INSTRUCTIONS

- Please don’t write your name anywhere on the exam, except in the space provided above (↑).
- Please answer all questions. Be concise, but if you need extra space, you can use the blank pages at the end.

Part 1: Definition and relevance (10 points each = 40 points) For each concept below, briefly (a) define the concept and (b) apply it to some contemporary or historical real-world issue we have studied.

1. The (first!) invisible hand theorem.

2. Stationary bandit.
3. The Coase theorem.

4. Economic backwardness.

Part 2: Short answer (12 points)
5. Your supervisor at Goldman Sachs asks you to predict the growth rate of GDP for South Africa over the next two decades (the growth rate of real GDP, i.e., ignoring inflation). Using the concept of an aggregate production function, explain briefly (in words, using equations only if you wish to) how you would approach this problem, and what considerations would determine how rapidly South Africa is likely to grow.
Part 3: Short essays (16 points each = 48 points) Read these questions carefully, and make sure you respond to the questions being asked. Bring in whatever material from our readings – or from other parts of the seminar – you feel is most relevant for crafting a clear and convincing answer. You do not have to use all of the allotted space!!

6. Olson argues that stable societies are subject to the efficiency-eroding activities of special interest groups. What evidence does he offer, in terms of the economic performance of countries in the 20th century? How is it that governments that are run by relatively encompassing interests – e.g., secure autocrats or majorities in a stable democracy – allow this ‘sclerosis’ effect to occur, when it is not in their interest to do so?
In his final chapter, Olson states two conditions that he claims are both necessary and sufficient for achieving economic prosperity in a market economy (defining ‘prosperity’ as living standards that are not dramatically below those of the advanced countries of the world). These are “secure and well-defined individual rights … and … the absence of predation of any kind” (pages 195-196). By these criteria, is Russia likely to experience rapid increases in prosperity over the next generation? Do you think these criteria are in fact the ones that will matter most in Russia’s economic success or failure?
8. Russia and China started their economic reforms at about the same time. Both started with centrally planned economies, and both took a gradualist approach to economic reforms, at least initially. Why did Russia abandon gradualism? Was this a mistake, in your view – i.e., was there a feasible gradual alternative that would have delivered a better economic outcome over the first decade of reforms?