

MACRO ECONOMICS AND FINANCIAL SYSTEM OF PAKISTAN – STAGE-I ISQ Examination (Summer-2010)

Q.1 State True or False in the answer column.

Q.2 Please write the alphabet of the selected answer in the given space:

Q.3 (A) A dialogue took place between two senior executives of a Bank:

Mr. A: The estimate of debt servicing has been revised upwards for the current fiscal which is an alarming sign.

Mr. B: “Of course, the issue of fiscal sustainability is important. However, the root cause of problem is inflationary pressure.

Mr. A: It is estimated that foreign debt servicing cost in the next fiscal year would be \$ 1.50 billion. The fall in rupee value would further worsen the situation.

Mr. B: First thing first. Inflation appears to be our major problem. High inflation leads to all kinds of distortion. We need make adjustments (by way of depreciation) in value of Pak rupee to offset the effect of inflation.

Mr. A: The total Government debt is around 60% of GDP and with depreciation of Pak rupee, the foreign debt servicing cost shall escalate further.

(i) Explain how does inflation effect exchange rate in an economy?

(ii) What are the pros and cons of depreciation of exchange rate in Pakistan?

Q.3 (B) In an economy income (Y) is 4,800, consumption is 3,500, Government spending is 1,000 and tax revenue is 800.

i) What shall be private saving?

ii) What shall be public saving?

iii) What is total (National) saving?

Q.3 (C) Marginal Propensity to consume in an economy is 0.8. The Government wishes to bring \$ 400 million increase in output.

i) What increase in Government spending is required?

ii) Suppose Government instead uses tax cuts, how much amount of tax cuts shall have to be made to achieve the \$ 400 million increase in output?

Q.4 (A) Can the value of the nominal GNP of a country be used as a measure of the economic welfare of its people? Explain your answer?

- Q.4 (B) Indicate the factors which were responsible for the emergence of Circular Debt Problem in Pakistan.
- Q.4 (C) What are the significant implications of Circular Debt Problem?
- Q.5 (A) Why the monetary policy is predominantly used to achieve stabilization in Pakistan. What advantages are attributed to monetary policy over fiscal policy?
- Q.5 (B) Explain why short-run aggregate supply curve differs with that of long-run aggregate? Supply curve?
- Q.6 (A) What is trade-off between inflation and unemployment in the short-run? Does this relationship also hold in the long-run?
- Q.6 (B) "Monetarists and Keynesians both agree that inflation can only be reduced at the cost of higher unemployment". Do you agree? Explain with justification.
- Q.7 (A) Explain why for an open economy the size of multiplier is directly related to marginal propensity to imports?
- Q.7 (B) What is likely impact of the following on Internal and External Balances in an open economy?
- i. An increase in Government spending
 - ii. A loss of export market
 - iii. A reduction in saving and corresponding increases in the demand for domestic goods
- Q.8 (A) How is equilibrium interest rate determined in money market?
- Q.8 (B) How does interest rate effect Bond Prices?
- Q.9 (A) How does restrictive monetary policy control inflation?
- Q.9 (B) A country barely has enough resources to meet the requirement of its people but does not have enough resources to devote to investment to increase per capita output. Indicate how such a country can increase its level of investment without reducing current expenditure?
- Q.10 (A) What is indicated by a horizontal LM curve?
- Q.10 (B) When would I.S. curve become more flatter?
