

Eastern University, Sri Lanka
Faculty of Commerce and Management
Second Year Second Semester Examination in Econ. -2003/2004 (June 2005)
ECN 2033: Advanced Economic Theory and Policy

Answer all questions

Time: Three Hours

- (01)
- (i) What is meant by value added method in national income accounting?
 - (ii) What is Autonomous consumption?
 - (iii) What is meant by real exchange rate?
 - (iv) Show the growth accounting equation
 - (v) Distinguish between fixed and flexible exchange rates
 - (vi) What is Purchasing Power Parity (PPP)?
 - (vii) Define structural and frictional unemployment?
 - (viii) Distinguish financial investment from physical investment
 - (ix) Define the concept of full employment
 - (x) Define fiscal and monetary policies.
- (02 x10 =20)
- (02)
- (i) How does government budget affect the circular flow of income?
 - (ii) Briefly explain how double counting can be avoided in measuring GDP
 - (iii) Explain the difference between income and expenditure methods in measuring national income
 - (iv) List out the precautions that should be taken while measuring national income using the income and expenditure methods.
- (5x4=20)

(03)

- (i) Show the structure of the IS – LM Model (02 Marks)
- (ii) Graphically explain, how changes in the following determinants change the level of income in an IS model (09 Marks)
- (a) Interest rate
 - (b) Multiplier
 - (c) Autonomous spending
- (iii) Briefly explain the components of LM equation and money market equilibrium (03 Marks)
- (iv) The following equations describe an Economy (Assume that C, G etc, are being measured in billions and I as a percentage)

$$C = 0.6 (1 - t) y$$

$$t = 0.3$$

$$I = 1000 - 60 i$$

$$G = 200$$

$$L + 63.5 i = 0.3 y$$

$$\bar{M} / P = 500$$

- (a) What are the equations that describe the IS and LM curves?
- (b) What are the equilibrium levels of income and the interest rate?
- (c) Suppose that open market operations by the Central Bank increases money supply by 100
What is the new equilibrium level of income and interest rate? Show your result in a diagram and give reasons for these changes

(06 Marks)

(04)

- (i) Explain, how Crowding out affects the level of income
- (ii) Briefly explain the determinants of Net Export (Nx)
- (iii) What is a Repercussion effect?
- (v) "Balance of Payments will always balance" Explain

(4x 5=20)

(05)

- (i) Define the concept of inflation and explain wage- price spiral effect on inflation
- (ii) Briefly explain how Keynes explains the Philips curve
- (iii) What is meant by marginal efficiency of capital? How is it calculated?
- (v) Briefly explain the main features of a Business cycle

(4x 5=20)
