

ECS1601	(496289)	October/November 2011
ECS1028	(471125)	
REC102Y	(490157)	
REC1601	(472444)	

ECONOMICS 1B

Duration 2 Hours

100 Marks

EXAMINERS

FIRST

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SECOND

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Use of a non-programmable pocket calculator is permissible.

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This partial fill-in paper consists of 16 pages plus instructions for the completion of a mark-reading sheet

Read the following instructions **CAREFULLY** before answering the paper

The paper is divided into two sections Section A and Section B

SECTION A

Candidates must answer **ALL** the questions in this section

SECTION B

In this section ALL the questions must be answered on the mark-reading sheet which is supplied
Carefully follow the instructions for the completion of the mark-reading sheet

Please ensure that you use the correct unique number on the mark-reading sheet
 If you are registered for ECS1601, use the unique number 496289
 If you are registered for ECS1028, use the unique number 471125
 If you are registered for REC102Y, use the unique number 490157
 If you are registered for REC1601, use the unique number 472444

As your mark-reading sheet can get lost, you **MUST** also write down your answers for this section On the last page of this paper space is provided for this purpose

SECTION A [50 MARKS]

Answer ALL the following questions in the blocks provided

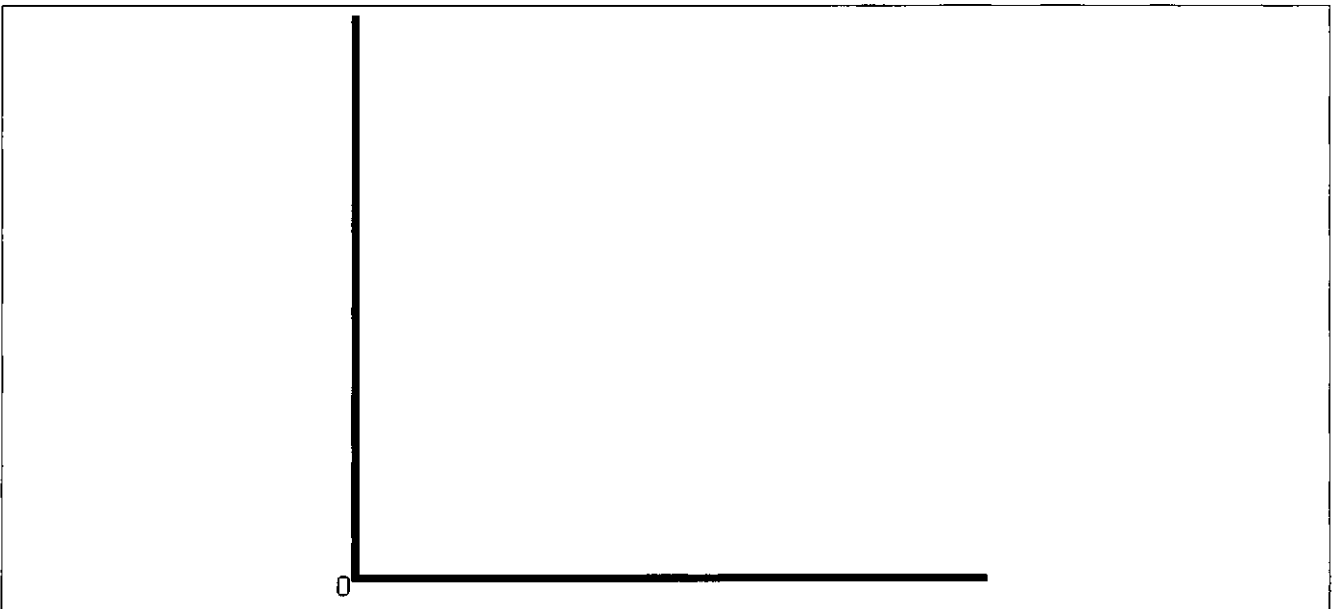
QUESTION 1 [7]

- (i) Define the Gross Domestic Product (GDP) (4)

- (ii) Define inflation (3)

QUESTION 2 [15]

- (i) Use the following diagram to show how the equilibrium in the money market changes if the level of income in the economy **increases**. Remember to label your diagram (3)



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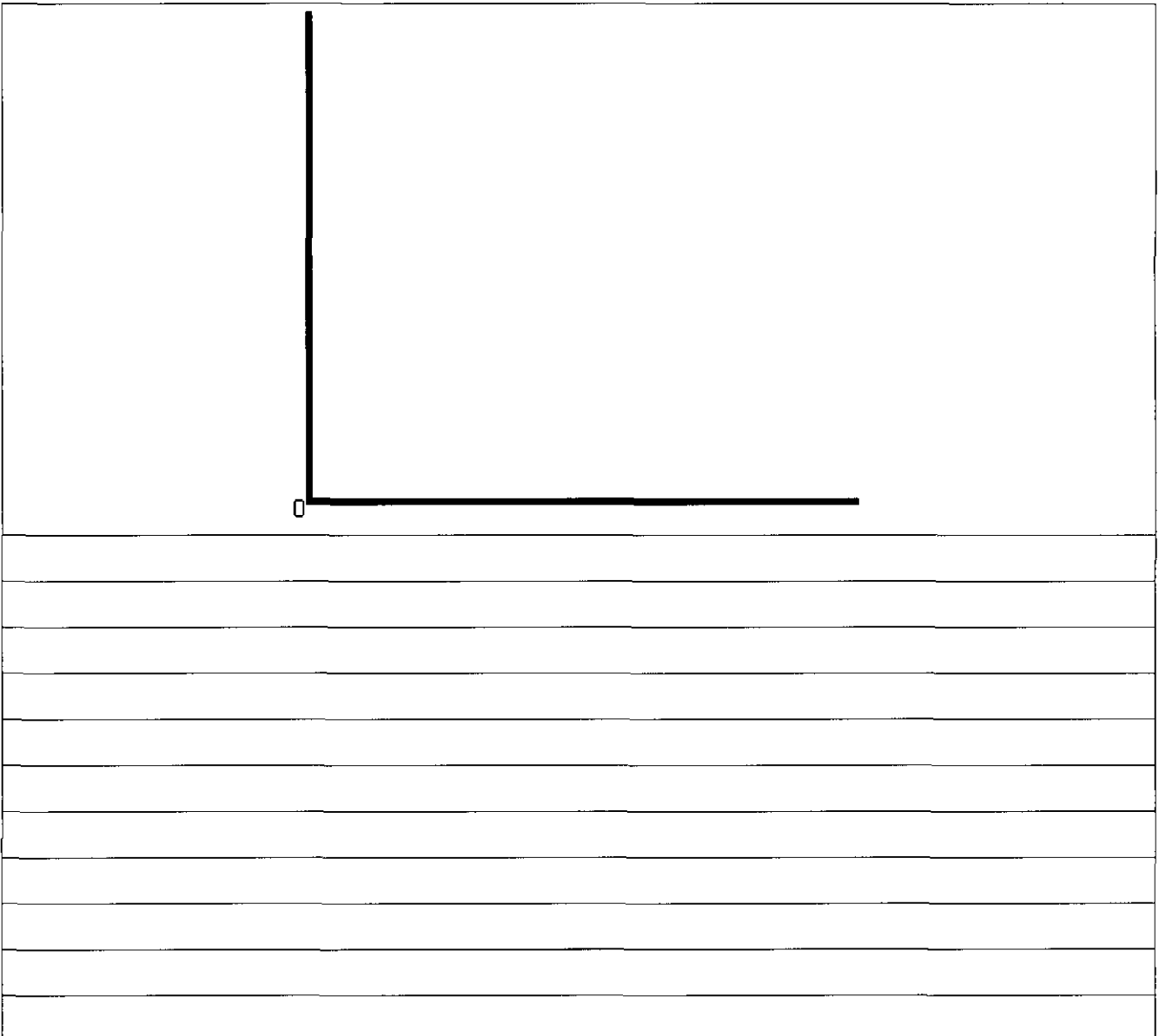
- (ii) Illustrate on the following diagram of the South African foreign exchange market what will happen to the exchange rate between the rand and the US dollar if South Africa implements import substitution measures. Remember to label your diagram. (3)



- (iii) You are the chief economic advisor for the government of Mahala. Mahala is experiencing demand-pull inflation despite the stated objective of the government to achieve price stability.

Explain, with the aid of the following diagram, what steps the government of Mahala should take to achieve this objective. (9)

- Clearly indicate on the diagram any changes to aggregate demand or aggregate supply, prices and production that might result from the actions taken by the government. The diagram counts three (3) marks.
- In your explanation you must deal with the following:
The instruments of fiscal policy, how they are applied and what effects they have.
Your explanation counts six (6) marks.

**QUESTION 3****[11]**

Given the following information

$$C = 400 + 0,8Y_d$$

$$T = 0,2Y$$

$$\bar{G} = 450$$

$$\bar{I} = 300$$

$$\bar{X} = 600$$

$$Z = 200 + 0,1Y$$

[TURN OVER]

Calculate (Show all your calculations)

- the multiplier (2)

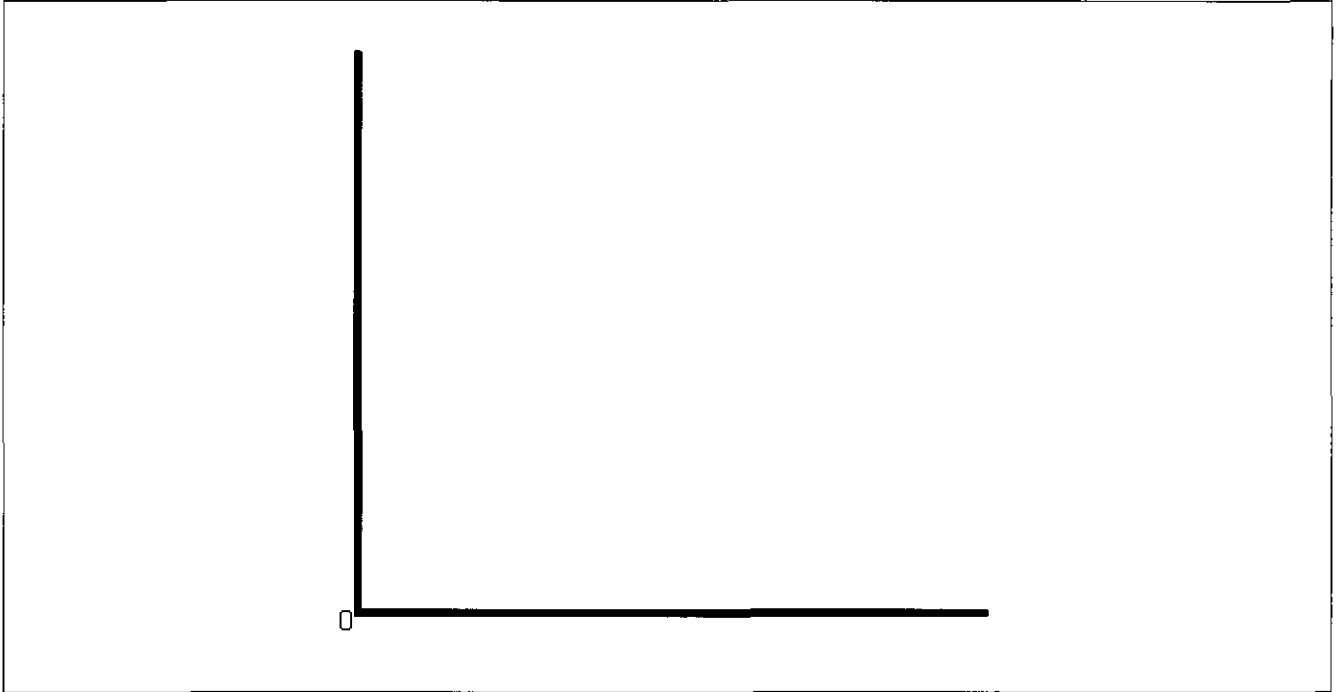
- the equilibrium level of income (2)

- the value of induced imports at the equilibrium level of income (2)

- the value of net exports at the equilibrium level of income (2)

[TURN OVER]

- Use the following set of axis to draw a diagram of the model. Clearly indicate the values of total autonomous expenditure and the equilibrium level of income (3)



QUESTION 4

[17]

- (i) The Swaziland government has discovered some diamond deposits in an area that is about 40km from the country's largest city, Mbabane. Explain how this discovery will affect the value of the Swaziland currency (the Lilangeni) (3)

- (ii) Distinguish between active balances and passive balances and mention the main determinant of the quantity demanded of each (4)

[TURN OVER]

- (iii) Use the aggregate demand-aggregate supply model to explain how an **increase** in the repo rate will affect the level of production and income in the economy (5)

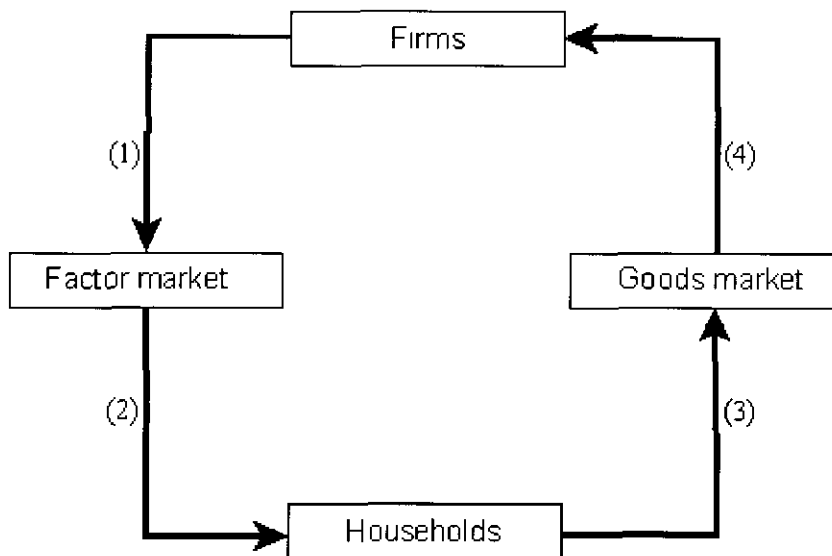
- (iv) Explain why policy makers cannot solve the stagflation dilemma using only demand management policies (5)

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SECTION B [50 MARKS]

Answer **ALL** the questions in this section on the mark-reading sheet which is supplied. Each question is worth 1¼ marks. **Note** Only **ONE** statement per question is correct.

- 1 The diagram below shows the circular flow of income and spending between households and firms.



Which one of the following statements is correct?

- [1] Flows (2) and (3) represent income
 - [2] Flows (2) and (4) represent spending
 - [3] Flows (1) and (2) represent spending
 - [4] Flows (1) and (3) represent spending
- 2 In the circular flow of income and spending, nominal Gross Domestic Product must be equal to
- [1] consumption of durable goods
 - [2] consumption of non-durable goods
 - [3] savings
 - [4] national income
- 3 Which is the largest component of the M1 money supply?
- [1] cash
 - [2] demand deposits
 - [3] travelers' checks
 - [4] savings-type deposits
- 4 When the entire banking system makes use of excess reserves to grant new loans in the form of deposits,
- [1] the credit multiplier decreases
 - [2] the credit multiplier increases
 - [3] the credit multiplier remains unchanged

[TURN OVER]

- 5 The demand for active balances will increase if
- [1] real GDP increases
 - [2] the GDP deflator decreases
 - [3] real interest rates decrease
 - [4] the supply of money increases
- 6 Commercial banks create money
- [1] by printing money
 - [2] through multiple rounds of extending loans and accepting deposits
 - [3] when they buy government bonds from the SARB
 - [4] when they decrease their desired reserve ratio
- 7 An appropriate measure of government's involvement in economic activity is
- [1] the volume of government subsidies
 - [2] the total government spending
 - [3] the share of government spending in total spending in the economy
 - [4] the growth of government spending
- 8 A good example of a pure public good is
- [1] public transport
 - [2] the national health service
 - [3] national defence
 - [4] rail transport
- 9 A tax is
- [1] regressive when all taxpayers pay the same amount of tax
 - [2] regressive when all taxpayers pay the same rate
 - [3] proportional when all taxpayers pay the same amount of tax
 - [4] proportional when it is levied on goods and services at the same standard rate
- 10 Many politicians argue that a good way to increase government's revenue is to increase the tax on gambling. Revenues from such a tax would be largest if the price elasticity of demand for gambling is
- [1] unit elastic
 - [2] highly inelastic
 - [3] highly elastic
 - [4] perfectly elastic

Consider the following table, which shows the production possibilities of the two countries A and B, and answer question 11

	Cocoa production (Output of 50 men in tons)	Tea production (Output of 50 men in tons)
Country A	90	60
Country B	20	40

- 11 Which one of the following statements is correct?
- [1] Country A has an absolute advantage in the production of both tea and cocoa, and a comparative advantage in the production of tea
 - [2] Country A has an absolute advantage in the production of both tea and cocoa, and a comparative advantage in the production of cocoa
 - [3] Country B has an absolute advantage in the production of tea, and a comparative in the production of cocoa
 - [4] Country B has an absolute advantage in the production of cocoa, and a comparative advantage in the production of tea
- 12 Given the domestic (South African) price of T-shirts is R50 and the world price is R30. Assume the South African government decides to eliminate an existing import tariff of R10 on T-shirts. As a result net exports
- [1] and domestic production will increase
 - [2] and domestic production will decrease
 - [3] will increase and domestic production will decrease
 - [4] will decrease and domestic production will increase
- 13 A decrease in the demand for USA dollar in the South African foreign exchange market would result if there is
- [1] a decrease in the South African exports to the USA
 - [2] a decrease in the gold price in South Africa
 - [3] a decrease in the South African tourists to the USA
 - [4] a decrease in the USA tourists to South Africa
- 14 If the SARB buys dollars in the South African foreign exchange market, the South African rand will
- [1] not be affected
 - [2] appreciate
 - [3] depreciate
- 15 If production remains the same and all prices double, then real GDP
- [1] and nominal GDP are both constant
 - [2] is constant and nominal GDP is reduced by half
 - [3] is constant and nominal GDP doubles
 - [4] doubles and nominal GDP is constant

[TURN OVER]

Questions 16 and 17 are based on the following information

Assume that in 2009 South Africa produced only three products soccer balls, beer bottles and vuvuzelas. Total production amounted to 12 soccer balls, 6 beer bottles and 30 vuvuzelas at a respective cost of R10, R4 and R2 each

16 The nominal GDP in 2009 was

- [1] R102
- [2] R120
- [3] R144
- [4] R204

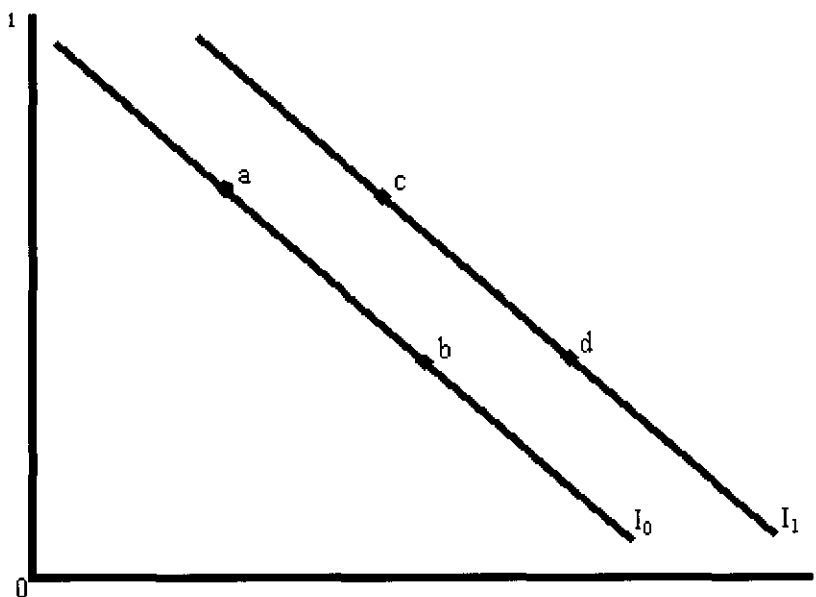
17 In 2010 South Africa produced 10 soccer ball, 5 beer bottles and 25 vuvuzelas at a respective cost of R11, R5 and R5 each. From this one can conclude that nominal GDP _____ from 2009 to 2010, whereas real GDP _____

- [1] decreased, increased
- [2] decreased, remained constant
- [3] increased, remained constant
- [4] increased, decreased

18 The sum of the marginal propensity to consume and the marginal propensity to save is

- [1] equal to disposable income
- [2] equal to zero
- [3] greater than one
- [4] equal to one

Questions 19 and 20 are based on the diagram below



[TURN OVER]

19 The shift in the investment function from I_0 to I_1 is as a result of

- [1] an increase in the repo rate
- [2] a decline in the prime rate
- [3] an improvement in profit expectations
- [4] an increase in savings by households

20 A movement from point b to a is due to

- [1] an increase in interest rate
- [2] a decrease in autonomous investment spending
- [3] a decrease in income
- [4] worsening profit expectations

21 If $C = 50 + 0,9Y$, then at an income level of 1000, savings are

- [1] -100
- [2] -50
- [3] 50
- [4] 100

Questions 22 to 24 are based on the following information about an open economy with a government sector

Autonomous consumption	= R 100 million
Investment spending	= R 300 million
Government spending	= R 200 million
Exports	= R 150 million
Autonomous imports	= R 100 million
Multiplier	= 2
Full employment income level	= R 2 150 million

22 The equilibrium level of income is

- [1] R1 300 million
- [2] R1 625 million
- [3] R1 950 million
- [4] R2 145 million

23 The budget surplus at the equilibrium level of income is

- [1] -R50 million
- [2] -R70 million
- [3] -R130 million
- [4] -R170 million

24 The full employment income level can be reached by

- [1] increasing government spending by R200 million
- [2] increasing exports by R175 million
- [3] increasing imports by R175 million
- [4] increasing investment spending by R425 million
- [5] increasing government spending by R525 million

- 25 The multiplier is
- [1] the exponential increase in aggregate spending caused by a decrease in interest rates
 - [2] the amount by which spending will multiply when real GDP increases
 - [3] the product of the increase in equilibrium income and an increase in induced spending
 - [4] the ratio of the increase in equilibrium income to the increase in autonomous spending
- 26 A decrease in leakages from the Keynesian model with a government leads to _____ in the multiplier
- [1] a decrease
 - [2] no change
 - [3] an increase
- 27 In the Keynesian model with a government sector, an increase in national income will lead to an increase in
- [1] consumption and government spending
 - [2] saving and investment
 - [3] saving and taxes
 - [4] consumption, saving, and taxes
- 28 Assume national output is at the full-employment level of output and the government budget is balanced. A reduction in investment spending would lead to
- [1] a decline in output and a government budget deficit
 - [2] a decline in output and a government budget surplus
 - [3] an increase in output and a government budget deficit
 - [4] an increase in output and a government budget surplus
- 29 The purchase of bonds by the SARB will have the greatest effect on real GDP if
- [1] the marginal propensity to consume is low, and the interest rate has a large effect on investment spending
 - [2] the required reserve ratio is low, and the interest rate has a small effect on investment spending
 - [3] the required reserve ratio is low, and the marginal propensity to consume is high
 - [4] the marginal propensity to consume is high, and the interest rate has a small effect on investment spending
- 30 The implementation lag for monetary policy is generally
- [1] much shorter than it is for fiscal policy
 - [2] much longer than it is for fiscal policy
 - [3] the same as it is for fiscal policy
- 31 Fiscal policy can be used to
- [1] manage the total demand for money
 - [2] control the exchange rates
 - [3] regulate the quantity of money
 - [4] manage the total demand for goods and services

- 32 Assume the economy experiences both a supply shock and a decrease in investment spending. This would cause the level of income
- [1] and the price level to increase
 - [2] to increase and have an indeterminate effect on the price level
 - [3] to decrease and the price level to increase
 - [4] to decrease and have an indeterminate effect on the price level
- 33 The production price index
- [1] includes all goods and services
 - [2] measures the consumer's living standards
 - [3] includes only capital goods
 - [4] excludes the interest rates

Question 34 is based on the following information

Nominal interest rate	9 percent
Expected inflation rate	4 percent
Actual inflation rate	2 percent

- 34 What is the difference between the real interest rate a lender of money receives and the real interest rate the lender expected to receive?
- [1] 2 percent
 - [2] 4 percent
 - [3] 5 percent
 - [4] 7 percent
- 35 Workers and retirees would want to have their wages and benefits indexed to the Consumer Price Index in order to
- [1] maintain their purchasing power during years of rising output
 - [2] maintain their purchasing power during years of declining output
 - [3] increase their purchasing power during years of inflation
 - [4] maintain their purchasing power during years of rising prices
- 36 A depreciation of the rand may have inflationary consequences in South Africa because it
- [1] discourages exports
 - [2] decreases the international competitiveness of South African producers
 - [3] discourages international tourists to visit South Africa
 - [4] increases the price of imported goods
- 37 Which of the following will most likely occur as a result of an increase in labor productivity?
- [1] An increase in output and a decrease in inflation
 - [2] An increase in interest rates and a decrease in investment
 - [3] A decrease in exports and an increase in employment
 - [4] A decrease in unemployment and an increase in inflation

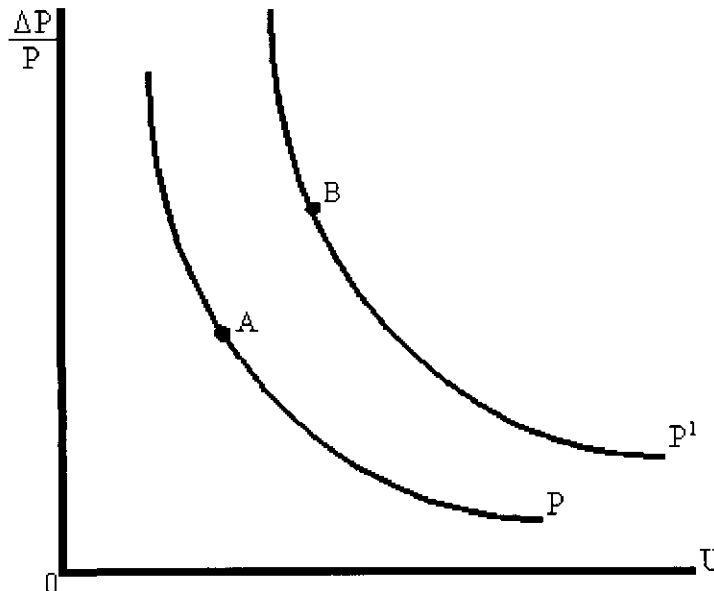
Use the information below for country Z and answer question 38. All the figures are in millions.

Total population in 2001	1 800
Total labour force in 2000	550
Total labour force in 2001	675
Number of people unemployed in 2001	225

38 The unemployment rate in 2001 is approximately

- [1] 12,5%
- [2] 22,7%
- [3] 33,3%
- [4] 40,9%

Use the diagram below, which represents Phillips curves to answer question 39



39 A simultaneous increase in inflation and unemployment from points A to B results in

- [1] hyperinflation
- [2] stagflation
- [3] cyclical unemployment
- [4] seasonal unemployment

40 For a given government spending and tax rate, the government budget deficit will grow during _____ and decline during _____

- [1] booms, booms
- [2] recessions, recessions
- [3] booms, recessions
- [4] recessions, booms

*** ** *

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As your mark-reading sheet can get lost, you **must** also write down your answers for Section B in the space provided below

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PART 1 (GENERAL/ALGEMEEN) DEEL 1

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 EKSAMENSENTRUM (BY PRETORIA)

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For use by examination invigilator
 Vir gebruik deur eksamenopsiener

IMPORTANT **BELANGRIK**

- | | |
|---|---|
| 1 USE ONLY AN HB PENCIL TO COMPLETE THIS SHEET
2 MARK LIKE THIS
3 CHECK THAT YOUR INITIALS AND SURNAME HAS BEEN FILLED IN CORRECTLY
4 ENTER YOUR STUDENT NUMBER FROM LEFT TO RIGHT
5 CHECK THAT YOUR STUDENT NUMBER HAS BEEN FILLED IN CORRECTLY
6 CHECK THAT THE UNIQUE NUMBER HAS BEEN FILLED IN CORRECTLY
7 CHECK THAT ONLY ONE ANSWER PER QUESTION HAS BEEN MARKED
8 DO NOT FOLD | 1 GEBUIK SLEGS N HB-POTLOOD OM HIERDIE BLAD TE VOLTOOI
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PART 2 (ANSWERS/ANTWOORDE) DEEL 2

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Specimen only