Department of Economic Science

IISER Bhopal

End-Semester Examination

Principle of Economics 2 - ECO 102

Time: 3 Hours Total Marks: 100

1. (20 marks). Contractionary policies are designed to slow economy and reduce inflation by decreasing aggregate demand and aggregate output. Explain why contractionary fiscal policy and contractionary monetary policy have opposite effects on the interest rate despite having the same goal of decreasing aggregate demand and aggregate output. Illustrate your answer with graphs of the money market.

2. (20 marks) In 2003, the long term capital gain tax rates in the U.S. were slashed from 20/18 percent to around 15 percent. In what ways do you expect this amendment is going to affect economic growth.

3. (20 marks) Describe absolute advantage and comparative advantage. Describe graphically how international trade allows a country to consume outside its production possibility frontier.

4. (20 marks) By using aggregate supply and aggregate demand curves to illustrate your points, discuss the impacts of the following events on the price level and on equilibrium GDP (Y) in the short run:

   a) An increase in the money supply with the economy operating at near full capacity.

   b) A decrease in taxes and increase in government spending supported by a cooperative Fed acting to keep output from rising.

5. (20 marks) A new invention has led to fall in the price of oil. What impact might a new decrease in oil price have on the aggregate price level and on the real GDP in your country? Illustrate your answer with aggregate demand and aggregate supply curves.