FEEDBACK TUTORIAL LETTER

2ND SEMESTER 2019

Assignment 1

PRINCIPLES OF MACROECONOMICS
COURSE CODE: PMA512S
Dear Student

Thank you for submitting your first assignment on time. I trust that you have worked hard this far and will continue to do so because success is the best motivator. If you did not start off well, remember you still have one assignment to try and make up for this.

In this tutorial letter I would like to give feedback on Assignment 1 of Principles of Macroeconomics. If you did not answer Section A very well, it could be because you did not read the required units thoroughly before attempting to answer the questions. Always try to answer the questions as complete as possible providing all the facts and also show your calculations.

Use the opportunity to revise the questions with the memorandum in hand. Feel free to contact any of your tutor/markers if you need assistance with this assignment or with assignment 2. For the students in Windhoek I present face-to-face tutorials on Fridays.

We hope to see you at the vacation school and we are looking forward to your next assignment.

Regards,

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ASSIGNMENT 1

SECTION A

Instruction: Please use the answer sheet at the end of this tutorial letter. Cross the alternative you select with an X.

1. C
2. A
3. B
4. A
5. B
6. A
7. D
8. D
9. B
10. A
11. D
12. B
13. A
14. C
15. B
16. D
17. A
18. A
19. C
20. C
QUESTION 1 [10 marks]

The following is a simplified hypothetical example of the value added method of calculating GDP. Use the information given and show how the value added method is used to calculate GDP. According to this example, how much value added do the books contribute to the GDP, and explain why that specific figure?

(a) A forester chops down 100 trees and sells them @ N$100 each to the Paper and Pulp Factory.
(b) The Paper and Pulp Factory processes these trees into paper and sells the paper @ N$15 000 to the printers.
(c) The printers go to press and sell the 300 books they print @ N$80 each to CNA.
(d) CNA sells the 300 books @ N$120 each to consumers.

HINT: The best way to answer this question is in table format.

<table>
<thead>
<tr>
<th></th>
<th>Selling Price (N$)</th>
<th>Value Added (N$)</th>
</tr>
</thead>
<tbody>
<tr>
<td>a) Forester</td>
<td>10 000</td>
<td>10 000</td>
</tr>
<tr>
<td>b) Paper and Pulp Factory</td>
<td>15 000</td>
<td>5 000</td>
</tr>
<tr>
<td>c) Printers</td>
<td>24 000</td>
<td>9 000</td>
</tr>
<tr>
<td>d) CAN</td>
<td>36 000</td>
<td>12 000</td>
</tr>
<tr>
<td><strong>TOTALS:</strong></td>
<td><strong>85 000</strong></td>
<td><strong>36 000</strong></td>
</tr>
</tbody>
</table>

The books will increase the GDP by **N$36 000**

We cannot say that the GDP has increased by N$85 000 because the final product is only worth N$36 000. The amount of N$85 000 is obtained through double counting.
QUESTION 2 [10 marks]

Table 1 reflects some of Namibia's statistics. Use the relevant statistics to compile **Account 1: Gross Domestic Product and Expenditure**. On the income side, show the GDP at factor cost and the GDP at market prices.

**Account 1: Gross Domestic Product and Expenditure**

<table>
<thead>
<tr>
<th>Income</th>
<th>N$ millions</th>
<th>Expenditure</th>
<th>N$ millions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Compensation of employees</td>
<td>8 307</td>
<td>Final consumption expenditure by households</td>
<td>12 240</td>
</tr>
<tr>
<td>Net operating surplus</td>
<td>6 912</td>
<td>Final consumption expenditure by government</td>
<td>6 268</td>
</tr>
<tr>
<td>Consumption of fixed capital</td>
<td>2 850</td>
<td>Gross capital formation</td>
<td>4 818</td>
</tr>
<tr>
<td><strong>GDP at factor cost</strong></td>
<td><strong>18 069</strong></td>
<td><strong>Gross domestic expenditure</strong></td>
<td><strong>23 326</strong></td>
</tr>
<tr>
<td>Other taxes on production</td>
<td>991</td>
<td>Less: Residual item</td>
<td>(417)</td>
</tr>
<tr>
<td>Less: Other subsidies on production</td>
<td>(42)</td>
<td>Exports of goods and services</td>
<td>9 548</td>
</tr>
<tr>
<td>Taxes on products</td>
<td>1 780</td>
<td>Less: Imports of goods and services</td>
<td>(11 773)</td>
</tr>
<tr>
<td>Less: Subsidies on products</td>
<td>(114)</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>GDP at market prices</strong></td>
<td><strong>20 684</strong></td>
<td><strong>Expenditure on GDP</strong></td>
<td><strong>20 684</strong></td>
</tr>
</tbody>
</table>

Please note on the expenditure side of the account: If you add the expenditures by households and the government plus gross capital formation you get a total that is called gross domestic expenditure. The word domestic means it is expenditures of all the groups in the country and it excludes imports and exports.

The residual item is calculated as follows:

Expenditures: N$21 101

Less: Incomes: N$20 684

Residual item: N$ 417

(½ point each for every figure in the money columns, and 1 point each for the GDP at factor cost figure, the GDP at market prices figure, the Residual item figure and the Expenditure on GDP figure)
QUESTION 3 [4 marks]

Please refer to the statement printed in bold. What would happen to the money supply in that situation? Also, state whether monetary policy is expansionary or restrictive and explain your answer.

“The Executive Committee of the Bank of Namibia reduces the Repo rate from 10% to 9%.”

If the Bank of Namibia reduces the Repo rate it is an indication that they are following expansionary monetary policy to stimulate the economy during the recession. The commercial banks will follow by reducing their prime lending rates. This will decrease the cost of credit by making existing loans cheaper and borrowers will be left with more money to spend. It will also encourage the private sector to borrow more and result in an increase in the money supply.

(1 point each for the terms printed in bold, or anything similar to that)

QUESTION 4 [4 marks]

Consider the hypothetical situation where country X produces only two goods, namely potatoes and radios. Now look at the production and price information in Table 2 and calculate the following data as asked.

Table 2

<table>
<thead>
<tr>
<th>GDP Data for 2001</th>
<th>GDP Data for 2002</th>
</tr>
</thead>
<tbody>
<tr>
<td>Quantity</td>
<td>Price</td>
</tr>
<tr>
<td>Potatoes</td>
<td>50</td>
</tr>
<tr>
<td>Radios</td>
<td>100</td>
</tr>
</tbody>
</table>

(a) The nominal GDP in 2001

\[= (50 \times 2) + (100 \times 20) = 2100\]  
(1 point)

(b) The nominal GDP in 2002

\[= (100 \times 4) + (80 \times 25) = 2400\]  
(1 point)

(c) The Real GDP in 2002 with the Price Index being 109.54

\[= (2400 / 109.54) \times 100 = 2190.98\]  
(1 point)

(d) The (base year 2001) economic growth rate.

\[= (2400 - 2100) / 2100 \times 100 = 14.29\%\]  
(1 point)
QUESTION 5 [2 marks]

Please refer to the statement printed in bold. State whether fiscal policy is expansionary or restrictive and explain the effect of this policy on aggregate demand.

“Personal income tax rates are increased by 5% across the board.”

If the government increases personal income tax rates, fiscal policy is restrictive. Higher tax rates will decrease the personal disposable income of households. As a result consumption (C) will decrease and therefore aggregate demand will decrease.