

UNIVERSITY OF DAR-ES-SALAAM



BUSINESS SCHOOL

DEPARTMENT OF FINANCE

FN 101: PRINCIPLES OF MACROFINANCE

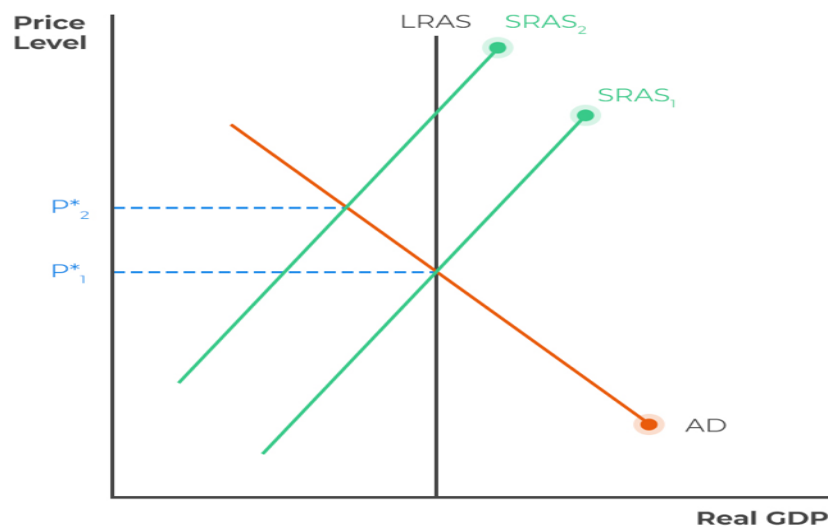
SEMINAR DISCUSION QUESTIONS GROUP NO. 7

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1. Aggregate supply means summation of various individual supplies of goods and services available in the market in a particular period of time.
- a. Short run aggregate supply curve is a graphical representation that shows the positive relationship between the aggregate price level and total output supplied in an economy in a given period of time. It's a positive curve since the amount of total output can be changed anytime with the change in price due to the fact that inputs are variable. Thus, suppliers can employ more input and produce more outputs when the prices are favorable and vice versa its true. WHILE Long run aggregate supply curve is a graphical representation with a vertical line at the potential level of output. Under long run all the inputs are fixed thus suppliers cannot respond to the change in price level at the market instead their supplies remain constant while prices change of a period of time.

AGGREGATE SUPPLY CURVE SR LR

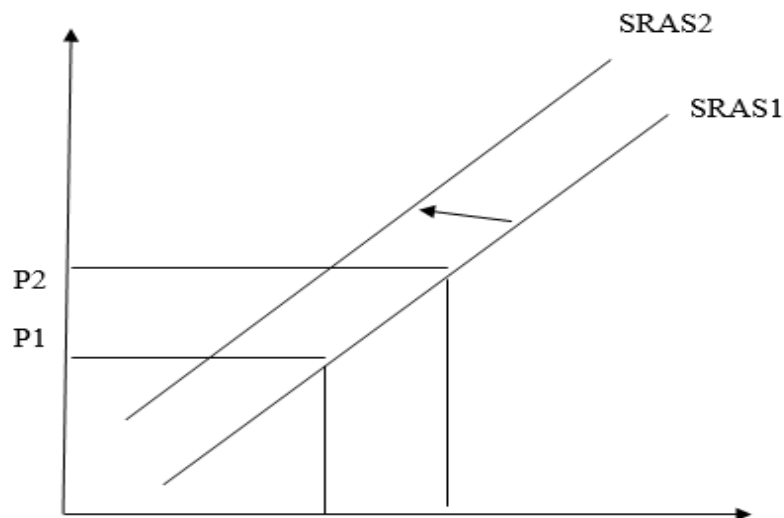


From the above graph there is shift in SRAS from SRAS₁ to SRAS₂ due to the fact that the inputs are not fixed thus suppliers can respond to the price change. But the LRAS is fixed due to the fact that all inputs in long run are fixed thus suppliers can not change their level of out in response to the change in price.

- b. There are number of factors that can change short run aggregate supply curve these include;

- Change in production costs; these cost involve taxes, labor costs, subsidies and so on, for example when taxes rises the cost of inputs will be high thus making firm to acquire less inputs than usual and produce less thus supplying less in the market causing the supply curve to move left ward. On the other hand, when taxes fall the supplies will be able to acquire more inputs thus producing more hence supplying more in the market causing the supply curve to move rightward.
- Change in technology; when the firm employs, more advanced technology it will be able to produce large amount of output in a very short period of time thus supplying more causing the short run aggregate supply curve to move rightward. On the other hand, when the firm employs old or outdated technology its level of efficiency will be very low thus making it to produce less output in a long period of time thus supplying less forcing the supply curve to move to the left-hand side.

SHIFT IN SHORT RUN AGGREGATE SUPPLY CURVES

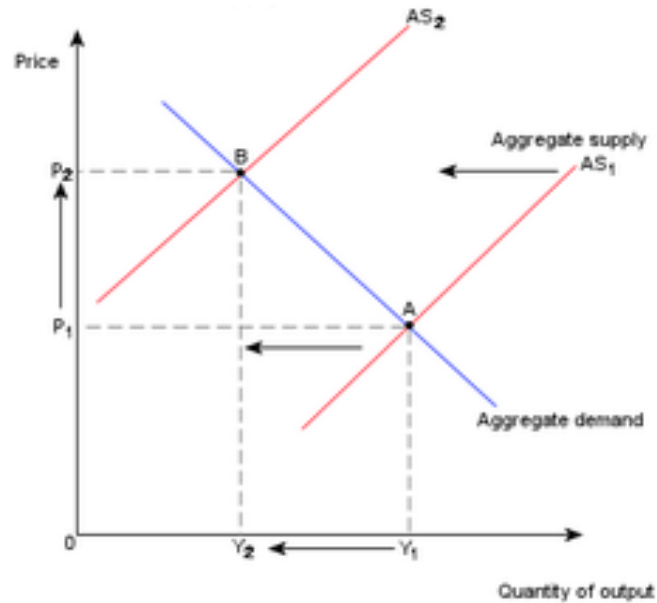


From the above diagram there is the shift in SRAS from SRAS1 to SRAS2 this is due to either increase in production cost or lowering of production costs, but also it may be due to the adaption of either new or old technology.

- c. According to Tejvan Pettinger (2019) adverse supply shock is an event that causes unexpected increase in cost or disruption to production, this will cause the short run aggregate supply curve to shift the left, leading to higher inflation and lower output. There are number of causes of adverse supply side shocks such as increase in oil prices,

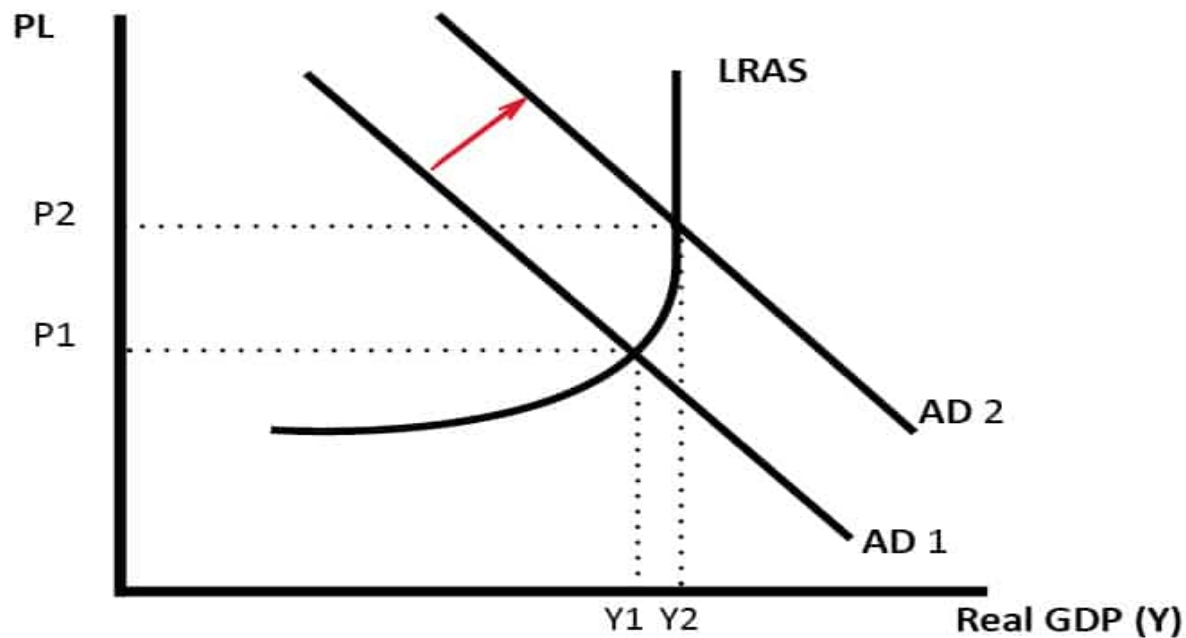
bas weather, declining productivity e.g. general strikes, wage push inflation, devaluation/ depreciation in the exchange rate and poor harvest disrupting supply of food.

ADVERSE SUPPLY SIDE SHOCK CURVE



From the above graph there is leftward shift in aggregate supply curve from AS_1 to AS_2 this is due to the fact that the rate of production has lowered causing the suppliers to lower their supplies to in the market. And the main causes for the low level is output is an increase in production costs from unexpected events such as increase in oil costs.

- d. According to Tejvan Pettinger (2019) when there is tax reduction at the full employment level of output there will be increase in purchasing power of people thus making the spending to increase thus aggregate demand will move to the right-hand side. On supply side tax cuts may increase incentives to work leading to higher productivity. Tax reduction at full employment level of output will also likely to cause inflationary pressures,



2. Central bank, this is an institution that is responsible for creating and managing money, it carries its function through the conduct of monetary policy. Its action affect interest rate, amount of credit, and money supply which have impact on aggregate output and inflation. Each country has its own central bank in case of Tanzania we are having Bank of Tanzania (BOT) which was established in 1965 by Bank of Tanzania Act to perform all traditional central banking functions in Tanzania.

The following are the functions of central bank

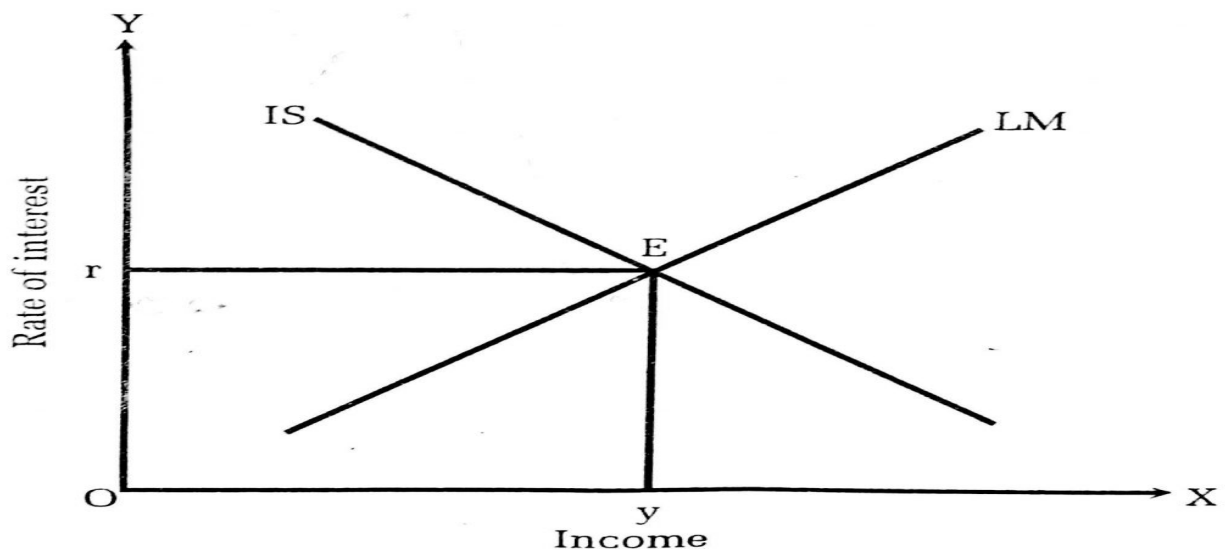
- The bank of issue; its only central bank with the sole right to issue notes and coins in the circulation, incase of Tanzania its on BOT has the right to issue notes and coins for the purpose of directly influencing the amount of currency in circulation.
- The Bankers Bank, every other bank is required to have an account with central bank by keeping the minimum reserves, and incase of any difficulties its central bank which will act as the lender of last resort to those banks.
- The Governments bank; there are number of government parastatals and public cooperation's which do have their account with central bank it also acts as lender and fiscal agent of the government.
- Advisor to the government; central bank may be requested to advice the government on any matter related to its functions, powers, duties, the credit, conditions in Tanzania thus acting as advisor to the government.

- The guardian of the country's International Reserve, it's the central bank that is responsible for keeping all the foreign exchanges reserves for example, according to bot.go.tz BOT has the reserves of 3930 million USD, apart from keeping foreign reserve they also keep other assets like gold.
- Supervision of Banks and Financial Institutions; this involve ensuring that commercial banks and other financial institutions conduct their business on the formulated laws and regulations in force but also according to the policy in force.

b. IS curve is a graph of all combination of interest rate and output that result in goods market equilibrium. WHILE LM curve shows the combinations of interest rate and level of real income for which the money market is in equilibrium.

From the graph below at lower interest rate, investment is higher, which translates into more total output (GDP), so the IS curve slopes downward and to the right. The LM slopes upward because higher level of income induces increased demand to hold money balance for transactions, which requires a higher interest rate to keep money supply and liquidity demand in equilibrium

IS-LM CURVE



REFERENCES;

- Tejvan Pettinger (2019),
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