MID-WESTERN UNIVERSITY

FACULTY OF MANAGEMENT

FINAL EXAMINATION: 2073

BACHELOR OF BUSINESS ADMINISTRATION (BBA)

SEMESTER – II

Subject: Macro Economics Course Code: MGMT 325

Full Marks: 100 Time: 3:00 Hours

*You are required to answer in your own words as far as applicable. The figures in the margin indicate full marks.*

**SECTION B: SHORT ANSWER QUESTIONS (8** $×$ **5 = 40 MARKS)**

*Answer any EIGHT questions:*

1. What is GDP? Distinguish between GDP and GNP. [2+3]
2. Define IS curve. Derive it graphically. [2+3]
3. What are instruments of monetary policy? Explain them briefly. [5]
4. Briefly describe budget formulation process in Nepal. [5]
5. Explain basic issues of macroeconomics. [5]
6. Construct CPI number for the year 2015 from the data given below. Find inflation rate. [2.5+2.5]

|  |  |  |
| --- | --- | --- |
| Commodity | Base Year 2014 | Price In 2015 |
| Price P0 | Quantity Q0 |
| Orange | 12 | 15 | 16 |
| Mango | 15 | 10 | 18 |
| Apple | 17 | 8 | 19 |

1. Suppose consumption and investment functions are as C = 20 + 0.5Y and I = 200 - 2,000i

Find the equilibrium level of income at interest rate 8% and 6%. [5]

1. In an economy, investment expenditure is increased by Rs. 700 core. The marginal propensity to consume is 0.9. You are required to:

a) Calculate coefficient of multiplier. [2]

b) Calculate total increase in income. [1.5]

c) Calculate total increase in consumption. [1.5]

1. Derive tax multiplier mathematically and calculate coefficient of tax multiplier if MPC= 0.8. [5]
2. Calculate National income from the following data. [5]

|  |  |
| --- | --- |
| Particulars  | Rs. (In Crore) |
| Private consumption expenditure | 5,000 |
| Gross private investment | 2,500 |
| Government expenditure | 1,500 |
| Export | 500 |
| Import | 1,500 |
| Depreciation | 900 |
| Net factor income abroad | 2,000 |
| Indirect taxes | 1,000 |
| Subsidies | 500 |
|  |  |

**SECTION C: LONG ANSWER QUESTIONS (3** $× $**10 = 30 MARKS)**

*Answer any THREE questions:*

1. Explain use of macroeconomics in business decision making. [10]
2. What is effective demand? Explain Keynesian theory of effective demand. [2+8]
3. Show your acquaintance with the general equilibrium of product market and money market under IS-LM framework. [10]
4. What is demand pull inflation? What are its causes? Explain. [2+8]
5. Explain Keynesian income determination model in two sector economy. [10]

**SECTION D: CASE STUDY (15 MARKS)**

1. *Read a case given below and answer the following questions:*

***Increasing Government Purchases to Stimulate the Economy: The Obama Spending Plan***

When President Barack Obama took office in January 2009, the economy was suffering from a significant recession. Even before he was inaugurated, the president and his advisers proposed a sizable stimulus package to increase aggregate demand. As proposed, the package would cost the federal government about $800 billion, or about 5 percent of annual GDP. The package included some tax cuts and higher transfer payments, but much of it was made up of increases in government purchases of goods and services.

Professional economists debated the merits of the plan. Advocates of the Obama plan argued that increased spending was better than reduced taxes because, according to standard Keynesian theory, the government-purchases multiplier exceeds the tax multiplier. The reason for this difference is simple: when the government spends a dollar, that dollar gets spent, whereas when the government gives households a tax cut of a dollar, some of that dollar might be saved. According to an analysis by Obama administration economists, the government purchases multiplier is 1.57, whereas the tax multiplier is only 0.99. Thus, they argued that increased government spends- ing on roads, schools, and other infrastructure was the better route to increase aggregate demand and create jobs.

Other economists were more skeptical about the plan. One concern was that spending on infrastructure would take time, whereas tax cuts could occur more immediately. Infrastructure spending requires taking bids and signing contracts, and, even after the projects begin, they can take years to complete. The Congressional Budget Office estimated that only about 10 percent of the outlays would occur in the first nine months of 2009 and that a large fraction of outlays would be years away. By the time much of the stimulus went into effect, the recession might be well over.

In addition, some economists thought that using infrastructure spending to promote employment might conflict with the goal of obtaining the infrastructure that was most needed. Here is how Gary Becker, the Nobel Prize–winning economist, explained the concern on his blog*: Putting new infrastructure spending in depressed areas like Detroit might have a big stimulating effect since infrastructure building projects in these areas can utilize some of the considerable unemployed resources there. However, many of these areas are also declining because they have been producing goods and services that are not in great demand, and will not be in demand in the future. Therefore, the overall value added by improving their roads and other infrastructure is likely to be a lot less than if the new infrastructure were located in growing areas that might have relatively little unemployment, but do have great demand for more roads, schools, and other types of long-term infrastructure.*

While Congress debated these and other concerns, President Obama responded to critics of the bill as follows: “So then you get the argument, well, this is not a stimulus bill, this is a spending bill. What do you think a stimulus is? That’s the whole point. No, seriously. That’s the point.” The logic here is quintessentially Keynesian: as the economy sinks into recession, the government is acting as the demander of last resort. In the end, Congress went ahead with President Obama’s proposed stimulus plans with relatively minor modifications. The president signed the $787 billion bill on February 17, 2009.

1. Why did Obama choose the increase in government purchase rather than tax cut policy to give stimulus to US economy? Explain. [5]
2. What is positive aspect of tax cut policy? Explain. [5]
3. Which policies are proposed in Obama's plan to stimulate the US economy? [5]

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