



AFRICAN ECONOMIC RESEARCH CONSORTIUM

Collaborative MA Programme in Economics for Anglophone Africa
(Except Nigeria)

Joint Facility for Electives
JULY - OCTOBER, 1999

Monetary Theory and Practice

Second Session: Final Examination

Time allowed: 3 Hours

September 30, 1999

Section I – Compulsory (30 points)

1. In the Fleming-Mundell model "... the impact of fiscal policy is enhanced. ...the ultimate impact of monetary policy on real income is zero.... the policy assignment problem becomes trivial".

- (i) Under what assumptions do these results obtain? (4 points).
- (ii) Demonstrate these results and discuss. (20 points)
- (iii) Critically appraise the "external equilibrium" achieved this way.(6points)

Section II

Answer any two of the following four questions (15 points each)

2. "Unless banks manage to evade ceilings on lending interest rates, non-price credit rationing must occur. ... credit rationing is alleviated when interest rates are liberalised".

"rationing is inherent in credit markets. ... interest rates do not fully reflect risk; instead lenders use portfolio allocation rules, including credit rationing, to reduce that risk."

Discuss these two statements. (7.5 points each)



3. To what extent is the McKinnon-Shaw hypothesis that low real interest rates retard savings and investment in developing countries supported by the available empirical evidence?

4. (a) Among the functions of financial intermediaries, according to the traditional (pre-1973) theory of financial intermediation, are 'alleviation of market imperfections and maturity transformation'. Elaborate. **(7.5 points)**

(b) the 'presence of externalities and information asymmetry justify regulation in the financial sector'. Discuss. **(7.5 points)**

5. Analysing the effects of financial development on economic growth in an endogenous growth model, King and Levine (1993) concluded:

"Better financial services expand the scope and improve the efficiency of innovative activity; they thereby accelerate economic growth" King and Levine (1993). Discuss.

GOOD LUCK!