**ECS2602**

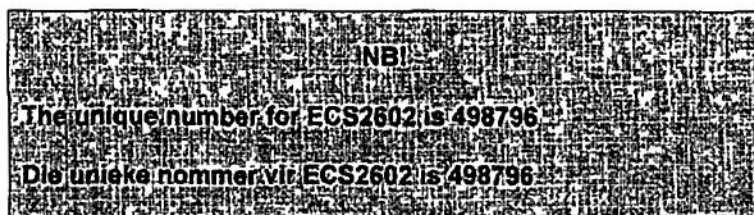
(498796)

October/November 2015
Oktober/November 2015**MACROECONOMICS
MAKRO-EKONOMIE**Duration 2 Hours
Tydsduur 2 Uur100 Marks
100 Punte**EXAMINERS / EKSAMINATORE .****FIRST / EERSTE****MRS/MEV MD UYS****SECOND / TWEEDE****MRS/MEV S KENNEDY-PALMER**Use of a non-programmable pocket calculator is permissible
Gebruik van 'n nie-programmeerbare sakrekenaar is toelaatbaar.Closed book examination
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This paper consists of 35 pages, instructions for the completion of a mark reading sheet and a special front page

Hierdie vraestel bestaan uit 35 bladsye, instruksies vir die voltooiing van 'n merkleesblad en 'n spesiale voorblad

STUDENT NUMBER / STUDENTENOMMER									

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The following abbreviations may appear in this examination paper

Die volgende afkortings mag in hierdie eksamenvraestel voorkom

ENGLISH

c	-	marginal propensity to consume
C	-	consumption spending
D _B	-	demand for bonds
E	-	nominal exchange rate
E ^e	-	expected nominal exchange rate
ε	-	real exchange rate
G	-	government spending
I	-	investment spending
i*	-	foreign interest rate
M ^d	-	demand for money
M ^s	-	supply of money
M/P	-	real money supply
NX	-	trade balance
P	-	price level
P _B	-	price of bonds
S _B	-	supply of bonds
W	-	nominal wage
W/P	-	real wage
X	-	exports
Y	-	output and income level
Y*	-	foreign output and income level
Y _N	-	natural level of output and income
Z	-	total demand
ZZ	-	demand for domestic goods

AFRIKAANS

c	-	grensverbruiksgeneigdheid
C	-	verbruiksbesteding
D _B	-	vraag na effekte
E	-	nominale wisselkoers
E ^e	-	verwagte nominale wisselkoers
ε	-	reele wisselkoers
G	-	owerheidsbesteding
I	-	investeringsbesteding
i*	-	buitelandse rentekoers
M ^d	-	vraag na geld
M ^s	-	aanbod van geld (geldvoorraad)
M/P	-	reele geldvoorraad
NX	-	handelsbalans
P	-	pryspeil
P _B	-	prys van effekte
S _B	-	aanbod van effekte
W	-	nominale loon
W/P	-	reele loon
X	-	uitvoer
Y	-	produksie- en inkompeil
Y*	-	buitelandse produksie- en inkompeil
Y _N	-	natuurlike produksiepeil
Z	-	totale vraag
ZZ	-	vraag na binnelandse goedere

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Read all instructions CAREFULLY before answering the questions
This paper consists of two (2) sections: A and B.

Lees al die instruksies NOUKEURIG voor u die vrae beantwoord
Hierdie vraestel bestaan uit twee (2) afdelings. A en B

SECTION A: COMPULSORY (50 marks)
AFDELING A VERPLIGTEND (50 punte)

INSTRUCTION ANSWER ALL THE QUESTIONS
INSTRUKSIE BEANTWOORD AL DIE VRAE

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QUESTION 1/VRAAG 1 (20 marks/20 punte)

Question 1 1/Vraag 1.1 (2 marks/2 punte)

The multiplier effect in the economy results from the behaviour of households. Briefly explain why.

(2)

Die vermenigvuldigerseffek vloei voort uit die gedrag van huishoudings. Verduidelik kortliks hoekom.

(2)

- As income and output rises, consumption spending rises and this causes the demand for goods to increase which, in turn, increases income and output and consumption spending.
- The process continues, hence multiplier effect.

CHAIN OF EVENTS: $Y \uparrow \rightarrow C \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow \rightarrow C \uparrow$

Question 1 2/Vraag 1.2 (5 marks/5 punte)

Taxes are part of autonomous spending in the goods market model.

Briefly explain why a decrease in taxes increases the demand for goods and shifts the demand for goods curve upwards in the goods market, equal to $c(T)$ and not T .

(5)

Belasting is deel van outonome besteding in die goederemarkmodel.

Verduidelik kortliks waarom 'n daling in die belasting die vraag na goedere verhoog en die goederevraagkromme opwaarts verskuif met gelyk aan $c(T)$ en nie T nie?

(5)

- It is because the initial effect of a change in taxes is on the disposable income of households, while a change

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in government spending directly influences the demand for goods.

- As disposable income changes, consumption spending changes, but the change in consumption spending is smaller than the change in disposable income because the mpc is less than one.

CHAIN OF EVENT : $T \downarrow \rightarrow Y_d \uparrow \rightarrow C \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$, but for G
if $G \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$,

Question 1.3/Vraag 1.3 (3 marks/3 punte)

Explain briefly in words why the net effect of an equal increase in government spending and taxes (in other words, the balanced budget) will still have a stimulatory effect on the level of output and income

(3)

Verduidelik kortliks in woorde waarom die netto effek van 'n gelyke toename in owerheids-besteding en belasting (met ander woorde, die begrotingsbalans) steeds 'n stimulerende effek op die produksie- en inkompeil sal uitoefen

(3)

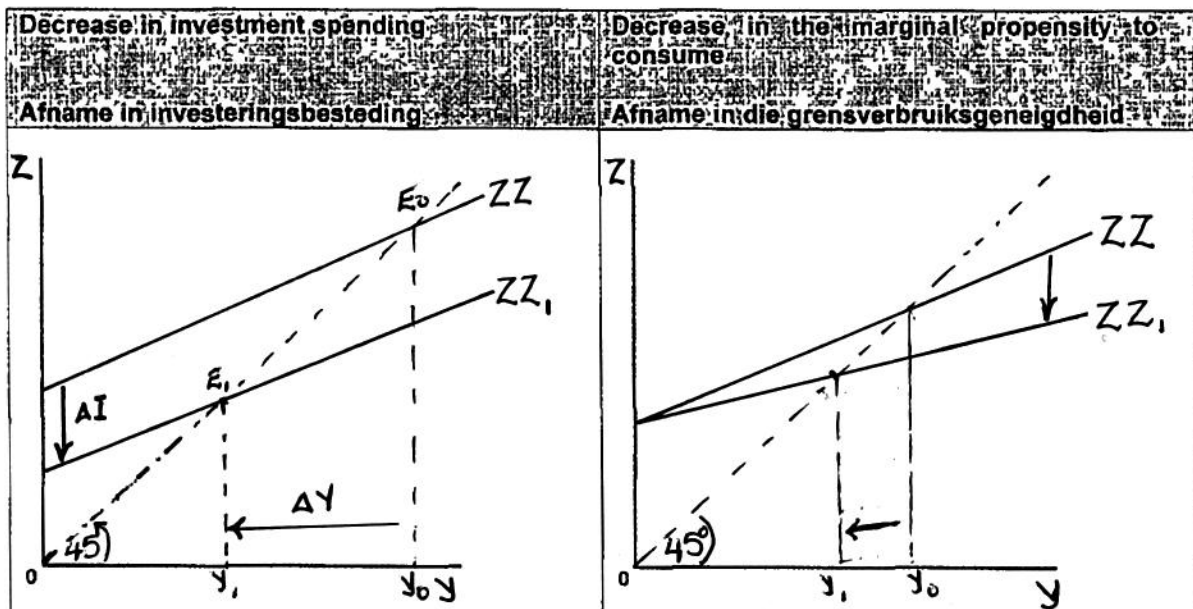
- The reason is that an increase in government spending has a direct impact on the demand for goods and the level of output and income while a change in taxes influence the demand for goods and output and income through household behaviour as captured by the consumption function.

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Question 1 4/Vraag 1 4 (4 marks/4 punte)

By using the two diagrams below show the difference between a decrease in investment spending and a decrease in the marginal propensity to consume on the equilibrium output and income level in the goods market model (4)

Maak gebruik van die twee onderstaande diagramme om die verskil aan te toon tussen 'n afname in investeringsbesteding en 'n afname in die grensverbruiksgeneigdheid op die ewewigsproduksie- en inkompeel in die goederemarkmodel (4)



PLEASE NOTE: THAT THE ARROWS SHOWING ΔZ IN GRAPHS AND ΔY IN Y ARE VERY IMPORTANT.

Question 1 5/Vraag 1.5 (6 marks/6 punte)

(a) What institution issues treasury bills? (1)

(a) Watter instansie reik skatkiswissels uit? (1)

• Government / National Treasury

• South African Reserve Bank, also acceptable since its the issuing agent.

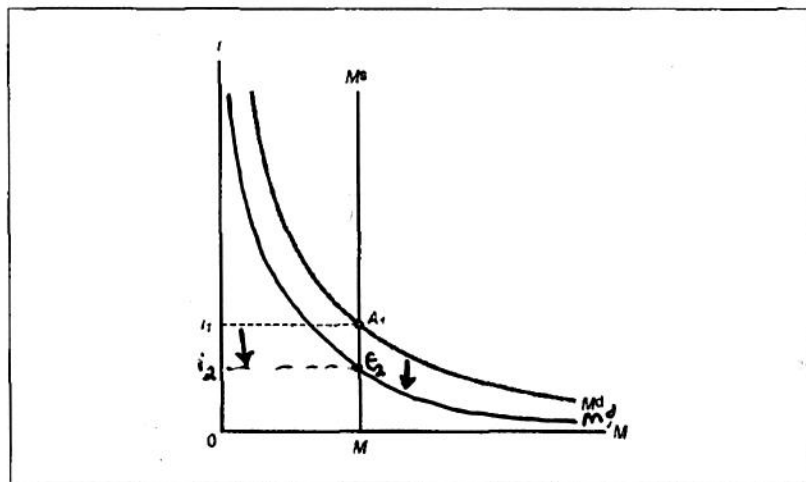
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- (b) Use the following diagram to illustrate on the diagram and briefly explain in words why a decrease in the level of output and income causes a decrease in the equilibrium interest rate (5)
- (b) Gebruik die onderstaande diagram om op die diagram te illustreer en kortliks in woorde te verduidelik waarom 'n afname in die produksie- en inkompeil 'n daling in die ewewigsrentekoers tot gevolg het (5)



Explanation/Verduideliking

- A decrease in income decreases the demand for money for transaction purposes.
- At the existing interest rate (i_1), an excess supply of money develops in the economy because people wish to hold less money for transaction purposes than before.
- to get rid of the excess money, financial market participants buy bonds, concurrently, the supply of bonds (treasury bills) decrease and this increases the price of treasury bills, and hence the interest rate decrease.

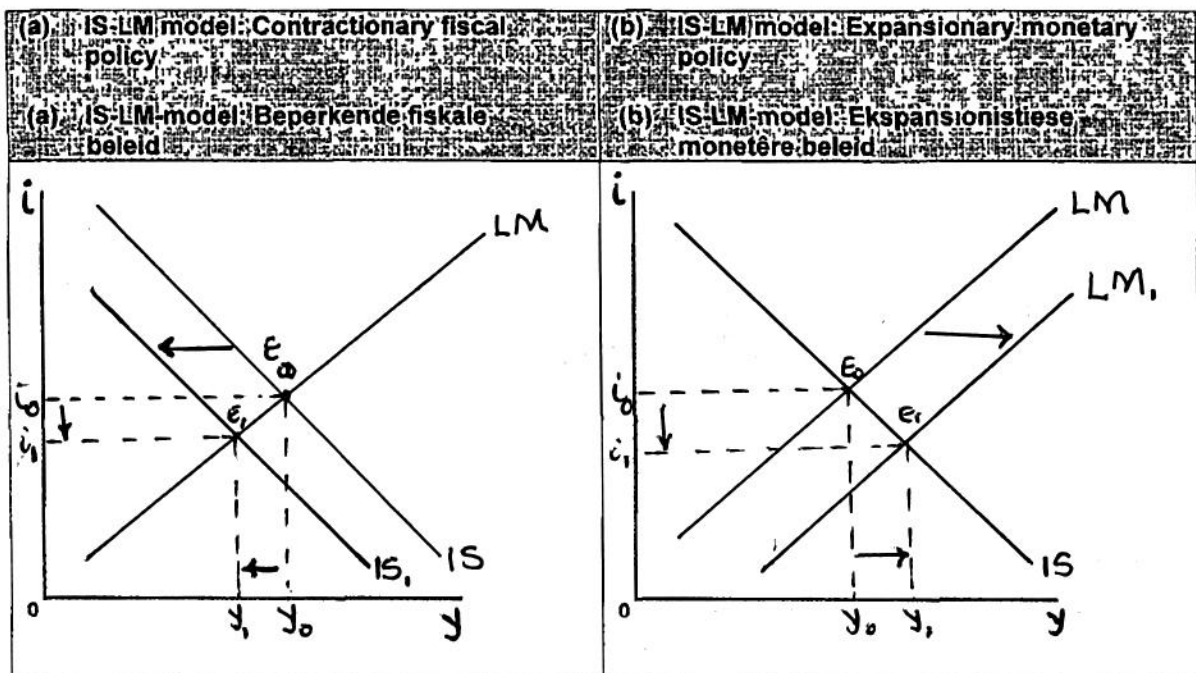
CHAIN OF EVENTS: $Y \downarrow \rightarrow M^d \downarrow \rightarrow P_b \uparrow \rightarrow i \downarrow$

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QUESTION 2/VRAAG 2 (6 marks/6 punte)

Use an IS-LM model to illustrate on the diagrams below and to compare the impact of a contractionary fiscal policy with that of an expansionary monetary policy (6)

Maak gebruik van 'n IS-LM-model om die impak van 'n beperkende fiskale beleid op die onderstaande diagramme te illustreer en te vergelyk met dié van 'n ekspanisionistiese monetêre beleid (6)



Comparison/Vergelyking

and understanding

To answer this question, knowledge of the policies is necessary.

To bring the points together, you may start by writing down the chain of events. However, answering along the following lines would be necessary and sufficient.

So, the first step is chain of events, to identify factors affected.

(a) Contractionary Fiscal Policy.

Goods Market: $G \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$ or $T \uparrow \rightarrow Y \downarrow \rightarrow C \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$

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Financial Market

$Y \downarrow \rightarrow M^d \downarrow \rightarrow i \downarrow$

Expansionary Fiscal Policy.

$M^s \uparrow \rightarrow Y \uparrow \rightarrow i \downarrow$

$i \downarrow \rightarrow I \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$

Comparison :

- Under a contractionary fiscal policy, the demand for goods decrease due to a decrease in government spending and/or ~~there~~ increase in taxes, and this leads to lower level of output and income; while under an expansionary monetary policy, there will be lower interest rates that leads to higher investment and hence higher level of output and income.
- Interest rates are lower under contractionary fiscal policy due lower demand for money, whilst under expansionary monetary policy they are also lower, but due to higher supply for money.
- Higher income and lower interest rates under expansionary monetary policy results higher level of investment whilst under contractionary fiscal policy it is uncertain due to lower interest rates ~~but~~ and lower level of income.

QUESTION 3/VRAAG 3 (13 marks/13 punte)**Question 3 1/Vraag 3 1 (6 marks/6 punte)**

Using the following diagrams, indicate what happens to the level of output and income and the trade balance if

- Exports increase
- Government spending increases
- Compare the results in (i) and (ii) above regarding the level of output and income and the trade balance

Clearly indicate the shifts of and/or movements along the curves on the diagrams

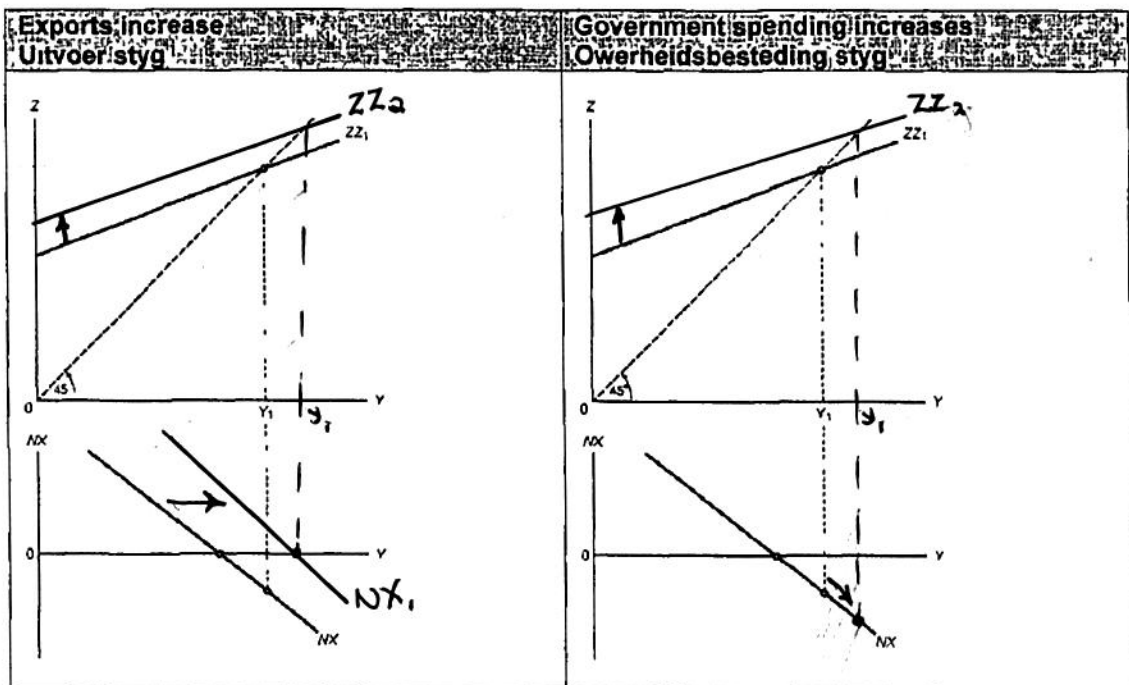
(6)

Gebruik die onderstaande diagramme om aan te toon wat sal gebeur met die produksie- en inkompeil en die handelsbalans indien

- Uitvoer styg
- Owerheidsbesteding styg
- Vergelyk die resultate in (i) en (ii) hierbo met betrekking tot die produksie- en inkompeil en die handelsbalans

Toon duidelik die verskuiwings en/of bewegings langs die krommes op die diagramme aan

(6)



Explanation/Verduideliking

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Impact on output and income

(i) Increase in exports
 $X \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$

(ii) Increase in Government Spending
 $G \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$

(c)

Impact on trade balance

(i) Increase in exports

• $X \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow \rightarrow IM \uparrow \rightarrow NX \downarrow$

• $X \uparrow \rightarrow NX \uparrow$

• positive effect of X on NX dominates

• $\therefore NX \uparrow$ (trade balance improves)

(ii) Increase in Government Spending

$G \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow \rightarrow IM \uparrow \rightarrow NX \downarrow$ (deteriorate)

Comparison/Vergelyking

• In both cases the level of output and income (Y) is higher

• An increase in exports results in an improvement in the trade balance while an increase in government spending results in a deterioration of the trade balance.

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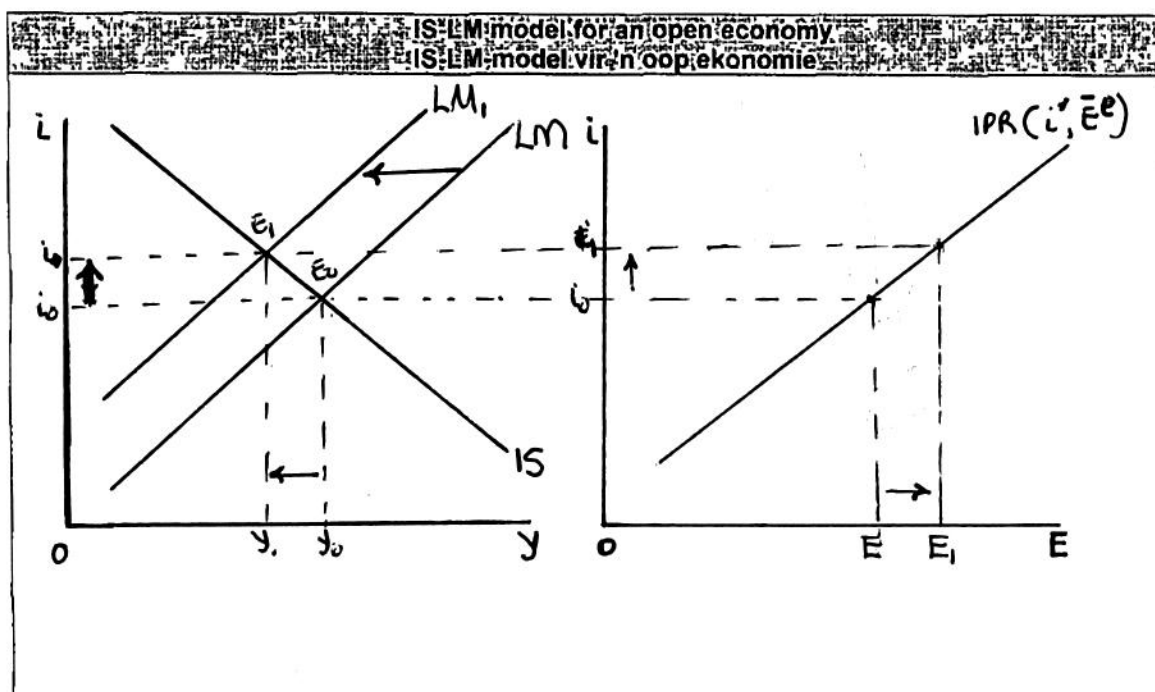
Question 3.2/Vraag 3 2 (7 marks/7 punte)

Draw a diagram of the IS-LM model for an open economy in the space below to indicate what will happen to the nominal exchange rate if a contractionary monetary policy is applied. Explain the impact of this policy on the financial market, the goods market, the exchange rate and trade balance by using chain of events and/or words

(7)

Trek 'n diagram van die IS-LM-model vir 'n oop ekonomie in die spasie hieronder om aan te toon wat sal met die nominale wisselkoers gebeur indien 'n beperkende monetêre beleid toegepas word. Verduidelik die impak van hierdie beleid op die finansiële mark, die goederemark, die wisselkoers en die handelsbalans deur gebruik te maak van gebeurtenis-kettings en/of woorde

(7)



Explanation/Verduideliking

Impact on the Financial Market

 $M \downarrow \rightarrow \frac{M}{P} \downarrow \rightarrow i \uparrow$

Impact on Goods Market

 $i \uparrow \rightarrow I \downarrow \rightarrow Z \downarrow \rightarrow y \downarrow$ $y \downarrow \rightarrow I \downarrow$ [TURN OVER]
[BLAAI OM]

Impact on exchange rate and trade balance

$i \downarrow \rightarrow \text{capital inflow} \rightarrow E \uparrow \rightarrow X \downarrow \rightarrow NX \downarrow;$
 $E \uparrow \rightarrow IM \uparrow \rightarrow NX \downarrow$

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QUESTION 4/VRAAG 4 (11 marks/11 punte)

Question 4 1/Vraag 4 1 (5 marks/5 punte)

- (a) Identify the three factors that impact on the nominal wage in the wage-setting relationship $W = p^e F(u, z)$ (3)
- (a) Identifiseer die drie faktore wat 'n uitwerking het op die nominale loon in die loonvasstellingsverwantskap (3)

- (1) Expected Price Level
- (2) unemployment
- (3) institutional factors

- (b) Briefly explain why it is not possible for labour to increase the real wage through nominal wage bargaining (2)
- (b) Verduidelik kortliks waarom dit nie moontlik vir arbeid is om die reele loon te verhoog deur nominale loonbedinging nie (2)

• if labour bargain for higher nominal wages, firms respond by increasing the price level, thus leaving the real wage unchanged.

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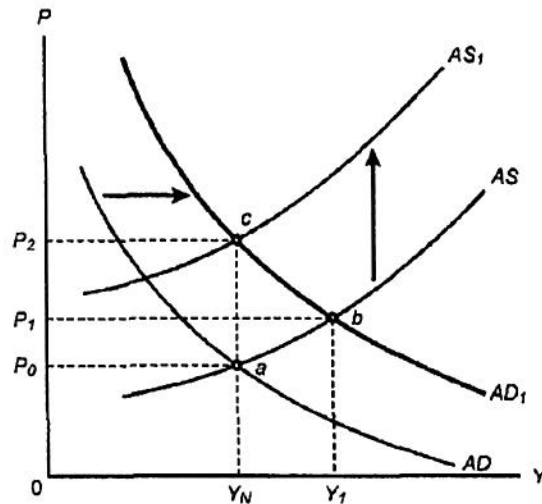
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Question 4 2/Vraag 4.2 (6 marks/6 punte)

Use the following AS-AD model to answer the question below

Maak gebruik van die onderstaande AS-AD-model om die vraag hieronder te beantwoord



Assuming that the rightward shift of the AD curve from AD to AD₁ is caused by an increase in government spending. Explain the impact of this action on the **goods market**, the **financial market** and the **labour market** in the medium to long run (the movement from point b to c) (6)

Veronderstel die regswaartse verskuiving van die AD-kromme van AD na AD₁ is deur 'n toename in owerheidsbesteding veroorsaak. Verduidelik die impak van die aksie op die **goederemark**, die **finansiele mark** en die **arbeidsmark** op die medium tot lang termyn (die beweging van punt b na punt c) (6)

Explanation/Verduideliking

- Question required impact of 'action' in the medium to long run.
- It is expected that you know short-run events before you start to explain medium to long run events.
- Medium - to - long run starts with expected price level in the labour market.
- the following was the expected answer:

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~~Medium to Long Run .~~
 ~~$p \uparrow \rightarrow y \uparrow \rightarrow p \uparrow$~~

Medium to Long Run
Labour Market

$p \uparrow \rightarrow w \uparrow \rightarrow p \uparrow$

Financial and Goods Mkt

$p \uparrow \rightarrow \frac{M}{P} \downarrow \rightarrow i \uparrow \rightarrow I \downarrow \rightarrow Z \downarrow \rightarrow y \downarrow$

SECTION B: COMPULSORY (50 marks)

THE ENGLISH VERSION OF THE MULTIPLE CHOICE QUESTIONS STARTS ON PAGE 18
THE AFRIKAANS VERSION OF THE MULTIPLE CHOICE QUESTIONS STARTS ON PAGE 27

INSTRUCTIONS

In this section ALL questions must be answered on the **mark reading sheet** which is supplied
Carefully follow the instructions for the completion of a mark reading sheet.

- (i) Suppose a question reads as follows

An increase in the level of production

- 1 decreases the level of income in the economy
- 2 has no impact on the level of income in the economy
- 3 increases the level of income in the economy
- 4 causes firms to employ less factors of production

The correct answer is 3 You must therefore mark 3 on your mark reading sheet

- (ii) Only one of the alternatives per question – listed as 1, 2, etc – is correct You must therefore not mark more than one alternative per question
- (iii) For a correct answer you receive **2½ marks** No marks are deducted for incorrect answers
- (iv) Section B consists of 20 questions and thus counts 50 marks out of the total of 100

Your mark reading sheet may get lost. You MUST therefore also write your answers to this section in page 26 of your examination answer book, for example 1(4), 2(3), 3(1), etc.

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AFDELING B VERPLIGTEND (50 punte)**DIE AFRIKAANSE MEERKEUSEVRAE BEGIN OP BLADSY 27****INSTRUKSIES**

In hierdie afdeling moet AL die vrae op die merkleesblad wat voorsien is, beantwoord word. **Volg die instruksies vir die voltooiing van 'n merkleesblad sorgvuldig**

- (i) Veronderstel 'n vraag lees soos volg

'n Styging in die produksiepeil

- 1 verminder die inkompeil in die ekonomie
- 2 het geen invloed op die inkompeil in die ekonomie
- 3 verhoog die inkompeil in die ekonomie
- 4 veroorsaak dat firmas minder produksiefaktore in diens neem

Die korrekte antwoord is 3. U moet dus 3 op u merkleesblad merk

- (ii) Slegs een van die alternatiewe per vraag, gelys as 1, 2, ens is korrek. U moet dus nie meer as een alternatief per vraag merk nie
- (iii) Vir 'n korrekte antwoord ontvang u **2½ punte**. Geen punte word vir verkeerde antwoorde afgetrek nie
- (iv) Afdeling B bestaan uit 20 vrae en tel dus 50 punte uit die totaal van 100

U merkleesblad mag wegraak. U MOET dus ook u antwoorde op hierdie afdeling op bladsy 35 in u eksamenantwoordboek neerskryf, byvoorbeeld 1(4); 2(3); 3(1); ens.

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SECTION B COMPULSORY (50 marks)

The unique number for ECS2602 is 498796

- 1 Which of the following statements with regards to the consumption function $C = c_0 + cY_D$ are correct?
- a A change in the marginal propensity to consume will result in a change in consumption ✓
 - b A change in income will change the marginal propensity to consume ✗
 - c A change in consumption will cause a change in disposable income ✗
 - d c_0 and c are the exogenous variables in the consumption function ✓
 - e Y_D is the endogenous variable in the consumption function ✓
- ☒ 1 Only a, d and e
☐ 2 Only b, d and e
☐ 3 Only a, b, d and e
☐ 4 Only a and d
☐ 5 a, b, c, d and e

Question 2 is based on the following information regarding a goods market model for a closed economy with a government sector

$$\begin{aligned}
 c &= 0.6 \\
 c_0 &= 400 \\
 I &= 300 \\
 G &= 300 \\
 T &= 100
 \end{aligned}$$

$$\begin{aligned}
 &= \frac{1}{1-0.6} \times 400 + 300 + 300 - 60 \\
 &= 2.5 \times 400 + 300 + 300 - 60 \\
 &= 2350
 \end{aligned}$$

- 2 The multiplier is equal to ____ and the equilibrium level of output and income is equal to ____

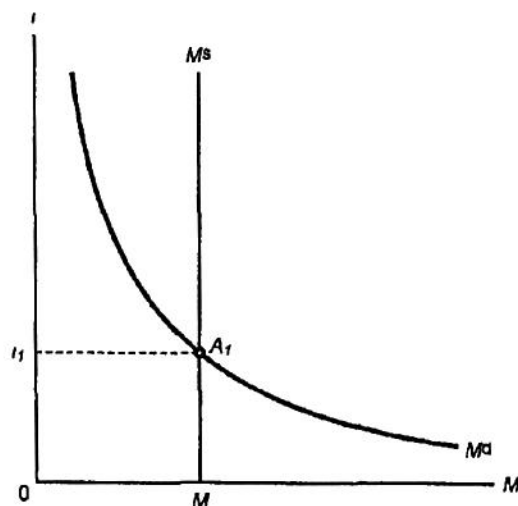
- | | | |
|------------------------------------|-------|---------|
| 1 | 6 | 5 640 |
| 2 | 2.5 ✓ | 2 500 |
| 3 | 4 | 3 840 |
| 4 | 6 | 5 400 |
| ☒ 5 | 2.5 ✓ | 2 350 ✓ |

- 3 The impact on the equilibrium interest rate of an increase in income with simultaneous expansionary open market operations by the central bank is

- ☐ 1 a lower equilibrium interest rate
☐ 2 a higher equilibrium interest rate
☒ 3 uncertain (the equilibrium interest rate can be higher, lower or the same)

[TURN OVER]
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Question 4 is based on the following diagram



4 Which of the following statements is/are correct?

- a If the central bank wishes to increase the interest rate in the economy it sells bonds on the open market and the M^s curve shifts to the left ✓
- b If the central bank wishes to increase the interest rate in the economy it buys bonds on the open market and the M^s curve shifts to the left ✗
- c The demand for money function (or M^d curve) will shift because of changes in the interest rate and there will be a movement along the curve because of changes in income ✗
- d The demand for money function (or M^d curve) will shift because of changes in income and there will be a movement along the curve because of changes in the interest rate ✓

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

[TURN OVER]
[BLAAI OM]

5 If the financial market is in a liquidity trap

- a monetary policy is ineffective in bringing about a decrease in the interest rate ✓
- b financial money market participants are willing to hold less money at the same interest rate ✗
- c a decrease in the interest rate can be brought about by buying of bonds by the central bank ✗
- d there is a high demand for bonds ✗

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

people do not prefer bonds,
they fear capital loss
people prefer holding money
monetary policy useless

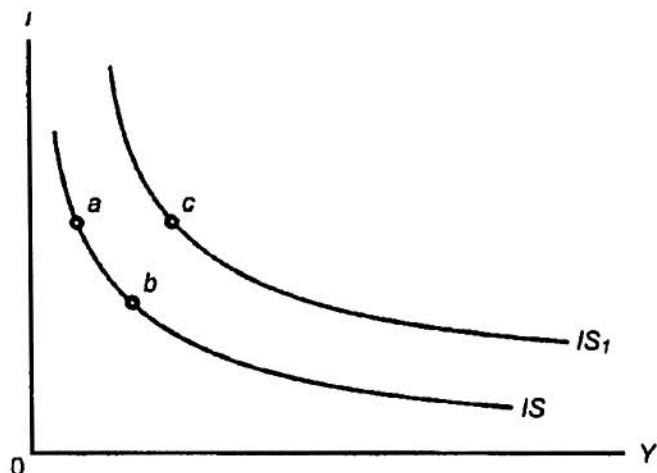
6 Which of the following statements is/are correct?

- a To derive the IS curve, we change the level of output and income to determine the effect on the interest rate ✗
- b To derive the IS curve, we change the interest rate to determine the effect on the demand for goods ✓
- c To derive the LM curve, we change the level of output and income to determine the effect on the interest rate ✓
- d To derive the AD curve, we change the price level to determine the effect on the level of output and income ✓

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

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Question 7 is based on the following diagram



7 Which one of the following statements is correct?

- 1 Goods market equilibrium exists only at points a and b
- 2 At point c the level of autonomous spending is lower than at point a
- 3 At point c the level of autonomous spending is the same as at point a
- 4 At point a the demand for goods is lower than at point b

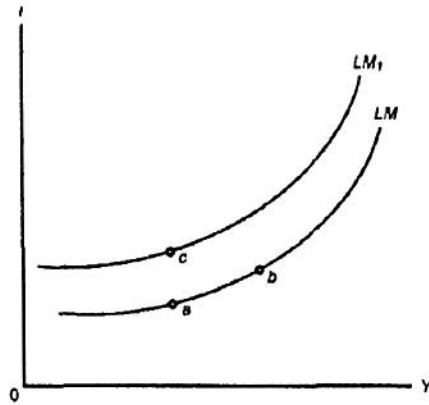
8 Which one of the following statements is **INCORRECT**?

- 1 The steepness of the IS curve depends on the interest sensitivity of investment spending and the output and income sensitivity of investment spending ✓
- 2 The size of the multiplier and the income sensitivity of the demand for money are factors that will have an impact on the effectiveness of fiscal policy ✓
- 3 A relatively more inelastic IS curve indicates a greater interest sensitivity of investment spending ✓
- 4 "Crowding out" of investment spending will occur if the output and income sensitivity of investment spending is low and the interest sensitivity of investment spending is high ✓

incorrect

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Study the following LM curve and answer question 9 that follows



9 Which of the following statements is/are correct?

- a At point a the demand for money is higher than at point b ✓
 - b At point c the money supply is higher than at point a ✗
 - c At point a, point b and point c the financial market is in equilibrium ✓
- 1 a, b and c
 - 2 Only a
 - 3 Only b
 - ④ Only c
 - 5 Only a and c

- 10 Which one of the following policy actions in the IS-LM model is appropriate if the objectives are to decrease the budget deficit and decrease the interest rate? — *expa. monetary policy*
- 1 An expansionary fiscal policy and an expansionary monetary policy
 - 2 An expansionary fiscal policy and a contractionary monetary policy
 - ③ A contractionary fiscal policy and an expansionary monetary policy
 - 4 An expansionary fiscal policy and a contractionary fiscal policy
 - 5 It is not possible to achieve the policy objectives

11 Which one the following statements is correct?

The exogenous variables in the IS-LM model are

- 1 government spending and investment spending ✗
- 2 investment spending and money supply ✗
- 3 interest rate and government spending ✗
- ④ government spending and money supply ✗
- 5 level of output and income and the interest rate ✗

[TURN OVER]
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- 12 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

- 13 Given the following information

Interest rate on RSA bonds 6%
Interest rate on USA bonds 9%

3% in favour of USA

Which one of the following statements is correct?

- 1 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
 - 2 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
 - ③ 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
 - 4 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
- 14 In an open economy the impact of an increase in the interest rate on the demand for goods and the level of output and income in the goods market 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 $E \downarrow \rightarrow X \uparrow \rightarrow NX \uparrow \rightarrow Z \uparrow \rightarrow Y \uparrow$
- 4 $I \uparrow \rightarrow I \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow \rightarrow NX \downarrow$

[TURN OVER]
[BLAAI OM]

Question 15 is based on the following information Country ABC is facing a recession and an unacceptable budget deficit To deal with the budget deficit taxes are raised and to deal with the recession the money supply is increased

balanced
budget
can do

15 Which of the following statements is/are correct?

- LM right IS left*
- a The IS curve will shift to the right and the LM curve will shift downwards
 - b The IS curve will shift to the left and the LM curve will shift downwards ✓
 - c The results of these policy actions are that the interest rate increases, a capital inflow occurs, the domestic currency appreciates and the trade balance worsens
 - d The results of these policy actions are that the interest rate declines, a capital outflow occurs, the domestic currency depreciates and the trade balance improves ✓

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

16 Which of the following statements is/are correct?

According to the price-setting relation a(n)

- a ✓ decrease in the unemployment rate, will increase nominal wage demands
- b ✓ decrease in the markup of firms, given the nominal wage, will decrease the price per unit
- c decrease in the nominal wage, given the markup of firms, will increase the price per unit
- d increase in the unemployment rate, will decrease nominal wage demands

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

$$P = \frac{W}{1} (1 + \frac{m}{1})$$

17 Which of the following statements is/are correct?

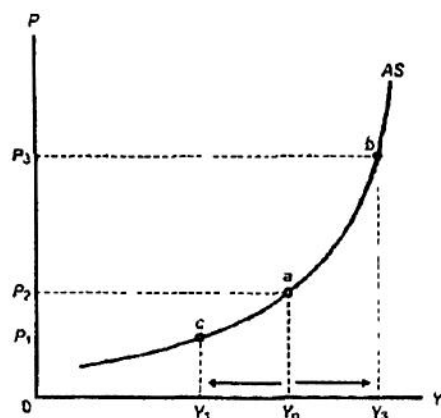
The natural rate of unemployment

- a ✓ increases if there is an increase in the bargaining position of workers
- b ✗ increases if there is a decrease in the markup
- c ✗ decreases if there is an improvement in the protection of workers through labour legislation
- d ✗ increases if the unemployment rate increases

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

[TURN OVER]
[BLAAI OM]

Question 18 is based on the following diagram



*properties of AS
refer to previously
done papers in
pack*

18 Which one of the following statements is **INCORRECT**?

- 1 At point c the actual price level is lower than the expected price level ✓
- 2 At point b the output level is higher than the natural level of output ✓
- 3 At point b the real wage is the higher compared to point a *real wage is constant*
- 4 As the level of output increases the price level rises
- 5 The AS curve will shift upwards when the expected price level increases

19 The chain of events $P \uparrow \rightarrow (M/P) \downarrow \rightarrow i \uparrow \rightarrow I \downarrow \rightarrow Z \downarrow \rightarrow Y \downarrow$ represents the

- 1 IS relation in the open economy
- 2 effect of a monetary expansion in the AS-AD model
- 3 derivation of the AD curve
- 4 effect of an expansionary fiscal policy in the AS-AD model
- 5 LM relation in the open economy

20 The neutrality of money refers to the impact of a _____ policy which means that only _____ variables changes in the AS-AD model in the medium to long run

- | | | |
|---|-------------------------|---------|
| 1 | contractionary monetary | nominal |
| 2 | contractionary monetary | real |
| 3 | expansionary monetary | nominal |
| 4 | expansionary monetary | real |
| 5 | expansionary fiscal | nominal |

[TURN OVER]
[BLAAI OM]