

[Frequently Asked Questions]

IS-LM Curve - I

Subject:

Business Economics

B. A. (Hons.), 3rd Semester,

Course:

Paper No. & Title:

Paper – 301 Macroeconomics - I

Undergraduate

Unit No. & Title:

Lecture No. & Title:

Unit – 2 IS-LM MODEL

Lecture – 1 IS-LM Curve - I

Frequently Asked Questions

Q1. Define IS Curve.

A1. The IS curve is defined as the locus of various combinations of rate of interest and national income where goods market is in equilibrium.

Q2. State the reasons for downward sloping IS curve. A2.

ROI \longrightarrow Investment $\uparrow \longrightarrow$ AD shifts upward,

AD shifts upward \longrightarrow Equilibrium level $\uparrow \longrightarrow$ NI \uparrow

Q3. State the two things on which slope of IS curve depends.

A3. The slope of the IS curve depends upon two things.

- a) First the responsiveness of investment demand curve to changes in ROI. i.e. the elasticity of investment demand curve.
- b) The size of the multiplier.

Q4. Why is the supply of money a vertical straight line?

A4. The money supply curve a vertical straight line because in short run the supply of money remains constant.

Q5. The income level corresponding to the various rate of interest determined at which income levels?

A5. The income level corresponding to the various rate of interest determined at those income levels through money market equilibrium by equality of demand for money and supply of money.

Q6. What is goods market equilibrium?

A6. The goods market or the real sector is in equilibrium when aggregate demand for goods is equal to aggregate supply.

Q7. What is money market equilibrium?

A7. The LM curve represents equilibrium in money market, the money market is in equilibrium when demand for money equals supply of money.

Q8. State the different reasons for demand for money

A8. Demand for money includes:

- Transaction demand
- Precautionary demand and
- Speculative demand.

Q9. What is speculative demand?

A9. The demand for money which is used for speculation is known as speculative demand for money. The speculative demand for money is the function of the rate of interest. Given the level of income, higher the ROI, lower is the speculative demand for money.

Q10. State the two factors determining Slope of LM curve.

A10. The two factors that determines the slope of LM curve are

- Income elasticity of demand for money. i.e. responsiveness of demand for money to the changes in level of income
- Interest elasticity of demand for money i.e. responsiveness of demand for money to the changes in rate of interest.