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**SCHOOL OF ACCOUNTING AND BUSINESS**  
**BSc. (APPLIED ACCOUNTING) GENERAL / SPECIAL DEGREE**  
**PROGRAMME**

**YEAR II SEMESTER II**  
**END SEMESTER EXAMINATION – AUGUST 2015**

**BEC 20225 Macroeconomics**

Date : 10th August 2015  
Time : 5.30 p.m. - 8.00 p.m.  
Duration : Two and a half (02 ½) Hours

**Instructions to Candidates:**

- Paper consists of three Parts (I, II, and III)
- Part I – Answer **ALL** questions in the separate sheet provided.  
Part II – Answer **FOUR** questions out of five.  
Part II – Answer **ONE** questions out of two.
- The total marks for the paper is 100.
- The marks for each question are shown in brackets.
- Answers should be written neatly and legibly.

## PART I

### MULTIPLE CHOICE QUESTIONS

All Questions of this section are compulsory

1. Which of the following statements is **correct**?
  - A. **Real GDP** is the total market value of all final goods and services produced in a country during a year valued in the prices of a base year.
  - B. An individual buying stock in the stock market is an example of **investment spending**
  - C. **Potential Real GDP** is always greater than **Equilibrium Real GDP**
  - D. Social security and welfare are examples of spending on **infrastructure**.
  - E. Exports, taxes, and public investment are example of **injections** in an economy.
2. The period of the **business cycle** in which **real GDP is increasing** is called the:
  - A. Expansion
  - B. Peak
  - C. Recession
  - D. Trough
  - E. Stagflation
3. A type of **unemployment** in which workers are switching in-between jobs or are searching for new and better jobs is called \_\_\_\_\_ unemployment:
  - A. Frictional
  - B. Cyclical
  - C. Structural
  - D. Seasonal
  - E. Voluntary
4. Which of the following is a "loser" from **unexpected inflation**?
  - A. Workers with cost of living allowances
  - B. People who own Treasury Bills
  - C. The middle class who borrowed funds for consumption
  - D. People who own homes and have fixed-rate mortgages
  - E. People who purchased diamonds and gold jewelry

5. If the nominal interest rate on a deposit account is 2% and the inflation rate is 3% this year, the **real interest rate** is:
- A. 5%
  - B. 2%
  - C. 2/3%
  - D. -1%
  - E. 3%
6. Which of the following would cause the **aggregate demand** curve to **shift to the right**?
- A. An increase in purchases by the central government
  - B. An increase in real interest rates
  - C. An appreciation of the American dollar
  - D. A decrease in the money supply
  - E. A recession in the foreign export markets
7. At an income of Rs.100,000, I spent Rs.90,000 on consumer goods. When my income rose to Rs.200,000, I spent Rs.160,000 on consumer goods. My **marginal propensity to consume** is:
- A. 0.9
  - B. 0.8
  - C. 0.7
  - D. 1
  - E. Rs.70,000
8. Assume that Equilibrium GDP is Rs.4,000 billion. Potential GDP is Rs.5,000 billion. The marginal propensity to consume is  $\frac{4}{5}$  (0.8). By how much and in what direction should **government purchases** be changed?
- A. Increase by Rs1,000 billion
  - B. Increase by Rs.100 billion
  - C. Decrease by Rs.1,000 billion
  - D. Increase by Rs. 200 billion
  - E. Decrease by Rs. 500 billion

9. The **Phillips curve** describes the relationship between:
- A. The central government budget deficit and the trade deficit
  - B. Savings and investment
  - C. The unemployment rate and the inflation rate
  - D. Marginal tax rates and tax revenues
  - E. The unemployment rate and the interest rate
10. An **increase in the money supply** causes:
- A. Interest rates to fall, investment spending to rise, and aggregate demand to rise
  - B. Interest rates to rise, investment spending to rise, and aggregate demand to rise
  - C. Interest rates to rise, investment spending to fall, and aggregate demand to fall
  - D. Interest rates to fall, investment spending to fall, and aggregate demand to fall
  - E. Interest rates to fall, investment to stay the same, and aggregate demand to stay the same

## PART II

Answer **any FOUR (04)** questions

### **Question No. 01**

The macroeconomic data pertaining to an open economy are given below. All figures are in Million Rupees.

$$\text{Consumption Spending } C = 200 + 0.75Y_d$$

$$\text{Disposable income } T_d = Y - T + R$$

Y = National Income,

T (Taxation) = 60

R (Government Transfers) = 40

I (Private Investment) = 130

G (Government Purchases) = 60

X (Exports) = 75

M (Imports) 50

- a. Calculate the equilibrium national income of the economy
- b. What is the value of government spending multiplier and the tax multiplier of this economy?
- c. What is the nature of the government budget of this economy? What would be the impact of this budget on the national income?
- d. Calculate the consumption expenditure at equilibrium
- e. Explain what are injections and withdrawals of an open economy?

**(Total 15 Marks)**

**Question No. 02**

- a. Illustrate the four phases of a business cycle in a diagram and discuss the output gaps
- b. Why do business cycles arise in a market economy? How would do you reduce the impact of the business cycle using fiscal policy?
- c. What is meant by a depression? How does it differ from a recession?

**(Total 15 Marks)**

**Question No. 03**

- a. Explain what is meant by the equilibrium of the IS and LM curves
- b. Show how is the impact of an expansionary fiscal policy and an expansionary monetary policy differ in the ISLM framework
- c. What is meant by crowding out impact? Explain how to minimize the impact of crowding out effect?

**(Total 15 Marks)**

**Question No. 04**

- a. Describe the causes for inflation using appropriate diagrams.
- b. How inflation affects the economy? Explain
- c. What are the main causes for unemployment?

**(Total 15 Marks)**

**Question No. 05**

- a. Explain the sources of comparative advantage
- b. Outline the conclusions of the Ricardian and Heckscher-Ohlin theories
- c. Discuss the arguments for and against free trade

**(Total 15 Marks)**

### **PART III**

Answer **only ONE (01)** question

#### **Question No. 01**

Identify the weaknesses of the export and import structure of Sri Lanka and propose remedial measures to address the weaknesses

**(Total 20 Marks)**

#### **Question No. 02**

Sri Lankan political parties are famous for setting ambitious targets without resources to achieve them. Discuss the key macroeconomic proposals outlined in the election manifesto of a political party of your choice for the general election in August 2015 and comment on how feasible those proposals are.

**(Total 20 Marks)**