

UNIVERSITY OF FORT HARE

**MONETARY ECONOMICS  
ECO 516/516E**

MAIN EXAM

NOVEMBER

2018

.....

**Time: 3 Hours**

**Subject: ECO 516/516E**

**Marks: 100**

**This paper consists of 3 pages including the cover page**

**Internal Examiners**  
Mr P. Ngonisa  
Dr K. Sibanda

**External Examiners**  
Prof A. Maredza

**INSTRUCTIONS**

Answer any **FOUR** questions  
Make use of **relevant examples** where applicable. The graphical  
illustrations must be clearly shown.

### **Question 1**

- a) Outline the different types of transmission mechanisms through which changes in the SARB policy rate can be transmitted to inflation and the real economy. [15]
- b) Which of these mechanisms would you consider to be more effective in South Africa? [10]

### **Question 2**

- a) Why should commercial banks be regulated in a regime of financial deregulation? [10]
- b) What do you understand by the independence of the central bank? Are there any benefits that can be garnered from central bank independence especially in developing countries? Illustrate your answer with reference to any empirical study you are familiar with. [15]

### **Question 3**

Monetary policy in South Africa is conducted using the inflation targeting framework.

- a) What is meant by inflation targeting? Outline the major tenets or characteristics of this framework. [5]
- b) Briefly discuss the reasons behind South Africa's adoption of the inflation targeting framework. [8]
- c) In order for inflation targeting to be successful, there are key institutional arrangements that must be in place. Discuss these arrangements with respect to how South Africa has adopted them. [12]

### **Question 4**

- a) Discuss the techniques of monetary control available to the central bank. [12]
- b) The two key theories that explain the determination of money supply are the flow of funds theory and the base money approach. Outline the key ideas behind these theories and discuss which of these two is more relevant to South Africa. [13]

### **Question 5**

- a) Compare and contrast Keynes liquidity preference theory of the demand for money and Baumol/Tobin's portfolio selection model [10]
- b) Critically examine the Stiglitz-Weiss explanation of credit rationing in banking markets. [15]

**Question 6**

- a) Interest rates are often said to be the price of loanable funds. What are the main 'sectors' in the loan market? Briefly outline whether a sector is likely to be a net borrower or a net lender. Justify [10]
- b) Briefly explain the McKinnon-Shaw model of financial liberalisation and provide a critical overview of the empirical evidence for their claim that deregulation fosters economic growth. [15]