

(v) Advantages of flexible exchange rate system

(vi) Natural rate of unemployment (20)

[This question paper contains 8 printed pages.]

Your Roll No.....

Sr. No. of Question Paper : 565

G

Unique Paper Code : 2922062302

Name of the Paper : Macroeconomics

Name of the Course : BMS

Semester : III

Duration : 3 Hours

Maximum Marks : 90

**Instructions for Candidates**

1. Write your Roll No. on the top immediately on receipt of this question paper.
2. Attempt ALL questions.
3. Use of Simple Calculator is allowed.

1. Attempt any four of the following

(a) What is the effect of an increase in lump sum tax of Rs. 500 crores on equilibrium level of income if marginal propensity to save is 20%?

- (b) "If desired investment is greater than actual investment then there is a tendency for output to fall" True or false. Explain.
- (c) Why does the demand for money curve flatten at very low rates of interest.
- (d) "The sum of average propensity to consume and average propensity to save is always equal to one" True or false. Explain.
- (e) LM curve is upward sloping because there is a direct relationship between supply of money and demand for money" True or False. Explain.

(16)

2. (a) Explain how the rate of interest is determined in an economy that is operating at full employment level of output and how it works to stabilize aggregate demand in face of autonomous changes in components of aggregate demand such as investment?

(10)

- (b) What is a BP curve? What will be the impact of the following changes on BP curve :
- (i) Liberalization of foreign investment coming into the country.
- (ii) Liberalization of import of precious metals by the country. (2,3,3)

5. Write short notes on any **four** of the following :

- (i) Properties of IS curve
- (ii) Keynesian theory of determination of rate of interest
- (iii) Kautilya's notion of wealth
- (iv) 2 reasons for inflation in India

(b) "The extent to which an expansionary monetary policy will impact national output and rate of interest depends on the interest sensitivity of investment" Explain with the help of diagrams.

(9)

4. (a) "If domestic and foreign assets are imperfect substitutes, then the rise in income as a result of changes in supply of money by central bank is greater if exchange rates are flexible than if they are fixed" Explain with diagrams. (10)

**OR**

(a) "Under fixed exchange rate system monetary policy is not effective in the presence of perfect capital mobility whereas fiscal policy is effective in bringing about growth in the economy" Discuss with diagram. (10)

(b) "Government cannot permanently trade higher inflation for lower employment." Explain with the help of diagrams. (8)

3. The following equation describes an economy

$$C = 100 + 0.6 Y_d$$

$$I = 220 - 10i$$

$$G = T = 100$$

$$M_d = 0.2Y - 5i$$

$$M^s = 110$$

Where

C = aggregate consumption

$Y_d$  = disposable income

$I$  = aggregate investment

$T$  = Taxes

$G$  = Government expenditure

$i$  = rate of interest

$M_d$  = demand for money

$M^s$  = money supply

- (i) Derive the equation for IS & LM curve.
- (ii) Calculate equilibrium income and rate of interest.
- (iii) What happens to equilibrium income if  $G$  increases from 100 to 200. (3,3,3)

**OR**

(a) In an economy

$C = 50 + 0.8 Y_d$  (Consumption)

$I = 100$  crores (Investment)

$G = 50$  crores (Government spending)

$T = 20$  crores (Taxes)

$Y_f = 1160$  crores (Full employment level of income)

- (i) Find the change required in government spending to achieve  $Y_f$ .
- (ii) What change in taxes will ensure that the economy reaches  $Y_f$ ?
- (iii) What change in government spending and tax is needed to achieve  $Y_f$ , if the government follows a balanced budget policy? (3,3,3)