



# **MACHAKOS UNIVERSITY**

**University Examinations for 2021/2022 Academic Year**

**SCHOOL OF BUSINESS AND ECONOMICS**

**DEPARTMENT OF ECONOMICS**

**THIRD YEAR SECOND SEMESTER EXAMINATION FOR**

**BACHELOR OF ECONOMICS AND STATISTICS**

**BACHELOR OF ECONOMICS AND FINANCE**

**BACHELOR OF ECONOMICS**

**BACHELOR OF EDUCATION**

**BACHELOR OF ECONOMICS**

**EAE 310: ECONOMICS OF MONEY AND BANKING**

**DATE: 15/12/2021**

**TIME: 11.00-1.0 PM**

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## **INSTRUCTIONS:**

**(i) Answer question ONE and any other two questions**

**(ii) Show ALL your workings clearly**

### **QUESTION ONE (COMPULSORY) (30 MARKS)**

- a) Explain the limitations of the process of credit creation (8 marks)
- b) Briefly explain the concept of money “illusion.” (7 marks)
- c) Discuss the importance of non-bank financial institutions in economic growth and development process of a country. (8 marks)
- d) Outline factors that influence the velocity of money (7 marks)

### **QUESTION TWO (20 MARKS)**

- a) Illustrate and explain the impacts of central bank’s sale of government securities to the public when demand for money is perfectly elastic (10 marks)
- b) Illustrate and explain the money market equilibrium (4 marks)
- c) What are the supply and demand for money shift factors that may alter this equilibrium (6 marks)

**QUESTION THREE (20 MARKS)**

- a) What are the reasons for holding money in the Keynesian system? (8 marks)
- b) How is the Keynesian theory of demand or money different from the classical. (4 marks)
- c) Why does the speculative demand for money change with the interest rate? Explain in this regard the relationship between the interest rate and the bond prices (8 marks)

**QUESTION FOUR (20 MARKS)**

- a) Mention four different types of money (2 marks)
- b) Why might be pro-cyclical behaviour of interest rates (rising during business cycle expansion and falling during recession) lead to pro-cyclical movements in the money supply? (8 marks)
- c) Explain the abandonment of barter trade and how the introduction of money in financing transaction helped in the economic growth and development of countries (10 marks)

**QUESTION FIVE (20 MARKS)**

- a) Write short notes on the following
  - i) Minimum legal cash reserves ratio (3 marks)
  - ii) Selective credit control (3 marks)
  - iii) Moral suasion (2 marks)
  - iv) Fiat money (2 marks)
  - v) Full bodied money (2 marks)
- b) State five attributes that any commodity should possess in order to serve as medium of exchange (5 marks)
- c) Money is described as “hot potato” that is quickly passed from one person to another during a hyperinflation. Explain why this is the case. (3 marks)