



# CENTRAL UNIVERSITY

**RESIT EXAMINATION: 2016/2017**

**FACULTY OF ARTS AND SOCIAL SCIENCES**

**DEPARTMENT OF ECONOMICS**

**ECON 202 (3 CREDITS)**

**PRINCIPLES OF ECONOMICS II**

**LEVEL 200**

**JULY, 2017**

**DURATION: 2 HOURS**

STUDENT ID No.....

## INSTRUCTIONS

ANSWER ALL QUESTIONS IN SECTION A AND ONE (1) QUESTION EACH IN SECTIONS A AND B

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THE INVIGILATOR

LECTURER: Paragon POMEYIE

**SECTION A: OBJECTIVE TEST – 60 marks**  
**Answer all questions in this section**

1. If in an economy gross domestic product increases precautionary demand for money
  - a. increases
  - b. decreases
  - c. fluctuates
  - d. remains constant
  
2. When bond prices are increasing it is an indication that the interest rate is
  - a. decreasing
  - b. increasing
  - c. constant
  - d. unaffected
  
3. The following are qualities of a good tax system **except**
  - a. economy
  - b. convenience
  - c. equity
  - d. affordable
  
4. Which of the following problems is not common to all three approaches to national income accounting
  - a. changing prices of goods and services
  - b. depreciation
  - c. multiple counting
  - d. fringe benefits
  
5. The following are factors determines the level of private savings **except**
  - a. inflation rate
  - b. stock of durable goods on hand
  - c. level of disposable income
  - d. government spending
  
6. The 45<sup>0</sup> line is also referred to as
  - a. aggregate demand equals aggregate supply identity
  - b. aggregate demand equals aggregate consumption identity
  - c. aggregate demand equals aggregate output identity
  - d. gross output equals net output identity
  
7. Which of the following equations shows equilibrium national income in an open economy?
  - a.  $AE = C + I + G$
  - b.  $Y = C + I + G$
  - c.  $Y = C + I + G + X - M$
  - d.  $AE = C + I + G + X - M$

8. Average Propensity Save is equal to
- $C/Y_d$
  - $\Delta C/\Delta Y_d$
  - $S/Y_d$
  - $\Delta S/\Delta Y_d$
9. Which of the following is a leakage of spending?
- net taxes
  - consumption
  - investment
  - net national product
10. Which of the following equations depicts injections in an open economy?
- $J = I + G + X$
  - $L = S + T + M$
  - $Y = C + S + T$
  - $AE = C + I + G + X - M$
11. A fall in taxation
- raises equilibrium national income
  - lowers equilibrium national income
  - equates national output with AE curve
  - equates NNP and GNP
12. A rise in import
- raises equilibrium national income
  - lowers equilibrium national income
  - equates national output with AE curve
  - equates NNP and GNP
13. A rise in investment
- raises equilibrium national income
  - lowers equilibrium national income
  - equates national output with AE curve
  - equates NNP and GNP
14. A fall in government expenditure
- raises equilibrium national income
  - lowers equilibrium national income
  - equates national output with AE curve
  - equates NNP and GNP
15. An increase in government expenditure
- shifts AE function upward

- b. shifts AE function downward
  - c. shifts AS function aside
  - d. leaves AE function unaltered
16. A fall in injections causes the AE curve to
- a. remain unchanged
  - b. shift to the left
  - c. shift upwards
  - d. shift downwards
17. An increase in leakages will cause AE function to
- a. shift upward
  - b. shift downward
  - c. fall along the  $45^\circ$  line
  - d. rise along the  $45^\circ$  line
18. A financial market involved in the mobilization of short term funds is known as
- a. money market
  - b. capital market
  - c. stock market
  - d. bonds market
19. Given that the MPC is 0.8, calculate the autonomous investment multiplier
- a. 2
  - b. 3
  - c. 6
  - d. 5
20. If the expenditure multiplier in a closed economy without government activities equals 4, what is the MPC in this economy?
- a. 0.25
  - b. 0.20
  - c. 0.75
  - d. 0.80

**Use the information below to answer questions 21- 23.**

In an economy at zero disposable income consumption is ₦1200 million. The marginal propensity to save in this economy is 0.25

21. What is the consumption function for this economy?
- a.  $C = ₦1200 + 0.25Y_d$
  - b.  $C = ₦1200 + 0.75Y_d$
  - c.  $C = ₦0 + 0.75Y_d$
  - d.  $C = -₦1200 + 25Y_d$
22. If  $Y_d = 6000$  million, what is consumption expenditure in this economy?

- a. €6000 million
- b. €5700 million
- c. €7200 million
- d. €5200 million

23. What is saving in this economy at  $Y_d = 6000$  million?

- a. -€1200
- b. €300
- c. €1200
- d. -€300

24. An increase in minimum wages unmatched by high productivity leads to

- a. demand pull inflation
- b. cost push inflation
- c. imported inflation
- d. creeping inflation

25. Full employment occurs when

- a. actual output exceeds potential output
- b. actual output is less than potential output
- c. actual output is equal to potential output
- d. actual output and potential rise together

26. Inflationary gap occurs when

- a. actual output exceeds potential output
- b. actual output is less than potential output
- c. actual output is equal to potential output
- d. actual output and potential rise together

27. To close a recessionary gap, the central bank must use

- a. contractionary monetary policy
- b. contractionary fiscal policy
- c. expansionary monetary policy
- d. expansionary fiscal policy

28. To close an inflationary gap, contractionary fiscal policy

- a. shifts AE line upward
- b. shifts AE downward
- c. shifts  $AE = Y$  identity away from the origin
- d. leaves  $AE = Y$  identity unaltered

29. In the Keynesian aggregate expenditure – real output model for the determination of equilibrium output, the price level is assumed to be

- a. zero
- b. constant
- c. rising
- d. declining

30. As disposable income increases, average propensity to save
- increases
  - decreases
  - fluctuates
  - remains constant
31. Personal Income is an example of ..... tax.
- indirect
  - direct
  - value added
  - sales
32. A tax system in which the tax rate increases as income increases is
- proportional
  - regressive
  - progressive
  - flat
33. The following are features of money, except
- unit of account
  - homogenous
  - portable
  - generally acceptable
34. The investment needed to replace worn out capital in an economy is known as
- gross investment
  - net investment
  - replacement investment
  - stock investment
35. If desired AE equals actual output, unplanned inventory investment is
- positive
  - negative
  - zero
  - increasing
36. In Keynesian analysis, demand for money is also referred to as
- liquidity preference
  - supply of money
  - quantity demanded for money
  - real money balances
37. Which of the following is not a motive for holding money according to Keynes
- transactionary motive
  - precautionary motive
  - speculative motive

- d. money motive
38. A firm's demand for money to buy spare parts to fix expected breakdown of a machine can be described as a
- transactions demand for money
  - precautionary demand for money
  - speculative demand for money
  - money motive
39. Which of the following relationships best describes that between interest rate and demand for money?
- inverse
  - direct
  - equidistant
  - discrete
40. When someone decides on the mixture of financial assets to hold he is making
- asset decision
  - portfolio decision
  - monetary decision
  - capital investment decision
41. The demand for money curve is negatively sloped because of
- transactions demand
  - precautionary demand
  - speculative demand
  - None of the above
42. The stock of money in an economy at any point in time is referred to as
- supply of money
  - demand for money
  - quantity supplied of money
  - quantity demanded for money
43. Money supply is narrowly defined as
- $M_1$
  - $M_2$
  - $M_3$
  - $M_4$
44. If a person's nominal income increases by 25% while price level increases by 15%, the person's real income
- increases by 35%
  - increases by 10%
  - decreases by 10%

- d. decreases by 35%
45. If the average level of nominal income is GH¢ 21,000 and the price level index is 154, the average real income would be about
- GH¢ 12,546
  - GH¢ 13,636
  - GH¢ 15,299
  - GH¢ 17,823
46. Who would not be hurt by unanticipated inflation?
- those living on flexible income schemes
  - those who expect rises in future prices
  - those who borrowed money at flexible interest rate
  - those who lent money at a fixed interest rate
47. If an economy's output is below the potential output, demand-pull inflation may result in
- increasing price level and rising employment
  - falling real output and employment
  - increasing price level and falling employment
  - falling price level increasing employment
48. Which of the following may cause cost-push inflation?
- rise in input prices
  - rise in output
  - decrease in price of resources
  - increase in unemployment
49. Which of the following is associated with hyperinflation?
- The use of money as a medium of exchange and a store value
  - increasing output in the economy
  - economic growth
  - the hoarding of goods and speculation
50. Commercial Banks' lending ability is influenced by the
- policy rate
  - Gross Domestic Product
  - Money supply
  - the existence of a clearing house
51. Bank of Ghana's decrease in the policy rate is expected to
- increase money supply
  - decrease money supply
  - increase the commercial bank' lending rates
  - leave money supply unchanged



52. To keep the value of money reasonably constant, the Bank of Ghana
- uses wage control
  - uses price control
  - employs fiscal policy
  - controls the money supply
53. The money supply in Ghana is determined by the Bank of Ghana and does not change when the interest rate changes; therefore
- the supply of money curve is vertical
  - the supply of money curve is horizontal
  - the supply of money curve is upward sloping
  - the supply of money curve is downward sloping
54. The main purpose of the Open Market Operation system of the Bank of Ghana is
- directing the buying and selling of government securities
  - issuing currency
  - adjusting legal reserves among banks
  - monitoring banks to ensure that they do not engage in fraud
55. Which of the following is not a function of commercial bank?
- managing national debt
  - lending money to customers
  - accepting of deposits
  - act as trustees
56. An ad valorem tax is
- based on the weight of an imported item
  - placed on imported goods
  - a given percentage of the value of goods
  - charged on the earnings of entrepreneurs

Use the hypothetical data in the Table below to answer questions 57 to 60

1	2	3	4	5
Real GDP	Consumption Expenditure	Saving	Investment	Aggregate Expenditure (C + I)
430	420		20	
450	435		20	
470	450		20	
490	465		20	
510	480		20	

57. What is saving when real GDP equals 430?

- a. 20
- b. -10
- c. 10
- d. -20

58. What is the equilibrium real GDP?

- a. 430
- b. 450
- c. 470
- d. 510

59. What is the value of the unplanned inventory investment at real GDP of 470?

- a. 20
- b. -20
- c. 0
- d. -470

60. The Table captures expenditure totals for

- a. a three sector economy
- b. a two sector economy
- c. a four sector economy
- d. any of the above

### SECTION B (20 marks)

[Answer one (1) question from this section]

#### QUESTION 1

Suppose an economy is represented by the following equations. The values are in billions of cedis.

$$C = 2000 + 0.8Y_d$$

$$T = 200 + 0.2Y$$

$$I_o = 1300$$

$$G_o = 1200$$

$$(X - M) = 500 - 0.2Y$$

$$Y_d = Y - T$$

Where  $C$  = Consumption Function,  $T$  = Tax Function,  $I_0$  = Investment expenditure,  $G_0$  = Government Expenditure,  $(X-M)$  = Net Exports and  $Y_d$  = Disposable Income.

Required:

- a. What is the meaning of the ₵200 billion in the Tax function? (2 marks)
- b. Derive the aggregate expenditure function. (5 marks)
- c. Compute the equilibrium income. (4 marks)
- d. What is the equilibrium tax revenue? (3 marks)
- e. Determine the state of government budget and explain your answer. (3 marks)
- f. Calculate the net exports for this economy. Explain your answer. (3 marks)

(Total 20 marks)

## QUESTION 2

- a. Define Inflation (3 marks)
- b. How is inflation measured? (3 marks)
- c. With diagrams show that Inflation whether demand pull or cost-push the source of the inflation is excess demand for goods and services at the current price level. (14 marks)

(Total 20 marks)

## SECTION C (20 marks)

[Answer one (1) question from this section]

## QUESTION 3

a. Congratulations for being successful at the current Airtel promotion. Your prize money is Gh₵75,000. This was a text message you received on your phone.

Suppose you have deposited your prize money with Ghana Commercial Bank (GCB) on your current account. GCB maintains the mandatory cash ratio of 12.5% and any cash that leaves GCB returns to it.

**Required**

- a) Determine the cash reserves that GCB should keep because of your deposit. (2 marks)
- b) Compute the excess reserves your deposit will generate for GCB. (2 marks)
- c) Calculate the reserve multiplier for GCB. (2 marks)
- d) Determine the total loans that GCB can create with your deposit. (4 marks)
- e) Calculate the change in demand deposit your deposit can support for GCB. (4 marks)

b. Explain how the Bank of Ghana can influence the extent to which GCB can create loans with your deposit with the following monetary policy tools:

- i. Cash ratio (3 marks)
- ii. Monetary policy rate (3 marks)

(Total 20 marks)

**Question 4**

The following were statements made by five students of Central University who were studying for their end of second semester examination in Economics.

Ama – Now that the rate of inflation has fallen to 16.5%, I expect the price of goods and services to fall by the same margin.

Kwame - Ama, have you heard that the Bank of Ghana has reduced its policy rate? I think the Bank of Ghana is implementing expansionary fiscal policy.

Monica - Kwame, all other things being equal, I believe that the reduction in the policy rate by Bank of Ghana may enhance the ability of our bank to expand credit to our clients.

Emmanuel – I read in the Business News that the Ghanaian Economy is in a state of recession. I think the government should implement contractionary fiscal policy.

Winnifred – The nominal values for the 2014 and 2015 Gross Domestic Product (GDP) for Ghana were GH¢23.5 billion and GH¢24.6 million respectively. Well, we can conclude that the economy did better in 2015 than 2014.

(5 marks each)

**Required:**

Ascertain whether these statements are TRUE or FALSE and explain.

(Total 20 marks)