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1 (Sem-4) ECO 2

2025

ECONOMICS

Paper : ECO0400204

(Advanced Macroeconomics)

Full Marks : 60

Time : 2½ hours

The figures in the margin indicate full marks for the questions.

1. All the questions are compulsory : $8 \times 1 = 8$
 - (a) In the IS-LM model, what happens to equilibrium income when government spending increases ?
 - (b) What is the effect of an increase in money supply on LM curve.
 - (c) Name *one* limitation of Harrod-Domar Model.
 - (d) What is meant by diminishing returns to capital in the Solow Model.
 - (e) Given the consumption function: $C = 1000 + 0.27Y$. Calculate the value of MPS.
 - (f) State whether the following statement is True or False : Keynes thought that income is the primary determinant of consumption and that interest rate does not influence consumption.

- (g) State *one* similarity between the Life Cycle Hypothesis and Permanent Income Hypothesis.
- (h) What will be the effect of an increase in relative price of housing on the flow of residential investment ?

2. Answer **any six** out of the following : $2 \times 6 = 12$

- (a) State the effect of an increase in interest rate on the firm's inventory to sales ratio.
- (b) Define MEC.
- (c) State Keynes' Psychological Law of Consumption.
- (d) What are the factors that may lead to an increase in demand for housing ?
- (e) Briefly explain the concept of Purchasing Power Parity (PPP).
- (f) What are the *two* main components of the Balance of Payments ?
- (g) What is the difference between warranted growth and natural growth in Harrod-Domar Model ?
- (h) Name *two* key factors that drive endogenous growth.
- (i) What happens to an economy's unemployment and inflation rate, if the Central Bank repeatedly increases the money supply ?
- (j) What are the determinants of Induced Investment ?

3. Answer **any four** out of the following :

$5 \times 4 = 20$

- (a) Distinguish between anticipated and unanticipated inventory investment.
 - (b) Briefly discuss the Permanent Income Hypothesis of Consumption.
 - (c) Briefly discuss the anomalies with Keynes' Consumption Function.
 - (d) Discuss how fiscal policy affects output and interest rates in the IS-LM framework.
 - (e) Analyse the impact of monetary expansion on income and interest rates in the IS-LM Model.
 - (f) Discuss the role of savings and investment in economic growth as per the Solow Model.
 - (g) Briefly discuss the Accelerator model of Inventories.
 - (h) The following equations describe an economy consumption function ; $C = 200 + 0.6Y$
Government Spending, $G = 600$
Investment, $I = 900 - 50r$
Money Demand Function, $L = 0.25Y - 62.5r$
Real money supply, $\frac{M}{P} = 50$
 C, I, G are measured in cross and r in %.
- (i) Find the equation of IS Curve
 - (ii) Find the equation of the LM Curve

4. Answer **any two** out of the following :

10×2=20

- (a) Discuss a firm's decision to add capital stock or not using the Neo-Classical model of investment.
- (b) Explain the multiplier and accelerator interaction process that results in cyclical fluctuations in economic activity.
- (c) Illustrate that the trade-off between inflation and unemployment in the short-run and why it doesn't work in the long-run.
- (d) Derive the IS and LM curves and explain how they interact to determine equilibrium income and interest rates in a closed economy.
- (e) Describe the Mundell-Flemming Model under a fixed exchange rate system and perfect capital mobility.