



AFRICAN ECONOMIC RESEARCH CONSORTIUM

JOINT FACILITY FOR ELECTIVES
JULY – OCTOBER, 1998

MONETARY THEORY AND PRACTICE

Second Session: Final Examination

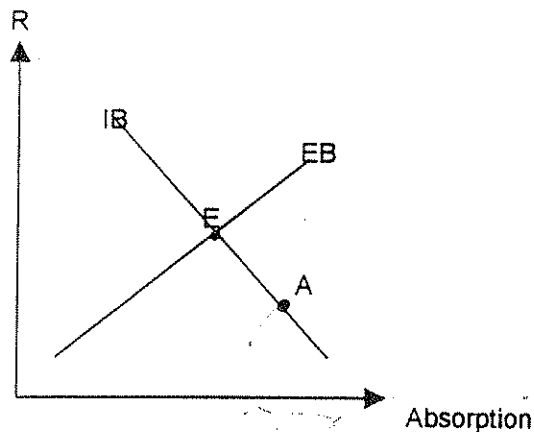
Wednesday, 30th September, 1998

Time: 9:00 a.m – 12:00 noon (3 hours)

INSTRUCTIONS: Attempt FOUR questions: ONE question from each section. Allocate your time carefully and start each full question on a fresh page.

SECTION A(18 MARKS)

1. Consider the Swan diagram, with the internal balance (IB) and external balance (EB) curves intersecting at E, as shown in the diagram below:



- (a) Show that indeed the IB curve is negatively sloped and the EB curve has a positive slope. (6 marks)
- (b) Now consider point A in the diagram. Explain how "built-in stabilizers" work to return the economy from point A to E. (6 marks)
- (c) Why and how can monetary policy be used to reinforce the stabilizers? (6 marks)



SECTION B (14 MARKS)

2. (a) Discuss how the Gold Standard (1870 – 1914) operated. Relate its collapse in 1914 to its failure to solve the problems of liquidity, adjustment and confidence. (7 marks)
- (b) Do structural adjustment programmes (SAPs), in your opinion, offer a solution to the debt problems of a developing country? Elaborately explain your answer with the use of empirical evidence from sub-Saharan Africa. (7 marks)
3. (a) Discuss the advantages and disadvantages of controls on external trade. (7 marks)
- (b) "The portfolio balance approach to the balance of payments is also a theory of exchange rate determination." Discuss. (7 marks)

SECTION C (14 MARKS)

4. (a) It is claimed that inflation may stimulate growth. If this is so, why do countries bother about fighting inflation? (6 marks)
- (b) Compare and contrast the monetarist and the Keynesian approaches to inflation determination and anti-inflation policy. (8 marks)
5. Compare and contrast the adaptive expectations theory with the rational expectations theory. In your discussion, point out, among other things, the shortcomings of each of the theories. (14 marks)

SECTION D (14 MARKS)

6. (a) Discuss the neoclassical Solow-Swan growth model. Does it bear out all the "stylized facts" of economic growth? Explain. (7 marks)
- (b) Use a simple neoclassical growth model to show that whether money is exogenous or endogenous, it enhances economic growth. (7 marks)
7. "A country with financial intermediaries attains a higher steady state level of output per capita and capital per capita than one without financial intermediation." Use an appropriate growth model to discuss this statement. (14 marks)

END