**Major Assignment**

**Macroeconomics**

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**Q1. Select the best suitable answer.** (**10)**.

**1.** The circular flow of income diagram is a **visual model of how the economy is organized**

a. visual model of how the economy is organized.

b. visual model of the relationships among money, prices, and businesses.

c. model that shows the effects of government on the economy.

d. mathematical model of how the economy works.

**2.** The two loops in the circular-flow diagram represent **inputs into production processes and (ii) outputs from production processes**

a. (i) the flow of goods and (ii) the flow of services.

b. (i) the flow of dollars and (ii) other financial flows.

c. (i) inputs into production processes and (ii) outputs from production processes.

d. (i) the flows of inputs and outputs and (ii) the flow of dollars.

**3.**During a recession the economy experiences . **falling employment and income.**

a. rising employment and income.

b. rising employment and falling income.

c**.** rising income and falling employment.

d. falling employment and income.

**4.** Real GDP **. is not adjusted for inflation**

a. moves in the same direction as unemployment.

b**.** is not adjusted for inflation.

c. also measures real income.

d. is the same as nominal GDP

**5.** If we deduct direct taxes from the personal income, we get . **Disposable personal income**

a. Per capita income

b. Disposable personal income

c. Net national income

d. Personal saving

**6.** GNP includes **A loan from bank**

a. A loan from bank

b. Gifts and donations

c. Parents spending and scholarships

d. Commission payments

**7.** Which of the following is not macroeconomics. **Level of wages in a factory**

a. Inflation

b. Unemployment

c. Output level of the economy

d. Level of wages in a factory

**8.** In equilibrium of national income . **S=I**

a. S>I

b. S=I

c. S<I

d. S-I=1

**9.** For 3 sector economy, the income equation is . **Y=C+I+G**

a. Y=C+I+G

b. Y=C-I+G

c. Y=C+I+T

d. Y=C+I

**10.** Which type of unemployment is considered as a healthy sign for economy? **. Y=C+I+G**

a. Structural unemployment

b. Classical unemployment

c. Seasonal unemployment

d. Frictional unemployment

**Q2. Give brief answers to the following questions. (2+2+3+2+3+3=15)**

1. **Thinking about the definition of GDP, explain why transfer payments (zakat, donations etc) are excluded from the calculation of GDP?**

 **Ans**

GDP is total market values of all final goods and service produced within a country in a fiscal year.Transfer payment are excluded. Because nothing gets produced and these are not earning but only exchange from one person to another person.

1. **Why Net National Product(NNP) isn’t commonly used for the calculation of national income figures**?

**Ans**

National income means production of all goods and services in a fiscal years in a country. Net national product is not use commonly

for the calculation of national income because NNP=GNP – depreciation

 Depreciation means wear and tear of capital which is consider to be payment to a factor of production but it’s a past of total expenditure.

 The reason is a problem of double counting therefore NNP is not commonly used for the calculation of national income

1. **The Bureau of Labor Statistics announced that in December 1998, of all adult Americans 138,547,000 were employed, 6,021,000 were unemployed and 67,723,000 were not in the labor force. How big was the total labor force? What was the unemployment rate?**

**Ans**

Not in labors force = 67,723,000

 Employed people = 138,547,000

 Unemployed people= 6,021,000

 T.PoP = 212,291,000 L,F = 144,568,000

 **(1)** Total labor force = $\frac{L.F}{T. PoP}$

 = 0.681

 Unemployment rate = $\frac{Unemplyed people }{L.F }$\*100

 =$\frac{6,021,000}{144,568,000}$\*100

 =4.16%

**4. What is the concept of “natural rate of unemployment”?**

**Ans**

**“**Concept of natural rate of unemployment**”**

 The natural rate of unemployment when the labor market is equilibrium

 ASL = aggregate supply of labor

 ASL = aggregate demand of labor

**5. Briefly discuss Okun’s Law.**

**Ans**

 **OKUM’S LAW:**

The relation between unemployment and production varies by a country.According to the Okum when the unemployment falls the production of a country will increase. This measure can be used for estimating both GNP and GOP

**6.** Classical macroeconomics considers the two assumptions of

* Money as just the medium of exchange and Automatic adjustment mechanism

 Briefly discuss these two.

**Ans:** Money solves the problem to created by bartes system. Money as just medium of exchange which means That money acts

on intermediary between the buyers and theseller**.**

**Q3. (a)** Explain the “**consumption equation** “as given by Keynes in his theory. **(2+3)**

**ANS:**

Keynes's theory of the determination of equilibrium real GDP, employment, and prices focuses on the relationship between aggregate income and expenditure. Keynes used his **income‐expenditure** model to argue that the economy's equilibrium level of output or real GDP may not corresPond to the natural level of real GDP. In the income‐expenditure model, the equilibrium level of real GDP is the level of real GDP that is consistent with the current level of aggregate expenditure. If the current level of aggregate expenditure is not sufficient to purchase all of the real GDP supplied, output will be cut back until the level of real GDP is equal to the level of aggregate expenditure. Hence, if the current level of aggregate expenditure is not sufficient to purchase the natural level of real GDP, then the equilibrium level of real GDP will lie somewhere below the natural level.

##  Calculating the Consumption Function

The consumption function is represented :

C = A+MD

WHERE:

C= consumer spending

A= autonomus consumption

M= marginal propensity to consume

D= real disposable income

 **(b)** Suppose the consumption function for two sector economy is given by

 C= 100+ 0.8Y, while I =50

1. **What is the equilibrium level of income?**
2. **What is the level of savings at equilibrium level?**

**Ans:** 1

NI ←Y = C+I

 Putting the values

 Y = 100+0.8 + 50

 Y=150+0.8Y

 Y-0.8Y =150

 Y= $\frac{150}{0.2}$

 Y=750 (two sector)

 We know that

 C = 100+ 0.8y

 Put the values of y in the above equation

 C= 100+ 0.8(750)

 C = 100+ 600

 C = 700

 Y= 750

 S = ?

Know part (2)

Y = C+5 where S = ?

 Y = C+S

 S = 50 = I

 Hence Y= 750 , S=I for income is determine at level Y = 750

 S= -100+0.2yand I =50

 -100+0.2y +50

 0.2y = 50+100

 Y = $\frac{150}{0.2}$

 Y = 750

 S = -100+0.2(750)

 S = -100+ 150

 S = 50 = I