



UNIVERSITY OF ESWATINI

SECOND SEMESTER MAIN EXAMINATION PAPER, NOVEMBER
2021

FACULTY OF SOCIAL SCIENCES

DEPARTMENT OF ECONOMICS

COURSE CODE: ECO 402/ ECON 404

TITLE OF PAPER: MONETARY POLICY

TIME ALLOWED: 2 HOURS

Instructions

1. This paper consists of Sections (A) and (B).
2. Section A is compulsory.
3. Answer any two questions from Section B.

Special Requirements

Scientific calculator

Candidates may complete the front cover of their answer book when instructed by the Chief Invigilator and sign their examination attendance cards but must NOT write anything else until the start of the examination period is announced.

No electronic devices capable of storing and retrieving text, including electronic dictionaries and any form of foreign material may be used while in the examination room.

DO NOT turn examination paper over until instructed to do so.

SECTION A

Question One (Compulsory)

(40 Marks)

1. (a) Briefly state what the Impossible Trinity Principle is. [5]
- (b) With the aid of a diagram, illustrate the concept in (a) above using an example of an expansionary monetary policy action as depicted by the Mundell-Fleming model, under fixed exchange rates and perfect capital mobility. [15]
- (c) What is the implication of the Impossible Trinity Principle on the conduct of monetary policy for the Central Bank of Eswatini? [5]
- (d) With the aid of a diagram, explain how a monetary union overcomes the inconsistencies of the Impossible Trinity. Use the case of the EU to illustrate your answer. [15]

SECTION B

Answer Any Two (2) of the Following Questions:

(30 Marks Each)

Question Two

(30 Marks)

2. (a) Using appropriate examples, explain how monetary policy goals can be conflicting. [8]
- (b) Explain how a sharp rise in interest rates can provoke a financial crisis. [12]
- (c) Outline the Interest Parity Condition and its implications for the conduct of monetary policy in a small open economy. [10]

Question Three

(30 Marks)

3. (a) Distinguish between monetary targeting and inflation targeting. Be sure to highlight the pros and cons of each regime. [18]
- (b) Explain how bank panics can result in recessions? [12]

Question Four

(30 Marks)

4. (a) Outline the benefits and costs of capital mobility. [12]
- (b) (i) Describe the monetary transmission mechanism under the exchange rate channel. [10]
- (ii) In your opinion, is the channel in (i) above an effective transmission mechanism in Swaziland? Give reasons to support your answer. [3]
- (c) What are the benefits of using a nominal anchor in the conduct of monetary policy? [5]