Advanced Monetary Theory & Policy
EKN04X7
SUPPLEMENTARY ASSESSMENT

DEPARTMENT OF ECONOMICS

Date	September 2014
Marks	40
Time	3 hours
Examiner:	Arnold Wentzel
Internal moderator:	Prof Lorraine Greyling
External examiner:	Dr Sandra Mollentze (SARB)

Answer all the following questions:

Question 1 **[18]**

a) Why is central bank independence regarded as critical to the success of inflation targeting according to the monetary policy consensus? (4)

b) Is central bank independence in South Africa likely to ensure the success of inflation targeting? Explain why/why not with reference to the monetary policy transmission mechanism. (4)

c) Should central banks in developing countries be independent? Argue both sides and come to a reasoned conclusion. (10)

Question 2 **[10]**

Macroprudential policy was a response to the financial instability and rising levels of risk in the banking system in recent years.

a) Explain why proponents of the monetary policy consensus did not see the need for macroprudential policy. (4)

b) What is the difference between microprudential policy and macroprudential policy in the way they try to address risk in the banking system? (2)

c) How does macroprudential policy (as envisaged by Basel III) aim to address: (i) solvency risk; and (ii) liquidity risk? (4)

Question 3 **[12]**

a) Explain how the recent *reduction* of quantitative easing by the Federal Reserve in the USA is likely to influence the slope of their yield curve. (4)

b) How does *more* quantitative easing affect the liquidity shortage that a central bank tries to maintain? Explain with reference to the central bank's balance sheet. (4)

c) If a government runs a budget *deficit* how will that affect the central bank's balance sheet and its liquidity shortage? (4)

END