



(University of Choice)

**MASINDE MULIRO UNIVERSITY OF
SCIENCE AND TECHNOLOGY
(MMUST)**

MAIN EXAMINATION

**UNIVERSITY EXAMINATIONS
2023/2024 ACADEMIC YEAR**

SECOND YEAR FIRST SEMESTER EXAMINATIONS

**FOR
BSC ECONOMICS AND BCS MATHEMATICS AND STATISTICS**

COURSE CODE: ECO 209

COURSE TITLE: MONEY AND BANKING

DATE: WEDNESDAY, 13-12-2023

TIME: 3:00 -5:00

INSTRUCTIONS TO CANDIDATES

ATTEMPT QUESTION ONE AND ANY OTHER TWO

TIME: 2 Hours

MMUST observes ZERO tolerance to examination cheating

This Paper Consists of 2 Printed Pages. Please Turn Over

QUESTION ONE (30 marks)

- a) With an example, explain what you understand by the term barter system of exchange? (4 Marks)
- b) List and explain four challenges encountered in barter system of exchange? (8 Marks)
- c) How does money overcome the problems encountered in barter trade? (6 Marks)
- d) In any economy, the importance of money is drawn from the performance of its functions. With illustration, briefly explain what the secondary and contingent functions of money are? (8 Marks).
- e) The central Bank of Kenya which is the regulator of the banking sector can use open market operation to regulate the amount of credit available in the economy. Explain how the Central Bank can apply this mechanism?(4 Marks)

QUESTION TWO (20 Marks)

- a) What do you understand by the term “a financial system”? (2 Marks)
- b) Explain any three functions that a financial system performs in an economy?(6 Marks)
- c) Explain how the following financial markets operate.(6Marks)
 - i. Money Markets
 - ii. Futures markets
 - iii. Spot markets
- d) List and explain any three roles of financial intermediaries. (6 Marks).

QUESTION THREE (20 Marks)

- a) What makes information central in the efficient operating of financial markets? (2 Marks).
- b) What do you understand by the following terms as used in information economics? (6 Marks)
 - i. Information asymmetry
 - ii. Moral Hazard
 - iii. Adverse Selection
- c) With an example explain how adverse selection can increase or decrease the risks in the banking system (4 Marks)
- d) How does moral hazard affect the outcome of most credit institutions in Kenya? Provide an example?(4Marks)

- e) You are a manager in one of the car Bazaars in Kakamega. The motor vehicle industry has been not been doing well lately. You have discovered that due to perception, customers are shunning buying from certain car sellers. How will you apply your expertise in solving the problems arising from adverse selection to increase your car sales? (4 Marks)

QUESTION FOUR (20 Marks)

- a) What do you understand by the term Credit Creation Function as operationalized by the Commercial Banks? (2 Marks)
- b) How does credit creation differ from the printing of money? (2 Marks)
- c) List and explain four main functions of central bank in any given economy. (8 Marks)
- d) Currently Kenya has a number of banks. If a loan of Kshs 1 Million is issued by the Kenya Commercial Bank (KCB) one of the banks in Kenya, it will result to advance of loans many times greater than this amount. Assuming the Central Bank of Kenya Cash Reserve Ratio is 15 percent.
- i). Hypothetically, explain how this is possible and the assumptions undelaying the outcome? (4 Marks)
- ii). Calculate the credit that will be created by the loan facility issued by the Kenya Commercial Bank. (4 Marks)

QUESTION FIVE (20 Marks)

- a) What is the meaning of money demand? (2 Marks)
- b) Explain the three motives which can lead to money demand in an economy (9 Marks)
- c) What is the difference between the Keynesian, Gurley and Shaw as well as the Milton Friedman definition of money supply? (6 Marks)
- d) A number of banks failed because of bank runs. How does it arise and what are the remedies (3 Marks)

