

OLLSCOIL NA hÉIREANN, GAILLIMH  
NATIONAL UNIVERSITY OF IRELAND, GALWAY

SUMMER EXAMINATIONS 1999

**ECONOMICS PAPER 2 (EC100, EC102)**

1<sup>st</sup> Arts, 1<sup>st</sup> BComm, 1<sup>st</sup> FinMath, 1<sup>st</sup> BScIT, 1<sup>st</sup> CorpLaw

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**Time Allowed: THREE HOURS**

**N.B. There are specific instructions for each of the three sections. Please read them and the questions carefully. Use a separate answer book for each section. (Each section is worth 100 marks out of a total of 300. Marks for each question are in parentheses.)**

**SECTION A MICROECONOMICS**

**Answer the following question (100 marks):**

Explain the derivation of the supply curve using graphs. Why is the lowest point on the supply curve associated with the average variable cost curve rather than the average total cost? Show what happens to equilibrium price and quantity when the price of resources rise.

## SECTION B MACROECONOMICS

**Part 1: Look at the following table and answer the questions below. (20 marks)**

	Annual change in GDP	Annual change in CPI	Most recent Unemployment rate	Annual change in the Trade balance (in billion \$)
<b>Euro-11</b>	2.4 %	0.8 %	10.6 %	+ 94.9
<b>U. S.</b>	4.3 %	1.7 %	4.4 %	-248
<b>France</b>	2.8 %	0.2 %	11.4 %	+27.2
<b>Germany</b>	2.6 %	0.2 %	10.5 %	+75.7
<b>Britain</b>	1.3 %	2.4 %	6.2 %	-34.5
<b>Italy</b>	1.2 %	1.5 %	12.3 %	+26
<b>Ireland</b>	7.8%	2.8 %	8 %	+1.7

(Sources: The Economist, March 13<sup>th</sup>, Irish Central Bank, Autumn 1998 report.)

- Which country has the highest inflation? Gives some reasons why this may be the case.
- Which country has the largest change in its trade balance? Speculate as to what may happen to the value of that country's currency.
- Do you see any relationship between the annual change in CPI and the most recent Unemployment rate for these countries? Explain your answer.

**Part 2: Answer ONE of the following two questions. (80 marks)**

- The two main schools of thought in macroeconomics studied were Keynesian economics and Neo-classical economics.
  - What is the historical background behind the popularity of each school of thought?
  - Explain the differences between Keynesian economics and Neo-classical economics regarding their view on how a government can increase the wealth of a country.
  - What policy recommendations does each of these schools of thought propose?

2) As a member of the European Union and due to its joining the Euro on January 1, 1999, Ireland's economy is tied closely to Europe's.

- a) What are the Maastricht criteria regarding budget deficits and debts?
- b) What are the limitations for Ireland's fiscal and monetary policy given its EU membership and adoption of the Euro?
- c) What difficulties for Ireland do you foresee because the U. K. has not adopted the Euro?
- d) Given the limitations you have listed above, what policies are still available to the Irish government to influence the economy? Explain your answer.

## SECTION C APPLIED ECONOMICS

**Answer FOUR of the following questions. (25 marks each)**

- 1 (a). A farmer's land lies next to a river which is fished by one fisherman. The farmer spreads fertiliser on her land which increases the value of her crops by £100 per year. The fisherman estimates that the value of his catch is reduced by £40 per year because of pollution from the fertiliser. State the Coase theorem. What outcome would the Coase Theorem predict if (a) the farmer is liable for the damage caused to the fish; and (b) the farmer is not liable. What are the limitations of the Coase theorem?
- (b). There are 51,000 citizens in a city called Happyway. Each of them places a value of £10 on having a spectacular fireworks display in the city on 31/12/1999. This display can be seen at any place in the city. The cost of this display is £200,000. Suppose a local private company Ents. Ltd. decided to organise this fireworks display and sold tickets for it. What is likely to happen? Explain briefly your answer.
2. What do economists mean by allocative efficiency? Show diagrammatically why a monopoly is less efficient than perfect competition. What is the relationship between this theory and policy in Ireland regarding mergers?
3. In the current debate over taxi licences in Dublin the existing owners of licences are unanimous in their protest against any increase in the number of licences. Their argument is that an increase in the number of licences would have a negative affect on their income.
- (a) Illustrate how the two markets - the 'market' for new licences and the market in existing licences - are inter-related.
- (b) 'Since there are hundreds of thousands of potential users of taxi services in Dublin and only a few thousand licence holders one would expect that the customers would have far more political power than the licence holders.' True/False (explain your answer).
4. "The current economic boom in Ireland is due to the cumulative effect of a number of causes." Discuss.

5. (a) For the midwestern United States, 1988 brought one of the worst droughts ever recorded. Corn production was 35 percent lower than had been expected before the drought; soybean production was down more than 20 percent, wheat was down more than 10 percent, and oats and barley were down more than 40 percent.

Analyse the consequences of these events using the basic laws of supply and demand. Your answer should consider the likely effects on

- (i) the price of these crops
- (ii) the effects on meat production (given that these crops are a major input into the production of cattle and chicken)
- (iii) the market for eggs, and
- (iv) the market for vegetables whose supply was not affected by the drought

- OR -

- (b) Consider the market for an agricultural commodity such as milk. Suppose dairy farmers think the price of milk is too low. Suppose the government orders each dairy farmer to reduce production by the same percentage amount. Analyse the effects of such a policy on the market for milk. Will farmers gain from such a policy? Explain your answer.

6. The case study Consumers and Information uses a model that is built on the concept that consumers derive benefits from information and that these benefits must be balanced with the cost of attaining that information. Show how this model can be used to explain a consumer's search behaviour. What particular problems arise in markets where the buyer has less information than the seller such as the market for second-hand cars?