

University of Ruhuna

2015/2016 Academic Year  
Bachelor of Arts (Special) Degree 2000 Level  
Second Semester Examination – March 2017

ECN/STS 22653 – Monetary Theory

Answer Four (04) Questions Only.

Time: 03 Hours



1. (i). “The components of micro Economics and macro Economics are the base in strengthening the monetary theory” Explain brief with emphasizing the nature and contents of monetary theory.  
(05 Marks)
- (ii). “The difficulties generated from the barter system of exchange resulted to create money which necessary for effective exchange system” List and explain these difficulties.  
(03 Marks)
- (iii). What do you mean by a financial system? Discuss the economic functions of a financial market.  
(04 Marks)
- (iv). What are the primary functions of money? Describe clearly how money performs these functions.  
(03 Marks)
2. (i). Give definition to circular flow of money and explain the circular flow of money in an economy with government sector using appropriate diagrams.  
(10 Marks)

(ii). Why is the circular flow of money important in an economy?

(05 Marks)

3. (i). State the assumptions which are based for the classical theory of money.

(05 Marks)

(ii). "Money is neutral in determination of employment, income and output in an economy" critically examine the above statement focusing on the classical economic theory.

(10 Marks)

4. (i). Explain with numerical example the relationship between rate of interest and bond prices.

(04 Marks)

(ii). How does an increase in the monetary aggregates affect the rate of interest? Is there any limit beyond which the increase in the money supply will not decrease the rate of interest?

(06 Marks)

(iii). Explain the role of money in the Keynesian theory.

(05 Marks)

5. (i). Distinguish between monetary policy and fiscal policy in brief.

(03 Marks)

(ii). Draw IS-LM diagrams with differently sloped LM curves and examine the relative effectiveness of expansionary monetary policy in hypothetical economy.

(04 Marks)

(iii). Explain the relative effectiveness of the followings diagrammatic forms using IS-LM framework.

- (a). The situation where the fiscal policy is completely ineffective.
- (b). The situation where the fiscal policy is completely effective.
- (c). The situation where the fiscal policy is less effective.
- (d). The situation where the fiscal policy is more effective.

(08 Marks)

6. Write short notes on the followings

- (i). Quantity theory of money
- (ii). Keynesian views on neutrality of money.
- (iii). Liquidity trap.
- (iv). Fiscal policy and crowding out effect.

(15 Marks)

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