MODEL ANSWERS

SECTION A – MULTIPLE CHOICE

1. a
2. d
3. c
4. a
5. a
6. b
7. a
8. d
9. a
10. b
11. c
12. c
13. d
14. a
15. c
16. b
17. c
18. a
19. d
20. c

SECTION B – ESSAY QUESTIONS

1. Financial System
2. Financial system is a complex composition of institutions that play different functions in providing financial services in an economy
3. Financial Intermediation is the process of uniting units of surplus units to those that in deficit. The surplus units are called depositors, and the intermediation process is, for example handled by a commercial bank, which identifies a deficit unit, called borrower, and lend the funds, with ultimate risk being retained by the intermediary.
4. Classifications of markets is based on the following;

* Based on maturity as follows:
* money market, where funds are loaned to borrowers for less than a year and interest is relatively lower due short term nature of facilities
* capital market are for securities with longer period of maturity, more than one year, with interest relatively higher interest,
* Based on whether the traded securities are new or old.
* Primary markets are where all new capital are traded
* Secondary markets are where previously issued stocks, shares or treasury bills are traded

1. RBM as the most important institution, support hypothesis:

* Banker to commercial banks, as commercial banks maintain accounts at the central bank
* Issue legal tender currency in Malawi as guided by Reserve Bank of Malawi Act, 1989
* Banker and advisor to Malawi government
* Managing government debt
* Maintaining external value of the Malawi Kwacha
* Managing the bank rate, that is rate at which banks borrow from Reserve Bank of Malawi
* Enforcing the Liquidity Reserve Ratio (Requirement)
* Responsible for promoting developments in payment systems, settlement and clearing inspectorate in the country
* Lender of last resort when commercial banks are in distress
* Supervising commercial banks and other financial institutions
* Providing information to investors
* Ensure soundness of the financial system
* Enhancing the monetary policy, through control of money supply

1. A paper on barter trade.

In introduction highlight that there is a problem in the economy and try to define hyperinflation by explain the

1. Barter trade is a type of transaction where goods and services are directly exchange for other goods and services without employing the use of money as a medium of exchange. For example, salt being exchange to maize.
2. Eight problems that might be encountered if barter trade is adopted:

* Deciding the relative values of one product in terms of the other
* Double coincident of wants
* Divisibility problems
* Portability, where one has to travel to a place where to find the commodity he wants
* Durability of the commodities, for example, vegetables that might lose value and flavor if kept long
* Lack of uniqueness of the items being exchanged to be recognized by several parties in trading
* Storing the items for deferred payment will be difficult
* Lack of homogeneity, for example cattle that might be different thereby giving problems to traders as afar as comparability is concerned

1. Monetary policy
2. Refers to the measures that the monetary authorities take to ensure proper functioning of the financial system of the country’s economy. Directs economic activity of the country in the manner that government desires.
3. Why it is developed:

* To prevent price instability which is associated with inflation and deflation
* To manage balance of payments of a country by ensuring proper functioning of the financial sector and promoting capital investment and growth

1. Four instruments that are used in monetary policy

* Open market operations where the central bank can go directly into the market to buy or sell securities to control liquidity in the economy
* Discount rate, which is the cost of borrowing from the central bank. Movements upwards or downwards of the discount rate affects the amount of money in circulation in an economy
* Liquidity Reserve Requirement is the statutory requirement that is imposed on commercial banks to keep a certain percentage of the deposits they collect in a non interest earning account at the central bank

Moral suasion is where the central bank engages the commercial banks to mutually agree on a course of action to control the supply of money in the economy. For example the central bank can ask commercial banks to reduce giving loans to control inflation.

1. Commercial Banks and banking transformation
2. A commercial bank – a legally licensed bank which is authorized to carry out banking business in a country after meeting all the requirements as defined by the central bank.
3. the three main sources of revenue for commercial banks

* Revenue from loans – the provision of loans and overdrafts generate revenue in a form of interest earnings and fees.
* Revenue from fees and charges – payments on various services offered such as provision of statements, production of bank cheques, special clearances, etc.
* Returns on investments and securities – banks use part of customers’ deposits to purchase securities such as treasury bills that have yields or interest earnings on top of the purchase price.

1. Four reasons for great transformation in the banking and financial sector of late

* Changes in real sector of the economy – leading to demand for new types of financial services, such as growth of multinationals that has made banks to be outward focused, than concentrating in their primary economy.
* Improvements in technology – the growth of electronic funds transfer systems and plastic card-using devices have been the most obvious effect of computers revolution and the need for banks to embrace more radical changes as well as enhanced security measures.
* Financial liberalization or deregulation – the relaxing down of the controls over banks by respective governments in terms of rules and regulations with which banks are supposed to comply or making it easier for new entrants into the banking sector to commence business.
* Internal innovations – the ever growing competition within the banking and financial services sector has forced banks to change internally to embrace a more effective and innovative work force in a bid to be more competitive.