

**MERU UNIVERSITY OF SCIENCE AND TECHNOLOGY**

**P.O. Box 972-60200 – Meru-Kenya.**

**Tel: 020-2069349, 061-2309217. 064-30320 Cell phone: +254 712524293, +254 789151411**

**Fax: 064-30321**

**Website:** [**www.must.ac.ke**](http://www.must.ac.ke) **Email:** **info@must.ac.ke**

**University Examinations 2014/2015**

FIRST YEAR, SECOND SEMESTER EXAMINATION FOR THE DEGREE OF BACHELOR OF COMMERCE, BACHELOR OF PURCHASING AND SUPPLIES MANAGEMENT, BACHELOR OF BUSINESS ADMINISTRATION, BACHELOROF SCIENCE INFORMATION TECHNOLOGY, BACHELOR OF SCIENCE ECONOMICS, BACHELOR OF STATISTICS AND BACHELOR OF ACTURIAL SCIENCE

**BEC 3150: PRINCIPLES OF MACROECONOMICS**

**DATE: APRIL 2015 TIME:** $2 $**HOURS**

**INSTRUCTIONS:** *Answer question* ***one*** *and any other* ***two*** *questions*

**QUESTION ONE (30 MARKS)**

1. Label each of the following statements TRUE, FALSE or UNCERTAIN and justify your answer with a short explanation.
2. When the marginal propensity to consume increases and investment decreases, goods market equilibrium output increases. (2 Marks)
3. An increase in the price of good that is imported into Kenya –holding all other prices and quantities fixed-will tend to increase the GDP deflator in Kenya. (2 Marks)
4. A fall in population always increases the value of per capita GDP. (2 Marks)
5. A fall in sales reduces the value of GDP. (2 Marks)
6. What is a savings function? Describe the savings function giving an explanation of all components of the function. (4 Marks)
7. Describe the three approaches to measurement of national income in an economy.(6 Marks)
8. Describe the different kinds of money. ( 4 Marks)
9. Distinguish between the following terms:
10. Real and Nominal Interest Rate (4 Marks)
11. Net exports and Net Capital Outflows (4 Marks)

**QUESTION TWO (20 MARKS)**

1. What is the meaning of the following terms?
2. Nominal exchange rate (2 Marks)
3. Real exchange rate (2Marks)
4. Describe in detail the theory of purchasing power parity. (10 Marks)
5. Suppose purchasing parity holds, what would happen to the nominal exchange rate (domestic to foreign rate) in the following cases:
6. The price level at home is constant while the price level abroad is falling.(3 Marks)
7. The price level at home is falling but prices abroad are falling at a faster rate. (3Marks)

**QUESTION THREE (20 MARKS)**

1. Define the following terms as used in macroeconomics;

 (i) The marginal propensity to consume (MPC). (2 Marks)

(ii) The marginal propensity to save (MPS) (2 Marks)

1. The Keynesian multiplier. (2 Marks)
2. The figure below shows the goods market equilibrium in a given economy.

Using information provided in the figure determine the following:

1. The marginal propensity to consume (MPC) (2 Marks)
2. The marginal propensity to save (MPS) (2 Marks)
3. The Keynesian multiplier (2 Marks)
4. Autonomous spending (2 Marks)
5. Equilibrium GDP (2 Marks)
6. Suppose government expenditure increase by 50 and taxes fall by 20, what is the change in autonomous spending and equilibrium GDP? (4 Marks)

**QUESTION FOUR (20 MARKS)**

1. Define the meaning of the following:
2. Laspeyres index (2 Marks)
3. Pasches index (2 Marks)
4. In using the CPI as a measure of the cost of living, state the problem that is illustrated by each of the following situations and explain your answer.
5. The invention of the mobile phone (2 Marks)
6. The introduction of airbags in cars (2 Marks)
7. Increased purchase of personal computers as a result in the decline of their price. (2 Marks)
8. In the Lake Victoria Island of Migingo, the only activity residents care about is fishing. All they produce and consume are paddle boats and fishing nets. In the year 2009, they spend 400,000/= on 8 boats and 20,000/= on 5 fishing nets. In the year 2010, they spend 600,000/= on 12 boasts and 30,000/= on 6 fishing nets.
9. Using 2009 as the base year and fixing the basket of goods at one boat and 2 fishing nets, compute the rate of inflation between 2009 and 2010 using the CPI.(4 Marks)
10. Compute inflation between 2009 and 2010 using the GDP deflator. (4 Marks)
11. Is there a difference between the rates of inflation computed using the CPI and the deflator? Why or why not? (2 Marks)

**QUESTION FIVE (20 MARKS)**

1. What does each of the following terms mean as used in central banking?
2. A fractional reserve banking system (2Marks)
3. The reserve ratio (2 Marks)
4. The money multiplier (2 Marks)
5. You take Ks. 100 you had kept under your mattress and deposit it in your bank account. It this Ksh.100 stays in the banking system as reserves and if banks hold reserves equal to 10 percent of deposits, by how much does the total amount of deposits in the banking system increase? By how much does the money supply increase? (4 Marks)
6. The Central Bank conducts a Ksh. 10 million open-market purchase of government bonds.If the required reserve ratio is 10 percent, what is the largest possible increase in the money supply that could result? Explain. What is the smallest possible increase? Explain. (4 Marks)
7. Assume that the reserve requirement is 5 percent. All other things equal, will the money supply expand more if the Central Bank buys Ksh. 2,000 worth of bonds or if someone deposits in a bank Ksh 2,000 that he had been hiding in his flower pot? If one creates more, how much more does it create? Support your thinking. (6 Marks)