

ECON 133 “Global Inequality and Growth”
Final 2, May 18

Student name:

Student ID number:

You have 3 hours

Instruction: Write your answers in the boxes: nothing outside of the boxes will be graded. You can use the computer or print the assignment and scan your answers. **If writing in word, don't expand the boxes!**

If using word to answer the questions you can either use the equation editor (click insert -> equation) or simply use computer typography: e.g. you can write $s_t \cdot \frac{Y_t}{W_t}$ as s_t*(Y_t/W_t)

Exercise 1: True or false statements (12 points)

a) True or false: The goal of government is to maximize tax revenue. (2 points)

b) True or false: The corporate tax disincentivizes investment by lowering the investor return. Therefore, the optimal corporate tax rate is zero. (2 points)

c) *True or false: Suppose there are no behavioral responses to labor income taxation and the social planner maximizes a Rawlsian social welfare function. The optimal labor income tax rate is in this case equal to 100%. (2 points)*

d) *True or false: Highly unequal countries are usually countries where an individual's effort predominantly determines their economic outcomes. That is, highly unequal countries usually have low intergenerational inequality". (2 points)*

e) *True or false: Most projections point to lower overall economic growth (g) in the 21st century due to lower population growth (n), scarcity of resources and lower productivity growth (h). Everything else equal, this will imply an increase in the global wealth-to-income ratio. (2 points)*

f) *True or false: The largest determinant of income today is not class (measured by within country inequality) but instead location (measured by between country inequality). (2 points)*

Exercise 2: Wealth (10 points)

- a) *Governments across the world have seen a decline in public wealth as a share of national income – why is that? And is it important? (1 point)*

- b) *How can economists measure wealth inequality? (2 points)*

c) Describe how $r > g$ may impact wealth inequality. (1 points)

d) What are the other long-run factors that impact wealth inequality? (2 points)

e) Individual i wealth accumulation at time $t + 1$ can always be written:

$$W_{t+1}^i = (1 + q_t^i) \cdot (W_t^i + s_t^i Y_t^i)$$

Where W_t^i is wealth, Y_t^i is income, s_t^i is net savings rate,

$1 + q_t^i$ is rate of capital gains (price effect) in year t

Write the expression for the long-term steady-state top wealth share (no need to derive).
How does q_t^i enter the expression? (2 points)


f) Is inherited wealth a meaningful share of total wealth today in the United States? Why does that matter when deciding whether to tax capital income? (2 points)

Exercise 3: Labor institutions and wage inequality (10 points)

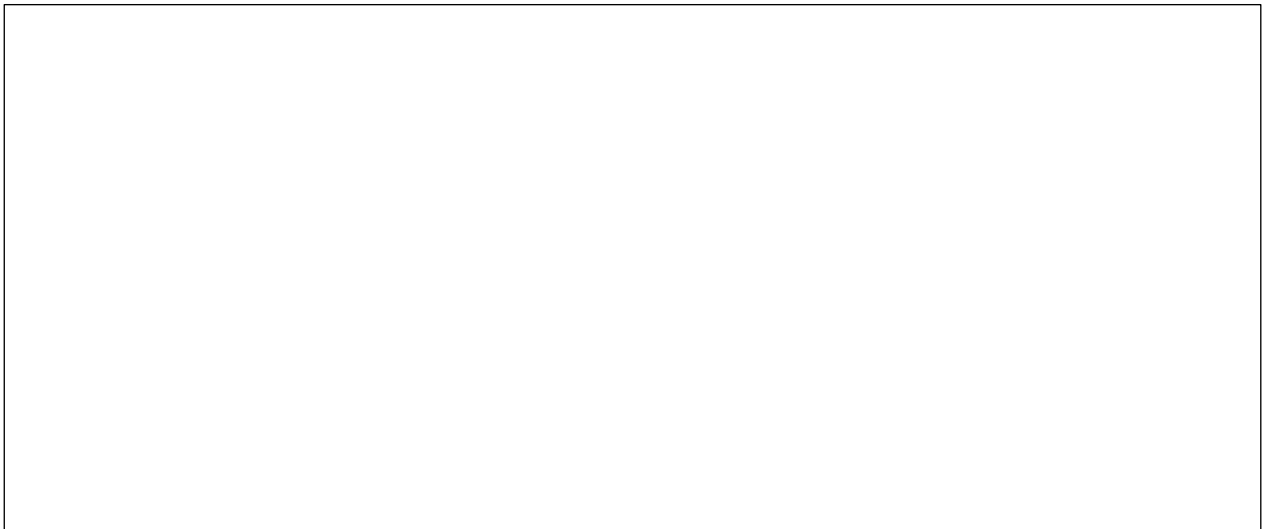
a) What considerations should a government have when setting a minimum wage? (1 point)

b) How has the minimum wage impacted racial inequalities in the United States? (1 point)

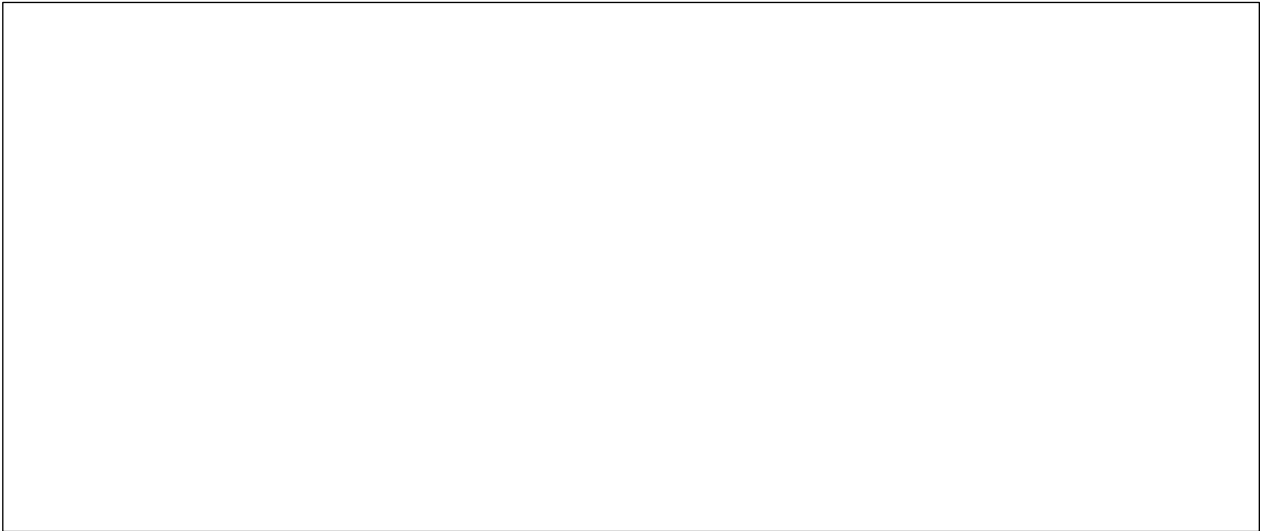
c) *Union membership has been in free fall in the US since 1980. What are the issues confronting unions in the United States? (2 points)*



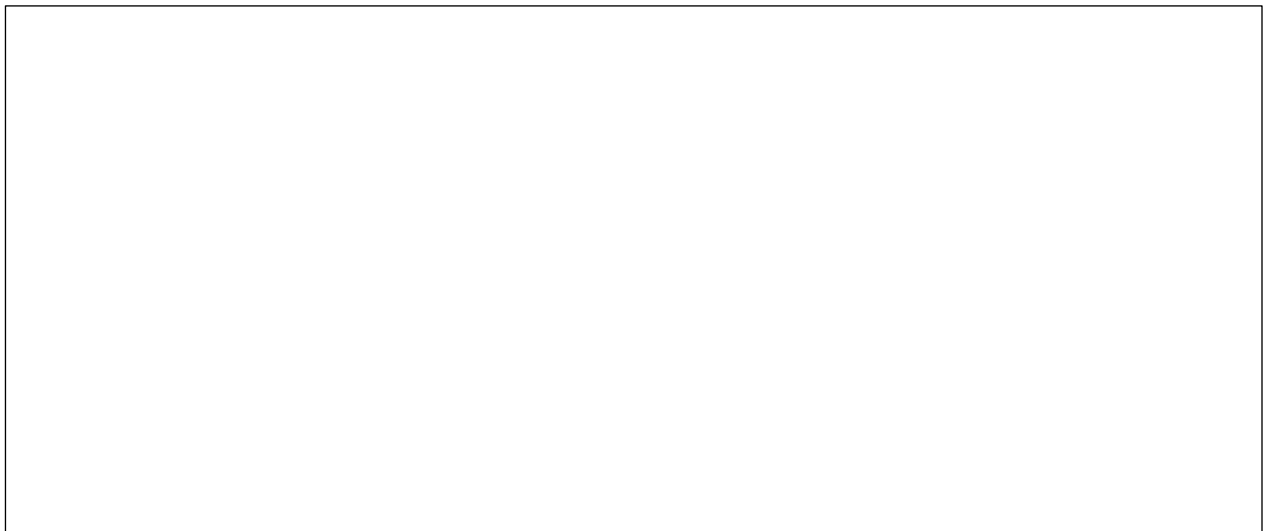
d) *What are the benefits/disadvantages of having unions set minimum (floor) wages vs government set minimum wages? (1 point)*



e) *How do trends such as globalization and technology affect wage inequality? (2 points)*



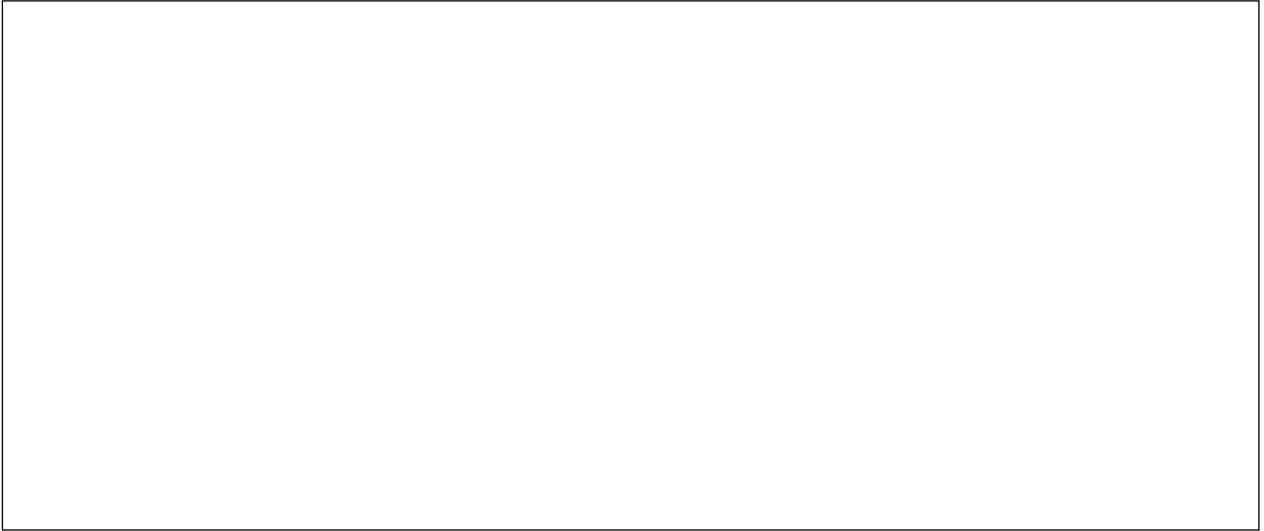
f) *Since 1980 the US has seen a dramatic increase in wage inequality compared to continental Europe. Was this an unavoidable consequence of globalization and technology? (1 point)*



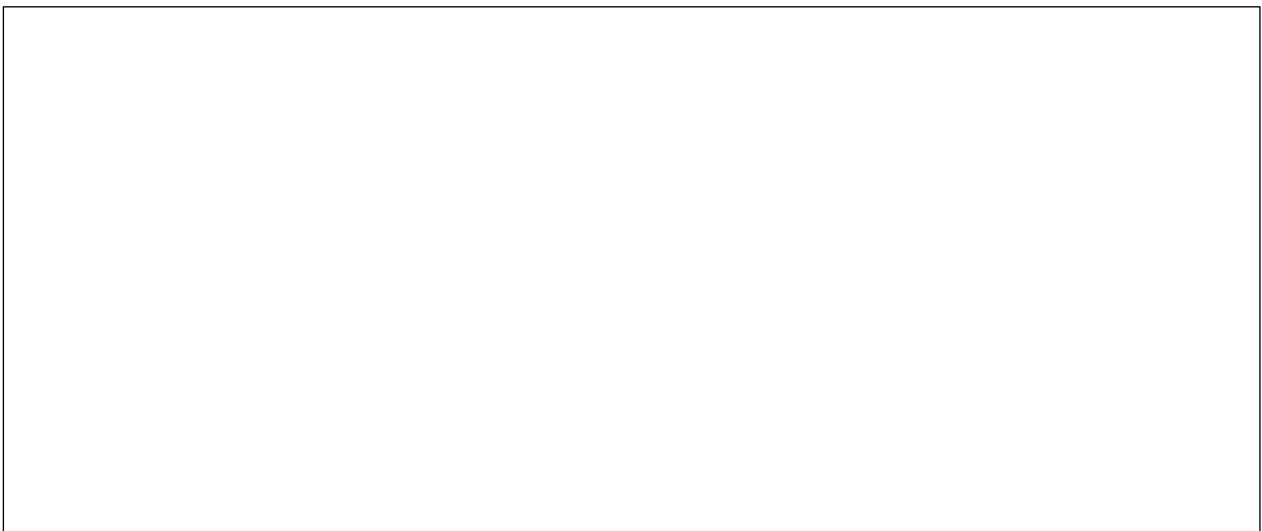
g) The average income in the Denmark in 2016 was \$60K. The Bottom 50% share was 20%, the top 10% share was 30% and the top 1% share was 10%. What is the average income of each group? (2 points)

Exercise 4: Global development (10 points)

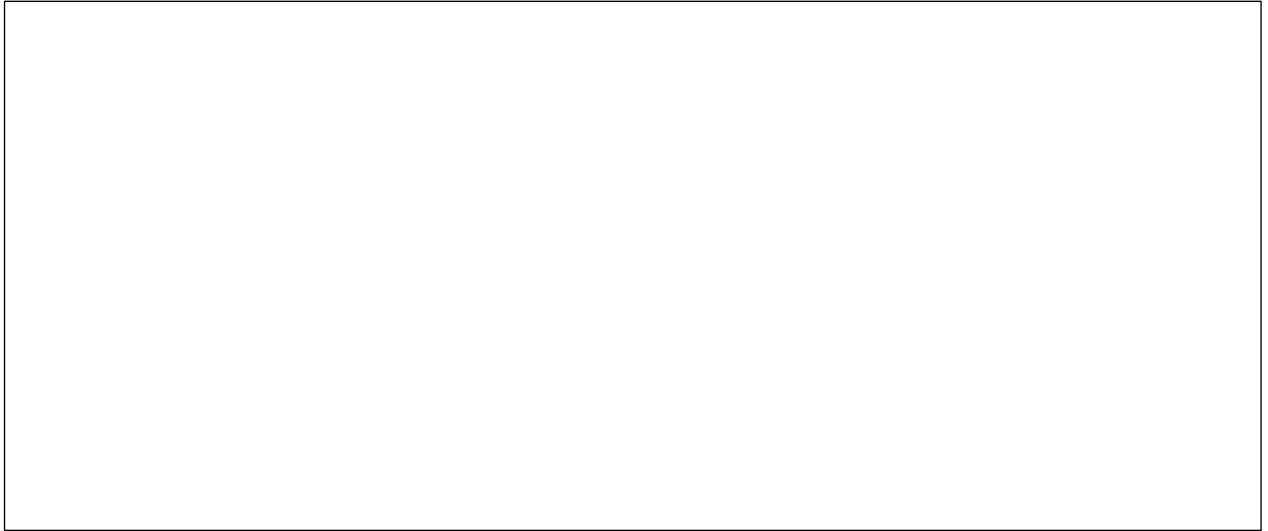
a) Have the last 30 years of fighting global poverty been a success? (1 point)



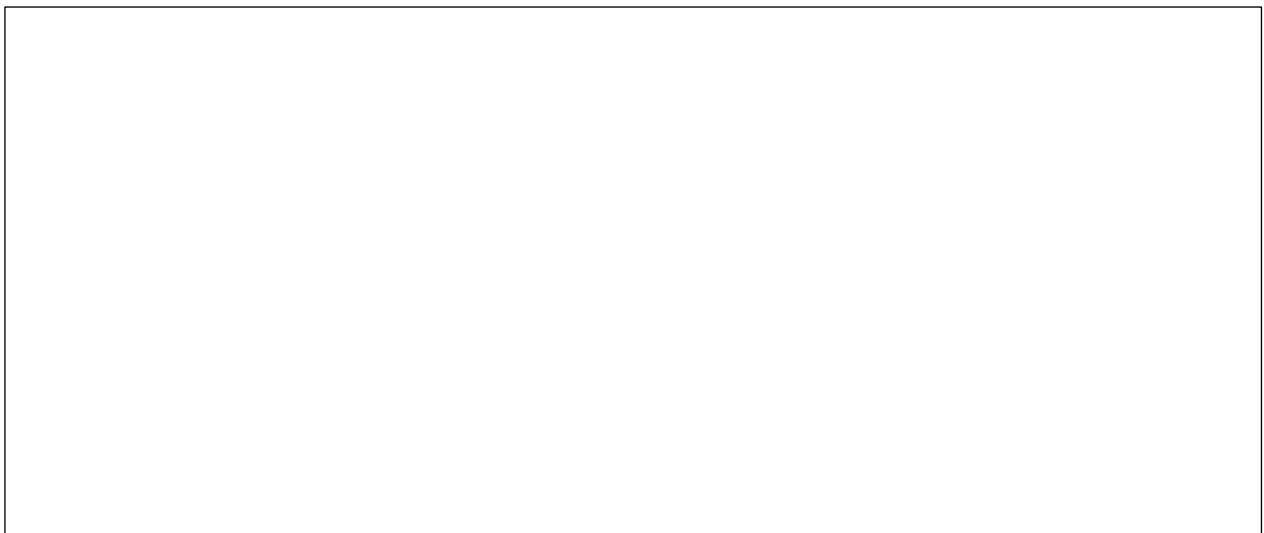
b) Where do the extremely poor live today compared to in 1980 – and how does that impact the role of development aid? (1 point)



c) *Opponents to development aid often cite cross-sectional analyses showing that countries receiving the most aid have experienced less economic growth than countries receiving little aid. Please comment on this. (1 point)*



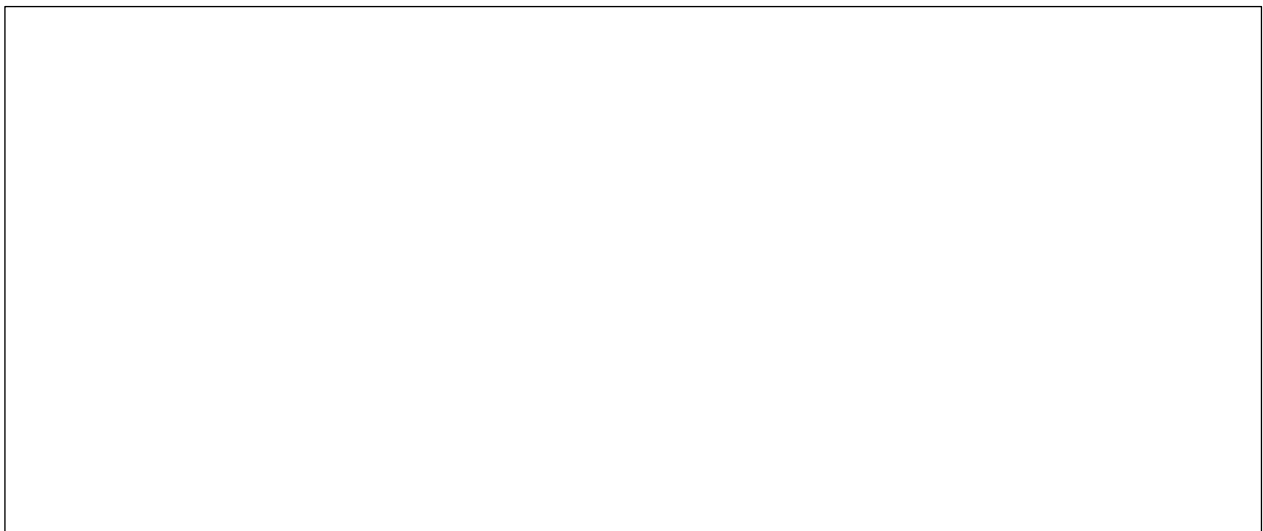
d) *Opponents to development aid also often argue that development aid foster corruption and weak institutions. How does that view align with the study “Does foreign aid harm political institutions” by Jones and Tarp (2015). (1 point)*



e) *What are the issues facing many developing countries when trying to collect additional tax revenue? What are the potential solutions? (2 points)*



f) *Page and Pande (2018) discuss building “invisible infrastructure” to fight poverty – what is that? (2 points)*



g) What should be the role of development aid in the future according to Page and Pande (2018)? (2 points)

