Wilf Csaplar Jr.   Economics 113   Homework #2   **Due Tuesday 9/5 by 9:30 AM**

Place your name on the back of this sheet of paper and nowhere else. Staple your answers face up on the front of this sheet of paper. Failure to follow these directions will cost you 10 points. Your assignment will be typed, except graphs can be drawn by hand and mathematical equations can be done by hand. Failure to type it will cost you 10 points. If you use double-sided printing or print on the back of scrap paper, I will give you one additional point.

1) (20 points) The article below, goes through the reasons why Fitch and S & P have both downgraded the US government debt. There are multiple references to debt ceiling crises. If the government defaults on its debt, it can have a major negative impact on the economy in both the short-run and the long-run. Why would politicians on both sides risk that repeatedly? How does that relate to the *principal-agent problem*? Explain how their actions are explained by the *principal-agent problem*?   https://www.thetelegraph.com/news/article/us-losing-fitch-s-top-aaa-credit-rating-may-18289123.php

2) (15 points) Define the *moral hazard* problem. Give an example from insurance. Explain how it leads to inefficient production.

3) (20 points) Draw a PPF for hats and cars. Illustrate a static improvement in efficiency. Explain why the graph changed as drawn.

4) (15 points) Often improving one outcome will cause another outcome to deteriorate. Explain how an improvement on the outcome of *income distribution* can cause a deterioration of the outcome of *economic growth*.

5) (15 points) Question #4 illustrates a problem. How do we weight the different outcomes when determining whether a country is improving or not? In other words, why might we not want equal weights when calculating the average? What is the problem with using unequal weights? Explain your logic.

6) (15 points) I added *environmental sustainability* to the list of desirable outcomes. Why is that an important outcome?