



MACHAKOS UNIVERSITY

University Examinations for 2017/2018

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF ECONOMICS

SECOND YEAR FIRST SEMESTER EXAMINATION FOR

BACHELOR OF ECONOMICS AND STATISTICS

BACHELOR OF ECONOMICS AND FINANCE

BACHELOR OF ECONOMICS

EAE 201: ECONOMICS OF PUBLIC EXPENDITURE

DATE: 15/12/2017

TIME: 8:30 – 10:30 AM

INSTRUCTIONS

Answer Question **ONE** and any other **TWO** questions

QUESTION ONE (COMPULSORY) (30 MARKS)

- a) Discuss the three conditions for welfare maximization. (6 marks)
- b) Explain the rationale for government intervention in the economy of your country. (8 marks)
- c) Various factors have contributed to the growth of public expenditure and the growth of the public sector in developing countries. Discuss. (10 marks)
- d) Under what circumstances are private market forces likely to solve the free rider problem? (6 marks)

QUESTION TWO (20 MARKS)

For each of the examples below, please answer the following:

- a) Does an externality exist? If so, classify the externality as positive/negative (or both).
- b) If an externality exists which of the government's tools are best suited to address the issue: quantity regulation, taxes/subsidies, tradable permits, or something else?
 - i. Carbon emissions from vehicles. (5 marks)
 - ii. Your upstairs neighbours throwing an awesome, but loud party. (5 marks)
 - iii. Buying a car with added safety features that prevent the drivers/passengers' deaths in the event of an accident. (5 marks)
 - iv. Bringing crying babies on a plane. (5 marks)

QUESTION THREE (20 MARKS)

- a) Discuss the Arrows impossibility theorem explaining its criteria for collective decision making. (6 marks)
- b) Discuss principles proposed to govern the public expenditure decisions. (8 marks)
- c) Explain the reasons why the budget may be presented in parts (split). (6 marks)

QUESTION FOUR (20 MARKS)

- a) Despite the efforts made by governments of developing countries in the efficient allocation of resources, Pareto efficiency has not been achieved. Discuss the reasons for this Pareto inefficiency in your country. (8 marks)
- b) Discuss the functions of the government. (5 marks)
- c) Explain the rationale for Performance and Programme Budgeting System (PPBS). (7 marks)

QUESTION FIVE (20 MARKS)

Write brief notes on the following concepts

- i. Adverse selection (5 marks)
- ii. Moral hazard (5 marks)
- iii. Free rider problem (5 marks)
- iv. Pareto – optimal condition (5 marks)