



# MAASAI MARA UNIVERSITY

**REGULAR UNIVERSITY EXAMINATIONS  
2018/2019 ACADEMIC YEAR**

**BACHELOR OF ARTS IN ECONOMICS  
FOURTH YEAR SECOND SEMESTER**

**SCHOOL OF BUSINESS AND ECONOMICS**

**COURSE CODE: ECO 421**

**COURSE TITLE: MONETARY THEORY AND  
POLICY**

**DATE: 26<sup>TH</sup> APRIL, 2019  
HRS**

**TIME: 0830 - 1030**

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**INSTRUCTIONS TO CANDIDATES**

Answer Question **ONE** and any other **THREE** questions

*This paper consists of **three** printed pages. Please turn over.*

### **QUESTION ONE.**

Discuss macroeconomic variable that affect the aggregate demand for money.

**(5 marks)**

(b) Explain how the supply of money could be expanded or reduced in an economy in which all money is in form of currency.

**(5 marks)**

(c) Explain the following concepts as used in monetary theory and policy.

**(10 marks)**

i) The exchange fund account

ii) Intermediate targets

iii) Bank runs

iv) Money multiplier

(d) Explain the modern theory of money.

**(5 marks)**

### **QUESTION TWO.**

**a(i)** Describe the differences between Keynesian and monetarist monetary transmission mechanisms.

**(3 marks)**

**(ii)** In what ways does Keynesian fiscal policy short-circuit the difficulties they perceive in transforming new money that interfere new spending. **(3 marks)**

**(b)** Discuss the relationship between inflation and nominal money supply.

**(4 marks)**

**(c)** "A government deficit is bad because it leads to rapid monetary growth". Explain why this statement is wrong.

**(5 marks)**

### **QUESTION THREE.**

**a)** Discuss the objectives of monetary in closed economy

**(5 marks)**

**(b)** Explain the relationship between price level and nominal money supply when all markets are in equilibrium.

**(5 marks)**

**(c)** Explain the components of  $M_1$  and  $M_2$ .

**(5marks)**

### **QUESTION FOUR**

a) Explain the role and functions of central bank in the following economies.

**(6marks)**

- I. Developed economies
- II. Developing economies

(b) Discuss factors that determine demand for money.

**(9marks)**

- I. Keynesian approach
- II. Classical approach

### **QUESTION FIVE**

Explain how interest rates are determined under the following approaches.

I. Classical

**(3marks)**

II. monetarism

**(3marks)**

(b) Explain the following concepts as used in monetary theory and policy.

**(9marks)** Monetary transmission mechanism

I. Fractional reserve banking

II. High powered money

III. Liquidity trap

(c) Explain three functions of money.

**(3marks)**

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