	Part A	Topic	Year 2018	2017	2016	2015	2014	2013	2012	2011	2010
MCQ	Q5	Main circular flow of income	5 MCQs	6 MCQs	5 MCQs	4 MCQs	1 MCQs	4 MCQs	5 MCQs	6 MCQs	2 MCQs
		Business cycle									
		Leakages and Injections									
		Macro-equilibrium conditions									
		Consumption and savings function									
		MPC, APC, MPS, APS									
		Unplanned changes in inventory									
		Investment and tax multiplier									
		Actual and potential output									
		Inflationary and deflationary gap									

Past Paper Question 2018 -2004

1. Common concepts

1. When other things remain unchanged, an increase in household disposable income leads to (A/L 2005)
   - I. Decrease in consumption and increase in saving
   - II. Increase in consumption and decrease in saving
   - III. Increase both savings and consumption
   - IV. Consume the entire increase in income
   - V. Save the entire increase in income

2. Which one of the following is not true? (A/L 2004)
   - I. Y = C+I+G+X-M
   - II. I +G+X = S+T+M
   - III. Y=C+I+G+NX(NX=Net Exports)
   - IV. Y+M=C+I+G+X
   - V. Y=C+S+T

2. Business cycle

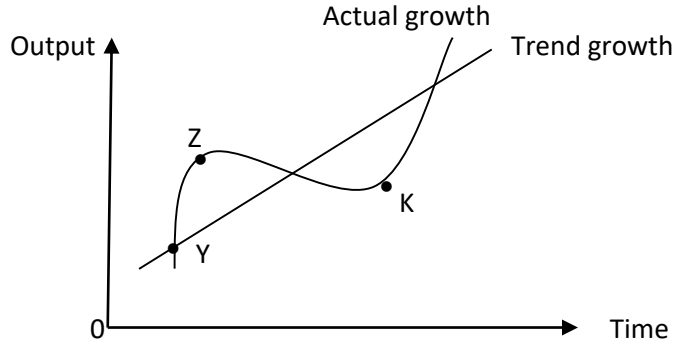
3. The sequence of phases of the business cycle are (A/L 2017)
   - I. Contraction, expansion, trough and peak.
   - II. Contraction, peak, expansion and trough.
   - III. Contraction, trough, peak and expansion.
   - IV. Contraction, trough, expansion and peak.
   - V. Contraction, peak, trough and expansion.

4. In the contractionary phase of the business cycle, (A/L 2015)
   I. Investment is rising and the output is falling.
   II. Unemployment is rising and the output is falling.
   III. Unemployment is falling and the price level is rising.
   IV. Unemployment is falling and the output is rising.
   V. Unemployment is rising and the output is rising.

5. The characteristics that can be observed when an economy moves from the bottom to the peak of a business cycle are (A/L 2014)
   I. Increase in actual output, decrease in inflation and unemployment
   II. Increase in actual output, decrease in employment and inflation.
   III. Increase in actual output, increase in employment and inflation
   IV. Increase in potential output, decrease in inflation and increase in unemployment.
   V. Increase in actual output, increase in potential output and decrease in inflation

6. Which of the following will most likely occur during the expansionary phase of the business Cycle? (A/L 2012)
   I. Real GDP rises and unemployment falls
   II. Real GDP rises and unemployment rises
   III. Real GDP declines and inflation rises.
   IV. Interest rates rise and the number of business failures rise.
   V. Inflation rises and employment falls.

7. The diagram shows trend and actual growth path for an economy. (A/L 2011)



Which one of the following combinations describes the state of the economy when it moves from point Y to point Z on its actual growth path?

	Stage of the Business Cycle	Output Gap
I.	Boom (Expansion)	Negative
II.	Recession (Contraction)	Positive
III.	Boom (Expansion)	Positive
IV.	Recession (Contraction)	Negative
V.	Trough	Positive

3. Main circular flow of income

8. For an economy consisting of households and business firms only, which of the following is consistent with the circular flow of income? (A/L 2018)
   - I. Households are producers of goods and services and business firms are consumers of productive resources.
   - II. Households are users of productive resources and business firms are sources of savings.
   - III. Households are suppliers of productive resources and business firms are producers of goods and services.
   - IV. Business firms are collectors of taxes and households are sources of taxes.
   - V. Business firms are suppliers of productive resources and households are consumers of goods and services.

9. One of the "real " flows in the circular flow model of income is (A/L 2016)
   - I. The flow of goods and services going from firms to households.
   - II. The flow of factor services going from firms to households.
   - III. The flow of goods and services going from households to firms.
   - IV. The flow of money payments going from firms to households.
   - V. The flow of money payments going from households to firms.

10. In the circular flow of income diagram of an economy, which one of the following flows directly from government? (A/L 2015)
    - I. Taxes (T)
    - II. Exports (X)
    - III. Savings (S)
    - IV. Transfer payments (Tr.)
    - V. Investment expenditure (I)

4. Leakages and Injections

11. Which one of the following represents an injection into an economy's circular flow of income? (A/L 2016)
    - I. A deficit in the trade balance
    - II. A government budget deficit
    - III. An increase in net taxes
    - IV. Retained profits of private companies
    - V. Household savings

12. The table below shows selected macroeconomic data for a hypothetical economy. (A/L 2009)

Item	(Rs. Billion)
Savings	50
Investment	30
Taxation	40
Exports	50
Government Purchases	20
Imports	30

Which statement is correct for the economy according to the information given in the table?

I. There is a budget deficit.
II. The economy is in equilibrium.
III. There is a current account deficit in the balance of payments.
IV. Withdrawals are greater than injections.
V. Economy will expand.

5. Calculations

13. As income level increases from Rs.5000 to Rs. 10000, consumption expenditure increases from Rs.7000 to Rs, 11 000. The marginal propensity to consume is equal to (A/L 2018)

I. 0.8
II. 0.9
III. 1.0
IV. 1.2
V. 1.4

14. Which of the following will decrease the gross Domestic product by the greatest amount? (A/L 2018)

I. Rs. 50 billion increase in both government purchases and taxes
II. Rs. 50 billion decrease in both government purchases and taxes
III. Rs. 50 billion increase in taxes
IV. Rs. 50 billion decrease in government purchases
V. Rs. 50 billion increase in net exports

15. In an economy without a government sector, consumption (C), investment (I), exports (X) and imports (M) are given below:

C = 200 + 0.75 Y I = 500 X = 150 M = 100

What will be the equilibrium level of national income (Y) in this economy? (A/L 2018)

I. 3000
II. 3400
III. 3 600
IV. 3 750
V. 3 800

16. Assume that in a closed economy, the aggregate consumption function is C = 200 + 0.8Y, and the equilibrium level of national income is Rs. 4000 billion. What is the level of investment for this economy? (A/L 2017)

I. Rs. 1 600 billion.
II. Rs. 600 billion.
III. Rs. 400 billion.
IV. Rs. 380 billion
V. Rs. 300 billion.

17. Suppose an economy is currently operating at an equilibrium level of output at Rs. 3 000 billion and to achieve full employment equilibrium, it requires to produce an output level of Rs. 4 000 billion. This economy's marginal propensity to save is 0.2. What would be the most appropriate policy recommendation for this economy to achieve full employment equilibrium? (A/L 2017)
    I. Increase government spending by Rs. 1 000 billion.
    II. Increase government spending by Rs. 500 billion.
    III. Increase government spending by Rs. 250 billion.
    IV. Decrease direct taxes by Rs. 1000 billion.
    V. Decrease direct taxes by Rs. 250 billion.

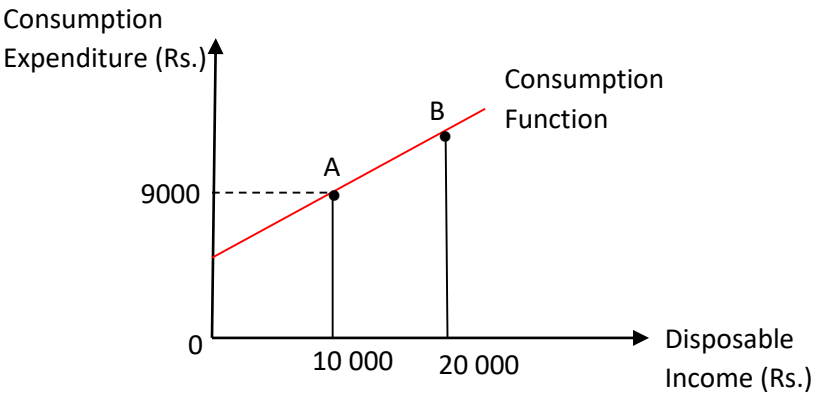
18. The table below presents data on the components of aggregate expenditure and national income for an open economy with a government sector where,
    C = Consumption expenditure, I = Investment, G = Government purchases, X = Exports, M= Imports and Y = National income.
    Under which situation is this economy in disequilibrium? (A/L 2017)

(All figures are in Rs. Billion)

	C	I	G	X	M	Y
I.	250	50	100	75	25	400
II.	300	50	100	75	25	500
III.	450	50	100	75	25	650
IV.	600	50	100	75	25	800
V.	750	50	100	75	25	950

19. Assume that in a simple economy, the aggregate consumption function is C = 250 + 0.75Y and investment is I = 450. The equilibrium level of income in this economy is (A/L 2016)
    I. 1 800.
    II. 2 800.
    III. 3 600.
    IV. 7 200.
    V. 9 000.

20. (A/L 2015)



The diagram above displays a linear consumption function. If the autonomous consumption is Rs. 4000, what is the amount of consumption expenditure does point B correspond to?

I. Rs. 18000
II. Rs. 17000
III. Rs. 16000
IV. Rs. 14000
V. Rs. 10000

21. Consider the following macroeconomic data for an economy which is operating at an equilibrium national income level. (A/L 2015)

Item	Rs. Million	Item	Rs. million
Consumption expenditure	5000	Imports	1200
Tax revenue	1000	Exports	980
Government purchases	1500	GDP at market price	8000

The level of investment in this economy is

I. Rs. 310 million
II. Rs. 320 million.
III. Rs. 1220 million.
IV. Rs. 1720 million.
V. Rs. 1940 million.

22. Suppose that autonomous consumption is Rs. 400 and that the marginal propensity to consume is 0.8. If disposable income increases by Rs. 1,200, consumption spending will increase by. (A/L 2013)

I. Rs. 1600.
II. Rs. 1360.
III. Rs. 1200.
IV. Rs. 960
V. Rs. 400.

23. In a closed economy with only lump-sum taxation, if the marginal propensity to save is equal to 0.25. a Rs. 80 billion increase in government purchases could cause a maximum increase in output of (A/L 2013)

I. Rs. 80 billion.
II. Rs. 80.25 billion.
III. Rs. 160 billion.
IV. Rs. 240 billion.
V. Rs. 320 billion.

24. In a closed economy with no government, C = 30 + 0.7Y, where C is consumption and Y is income. The equilibrium level of income is Rs. 300 million. What is the level of investment? (A/L 2013)
    I. Rs. 60 million.
    II. Rs. 100 million.
    III. Rs. 210 million.
    IV. Rs. 240 million.
    V. Rs. 300 million.

25. Assume that in an economy operating at equilibrium, exports = Rs. 400 million, imports = Rs. 500 million. Taxes = Rs. 1200 million, government purchases = Rs. 1500 million and saving Rs. 1000 million. Then the level of investment is (A/L 2012)
    I. Rs. 700 million.
    II. Rs. 800 million.
    III. Rs. 1000 million.
    IV. Rs. 1200 million
    V. Rs. 1300 million

26. If an autonomous increase in spending in an economy of Rs. 100 million leads to an increase in real GDP of Rs. 500 million, then for that economy the marginal propensity to consume must have been. (A/L 2012)
    I. 0.2
    II. 0.4
    III. 0.5
    IV. 0.8
    V. 5.0

27. In a closed economy with no government, the value of the investment multiplier is 5. By how much will consumption increase, if investment increases by Rs. 200 million? (A/L 2011)
    I. Rs. 200 million
    II. Rs. 400 million
    III. Rs. 600 million
    IV. Rs. 800 million
    V. Rs. 1000 million

28. (A/L 2011)

Item	Amount (Rs.. billion)
Household consumption	70
Government purchases	20
Net taxes (= taxes- transfers)	25
Investment	15
Imports	5
Exports	10

According to the information given in the table, the value of household savings in this economy is

I. -40 billion rupees.
II. -15 billion rupees.
III. 15 billion rupees.
IV. 40 billion rupees.
V. 45 billion rupees.

29. Other things being equal, if an increase of Rs. 75 million investment expenditure resulted in an increase in national income of Rs. 300 million, what is the value of Marginal propensity to consume (MPC)? (A/L 2010)

I. 0.80
II. 0.75
III. 0.50
IV. 0.40
V. 0.25

30. The Table below shows selected macro-economic data for an economy. (A/L 2010)

Year	Level of Income (Y) (Rs. Billion)	Level of Consumption (C) (Rs. Billion)
1	400	300
2	500	350
3	600	400
4	?	500

What would be the new level of income (Y) in Year 4, if consumption (C) in this economy increases to Rs. 500 billion in Year 4 and the Marginal propensity to Consume (MPC) remains constant?

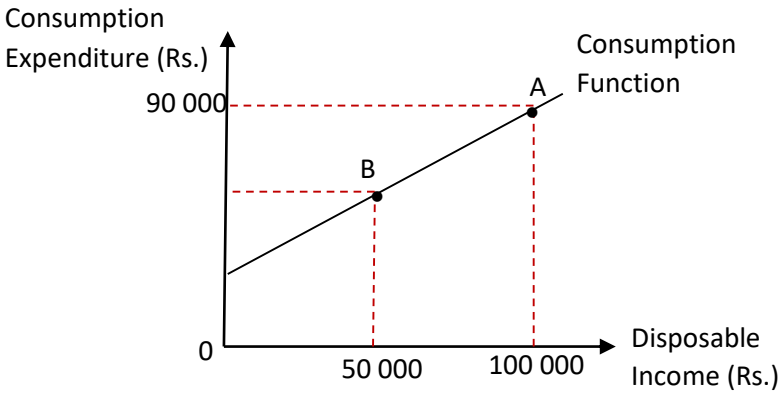
I. Rs. 200 billion
II. Rs. 400 billion
III. Rs. 650 billion
IV. Rs. 800 billion
V. Rs. 850 billion

31. Suppose the Marginal Propensity to Consume (MPC) for a closed economy is 0.8. An increase in investment leads to an increase in national income by Rs. 250 billion. Other things being equal, what is the value of increase in investment? (A/L 2009)

I. Rs. 20 billion
II. Rs. 50 billion
III. Rs. 150 billion
IV. Rs. 200 billion
V. Rs. 250 billion

32. The consumption function of an economy with no government sector and no foreign trade is, C = 180 + 0.6 Y (where C = aggregate consumption and Y = national income). If investment expenditure is autonomous and equal to Rs. 300 billion, what is the equilibrium level of national income? (A/L 2008)
    I. Rs. 480 billion.
    II. Rs. 640 billion.
    III. Rs. 800 billion
    IV. Rs. 1,200 billion
    V. Rs. 2,800 billion.

33. The diagram below displays a linear aggregate consumption function with a Marginal propensity to Consume (MPC) of 0.82. (A/L 2008)



What is the amount of consumption expenditure corresponding to point B?
    I. 82, 000
    II. 50,000
    III. 49,000
    IV. 41,000
    V. 33,000

34. If the aggregate consumption function is given to be C=80 + 0.7 Y and the national income (Y) = 1,000 then the level of savings in a two-sector economy equals (A/L 2006)
    I. 220
    II. 300
    III. 700
    IV. 780
    V. 920

35. In a simple economy without foreign trade and government activities, over a one year period, an increase in new investment expenditure of Rs. 200 billion leads to increase the equilibrium national income by Rs. 800 billion . What is the value of MPC of this economy? (A/L 2006)
    I. 0.25

II. 0.75
III. 0.8
IV. 4.0
V. 7.5

36. Suppose that a Rs. 6,000 increase in income is accompanied by a Rs. 4,500 increase in consumption. The marginal propensity to save is (A/L 2006)
    I. 1.33
    II. 0.75
    III. 0.25
    IV. 0.20
    V. 0.15

37. Refer to the following information (Data is in Rs. Millions.) (A/L 2005)

Savings =	550	Investment	=	400
Taxation=	200	Total government expenditure	=	250
Imports=	250	Exports	=	300

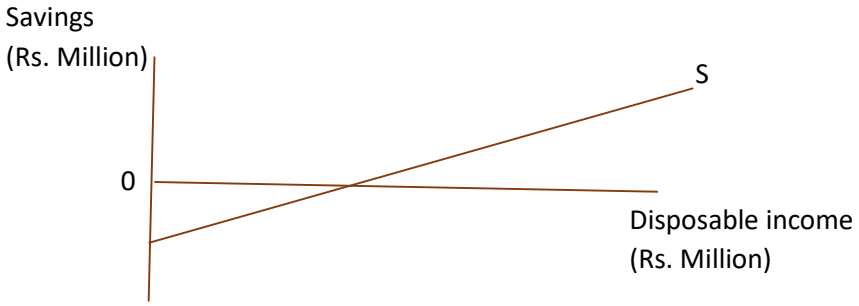
    Which of the following statements is correct?
    I. Total output will increase and the budget is in surplus
    II. Total output will increase and the budget is in deficit
    III. Total output will decrease and the budget is in surplus
    IV. Total output will decrease and the budget is in deficit
    V. Total output will not change

38. If the consumption function is C = 0.75 (Y-T) + 100 when T = 50, the n the savings functions is (A/L 2004)
    I. S = 0.75 (Y-T) -100
    II. S = 0.75 (Y-T) +150
    III. S = 0.25 (Y-T) -100
    IV. S = 0.25 (Y-T) -175
    V. S = 0.25 (Y-T) +-100

6. MPC, MPS, APC, APS

39. The consumption function of an economy is given by the equation, C = 600 + 0.8Y where C = Consumption and Y = national income. What is the correct conclusion that can be drawn from this information? (A/L 2011)
    I. Savings are positive at all levels of income.
    II. Marginal propensity to save declines as income increases.
    III. Marginal propensity to consume declines as income increases.
    IV. The average propensity to consume in constant.
    V. The average propensity to consume declines as income increases.

40. The diagram shows the aggregate savings function in a given economy. (A/L 2009)

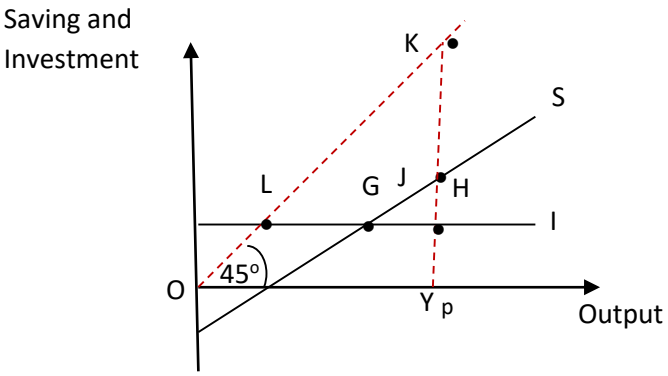


What happens to the Marginal Propensity of Save (MPS) and the Average Propensity to Save (APS) as disposable income rises in this economy?

	MPS	APS
I.	Remains constant	Falls
II.	Falls	Rises
III.	Rises	Falls
IV.	Rises	Rises
V.	Remains constant	Rises

7. Gap between actual and potential output

41. The diagram below shows the saving and investment curves of a closed economy with no government. (A/L 2013)



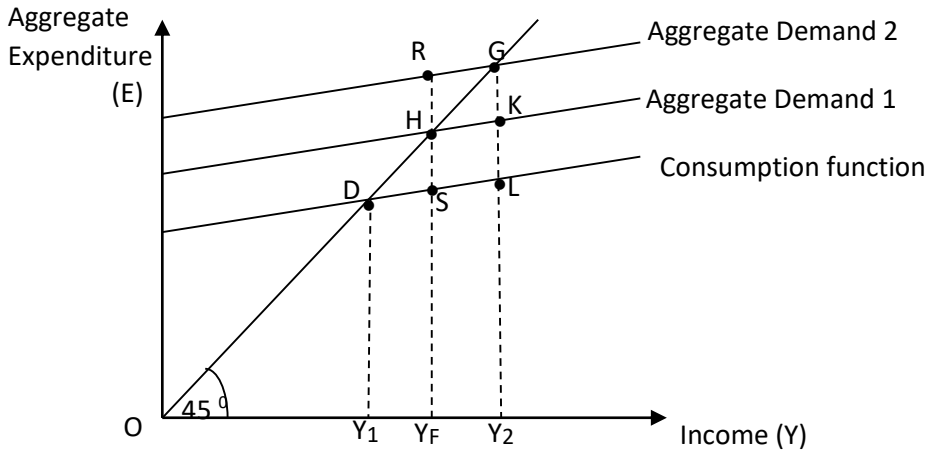
The potential level of output is Yp. Therefore, the gap between actual and potential output can be measured by the distance

I. LG
II. GH
III. JH.
IV. KJ.
V. HK.

8. Inflationary gap

42. An inflationary gap could be reduced by (A/L 2017)
    - I. An increase in government spending
    - II. An increase in the supply of money.
    - III. An increase in the income tax rate.
    - IV. A decrease in the Central Bank discount rate.
    - V. A decrease in the statutory reserve ratio.

43. The diagram below shows different equilibrium income levels for an economy under different aggregate demand conditions. (A/L 2012)

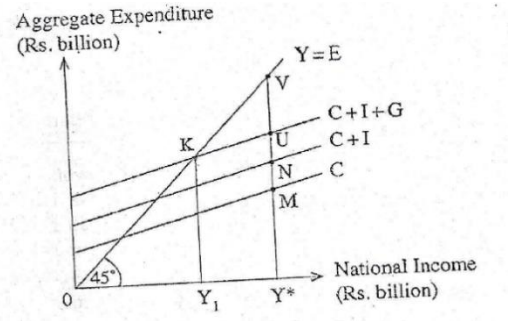


If the full employment level of income is Y_F which distance measures the inflationary gap?

- I. SH
- II. RH
- III. LG
- IV. Y_FR
- V. Y_2G

9. Deflationary gap

44. In the diagram below, $0Y_I$ is the equilibrium level of national income and 0Y* is the full employment level of national income. (A/L 2018)



What is the deflationary gap of this economy?

I. Y * U
II. UV
III. KV
IV. MV
V. Y_1Y^*

10. Aggregate expenditure and Aggregate demand

45. An increase in which of the following may result in a decrease in aggregate expenditure in an economy? (A/L 2017)
    I. Consumption expenditure
    II. Government purchases
    III. Import expenditure
    IV. Investment expenditure
    V. Inflow of foreign remittances

46. Which of the following will result in the greatest increase in aggregate demand? (A/L 2012)
    I. A Rs. 100 million increase in taxes.
    II. A Rs. 100 million decrease in taxes.
    III. A Rs. 100 million increase in government purchases
    IV. A Rs. 100 million increase in government purchases coupled with a Rs. 100 million increase in taxes
    V. A Rs. 100 million increase in government purchases, coupled with a Rs 100 million decrease in taxes

47. Other things remaining constant, which one of the following would cause aggregate demand to increase? An increase in (A/L 2011)
    I. Taxation on income
    II. Interest rates
    III. Savings
    IV. Government expenditure
    V. Imports.

48. Which of the following is not a component of aggregate demand (A/L 2005)
    I. Exports
    II. Private consumption
    III. Productivity
    IV. Investment
    V. Government consumption

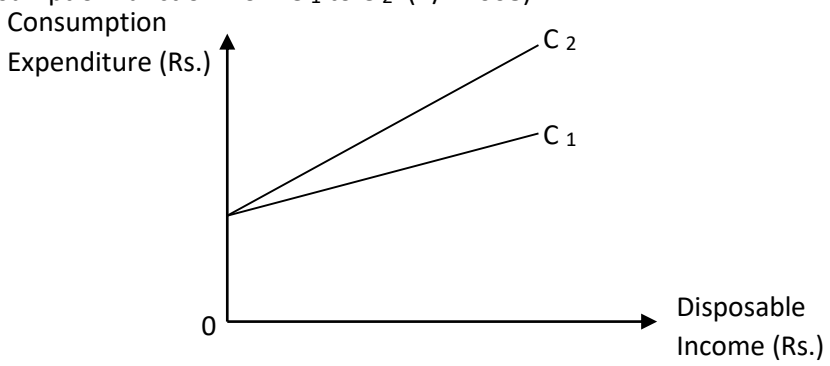
11. Investment multiplier

49. An increase in which of the following will increase the value of the investment multiplier? (A/L 2016)
    - I. The supply of money
    - II. Equilibrium output
    - III. Personal income tax rates
    - IV. The marginal propensity to consume
    - V. The statutory reserve ratio

50. "The multiplier" usually refers to how an initial increase in investment, government spending, or exports leads to a large increase in the level of (A/L 2011)
    - I. Prices
    - II. Interest rate
    - III. Unemployment
    - IV. Savings
    - V. Income

12. Multiplier and MPC

51. In the diagram below, a change in the pattern of savings in the economy causes a change in the consumption function from C_1 to C_2. (A/L 2008)

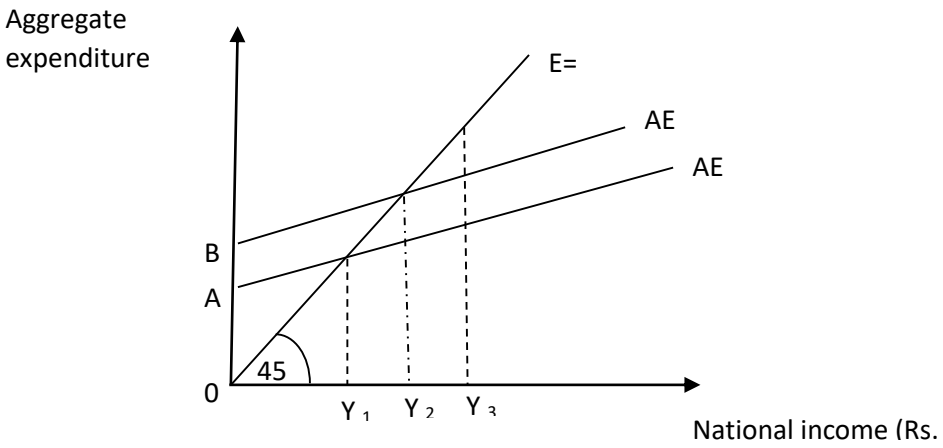


What are the effects of this change on the multiplier and on the marginal propensity to consume?

	Multiplier	Marginal propensity to Consume
I.	Decreases	Increases
II.	Increases	Decreases
III.	Increases	Increases
IV.	Decreases	Decreases
V.	Remains unchanged	increases

13. Unplanned change in inventory

52. The diagram below displays the behavior of some macroeconomic variables in an economy. (A/L 2016)



If the national income of this economy is Y_3 and the aggregate expenditure function is AE_1.

I. The economy is in equilibrium.
II. There is an unintended inventory accumulation and national income will rise.
III. There is an unintended inventory accumulation and national income will fall.
IV. There is an unintended inventory reduction and national income will rise.
V. There is an unintended inventory reduction and national income will fall.

QUESTION NUMBER	ANSWER	QUESTION NUMBER	ANSWER	QUESTION NUMBER	ANSWER	QUESTION NUMBER	ANSWER
1		14		27		40	
2		15		28		41	
3		16		29		42	
4		17		30		43	
5		18		31		44	
6		19		32		45	
7		20		33		46	
8		21		34		47	
9		22		35		48	
10		23		36		49	
11		24		37		50	
12		25		38		51	
13		26		39		52	

MOCK Questions

1. Which stage of the business (trade) cycle is most likely to be characterised by an increasing negative output gap?
   I. Boom
   II. Recession
   III. Recovery
   IV. Trough

2. What would be an increase in leakages or withdrawals from the circular flow of income?
   I. Increase in government spending on anti-smoking campaigns
   II. Increase in spending on imports of luxury cars
   III. Increase in spending on transfer payments
   IV. Increase in wages paid to government employees

3. What is used to measure the deflationary gap?
   I. The increase in injections needed to reach full employment
   II. The public sector borrowing requirement
   III. The rate of deflation
   IV. The rate of unemployment

4. The following data describes an economy's consumption function.

Income (Rs.m)	Consumption (Rs.m)
100	90
140	122
180	154
220	186

   What can be deduced about the value of the marginal propensity to consume in this economy?
   I. It increases as income increases.
   II. It decreases as income increases.
   III. It is 0.90.
   IV. It is 0.80.

5. In a closed economy with neither government expenditure nor taxation, the initial income is $2000 million. All savings are carried out by consumers, who save 25 % of any income received above $2000 million. Businesses plan to invest $2000 million. What is the value of the multiplier?
   I. 5
   II. 4
   III. $^4/_3$

IV. $^{3}/_{4}$

6. Equilibrium income in the economy is the level of national income at which
   I. The economy is producing at full employment national income.
   II. The inflow and outflow of currency is equal.
   III. The government's expenditure is equal to the government's revenue.
   IV. There is no tendency for the national income to change.

7. What would not exist in a free market, open economy?
   I. Autonomous investment
   II. Household saving
   III. Import spending
   IV. Indirect taxation

8. In a four sector economy in equilibrium, these values exist.

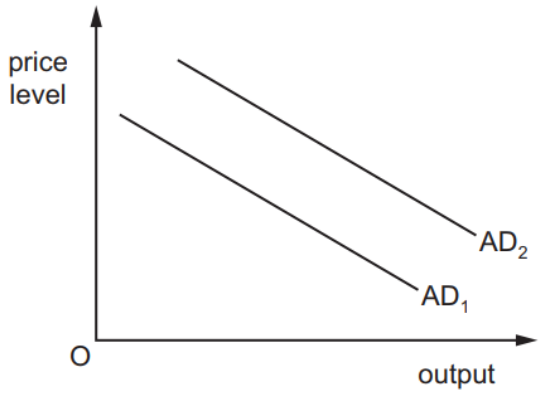
	Rs.m
Investment	15
Exports	40
Government expenditure	50
Savings	15
Imports	45
Taxes	X

What is the tax revenue?
   I. 20
   II. 35
   III. 45
   IV. 60

9. In a closed economy with no government C = 40 + 0.7 Y and I = 50, where C is consumption, Y is income and I is investment. What is the equilibrium level of income?
   I. 90
   II. 210
   III. 300
   IV. 640

10. How does a rise in the price of factors of production affect the aggregate supply (AS) curve?
   I. A move left along the AS curve
   II. A move right along the AS curve
   III. A shift to the left of the AS curve
   IV. A shift to the right of the AS curve

11. In the diagram, AD1 is an economy's initial aggregate demand curve.



What could cause the curve to shift to AD2?

I. A decrease in real wages
II. An appreciation of the currency
III. An increase in the money supply
IV. An increase in the price level

12. What does an aggregate demand curve show?

I. The level of aggregate demand corresponding to different levels of aggregate supply
II. The aggregate output demanded corresponding to different average price levels
III. The equilibrium price level corresponding to different levels of aggregate expenditure
IV. The equilibrium level of income corresponding to different levels of aggregate expenditure

13. The table shows the levels of consumption expenditure for given family incomes.

Disposable family income (Rs.)	Consumption expenditure (Rs.)
2000	2150
3000	3100
4000	4000
5000	4850
6000	5650
7000	6380

Over the range of disposable income shown, as income rises what happens to the marginal propensity to consume?

I. It falls and then rises.
II. It falls continuously.
III. It rises and then falls.
IV. It rises continuously.

14. The table refers to an open economy with a government sector.
In which situation is the economy in disequilibrium?

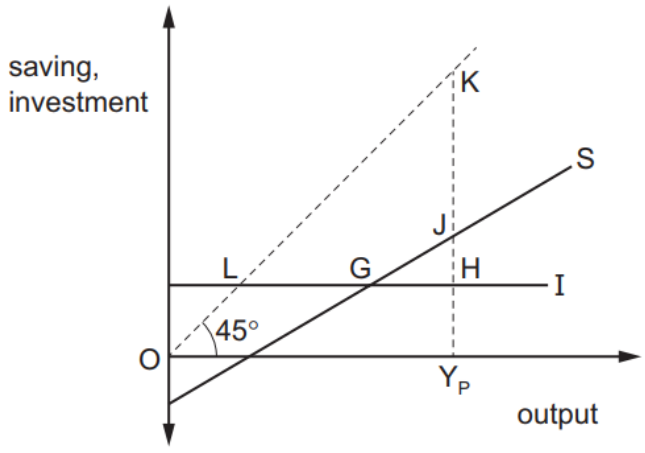
	C	I	S	G	T	X	M
I.	400	150	80	150	200	120	100
II.	450	150	100	150	230	120	90
III.	480	150	110	150	210	120	100
IV.	520	150	120	150	210	120	90

15. What will result in the short run from rising unemployment in an economy?
    I. The government's budget deficit will fall.
    II. Any existing inflationary pressure will be reduced.
    III. Potential output will fall.
    IV. The economy's production possibility curve will move inwards.

16. In a closed economy a rise in aggregate demand is needed to increase output in the country.
What is necessary to achieve this increase in output in the economy?
    I. Enough capacity to produce the extra goods and services demanded
    II. Free trade to allow imports to make up any shortages in supply
    III. Government spending to be less than tax revenue
    IV. Reduced credit to lower inflation

17. Other things remaining equal, what will reduce the level of national income in an economy?
    I. A fall in planned savings
    II. A fall in the marginal propensity to import
    III. An increase in the average propensity to consume
    IV. A reduction in the level of defence expenditure

18. The diagram shows the saving and investment curves of a closed economy with no government.



The potential level of output is OYP.

Which distance measures the gap between actual and potential output?

I. KJ
II. JH
III. LG
IV. GH

19. The table shows the values of selected macroeconomic variables over a two-year period.

	Year 1 (Rs.m)	Year 2 (Rs.m)
investment	250	350
saving	280	340
government expenditure	150	200
taxation	140	200
exports	200	250
imports	180	260
equilibrium national income	3600	4200

What is the value of the multiplier?

I. 3
II. 4
III. 6
IV. 12

20. Which row correctly identifies net injections into a country's circular flow of income?

	government expenditure > taxation	savings > investment	exports > imports
I.	no	no	yes
II.	no	yes	no
III.	yes	no	yes
IV.	yes	yes	no

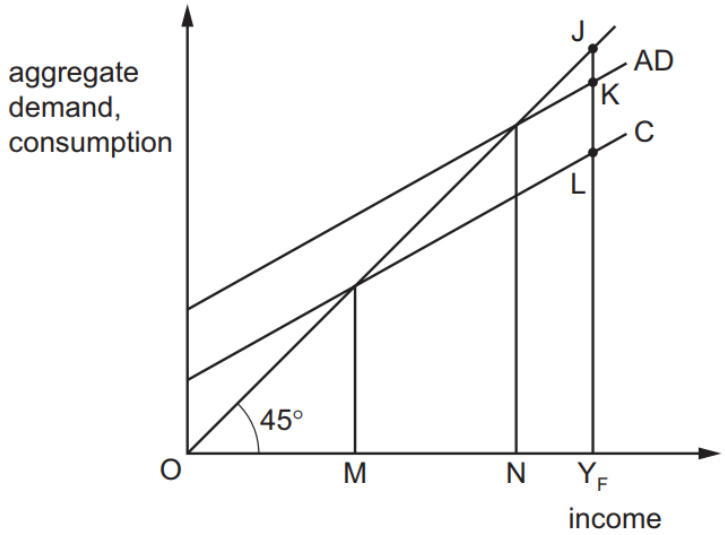
21. In an economy with no government sector:

C = consumption
I = investment
X = exports
M = imports
Y = national income

If C = 40 + 0.5Y, I = 80, X = 100 and M = 100, what will be the equilibrium level of Y?

I. 60
II. 240
III. 280
IV. 640

22. The diagram shows a closed economy in which the full employment level of income is YF.



Which distance measures the deflationary gap?

I. JK
II. JL
III. NY_F
IV. MY_F

23. What moves from households to firms within the circular flow of income?

I. Factor services
II. Investment
III. Savings
IV. Taxes

24. What is an appropriate government policy for closing a deflationary gap?

I. An increase in the rate of interest
II. An open market sale of bonds
III. An increase in government spending
IV. An increase in income tax

25. What is the value of the multiplier in an economy with no government where the marginal propensity to save is $^1/_6$ and the marginal propensity to import is $^1/_3$?

I. $^1/_2$
II. $1\ ^1/_2$
III. 2
IV. 3

			Year								
	Part A	Topic	2018	2017	2016	2015	2014	2013	2012	2011	2010
Essay	Q5	Equilibrium level of national income	1	2	1	2	1	1	1	1	1
		Main circular flow of income							1		
		Business cycle		1							
		Aggregate demand		1	1					1	1
		Consumption and savings function	1	1					1	1	1
		Leakages and injections	1	1					1		
		Autonomous and induced expenditure	1			1					
		MPC, MPS, APC, APS	1								
		Autonomous expenditure		1							
		Multiplier effect	1			1	1	2			
		Unplanned change in inventory		1						1	
		Inflationary and deflationary gap						1			

Past Paper Question 2018 -2004

1. Macroeconomic equilibrium and Equilibrium level of national income

1. What is meant by the equilibrium level of national income? What are the conditions required for the equilibrium level in national income in an open economy? (4 marks) (A/L 2015)

2. Explain what is meant by equilibrium level of national income. What are the conditions required for the equilibrium in national income level? (06 marks) (A/L 2012)

3. How is the equilibrium level of income determined in an open economy? (03 marks) (A/L 2009)

4. Briefly explain macroeconomic equilibrium in an open economy. (4 marks) (A/L 2005)

2. Equilibrium level of national income Vs. full employment level of national income

5. "The equilibrium level of national income, is not necessarily equal to the full employment level of national income". Explain this statement. (4 marks) (A/L 2017)

3. Main circular flow of income

6. Sketch a circular flow of goods, services and resources through households and firms. Draw money flows also in the same diagram indicate the direction of each flow. (04 marks) (A/L 2012)

4. Business cycle

7. Why do we consider a business cycle expansion to be different from economic growth? (4 marks) (A/L 2017)

5. Aggregate expenditure and Aggregate demand

8. What are the components of aggregate expenditure in an open economy? Define each component. (06 marks) (A/L 2011)

9. Define 'aggregate demand'? (02 marks) (A/L 2009)

10. How does aggregate demand determine the level of income? (04 marks) (A/L 2009)

6. Leakages and injections

11. Explain what is meant by "injections" and "leakages" from the circular flow of income and identify the leakages in the aggregate expenditure in an open economy with government activities. (4 marks) (A/L 2017)

12. Why is saving called a 'leakage'? (02 marks) (A/L 2012)

13. Explain what is meant by "injections" and "withdrawals" from the circular flow of income in an open economy. (4 marks) (A/L 2004)

7. Changes in savings and investment

14. Suppose in a closed economy, planned saving is greater than planned investment. Under such situation explain how the economy achieves equilibrium level of national income. (4 marks) (A/L 2015)

15. Explain how changes in savings and investment influence the level of economic activity. (04 marks) (A/L 2009)

8. Consumption and Savings Function

16. What is the relationship between the savings function and the consumption function? (02 marks) (A/L 2011)

9. Autonomous and Induced consumption

17. Distinguish between induced consumption and autonomous consumption. (4 marks) (A/L 2018)

18. Consider the following aggregate consumption function: (A/L 2015)

    $$C = a + bY_d$$

    In this equation, C is aggregate consumption expenditure and Yd is the disposable national income level. Explain how you interpret the coefficients **a** and **b.** (4 marks)

10. MPC and MPS

19. Why is the sum of the marginal propensity to consume and the marginal propensity to save always equal to one? (3 marks) (A/L 2004)

11. Diagrams

20. Explain the macroeconomic equilibrium of a simple economy using a diagram. (4 marks) (A/L 2014)

21. "The simple income-expenditure model of income determination shows that that the economy can be in equilibrium with **either** inflation or unemployment **or** neither" Explain using appropriate diagrams. (04 marks) (A/L 2013)

22. Explain graphically the determination of the equilibrium GDP through **bath** the aggregate expenditure approach and the leakages-injections approach, for an economy comprising of government sector and foreign trade sector. (06 marks) (A/L 2010)

23. Using an appropriate diagram explain what is meant by the equilibrium level of national income. (05 marks) (A/L 2008)

12. Calculations

24. Consider the following macroeconomic data for an economy. (A/L 2018)

    $C = 60 + 0.8\ Y_D$ I = 100 G = 200 T = 150 Tr = 75

Y_D	=	Disposable National Income
I	=	Investment
T	=	Taxes
C	=	Consumption
G	=	Government purchases
Tr	=	Transfers

a) What is the savings function of this economy? (2 marks)
b) When Y_D = 500, Calculate the average propensity to consume and average propensity to save? (4 marks)
c) What is the equilibrium level of National Income? (4 marks)
d) What is the value of the investment multiplier? (2 marks)

25. Assume in a hypothetical economy that government purchases (G) are Rs. 400 billion, taxes (T) are Rs. 300 billion, and private savings (S) are Rs. 200 billion and private investment (I) is Rs. 250 billion.
What is the value of net exports of this economy? (4 marks) (A/L 2018)

26. Suppose an aggregate consumption faction for a simple economy is given by C = 100 + 0.8 Y. While investment is given by I = 200. (A/L 2017)
a) What is the equilibrium level of income in this economy? (2 marks)
b) What is the level of saving at the equilibrium? (2 marks)
c) If, for some reason, aggregate output were at the level of 1700, what would the level of involuntary inventory accumulation be? (2 marks)

27. Assume that GDP (Y) is Rs. 6000 million, personal disposable income is Rs. 5100 million. Government budget deficit is Rs. 200 million, consumption expenditure is Rs. 3800 million and trade deficit is Rs. 100 million. (A/L 2017)
a) What is the amount of savings (S)? (2 marks)
b) What is the size of investment (I)? (2 marks)
c) How much is government spending (G)? (2 marks)

28. The following macroeconomic data are given for an economy. (All figures are in Rs. Million) (A/L 2016)

Autonomous consumption	=	500
Planned investment (I)	=	1250
Government purchases (G)	=	1000
Net exports (NX)	=	-250
Marginal propensity to consume (MPC)	=	0.8

Determine the equilibrium level of National income for this economy. (04 marks)

29. The following macroeconomic data are given for an economy. (All figures are in Rs. Million) (A/L 2016)

National Income	=	1 000
Consumption	=	500
Government Expenditure	=	250
Net exports	=	100
Budget deficit	=	40

a) Calculate disposable national income. (02 marks)
b) What is the value of investment of this economy? (02 marks)

30. The following macroeconomic data is given for a closed economy: (All figures are in Rs. Million) (A/L 2015)

Consumption (c)	=	$50+0.8\ Y_d$
Investment (I)	=	120
Government purchases (G)	=	100
Taxes (T)	=	80
Government transfers to households (Tr.)	=	55

a) Determine the equilibrium level of national income for this economy. (2 marks)
b) If Government purchases rises to Rs. 200 million, what would be the new equilibrium level of national income? (2 marks)
c) What is the value of the government expenditure multiplier? (2 marks)
d) If the government intends to achieve a target level of the national income of Rs. 2000 million, what would be the required level of total government purchases? (2 marks)

31. Suppose that for a particular closed economy, for some given time period, investment was equal to 100, government purchases were equal to 75, net taxes were fixed at 100, and consumption (C) given by the consumption function,

$$C = 25 + 0.8\ Y_d$$

Where, Yd is disposable income. (A/L 2013)

a) What are the values of the government expenditure multiplier and the tax multiplier? (04 marks)
b) Suppose that the full-employment level of income for this economy is 1000. What would be the increase in government spending required to reach full-employment income level? Alternatively, what reduction in tax collection would be sufficient to reach full-employment income level? (04 marks)

32. Assume that, without taxes the consumption schedule of an economy is as shown below: (Figures are in Rs. billion) (A/L 2012)

GDP (Y)	Consumption (C)	GDP (Y)	Consumption (C)
100	120	400	360
200	200	500	440
300	280	600	520

a) Graph this consumption schedule and derive the equation representing the consumption function. (06 marks)

b) Assume now that a lump-sum tax system is imposed, such that the government collects Rs. 20 billion in taxes at all levels of FGDP. Graph the resulting consumption schedule and derive the equation representing the new consumption schedule. (06 marks)

33. Suppose the aggregate consumption function for a simple economy is as follows. (A/L 2010)
    C = 200 + 2/3 Y
    a) What would the equation be for the aggregate savings function? (03 marks)
    b) At which level of income would savings be Zero? (02 marks)

34. From the macroeconomic data given below, calculate the Level of investment (I) and government purchases (G). (A/L 2010)

National Income (Y)	=	5,200
Disposable income (Y_d)	=	4,400
Consumption (C)	=	4,100
Budget balance (G-T)	=	150
Net exports (X-M)	=	-110

(04 marks)

35. If equilibrium national income is (Y) – 5,200, disposable income is (Yd) = 4,400, consumption is (c) = 4,100, net exports is (NX) = -110, and the budget deficit is (BD) =150, what is the level of investment (I) at equilibrium? (05 marks) (A/L 2008)

36. Consider an economy with no government, imports, or exports and with fixed prices and interest rates. The aggregate consumption function of the economy is C = 150 + 0.60 Yd and investment (i) = 50 (All figures are in Rs. Billions) (A/L 2006)
    a) What is the equilibrium level of aggregate output of this economy? (4 marks)
    b) What is the value of the investment multiplier? (2 marks)

37. Suppose a government sector is now added to the original economy described in part (i). The government spends 100 on goods and services and receives taxes of 100. (A/L 2006)
    a) What is the equilibrium level of aggregate output now?(4 marks)
    b) Full employment output in this economy is 800. Suppose government spending is raised to attain this level of output, but taxes are not changed. What level of government spending will result in an equilibrium output of 800? (5 marks)

13. Calculations and diagrams

38. For a closed economy with no government, suppose the consumption function is given by C = 100 + 0.8Y, while investment is given by I = 50. (A/L 2011)
    a) What is the equilibrium level of income of this economy?(02 marks)
    b) What is the level of savings in equilibrium? (02 marks)

c) If, for some reason, income is at the level of 800, what will the level of involuntary inventory accumulation be? (02 marks)
d) If investment (I) rises to 100, what will the effect be on the equilibrium income? (02 marks)
e) Draw a diagram indicating the equilibrium in both (a) and (d). (04 marks)

39. Some information pertaining to aggregate consumption and investment in a simple economy is given below: (A/L 2005)
    - Autonomous (determined independent of current income) consumption = Rs. 50 million.
    - Every one rupee increase in income causes 75 cents increase in consumption.
    - Investment = Rs. 100 million.

    a) Using the above information, construct the consumption and savings functions for this economy. (5 marks)
    b) Determine the equilibrium level of national income for this economy. (5 marks)
    c) Draw consumption savings and investment functions in a diagram and show the determination of equilibrium level of income. (5 marks)

14. Autonomous expenditure ($A_o = a_o - bT_o + bR_o + I_o + G_o + NX_o$)

40. Explain why a Rs. 500 million reduction in government purchases (G) will generate a larger fall in real GDP than a Rs. 500 million tax (T) increase. (4 marks) (A/L 2017)

41. Suppose the government is considering whether to reduce personal income taxes by Rs. 40 billion or to increase government expenditure by Rs. 40 billion to combat a recession. Assume that price level is constant and the Marginal Propensity to Consume (MPC) is 0.8. What effect would each of these measures have on aggregate demand? Which measure is more expansionary? Why? (05 marks) (A/L 2008)

15. Multiplier effect

42. What is the impact of investment multiplier in determining the national income? Explain with an example. (4 marks) (A/L 2014)

43. Briefly explain the meaning of the meaning of the "Investment multiplier". (04 marks) (A/L 2013)

44. Calculate the first four rounds of the multiplier effect for an increase of Rs. 100 billion in investment spending for a closed economy without a government sector where the MPC is 0.8 (4 marks) (A/L 2004)

16. Inflationary and deflationary gap

45. Distinguish between "inflationary gap" and "recessionary gap". (04 marks) (A/L 2013)