

UNIVERSITY OF WARWICK

Summer Examinations 2015/2016

Topics in Applied Economics (3b)

Time Allowed: 2 hours plus 15 minutes reading time during which notes may be made (on the question paper) BUT NO ANSWERS MAY BE BEGUN.

Answer **FOUR** questions, including (i) **TWO** short-answer questions and **TWO** long-answer questions and (ii) at least **ONE** question from EACH section. The paper consists of 3 Sections, one for each Topic. Each Section contains one short-answer question (worth 15 marks) and one long-answer question (worth 35 marks). Answer Section A questions in one booklet, Section B questions in a separate booklet; and Section C questions in a separate booklet

Approved pocket calculators are allowed.

Read carefully the instructions on the answer book provided and make sure that the particulars required are entered on each answer book. If you answer more questions than are required and do not indicate which answers should be ignored, we will mark the requisite number of answers in the order in which they appear in the answer book(s): answers beyond that number will not be considered.

Section A: Answer AT LEAST ONE Question

1. Short-Answer Question:

Explain and contrast the principles of the Victorian and Keynesian fiscal constitutions. In particular, did their views on tax- versus bond-financed government spending differ?

Answer with reference to the appropriate thinkers and sources from the time where possible. **(15 marks)**

2. Long-Answer Question:

- (a) Explain the emergence of trade imbalances between Germany and the Eurozone periphery. **(10 marks)**
 - (b) Why might these imbalances be a problem? What could be done to correct them? What should be done? How would looser monetary policy affect Eurozone rebalancing? **(25 marks)**
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Section B: Answer AT LEAST ONE Question

3. Short-Answer Question:

- (a) Why have Central Banks turned to Quantitative Easing (QE) as a tool of monetary policy? Briefly outline how it might affect the economy through **one** of the following channels of transmission: via banks, via non-bank financial institutions, via the exchange rate. **(6 marks)**
 - (b) According to Joseph Stiglitz, “The standard macroeconomic models not only failed to predict the Great Recession, they also said it couldn’t happen.” With respect to DSGE models, explain which assumptions rule out the risk of financial crisis. **(9 marks)**
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4. Long-Answer Question:

- (a) “How fast the debt/ income ratio will fall in the process of fiscal consolidation depends crucially on $\rho - \gamma$, where ρ is the real interest rate and γ the growth rate of national income.” Explain and discuss with examples, assuming the economy continues to expand at its capacity growth rate and interest rates remain constant as well. **(15 marks)**
- (b) Explain and discuss **ONE** of the following critiques of policy rules:

EITHER

- i. The Basel value-at-risk rules for regulating investment banks before the financial crisis failed to realise that - like pedestrians on the Millennium Bridge - the responses by those involved will amplify the impact of external shocks.” **(20 marks)**

OR

- ii. “The rules for fiscal consolidation in the Eurozone after the crisis made the mistake of ignoring the impact of simultaneous tightening of fiscal policy across the Eurozone on European GDP”. **(20 marks)**
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Section C: Answer AT LEAST ONE Question

5. Short-Answer Question:

- (a) Explain how capital market failures justify government intervention in the market for education. **(6 marks)**
- (b) Discuss the extent to which education in the UK is and should be financed by progressive taxation. **(9 marks)**

6. Long-Answer Question:

- (a) Increased consumer and producer sovereignty can create many benefits, including a more competitive market and greater choice. With reference to the key microeconomic objectives, discuss how effective choice and competition are in school education. Does your answer change for higher education? **(15 marks)**
- (b) Finding ways to introduce more competition and choice has been a key objective of quasi markets in education, attempting to improve efficiency and equity. It has been suggested that “Education vouchers present a problem-free solution to the inequalities in achievement that are observed between the richest and poorest families.” With reference to relevant examples, evaluate the case for and against education vouchers, in light of their objectives.

Where possible you should refer to appropriate literature for both empirical and theoretical evidence. **(20 marks)**