MACHAKOS UNIVERSITY COLLEGE

(A Constituent College of Kenyatta University)
University Examinations for 2015/2016

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF BUSINESS ENTREPRENEURSHIP AND MANAGEMENT SCIENCES

SECOND SEMESTER EXAMINATIONS FOR DEGREE IN BACHELOR OF COMMERCE (FINANCE OPTION)

EAE 401: MONETARY THEORY AND POLICY

Date: 3/8/2016 **Time: 8:30 – 10:30 AM**

INSTRUCTIONS:

Answer question one (compulsory) and any other two questions.
Do not write on the question paper

QUESTION ONE (COMPULSORY)

(a) Write notes on the following as used in Monetary theory and policy

(i) Stock variable

(ii) Flow variable (3 marks)

(b) With the aid of a well labelled diagram, demonstrate Baumol's approach

(i) to the transactions demand for money (4 marks)

(ii) and distinguish it from the Keynesian transactions demand for money. (3 marks)

(c) Present in brief the two versions of the classical demand for money (7 marks)

(d) Highlight three factors that determine money supply (3 marks)

(e) Briefly evaluate the effectiveness of monetary policy in maintaining equilibrium in the balance of payment (BOP) in Kenya (4 marks)

(f) State the limitations of Monetary policy in Kenya (3 marks)

(g) Analyze the limitation of bank rate policy in kenya given the state of capital markets development (3 marks)

QUESTION TWO

(a) Provide the Keynesian critique of the effectiveness of monetary policy (4 marks)

(b) Discuss two instruments of monetary policy in Kenya (5 marks)

(c) Evaluate the roles of the central bank of Kenya in

(i) Maintaining economic stability (4 marks)

(ii) Tackling the challenges of conducting monetary policy (3 marks)

(d) Derive and interpret the money multiplier (4 marks)

QUESTION THREE

(a) Briefly discuss with examples the three types of financial Markets in Kenya. (6 marks)

(b) Demonstrate your understanding on the evolution of monetary policy in Kenya (6 marks)

(c) Evaluate

(i) The main arguments in the Cambridge cash balance version of the quantity theory of money (5 marks)

(ii) Keynes critique of the quantity theory of money (3 marks)

QUESTION FOUR

(a) Using a well labelled diagram, demonstrate the transmission mechanism that in the Keynesian view is associated with an increase in money supply in the economy. (5 marks)

(b) Explain the main role of financial intermediaries in Kenya (2 marks)

(c) Briefly evaluate the deposit multiplier as a determinant of money supply. (5 marks)

(d) Use specific examples from a developing country of your choice to demonstrate any four limitations of credit creation (8 marks)

QUESTION FIVE

(a) Evaluate two limitations of open market operations (OMO) in affecting money supply in the economy (4 marks)

(b) Evaluate with specific examples the role of monetary policy in:
   (i) Savings
   (ii) Investment (6 marks)

(c) Explain the term wealth as used in the Friedman theory of money demand (5 marks)

(d) Analyze the conflicting goals of monetary policy while relating to the Kenyan economy (5 marks)