

Question 3

- a) Distinguish between economic efficiency and equity. How does the Hicks-Kaldor test differ from the Scitovsky Double test?
[8 marks]
- b) Using a suitable example, describe the Coarse Theorem and explain the limitations of this theorem.
[11 marks]

Question 4

Discuss the six phases in project evaluation

[25 marks]

Question 5

- a) Explain the Arrow-Lind Theorem. What are the limitations of this theorem?
[12 marks]
- b) With the aid of a diagram, explain the welfare effects of a per unit tax aimed at reducing the impact of a negative externality in production.
[13 marks]

SECTION A (COMPULSORY)

Question 1

a) With the aid of examples, write short notes on the efficacy of shadow prices.

[12marks]

b) Give an example of a negative externality in consumption and with the aid of a diagram, demonstrate how taxation could be used to alleviate its impact on society.

[13 marks]

c) Suppose a project is considered by a single person and the outcomes 1 and 2 have probabilities $P_1 = 0.6$ and $P_2 = 0.4$ with pay offs $Y_1 = + 50$ $Y_2 = - 20$. Suppose the person begins with assets of 100 and the Certainty equivalent = 102. Calculate the cost of risk bearing and compare to the case where there are two people in the project sharing the gains and losses equally and the second person has the same utility function as the first one. Now suppose the pay offs for each individual are +25 and -10 and each individual has initial assets of 100. Given the new certainty equivalence of 103 determine the cost of risk bearing. Use the results from this example to explain the concept of risk spreading.

[15 marks]

SECTION B (ANSWER ANY TWO QUESTIONS)

Question 2

a) Explain the conditions necessary for success in risk-pooling.

[5 marks]

With the aid of a suitable example, demonstrate how a Pareto efficient outcome can be realized through voluntary bargaining in the allocation of a contestable resource. Discuss the merits and demerits of the concept juxtapose alternatives.

[20 marks]

**UNIVERSITY OF SWAZILAND
FINAL EXAMINATION PAPER, 2014**

TITLE OF PAPER : PROJECT EVALUATION

COURSE CODE : ECON 309

TIME ALLOWED : THREE (3) HOURS

**INSTRUCTIONS : ANSWER THREE QUESTIONS:
QUESTION 1 AND TWO OTHER
QUESTIONS**

**DO NOT OPEN THIS PAPER UNTIL PERMISSION HAS BEEN
GRANTED BY THE INVIGILATOR.**