



**AFRICA  
UNIVERSITY**

*(A United Methodist-Related Institution)*

***"Investing in Africa's Future"***

**FACULTY OF MANAGEMENT AND ADMINISTRATION**

**COURSE TITLE: MEC102 ECONOMIC PRINCIPLES 2**

**SEMESTER 2: FINAL EXAMINATION 2016**

**LECTURER: MR P.SIKANDA**

**TIME: 3 HOURS**

***INSTRUCTIONS***

Answer **ALL** questions in Section A. Answer **ANY THREE** questions in Section B.

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Start each question on a new page in your answer booklet.

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The marks allocated to each question are shown at the end of the question.

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Show all your workings.

## SECTION A: ANSWER ALL THE QUESTIONS

- 1(a) Briefly explain an four objectives of macroeconomic policy (8 marks)
- (b) What do you understand by the term "natural rate of unemployment"? (1 mark)
- (c) During the Contraction Phase of business cycle, there is a depression and recession. Define a recession (1 mark)
- d) Define the marginal propensity to consume, the marginal propensity to save, the average propensity to consume and the average propensity to save. Again also explain their behavior in relationship to either income or savings. (5 marks)
- e) Define and distinguish between Gross Domestic Product and Gross National Product. Again also state the formula for calculating Gross National Product (3 marks)
- f) Give any three main usages of the national production data and in what ways may national incomes statistics understate the actual living standards in an economy (5 marks)
- g) Why is the long-run aggregate supply vertical? (2 marks)

**SECTION B (ANSWER ANY THREE (3) QUESTIONS IN THIS SECTION)**  
Each question has a total of 25 marks

2(a) The following data is for country X

	2011		2012		2013	
	P	Q	P	Q	P	Q
Good A	\$30	900	\$31	1 000	\$36	1050
Good B	\$100	192	\$102	200	\$100	205

Using the data given above and using the incomplete table below:

- Compute nominal GDP in each year. **(3 marks)**
- Compute real GDP in each year using 2011 as the base year. **(3 marks)**
- Use your previous answers to compute the GDP deflator in each year. **(3 marks)**
- Use GDP deflator to compute the inflation rate from 2011 to 2012, and from 2012 to 2013. **(2 marks)**

	Nominal GDP	Real GDP	GDP Deflator	Inflation rate
2011	?	?	?	N/a
2012	?	?	?	?
2013	?	?	?	?

- Calculate the rate of growth in real GDP between year 2012 and 2013 using answers obtained in (ii) above. **(1 mark)**
- b(i) Define a multiplier **(1 mark)**
- In a Two Sector Model or Simple Keynesian Model, derive the multiplier and name the multiplier for the model. **(4 marks)**
- (c) Given an open economy macroeconomics model with the following structural equations:
- $$Y = C + I + G + X - M$$
- $$C = 800 + 0.6Y_d$$
- $$T = 0.2Y$$
- $$I = 2\,000$$
- $$G = 1\,000$$
- $$X = 3\,000$$
- $$M = 1\,000 + 0.2Y$$
- Find the value of total autonomous expenditures **(2 marks)**
  - State the values of the marginal propensities to consume and import **(2 marks)**

- (iii) Find the equilibrium level of income.(4 marks)
- 3(a) The Zimbabwean National Statistics Agency (Zimstats) estimated that Zimbabwe's unemployment rate is 6%.If the population 15 years of age and over is 12 million and the labour force is 9 million,
- (i) Define an unemployed person and state the formulae for calculating unemployment rate(2 marks)
  - (ii) How many people are unemployed (1mark)
  - (iii) What is Zimbabwe's labour force participation rate?(2 marks)
- b(i) Unemployment arises for frictional, structural, and cyclical reasons.Describe three types of unemployment.(5 marks)
- (ii) From the three types of unemployment, which one(s) should the government be worried more of and why?(3 marks)
- (c) Using a clearly labelled diagram, explain demand-pull inflation (5 marks)
- (d) Besides demand pull inflation, explain any other two factors that cause inflation(4 marks)
- (e) In Zimbabwe the government and economists are worried about deflation continual being experienced in the economy for the period 2015 to 2016, yet inflation should be of concern. Briefly explain why deflation is of concern in an economy like Zimbabwe.(3 marks)
- 4(a) State and explain briefly any three functions of money (6 marks)
- (b) How does inflation affect each of the functions of money?(3 marks)
- (c) How do commercial banks create money? Explain the two tools that can be used by the Central Bank to control money creation by commercial banks. [6 marks]
- (d) Using the quantity theory of money whileindicating all your assumptions, show how does the quantity of money trigger inflation. (5 marks)
- (e) According to John Maynard Keynes, a famous English economist, money demand exists for three main reasons.State and explain any two motives for holding or demanding money(4 marks)

- (f) Given that the central bank has pegged the rate of required reserve at 10% for banks, calculate the money multiplier. **(1 mark)**
- 5(a) Define the following terms:
- (i) Discretionary fiscal policy **(2 marks)**
  - ii) Expansionary fiscal policy **(2 mark)**
  - (iii) Crowding out effect **(3 marks)**
- b) What is an automatic fiscal stabilizer? Use an example in your explanation **(2 marks)**
- c) Suppose the Zimbabwean government is worried of sustained economic recession
- (i) Using AD-AS framework, explain what is meant by a recessionary gap? Include the causes and reveal its undesirability in your analysis **(6 marks)**
  - (ii) With the aid of diagrams, demonstrate how the Classical and the Keynesians would remove recessionary gaps in the AD-AS Model while clearly stating your policy objectives. (State their assumptions about the economy). How effective will be both fiscal and monetary policy in attaining your goals. **(10 marks)**
- 6(a) List all the items which forms contents or recordings of balance of payments accounts **(4 marks)**
- (b) (Exports – imports) is the main constituent of Current Account Balance (CAB) hence it has huge bearing on CAB balance. What do you understand by the term trade deficit? State and explain one possible consequence for a country continually running in trade deficit **(3 marks)**
- (c) State any two possible causes of current account deficit being experienced in Zimbabwe for the period 2015- 2016. **(3 marks)**
- (d) How can a government rectify or deal with a current account deficit? **(4 marks)**
- (e) Besides free floating exchange rate, state and explain any other two types of exchange rate determination you know of. **(4 marks)**
- (f) Discuss the merits and demerits of floating exchange rate determination **(6 marks)**
- (g) Define deflation **(1 mark)**