

NATIONAL UNIVERSITY OF LESOTHO
BA SUPPLEMENTARY EXAMINATIONS
EC2502: INTERMEDIATE MACROECONOMICS

AUGUST 2023

TIME: 3 HOURS

MARKS 100

Instructions:

- 1. There are two sections, answer **all** questions from each section.*
- 2. Show all necessary workings and make clear drawings of graphs.*

SECTION A

Question 1

Explain how each of the following events affect the monetary base, the money multiplier, and the money supply.

- a) The Central Bank buys bonds in an open market operation. [5]
- b) The Central Bank increases the interest rate it pays banks for holding reserves. [5]
- c) The Central Bank reduces its lending to banks through its Term Auction Facility. [5]
- d) Rumors about a computer virus attack on ATMs increase the amount of money people hold as currency rather than demand deposits. [5]
- e) The Central Bank of Lesotho flies a helicopter over Maseru City and drops newly printed M100 bills. [5]

Question 2

Use the model of the small open economy to predict what would happen to the trade balance, the real exchange rate, and the nominal exchange rate in response to each of the following events:

- a) A fall in consumer confidence about the future induces consumers to spend less and save more. [5]
- b) A tax reform increases the incentive for businesses to build new factories. [5]
- c) The introduction of a stylish cars make some consumers prefer foreign cars over domestic car. [5]
- d) The Central Bank doubles the money supply. [5]
- e) New regulations restrict the use of credit cards increase the demand for money. [5]

SECTION B

Question 3

- a) Use a graph of the *Keynesian Cross* to show the impact of an increase in planned investment on the equilibrium level of income/output. [5]
- b) Why is the *IS* curve negatively sloped? [3]
- c) How will the Fiscal Policy Shifts the *IS* Curve? [4]
- d) Draw a separate diagram of the *AD* curve for each scenario and show on the diagram what happens to the curve if:
- i. A ten-year-old investment tax credit expires. [5]
 - ii. The Lesotho exchange rate falls. [4]
 - iii. A fall in prices increases the real value of consumers' wealth. [4]

Question 4

- a) The Lesotho Bureau of Statistics Systematic Diagnostic Update (2022) notes that most of the investment in the country is led by the government. This has increased government debt and tends to crowd out private investment. Therefore, the government is advised to raise private investment. Use the IS–LM model to explain a mix of monetary and fiscal policy that will achieve higher investment but keep output constant. [12]
- b) Discuss briefly the organizational structure of secondary markets in an economy. [4]
- c) Succinctly discuss the following:
- i) Money Market Securities [3]
 - ii) Capital Market Securities [3]
- d) The role of financial system/institutions is to facilitate the flow and efficient allocation of funds in the economy. Use an appropriate diagram to describe the transfer of funds from the surplus to the deficit spending units. [3]