



Kasarani Campus
Off Thika Road
Tel. 2042692 / 3
P. O. Box 49274, 00100
NAIROBI
Westlands Campus
Pamstech House
Woodvale Grove
Tel. 4442212
Fax: 4444175

KIRIRI WOMENS' UNIVERSITY OF SCIENCE AND TECHNOLOGY
UNIVERSITY EXAMINATION, 2024/2025 ACADEMIC YEAR
FOURTH YEAR, FIRST SEMESTER EXAMINATION
FOR THE DEGREE OF BACHELOR OF SCIENCE
(BUSINESS ADMINISTRATION)

Date: 10th December, 2024
Time: 8.30am – 10.30am

KFI 2402 - MONEY AND BANKING

INSTRUCTIONS TO CANDIDATES

ANSWER QUESTION ONE (COMPULSORY) AND ANY OTHER TWO QUESTIONS

QUESTION ONE (30 MARKS)

US FEDERAL RESERVE INTEREST RATE CUT

The Federal Reserve, US central bank on Wednesday, 18th September, 2024 enacted its first interest rate cut since the early days of the Covid pandemic, slicing half a percentage point off benchmark rates in an effort to head off a slowdown in the labor market. With both the jobs picture and inflation softening, the central bank's Federal Open Market Committee chose to lower its key overnight borrowing rate by a half percentage point, or 50 basis points, affirming market expectations that had recently shifted from an outlook for a cut half that size. Outside of the emergency rate reductions during Covid, the last time the FOMC cut by half a point was in 2008 during the global financial crisis. The decision lowers the federal funds rate to a range between 4.75%-5%. While the rate sets short-term borrowing costs for banks, it spills over into multiple consumer products such as mortgages, car loans and credit cards.

In addition to this reduction, the committee indicated through its “dot plot” the equivalent of 50 more basis points of cuts by the end of the year, close to market pricing. The matrix of individual officials’ expectations pointed to another full percentage point in cuts by the end of 2025 and a half point in 2026. In all, the dot plot shows the benchmark rate coming down about 2 percentage points beyond Wednesday’s move. The Committee has gained greater confidence that inflation is moving sustainably toward 2 percent, and judges that the risks to achieving its employment and inflation goals are roughly in balance,” the post-meeting statement said. Trading was volatile after the decision with the Dow Jones Industrial Average jumping as much as 375 points after it was released, before easing somewhat as investors digested the news and considered what it suggests about the state of the economy. Stocks ended slightly lower on the day while Treasury yields bounced higher.

Required:

- a) The US central bank's Federal Open Market Committee (FOMC) had suggested the use of the open market operations as a monetary policy tool to deal with inflation. Describe your understanding of open market operations and discuss how it helps reduce inflation. (6 marks)
- b) Discuss any limitation of open market operations as a monetary tool employed by the US central bank's Federal Open Market Committee (FOMC). (2 marks)
- c) Discuss any other two monetary policy tools at the US central bank disposal that can be used to bring price stability and reduce unemployment. (4marks)
- d) The US central bank has a major role of preventing bank runs. Describe your understanding of bank run and identify probable causes of bank runs and what steps can be taken to prevent them from happening. (6 marks)
- e) The US Federal reserve bank has many other roles besides bank supervision. Discuss any other functions of the US central bank. (6 marks)
- f) The US central bank interest rate cut news had an effect on major world financial markets. This behavior by investors underscores the role of information in financial markets. Describe the three information sets in connection with market efficiency. (6 marks)

QUESTION TWO (20 MARKS)

- a) Describe four roles of the retirement benefits authority (RBA) in the regulation of the financial systems in Kenya. (8 marks)
- b) Distinguish the following terms as used in monetary economics
- i) Creative accounting and currency hoarding. (6 marks)
- ii) Floating exchange rate and Fixed exchange rate. (6 marks)

QUESTION THREE (20 MARKS)

- a) Moral hazard is a term frequently heard in recent debates over the reform of financial institutions. Describe any three types of moral hazards likely to be witnessed in a financial system. (8 marks)
- b) As elucidated by Eugene Fama on information efficiency, there has been a discussion on whether or not investors can be able to beat the market and therefore one can be able to predict future price movements. However, financial market anomalies Dimson(1989)challenge the principles of efficient markets. Discuss any three stock market anomalies. (6 marks)
- c) Financial market failure occurs when money, equity and bond markets failure to achieve an efficient and equitable outcome. This can lead to economic and social costs including macro instability and loss of trust and confidence in financial institutions. Describe the following terminologies used in relation to financial market failure.
- i) Insider trading
- ii) Adverse selection (6 marks)

QUESTION FOUR (20 MARKS)

- a) Discuss any four features of informal finance. (8 marks)
- b) The global financial crisis of 2007/2008 has necessitated the reconsideration of even basic principles of financial regulation. Meanwhile, the need for financial development remains as strong as ever in emerging markets. Describe any likely consequences of under regulation of financial markets. (6 marks)
- c) The barter system of exchange has been used in many societies in trade for several years. Explain limitations of the barter system and identify how money deals with those limitations. (6 marks)

QUESTION FIVE(20 MARKS)

- a) The U.S. Treasury Department officially named China a currency manipulator after the Peoples Bank of China devalued the yuan in response to new tariffs that were imposed by the U.S in 1st September, 2019. Describe effects of currency devaluation on a country's economic condition. (6 Marks)
- b) Discuss any four limitations of monetary policy in developing countries. (8 marks)
- c) Financial markets play a very important role in a country's financial system. Explain consequences of undersupply of information in financial markets. (6 Marks)