



Kasarani Campus
Off Thika Road
Tel. 2042692 / 3
P. O. Box 49274, 00100
NAIROBI
Westlands Campus
Pamstech House
Woodvale Grove
Tel. 4442212
Fax: 4444175

**KIRIRI WOMENS' UNIVERSITY OF SCIENCE AND TECHNOLOGY
UNIVERSITY EXAMINATION, 2019/2020 ACADEMIC YEAR
FOURTH YEAR, FIRST SEMESTER EXAMINATION
FOR THE DEGREE IN BACHELOR OF SCIENCE
(BUSINESS ADMINISTRATION)**

Date: 12th April, 2019
Time: 11.00am – 1.00pm

KFI 303 - MONETARY THEORY AND POLICY

INSTRUCTIONS TO CANDIDATES

ANSWER QUESTION ONE (COMPULSORY) AND ANYOTHER TWO QUESTIONS

QUESTION ONE (30 MARKS)

- a) The standard was the dominant system in the first, second and third generation central banking. Explain how a trade deficit affected gold reserves and how this reserve position was corrected in the gold standard system. (6 marks)
- b) Discuss the Baumol theory of money demand and highlight the assumptions of the model. (7 marks)
- c) Using examples, where necessary, distinguish between the following pair of terms as used in monetary economics:
- i) Nominal inflation and real inflation. (3 marks)
 - ii) High Powered Money and Money Supply. (3 marks)
 - iii) Time deposits and Checkable deposits. (3 marks)
 - iv) Monetary policy and Monetary theory. (3 marks)
- d) Kenya had experience a depressed economic performance between 2008 and 2011. Explain how the Central Bank of Kenya (CBK) pulled the economy out of this trough. (5 marks)

QUESTION TWO (20 MARKS)

- a) In developing economies, credit inflation has been a major source of price instability. How does the central bank use monetary policy to solve the problem? (10 marks)
- b) Discuss the very vital determinants of money supply. (10 marks)

QUESTION THREE (20 MARKS)

- a) Illustrate and explain the effect of a sale of government bond in an economy whose money demand function is perfectly elastic. (10 Marks)
- b) Discuss the functions of the Central Bank in a developing economy. (10 Marks)

QUESTION FOUR (20 MARKS)

- a) Explain the Tobin's Portfolio Approach to Money Demand and show how it overcomes some weaknesses of the Keynesian thought. (10 marks)
- b) Explain how a current account deficit problem can be addressed by monetary policy. (10 marks)

QUESTION FIVE (20 MARKS)

- a) Is the Central Bank involved in the credit creation process? Explain your answer. (5 marks)
- b) Using the Keynesian theory, explain how an increase in money supply affects prices in the economy. (10 marks)
- c) Explain how the Central Bank can help in improving a deficit situation in the capital account. (5 marks)