

**NDIRANGU MOSES KARIUKI 656954**

**Principles of Macroeconomics (ECO1020- SECTION A)**

**Fall 2020 Final Examination**

**Date: 16th April 2020 Time: 5.30 p.m.**

***EXAMINATION INSTRUCTIONS: Answer QUESTION ONE and any TWO questions from SECTION B***

***Additional questions answered will not be marked.***

Course Instructor: Mrs. Opondo

***SECTION A***

**Question One**

a) State and explain any three functions of the Central Bank. (6 marks)

**Acts as the Bankers bank**

The central bank lends to other banks in need of demand and controls money supply in the banking system.Central bank also accepts deposits from commercial banks

**Financial advisor of the government**

Central bank holds government balances known as public deposits ie government income from taxes

**Issue of currency**

Central bank issues legal tender to the country making sure there is just enough money in circulation in the economy

b) Use the figures in the table below to answer the following questions.

Shs **Billions**

Fixed / time deposits 4050

Saving deposits 2832

Money-market mutual funds 980

Checkable deposits 875

Currency (coins and notes in circulation) 453

Foreign currency deposits 1890

1. What is the value of *M*1? (3 marks)

**875+453 =1328**

(ii) What is the value of *M*2? (3 marks)

**4050+2832+980+M1=9190**

1. What is the value of *M*3?

**M1 +M2 + 1890=11080** (3 marks)

c) Using a graph explain the liquidity preference theory of interest rate determination. (10 marks)

Sm

IR

iE

DM

QM

**The interaction of the forces of demand and supply for money determine the equilibrium market rate of interest.**

**Basically,people demand money for transactional demand.So when the interest rate is high,the opportunity cost of having money In your account is high you do not want to hold a lot of money in your pocket that’s why the quantity of demand is very low ,however when the interest rate falls, its not a big deal to have money in your pocket so quantity of demand increases**

d) State any five ways through which a country can benefit from international trade. (5 marks)

**It enables a country to dispose its surplus goods produced**

**Enables a country get what she cannot produce e.g In Kenya we import most technology devices**

**Enables a country to specialize in what she is good at over the others,e.g Tea in Kenya**

**Healthy competition among local and foreign producers**

**Promotes international relations and understanding when people intermingle from different counties**

***SECTION II: ANSWER any TWO QUESTIONS***

**Question Three**

1. Define money (3 marks)

**Money is any asset that is easily acceptable in settlement of debt,eg.coins and notes,cheques**

1. Explain any three functions of money.

**FUNCTION OF MONEY**

**Medium of exchange or means of Payment**

**An individual will not accept money as a means of payment unless he is confident that he can in turn dispose it in payments of debts or when acquiring other goods**

**Store of wealth**

**Money is liquid and can be readily transferred into other forms of wealth eg livestock. Money can also be accumulated for future spending**

**Standard of value**

**Prices of goods and services reflect their relative value. Money provides a common basis for calculating rates of exchange between all goods and services**

1. The implementation of the interest rate cap in Kenya sought to facilitate cheap credit to boost economic growth in the country. State any additional *six* factors that could have affected the uptake of loans in the economy.

**Bank rate**

**Open market operation**

**Raising cash and liquidity ratio**

**Selective credit control**

**Direct control and moral suasion**

**Supplementary reserve requirements (6 marks)**

**Question Four**

1. Define the following terms:
2. Inflation (3 marks)

**This is the tendency of general rise of price of general goods over time,this may be due to rising labour costs,high taxes etc**

1. International trade (3 marks)

**This is the exchange of goods and services and capital across international boarders. eg. kenya selling khart to the united kingdom and importing fish from china**

1. State and explain three types of unemployment. (6 marks)

**FRICTIONAL ENEMPLOYMENT**

**This is when one is moving from one job to another,It occurs in the period between which one is still searching for the best suitable job**

**STRUCTURAL UNEMPLOYMENT**

**This is the form of unemployment caused by the changes in the structural demand of goods and services and by technological changes.eg. Due to mobile phones and communication technologies , there is less demand for messangers since communication methods have evolved**

**SEASONAL UNEMPLOYMENT**

**This is basically based on demand and supply. EG. When there is a high season for tourism in the country,there are more tour guards and vice versa. Meaning that when there is a low season ,workers are laid off.**

1. Kenya faces high levels of unemployment reported as 12.1 percent in 2010 and presently 9.31 percent. Explain any three ways that the government has over time used to achieve the reflected reduction. (3 marks)

**Monetary policy. Cutting interest rates to boost demand.**

**Fiscal policy, cutting taxes to boost aggregate demand**

**Lower minimum wage to reduce real wage unemployment**

**Education and training to reduce structural unemployment,eg Technical schools have been introduced**