



ECONOMICS

Higher Level

Monday 17 May 1999 (afternoon)

Paper 1

1 hour

This examination paper consists of 40 questions.

Each question offers 4 suggested answers.

The maximum mark for this paper is 40.

INSTRUCTIONS TO CANDIDATES

Do NOT open this examination paper until instructed to do so.

Answer ALL the questions.

For each question, choose the answer you consider to be the best from the 4 answers given.
Indicate your choice on the answer sheet provided.

EXAMINATION MATERIALS

Required:

Optically Mark Read (OMR) answer sheet

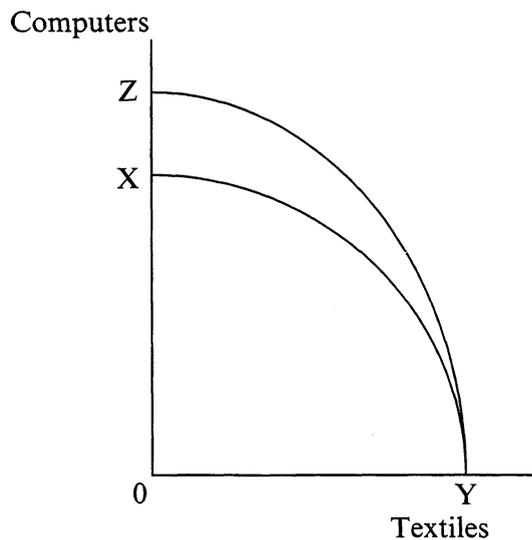
Allowed:

A simple translating dictionary for candidates not working in their own language

Calculator

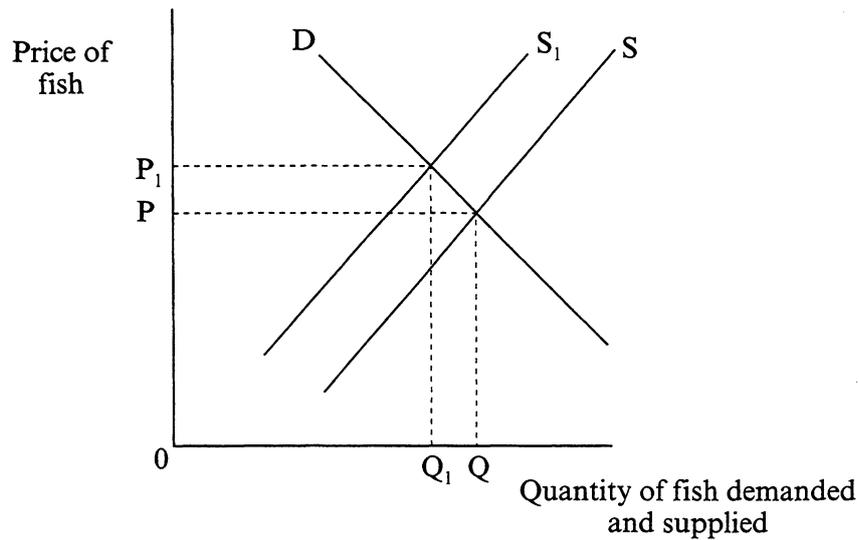
1. Economics is primarily concerned with the question of how
 - A. limited human wants may be satisfied through the use of limited resources.
 - B. unlimited factors of production can be best allocated for different uses.
 - C. limited government funds should be used to achieve specific social and political goals.
 - D. unlimited human wants can be satisfied using limited productive resources.

2. The diagram below depicts two production possibility curves YX and YZ.



- The shift of the curve from YX to YZ could have been caused by
- A. more resources being allocated to the production of computers.
 - B. labour shortages in the textile industry.
 - C. shifts in the pattern of demand as between computers and textiles.
 - D. improved technology in the computer industry.
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3. A basic difference between a centrally planned economy and a market economy is that in a planned economy
 - A. there is always an equal distribution of income and wealth.
 - B. factor and product markets are perfectly competitive.
 - C. resource allocation is achieved through directives rather than prices.
 - D. substantial subsidies are granted to private sector production.

4. The diagram below shows the market for fresh fish.



The shift of the supply curve from S to S_1 is most likely to have resulted from

- A. an increase in wages in the fishing industry.
 - B. improved technology in the fishing industry.
 - C. an increased preference for fish on behalf of consumers.
 - D. a fall in consumer incomes.
5. An increase in the price of good X causes a fall in the demand for good Y. This could be explained by
- I. X and Y being in joint demand.
 - II. good Y being an inferior good.
 - III. X and Y being substitutes.
- A. I only
 - B. I and II only
 - C. II and III only
 - D. I, II and III

6. A rise in house prices may be caused by a fall in
- I. interest rates.
 - II. house building.
 - III. the level of disposable incomes.
- A. I only
 - B. I and II only
 - C. II and III only
 - D. I, II and III
7. A parallel market for a product is most likely to arise as a result of
- A. the setting of a minimum price above the equilibrium.
 - B. a substantial shift of the demand curve to the right.
 - C. a sudden reduction in supply.
 - D. the imposition of a maximum price below the equilibrium.
8. Which of the following is a characteristic of a merit good?
- A. It could be provided by the free market, but not in sufficient quantities.
 - B. It is always provided free to consumers.
 - C. It tends to generate negative externalities, so governments restrict its consumption.
 - D. Once the good has been supplied to one consumer, there is no additional cost in supplying it to others.
9. A person's income rises from \$16 000 per year to \$20 000 per year. Subsequently, spending on clothes by this person rises from \$1000 to \$1500 per year. This person's income elasticity of demand for clothes is
- A. income elastic.
 - B. unit elastic.
 - C. income inelastic.
 - D. cross elastic.

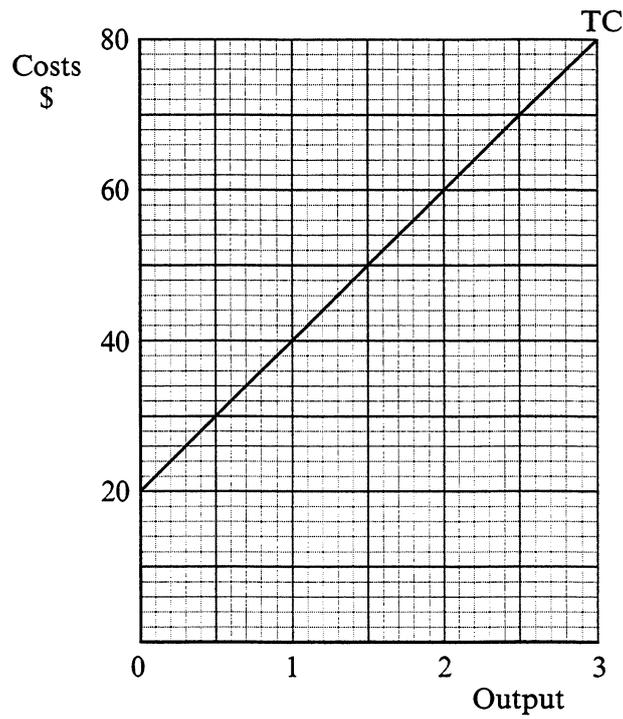
10. The following data represents the supply and demand schedules for a particular commodity over a given period of time.

Price per unit (£)	Quantity demanded	Quantity supplied
10	40	80
9	50	70
8	60	60
7	70	50
6	80	40

If a subsidy of £2 per unit was paid to producers of this commodity by the government, the new equilibrium price would be

- A. £9.
- B. £8.
- C. £7.
- D. £6.

11. The diagram below shows the total costs (TC) of producing good X.



Which of the following statements is/are correct?

- I. At an output of 3 units, average fixed costs are \$20.
 - II. At an output of 3 units, total variable costs are \$60.
 - III. The marginal cost of the third unit of output is \$20.
- A. I only
- B. I and II only
- C. II and III only
- D. I, II and III

12. The table below shows weekly output from Plant Z, using different factor input combinations.

PLANT Z

OUTPUT PER MONTH (TONS)

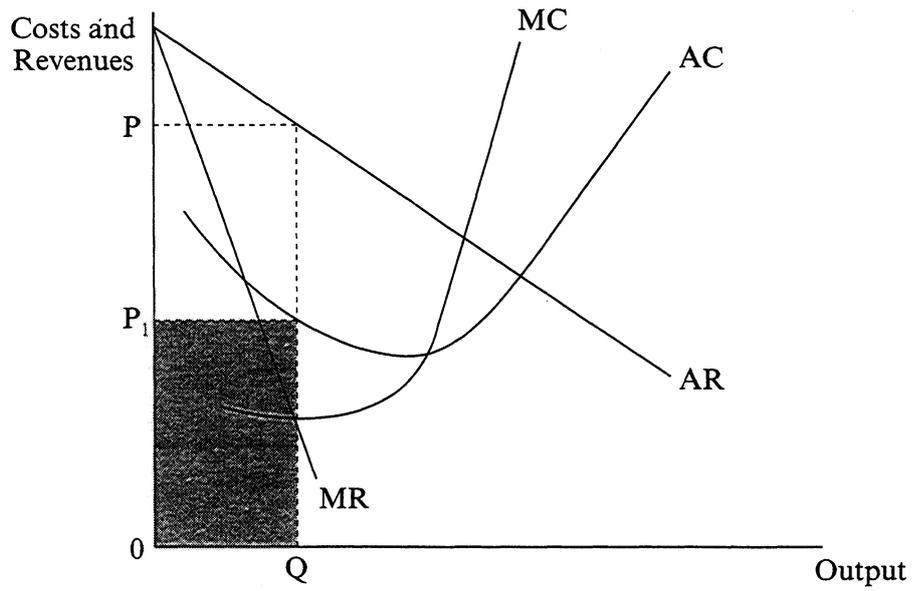
Units of Capital Input	3	66	126	180
	2	42	80	114
	1	20	38	54
		1	2	3

Units of Labour Input

It can be deduced from the data that Plant Z exhibits increasing returns to

- I. labour.
 - II. capital.
 - III. scale.
- A. I only
 - B. I and II only
 - C. II and III only
 - D. I, II and III
13. For a price discriminating monopoly to be **both** possible and profitable, it is necessary that
- A. average cost equals average revenue.
 - B. two or more markets with different demand elasticities can be separated.
 - C. the monopolist is achieving economies of scale.
 - D. demand for the product is relatively inelastic.

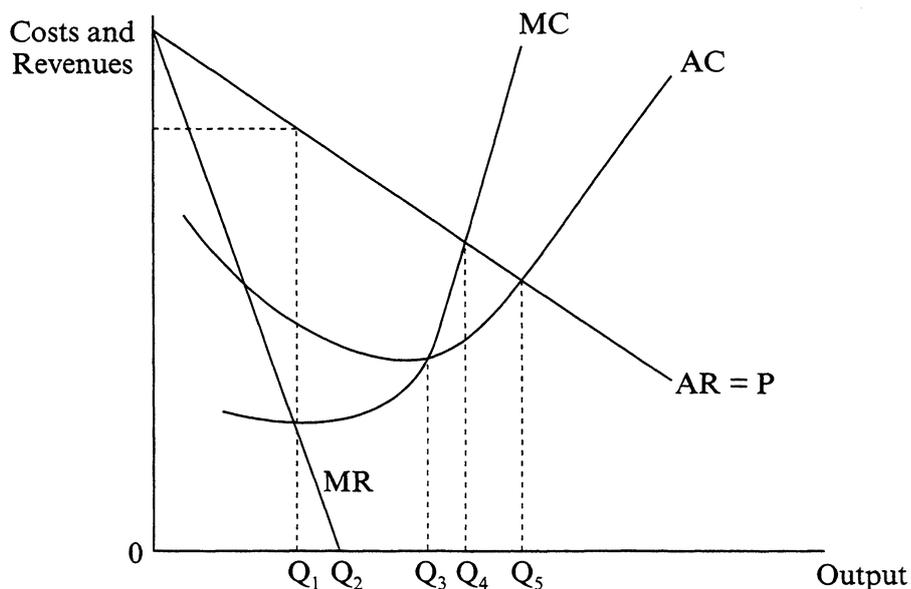
14. The diagram below shows the cost and revenue curves of a firm.



The shaded area of the diagram could represent

- A. normal profits in imperfect competition.
- B. monopoly costs.
- C. oligopoly profits.
- D. abnormal profits.

15. The diagram below shows the cost and revenue curves of a monopolist.



The objective of the firm changes from profit maximisation to sales revenue maximisation. As a result, the firm's output would change from

- A. $0Q_1$ to $0Q_2$.
- B. $0Q_1$ to $0Q_3$.
- C. $0Q_3$ to $0Q_4$.
- D. $0Q_4$ to $0Q_5$.

16. The table below provides details of the costs and benefits of hospital beds.

Number of Hospital beds	Marginal Private Benefit (£M)	Marginal External Benefit (£M)	Marginal Social Cost (£M)
1000	30	33	14
2000	20	25	18
3000	8	17	25
4000	3	9	31

The socially efficient quantity of hospital beds is

- A. 1000 beds.
- B. 2000 beds.
- C. 3000 beds.
- D. 4000 beds.

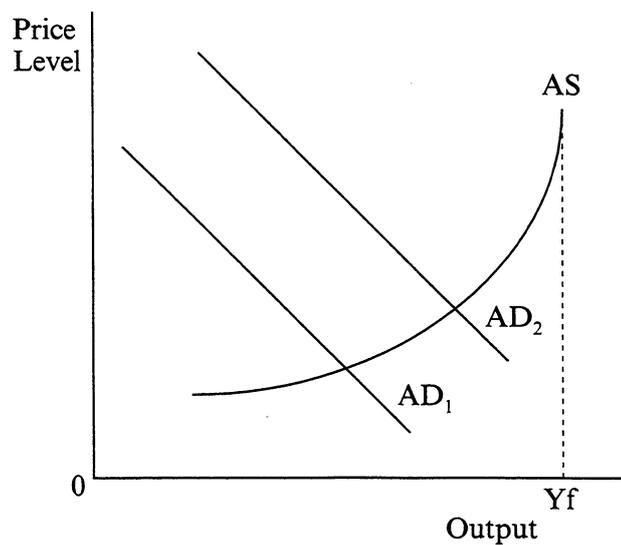
17. The following table relates to an economy in a particular year.

	£ million
GDP at market prices	400
Net property income from abroad	30
Indirect taxes	20
Subsidies	10
Depreciation	50

What is net national product at factor cost?

- A. £510 million
- B. £370 million
- C. £310 million
- D. £290 million

18. The diagram below illustrates the aggregate demand and supply curves for an economy, and Y_f represents the full employment level of output.

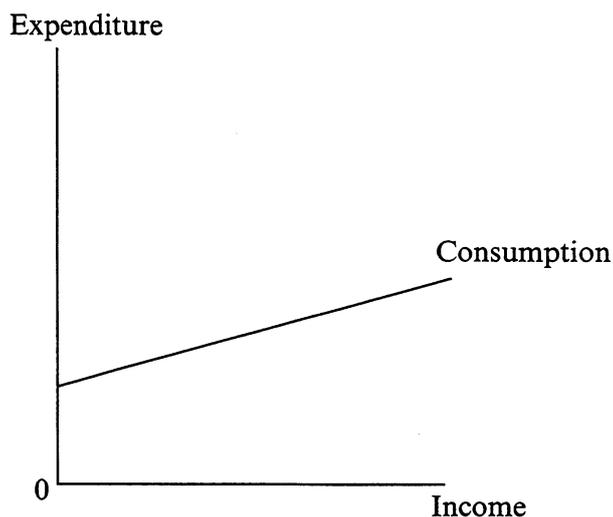


The shift of the aggregate demand curve from AD_1 to AD_2 will increase

- I. employment.
 - II. output.
 - III. prices.
- A. I only
 - B. I and II only
 - C. II and III only
 - D. I, II and III

19. The accelerator principle relates a change in investment to a change in the rate of growth of
- A. interest rates.
 - B. prices.
 - C. profits.
 - D. gross domestic product.

20. The diagram below shows a straight line consumption function.

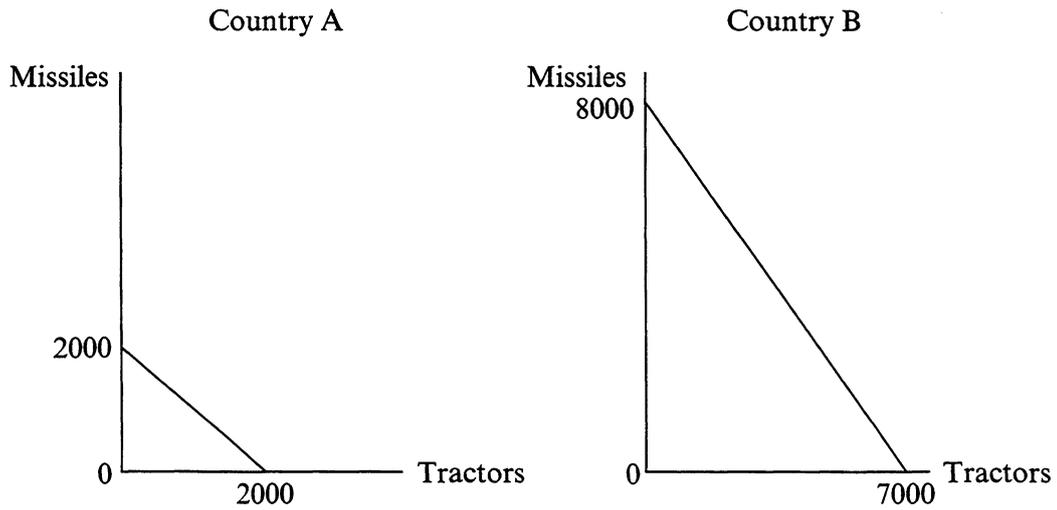


It can be deduced from the diagram that

- I. the marginal propensity to consume will remain constant as income rises.
 - II. saving will be negative at low levels of income.
 - III. the average propensity to consume will fall as income rises.
- A. I only
 - B. I and II only
 - C. II and III only
 - D. I, II and III

21. Which of these problems is most likely to improve after a cut in personal income tax rates?
- A. Demand inflation
 - B. Unemployment
 - C. The budget deficit
 - D. Balance of payments deficit
22. Which of the following statements might represent the view of a monetarist economist?
- I. In the long run, an increase in government spending, financed by an increase in the PSBR, will be unsuccessful in reducing unemployment below its natural rate.
 - II. Budgeting for a deficit is an effective way of reducing unemployment.
 - III. Inflation is always and everywhere caused by cost push factors.
- A. I only
 - B. I and II only
 - C. II and III only
 - D. I, II and III
23. Increased borrowing by the government results in the private sector being able to borrow less. This would be an example of
- A. diminishing credit worthiness.
 - B. the multiplier effect.
 - C. crowding out.
 - D. fiscal drag.
24. The use by the government of a high interest rate policy as a counter inflationary device is based on the assumption that one of its effects will be to increase the
- A. cost of borrowing for private businesses.
 - B. interest repayments on the national debt.
 - C. level of investment.
 - D. external exchange rate.

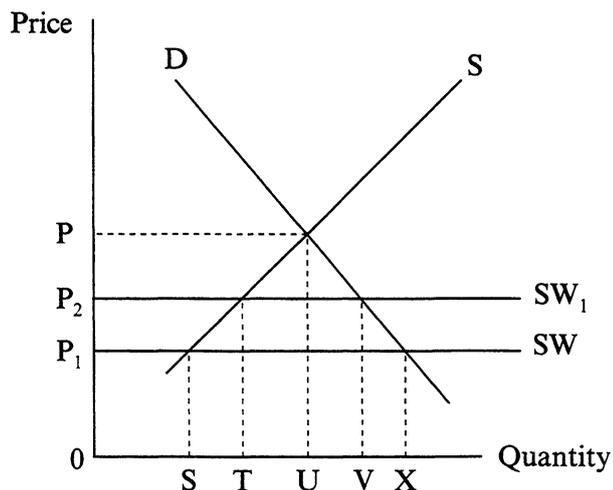
25. The diagrams below indicate the production possibility frontiers for two countries, A and B.



From the diagrams it can be concluded that country A has

- A. a comparative advantage in both lines of production, and so will not trade.
 - B. a comparative advantage in the production of tractors only.
 - C. an absolute advantage in the production of both products.
 - D. a comparative advantage in the production of missiles.
26. The objectives of the World Trade Organisation include
- I. the elimination of existing barriers to trade.
 - II. the establishment of fixed exchange rates.
 - III. the supply of international liquidity.
- A. I only
 - B. I and II only
 - C. II and III only
 - D. I, II and III

27. The diagram below shows the market for good Y.



OP is the price of good Y before trade and S is the domestic supply curve. OP_1 is the price of good Y resulting from free trade and SW represents the world supply curve. The imposition of a tariff on good Y brings about a price of OP_2 .

This tariff will reduce imports of good Y by

- A. ST and VX .
 - B. ST and UV .
 - C. SU .
 - D. UX .
28. Which of the following, in principle, represents a difference between a customs union and a free trade area? A customs union
- A. always has fixed exchange rates among its members.
 - B. uses a single currency for trade within the area.
 - C. imposes a common external tariff on goods imported from outside the union.
 - D. establishes tariff-free trade between member countries.

29. Which of the following describe expenditure switching as opposed to expenditure reducing?
- I. A fall in the rate of inflation making domestically produced goods more competitive in comparison to imports
 - II. An increase in the demand for exports resulting from relatively lower export prices
 - III. Economic recession leading to less demand for imported consumer goods, raw materials and capital goods
- A. I only
 - B. I and II only
 - C. II and III only
 - D. I, II and III

30. The table below indicates alternative price elasticities of demand for the imports and exports of country Y.

Combination (x + m)	Exports (x)	Imports (m)
A.	0.4	0.6
B.	0.5	0.3
C.	0.9	1.1
D.	1.5	1.5

Following a depreciation of the external exchange rate of country Y, other things being equal, which combination of price elasticities would be most likely to bring about an improvement in the balance of payments on current account?

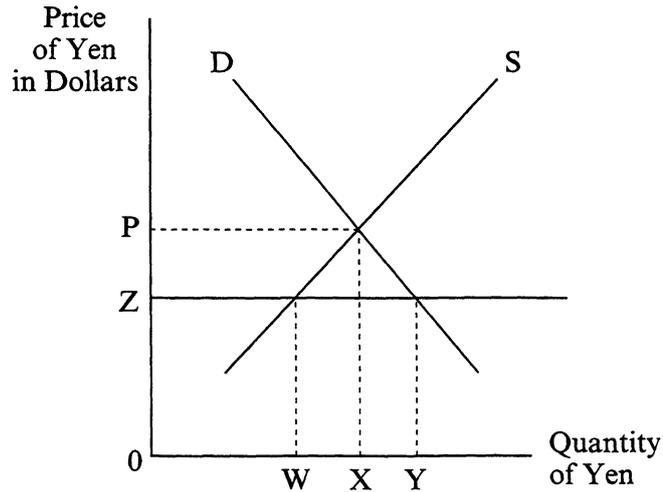
31. The following table shows the relationship between import and export prices for a country.

Index of Export Prices		Index of Import Prices	
Year 1	Year 2	Year 1	Year 2
100	110	100	80

What is the terms of trade index in Year 2?

- A. 190
- B. 137.5
- C. 72.7
- D. 1.375

32. The diagram below shows the determination of the exchange rate of the Yen.

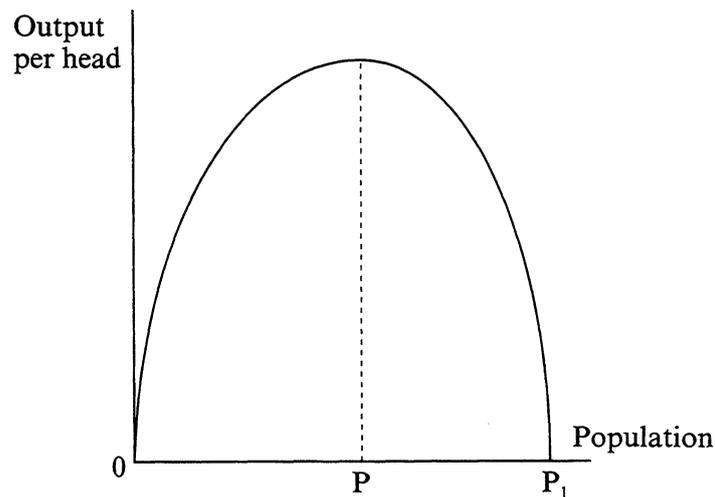


If the central bank of Japan wished to intervene in the free market to maintain an exchange rate of 0Z it should

- A. buy WY Yen.
 - B. buy WX Yen.
 - C. sell WY Yen.
 - D. sell WX Yen.
33. Many Less Developed Countries have specialised historically in the production of primary products for export. A number of problems have arisen from this pattern of specialisation. Which **one** of the following does **not** apply?
- A. Primary products have a high income elasticity of demand.
 - B. The world price of primary products is subject to greater fluctuations than that of manufactured products.
 - C. Relying on the export of primary products may lead to a long run deterioration in the terms of trade.
 - D. Technological progress is more rapid in the production of manufactured products than primary products.

34. A country has a Human Development Index of 0.94. This country is most likely to have
- A. a small proportion of its population engaged in the tertiary sector.
 - B. low levels of literacy.
 - C. a rapid rate of population growth.
 - D. a high level of life expectancy.

35. The diagram below relates output per head to population size, with given resource availability.



On the basis of this diagram, overpopulation occurs

- A. at 0P.
 - B. between points 0 and P.
 - C. only at $0P_1$.
 - D. between points P and P_1 .
36. For Less Developed Countries, appropriate technology may best be defined as that technology which
- A. provides the highest capital/labour ratio.
 - B. yields the greatest rate of return when social costs and benefits are taken into account.
 - C. provides the highest labour/capital ratio.
 - D. generates substantial economies of scale and cost minimisation.

37. The policy of import substituting industrialisation pursued by several Less Developed Countries has resulted in a variety of disadvantages. However, a **consequence** of such a policy is that it has
- A. caused exchange rates to be overvalued.
 - B. encouraged the establishment of monopolies.
 - C. led to less dependence on the export of primary commodities.
 - D. created a bias against the primary sector.
38. The World Bank normally makes loans to
- I. finance long term capital projects.
 - II. develop resources in Less Developed Countries.
 - III. finance short-term balance of payments deficits.
- A. I only
 - B. I and II only
 - C. II and III only
 - D. I, II and III
39. The IMF and the World Bank have imposed structural adjustment policies (SAPs) on Less Developed Countries with large debt repayment obligations. These SAP packages have usually been based upon
- A. Keynesian interventionist policies.
 - B. greater state direction of resources.
 - C. free market Monetarist policies.
 - D. a desire to eradicate poverty.
40. The extent of rural-urban migration in Less Developed Countries is most likely to be reduced if
- A. there is high income differential between the towns and rural areas.
 - B. the governments encourage a more equal distribution of land ownership.
 - C. there is a high degree of disguised unemployment in the countryside.
 - D. the costs of migration are low.