

UNIVERSITY OF FORT HARE

ALICE AND EAST LONDON

ECO 121/ECO 121E

DEGREE EXAMINATIONS

MAIN EXAMINATION

NOVEMBER 2018

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Time: 3 HOURS

Subject: INTRODUCTION TO ECONOMICS (MACROECONOMICS)

Marks: 100

This paper consists of 16 pages including the cover  
page

Internal Examiners

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INSTRUCTIONS

Answer All Questions in Section A

Answer ANY two Questions in Section B

Make use of relevant contemporary examples where applicable. The  
graphical illustrations must be clearly shown.

## SECTION A

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ANSWER ALL QUESTIONS IN THIS SECTION

EACH QUESTION IN THIS SECTION CARRIES 1 (ONE) MARK

### Question 1

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Which one of the following statements is incorrect?

- A. GDP estimated from the production side is also called gross value added (GVA).
- B. To estimate GDP from the expenditure side, the expenditure on final goods and services should be taken into account.
- C. GDP can also be estimated as the total value of all incomes (wages and salaries, rent, interest and profit) in the economy.
- D. The three methods of estimating GDP should in principle yield the same results.
- E. GDP can be estimated by adding the total value of primary inputs to total value of intermediate goods and services.

### Question 2

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If 2010 is the base year for real GDP calculations, we know for certain that nominal GDP:

- A. is less than real GDP in 2010.
- B. is greater than real GDP in 2010.
- C. equals real GDP in 2010.
- D. in 2009 was greater than real GDP in 2010.
- E. in 2009 was less than real GDP in 2010.

### Question 3

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To derive GDP at market prices from Gross Domestic Expenditure, we must:

- A. subtract spending on exports and add spending on imports.
- B. subtract spending on imports and add spending on exports.
- C. subtract spending on intermediate goods and add spending on exports.
- D. subtract spending on exports and add spending on intermediate goods.
- E. subtract spending on net exports.

### Question 4

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A consumer's real purchasing power refers to:

- A. the nominal income level of the consumer.
- B. wage income earned through employment.
- C. the maximum volume of goods and services that the consumer can buy.
- D. nominal GDP per capita.
- E. real GDP deflated by the price level.

#### Question 5

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Which of the following would most likely contribute to a deficit (or reduce the surplus) on the South African current account?

- A. A depreciation of the Rand.
- B. A Malaysian company invests in a South African oil company.
- C. An increase in transfers from Italian citizens to their South African relatives.
- D. A decline in imports.
- E. An increase in mine workers' transfer earnings to Mozambique.

#### Question 6

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The area between the Lorenz curve of a country and the diagonal of perfect equality represents:

- A. the area of equality.
- B. the area of inequality.
- C. The Gini coefficient.
- D. The quantile ratio.
- E. the cumulative percentage of the population.

#### Question 7

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Which one of the following statements is correct?

- A. In a monetary economy there always has to be a double coincidence of wants.
- B. Money can never lose its usefulness as a unit of account.
- C. Money is always the best possible store of value.
- D. The stock of money consists largely of notes and coins.
- E. Money is not the only possible store of value.

#### Question 8

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The repo rate is:

- A. the rate at which the SARB advances loans to the government.
- B. the best interest rate an investor can obtain on a long-term deposit.
- C. the rate at which banks provide loans to their best customers.
- D. the rate at which the SARB provides loans to other banks.
- E. the rate at which the quantity of money demanded is equal to the quantity of money supplied.

#### Question 9

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When the inflation rate is expected to exceed the target rate by a significant margin, the SARB will tend to:

- A. reduce the cost of credit to the banks.
- B. increase the repurchase rate (repo rate).
- C. purchase government bonds on the open market.
- D. decrease the repurchase rate (repo rate).
- E. use moral suasion to persuade banks to provide more loans to their clients.

#### Question 10

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Which one of the following statements is incorrect?

- A. The opportunity cost of holding money balances is the interest that could have been earned if the money had been used to purchase interest-bearing assets instead.
- B. Anyone who wishes to enter into transactions in a monetary economy has to hold money as a medium of exchange.
- C. The quantity of money demanded for transaction purposes depends on the level of income.
- D. The demand for money as an asset is also called the speculative demand for money.
- E. The quantity of money demanded for speculative purposes is positively related to the interest rate.

#### Question 11

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Which one of the following statements is incorrect?

- A. As interest rates increase, bond prices decrease.
- B. As interest rates decrease, bond prices increase.
- C. There is a positive relationship between interest rates and bond prices.
- D. If interest rates are high, the quantity of money demanded will tend to be low.
- E. If interest rates are low, the quantity of money demanded will tend to be high.

#### Question 12

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Which one of the following is not a function of the South African Reserve Bank?

- A. To formulate and implement monetary policy.
- B. To maintain financial stability.
- C. To finance government expenditure.
- D. To provide economic and statistical services.
- E. To act as banker to other banks.

**Question 13**

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The \_\_\_\_\_ demand for money arises out of the need to hold money as a medium of exchange. This demand for money is a function of \_\_\_\_\_.

- A. precautionary; interest rates
- B. transactions; national income
- C. speculative; interest rates
- D. precautionary; national income
- E. transactions; interest rates

**Question 14**

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Which of the following is not a legitimate area of intervention by government in a mixed economy?

- A. Regulation of the pricing behaviour of monopoly industries.
- B. Regulation of price increases that result from changes in patterns of demand and supply in competitive markets.
- C. Stabilisation of the economy during periods of cyclical instability.
- D. Redistribution of purchasing power via progressive taxation and transfers.
- E. The provision of funds for public goods such as parks and street lights.

**Question 15**

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Which of the following would be classed as an expansionary fiscal policy?

- A. An increase in the quantity of money.
- B. A reduction in the number of goods exempted from VAT.
- C. An increase in government taxation.
- D. An increase in government expenditure.
- E. An increase in the VAT rate.

**Question 16**

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Which one of the following statements is incorrect?

- A. Central government forms part of general government.
- B. Provincial government forms part of the public sector.
- C. Local government forms part of general government.
- D. Public corporations form part of general government.
- E. Provincial government forms part of the public sector.

**Question 17**

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Which one of the following is a direct tax?

- A. Company tax
- B. Customs duties
- C. Excise duties on tobacco and alcohol
- D. Fuel levy
- E. Value-added tax

**Question 18**

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Which of the following is least likely to be associated with market failure, and is consequently least likely to require any form of state regulation or intervention?

- A. Hake fishing off the west coast of South Africa.
- B. The provision of education services in government schools.
- C. The provision of education services in private schools.
- D. The market for fast foods.
- E. The provision of lifeguards on Durban's beaches.

**Question 19**

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A tax such as VAT would generally be viewed as:

- A. progressive, because the consumption expenditure of the rich is greater than that of the poor.
- B. regressive, because low-income households spend a greater proportion of their income on goods that attract VAT.
- C. proportional, because the VAT rate is constant across goods that attract VAT.
- D. progressive, because most goods consumed by poor households are zero rated.
- E. regressive, because the VAT burden increases as household income rises.

**Question 20**

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If government spending is higher than current government revenue, this is known as:

- A. a deficit on the current account of the balance of payments.
- B. the budget deficit.
- C. the public debt.
- D. money financing.
- E. good fiscal management.

**Question 21**

The exchange rate between the euro (€) and the US dollar (\$) is \$1,20 per euro. If an American tourist in Paris purchases a good valued at 60 euros, then in his own currency this would cost:

- A. \$50
- B. \$72
- C. \$48
- D. \$720
- E. \$18

Consider the case of two countries, Afghanistan and the US, both producing carpets and fighter aircraft. The table below shows output rates per day in the two countries if all resources are fully and efficiently employed. Use this information to answer Question (22), (23) and (24).

	Carpets	Fighter aircraft
Afghanistan	100	4
US	500	25

**Question 22**

Based on this information:

- A. there is no opportunity for mutually beneficial trade between the two countries.
- B. Afghanistan has an absolute advantage in the production of both goods.
- C. Afghanistan should import carpets from the US.
- D. Afghanistan has a comparative advantage in the production of aircraft.
- E. the US should export fighter aircraft to Afghanistan.

**Question 23**

An appropriate international exchange ratio that would allow mutually advantageous trade to take place would be:

- A. 1 aircraft = 25 carpets.
- B. 1 aircraft = 20 carpets.
- C. 1 carpet = 4 aircraft.
- D. 1 carpet = 0,04 aircraft.
- E. 1 aircraft = 22 carpets.

**Question 24**

If Afghanistan raised its aircraft productivity to 5 units per day, then:

- A. mutually beneficial trade would no longer be possible.
- B. Afghanistan would continue to import fighter aircraft from the US.
- C. Afghanistan should switch from the export of carpets to the export of aircraft.
- D. the US would retain its comparative advantage in carpet manufacture.
- E. the US would retain its absolute disadvantage in the manufacture of both goods.

**Question 25**

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South Africa has a comparative (relative) advantage over France in the production of maize if it:

- A. produces maize with fewer material inputs than France.
- B. can match France's output of maize and have resources left over.
- C. can produce maize with the same resources as France but faster.
- D. has an absolute advantage over France.
- E. produces maize at a lower opportunity cost than France.

**Question 26**

Which one of the following would not necessarily enhance economic growth in South Africa?

- A. Technological improvements.
- B. Increased labour productivity through on-the-job training.
- C. Higher levels of net investment in the economy.
- D. Higher levels of government spending that raise local interest rates.
- E. All of the above.

**Question 27**

Investment in human capital:

- A. can be illustrated by a shift of the aggregate supply curve to the left.
- B. increases structural unemployment.
- C. increases labour productivity.
- D. can be illustrated by a shift of the Phillips curve to the right.

**Question 28**

During a recession, cyclical unemployment will \_\_\_\_\_ and cyclical inflation will \_\_\_\_\_.

- A. decrease; decrease
- B. decrease; increase
- C. increase; increase
- D. increase; decrease

**Question 29**

The phase of the business cycle at which almost all available resources in the economy are in use is referred to as:

- A. the recovery phase.
- B. the expansion phase.
- C. the peak or boom phase.
- D. the trough phase.

**Question 30**

Keynesians believe that the fluctuations in economic activity (business cycles):

- A. are caused by external factors such as the inappropriate use of government policy.
- B. are caused by changes in weather patterns.
- C. are caused by structural or institutional changes.
- D. occur naturally in market economies and require government intervention.

**Question 31**

Capital widening refers to:

- A. a situation where capital replaces labour in the production process.
- B. a situation where the capital to labour ratio in the economy increases.
- C. a situation where additional purchases of capital are made in order to match a growing labour force.
- D. a situation where labour replaces capital in the production process.
- E. an increase in the current account deficit as more capital is imported.

**Question 32**

Import substitution involves:

- A. the reduction of import tariffs so that an economy can export goods that were previously imported.
- B. the use of import tariffs so as to encourage the local production of goods that were previously imported.
- C. the protection of industries in which an economy would traditionally have enjoyed comparative advantage.
- D. the substitution of local labour with imported capital so as to reduce the costs of production and ensure the competitiveness of strategic industries.

**Question 33**

According to Keynesian economists, during a boom in economic activity:

- A. the quantity of money should be increased.
- B. interest rates should be cut.
- C. government should increase its spending.
- D. tax rates should be raised.
- E. all of the above should be undertaken

**Question 34**

Which one of the following statements is incorrect?

Economic growth:

- A. may be measured as the annual rate of increase in real GDP.
- B. may be measured as the annual rate of increase in GDP at constant prices.
- C. may be measured as the annual rate of increase in GDP at current prices.
- D. should preferably be measured on a per capita basis.

**Question 35**

Which one of the following is not a problem associated with GDP?

- A. GDP pertains only to production inside the country.
- B. The estimation of the value of production that is not sold in a market.
- C. Many activities are not recorded.
- D. GDP data are inevitably revised as more and better information become available.
- E. GDP is not a good measure of economic welfare.

**Question 36**

People leave the labour force when they:

- A. find employment.
- B. become unemployed.

- C. retire.
- D. work in the informal sector.
- E. all of the above

**Question 37**

Which one of the following statements is true? In South Africa:

- A. rising unemployment has been associated with increased foreign competition.
- B. school-leavers, who cannot find employment, qualify for unemployment benefits.
- C. most unemployment is frictional unemployment.
- D. all unemployment is voluntary.
- E. there is a negative correlation between unemployment and crime.

**Question 38**

If a country's rate of unemployment increases then we can conclude that:

- A. the country is experiencing jobless growth.
- B. no new jobs are being created.
- C. GDP growth must be falling.
- D. the proportion of people of working age who want employment and who cannot find employment is increasing.
- E. all of the above are true.

**Question 39**

During an economic downturn, sales fall and some workers lose their jobs. This unemployment is referred to as:

- A. seasonal unemployment.
- B. frictional unemployment.
- C. cyclical unemployment.
- D. structural unemployment.
- E. technological unemployment.

**Question 40**

Pitso resigns his job as an economist in Durban and moves to Port Elizabeth to be closer his parents. It takes Pitso three months to find new employment as an economist in Port Elizabeth. During these three months, Pitso was:

- A. structurally unemployed.
- B. seasonally unemployed.
- C. cyclically unemployed.
- D. casually unemployed.
- E. frictionally unemployed.

**Question 41**

Which of the following situations describe structural unemployment?

- i. Julia is qualified as an economist, but cannot find employment because employers prefer to hire male economists.
- ii. Jacob used to work in a gold mine and lost his job after the price of gold fell and the mine closed.
- iii. Johanna is a typist and cannot find employment because she does not know how to use a word processor (personal computer).
- iv. Jim can only find work as a tourist guide on the Cape Wine Route during the summer months.

- A. i, ii and iii
- B. i, ii, iii and iv
- C. ii, iii and iv
- D. i and iv
- E. i, ii and iv

**Question 42**

Reasons on the demand-side of the labour market for increasing unemployment in South Africa could include:

- i. an increase in population growth.
- ii. an increase in the capital intensity of production.
- iii. an increase in immigration.
- iv. a decrease in the production of goods and services.
- v. an increase in the cost of employing labour.

- A. i, iii and v
- B. i, ii and iv
- C. ii, iv and v
- D. ii and iv
- E. i and iii

**Question 43**

Which of the following might be expected to generate employment?

- A. Economic growth that is capital intensive.
- B. Higher taxes for small businesses.
- C. An increase in the wage rate, ceteris paribus.
- D. A fall in the productivity of workers.
- E. The promotion of exports and investment.

**Question 44**

Which of the following would NOT be expected to generate employment?

- A. Easier access to credit for small business.
- B. Public works programmes.
- C. An increase in imports.
- D. An increase in the labour intensity of production.
- E. A decrease in the relative price of labour.

**Question 45**

In an industry, if wages increase more than the productivity of workers, we would expect:

- A. an upward pressure on prices.
- B. a decrease in unemployment.
- C. investment in the industry to increase.
- D. costs of production to fall.
- E. the demand for labour to rise.

**Question 46**

Which one of the following statements about inflation is true? Inflation refers to:

- A. a sudden and self-contained increase in prices.
- B. a small increase in prices.
- C. "too much money chasing too few goods".
- D. a sustained increase in the general price level.
- E. an increase in the purchasing power of money.

**Question 47**

If the consumer price index at the end of 2011 was 100 and at the end of 2012 was 120, then the rate of inflation for 2012 was:

- A. 25%.
- B. 20%.
- C. 16,66%.
- D. 1,5%.
- E. -16,66%.

**Question 48**

Use the table below to answer the question.

Year	GDP at current prices	GDP at constant 2012 prices	GDP deflator
2011	400 000	600 000	A
2012	500 000	B	C

- i. In the table above, A, B and C are respectively equal:
  - A. 66,67, 500 000 and 100.
  - B. 80, 900 000 and 100.
  - C. 133,33, 600 000 and 66,67.
  - D. 66,67, 600 000 and 1.
  - E. 133,33, 500 000 and 100.

**Question 49**

If inflation was 10% in a particular year and you received a 20% increase in income during the same year, then over the year your:

- A. real and nominal income both fell.
- B. real and nominal income both rose.
- C. real income fell, but nominal income rose.
- D. real income rose, but nominal income fell.
- E. nominal income rose, but real income was unchanged.

**Question 50**

Bracket creep would be eliminated if tax rates were based on:

- A. nominal income.
- B. real income.
- C. per capita income.
- D. real disposable income.
- E. nominal disposable income.

**SECTION B**

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**ANSWER ANY TWO QUESTIONS IN THIS SECTION**

**EACH QUESTION CARRIES EQUAL MARKS**

**Question Two [25 Marks]**

- A. Explain the difference between the ability to pay principle and the benefit principle with regards to taxation. [4]
- B. Briefly explain the three different approaches to measuring GDP in an economy. [6]
- C. What are the main determinants of the demand for money? Explain the link between each determinant and the quantity of money demanded. [6]
- D. Draw a demand and supply curve for British pounds (on the vertical axis plot rand per British pound).
  - i. What factors are likely to cause an increase in the demand for British pounds (in exchange for South African rands) and how can this be illustrated in the diagram you have drawn?
  - ii. Does this represent an appreciation or depreciation of the South African rand relative to the British pound? [9]

**Question Three [25 Marks]**

- A. Define the consumer price index. [3]

- B. Explain the difference between progressive, proportional and regressive taxes and give an example of each type. [6]
- C. Discuss the different roles that money can assume in an economy. [8]
- D. A country produces only two products: gold and platinum. In 2005 the country produced 100 tons of gold at R500 000/ton and 60 tons of platinum at R1 000 000/ton.

In 2006 the country produced 90 tons of gold at R600 000/ton and 80 tons of platinum at R1 100 000/ton.

- i. Calculate the value of nominal GDP in 2005.
- ii. Calculate the value of GDP at current prices in 2006.
- iii. Calculate the value of GDP in 2006 at constant 2005 prices.
- iv. When comparing the performance of the economy over time, should one calculate the growth rate in real or nominal GDP? Explain. [8]

Question four

- A. How does a proportional income tax affect: (a) autonomous spending, (b) aggregate spending and (c) the multiplier? [9]
- B. Can monetary and fiscal policy be used to counteract (or combat) demand-pull inflation? Use a diagram (or diagrams) to explain your answer. (10)
- C. What is meant by the consumption function? Use a diagram to explain the three main characteristics of the consumption function. [6]

[25 Marks]

Question five

- A. Use the AD-AS model to illustrate and explain how the authorities can use monetary and fiscal policies to stimulate the economy. What side-effects would such policies have? What is the significance of the slope/condition of the AS curve in this regard? [10 Marks]
- B. Describe the various lags associated with monetary and fiscal policy. [7 Marks]
- C. What type of unemployment does each of the following represent? Explain your answers.

- (i) Workers at a clothing factory in Newcastle lose their jobs when the firm relocates to Lesotho.
- (ii) Workers at a factory making cassette tapes lose their jobs when the firm goes under due to competition from compact discs.
- (iii) Migrant farm workers' employment is terminated when the harvest is finished.
- (iv) Workers at the BMW plant in Rosslyn are laid off as a result of a slump in motorcar sales. [8 Marks]

[25 Marks]

**SECTION A: MULTIPLE CHOICE ANSWER SHEET**

NAME.....STUDENT NO:..... COURSE.....

Indicate your choice by making a CROSS in the choice block:

Question number	Options: choose only one				
	USE an 'X' to select your answer				
1	a	b	c	d	e
2	a	b	c	d	e
3	a	b	c	d	e
4	a	b	c	d	e
5	a	b	c	d	e
6	a	b	c	d	e
7	a	b	c	d	e
8	a	b	c	d	e
9	a	b	c	d	e
10	a	b	c	d	e
11	a	b	c	d	e
12	a	b	c	d	e
13	a	b	c	d	e
14	a	b	c	d	e
15	a	b	c	d	e
16	a	b	c	d	e
17	a	b	c	d	e
18	a	b	c	d	e
19	a	b	c	d	e
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21	a	b	c	d	e
22	a	b	c	d	e
23	a	b	c	d	e
24	a	b	c	d	e
25	a	b	c	d	e
26	a	b	c	d	e
27	a	b	c	d	e
28	a	b	c	d	e
29	a	b	c	d	e

30	a	b	c	d	e
31	a	b	c	d	e
32	a	b	c	d	e
33	a	b	c	d	e
34	a	b	c	d	e
35	a	b	c	d	e
36	a	b	c	d	e
37	a	b	c	d	e
38	a	b	c	d	e
39	a	b	c	d	e
40	a	b	c	d	e
41	a	b	c	d	e
42	a	b	c	d	e
43	a	b	c	d	e
44	a	b	c	d	e
45	a	b	c	d	e
46	a	b	c	d	e
47	a	b	c	d	e
48	a	b	c	d	e
49	a	b	c	d	e
50	a	b	c	d	e