UNIVERSITY OF JOHANNESBURG	**Monetary Policy B** **EKN4807|MTE8x02** **FINAL ASSESSMENT** **DEPARTMENT OF ECONOMICS**

Date	20 November 2017
Marks	70
Time	3 hours
Examiner:	Mr F Kirsten
Internal moderator:	Dr K Osei-Assibey
External examiner:	Prof AM Pretorius

Answer all of the questions below:

Question 1 (5)

"2017-South Africa's central bank cut borrowing costs for the first time in five years as inflation eases and after the country slipped into a recession. The Monetary Policy Committee reduced its key rate by 25 basis points to 6.75%, governor Lesetja Kganyago told reporters on Thursday in the capital, Pretoria, citing concern about the nation's growth outlook. Only three of 23 economists in a Bloomberg survey predicted a reduction." MONEYWEB.

1.1 Read the extract above. Explain a potential time inconstancy problem in relation with South Africa's foreign investment outlook and the decision by the Reserve Bank to reduce the repo rate. (5)

Question 2 (10)

2.1 "Central banks in emerging markets have come out of the crisis looking a lot better than their advanced economy counterparts" (Prasad, 2010).

Explain this comment by referring to the reasons why central banks in emerging markets came out of the global financial crisis looking better than the central banks of more developed countries (like the USA, EU and UK). (5)

2.2 The 2008 financial crisis was experienced in two waves in South Africa. Explain these two waves briefly and mention how these two waves were linked. (5)

Question 3 (25)

3. 1 Recent stock market crashes may have a severe impact on the economy, with some academics calling for intervention.

a) Explain how decreasing asset prices affect the inflation rate in the conventional monetary policy transmission mechanism. (3)

b) Explain how interest rate policy can be used to counter dramatic falls in asset prices. (2)

c) How can these lower asset prices negatively impact on bank lending and credit extension? (3)

d) Explain how macroprudential policy can counter some of the harmful effects of asset price bubbles. (3)

e) Explain why the monetary policy consensus is against any intervention in the asset market aimed at stabilising asset prices.(4)

3.2 Explain the difference between liquidity and credit risk in terms of threat and solutions (6)

3.3 Since the financial crisis of 2007/8, the thinking about macroeconomic and monetary policy has changed. Explain the role of fiscal policy before the crisis <u>and</u> how this has changed after the crisis. (4)

Question 4 **[15]**

4. 1 Explain how a central bank can influence the slope of their yield curve through quantitative easing. (4)

4.2 Explain how the European Central Bank (ECB) tried to manage the sovereign debt crisis in Europe through open-market operations in the bonds of debt-ridden countries. (4)

4.3 In a fiat money system, an increase in government spending does not have a crowding-out effect, but will most likely put downward pressure on short-term interest rates. Explain this process. (7)

Question 5 **(7)**

If a country defaults on its sovereign debt, how would this affect the central bank of the specific country? In your answer focus on: (i) how it would affect this central bank's function as lender of last resort; and (ii) how it would affect the balance sheet of that central bank.(7)

Question 6 **(8)**

Explain the various positive and negative impacts of virtual money (like bitcoin) on monetary policy and the economy. (8)

END