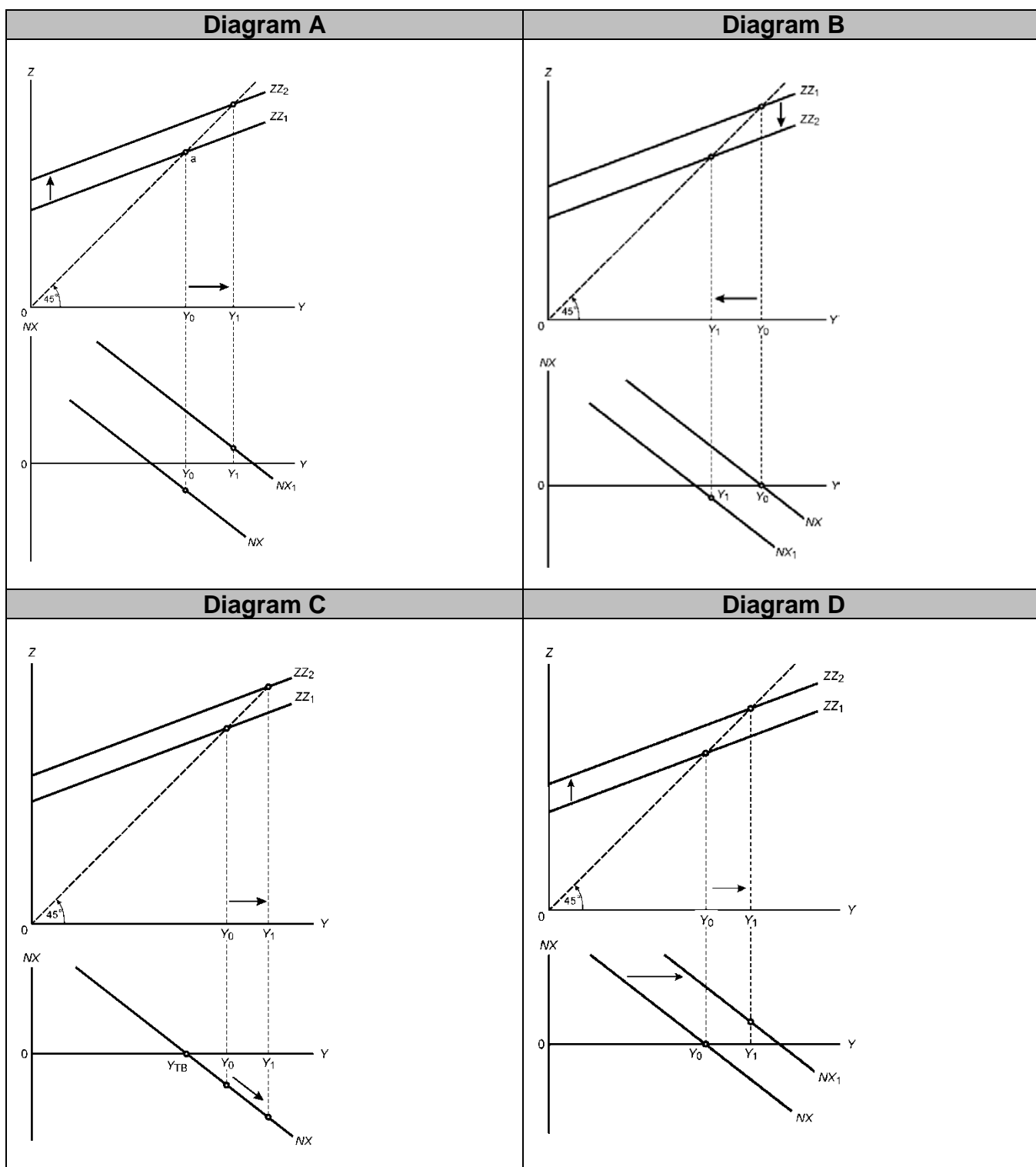
1. If the expected appreciation of the rand is 2% in a year's time, investment in RSA bonds are more attractive and financial market participants will buy RSA bonds.
2. If the expected appreciation of the rand is 4% in a year's time, investment in RSA bonds are more attractive and financial market participants will buy RSA bonds.
3. If the expected depreciation of the rand is 3% in a year's time, investment in RSA bonds are more attractive and financial market participants will buy RSA bonds.
4. If it is expected that the R/\$ exchange rate will be unchanged in a year's time, financial market participants will be indifferent between RSA and USA bonds.

8. If the SA rand depreciates against the USA dollar, it leads to ...

- a. more imports of goods and services.
- b. less imports of goods and services.
- c. more exports of goods and services.
- d. less exports of goods and services.

1. a and c
2. a and d
3. b and c
4. b and d
5. Only c

9. If the SA rand depreciates against the USA dollar as indicated in question 8 above, it can graphically illustrated as follows:



1. Diagram A.
2. Diagram B.
3. Diagram C.
4. Diagram D.
5. Diagrams A and D.

10. An increase in the demand for domestic goods takes place if ...

1. imports increase.
2. exports increase.
3. investment spending declines.
4. consumption spending declines.
5. government spending declines.

11. If exports are less than imports, then:

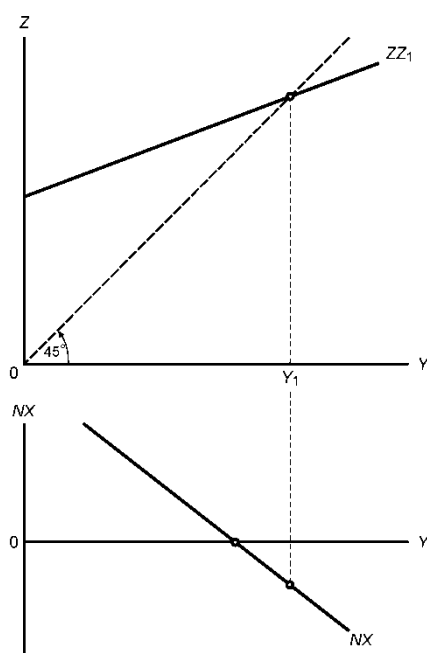
1. A trade surplus exists.
2. A trade balance exists.
3. A trade deficit exists.
4. A budget deficit exists.
5. A budget surplus exists.

12. Regarding the determinants of exports, which of the following are correct?

- a. $Y \downarrow \rightarrow X \downarrow$
- b. $Y^* \downarrow \rightarrow X \downarrow$
- c. $Y^* \uparrow \rightarrow X \downarrow$
- d. $\epsilon \uparrow \rightarrow X \uparrow$
- e. $\epsilon \uparrow \rightarrow X \downarrow$

1. a and e
2. a and d
3. b and e
4. b and d
5. c and e

13. Based on the following diagram, which one of the following policy actions would be likely to achieve a higher output level and a trade surplus?

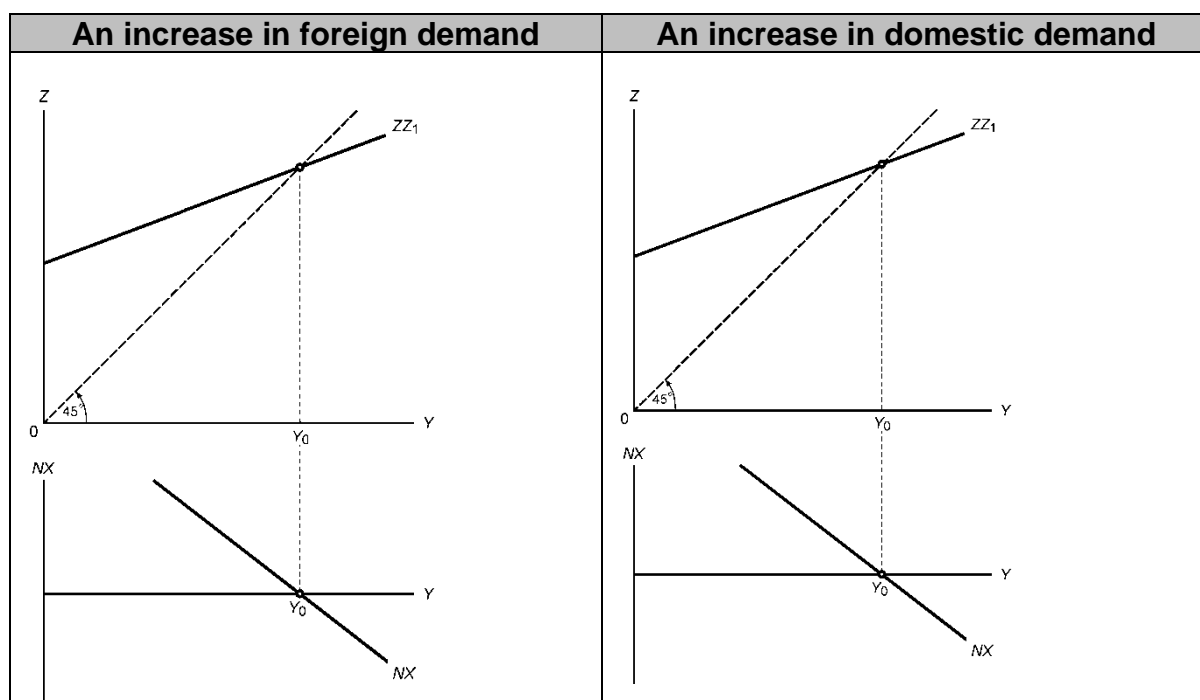


1. A reduction in taxation.
2. A simultaneous decrease in government spending and an appreciation of the exchange rate.
3. A depreciation of the exchange rate.
4. An appreciation of the exchange rate.

Questions 14 and 15 are based on the following:

Compare the impact on the level of output and the trade balance of an increase in foreign demand with that of an increase in domestic demand.

Hint: Complete the following diagrams and then answer questions 14 and 15.



14. Which of the following statements is/are correct?

- a. An increase in foreign demand and an increase in domestic demand will shift the demand curve ZZ_1 in both instances upwards.
- b. An increase in foreign demand will shift the demand curve ZZ_1 upwards while an increase in domestic demand will shift the demand curve ZZ_1 downwards.
- c. An increase in foreign demand and an increase in domestic demand will increase the level of output and income.
- d. An increase in foreign demand will increase the level of output and income while an increase in domestic demand will decrease the level of output and income.

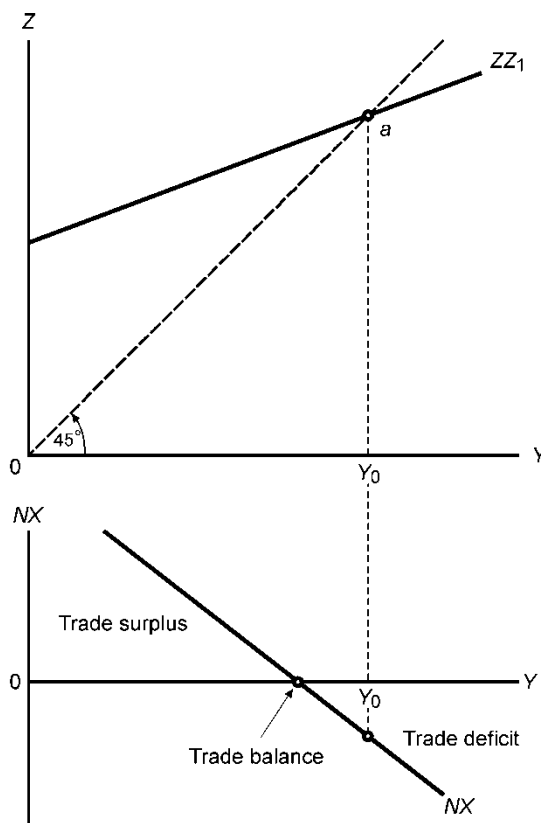
1. a and c
2. b and c
3. a and d
4. b and d
5. Only a

15. Which of the following statements are correct?

- An increase in foreign demand and an increase in domestic demand will shift the NX curve to the right.
- An increase in foreign demand will shift the NX curve to the right while an increase in domestic demand will cause a downward movement along the NX curve.
- An increase in foreign demand will shift the NX curve to the right while an increase in domestic demand will cause an upward movement along the NX curve.
- In the case of an increase in foreign demand the trade balance will improve and in the case of an increase in domestic demand the trade balance worsens.
- In the case of an increase in foreign demand a trade surplus occurs and in the case of an increase in domestic demand a trade deficit occurs.

- a, c and e
- b, c and d
- b, d and e
- a, d and e
- Only b and e

16. Given point a in the following diagram, what would the most likely impact of a depreciation of the domestic currency be?

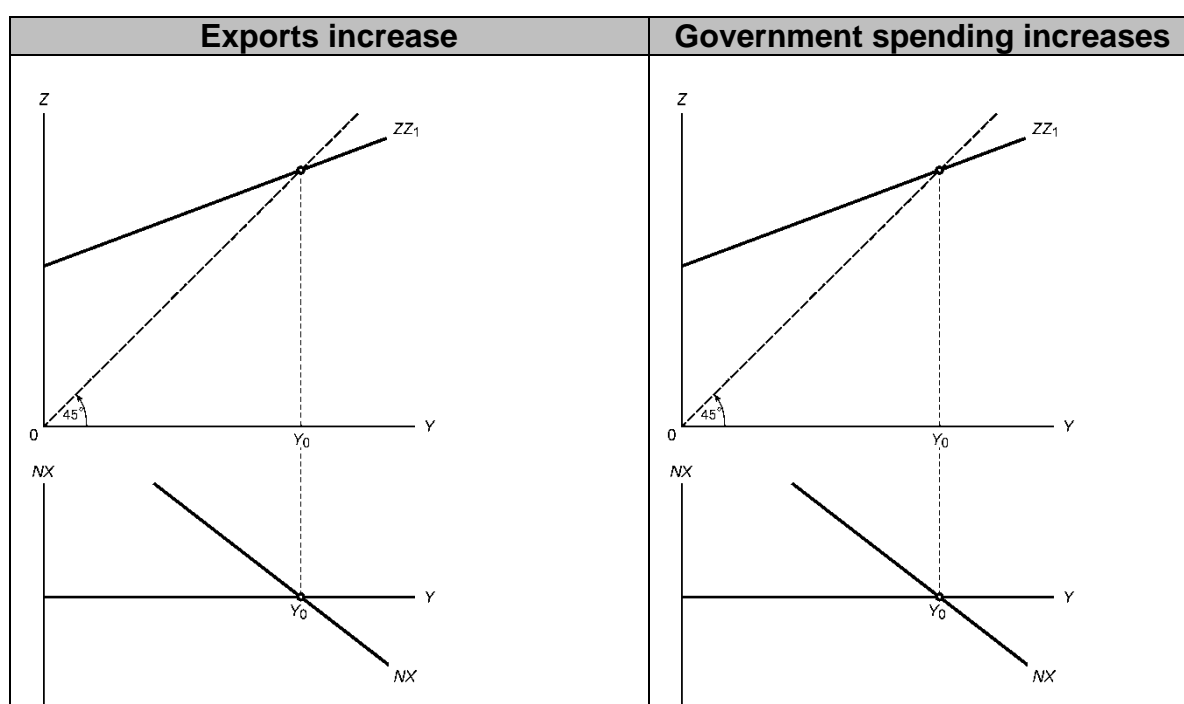


- The domestic level of output will increase and there will be a trade deficit.
- The domestic level of output will decrease and there will be a trade surplus.
- The domestic level of output will decrease and there will be a trade deficit.
- The domestic level of output will be unchanged and there will be a trade surplus.
- The domestic level of output will increase and there will be a trade surplus.

17. For the Marshall-Lerner condition to hold a(n) ...

1. depreciation must eventually lead to an increase in exports and an improvement in the trade balance.
2. appreciation must eventually lead to an increase in exports and an improvement in the trade balance.
3. depreciation must eventually lead to an increase in imports and deterioration in the trade balance.
4. appreciation must eventually lead to an increase in imports and an improvement in the trade balance.

Use the following diagrams to answer questions 18 and 19:



18. Which one of the following statements is correct?

The chain of events in the case of an increase in exports is as follows:

1. $X \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow \rightarrow IM \uparrow \rightarrow NX \downarrow$
2. $X \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow \rightarrow IM \downarrow \rightarrow NX \uparrow$
3. $X \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow \rightarrow IM \uparrow \rightarrow NX \uparrow$
4. $X \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow \rightarrow IM \downarrow \rightarrow NX \uparrow$

19. Which one of the following statements is correct?

The chain of events in the case of an increase in government spending is as follows:

1. $G \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow \rightarrow IM \uparrow \rightarrow X \uparrow \rightarrow NX \downarrow$
2. $G \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow \rightarrow IM \uparrow \rightarrow X \uparrow \rightarrow NX \uparrow$
3. $G \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow \rightarrow IM \uparrow \rightarrow NX \downarrow$
4. $G \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow \rightarrow IM \downarrow \rightarrow NX \uparrow$

20. The impact of a change of the nominal exchange rate on the demand for goods and the level of output in the goods market in an open economy can be illustrated by the following chain of events:

1. $i \uparrow \rightarrow E \downarrow \rightarrow X \uparrow \rightarrow NX \downarrow$
2. $i \uparrow \rightarrow E \uparrow \rightarrow X \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$
3. $E \downarrow \rightarrow X \downarrow \rightarrow NX \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$
4. $E \downarrow \rightarrow X \uparrow \rightarrow NX \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$

21. In the IS-LM model for an open economy, a downward movement along the IS curve implies:

1. A decrease in the interest rate, an appreciation of the exchange rate and a decrease in exports.
2. An increase in both government spending and the demand for goods.
3. A decrease in the interest rate, a depreciation of the exchange rate and an increase in exports.
4. A decrease in the interest rate, a depreciation of the exchange rate and a decrease in imports.
5. An increase in the money supply, a decrease in the interest rate and an increase in investment.

22. According to the interest-parity relation...

1. a higher domestic interest rate leads to a depreciation of the nominal exchange rate.
2. a higher domestic interest rate leads to an appreciation of the nominal exchange rate.
3. the domestic interest rate has no impact on the nominal exchange rate.
4. a depreciation of the nominal exchange rate leads to a lower domestic interest rate.
5. an appreciation of the nominal exchange rate leads to a higher domestic interest rate.

23. If the interest rate increases in SA relative to the interest rate in the rest of the world, *ceteris paribus*, it leads to a(n) ...

- a. appreciation of the rand.
- b. depreciation of the rand.
- c. inflow of funds into SA.
- d. outflow of funds out of SA.

1. a and d
2. b and c
3. b and d
4. a and c
5. Only a

24. Which one of the following chain of events indicates the impact of a depreciation of the nominal exchange rate on the demand for goods and the level of output and income in the goods market for an open economy?

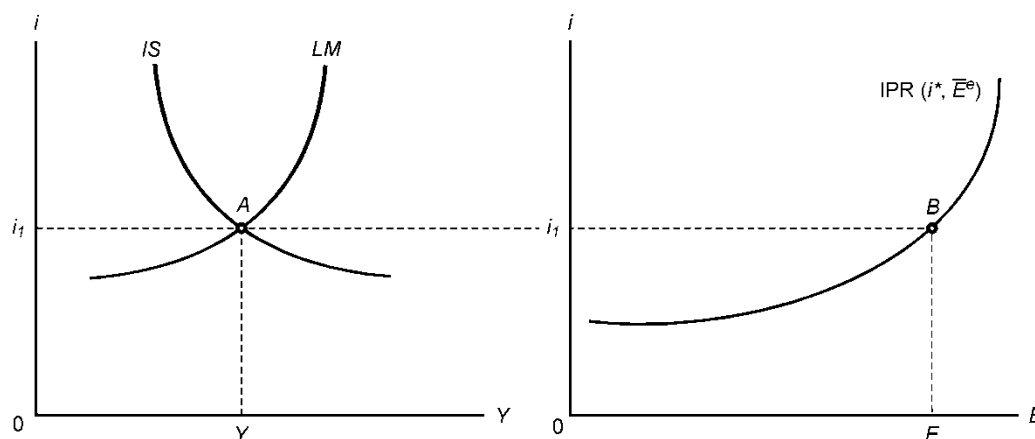
1. $i \downarrow \rightarrow I \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$
2. $i \downarrow \rightarrow E \downarrow \rightarrow X \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$
3. $Y \uparrow \rightarrow M^d \uparrow \rightarrow i \uparrow$
4. $E \downarrow \rightarrow X \uparrow \rightarrow NX \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$
5. $E \uparrow \rightarrow X \downarrow \rightarrow NX \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$

25. A country that takes the following policy actions will cause net exports to worsen.

- a. Expansionary fiscal policy.
- b. Expansionary monetary policy.
- c. Contractionary fiscal policy.
- d. Contractionary monetary policy.

1. a and b
2. b and c
3. c and d
4. a and d
5. Only a

Questions 26, 27 and 28 are based on the following diagram of an IS-LM model for an open economy.



26. An expansionary monetary policy causes:

1. A capital inflow, an appreciation of the exchange rate and a deterioration of the trade balance.
2. A capital outflow, a depreciation of the exchange rate and an improvement of the trade balance.
3. A capital outflow, a depreciation of the exchange rate and a deterioration of the trade balance.
4. A capital inflow, a depreciation of the exchange rate and an improvement of the trade balance.

27. A decrease in the money supply causes:
1. A capital inflow, an increase in the demand for rands, an appreciation of the exchange rate and a deterioration of the trade balance.
 2. A capital outflow, a decrease in the demand for rands, a depreciation of the exchange rate and an improvement of the trade balance.
 3. A capital outflow, an increase in the demand for rands, an appreciation of the exchange rate and an improvement of the trade balance.
 4. A capital inflow, a decrease in the demand for rands, a depreciation of the exchange rate and an improvement of the trade balance.
28. A decrease in government spending causes:
1. A capital inflow, an increase in the demand for rands, an appreciation of the exchange rate and a deterioration of the trade balance.
 2. A capital outflow, an increase in the demand for rands, a depreciation of the exchange rate and a deterioration of the trade balance.
 3. A capital inflow, a decrease in the demand for rands, a depreciation of the exchange rate and an improvement of the trade balance.
 4. A capital outflow, a decrease in the demand for rands, a depreciation of the exchange rate and an improvement of the trade balance.
29. The following question refers to an IS-LM model in an open economy.
- Which of the following statements are correct regarding the impact of a contractionary fiscal policy in an open economy?
- a. On the goods market the demand for goods decreases and the level of output and income declines.
 - b. The LM curve will shift upwards.
 - c. On the financial market the interest rate declines since the demand for money is lower.
 - d. The lower domestic interest rate relative to the interest rate in the rest of the world lead to a capital outflow, a decrease in the demand for the rand and a depreciation of the currency.
 - e. The trade balance improves since imports are lower and exports are higher.
1. a, b, c, d and e
 2. Only b and c
 3. Only a and d
 4. Only a, d and e
 5. Only a, c, d and e
30. Which of the following is a plausible explanation for an increase in the current account deficit on the balance of payments of South Africa?
- a. A decline in exports might be due to a decline in the economic growth rate of our major trading partners.
 - b. An increase in imports might be due to an increase in economic growth in South Africa.
 - c. A higher interest rate in South Africa relative to the rest of the world might have caused an appreciation of the exchange rate.

1. a, b and c
2. Only a and c
3. Only a and b
4. Only b and c
5. Not a, b or c

31. Which of the following statements is/are correct?

- a. An increase in the money supply will shift the IS curve to the right and leads to an improvement in the trade balance.
- b. An increase in the money supply will shift the LM curve downwards and leads to deterioration in the trade balance.
- c. An increase in government spending will shift the IS curve to the right and leads to an appreciation of the nominal exchange rate.
- d. Expansionary fiscal policy will lead to an improvement in the trade balance.
- e. Expansionary monetary policy will lead to an improvement in the trade balance.

1. b, c, d and e
2. Only c and e
3. a, b and d
4. a, c and e
5. Not option 1, 2, 3 or 4

Questions 32 to 34 are based on the following comparison between the impact of a contractionary fiscal policy with a contractionary monetary policy in the IS-LM model for an open economy:

	Contractionary fiscal policy	Contractionary monetary policy
Exchange rate	Depreciate	Appreciate
Capital flows	Outflow	Inflow
Exports	Higher	Lower
Trade balance	Improves	Worsens

32. The reason for the depreciation of the exchange rate for a contractionary fiscal policy is because of the _____ while for a contractionary monetary policy the exchange rate appreciates because of the _____.

1. increase in the domestic interest rate relative to the world interest rate; increase in the domestic interest rate relative to the world interest rate
2. decrease in the domestic interest rate relative to the world interest rate; decrease in the domestic interest rate relative to the world interest rate
3. increase in the domestic interest rate relative to the world interest rate; decrease in the domestic interest rate relative to the world interest rate
4. decrease in the domestic interest rate relative to the world interest rate; increase in the domestic interest rate relative to the world interest rate

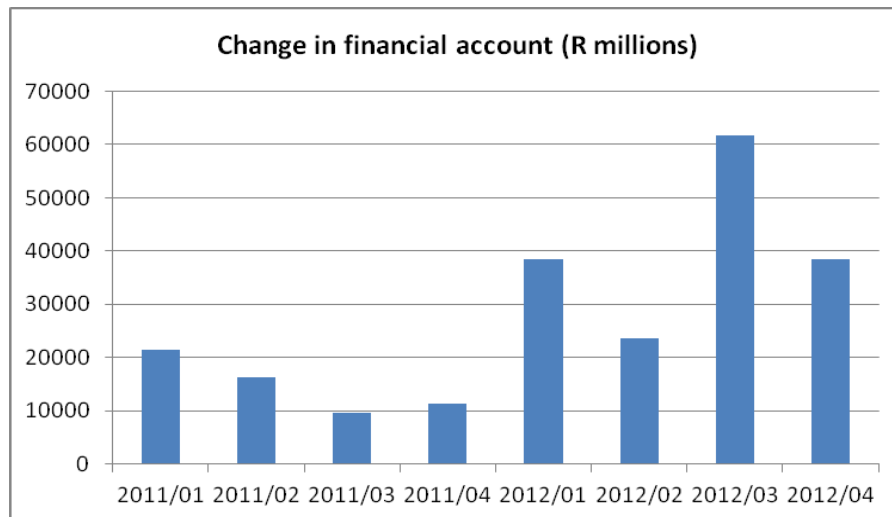
33. The reason for the capital outflow for a contractionary fiscal policy is because of the _____ while for contractionary monetary policy there is a capital inflow because of the _____.

- | | |
|-----------------------------------|-------------------------------|
| 1. increase in the interest rate; | decrease in the interest rate |
| 2. decrease in the interest rate; | increase in the interest rate |
| 3. increase in the interest rate; | increase in the interest rate |
| 4. decrease in the interest rate; | decrease in the interest rate |

34. The reason for higher exports in the case of a contractionary fiscal policy is because of the _____ while for monetary policy exports are lower since _____.

- | | |
|---------------------------------------|-------------------------------|
| 1. depreciation of the exchange rate; | the exchange rate appreciates |
| 2. appreciation of the exchange rate; | the exchange rate depreciates |
| 3. appreciation of the exchange rate; | the exchange rate appreciates |
| 4. depreciation of the exchange rate; | the exchange rate depreciates |

Question 35 is based on the following diagram. The diagram shows the change in the financial account of the balance of payments for South Africa:



35. Using the IS-LM model for an open economy which of the following is a plausible explanation for the change in the financial account of the balance of payments?

- The decline in the exports might be due to a decline in the economic growth rate of our major trading partners and the increase in imports might be due to an increase in economic growth in South Africa.
 - A higher interest rate in South Africa relative to the rest of the world might have caused an inflow of capital.
 - An appreciation of the exchange rate might have caused a lower demand for rands.
- Only a
 - a and c
 - a and b
 - b and c
 - Only b

SEMESTER 1

ASSIGNMENT 05

LEARNING UNITS 8 AND 9

CASE STUDIES ON LEARNING UNITS 5 TO 9

SELF-ASSESSMENT ASSIGNMENT

DO NOT SUBMIT THIS ASSIGNMENT

NOTE: Do not submit your answers. Assess or mark your answers once you have received Tutorial Letter 204.

The Labour Market

1. In our analysis of the labour market we assume the following:
 - a. Labour is the only factor of production used in the production of output.
 - b. Labour productivity is constant.
 - c. The price of oil and other raw material stays constant.
 - d. The price of products set by firms is based on cost plus a mark-up.
 1. a, b, c and d
 2. Only a, b and d
 3. Only b, c and d
 4. Only a and b
 5. Only c and d

2. Our analysis of the labour market implies the following:
 - a. There is a negative relation between the targeted real wage and the unemployment rate.
 - b. The higher the unemployment rate, the weaker the workers' position in bargaining.
 - c. The higher the unemployment rate, the lower the targeted real wage.
 - d. An improvement in the bargaining position of workers' makes it possible to bargain for higher wages.
 1. a, b, c and d
 2. Only a, b and c
 3. Only a, c and d
 4. Only b, c and e
 5. Only b and d

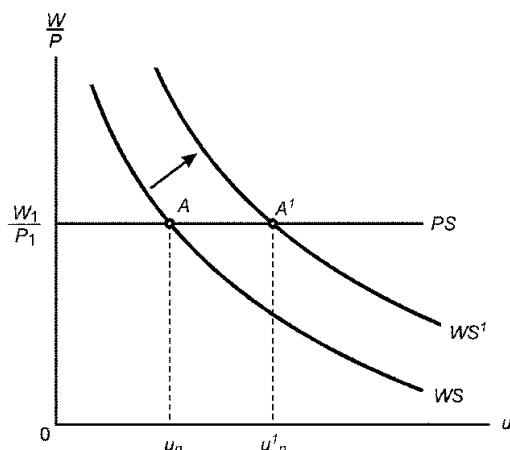
3. Which of the following factors will increase the bargaining position of workers?
 - a. The more expensive it is to dismiss workers.
 - b. A higher level of output and a lower unemployment rate.
 - c. A lower level of output and a higher unemployment rate.
 - d. An increase in unemployment benefits.
 - e. Labour laws that protect workers from being dismissed.

1. Only factors a, d and e
 2. Only factors a, b and d
 3. Only factors b, d and e
 4. Only factors d and e
 5. Factors a, b, d and e
4. Which of the following statements are correct?
- a. Higher unemployment is associated with both a lower chance of finding a job and a higher chance of losing your job.
 - b. An increase in the nominal wage for a given general price level will decrease the real wage.
 - c. For a given nominal wage, an increase in the general price level will decrease the real wage.
 - d. The real wage is the quantity of goods and services that can be purchased with the nominal wage.
1. a, b, c and d
 2. Only b, c and d
 3. Only a, c and d
 4. Only b and d
 5. Only a and d
5. Institutional factors play an important role in the way wages are determined in a country. Which of the following are institutional factors that are common in most countries?
- a. Most workers are paid a high enough wage that they prefer being employed to being unemployed.
 - b. The lower the unemployment rate, the higher the wages.
 - c. Wages depend on labour market conditions.
 - d. The expected price level, the unemployment rate and institutional factors will influence the behaviour of workers when negotiating for wages.
1. a, b, c and d
 2. Only a, c and d
 3. Only b, c and d
 4. Only a, b and d
 5. Only a, b and c
6. Which one of the following, according to the wage-setting relationship, is **not** an institutional factor that may affect the outcome of wage setting?
1. Minimum wages.
 2. Unemployment benefits.
 3. Labour law protection.
 4. Unemployment rate.
 5. Collective bargaining.

7. Which of the following statements are correct?
- Workers are able to determine the real wage through nominal wage bargaining.
 - Through an increase in their nominal wages workers are able to increase their real wages.
 - An increase in the mark-up by firms causes a decrease in real wages.
 - A positive relationship exists between the mark-up and the price per unit.
- a, b, c and d
 - Only a, c and d
 - Only b, c and d
 - Only a and d
 - Only c and d
8. Which of the following influences price-setting by firms in an imperfectly competitive market?
- The nature of the production function.
 - The relation between the inputs used in production and the quantity of output produced.
 - The prices of the inputs.
 - The nominal wage per unit of output.
 - The mark-up of the firm.
- Only a, b, d and e
 - Only b, c and d
 - Only a, c, d and e
 - a, b, c, d and e
 - Only c and e
9. Which of the following statements are correct?
- The price level in the economy is partly the outcome of nominal wage bargaining and the price setting behaviour of firms in the economy.
 - An increase in the nominal wage is enough to ensure an increase in the real wage.
 - A decrease in the mark-up by firms causes an increase in feasible real wages.
 - The PS curve will shift upwards if the mark-up by firms decreases.
- a, b, c and d
 - Only c and d
 - Only a, c and d
 - Only b, c and d
 - Only a and d
10. Which of the following statements are correct?
- A positive relationship exists between the ...
- expected price level and the bargained nominal wage.
 - unemployment rate and the bargained nominal wage.
 - mark-up and the price per unit.
 - nominal wage and the price per unit.
 - better unemployment benefits and the nominal wage.

1. a, b, c, d and e
2. Only b, c and d
3. Only c, d and e
4. Only a, c, d and e
5. Only a, c and d

Question 11 is based on the following diagram:



11. Which factors will shift the WS curve to WS^1 ?

- a. A higher unemployment rate.
- b. A higher level of output.
- c. An increase in unemployment benefits.
- d. Labour laws that protect workers from being dismissed.
- e. A better bargaining position of workers.

1. b, c, d and e
2. a, b, d and e
3. Only c, d and e
4. Only a and b
5. a, c, d and e

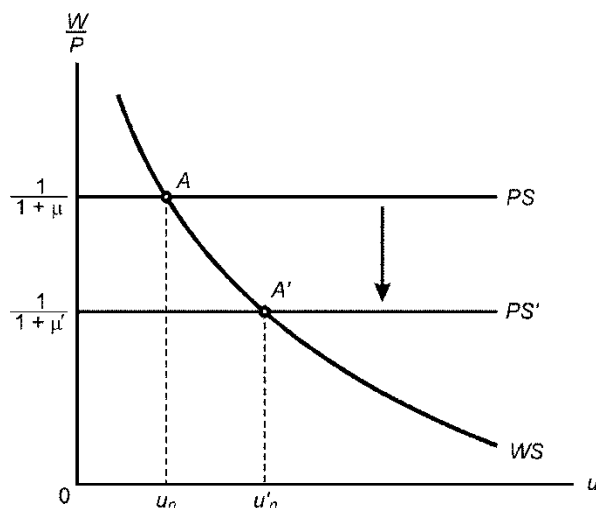
12. Which of the following statements is/are correct?

The WS curve will shift down because of ...

- a. a lower mark-up.
- b. a lower unemployment rate.
- c. lower nominal wages.
- d. labour laws that provide workers with less protection against layoffs.
- e. better unemployment benefits.

1. a and c
2. b and d
3. Only b
4. Only c
5. Only d

Question 13 is based on the following diagram:



13. The diagram illustrates a(n)...

- higher mark-up.
- lower mark-up.
- decrease in the price determined real wage accompanied by an increase in the natural rate of unemployment.
- increase in the workers' bargaining position.
- increase in the actual price level.

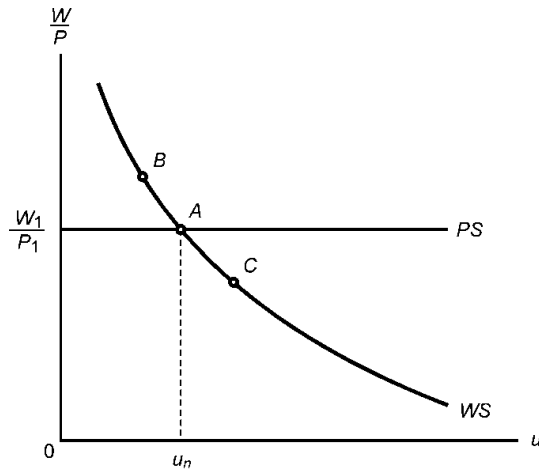
- Only a and c
- b and c
- a, d and e
- a, c and e
- b, d and e

14. The PS curve will shift downwards because of a ...

- lower mark-up.
- higher mark-up.
- lower unemployment rate.
- higher unemployment rate.

- a and c
- a and d
- b and c
- b and d
- Only b

Question 15 is based on the following wage-setting and price-setting relationships:



15. Which of the following statements is/are correct?

At point C the ...

- unemployment rate is higher which decreases the bargaining position of workers and the nominal wage they can bargain for decreases.
- unemployment rate is lower which increases the bargaining position of workers and the real wage implied by price setting increases.
- targeted real wage is lower than the implied real wage.
- targeted real wage is higher than the implied real wage.

- b, c and d
- a, b and c
- Only a and c
- Only b and c
- Only a

16. A decrease in the level of output will cause the following events on the labour market:

- The level of unemployment decreases causing an increase in the bargaining position of workers which enables them to bargain for a nominal wage increase.
- The level of unemployment increases which causes a decline in the bargaining position of workers resulting in a lower bargained nominal wage.
- The natural level of unemployment decreases causing an increase in the bargained real wage.
- The natural level of unemployment increases causing a decrease in the bargained real wage.

17. Which one of the following chain of events describes the impact of an increase in output on the labour market?

- $Y \uparrow \rightarrow u \uparrow \rightarrow N \downarrow \rightarrow W \uparrow$
- $Y \uparrow \rightarrow N \uparrow \rightarrow u_n \downarrow \rightarrow W \uparrow$
- $Y \uparrow \rightarrow N \uparrow \rightarrow u \downarrow \rightarrow W \uparrow$
- $Y \downarrow \rightarrow N \downarrow \rightarrow u \uparrow \rightarrow W \downarrow$
- $W \uparrow \rightarrow N \downarrow \rightarrow u \uparrow$

AS-AD model

18. Which of the following events is/are represented by the AS curve?

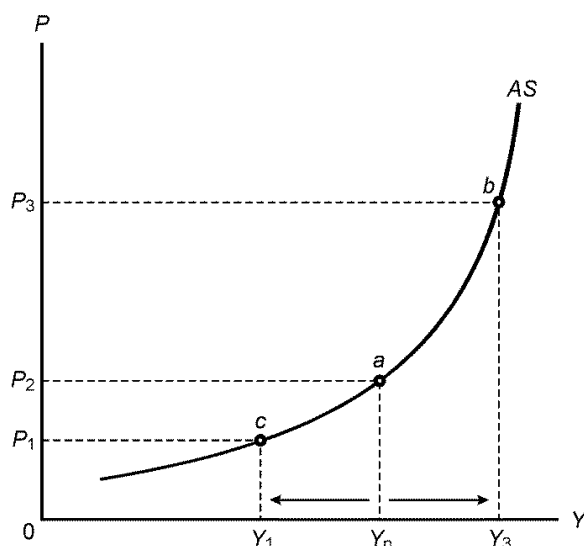
- $Y \uparrow \rightarrow u \uparrow \rightarrow N \downarrow \rightarrow W \uparrow \rightarrow P \downarrow$
- $Y \uparrow \rightarrow N \uparrow \rightarrow u_n \downarrow \rightarrow W \uparrow \rightarrow P \downarrow$
- $Y \downarrow \rightarrow N \downarrow \rightarrow u \uparrow \rightarrow W \downarrow \rightarrow P \downarrow$
- $Y \downarrow \rightarrow u \downarrow \rightarrow N \uparrow \rightarrow W \downarrow \rightarrow P \uparrow$
- $W \uparrow \rightarrow N \downarrow \rightarrow u \uparrow \rightarrow P \uparrow$

- Only a
- Only b
- Only c
- Only d
- b and c

19. The AS curve has a positive slope because of which the following chain of events?

- $Y \uparrow \rightarrow u \uparrow \rightarrow N \downarrow \rightarrow W \uparrow \rightarrow P \downarrow$
- $Y \uparrow \rightarrow N \uparrow \rightarrow u_n \downarrow \rightarrow W \uparrow \rightarrow P \uparrow$
- $W \uparrow \rightarrow N \downarrow \rightarrow u \uparrow \rightarrow P \uparrow$
- $Y \downarrow \rightarrow u \downarrow \rightarrow N \uparrow \rightarrow W \downarrow \rightarrow P \uparrow$
- $Y \uparrow \rightarrow N \uparrow \rightarrow u \downarrow \rightarrow W \uparrow \rightarrow P \uparrow$

Question 20 is based on the following diagram.

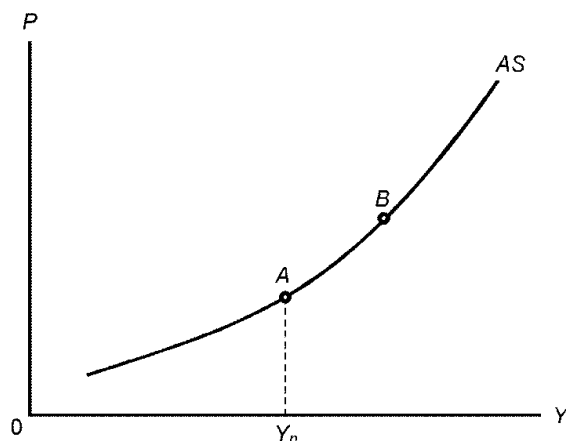


20. Which of the following statements are correct?

- At point c the actual price level is lower than the expected price level.
- At point b the output level is higher than the natural level of output.
- The real wage is the same at point a and point b .
- As the level of output increases the price level rises.
- The AS curve will shift up when the expected price level increases.

1. a, b, c, d and e
2. Only a, b, d and e
3. Only b, c, d and e
4. Only a, d and e
5. Only a, b, c and d

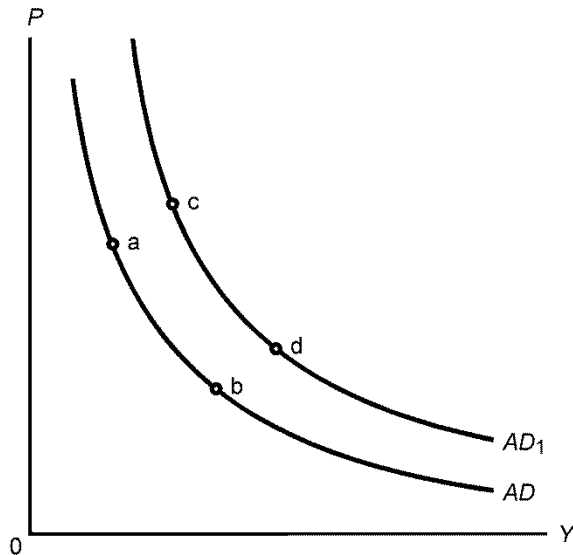
Questions 21 and 22 are based on the following AS curve:



21. At point B compared to point A the expected price level is ...
 1. lower than the actual price level.
 2. higher than the actual price level.
 3. the same as the actual price level.
22. Which one of the following events describes the adjustment from the short to the medium to long run if the economy is at point B?
 1. The expected price level is lower than the actual price level. Workers respond to this by increasing their nominal wage demands and the AS curve shifts down.
 2. The expected price level is higher than the actual price level. Workers respond to this by increasing their nominal wage demands and the AS curve shifts up.
 3. The expected price level is lower than the actual price level. Workers respond to this by increasing their nominal wage demands and the AS curve shifts up.
 4. The expected price level is higher than the actual price level. Workers respond to this by increasing their nominal wage demands and the AS curve shifts down.
23. Which of the following factors will cause an upwards shift of the AS curve?
 - a. An increase in real wages.
 - b. An increase in the expected price level.
 - c. An increase in the actual price level.
 - d. A decrease in the nominal money supply.
 - e. A decrease in government spending.
 1. Only factor b
 2. Factors a and b
 3. Factors c, d and e
 4. Factors b, d and e
 5. Only factor c

24. Which one of the following applies when the aggregate demand curve (AD-curve) is derived?
1. A decrease in the nominal money supply causes an increase in the interest rate which in return causes a decrease in investment spending, the demand for goods and the level of output.
 2. A decrease in the price level decreases the real money supply which causes an increase in the interest rate which in return causes a decrease in investment spending, the demand for goods and the level of output.
 3. An increase in the price level decreases the real money supply which causes an increase in the interest rate which in return causes a decrease in investment spending, the demand for goods and the level of output.
 4. An increase in government spending causes an increase in the interest rate which in return causes a decrease in investment spending, the demand for goods and the level of output.
25. Which of the following events is represented by the AD curve?
- a. $P \downarrow \rightarrow M/P \uparrow \rightarrow i \downarrow \rightarrow I \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$
 - b. $M^s \downarrow \rightarrow M/P \downarrow \rightarrow i \uparrow \rightarrow I \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$
 - c. $M^s \uparrow \rightarrow M/P \uparrow \rightarrow i \downarrow \rightarrow I \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$
 - d. $P \uparrow \rightarrow M/P \downarrow \rightarrow i \uparrow \rightarrow I \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$
1. Only a
 2. Only b
 3. Only c
 4. Only d
 5. a and d
26. Which of the following factors cause a shift in the AD curve?
- a. A change in wages.
 - b. A change in the price level.
 - c. A change in the nominal money supply.
 - d. A change in government spending.
1. Factors a, b and c
 2. Only factors b and d
 3. Only factors a and c
 4. Factors b, c and d
 5. Only factors c and d

Questions 27 and 28 are based on the following diagram:



27. Which of the following statements is/are correct?

Comparing point a with point b on curve AD the ...

- a. real money supply is higher at point b.
- b. interest rate is lower at point b.
- c. investment spending is higher at point b.
- d. government spending is higher at point b.
- e. demand for goods is higher at point b.

- 1. a, b, c, d and e
- 2. Only a, b, c and e
- 3. Only b, c and d
- 4. Only b, c and e
- 5. Not one of the options 1 to 4

28. Which of the following statements are correct?

Assume that the rightward shift of the AD is due to an expansionary fiscal policy. Comparing point b on curve AD with point d on curve AD_1 the ...

- a. level of government spending is higher at point d.
- b. level of taxation is higher at point d.
- c. demand for goods is higher at point d.
- d. interest rate is higher at point d.
- e. nominal money supply is higher at point d.

- 1. a, b, c and d
- 2. a, c and e
- 3. Only b, c and d
- 4. Only a, c and d
- 5. b and e

29. Which one of the following events describes the adjustment from the short to the medium to long run in the case of an expansionary monetary policy?

	Labour market	Financial market	Goods market
1.	$P^e < P: W \uparrow \rightarrow P \uparrow$	$M^s \downarrow \rightarrow M/P \downarrow \rightarrow i \uparrow$	$I \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$
2.	$P^e < P: W \downarrow \rightarrow P \downarrow$	$M/P \downarrow \rightarrow i \uparrow$	$I \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$
3.	$P^e > P: W \downarrow \rightarrow P \downarrow$	$M/P \uparrow \rightarrow i \downarrow$	$I \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$
4.	$P^e > P: W \uparrow \rightarrow P \uparrow$	$M/P \uparrow \rightarrow i \uparrow$	$I \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$
5.	$P^e < P: W \uparrow \rightarrow P \uparrow$	$M/P \downarrow \rightarrow i \uparrow$	$I \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$

30. Which one of the following events applies in the medium to long run in the case of an expansionary monetary policy in the labour market?

1. $P^e > P: W \uparrow \rightarrow P \downarrow$
2. $P^e < P: W \uparrow \rightarrow P \uparrow$
3. $P^e < P: W \downarrow \rightarrow P \downarrow$
4. $P^e > P: W \downarrow \rightarrow P \downarrow$
5. $P^e > P: W \uparrow \rightarrow P \uparrow$

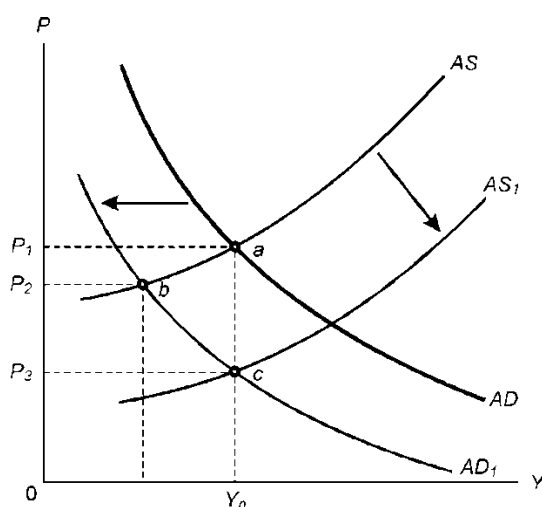
31. Which one of the following events applies in the medium to long run in the case of an expansionary monetary policy in the financial market?

1. $M/P \uparrow \rightarrow i \uparrow$
2. $M^s \downarrow \rightarrow M/P \downarrow \rightarrow i \uparrow$
3. $M/P \downarrow \rightarrow i \uparrow$
4. $M/P \uparrow \rightarrow i \downarrow$
5. $M/P \downarrow \rightarrow i \downarrow$

32. Which one of the following events applies in the medium to long run in the case of an expansionary monetary policy in the goods market?

1. $I \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$
2. $I \uparrow \rightarrow Z \downarrow \rightarrow Y \downarrow$
3. $I \uparrow \rightarrow Z \downarrow \rightarrow Y \uparrow$
4. $I \uparrow \rightarrow Z \uparrow \rightarrow Y \downarrow$
5. $I \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$

Question 33 is based on the following diagram which represents the impact of a contractionary fiscal policy:



33. Which of the following statements is/are correct?

- In the short run: the increase in the interest rate in the financial market will lead to a decrease in investment in the goods market, a decrease in the demand for goods and a decrease in the level of output and income. This is represented by a shift from AD to AD_1 .
- The movement along the AD curve from point b to point c is the result of the events in the labour market in the short run.
- In the medium run, the AS curve will shift from AS to AS_1 because of the following chain of events: $P^e \downarrow \rightarrow W \downarrow \rightarrow P \downarrow$.
- At point c the level of output is at the natural level of output and all the real values are equal to their original values.

- a, b, c and d
- Only b, c and d
- Only b, c, d and e
- Only c and d
- Only c

Case studies on learning units 5 to 7

Question 1

Question 1 is based on the following extract from the *Monetary Policy Review* June 2015. South African Reserve Bank. (2015). Pretoria:

"... monetary policy in South Africa remains in a tightening cycle... policy easing by the European Central Bank (ECB) and the Bank of Japan may support capital flows to emerging markets, further moderating the risk of an abrupt decline in emerging-market (EM) currency prices"

Which one of the following chain of events' illustrates the effect of the above extract on South Africa's trade balance.

1. $M \uparrow \rightarrow M/P \uparrow \rightarrow i \downarrow \rightarrow E \downarrow \rightarrow X \uparrow \rightarrow NX \uparrow$
2. $E \uparrow \rightarrow i \uparrow \rightarrow X \uparrow \rightarrow NX \uparrow$
3. $i \uparrow \rightarrow \text{Capital}_{\text{inflow}} \rightarrow E \uparrow \rightarrow X \downarrow \rightarrow NX \downarrow$
4. $i \downarrow \rightarrow \text{Capital}_{\text{outflow}} \rightarrow E \downarrow \rightarrow X \uparrow \rightarrow NX \uparrow$

Question 2

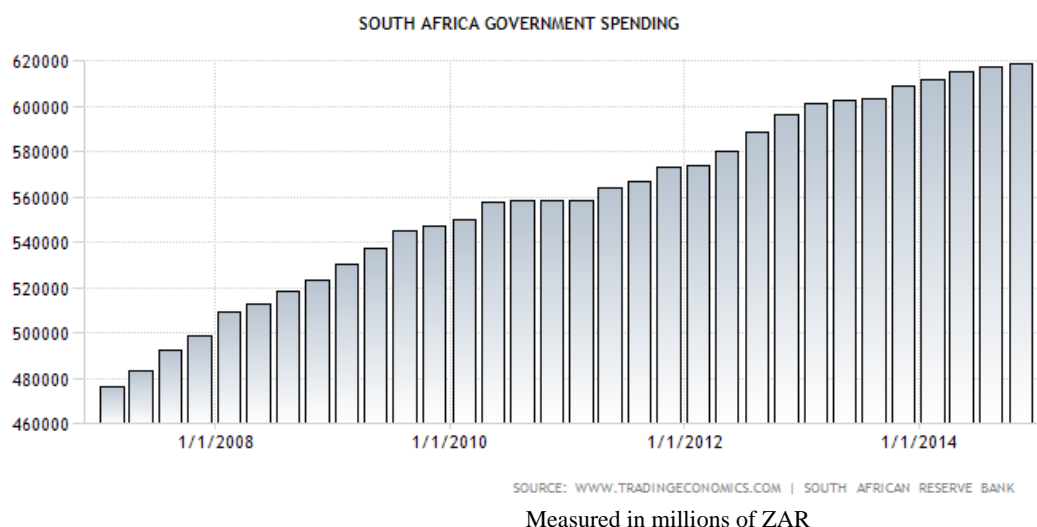
The following statements are based on information released in the SARBs *Monetary Policy Review* June 2015. Identify which of these statements will have a **positive** effect on South Africa's current account of the balance of payments:

2.
 - a. China's growth has slowed.
 - b. The price of iron ore has fallen by 65% from 2011 to the first quarter of 2015.
 - c. Sustained depreciation of the rand.
 - d. A reduction in OPECs monopoly power has seen a decline in the price of crude oil.
 - e. The non-tradable sector has expanded faster relative to the tradable sector. The tradable sector consists of those businesses that compete with foreign producers either domestically (import substitution) or abroad (exporting).
1. a, b, c, d and e
 2. Only a, b and d
 3. Only b and d
 4. Only c and d
 5. Only c and e

Case studies on learning units 8 and 9

Question 1

Question 1 is based on the following graph:



- a. Which stabilisation policy is represented by the data?
- b. Given the data and policy, what will happen in the AS-AD model? Explain in words and by using a chain of events and a diagram what will happen in the short run and in the medium run in the goods market, the financial market and the labour market.

Question 2

Read through the following and answer questions a and b that follow.

In 1999, the South African economy embarked on its longest expansion phase. It lasted for 99 months and come to an end in November 2007 and in the fourth quarter of 2008 the South African economy experienced an economic recession. (See figure 2).

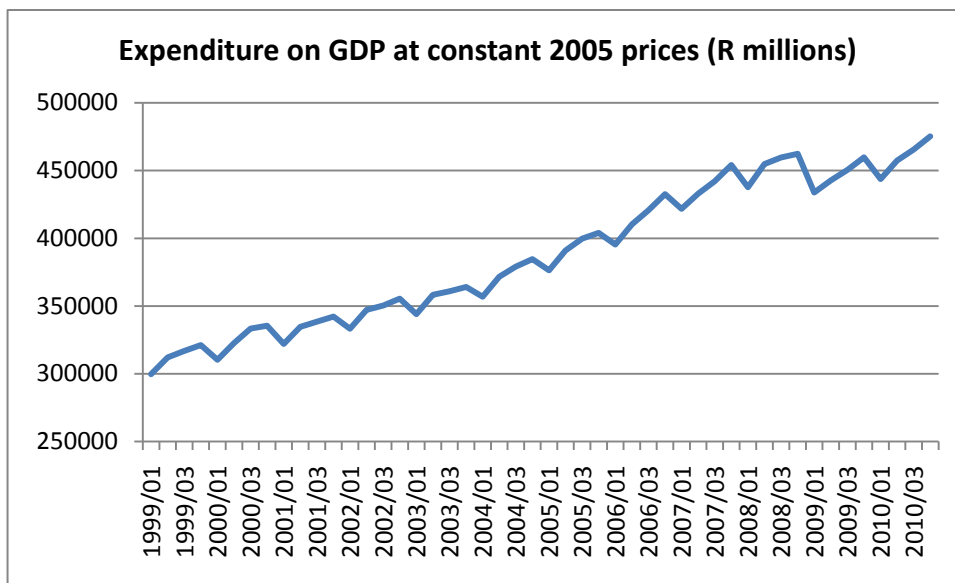


Figure 1

What triggered the end of the expansion phase and the economic recession in South Africa was falling house prices in the United States of America which led to the so-called “subprime mortgage” crisis. Preceding the crisis there was a rapid increase in mortgages to less creditworthy borrowers in America. A combination of falling house prices and default mortgage payments led to the failure and near failure of major financial institutions in America. This sent shockwaves across the financial markets of the world and resulted in a loss of confidence in financial markets and institutions, with the result that share prices fell sharply, investor confidence plunged and the availability of credit to firms and households were severely curtailed. This had the result that consumption spending by households and investment spending by firms declined worldwide which had a major impact on the level of output and income in the major economies of the world. Today this is referred to as the Great Recession.

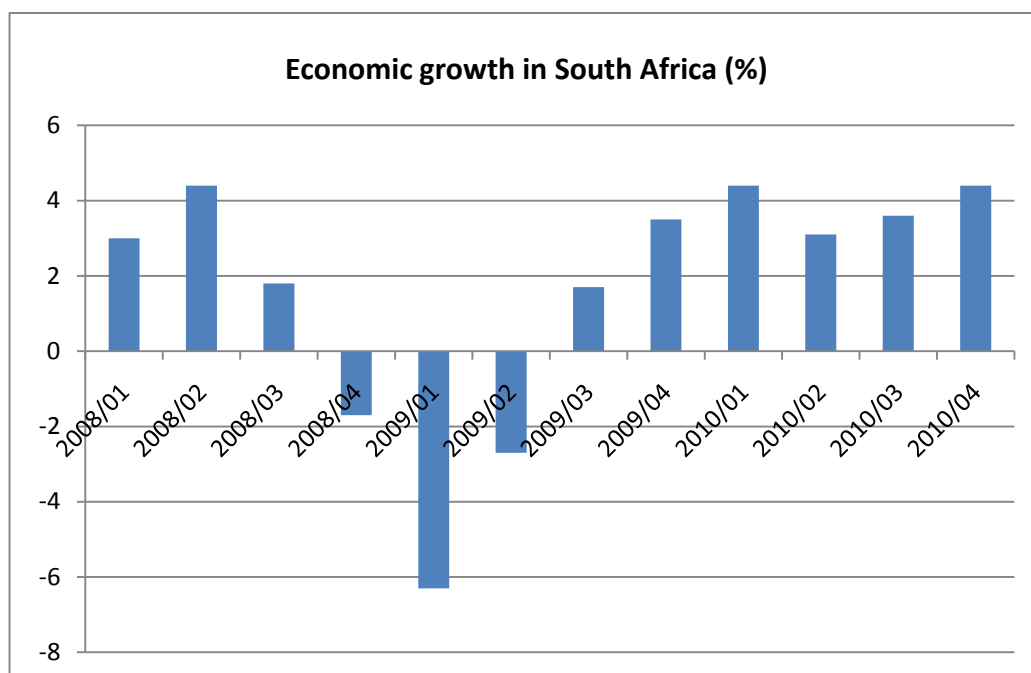


Figure 2

Due to the recession experienced by the major trading partners of South Africa there was a dramatic drop in our exports. In 2009 exports declined by 20% as shown in figure 3. The impact on the economy was worsened by a decline of both consumption spending and investment spending.

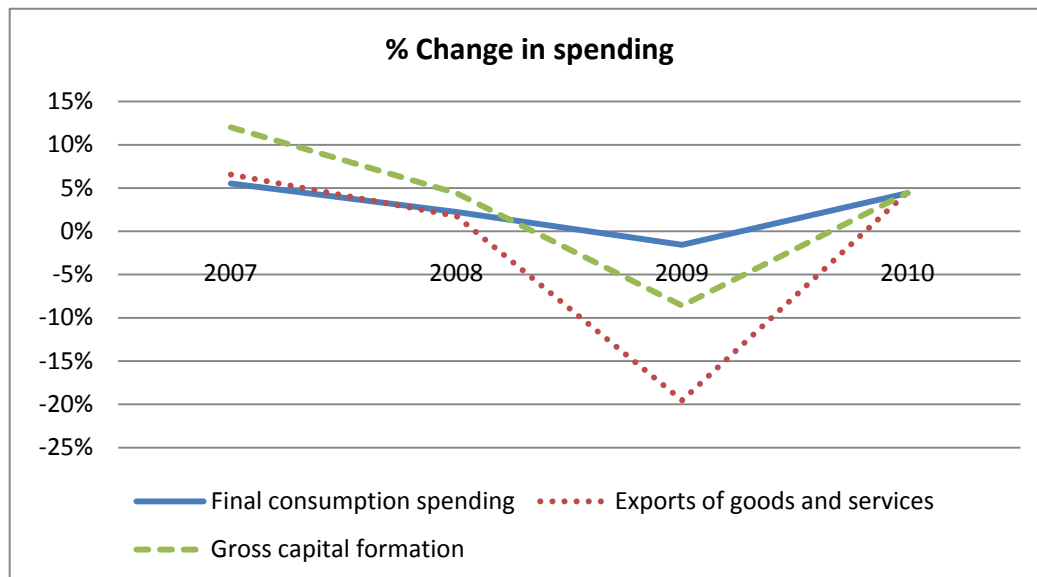


Figure 3

The recession could have been much worse. But it was met by a strong macroeconomic response, which certainly limited the depth and the length of the recession.

Take monetary policy first. In response to the economic slowdown the South African Reserve Bank started to decrease the repurchase rate. (Figure 4 shows the decline in the repurchase rate for the period 2008 to 2009.) In April 2008 the repurchase rate was 11.5% while at the end of 2009 it was 7%.

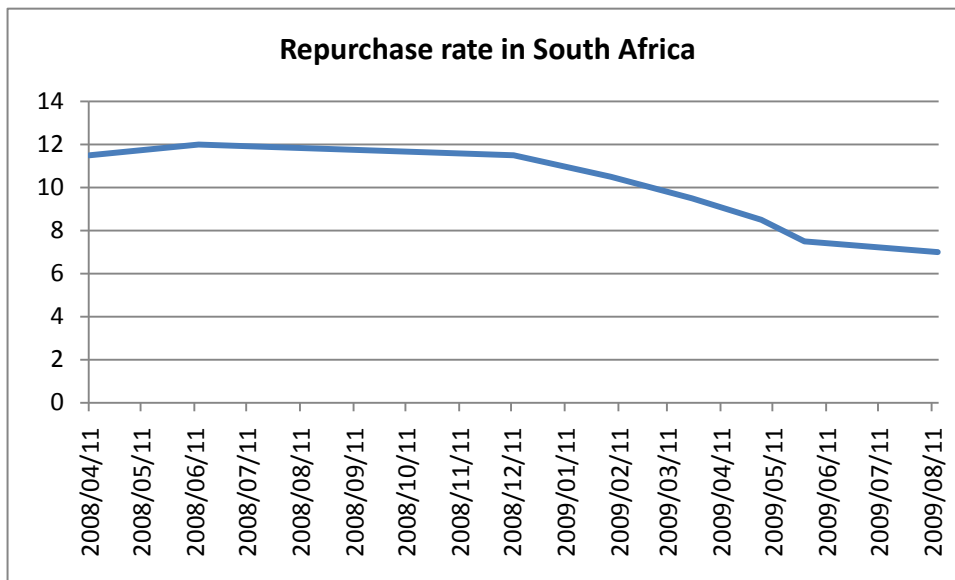


Figure 4

- a. Define the repurchase (repo) rate. Briefly explain the impact of a decrease in the repo rate on the money supply? Does it refer to a contractionary or expansionary monetary policy?
- b. Given the data and policy, what will happen in the AS-AD model? Explain in words and by using chain of events and a diagram what will happen in the short and medium run in the goods market, the financial market and the labour market.

Question 3

When comparing the impact of the two different policies (question 1 and question 2 above) in the AS-AD model, the impact in the medium run is different. Briefly explain why.

SECOND SEMESTER ASSIGNMENTS

<p style="text-align: center;">SEMESTER 2</p> <p style="text-align: center;">COMPULSORY ASSIGNMENT 01</p> <p style="text-align: center;">LEARNING UNITS 1 TO 3</p> <p style="text-align: center;">DUE DATE: 2016/08/22</p> <p style="text-align: center;">UNIQUE NUMBER: 850512</p>
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This assignment contributes 20% towards your semester mark.

Please ensure that this assignment reaches the university before the due date.

Answer all questions on a mark-reading sheet.

1. Which of the following statements is/are correct?
 - a. In this module we only study the demand side of the economy which includes the goods market and the financial market. The labour market forms part of supply side analysis and is therefore excluded from this module.
 - b. The two most important accounts of the balance of payments are the current account and the financial account.
 - c. If total output increases with 3% during a specific year and the general price level increases with 5% the real GDP will decrease and the nominal GDP will increase.
 - d. Fiscal policy deals with government spending and taxes while monetary policy deals with money supply.
 1. a, b, c and d
 2. Only a, b and d
 3. Only b, c and d
 4. Only b and d
 5. None of the options 1 to 4

2. Consider the consumption functions of country A and country B.
 Country A: $C = 1\,500 + 0.6Y_D$
 Country B: $C = 1\,000 + 0.9Y_D$

Which of the following statements are correct?

- a. In country A autonomous consumption is higher than in country B.
- b. In country B induced consumption is definitely higher than in country A.
- c. In country B total consumption is definitely higher than in country A.
- d. In country A 60 cents out of each rand is spent by the consumers while in country B 90 cents out of each rand is spent.

1. a, b and d
 2. Only a and b
 3. a and c
 4. Only a and d
 5. b, c and d
3. Which of the following events chain(s) is/are correct regarding the goods market model?
- a. $Y \uparrow \rightarrow G \uparrow$
 - b. $Y \uparrow \rightarrow I \uparrow$
 - c. $Y \downarrow \rightarrow T \downarrow$
 - d. $Y \downarrow \rightarrow C \downarrow$
1. Only a
 2. Only b
 3. Only c
 4. Only d
 5. b and d
4. In the goods market model a decrease in taxes will result in ...
- a. an increase in autonomous consumption.
 - b. an increase in disposable income.
 - c. an increase in income.
 - d. an increase in induced consumption.
1. a, b and c
 2. a, b and d
 3. b, c and d
 4. a, c and d
 5. None of the options 1 to 4
5. Goods market equilibrium exists ...
- a. in a situation that will maintain if existing forces do not change.
 - b. only in a situation where the level of output and income is equal to the supply of goods.
 - c. in a situation where the money supply equals the demand for liquid balances.
 - d. where quantity demanded is equal to quantity supplied.
1. a and c
 2. Only a
 3. Only b
 4. Only c
 5. Only d

6. Which of the following statements is/are correct regarding the goods market model?
- An increase in autonomous consumption of 200 will cause an increase in output and income of 200.
 - An increase in investment of 500 will cause an increase in output and income of more than 500.
 - An increase in government spending of 800 will cause an increase in output and income of more than 800.
- a, b and c
 - Only a and b
 - Only a and c
 - Only b and c
 - None of the options 1 to 4
7. Assuming a multiplier of 20, which of the following statements is/are correct?
- An increase in government spending of R10 million and an increase in taxation of R10 million will increase output and income with R10 million and will result in an increase in the budget deficit of R9 million.
 - An increase in government spending of R20 million and an increase in taxation of R20 million will increase output and income with R20 million and will result in an increase in the budget deficit of R9 million.
 - An increase in government spending of R9 million and an increase in taxation of R9 million will increase output and income with R9 million and will not change the budget deficit.
- a, b and c
 - Only a and b
 - Only b and c
 - Only c
 - None of the options 1 to 4
8. Which of the following statements is/are correct?
- An increase in the marginal propensity to consume will cause an increase in the multiplier.
 - An increase in the marginal propensity to consume will cause an increase in aggregate demand.
 - An increase in the marginal propensity to consume will cause an increase in output and income.
 - If the tax revenue of government is larger than government spending, a budget deficit exists.
- a, b and c
 - a, b and d
 - b, c and d
 - a, c and d
 - None of the options 1 to 4

9. Which of the following chain of events' are correct in terms of the goods market model?

- a. $G \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow \rightarrow Y_D \uparrow \rightarrow C \uparrow$
- b. $I \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow \rightarrow Y_D \uparrow \rightarrow C \uparrow$
- c. $T \downarrow \rightarrow Z \uparrow \rightarrow Y \uparrow \rightarrow Y_D \uparrow \rightarrow C \uparrow$
- d. $C_0 \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow \rightarrow Y_D \uparrow \rightarrow C \uparrow$

- 1. Only a, b and c
- 2. Only a, b and d
- 3. Only b, c and d
- 4. Only a, c and d
- 5. a, b, c and d

Questions 10 to 20 are based on the following approximate figures for South Africa in 2014

Investment expenditure	= R408 000 million
Government expenditure	= R424 000 million
Real GDP	= R1 993 000 million
Estimated population	= 50 million
Labour force	= 20 million
Unemployment rate	= 25%
Budget deficit	= R179 000 million
Government debt	= R1 137 000 million
Marginal propensity to consume	= 0.33
Multiplier	= 1.5

10. Given the structural constraints of the South African economy the South African Reserve Bank and the World Bank estimated that the potential growth rate for South Africa is 3.5%. Given a real GDP for South Africa of R1 993 000 million in 2014 by how much should real GDP have to increase to achieve an economic growth rate of 3.5%?

- 1. R64 225 000 million.
- 2. R69 755 million.
- 3. R1 993 000 million.
- 4. R524 285 million
- 5. R64 225 million.

11. Assuming a multiplier of 1.5 by how much should autonomous spending in the South African economy increase to achieve a growth rate of 3.5%?

- 1. R64 225 million.
- 2. R69 755 million.
- 3. R46 503 million.
- 4. R42 817 million.
- 5. R1 993 000 million.

12. If this growth rate of 3.5% is to be achieved through an increase in government spending by how much should government spending increase?
1. R64 225 million.
 2. R69 755 million.
 3. R46 503 million.
 4. R42 817 million.
 5. R1 993 000 million.

Questions 13 to 16 are based on the following additional information:

Assuming that the tax revenue stays the same and government spending increases to achieve a 3.5% growth rate.

13. What impact will it have on the budget deficit?
1. It will increase the budget deficit by R46 503 million.
 2. It will increase the budget deficit by R69 755 million.
 3. It will increase the budget deficit by R42 817 million.
 4. It will decrease the budget deficit by R64 225 million.
 5. It will decrease the budget deficit by R42 817 million.
14. What is the percentage change in the budget deficit?
1. It will increase the budget deficit by 26%.
 2. It will increase the budget deficit by 30%.
 3. It will increase the budget deficit by 36%.
 4. It will decrease the budget deficit by 26%.
 5. It will decrease the budget deficit by 36%.
15. The government debt will...
1. be unchanged at R1 137 000 million.
 2. increase to R1 090 497 million.
 3. decline with R46 503 million.
 4. increase to R1 183 503 million.
16. If the 3.5% growth rate is to be achieved by a change in taxation what should happen to taxation?
1. Taxes should be cut by R69 755 million.
 2. Taxes should be cut by R46 503 million.
 3. Taxes should be cut by R140 918 million.
 4. Taxes should be increased by R69 755 million.
 5. Taxes should be increased by R46 503 million.

17. If the change in the budget deficit is unacceptable which other component of expenditure might cause an increase in output and income?
- Autonomous consumption expenditure.
 - Investment expenditure.
 - Imports.
- a, b and c
 - Only a and b
 - Only a and c
 - Only b and c
 - None of the options 1 to 4
18. How many people were unemployed in South Africa in 2014?
- 30 million.
 - 12.5 million.
 - 5 million.
 - 20 million.
19. Assuming that the output per worker is R122 000 and for every additional worker employed output will increase with R122 000 (in other words, constant returns apply). By how much will employment increase if the economy grows at 3.5%?
- 950 555
 - 350 787
 - 571 762
 - 526 434
20. Which of the following statements is/are correct?
- It is possible to solve the unemployment problem in South Africa through an increase in government spending and/or a decrease in taxation.
 - An increase in the growth rate of 3.5% is sufficient to decrease the number of unemployed people by 50%.
 - The only way to achieve a growth rate of 3.5% is through fiscal policy actions.
- a, b and c
 - Only a and b
 - Only a and c
 - Only b and c
 - Not statement a, b or c
21. Which of the following statements is/are correct?
- The demand for money consists of the demand for active and the demand for passive balances.
 - The demand for passive balances is a function of the interest rate. This is a negative relationship.
 - The demand for active balances is a function of income. This is a negative relationship.

1. a, b and c
2. Only a and b
3. Only a and c
4. Only b and c
5. Only b

22. Which of the following statements is/are correct?

- a. The balance on the cheque account, cash, bonds, shares and the value of his/her house and paintings form part of the financial wealth of an individual.
- b. The demand for money is a function of income and the interest rate.
- c. The supply of money is a function of income and fiscal policy.

1. a, b and c
2. Only a and b
3. Only a and c
4. Only b and c
5. Only a

23. Which of the following statements is/are correct?

- a. In the financial market an increase in income will increase the interest rate.
- b. Expansionary monetary policy will increase the supply of bonds and the price of bonds will decrease.
- c. Exogenously determined money supply implies that as the money supply increases the interest rate will also increase.

1. Not a, b or c
2. Only a
3. Only b
4. Only c
5. a and b

24. Which of the following statements is/are correct?

- a. An increase in income shifts the demand for money curve to the right.
- b. An increase in the interest rate is represented by an upward movement along the demand for money curve.
- c. The money supply is determined by the central bank and is represented by a horizontal line, because it is not a function of the interest rate.

1. Only a
2. a and b
3. a and c
4. b and c
5. Only b

25. Which of the following statements is/are correct regarding the financial market?
- There is a negative relationship between the price of a treasury bill and the interest rate.
 - There is an inverse relationship between the price of a treasury bill and the interest rate.
 - If the price of a treasury bill is R9 700 and the rate of return is 3%, the rate of return will be lower than 3% if the price of the treasury bill decreases to R9 600.
- a, b and c
 - Only a and b
 - Only a and c
 - Only b and c
 - Only a
26. Which of the following statements is/are correct in terms of the events chain: $Y \downarrow \rightarrow M^d \downarrow \rightarrow P_B \uparrow \rightarrow i \downarrow$?
- The events chain applies to the financial market.
 - The events chain illustrates the impact of a decrease in income on the goods market.
 - The events chain illustrates what happens to the interest rate if market participants sell more bonds.
- Not a, b or c
 - Only a
 - Only b
 - Only c
 - a and b
27. Assuming that the face value of the treasury bill is R260 000 and the date to maturity is one year. Which of the following statements is/are correct?
(The rate of return is rounded off to one decimal point.)
- If the price paid for the treasury bill is R245 000 the rate of return is 6.1%.
 - If the price paid for the treasury bill is R243 000 the rate of return is 7%.
 - If the price paid for the treasury bill is R242 750 the rate of return is 7.1%.
 - If the price paid for the treasury bill is R210 000 the rate of return is 19.0%.
- Only a, b and c
 - Only a, b and d
 - Only b, c and d
 - Only a, c and d
 - a, b, c and d

28. Which of the following statements is/are correct?

- a. A decrease in income with a simultaneous increase in the money supply shifts the demand for money curve to the left and the money supply curve to the right. The equilibrium interest rate is lower.
- b. An increase in income with a simultaneous selling of treasury bills by the central bank shifts the demand for money curve to the right and the money supply curve to the left. The equilibrium interest rate is higher.
- c. An increase in income with simultaneous expansionary open market operations by the central bank shifts the demand for money curve to the right and the money supply curve to the left. The equilibrium interest rate is definitely higher.

1. a and b
2. Only a
3. Only b
4. Only c
5. None of the options 1 to 4

29. Which of the following statements are correct in terms of the events chain: $D_B \uparrow \rightarrow P_B \uparrow \rightarrow i \downarrow$?

- a. The events chain shows what happens if the central bank wants to increase the money supply: $M^s \uparrow$.
- b. The events chain illustrates what happens if the central bank wants to stimulate the economy.
- c. The events chain illustrates the inverse relationship between the price of treasury bills and the interest rate.

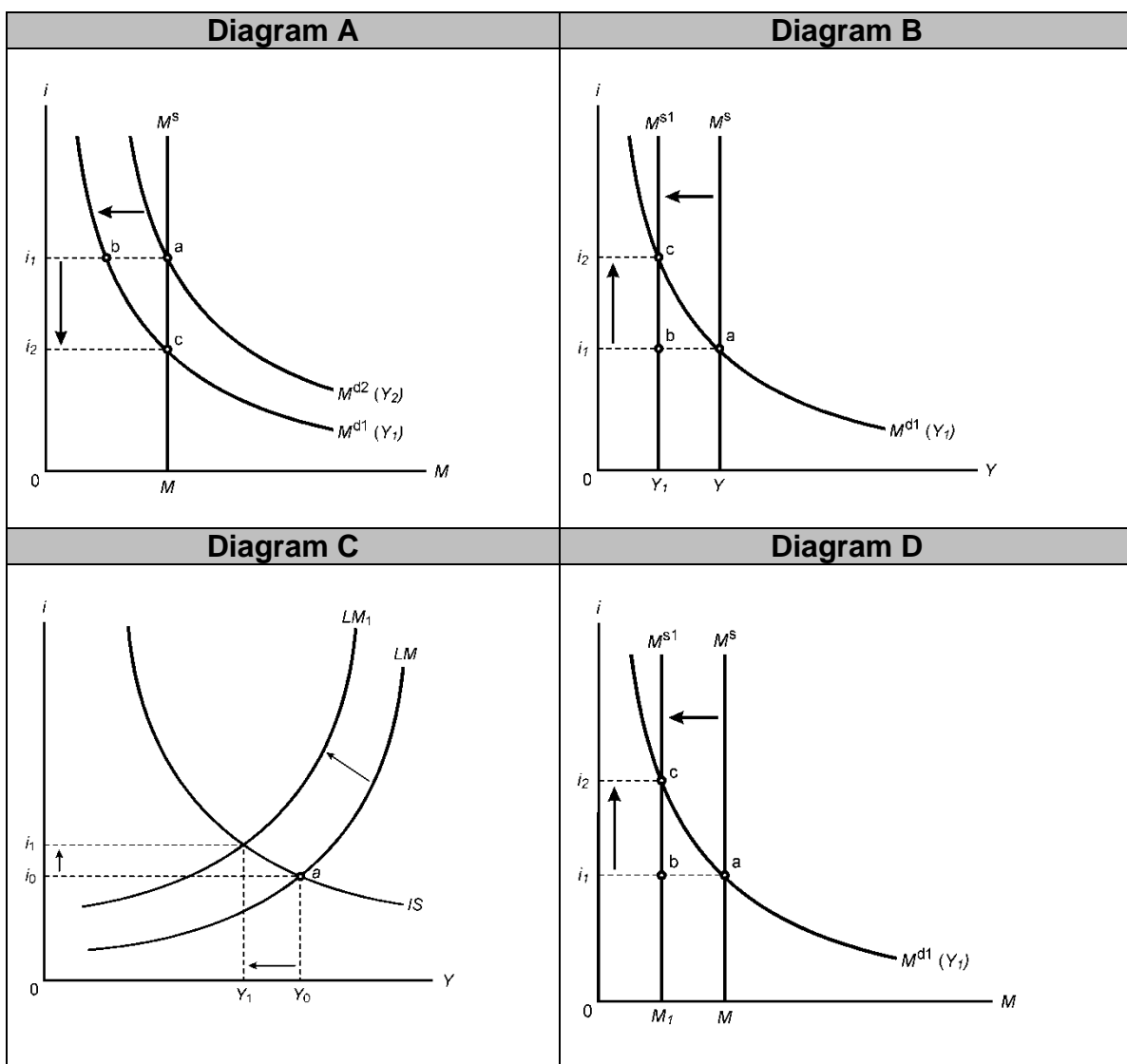
1. a, b and c
2. Only a and b
3. Only a and c
4. Only b and c
5. Only c

30. Which of the following statements is/are correct?

- a. The liquidity preference theory of money refers to the demand for passive balances which are determined by the need to do transactions.
- b. If bonds were to pay 25% interest, market participants would want to hold as much money as possible.
- c. If the interest rate drops from 25% to 5% market participants will tend to buy bonds.
- d. The price paid for treasury bills determines the interest rate in the market.

1. Not a, b, c or d
2. Only a
3. Only b
4. Only c
5. Only d

31. Which of the following statements are correct in terms of the financial market?
- An increase in uncertain economic conditions will cause the price of treasury bills to decrease because of the increase in the interest rate.
 - A rising interest rate can be offset by an increase in the money supply.
 - A rising interest rate can be offset by expansionary monetary policy.
 - The impact of a high economic growth rate on the interest rate can be offset by increasing the money supply.
- a, b, c and d
 - Only a, b and c
 - Only b, c and d
 - Only c and d
 - None of the options 1 to 4
32. Which one of the following diagrams illustrates the impact of the contractionary monetary policy on the interest rate in the financial market?



1. Diagram A
2. Diagram B
3. Diagram C
4. Diagram D

33. Which of the following statements is/are correct in terms of the financial market?

- a. A decrease in income shifts the money supply curve to the left.
- b. To increase the money supply the central bank makes use of open market operations.
- c. To increase the money supply the central bank sells treasury bills.
- d. A high economic growth rate will not affect the money supply while the demand for money is higher and the interest rate increases.

1. Only b and d
2. Only a
3. Only b
4. Only b and c
5. b, c and d

34. If the financial market is in a liquidity trap it implies that ...

- a. the return on holding bonds is extremely high.
- b. there is a high demand for money.
- c. there is a high demand for bonds.
- d. the return on holding money is high.
- e. the return on holding bonds is extremely low.

1. a, b and d
2. c and e
3. a and c
4. b, d and e
5. Only b and e

35. If the financial market is in a liquidity trap ...

- a. a decrease in the interest rate can be brought about by the buying of bonds by the central bank.
- b. financial money market participants will buy bonds if the money supply is increased
- c. financial money market participants will keep money if the money supply is increased.
- d. monetary policy is ineffective in bringing about a decrease in the interest rate.

1. Only c and d
2. a, c and d
3. a, b and d
4. Only c
5. Only d

SEMESTER 2
WRITTEN ASSIGNMENT 02
LEARNING UNITS 1 TO 4
SELF-ASSESSMENT ASSIGNMENT
DO NOT SUBMIT THIS ASSIGNMENT

HINT: Align the length of your answers to the marks indicated. Do not submit your answers. Assess or mark your answers once you have received Tutorial Letter 202.

Question 1 (5 marks)

The IS-LM model is a simplification of the interrelationship between selected economic variables. The model consists of a number of endogenous variables (those variables whose values are determined inside the model) and a number of exogenous variables (those variables whose values are determined outside the model).

List the various endogenous and exogenous variables in the IS-LM model.

Question 2 (6 marks)

Explain why investment spending is a negative function of the interest rate and a positive function of the level of output and income and name two determinants of autonomous investment in South Africa.

Question 3 (6 marks)

Use the following information to derive an IS curve:

- A decrease in the interest rate from 6% to 4% increases investment spending by 200.
- Autonomous spending before the decrease in the interest rate is 800.
- The multiplier is 5.

Question 4 (6 marks)

Derive the LM curve by assuming that the level of output and income decreases.

Question 5 (6 marks)

Critically discuss the following statement:

The more sensitive investment spending is for a change in the interest rate and the less sensitive it is for a change in the level of output and income the greater the impact of an expansionary fiscal policy on the level of output and income.

Question 6 (8 marks)

Use the IS-LM model to identify the variables that will have an impact on the effectiveness of an expansionary fiscal policy to increase the level of output and income and explain how these variables influence the effectiveness of fiscal policy.

Question 7 (8 marks)

Use the IS-LM model to identify the variables that will have an impact on the effectiveness of an expansionary monetary policy to increase the level of output and income and explain how these variables influence the effectiveness of monetary policy.

Question 8 (10 marks)

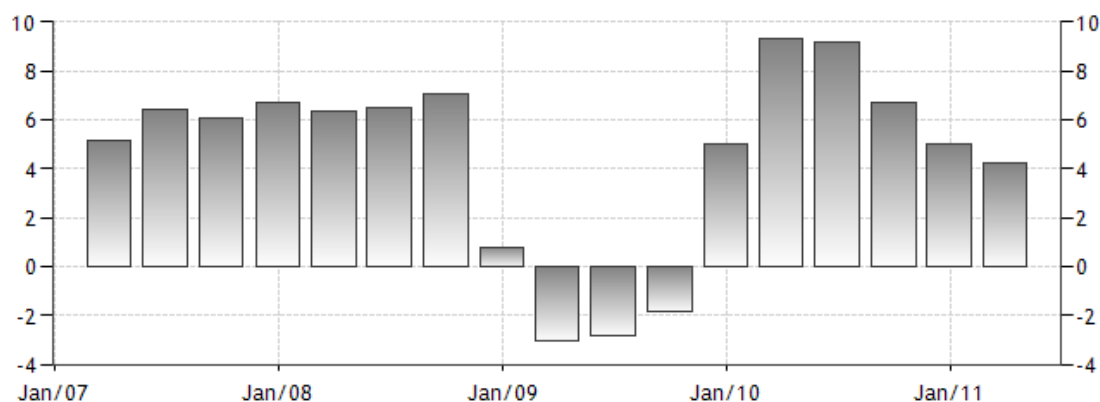
This question is based on the following text and information about the Brazilian economy.

The Great Recession

The Great Recession originated in the financial markets of the United States of America in 2007. It was triggered by falling house prices which led to the so-called “subprime mortgage” crisis. Preceding the crisis there was a rapid increase in mortgages to less creditworthy borrowers. A combination of falling house prices and default mortgage payments led to the failure and near failure of major financial institutions in America. This sent shockwaves across the financial markets of the world and resulted in a loss of confidence in financial markets and institutions, with the result that share prices fell sharply, investor confidence plunged and the availability of credit to firms and households was severely curtailed. This had the result that consumption spending by households and investment spending by firms declined which had a major impact on the level of output and income.

In response to the world wide economic crisis many countries used monetary and fiscal policies in an attempt to deal with the impact of the recession on the level of output and income.

BRAZIL GDP ANNUAL GROWTH RATE



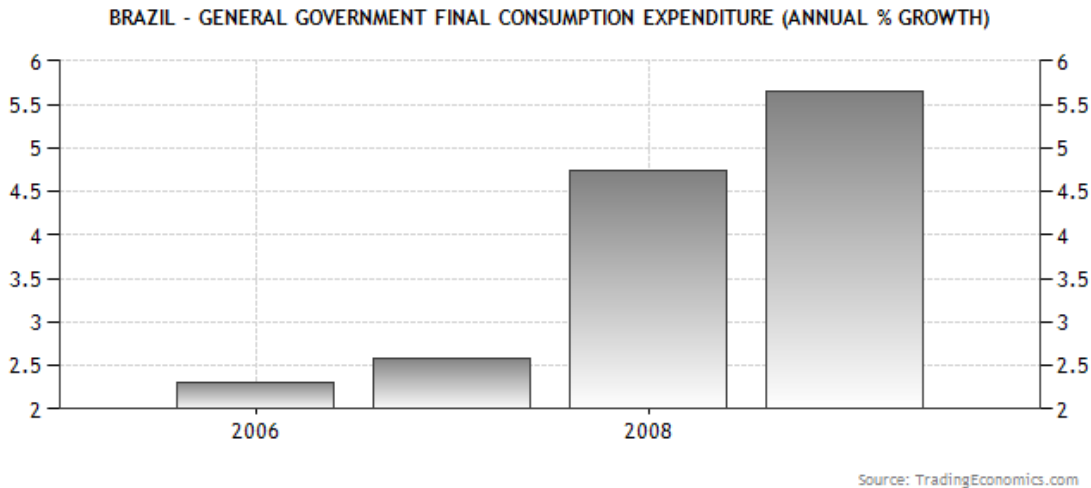
source: TradingEconomics.com; IBGE

BRAZIL INTEREST RATE

Benchmark Interest Rate



source: TradingEconomics.com; Banco Central do Brasil



- a. Given that an economic recession is defined as a decrease in real GDP for two consecutive periods (where a period is 3 months, also known as a quarter because there are four periods of 3 months in a year), during which year did Brazil experience an economic recession?
- b. Based on the above information use the IS-LM model to explain how Brazil made use of monetary and fiscal policies to deal with the economic recession they experienced.

Question 9 (4 marks)

The impact of an expansionary fiscal policy differs in the goods market model compared to the impact in the IS-LM model. What are the similarities and differences between the impact in the goods market model and the IS-LM model?

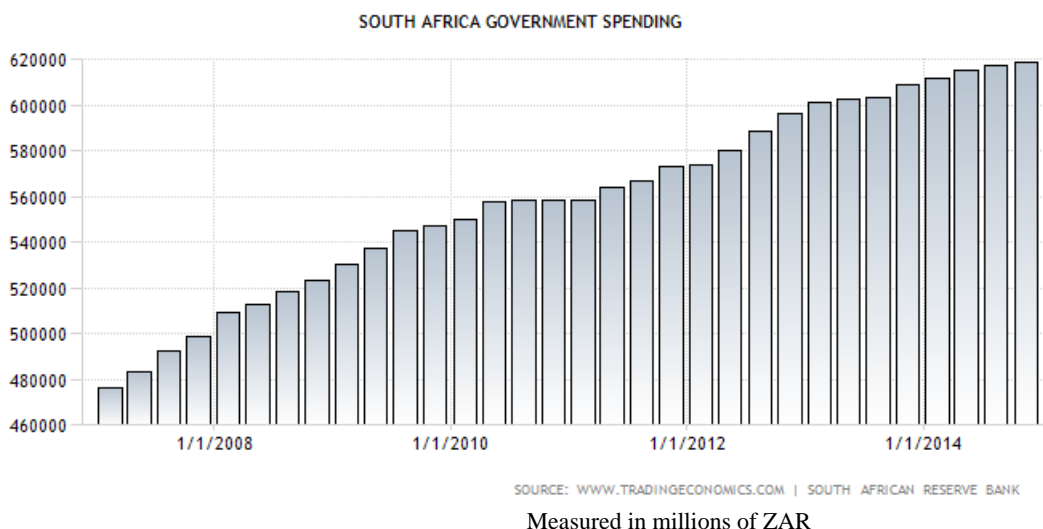
Question 10 (6 marks)

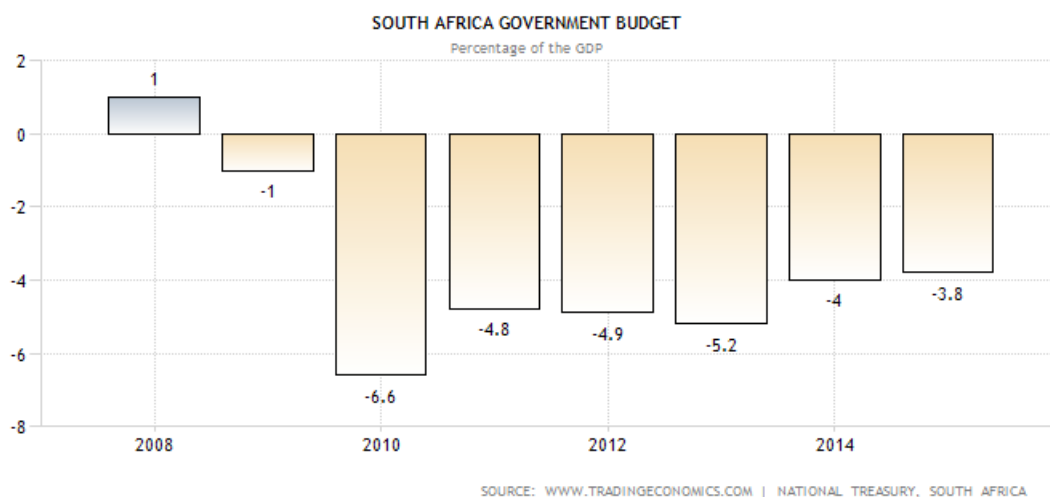
Use the IS-LM model to compare the impact of an expansionary fiscal policy with that of a contractionary monetary policy.

Questions 11 (2.5 marks) and question 12 (8 marks)

Questions 11 and 12 are based on the following graphs:

Question 11 (2.5 marks)





11. Which of the following statements are correct for South Africa?

- Government spending was below R480 000 million in the first quarter of 2007 and reached a high of just under R620 000 million in the fourth quarter of 2014.
- Government has sustained a budget deficit since 2008.
- The economic downturn which began in the last quarter of 2008 was caused by contractionary fiscal policy.
- The country suffered a recession in the beginning of 2014.

- a, b and d
- Only a and b
- Only c and d
- Only a and d

Question 12 (8 marks)

Policy makers in South Africa can use fiscal and monetary policies to deal with the impact of negative economic growth, stemming from an external shock such as a decline in world GDP, on the South African economy.

- a. Identify the period during which a recession took place in the South African economy.
- b. Use the IS-LM model to explain how fiscal and monetary policies were used to deal with this impact in order to boost the economy.

SEMESTER 2

ASSIGNMENT 03

LEARNING UNITS 1 TO 4

DUE DATE: 2016/09/05

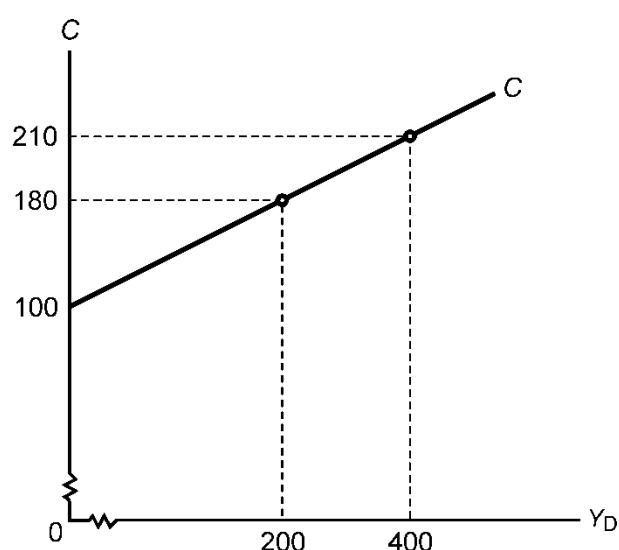
UNIQUE NUMBER: 707201

This assignment contributes 40% towards your semester mark.

Please ensure that this assignment reaches the university before the due date.

Answer all questions on a mark-reading sheet.

Question 1 is based on the following diagram:



1. Which of the following statements are correct?
 - a. Induced consumption is equal to R100 if the disposable income is R200.
 - b. The marginal propensity to consume is equal to 0.15. It means that if the disposable income of households increases by R100 million, the increase in consumer spending will be R15 million.
 - c. An increase in autonomous consumption will influence the slope of the consumption curve.
 - d. If the marginal propensity to save by households increases, the marginal propensity to consume will be lower. In other words, the slope of the C curve will be flatter.
1. a, b and c
 2. a, b and d
 3. Only b and d
 4. Only a and d
 5. Only b and c

2. Given that $c_0 = R800m$, $\bar{I} = R600m$, $G = R700m$, $c = 0.8$ and $T = R400m$ and $Y_f = R12\ 000m$ the equilibrium level of income is _____ and in order to reach the full-employment level of income, government spending must increase by _____.
- | | | |
|----|----------|---------|
| 1. | R12 500m | R620m |
| 2. | R12 100m | R3 100m |
| 3. | R8 900m | R620m |
| 4. | R2 100m | R1 980m |
| 5. | R1 424m | R2 115m |
3. If the multiplier is 3 and income increased by R96 million, the increase in autonomous spending must have been ...
1. R288 million.
 2. R0.03 million.
 3. R96 million.
 4. R32 million.
4. Which of the following statements are correct?
- a. Marginal propensity to consume and autonomous consumption are exogenous variables of the consumption function.
 - b. Nominal money supply and the part of the demand for money that is influenced by expectations, business confidence, and political and social factors are exogenous variables in the financial market.
 - c. Marginal propensity to consume and the level of output and income are endogenous variables in the goods market model.
 - d. Investment spending is an exogenous variable in the goods market model but in the IS-LM model the part of investment spending that is dependent on the level of output and income and the interest rate are endogenous variables.
 - e. Level of output and income, interest rate, investment, consumption spending are exogenous variables in the IS-LM model.
 - f. Taxes, government spending and the nominal supply of money are exogenous variables in the IS-LM model.
1. a, b, c and d
 2. b, c, e and f
 3. Only a, b and f
 4. a, b, d and f
 5. b, d and e
5. When firms increase their spending on capital goods ...
- a. financial investment takes place.
 - b. real investment takes place.
 - c. it means that the expected rate of return on investment projects exceed the market interest rate.
 - d. real investment increases.

1. a, c and d
 2. Only a and c
 3. Only c and d
 4. Only b and d
 5. b, c and d
6. In the goods market model the impact of the decline in the demand for goods due to a decline in consumption spending and investment spending can be represented by a(n)...
1. steeper demand for goods curve.
 2. flatter demand for goods curve.
 3. upward shift of the demand for goods curve.
 4. downward shift of the demand for goods curve.
7. Which of the following statements are correct?
In the IS-LM model:
- a. Investment is influenced only by the interest rate.
 - b. Investment is influenced by exogenous factors such as expectations, business confidence and regulations.
 - c. Investment is influenced by the interest rate and the level of output.
 - d. Investment is negatively related to the interest rate and the level of output.
 - e. Investment is negatively related to the interest rate and positively related to the level of output.
1. a and b
 2. b, c and e
 3. b, c and d
 4. a and e
 5. Only c and e
8. Which one of the following events takes place in the goods market if the level of output and income increases?
1. Consumption spending by households increases and government spending increases.
 2. Consumption spending by households increases and investment spending by firms increases.
 3. Taxation increases and government spending increases.
 4. Money supply increases and the interest rate declines.
9. In the event of a rise in the interest rate a(n) _____ an investment curve takes place while an increase in output will cause a(n) _____ an investment curve.
1. rightward shift of; downward movement along
 2. downward movement along; rightward shift of
 3. upward movement along; leftward shift of
 4. upward movement along; rightward shift of
 5. downward movement along; upward movement along

10. In the goods market an increase in investment due to a decrease in the interest rate is represented by an upward shift of the demand for goods curve while an increase in investment due to an increase in output is represented by a downward movement along the demand for goods curve.

The above statement is **incorrect** since an ...

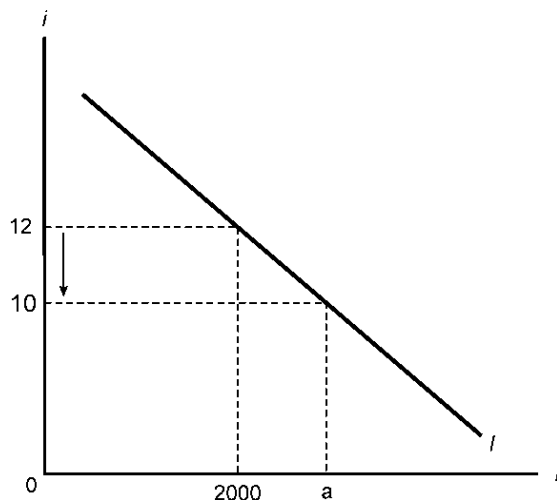
1. increase in investment due to a decrease in the interest rate is represented by a downward shift of the demand for goods curve.
2. increase in investment due to a decrease in the interest rate is represented by a downward movement along the demand for goods curve.
3. increase in investment due to an increase in output is represented by an upward shift of the demand for goods curve.
4. increase in investment due to an increase in output is represented by an upward movement along the demand for goods curve.

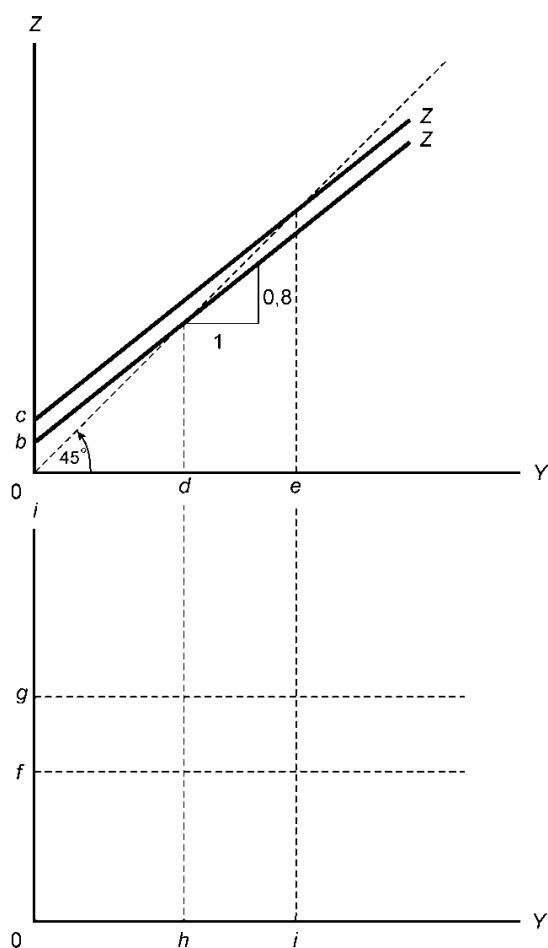
Questions 11 to 14 deal with the derivation of the IS curve and are based on the following information and diagram:

We assume that investment spending is the only component of autonomous spending.

The autonomous spending at an interest rate of 10% is 4 000.

A decrease in the interest rate from 12% to 10% increases investment spending by 2 000.





11. The value for a is _____ and the value of the multiplier _____.

- | | | |
|----|-------|------|
| 1. | 1 000 | 1.25 |
| 2. | 2 000 | 5 |
| 3. | 3 000 | 1.25 |
| 4. | 4 000 | 5 |
| 5. | 5 000 | 5 |

12. The values for b and c are:

- | | | |
|----|--------------|--------------|
| 1. | $b = 2\,000$ | $c = 4\,000$ |
| 2. | $b = 4\,000$ | $c = 2\,000$ |
| 3. | $b = 2\,000$ | $c = 3\,000$ |
| 4. | $b = 6\,000$ | $c = 4\,000$ |
| 5. | $b = 4\,000$ | $c = 6\,000$ |

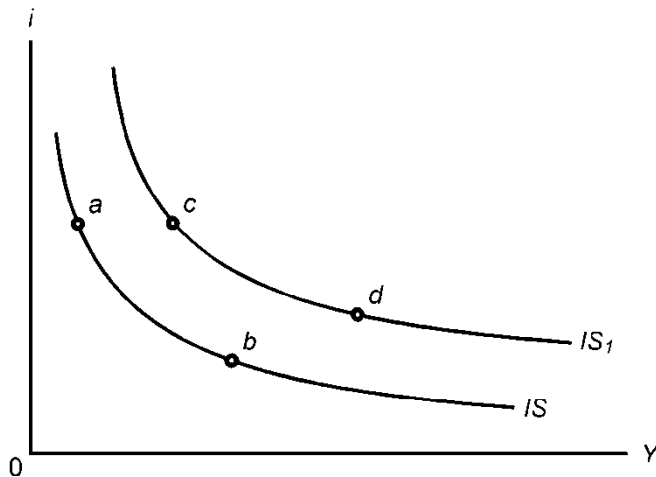
13. The values for d and e are:

- | | | |
|----|---------------|---------------|
| 1. | $d = 12\,000$ | $e = 16\,000$ |
| 2. | $d = 10\,000$ | $e = 20\,000$ |
| 3. | $d = 20\,000$ | $e = 30\,000$ |
| 4. | $d = 30\,000$ | $e = 20\,000$ |
| 5. | $d = 15\,000$ | $e = 20\,000$ |

14. The values for f and g are _____ and the values for h and i are _____.

- | | | | | |
|----|--------------|--------------|---------------|---------------|
| 1. | $f = 10\%$ | $g = 12\%$ | $h = 12\ 000$ | $i = 16\ 000$ |
| 2. | $f = 12\%$ | $g = 10\%$ | $h = 10\ 000$ | $i = 20\ 000$ |
| 3. | $f = 2\ 000$ | $g = 3\ 000$ | $h = 20\ 000$ | $i = 30\ 000$ |
| 4. | $f = 12\%$ | $g = 10\%$ | $h = 30\ 000$ | $i = 20\ 000$ |
| 5. | $f = 10\%$ | $g = 12\%$ | $h = 10\ 000$ | $i = 20\ 000$ |

Question 15 is based on the following diagram:



15. Which of the following statements are correct?

- The IS curve may shift from IS to IS_1 because of an increase in the tax rate.
 - The IS curve may shift from IS to IS_1 because of an increase in consumer confidence.
 - The movement from point c on curve IS_1 to point a on curve IS is caused by a change in any of the autonomous factors that decrease the demand for goods.
 - The movement from point a to point b on curve IS is caused by a decrease in the interest rate.
 - The IS curve may shift from IS_1 to IS because of a decrease in the interest rate.
 - An increase in the money supply will shift the IS curve from IS to IS_1 .
- a, b and d
 - b, c, e and f
 - Only b, c and f
 - Only b, c and e
 - b, c and d

16. The statement that the LM curve is upward sloping since an increase in the interest rate increases the demand for money is **incorrect** because it is ...

- upward sloping since an increase in the interest rate decreases the demand for money.
- upward sloping since an increase in the interest rate increases the money supply.
- upward sloping since an increase in income increases the demand for money and the interest rate.
- upward sloping since an increase in the interest rate increases the income level.
- upward sloping since an increase in income increases the money supply.

17. Which of the following statements are correct?

- a. To derive the IS curve we change the interest rate to determine the effect on the level of output and income.
- b. To derive the IS curve we change the level of output and income to determine the effect on the interest rate.
- c. To derive the IS curve we change government spending to determine the effect on the level of output and income.
- d. To derive the LM curve we change the income level to determine its effect on the demand for goods.
- e. To derive the LM curve we change the level of income to determine its effect on the interest rate.

- 1. a and d
- 2. a and e
- 3. b and d
- 4. c and d
- 5. b and e

18. Which one of the following will cause a downward shift in the LM curve?

- 1. An increase in the demand for money and expansionary monetary policy.
- 2. An increase in the level of output and income and expansionary monetary policy.
- 3. An increase in the money supply and expansionary monetary policy.
- 4. A decrease in the money supply and contractionary monetary policy.
- 5. An increase in the interest rate and expansionary monetary policy.

19. In the IS-LM model an increase in the nominal money supply causes the LM curve to shift ...

- 1. downwards and the interest rate decreases. As the interest rate decreases investment spending increases and the IS curve shifts to the right.
- 2. upwards and the interest rate increases. As the interest rate increases investment spending decreases and the IS curve shifts to the left.
- 3. downwards and the interest rate decreases. As the interest rate decreases the investment spending increases and a movement along the IS curve takes place.

20. In the IS-LM model an increase in government spending increases the demand for goods and the ...

- 1. IS curve shifts to the right. As government spending increases the supply of money increases and the LM curve shifts downwards.
- 2. IS curve shifts to the right. The demand for money increases and the interest rate rises and a movement along the LM curve takes place.
- 3. IS curve shifts to the left. The demand for money increases and the interest rate rises causing the LM curve to shift upwards.

21. In the IS-LM model which of the following policy actions will bring about an increase in the level of output and income and an increase in the interest rate?
- An increase in the money supply.
 - An increase in government spending.
 - A decrease in the money supply.
 - A decrease in government spending.
 - An increase in the budget deficit.
- a, b and d
 - b, c and e
 - Only b and c
 - Only b and e
 - a, b and e
22. In the IS-LM model the impact of the decline in the demand for goods due to the decline in consumption spending and investment spending can be represented by a ...
- upward shift of the LM curve.
 - downward shift of the LM curve.
 - leftward shift of the IS curve.
 - rightward shift of the IS curve.

Questions 23 to 27 are based on the following comparison between the impact of an **expansionary fiscal policy** with an **expansionary monetary policy** in the IS-LM model:

	Fiscal policy	Monetary policy
The demand for goods	Higher	Higher
The level of output and income	Higher	Higher
The interest rate	Higher	Lower
Investment spending	Indeterminate	Higher
Budget deficit	Higher	Unchanged

23. The reason for the higher demand for goods and level of output and income for an expansionary fiscal policy is that _____ while for an expansionary monetary policy it is higher since _____.
- investment spending is higher; government spending is higher
 - government spending is higher; investment spending is higher
 - government spending is lower; investment spending is higher
 - investment spending is lower; government spending is lower
24. The reason for the higher interest rate for an expansionary fiscal policy is that the _____ while for expansionary monetary policy it is lower since the _____.
- money supply is lower; money supply is higher
 - demand for money is higher; money supply is higher
 - money supply is higher; demand for money is higher
 - demand for money is higher; demand for money is higher

25. The reason investment spending is indeterminate in the case of an expansionary fiscal policy is because an increase in the interest rate ...
1. increases investment while the increase in output decreases investment.
 2. decreases investment while the increase in output increases investment.
 3. increases investment while the increase in output increases investment.
 4. decreases investment while the increase in output decreases investment.
26. The reason investment spending is higher in the case of an expansionary monetary policy is because the decrease in the interest rate....
1. decreases investment and the increase in the level of output increases investment.
 2. increases investment and the increase in the level of output decreases investment.
 3. increases investment and the increase in the level of output increases investment.
 4. decreases investment and the increase in the level of output decreases investment.
27. The reason the budget deficit increases in the case of an expansionary fiscal policy is because _____ while for an expansionary monetary policy it is unchanged since _____.
1. government spending increases and/or taxes decrease; government spending increases and/or taxes increase
 2. government spending increases and/or taxes increase; government spending and/or taxes are unchanged
 3. government spending and/or taxes are unchanged; government spending increases and/or taxes increase
 4. government spending increases and/or taxes decrease; government spending and/or taxes are unchanged

Question 28 is based on the following statement.

"...by expanding government's contribution to the economy, the fiscus is able to support economic activity at a time when global and domestic demand is faltering." (National Budget Review, 2009.)

28. The implication of this within the IS-LM model means ...
- a. a rightward shift of the IS curve takes place.
 - b. a downward shift of the LM curve takes place.
 - c. the demand for goods as well as the level of output and income increases.
 - d. an expansionary fiscal policy.
 - e. an expansionary monetary policy.
1. a, b, c, d and e
 2. Only b and e
 3. Only b, c and e
 4. Only a, c and d
 5. None of the options 1 to 4

29. When comparing a **contractionary fiscal policy** with an **expansionary monetary policy** in the IS-LM model the results are best described by the following?

1.	FISCAL POLICY	MONETARY POLICY
The demand for goods	Lower	Higher
The level of output	Lower	Higher
The interest rate	Higher	Lower
Investment spending	Lower	Higher
Budget deficit	Lower	Unchanged

2.	FISCAL POLICY	MONETARY POLICY
The demand for goods	Lower	Higher
The level of output	Lower	Higher
The interest rate	Lower	Lower
Investment spending	Higher	Higher
Budget deficit	Unchanged	Unchanged

3.	FISCAL POLICY	MONETARY POLICY
The demand for goods	Lower	Higher
The level of output	Lower	Higher
The interest rate	Lower	Lower
Investment spending	Indeterminate	Higher
Budget deficit	Lower	Unchanged

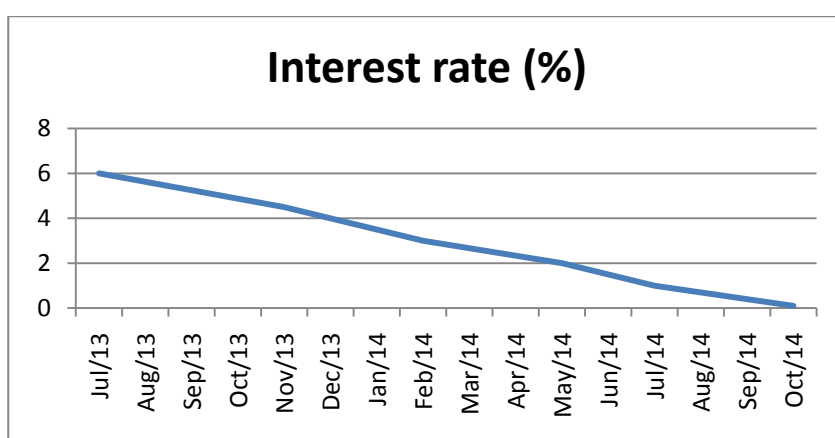
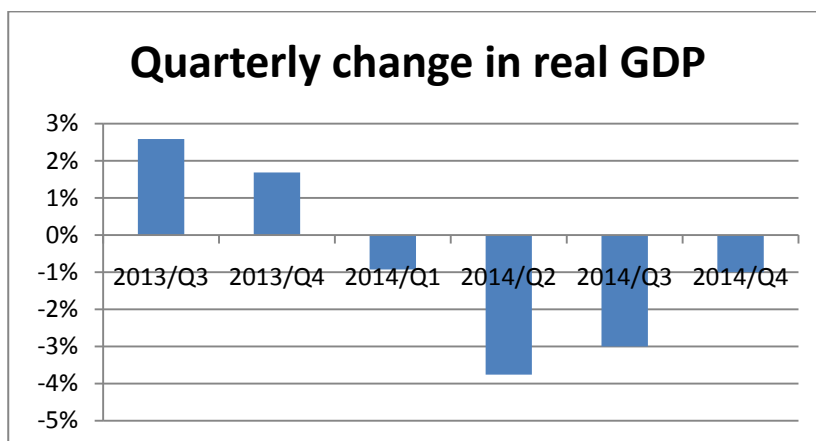
4.	FISCAL POLICY	MONETARY POLICY
The demand for goods	Higher	Lower
The level of output	Higher	Lower
The interest rate	Higher	Higher
Investment spending	Indeterminate	Lower
Budget deficit	Higher	Unchanged

5.	FISCAL POLICY	MONETARY POLICY
The demand for goods	Lower	Higher
The level of output	Lower	Lower
The interest rate	Lower	Lower
Investment spending	Indeterminate	Higher
Budget deficit	Lower	Unchanged

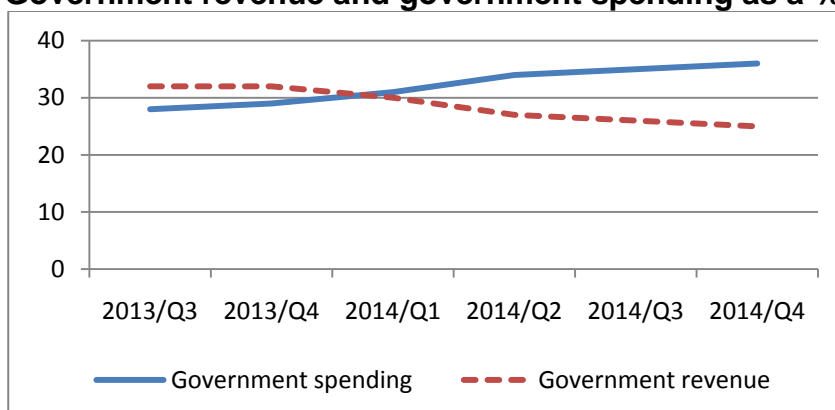
30. Which one of the following policy actions is appropriate if the objective is to decrease the budget deficit without decreasing the level of output and income?

1. An expansionary fiscal policy coupled with an expansionary monetary policy.
2. A contractionary fiscal policy coupled with a contractionary monetary policy.
3. An expansionary fiscal policy coupled with a contractionary monetary policy.
4. A contractionary fiscal policy coupled with an expansionary monetary policy.

Questions 31 to 33 are based on the following scenario for a hypothetical country:



Government revenue and government spending as a % of GDP



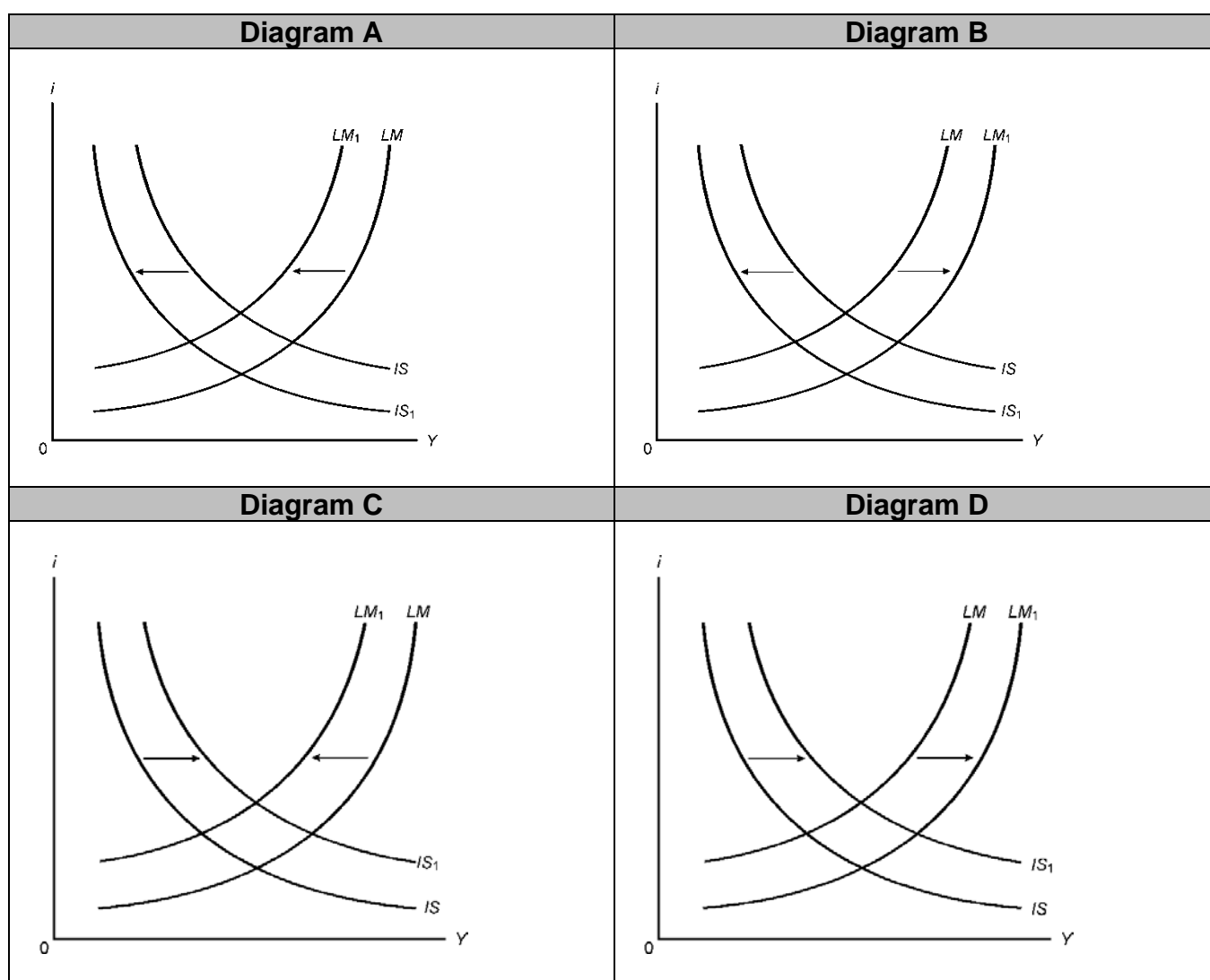
Government spending and government revenue as % of GDP		
Period	Government spending	Government revenue
2013/Q3	28%	32%
2013/Q4	29%	32%
2014/Q1	31%	30%
2014/Q2	34%	27%
2014/Q3	35%	26%
2014/Q4	36%	25%

31. Which of the following applies to the country during 2014?

- The country experienced an economic recession.
- It has implemented a contractionary fiscal policy
- It has implemented an expansionary monetary policy.
- Unemployment increased.
- The budget deficit increased.

- a, b, c, d and e
- Only a, b, c and d
- Only a, c, d and e
- Only a, d and e
- Only b, c and d

32. In terms of the IS-LM model the macroeconomic stabilisation policies the country has followed can be represented graphically as follows:

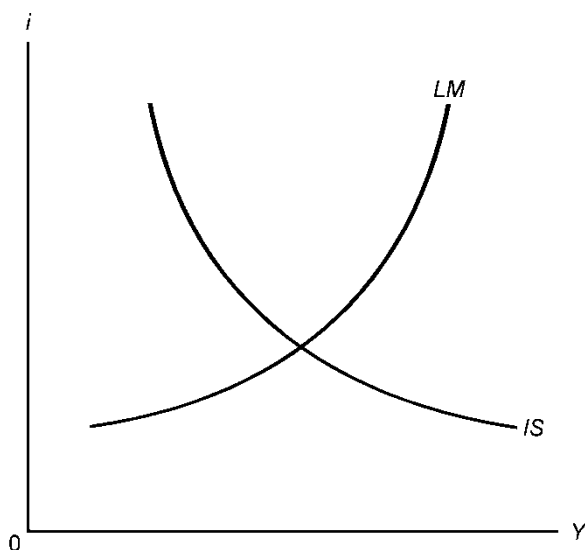


- Diagram A
- Diagram B
- Diagram C
- Diagram D
- Not Diagram A, B, C or D

33. During the third quarter of 2014 a _____ exists since _____ was greater than _____.

- | | | | |
|----|----------------|---------------------|---------|
| 1. | budget surplus | government spending | taxes |
| 2. | trade surplus | government spending | taxes |
| 3. | budget deficit | government spending | taxes |
| 4. | trade surplus | government spending | taxes |
| 5. | budget surplus | exports | imports |

Questions 34 and 35 are based on the following IS-LM model:



34. A decrease in the nominal money supply causes the LM curve to shift ...

1. downwards and the interest rate decreases. As the interest rate decreases investment spending increases and the IS curve shifts to the right.
2. upwards and the interest rate increases. As the interest rate increases investment spending decreases and a movement along the IS curve takes place.
3. upwards and the interest rate decreases. As the interest rate decreases the investment spending increases and a movement along the IS curve takes place.
4. upwards and the interest rate increases. As the interest rate increases the investment spending decreases and the IS curve shifts to the left.

35. An increase in taxation ...

1. decreases the demand for goods and the IS curve shifts to the left. As taxation decreases the supply of money decreases and the LM curve shifts downwards.
2. increases the demand for goods and the IS curve shifts to the right. The demand for money increases and the interest rate rises and a movement along the LM curve takes place.
3. decreases the demand for goods and the IS curve shifts to the left. The demand for money decreases and the interest rate falls causing the LM curve to shift upwards.
4. decreases the demand for goods and the IS curve shifts to the left. The demand for money decreases and the interest rate falls causing a movement along the LM curve.

<p>SEMESTER 2</p> <p>ASSIGNMENT 04</p> <p>LEARNING UNITS 5 TO 7</p> <p>DUE DATE: 2016/09/30</p> <p>UNIQUE NUMBER: 705374</p>

This assignment contributes 40% towards your semester mark.

Please ensure that this assignment reaches the university before the due date.

Answer all questions on a mark-reading sheet.

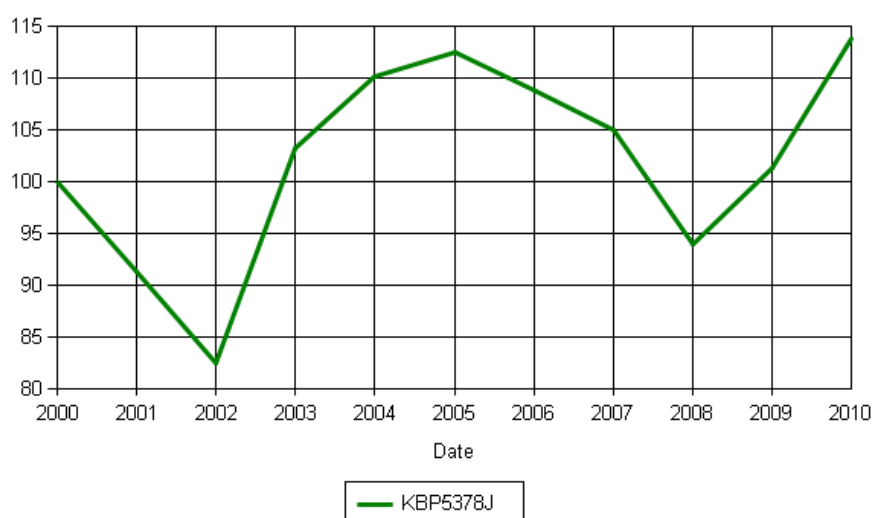
1. Which of the following statements are correct?
 - a. The nominal exchange rate is the relative price of domestic goods in terms of foreign goods.
 - b. The real exchange rate is the price of the domestic currency in terms of foreign currency.
 - c. The most popular way of measuring the openness of the goods market, is to express the imports and exports as a percentage of GDP.
 - d. Openness in goods markets is the ability of consumers and firms to choose between domestic goods and foreign goods.
 - e. Openness in financial markets is the ability of financial investors to choose between domestic financial assets and foreign financial assets.
 1. a, b, c, d and e
 2. Only a and b
 3. Only b, c and d
 4. Only a, b and e
 5. Only c, d and e

2. Which of the following refers to an appreciation of the rand?
 - a. R1 = \$0.30 to R1 = \$0.25
 - b. R1 = \$0.25 to R1 = \$0.30
 - c. R1 = \$0.50 to R1 = \$0.55
 - d. \$1 = R8 to \$1 = R7
 - e. \$1 = R7 to \$1 = R8
 1. a and c
 2. Only b and c
 3. a and e
 4. b, c and d
 5. b and e

3. If the exchange rate between South Africa and the USA changes from $R1 = \$0.30$ to $R1 = \$0.25$, *ceteris paribus*,
- the rand appreciates and South Africa will import more from the USA.
 - the rand appreciates and USA will import more from South Africa.
 - the rand depreciates and South Africa will import more from the USA.
 - the rand depreciates and USA will import more from South Africa.
- Only a
 - Only b
 - Only c
 - Only d
 - Not option 1, 2, 3 or 4
4. Which of the following statements are correct regarding the real exchange rate?
- The real exchange rate is the relative price of domestic goods in terms of foreign goods.
 - The real exchange rate is the price of the domestic currency in terms of foreign currency.
 - If a real appreciation has occurred it means that the relative price of South African goods compared with USA goods has increased.
 - If a real appreciation has occurred it means that the relative price of South African goods compared with USA goods has decreased.
 - If a real appreciation has occurred it means that the relative price of South African currency compared with USA currency has increased.
- a and c
 - b and c
 - a and d
 - b and d
 - b and e

Questions 5 and 6 are based on the following diagram:

Real effective exchange rate for South Africa (2000 is the base year; 2000 = 100)



Source: South African Reserve Bank, *Quarterly Bulletin Time Series*

5. For which periods was there a decline in the real exchange rate?
- Period 2000-2002.
 - Period 2002-2005.
 - Period 2005-2008.
 - Period 2008-2010.
- a and c
 - b and d
 - Only a
 - Only b
 - Only c
6. The possible reasons for a change in the real exchange rate are ...
- domestic price level.
 - foreign price level.
 - gross domestic product of trading partners.
 - gross domestic product of South Africa.
 - nominal exchange rate.
- a, b and c
 - b, c and e
 - a, b and e
 - Only a and b
 - Only b and e
7. A trade balance surplus indicates that a country earns more on _____ than it spends on _____ and this would be reflected as a _____ on the trade balance.
- imports; exports; improvement
 - exports; imports; deterioration
 - exports; imports; improvement
 - imports; exports; deterioration

Question 8 is based on the following information:

Year 1

GDP deflator for South Africa:	150
GDP deflator for the USA:	120
The nominal exchange rate:	R1 = \$0.30

Year 2

GDP deflator for South Africa:	190
GDP deflator for the USA:	130
The nominal exchange rate:	R1 = \$0.28

8. Which of the following statements are correct?
- The real exchange rate for year 1 is 0.38.
 - The real exchange rate for year 1 is 0.24.
 - The real exchange rate for year 2 is 0.19.
 - The real exchange rate for year 2 is 0.41.
 - Comparing the real exchange rate for year 2 with the real exchange rate for year 1, a real depreciation has occurred.
 - Comparing the real exchange rate for year 2 with the real exchange rate for year 1, a real appreciation has occurred.
- a, c and e
 - a, d and f
 - b, c and e
 - b, c and f
 - a, d and e
9. The interest parity condition implies that when an investor has to decide between domestic or foreign financial investment he/she would consider the difference in the _____ and the _____.
- expected changes in the exchange rate; inflation rate
 - interest rate; expected economic growth
 - level of output and income; expected changes in the exchange rate
 - expected changes in the exchange rate; balance of payments
 - interest rate; expected changes in the exchange rate.
10. Given the following information:
- Interest rate on RSA bonds: 6%
- Interest rate on USA bonds: 3%
- Which one of the following statements is correct?
- If the expected depreciation of the rand is 4% financial market participants will be indifferent between RSA and USA bonds.
 - If the expected appreciation of the rand is 4% financial market participants will buy USA bonds.
 - If the expected depreciation of the rand is 4% financial market participants will buy USA bonds.
 - If the expected depreciation of the rand is 4% financial market participants will buy RSA bonds.

Question 11 is based on the following information:

Suppose a South African investor has R100 000 available that he/she will not need for transactions. After doing some research on different financial investment opportunities the investor ended up having to choose between buying one-year South African bonds or one-year USA bonds. What would the investor decide based on the following information?

Interest rate on a one year South African bond = 12%

Interest rate on a one year USA bond = 2%

Current exchange rate: R1 = \$0.10

Expected exchange rate: R1 = \$0.09

11. Which of the following statements is/are correct?

- a. The South African investor will buy South African bonds.
- b. The South African investor will buy USA bonds.
- c. If the expected R/\$ exchange rate was R1 = \$0.08 rather than R1=\$0.09 in a years' time the South African investor would buy USA bonds.
- d. If the expected R/\$ exchange rate was R1 = \$0.08 rather than R1=\$0.09 in a years' the South African investor would buy South African bonds.

- 1. a and c
- 2. a and d
- 3. b and d
- 4. b and c
- 5. Only b

12. Which of the following statements are correct?

- a. Foreign demand for domestic goods is also known as exports.
- b. Domestic demand for foreign goods is also known as imports.
- c. Part of domestic demand falls on foreign/imported goods.
- d. The "domestic demand for goods" and the "demand for domestic goods" are the same.

- 1. a, b, c and d
- 2. Only a, b and c
- 3. Only b and d
- 4. Only c and d
- 5. Only b, c and d

13. An increase in the real exchange rate implies that ...

- a. SA goods are relatively cheaper than the goods produced in the rest of the world.
- b. SA goods are relatively more expensive than the goods produced in the rest of the world.
- c. exports will increase.
- d. exports will decrease.

- 1. a and c
- 2. b and c
- 3. a and d
- 4. b and d
- 5. Only d

14. Which of the following statements are correct?

A positive relationship exists between the ...

- real exchange rate and exports.
- domestic level of output and imports.
- real exchange rate and imports.
- domestic level of output and exports.
- level of foreign output and exports.

- a, b, c and d
- a, b, c and e
- Only b, c and e
- Only a and d
- c, d and e

15. Which one of the following statements is correct?

The NX curve represents the relationship between the

- real exchange rate and imports.
- level of output and income and imports.
- level of output and income and the trade balance
- level of output and income and exports.
- nominal exchange rate and the trade balance.

Question 16 is based on the following information:

Exports = R100 million

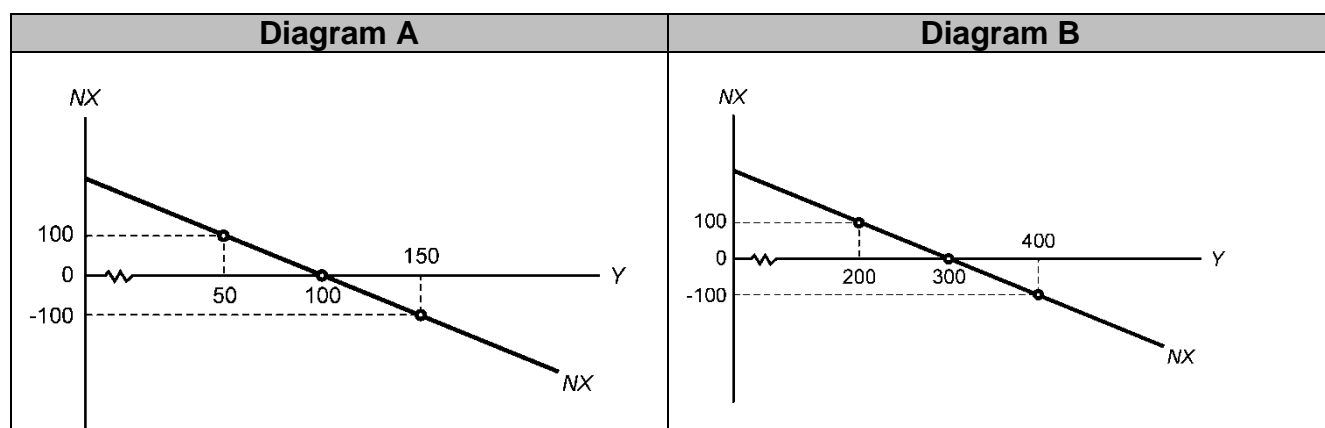
Imports:

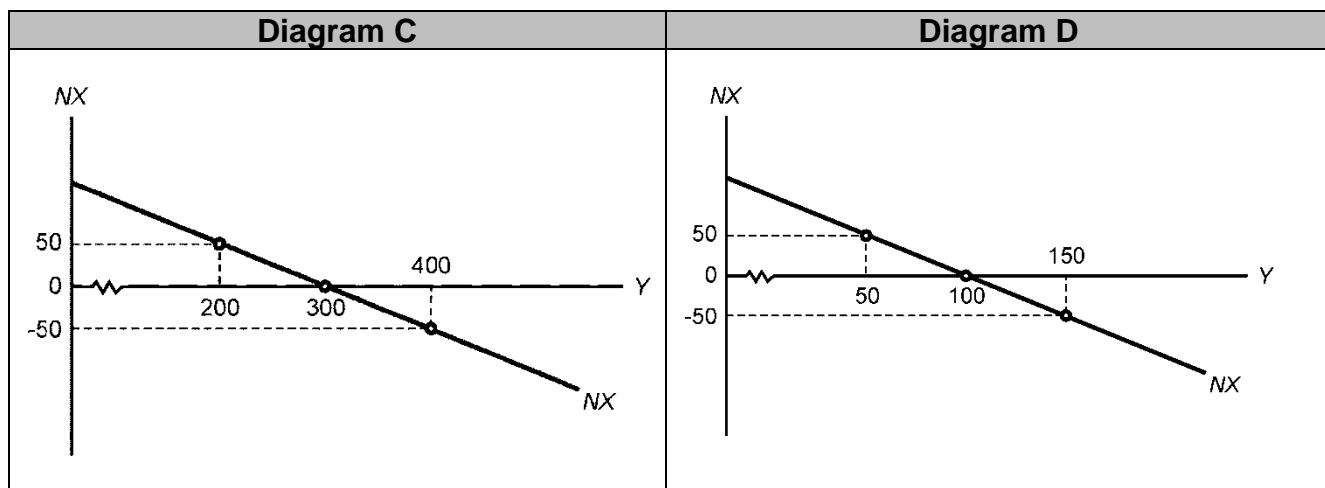
At $Y = \text{R}200$ million imports = R50 million

At $Y = \text{R}300$ million imports = R100 million

At $Y = \text{R}400$ million imports = R150 million

16. Given the information above a NX curve is constructed. Which one of the following diagrams represents the information?





1. Diagram A
2. Diagram B
3. Diagram C
4. Diagram D
5. Not Diagram A, B, C or D

17. Suppose the economy is in a recession, and the government decides to increase government spending in order to increase domestic demand and output.

If the original equilibrium level of output and income corresponds with a trade balance equilibrium position (Y_{TB} or Y_0), what will be the effect on the level of output and on the trade balance?

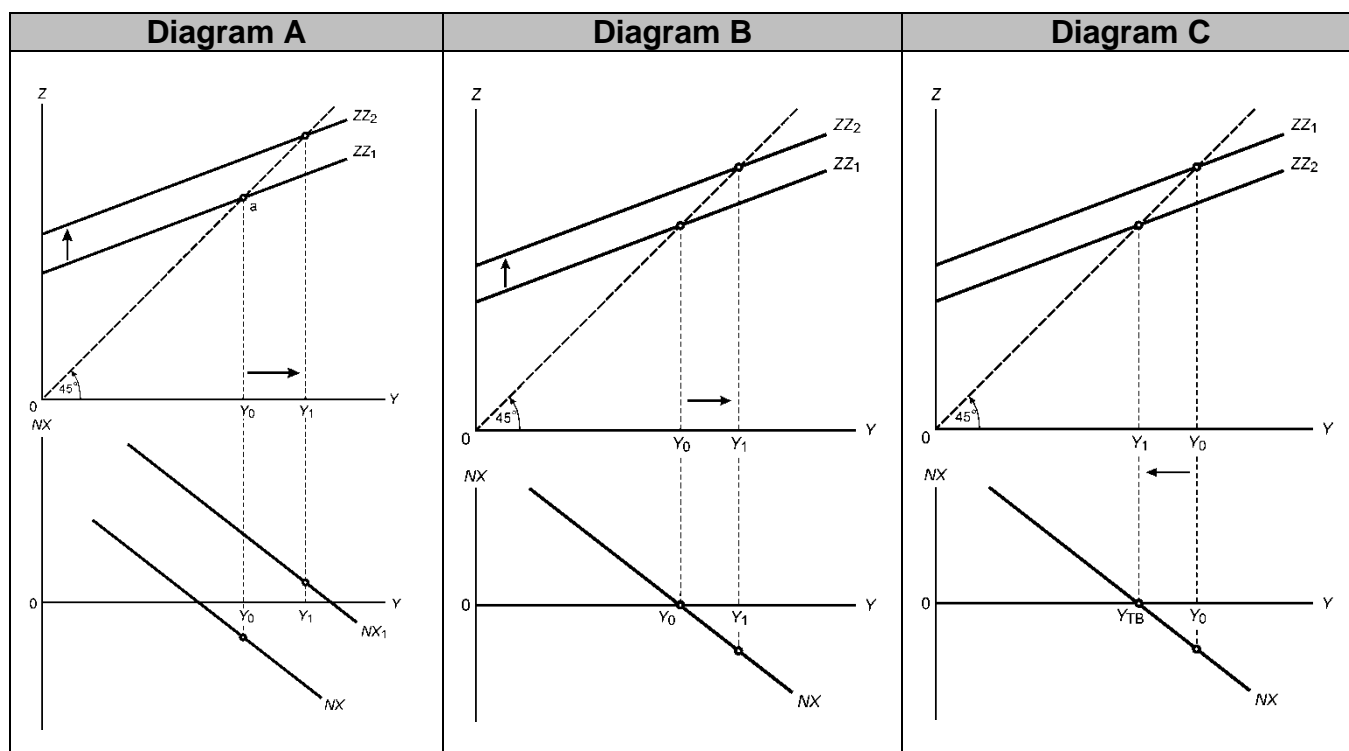
1. The domestic level of output and income will decrease and there will be a trade deficit.
2. The domestic level of output and income will decrease and there will be a trade surplus.
3. The domestic level of output and income will increase and there will be a trade deficit.
4. The domestic level of output and income will be unchanged and there will be a trade surplus.
5. The domestic level of output and income will increase and there will be a trade surplus.

18. Which of the following factors will shift the NX curve to the left?

- a. A decrease in imports.
- b. A decrease in exports.
- c. A decrease in government spending.
- d. An increase in domestic demand for goods.
- e. A decrease in demand for domestic goods.

1. a, b, c and d
2. b, c and e
3. Only a, c and d
4. Only b and e
5. Only d

19. Which one of the following diagrams illustrates the impact of increased government spending on the level of output and income and the trade balance of Country ABC.



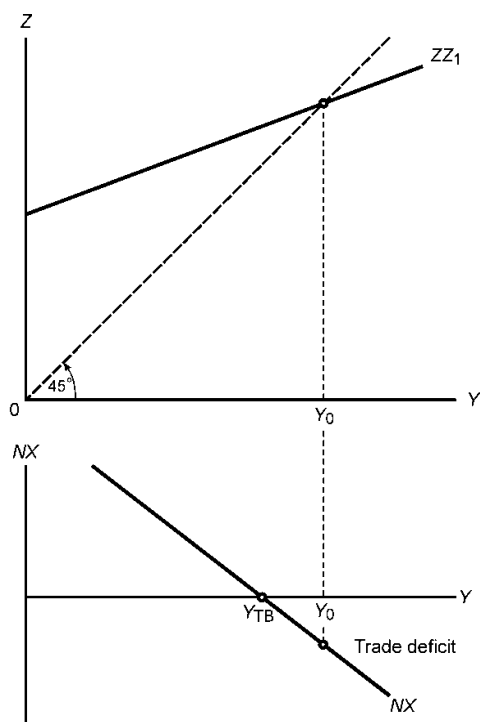
1. Diagram A
 2. Diagram B
 3. Diagram C
 4. Not Diagram A, B or c
20. Which of the following statements is/are correct regarding the impact of an increase in government spending on the level of output and income and the trade balance of Country ABC?

- a. The increased government spending has a multiplier impact on the level of output and income.
- b. The increase in income will lead to an increase in imports and the increase in imports causes a trade deficit. This is indicated by a movement along the NX curve.
- c. The increase in income will lead to an increase in exports and the increase in exports causes a trade surplus. This is indicated by a movement along the NX curve.
- d. The increase in income will lead to an increase in imports and the increase in imports causes a trade deficit. This is indicated by a shift of the NX curve to the right.
- e. The increase in income will lead to an increase in exports and the increase in exports causes a trade surplus. This is indicated by a shift of the NX curve to the right.

1. a and b
2. a and c
3. a and d
4. Only b
5. Not option 1, 2, 3 or 4

Question 21 and 22 are based on the following information:

Given goods market equilibrium in the following diagram, what would the likely impact of a depreciation of the domestic currency be?



21. Which one of the following statements is correct?

1. The ZZ_1 curve will shift upwards.
2. The ZZ_1 curve will shift downwards.
3. The ZZ_1 curve will stay constant
4. The ZZ_1 curve will shift upwards and then downwards.

22. Which one of the following statements is correct?

1. The domestic level of output will increase and there will be a higher trade deficit.
2. The domestic level of output will decrease and there will be a lower trade deficit.
3. The domestic level of output will decrease and there will be a trade surplus.
4. The domestic level of output will be unchanged and there will be a trade surplus.
5. The domestic level of output will increase and there will be a lower trade deficit.

23. Which of the following statements is/are correct?

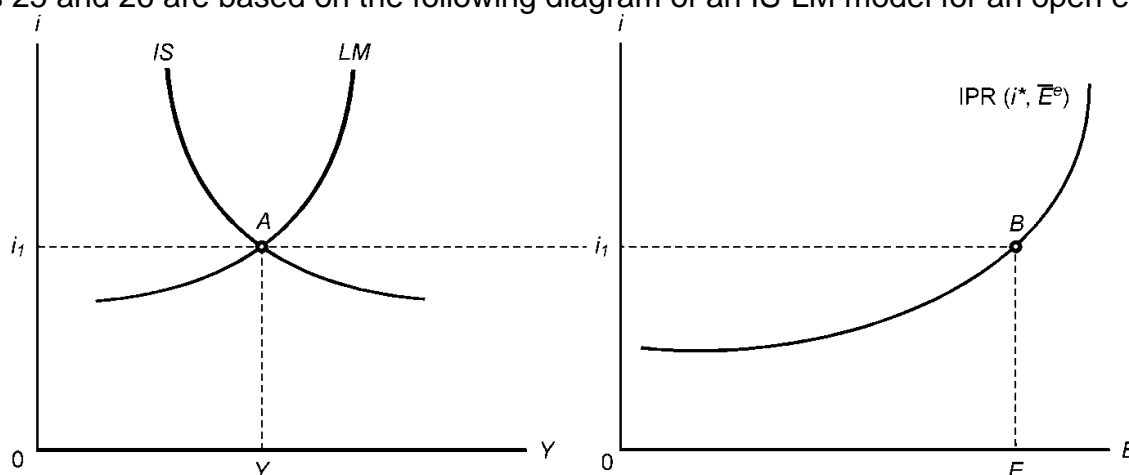
- a. The equilibrium condition in the financial market is $M^d = M^s$.
- b. Financial investors, domestic or foreign, go for the highest expected rate of return.
- c. By using the interest parity equation and by assuming that the expected exchange rate changes, a relationship between the domestic interest rate and the nominal exchange rate can be derived.
- d. A positive relationship exists between the domestic interest rate and the nominal exchange rate.

1. a, b, c and d
2. Only a, b and c
3. Only b, c and d
4. Only a, b and d
5. None of the options 1 to 4

24. Which one of the following statements is **incorrect** regarding the IS and LM relations in an open economy?

1. An increase in the interest rate will decrease the exchange rate.
2. The LM relation is exactly the same in an open economy as in a closed economy and is upward sloping.
3. Given the domestic interest rate and the interest parity relation, the equilibrium interest rate determines the equilibrium exchange rate.
4. The LM curve is upward sloping, because given the real money supply, an increase in output increases the interest rate.
5. The interest parity relations shows (given i^* , \bar{E}^e) the following relationship:
 $i \uparrow \rightarrow E \uparrow$ and $i \downarrow \rightarrow E \downarrow$.

Questions 25 and 26 are based on the following diagram of an IS-LM model for an open economy:



25. Which of the following statements is/are correct?

- a. A decrease in government spending is part of contractionary fiscal policy and will shift the IS curve.
- b. Monetary policy refers to changes in the money supply and will shift the LM curve.
- c. A decrease in government spending will shift the LM curve downwards.
- d. An increase in taxation will shift the IS curve to the left.
- e. A change in the interest rate will shift the LM curve downwards or upwards.

1. Only a, b and d
2. a, b and c
3. b, c, d and e
4. a, b, d and e
5. None of the options 1 to 4

26. A decrease in government spending causes a ...

1. decrease in the demand for goods and the level of output; a decrease in the demand for money and the interest rate; a depreciation of the domestic currency and the trade balance improves as exports increase.
2. decrease in the demand for goods and the level of output; a decrease in the demand for money and an increase in the interest rate; an appreciation of the domestic currency and the trade balance improves as exports increase.
3. decrease in the demand for goods and the level of output; an increase in the demand for money and the interest rate; a depreciation of the domestic currency and the trade balance improves as exports increase.
4. decrease in the demand for goods and the level of output; a decrease in the demand for money and the interest rate; a depreciation of the domestic currency and the trade balance deteriorates as exports increase.

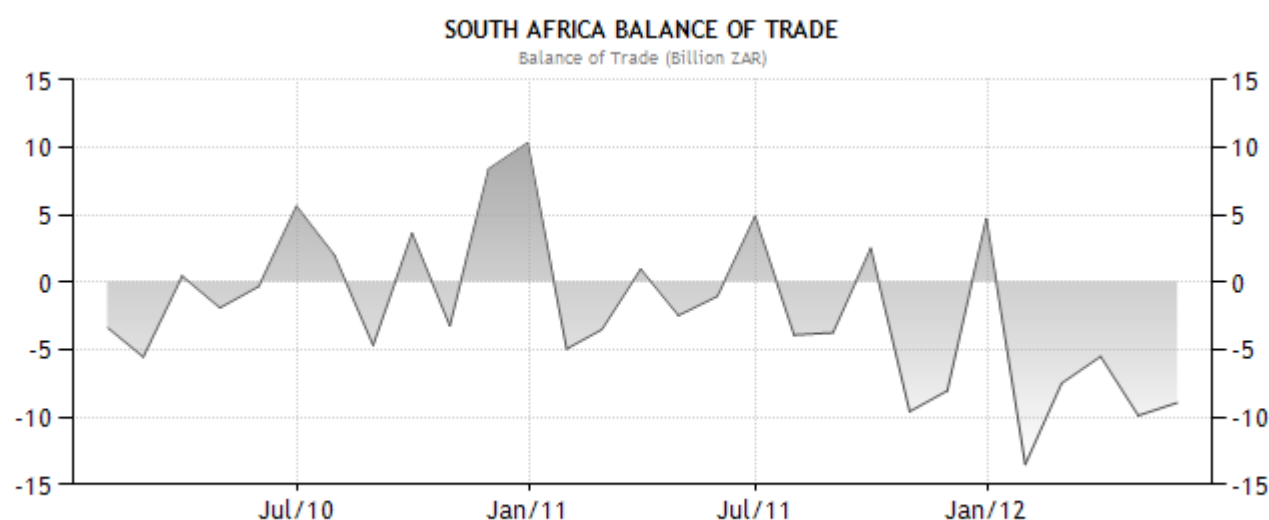
27. An increase in the money supply causes a ...

1. higher interest rate, a capital inflow, an appreciation of the exchange rate and a deterioration of the trade balance.
2. lower interest rate, a capital outflow, a depreciation of the exchange rate and an improvement of the trade balance.
3. lower interest rate, a capital outflow, an appreciation of the exchange rate and an improvement of the trade balance.
4. higher interest rate, a capital inflow, a depreciation of the exchange rate and an improvement of the trade balance.

28. In the IS-LM model for an open economy fiscal contraction implies that the ...

- a. IS curve will shift to the left and the interest rate decreases.
 - b. IS curve will shift to the right and the interest rate increases.
 - c. nominal exchange rate decreases and a depreciation of the domestic currency take place.
 - d. nominal exchange rate increases and an appreciation of the domestic currency take place.
-
1. a and d
 2. b and d
 3. a and c
 4. a and d

Questions 29 and 30 are based on the following information:



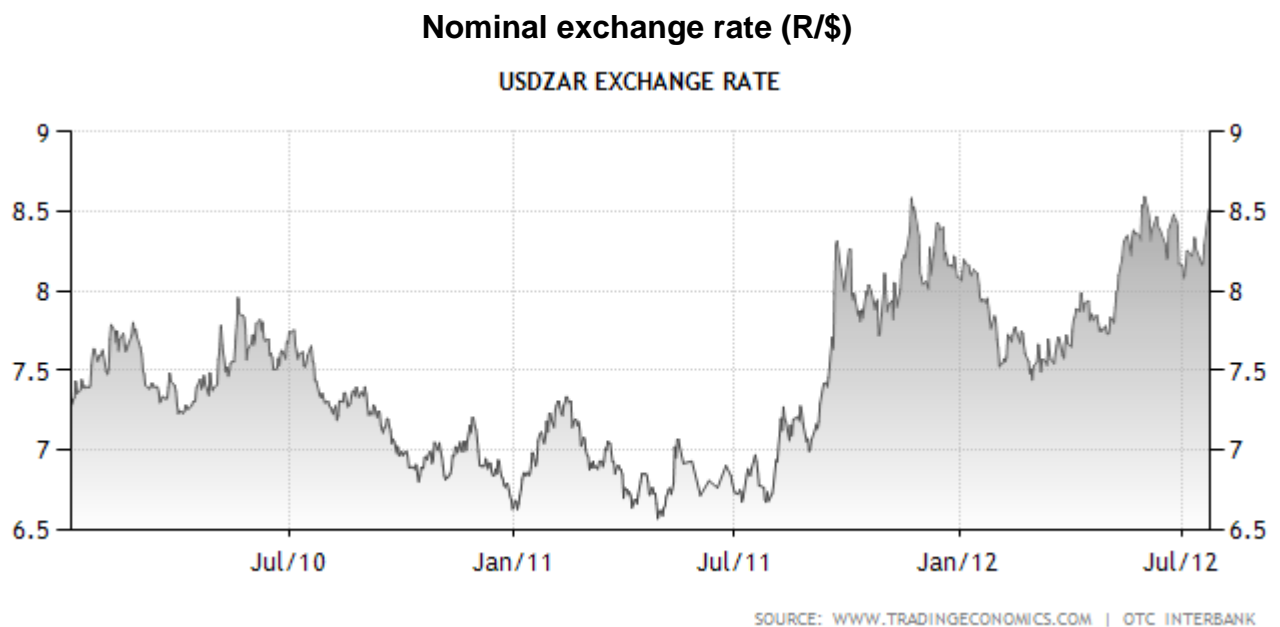
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SOURCE: WWW.TRADINGECONOMICS.COM | SOUTH AFRICAN REVENUE SERVICE



29. Which of the following statements are correct?

As at July 2011 and as at January 2012 South Africa experienced ...

- a. a trade surplus.
- b. a trade deficit.
- c. since exports exceeded imports.
- d. since imports exceeded exports.

- 1. a and c
- 2. b and d
- 3. a and d
- 4. b and c
- 5. a and b

30. For the period beginning July 2011 and ending January 2012 the R/\$ exchange rate _____ and over the period beginning July 2011 and ending January 2012 South African exports experienced an overall _____.
1. appreciated increase
 2. depreciated increase
 3. depreciated decrease

Question 31 is based on the following information.

During the first quarter of 2012 the interest rate in South Africa was higher than the interest rates of our major trading partners.

31. Which one of the following statements is correct?
Using the IS-LM model for an open economy which of the following correctly describes the impact of the relatively higher interest rate on the R/\$ exchange rate and the trade balance?
1. It caused a depreciation of the R/\$ exchange rate, exports increased and the deficit on the trade balance declined.
 2. It caused a depreciation of the R/\$ exchange rate, exports decreased and the deficit on the trade balance increased.
 3. It caused an appreciation of the R/\$ exchange rate, exports decreased and the deficit on the trade balance decreased.
 4. It caused an appreciation of the R/\$ exchange rate, exports decreased and the deficit on the trade balance increased.
32. The impact of an increase in government spending (or expansionary fiscal policy) on the exchange rate and the trade balance can be represented by the following chain of events:
1. $G \uparrow : i \uparrow \rightarrow \text{Capital}_{\text{inflow}} \rightarrow E \uparrow \rightarrow X \downarrow \rightarrow NX \uparrow$
 2. $G \uparrow : i \uparrow \rightarrow \text{Capital}_{\text{inflow}} \rightarrow E \uparrow \rightarrow X \downarrow \rightarrow NX \downarrow$
 3. $G \uparrow : i \downarrow \rightarrow \text{Capital}_{\text{outflow}} \rightarrow E \downarrow \rightarrow X \uparrow \rightarrow NX \downarrow$
 4. $G \uparrow : i \downarrow \rightarrow \text{Capital}_{\text{inflow}} \rightarrow E \downarrow \rightarrow X \uparrow \rightarrow NX \uparrow$
33. The impact of contractionary monetary policy on the exchange rate and the trade balance can be represented by the following chain of events:
1. $M \uparrow : i \uparrow \rightarrow E \uparrow \rightarrow X \downarrow \rightarrow NX \uparrow$
 2. $M \uparrow : i \uparrow \rightarrow E \uparrow \rightarrow X \downarrow \rightarrow NX \downarrow$
 3. $M \downarrow : i \downarrow \rightarrow E \downarrow \rightarrow X \uparrow \rightarrow NX \downarrow$
 4. $M \downarrow : i \downarrow \rightarrow E \downarrow \rightarrow X \uparrow \rightarrow NX \uparrow$

Questions 34 and 35 are based on the following comparison between the impact of a **contractionary fiscal policy** with a **contractionary monetary policy** in the IS-LM model for an open economy:

	Contractionary fiscal policy	Contractionary monetary policy
Exchange rate	Depreciate	Appreciate
Capital flows	Outflow	Inflow
Exports	Higher	Lower
Trade balance	Improves	Worsens

34. The reason for the depreciation of the exchange rate is due to a contractionary fiscal policy is because of the _____ while due to a contractionary monetary policy the exchange rate appreciates because of the _____.

1. increase in the domestic interest rate relative to the world interest rate; increase in the domestic interest rate relative to the world interest rate
2. decrease in the domestic interest rate relative to the world interest rate; decrease in the domestic interest rate relative to the world interest rate
3. increase in the domestic interest rate relative to the world interest rate; decrease in the domestic interest rate relative to the world interest rate
4. decrease in the domestic interest rate relative to the world interest rate; increase in the domestic interest rate relative to the world interest rate

35. The reason for the capital outflow occurring due to a contractionary fiscal policy is because of the _____ while due to a contractionary monetary policy there is a capital inflow because of the _____.

- | | |
|-----------------------------------|-------------------------------|
| 1. increase in the interest rate; | decrease in the interest rate |
| 2. decrease in the interest rate; | increase in the interest rate |
| 3. increase in the interest rate; | increase in the interest rate |
| 4. decrease in the interest rate; | decrease in the interest rate |

<p style="text-align: center;">SEMESTER 2</p> <p style="text-align: center;">ASSIGNMENT 05</p> <p style="text-align: center;">LEARNING UNITS 8 TO 9</p> <p style="text-align: center;">SELF-ASSESSMENT ASSIGNMENT</p> <p style="text-align: center;">DO NOT SUBMIT THIS ASSIGNMENT</p>

NOTE: Do not submit your answers. Assess or mark your answers once you have received Tutorial Letter 204.

The Labour Market

1. In our analysis of the labour market we assume the following:
 - a. Labour is the only factor of production used in the production of output.
 - b. Labour productivity is constant.
 - c. The price of oil and other raw material stays constant.
 - d. The price of products set by firms is based on cost plus a mark-up.
 1. a, b, c and d
 2. Only a, b and d
 3. Only b, c and d
 4. Only a and b
 5. Only c and d

2. Our analysis of the labour market implies the following:
 - a. There is a negative relation between the targeted real wage and the unemployment rate.
 - b. The higher the unemployment rate, the weaker the workers' position in bargaining.
 - c. The higher the unemployment rate, the lower the targeted real wage.
 - d. An improvement in the bargaining position of workers' makes it possible to bargain for higher wages.
 1. a, b, c and d
 2. Only a, b and c
 3. Only a, c and d
 4. Only b, c and e
 5. Only b and d

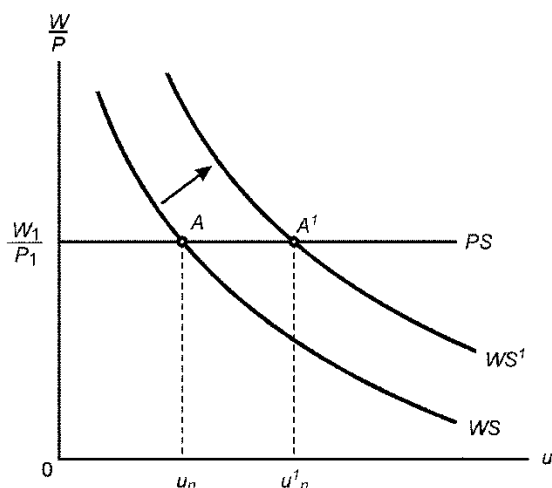
3. Which of the following factors will increase the bargaining position of workers?
 - a. The more expensive it is to dismiss workers.
 - b. A higher level of output and a lower unemployment rate.
 - c. A lower level of output and a higher unemployment rate.
 - d. An increase in unemployment benefits.
 - e. Labour laws that protect workers from being dismissed.

1. Only factors a, d and e
 2. Only factors a, b and d
 3. Only factors b, d and e
 4. Only factors d and e
 5. Factors a, b, d and e
4. Which of the following statements are correct?
- a. Higher unemployment is associated with both a lower chance of finding a job and a higher chance of losing your job.
 - b. An increase in the nominal wage for a given general price level will decrease the real wage.
 - c. For a given nominal wage, an increase in the general price level will decrease the real wage.
 - d. The real wage is the quantity of goods and services that can be purchased with the nominal wage.
1. a, b, c and d
 2. Only b, c and d
 3. Only a, c and d
 4. Only b and d
 5. Only a and d
5. Institutional factors play an important role in the way wages are determined in a country. Which of the following are institutional factors that are common in most countries?
- a. Most workers are paid a high enough wage that they prefer being employed to being unemployed.
 - b. The lower the unemployment rate, the higher the wages.
 - c. Wages depend on labour market conditions.
 - d. The expected price level, the unemployment rate and institutional factors will influence the behaviour of workers when negotiating for wages.
1. a, b, c and d
 2. Only a, c and d
 3. Only b, c and d
 4. Only a, b and d
 5. Only a, b and c
6. Which one of the following, according to the wage-setting relationship, is **not** an institutional factor that may affect the outcome of wage setting?
1. Minimum wages.
 2. Unemployment benefits.
 3. Labour law protection.
 4. Unemployment rate.
 5. Collective bargaining.

7. Which of the following statements are correct?
- Workers are able to determine the real wage through nominal wage bargaining.
 - Through an increase in their nominal wages workers are able to increase their real wages.
 - An increase in the mark-up by firms causes a decrease in real wages.
 - A positive relationship exists between the mark-up and the price per unit.
- a, b, c and d
 - Only a, c and d
 - Only b, c and d
 - Only a and d
 - Only c and d
8. Which of the following influences price-setting by firms in an imperfectly competitive market?
- The nature of the production function.
 - The relation between the inputs used in production and the quantity of output produced.
 - The prices of the inputs.
 - The nominal wage per unit of output.
 - The mark-up of the firm.
- Only a, b, d and e
 - Only b, c and d
 - Only a, c, d and e
 - a, b, c, d and e
 - Only c and e
9. Which of the following statements are correct?
- The price level in the economy is partly the outcome of nominal wage bargaining and the price setting behaviour of firms in the economy.
 - An increase in the nominal wage is enough to ensure an increase in the real wage.
 - A decrease in the mark-up by firms causes an increase in feasible real wages.
 - The PS curve will shift upwards if the mark-up by firms decreases.
- a, b, c and d
 - Only c and d
 - Only a, c and d
 - Only b, c and d
 - Only a and d
10. Which of the following statements are correct?
- A positive relationship exists between the ...
- expected price level and the bargained nominal wage.
 - unemployment rate and the bargained nominal wage.
 - mark-up and the price per unit.
 - nominal wage and the price per unit.
 - better unemployment benefits and the nominal wage.

1. a, b, c, d and e
2. Only b, c and d
3. Only c, d and e
4. Only a, c, d and e
5. Only a, c and d

Question 11 is based on the following diagram:



11. Which factors will shift the WS curve to WS^1 ?

- a. A higher unemployment rate.
- b. A higher level of output.
- c. An increase in unemployment benefits.
- d. Labour laws that protect workers from being dismissed.
- e. A better bargaining position of workers.

1. b, c, d and e
2. a, b, d and e
3. Only c, d and e
4. Only a and b
5. a, c, d and e

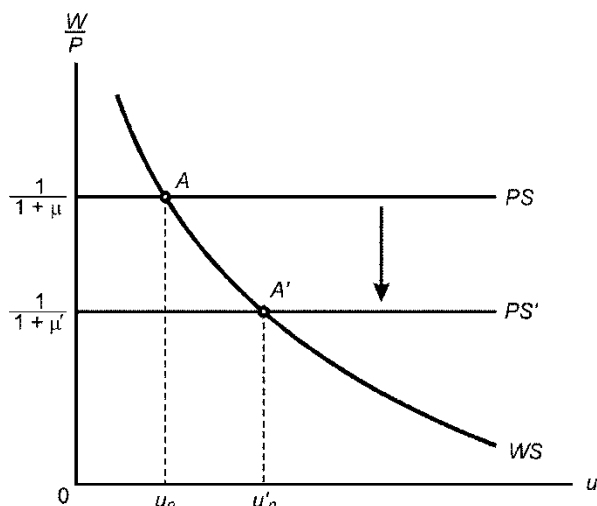
12. Which of the following statements is/are correct?

The WS curve will shift down because of ...

- a. a lower mark-up.
- b. a lower unemployment rate.
- c. lower nominal wages.
- d. labour laws that provide workers with less protection against layoffs.
- e. better unemployment benefits.

1. a and c
2. b and d
3. Only b
4. Only c
5. Only d

Question 13 is based on the following diagram:



13. The diagram illustrates a(n)...

- higher mark-up.
- lower mark-up.
- decrease in the price determined real wage accompanied by an increase in the natural rate of unemployment.
- increase in the workers' bargaining position.
- increase in the actual price level.

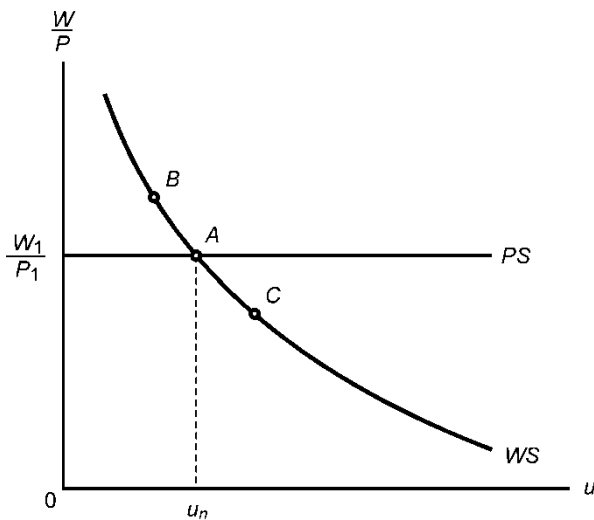
- Only a and c
- b and c
- a, d and e
- a, c and e
- b, d and e

14. The PS curve will shift downwards because of a ...

- lower mark-up.
- higher mark-up.
- lower unemployment rate.
- higher unemployment rate.

- a and c
- a and d
- b and c
- b and d
- Only b

Question 15 is based on the following wage-setting and price-setting relationships:



15. Which of the following statements is/are correct?

At point C the ...

- unemployment rate is higher which decreases the bargaining position of workers and the nominal wage they can bargain for decreases.
- unemployment rate is lower which increases the bargaining position of workers and the real wage implied by price setting increases.
- targeted real wage is lower than the implied real wage.
- targeted real wage is higher than the implied real wage.

- b, c and d
- a, b and c
- Only a and c
- Only b and c
- Only a

16. A decrease in the level of output will cause the following events on the labour market:

- The level of unemployment decreases causing an increase in the bargaining position of workers which enables them to bargain for a nominal wage increase.
- The level of unemployment increases which causes a decline in the bargaining position of workers resulting in a lower bargained nominal wage.
- The natural level of unemployment decreases causing an increase in the bargained real wage.
- The natural level of unemployment increases causing a decrease in the bargained real wage.

17. Which one of the following chain of events describes the impact of an increase in output on the labour market?

- $Y \uparrow \rightarrow u \uparrow \rightarrow N \downarrow \rightarrow W \uparrow$
- $Y \uparrow \rightarrow N \uparrow \rightarrow u_n \downarrow \rightarrow W \uparrow$
- $Y \uparrow \rightarrow N \uparrow \rightarrow u \downarrow \rightarrow W \uparrow$
- $Y \downarrow \rightarrow N \downarrow \rightarrow u \uparrow \rightarrow W \downarrow$
- $W \uparrow \rightarrow N \downarrow \rightarrow u \uparrow$

AS-AD model

18. Which of the following events is/are represented by the AS curve?

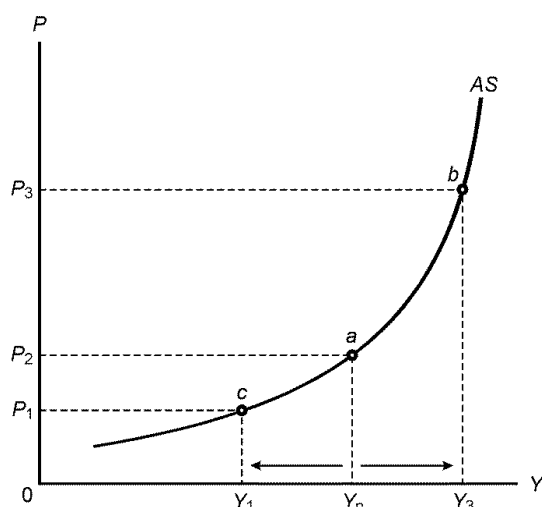
- $Y \uparrow \rightarrow u \uparrow \rightarrow N \downarrow \rightarrow W \uparrow \rightarrow P \downarrow$
- $Y \uparrow \rightarrow N \uparrow \rightarrow u_n \downarrow \rightarrow W \uparrow \rightarrow P \downarrow$
- $Y \downarrow \rightarrow N \downarrow \rightarrow u \uparrow \rightarrow W \downarrow \rightarrow P \downarrow$
- $Y \downarrow \rightarrow u \downarrow \rightarrow N \uparrow \rightarrow W \downarrow \rightarrow P \uparrow$
- $W \uparrow \rightarrow N \downarrow \rightarrow u \uparrow \rightarrow P \uparrow$

- Only a
- Only b
- Only c
- Only d
- b and c

19. The AS curve has a positive slope because of which the following chain of events?

- $Y \uparrow \rightarrow u \uparrow \rightarrow N \downarrow \rightarrow W \uparrow \rightarrow P \downarrow$
- $Y \uparrow \rightarrow N \uparrow \rightarrow u_n \downarrow \rightarrow W \uparrow \rightarrow P \uparrow$
- $W \uparrow \rightarrow N \downarrow \rightarrow u \uparrow \rightarrow P \uparrow$
- $Y \downarrow \rightarrow u \downarrow \rightarrow N \uparrow \rightarrow W \downarrow \rightarrow P \uparrow$
- $Y \uparrow \rightarrow N \uparrow \rightarrow u \downarrow \rightarrow W \uparrow \rightarrow P \uparrow$

Question 20 is based on the following diagram.

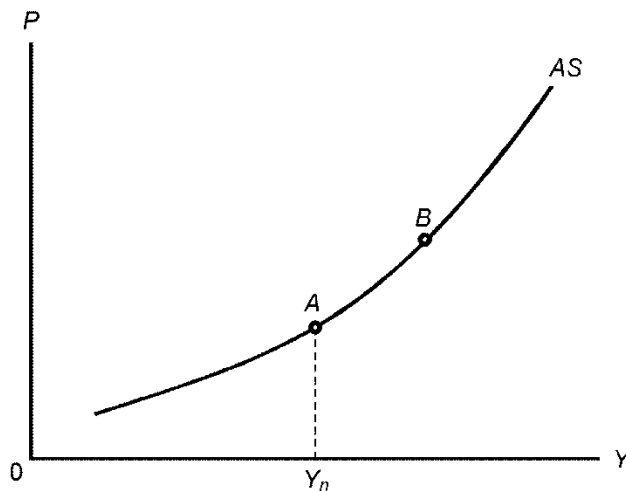


20. Which of the following statements are correct?

- At point c the actual price level is lower than the expected price level.
- At point b the output level is higher than the natural level of output.
- The real wage is the same at point a and point b .
- As the level of output increases the price level rises.
- The AS curve will shift up when the expected price level increases.

- a, b, c, d and e
- Only a, b, d and e
- Only b, c, d and e
- Only a, d and e
- Only a, b, c and d

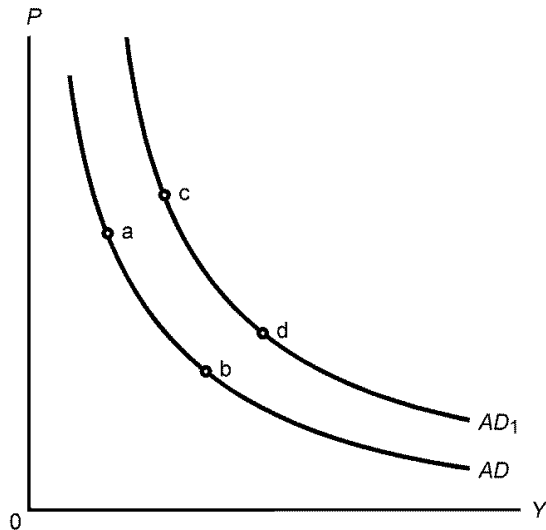
Questions 21 and 22 are based on the following AS curve:



21. At point B compared to point A the expected price level is ...
1. lower than the actual price level.
 2. higher than the actual price level.
 3. the same as the actual price level.
22. Which one of the following events describes the adjustment from the short to the medium to long run if the economy is at point B?
1. The expected price level is lower than the actual price level. Workers respond to this by increasing their nominal wage demands and the AS curve shifts down.
 2. The expected price level is higher than the actual price level. Workers respond to this by increasing their nominal wage demands and the AS curve shifts up.
 3. The expected price level is lower than the actual price level. Workers respond to this by increasing their nominal wage demands and the AS curve shifts up.
 4. The expected price level is higher than the actual price level. Workers respond to this by increasing their nominal wage demands and the AS curve shifts down.
23. Which of the following factors will cause an upwards shift of the AS curve?
- a. An increase in real wages.
 - b. An increase in the expected price level.
 - c. An increase in the actual price level.
 - d. A decrease in the nominal money supply.
 - e. A decrease in government spending.
1. Only factor b
 2. Factors a and b
 3. Factors c, d and e
 4. Factors b, d and e
 5. Only factor c

24. Which one of the following applies when the aggregate demand curve (AD-curve) is derived?
1. A decrease in the nominal money supply causes an increase in the interest rate which in return causes a decrease in investment spending, the demand for goods and the level of output.
 2. A decrease in the price level decreases the real money supply which causes an increase in the interest rate which in return causes a decrease in investment spending, the demand for goods and the level of output.
 3. An increase in the price level decreases the real money supply which causes an increase in the interest rate which in return causes a decrease in investment spending, the demand for goods and the level of output.
 4. An increase in government spending causes an increase in the interest rate which in return causes a decrease in investment spending, the demand for goods and the level of output.
25. Which of the following events is represented by the AD curve?
- a. $P \downarrow \rightarrow M/P \uparrow \rightarrow i \downarrow \rightarrow I \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$
 - b. $M^s \downarrow \rightarrow M/P \downarrow \rightarrow i \uparrow \rightarrow I \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$
 - c. $M^s \uparrow \rightarrow M/P \uparrow \rightarrow i \downarrow \rightarrow I \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$
 - d. $P \uparrow \rightarrow M/P \downarrow \rightarrow i \uparrow \rightarrow I \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$
1. Only a
 2. Only b
 3. Only c
 4. Only d
 5. a and d
26. Which of the following factors cause a shift in the AD curve?
- a. A change in wages.
 - b. A change in the price level.
 - c. A change in the nominal money supply.
 - d. A change in government spending.
1. Factors a, b and c
 2. Only factors b and d
 3. Only factors a and c
 4. Factors b, c and d
 5. Only factors c and d

Questions 27 and 28 are based on the following diagram:



27. Which of the following statements is/are correct?

Comparing point a with point b on curve AD the ...

- a. real money supply is higher at point b.
- b. interest rate is lower at point b.
- c. investment spending is higher at point b.
- d. government spending is higher at point b.
- e. demand for goods is higher at point b.

- 1. a, b, c, d and e
- 2. Only a, b, c and e
- 3. Only b, c and d
- 4. Only b, c and e
- 5. Not one of the options 1 to 4

28. Which of the following statements are correct?

Assume that the rightward shift of the AD is due to an expansionary fiscal policy. Comparing point b on curve AD with point d on curve AD₁ the ...

- a. level of government spending is higher at point d.
- b. level of taxation is higher at point d.
- c. demand for goods is higher at point d.
- d. interest rate is higher at point d.
- e. nominal money supply is higher at point d.

- 1. a, b, c and d
- 2. a, c and e
- 3. Only b, c and d
- 4. Only a, c and d
- 5. b and e

29. Which one of the following events describes the adjustment from the short to the medium to long run in the case of an expansionary monetary policy?

	Labour market	Financial market	Goods market
1.	$P^e < P: W \uparrow \rightarrow P \uparrow$	$M^s \downarrow \rightarrow M/P \downarrow \rightarrow i \uparrow$	$I \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$
2.	$P^e < P: W \downarrow \rightarrow P \downarrow$	$M/P \downarrow \rightarrow i \uparrow$	$I \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$
3.	$P^e > P: W \downarrow \rightarrow P \downarrow$	$M/P \uparrow \rightarrow i \downarrow$	$I \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$
4.	$P^e > P: W \uparrow \rightarrow P \uparrow$	$M/P \uparrow \rightarrow i \uparrow$	$I \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$
5.	$P^e < P: W \uparrow \rightarrow P \uparrow$	$M/P \downarrow \rightarrow i \uparrow$	$I \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$

30. Which one of the following events applies in the medium to long run in the case of an expansionary monetary policy in the labour market?

1. $P^e > P: W \uparrow \rightarrow P \downarrow$
2. $P^e < P: W \uparrow \rightarrow P \uparrow$
3. $P^e < P: W \downarrow \rightarrow P \downarrow$
4. $P^e > P: W \downarrow \rightarrow P \downarrow$
5. $P^e > P: W \uparrow \rightarrow P \uparrow$

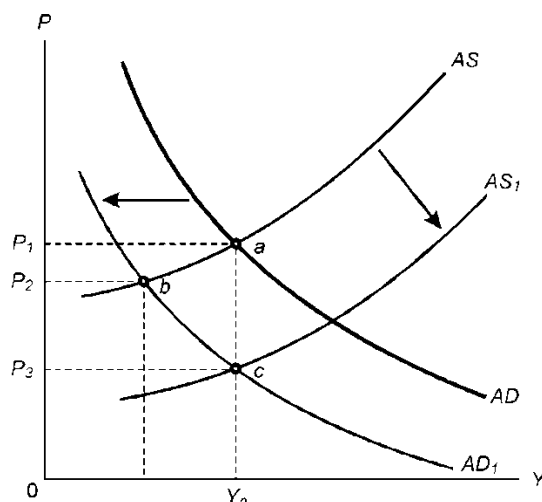
31. Which one of the following events applies in the medium to long run in the case of an expansionary monetary policy in the financial market?

1. $M/P \uparrow \rightarrow i \uparrow$
2. $M^s \downarrow \rightarrow M/P \downarrow \rightarrow i \uparrow$
3. $M/P \downarrow \rightarrow i \uparrow$
4. $M/P \uparrow \rightarrow i \downarrow$
5. $M/P \downarrow \rightarrow i \downarrow$

32. Which one of the following events applies in the medium to long run in the case of an expansionary monetary policy in the goods market?

1. $I \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$
2. $I \uparrow \rightarrow Z \downarrow \rightarrow Y \downarrow$
3. $I \uparrow \rightarrow Z \downarrow \rightarrow Y \uparrow$
4. $I \uparrow \rightarrow Z \uparrow \rightarrow Y \downarrow$
5. $I \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$

Question 33 is based on the following diagram which represents the impact of a contractionary fiscal policy:



33. Which of the following statements is/are correct?

- a. In the short run: the increase in the interest rate in the financial market will lead to a decrease in investment in the goods market, a decrease in the demand for goods and a decrease in the level of output and income. This is represented by a shift from AD to AD_1 .
 - b. The movement along the AD curve from point b to point c is the result of the events in the labour market in the short run.
 - c. In the medium run, the AS curve will shift from AS to AS_1 because of the following chain of events: $P^e \downarrow \rightarrow W \downarrow \rightarrow P \downarrow$.
 - d. At point c the level of output is at the natural level of output and all the real values are equal to their original values.
1. a, b, c and d
 2. Only b, c and d
 3. Only b, c, d and e
 4. Only c and d
 5. Only c

Case studies on learning units 5 to 7

Question 1

Question 1 is based on the following extract from the *Monetary Policy Review* June 2015. South African Reserve Bank. (2015). Pretoria:

"... monetary policy in South Africa remains in a tightening cycle... policy easing by the European Central Bank (ECB) and the Bank of Japan may support capital flows to emerging markets, further moderating the risk of an abrupt decline in emerging-market (EM) currency prices"

Which one of the following chain of events' illustrates the effect of the above extract on South Africa's trade balance.

1. $M \uparrow \rightarrow M/P \uparrow \rightarrow i \downarrow \rightarrow E \downarrow \rightarrow X \uparrow \rightarrow NX \uparrow$
2. $E \uparrow \rightarrow i \uparrow \rightarrow X \uparrow \rightarrow NX \uparrow$
3. $i \uparrow \rightarrow \text{Capital}_{\text{inflow}} \rightarrow E \uparrow \rightarrow X \downarrow \rightarrow NX \downarrow$
4. $i \downarrow \rightarrow \text{Capital}_{\text{outflow}} \rightarrow E \downarrow \rightarrow X \uparrow \rightarrow NX \uparrow$

Question 2

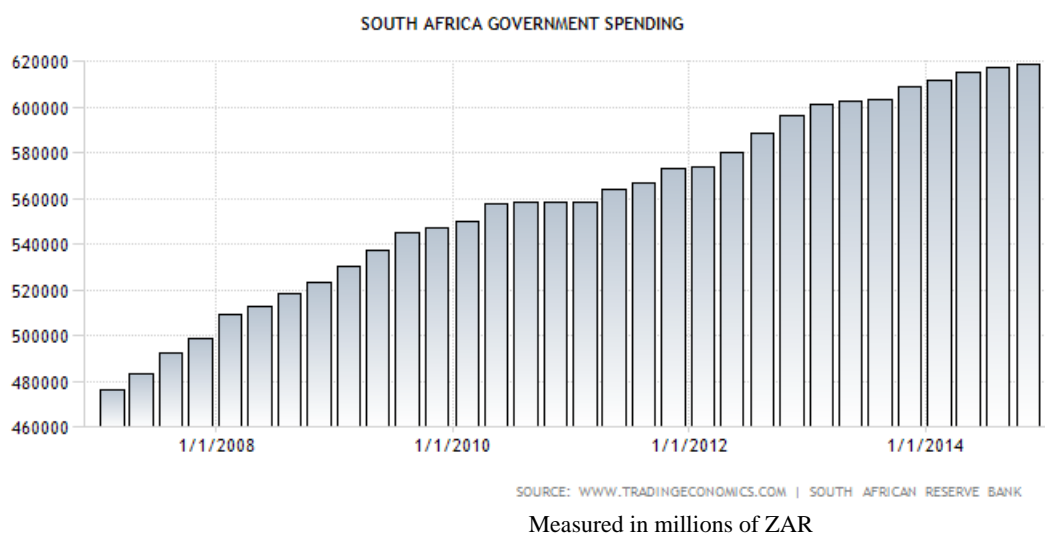
The following statements are based on information released in the SARBs *Monetary Policy Review* June 2015. Identify which of these statements will have a **positive** effect on South Africa's current account of the balance of payments:

2.
 - a. China's growth has slowed.
 - b. The price of iron ore has fallen by 65% from 2011 to the first quarter of 2015.
 - c. Sustained depreciation of the rand.
 - d. A reduction in OPECs monopoly power has seen a decline in the price of crude oil.
 - e. The non-tradable sector has expanded faster relative to the tradable sector. The tradable sector consists of those businesses that compete with foreign producers either domestically (import substitution) or abroad (exporting).
1. a, b, c, d and e
 2. Only a, b and d
 3. Only b and d
 4. Only c and d
 5. Only c and e

Case studies on learning units 8 and 9

Question 1

Question 1 is based on the following graph:



- a. Which stabilisation policy is represented by the data?
- b. Given the data and policy, what will happen in the AS-AD model? Explain in words and by using a chain of events and a diagram what will happen in the short run and in the medium run in the goods market, the financial market and the labour market.

Question 2

Read through the following and answer questions a and b that follow.

In 1999, the South African economy embarked on its longest expansion phase. It lasted for 99 months and come to an end in November 2007 and in the fourth quarter of 2008 the South African economy experienced an economic recession. (See figure 2).

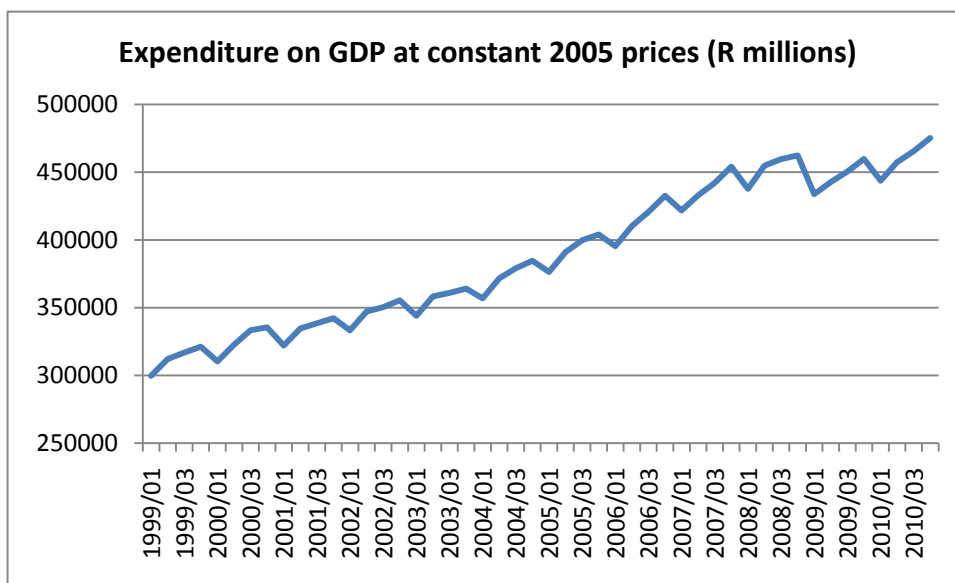


Figure 1

What triggered the end of the expansion phase and the economic recession in South Africa was falling house prices in the United States of America which led to the so-called “subprime mortgage” crisis. Preceding the crisis there was a rapid increase in mortgages to less creditworthy borrowers in America. A combination of falling house prices and default mortgage payments led to the failure and near failure of major financial institutions in America. This sent shockwaves across the financial markets of the world and resulted in a loss of confidence in financial markets and institutions, with the result that share prices fell sharply, investor confidence plunged and the availability of credit to firms and households were severely curtailed. This had the result that consumption spending by households and investment spending by firms declined worldwide which had a major impact on the level of output and income in the major economies of the world. Today this is referred to as the Great Recession.

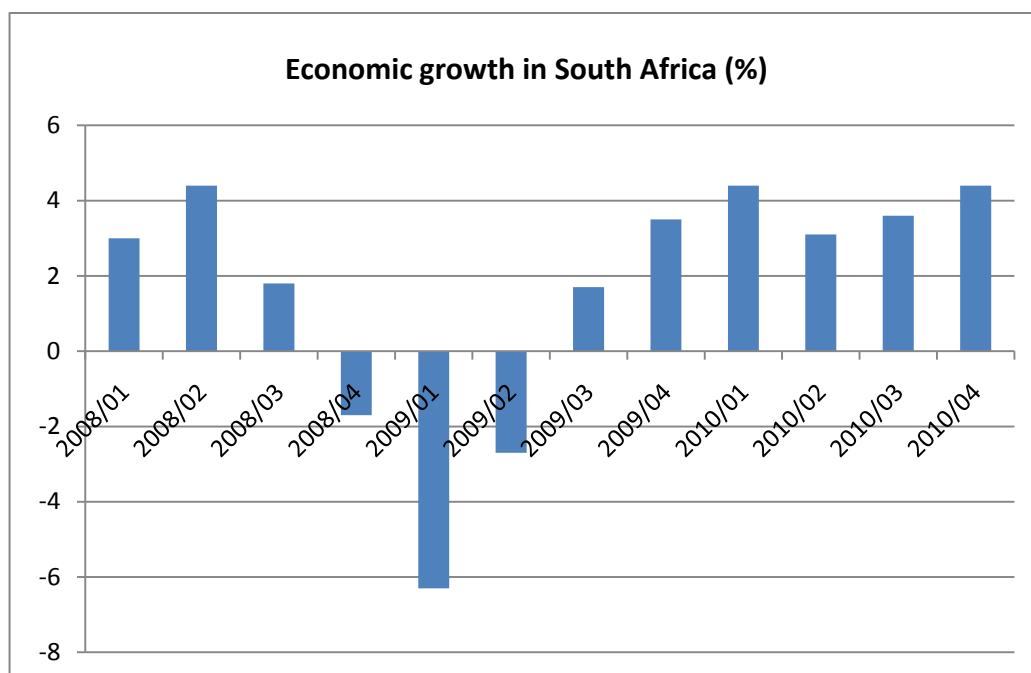


Figure 2

Due to the recession experienced by the major trading partners of South Africa there was a dramatic drop in our exports. In 2009 exports declined by 20% as shown in figure 3. The impact on the economy was worsened by a decline of both consumption spending and investment spending.

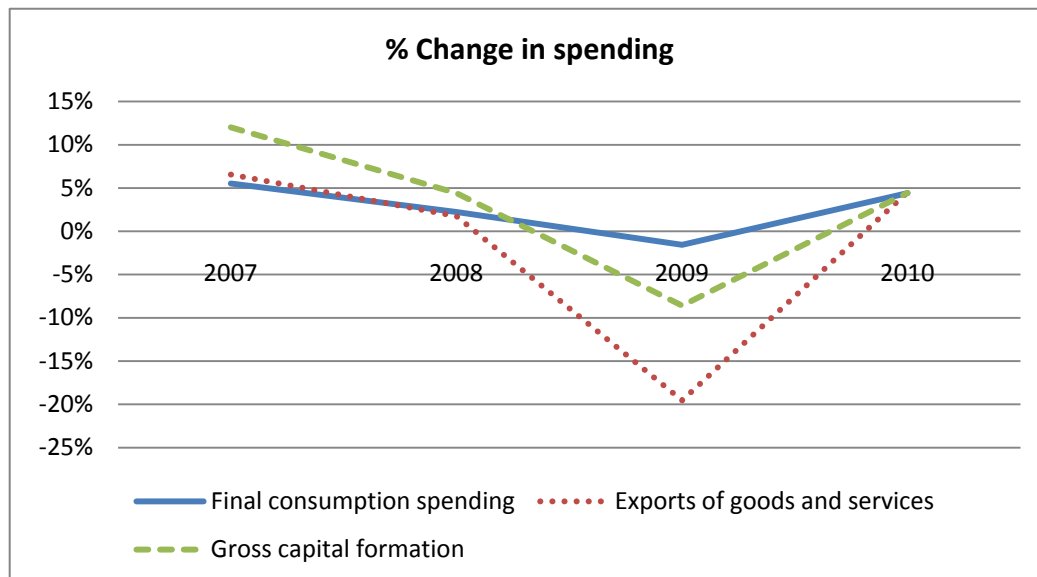


Figure 3

The recession could have been much worse. But it was met by a strong macroeconomic response, which certainly limited the depth and the length of the recession.

Take monetary policy first. In response to the economic slowdown the South African Reserve Bank started to decrease the repurchase rate. (Figure 4 shows the decline in the repurchase rate for the period 2008 to 2009.) In April 2008 the repurchase rate was 11.5% while at the end of 2009 it was 7%.

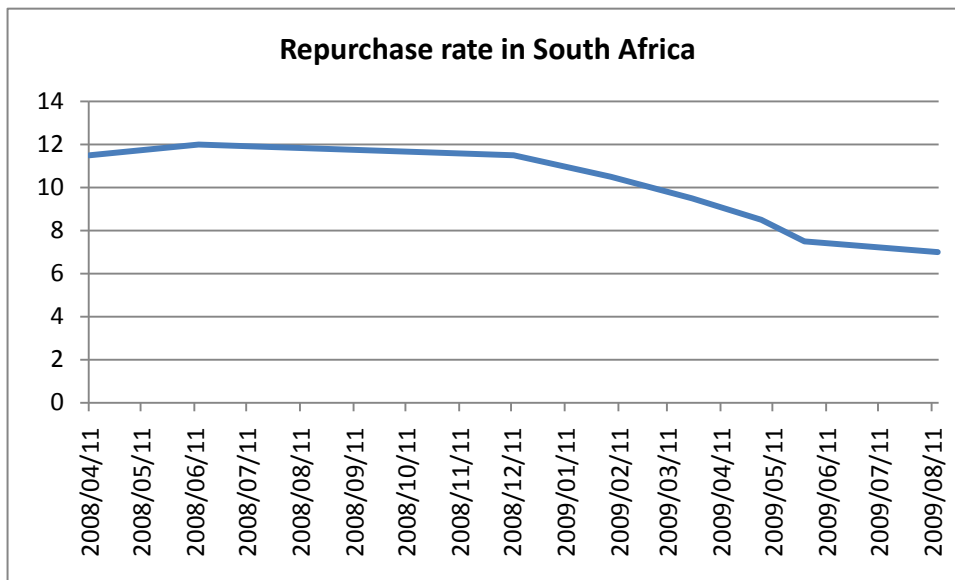


Figure 4

- a. Define the repurchase (repo) rate. Briefly explain the impact of a decrease in the repo rate on the money supply? Does it refer to a contractionary or expansionary monetary policy?
- b. Given the data and policy, what will happen in the AS-AD model? Explain in words and by using chain of events and a diagram what will happen in the short and medium run in the goods market, the financial market and the labour market.

Question 3

When comparing the impact of the two different policies (question 1 and question 2 above) in the AS-AD model, the impact in the medium run is different. Briefly explain why.

9 OTHER ASSESSMENT METHODS

My *Studies @ Unisa* brochure contains important information on the final year concession procedure (FI) to assist students with one or two modules outstanding for completion of their qualification. The Department of Examination Administration (DEA) will inform all students who qualify for a final year concession by sms/email.

10 EXAMINATIONS

For general examination guidelines and examination preparation guidelines, please refer to the *my Studies @ Unisa* brochure.

10.1 Examination period

This module is offered in a semester period of approximately 15 weeks. This means that if you are registered for the first semester, you will write the examination in May/June 2016 and the supplementary examination will be written in October/November 2016. If you are registered for the second semester you will write the examination in October/November 2016 and the supplementary examination will be written in May/June 2017.

During the semester, the Examination Section will provide you with information regarding the examination in general, examination venues, examination dates and examination times.

10.2 Examination paper

The format of the examination paper and guidelines on how to answer examination questions are discussed in detail in Tutorial Letter 103 which you will receive during the semester.

10.3 Previous examination papers

Some previous examination papers are available to students on *myUnisa* under the “official study material” folder and one example of a recent examination paper will be provided in Tutorial Letter 103. Should you make use of previous examination papers, we advise you not to focus on such old papers only as the content of the module and, therefore, examination papers may change from year to year. **To concentrate only on previous examination papers will not guarantee a pass.** You must be able to answer questions on all the prescribed work and learning unit outcomes as indicated in the Study guide (MO001).

Please revise all the learning units before trying to complete the examination papers. If you complete the papers do it under the same conditions as in the examination room. Therefore do not consult the study guide or any other help.

10.4 Tutorial letter with information on the examination

To help you in your preparation for the examination, you will receive Tutorial Letter 103 that will explain the format of the examination paper, give you examples of questions that you may expect and set out clearly what material you have to study for examination purposes.

11 FREQUENTLY ASKED QUESTIONS

The *my Studies @ Unisa* brochure contains an A-Z guide of the most relevant study information.

12 SOURCES CONSULTED

None.

13 CONCLUSION

Distance education is very tough on the student. It requires a lot of self-discipline, sacrifice and hard work. But it can be done!

Start early and work consistently throughout the semester. Do not leave it for the last two weeks before the examination. It is not possible to master the module in two weeks. You should at least spend a minimum of 8 hours per week on this module.

Work actively (with pen and paper) and make use of the activities in the workbook (TL102).

Do all the assignments. Start early by answering the questions as you finish the learning units.

Tell your family, friends and other students what you have learned in this module. Even if they don't understand it or are not interested.

Read and read and keep on reading (not only economics but other information as well).

We hope that you will enjoy this module and wish you all the best!