

Microeconomic and Environmental Policies

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Multiple Choice

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|----------|---|-----------|---|-----------|---|-----------|---|
| 1 | A | 6 | B | 11 | A | 16 | C |
| 2 | C | 7 | A | 12 | A | 17 | B |
| 3 | B | 8 | C | 13 | C | 18 | A |
| 4 | B | 9 | C | 14 | B | 19 | D |
| 5 | D | 10 | B | 15 | B | 20 | D |

Short Answers

Question 1

- (a) Productivity refers to the quantity of goods and services that can be produced for a given level of production inputs, such as labour and capital, over a given period of time.
- (b) Productivity and economic growth have a strong long-term relationship. If an economy can achieve sustained productivity growth, it means that over time, it is able to produce more goods and services from available inputs. Therefore, assuming the level of inputs to production remains constant or increases, the economy produce more goods and services than in previous years, and therefore achieve a higher level of economic growth. Without productivity growth, an economy must rely solely on growth through increased population and workforce participation.
- (c) Economists believe that the long-term impact of the extensive range of microeconomic reforms enacted since the 1980s has been a stronger and more sustained rate of economic growth. Australia achieved rising productivity growth in the 1981-82 to 1998-99 period, with record average labour productivity growth of 3.8 per cent in 1993-94 to 1998-99, following the implementation of a wide range of microeconomic reforms including deregulation of the financial sector and the labour market, trade liberalisation, privatisation of government enterprises and the introduction of competition laws. As the pace of microeconomic reform slowed since the late 1990s, with fewer large-scale reforms being implemented, the level of productivity growth has fallen, with the 2003-04 to 2007-08 period recording weak growth, with labour productivity growth falling to 1.6 per cent.
- (d) To the extent that microeconomic reforms can continue to result in an improvement in dynamic efficiency, technical efficiency and allocative efficiency, they should contribute to an increase in aggregate demand and a lift in productivity growth in the economy. However, most economists believe that further waves of microeconomic reform will have less impact on productivity than previous reforms, because Australia already has a relatively open economy with limited barriers to competition. Economic reports have pointed to the potential for future productivity growth from lifting workforce skills, improving the delivery of government services and streamlining regulations between states through the Council of Australian Governments (COAG) reform process. Achieving agreement on these reforms has proved difficult because of opposition by some state governments.

Question 2

- (a) Microeconomic reform refers to policies that are aimed to improve the efficient and productivity of individual industries, in order to increase aggregate supply in an economy.
- (b) Microeconomic reform aims to increase aggregate supply in an economy by increasing the level of productivity through improving technical efficiency, dynamic efficiency and allocative efficiency. By lifting the rate of productivity growth, an economy can produce more output for the same amount of inputs, and can therefore increase aggregate supply. Improvements in efficiency in a particular market lower the costs of production (improving technical efficiency), ensure resources go to the most productive areas of an economy (allocative efficiency) and improve the speed with which the economy responds to changing market conditions (dynamic efficiency). The cumulative effect of microeconomic reform across industries and markets increases aggregate supply in the economy.
- (c) One cost of microeconomic reform is an increase in structural unemployment in the short term, as resources shift away from some industries and regions, to parts of the economy where those resources can be more efficiently allocated. A second cost of microeconomic reform is that many reforms require an increase in spending by the government to enable those reforms (for example, to assist industries with restructuring or to help re-train employees in industries where jobs are being reduced). A third cost of some microeconomic reforms is an increase in income inequality, when market forces have a greater influence on economic outcomes such as through decentralised wage determination.
- (d) Microeconomic reform can reduce the level of inflation over time, by increasing the level of competition and reducing tariffs on imported goods. Such reforms should reduce consumer prices in the short term and the long-term, as a more competitive market structure results in slower price increases. This has occurred in Australia's passenger motor vehicle market during the past two decades as tariffs have largely been phased out. Micro reform can also reduce inflationary pressures by encouraging increased productivity. For example, the introduction of a national system of occupational health and safety laws allows businesses to adopt consistent practices across the country, reducing the costs of complying with separate rules in every state and reducing the amount of time required for training staff in those different laws. This should flow into higher productivity and contribute to lower inflation.

Question 3

- (a) Market based environmental management policy refers to the use of financial incentives and disincentives such as taxes and subsidies, to influence the economic behaviour of households and businesses.
- (b) The Fuel Quality Standards Act implemented in 2000 regulates the quality of fuel consumed in Australia. The aim of the legislation is to reduce the levels of pollutants and emissions from fuel, which may cause environmental and associated health problems. Such regulation governs the economic behaviour of the firms producing and selling fuel in Australia, by prohibiting environmentally-damaging practices and promoting environmental sustainability.
- (c) International agreements such as the 1987 Montreal Protocol, dedicated to eliminating use of ozone-depleting products, may be more effective in addressing environmental concerns due to the need for global cooperation in promoting environmental sustainability. Because most features of the natural environment such as air quality, carbon dioxide levels, water sources and oceans are affected by the actions of all countries, individual nations cannot successfully address global environmental problems by themselves. Instead, it is necessary for nations to come together and agree on common action to address environmental problems. Individual nations are often hesitant to impose strict environmental management policies on their own, if other nations are not willing to do the same.
- (d) Market-based policies have a significant role in improving Australia's environmental sustainability. For example, the government imposes a tax equal to 38 cents per litre on unleaded petrol. This should have the effect of 'internalising the externality' because it makes consumers and producers pay for some of the environmental costs of using petrol (including greenhouse gas emissions, congestion and pollution). The carbon tax introduced in 2012 is another example of a market-based policy that gives the industries that make the largest contribution to Australia's carbon emissions a financial incentive to reduce those emissions. The effectiveness of this approach has been widely debated, with some critics arguing that compensation for some carbon-emitting industries has been too generous, while others argue the tax will have little impact without a global agreement on reducing carbon emissions.