



**ECONOMICS
HIGHER LEVEL
PAPER 1**

Wednesday 10 May 2000 (afternoon)

1 hour

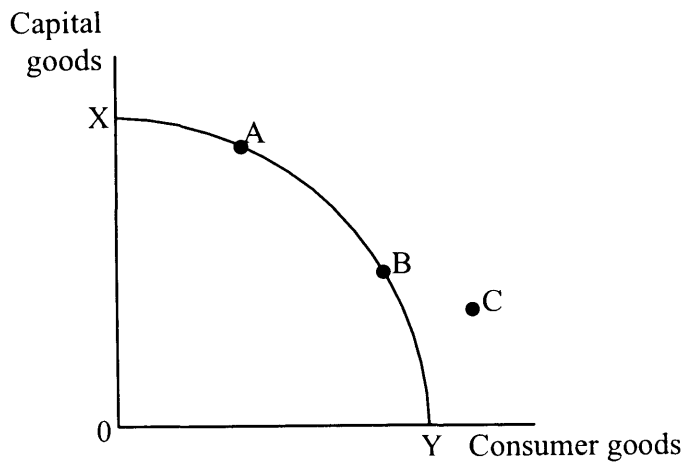
INSTRUCTIONS TO CANDIDATES

- 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 and indicate your choice on the answer sheet provided.

1. Choice is a central feature of economic behaviour because
 - A. people will always make rational choices.
 - B. consumers find it difficult to choose between various alternatives.
 - C. it is the main determinant of price.
 - D. resources are scarce relative to human wants.

2. Given the assumption of other things being equal, a law in economics may best be described as a
 - A. generalisation about the behaviour of economic agents.
 - B. positive statement concerning the technical relations of production.
 - C. mathematical forecast of a society's economic development.
 - D. behavioural relationship which will always occur.

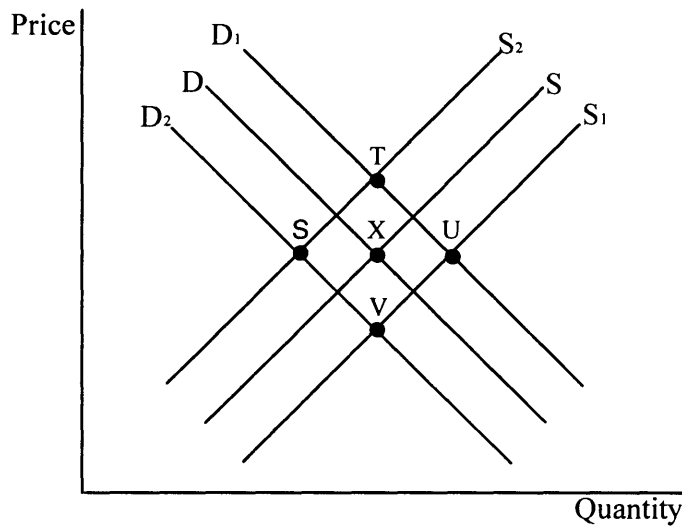
3. The diagram represents the production possibility frontier of a country.



Which **one** of the following statements is correct?

- A. In a free market economy, production would consist of 0X capital goods and 0Y consumer goods.
- B. Position C represents greater existing output of consumer goods relative to capital goods.
- C. Position A would create a larger potential future capacity than position B.
- D. Position A is more productively efficient than position B.

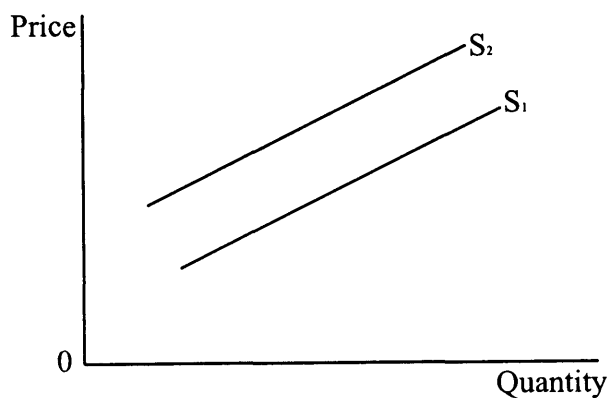
4. The diagram below indicates the demand for and supply of beef.



Given that point X is the initial equilibrium position, what would be the new equilibrium position following a health scare concerning the safety of beef consumption and a subsequent government policy of slaughtering cattle?

- A. Point S
- B. Point T
- C. Point U
- D. Point V

5. The diagram below shows two supply curves for a particular brand of soft drink.



The shift from S_1 to S_2 could have been caused by an increase in

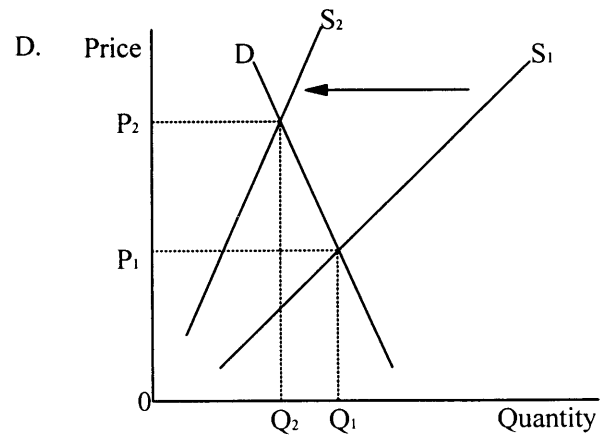
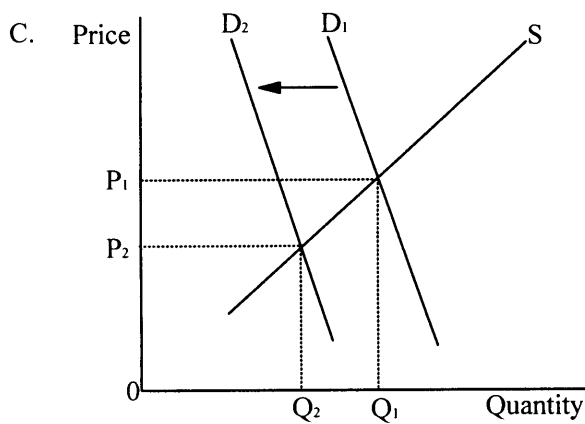
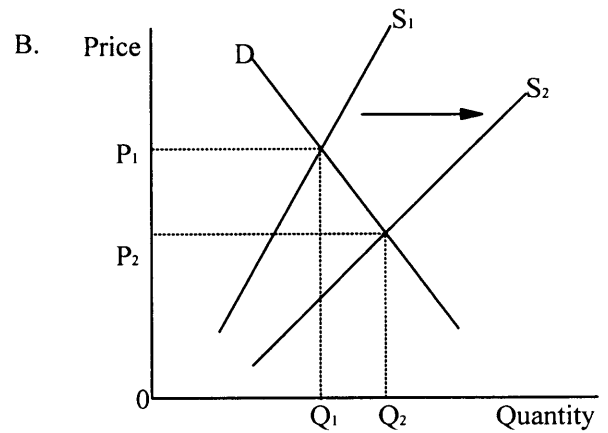
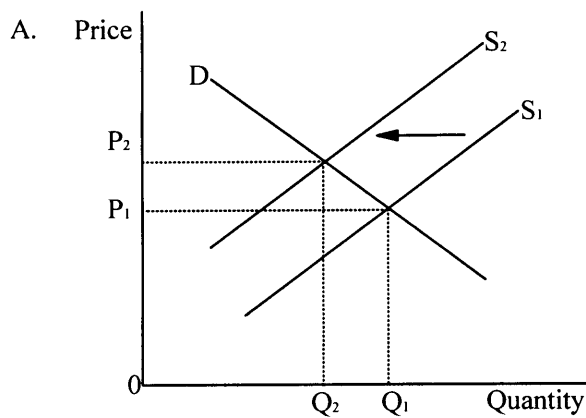
- I. the cost of raw materials.
 - II. government subsidies.
 - III. the level of real income.
- A. I only
 - B. I and II only
 - C. II and III only
 - D. I, II and III
6. Which **one** of the following statements that refer to the price system is **not** true?
- A. The consumer always has complete sovereignty in the market.
 - B. Factor mobility is a key requirement for resource re-allocation to occur.
 - C. High prices and profits tend to attract resources from less productive activities.
 - D. High prices ration scarce goods in accordance with effective demand by consumers.

7. Which **one** of the following does **not** apply to merit goods and services? They
- A. provide private and social benefits.
 - B. are limited in supply and require a system of allocation.
 - C. could be paid for by the consumer if a market system were allowed to operate.
 - D. have the characteristic of non-excludability.
8. A large chemical company is found guilty of polluting a nearby river. Which **one** of the following government measures would an economist describe as an appropriate market-based response?
- A. The imposition of regulations and direct controls on the company
 - B. Increased taxes on the chemicals produced
 - C. A reduction of private property rights over the river
 - D. Nationalisation of the chemical company
9. The cross elasticity of demand of good A with respect to good B is positive. The cross elasticity of demand of good B with respect to good C is negative. The income elasticity of demand of all three goods is positive. It therefore follows that
- I. A and B are substitutes.
 - II. B and C are complements.
 - III. A, B, and C are normal goods.
- A. I only
 - B. I and II only
 - C. II and III only
 - D. I, II and III

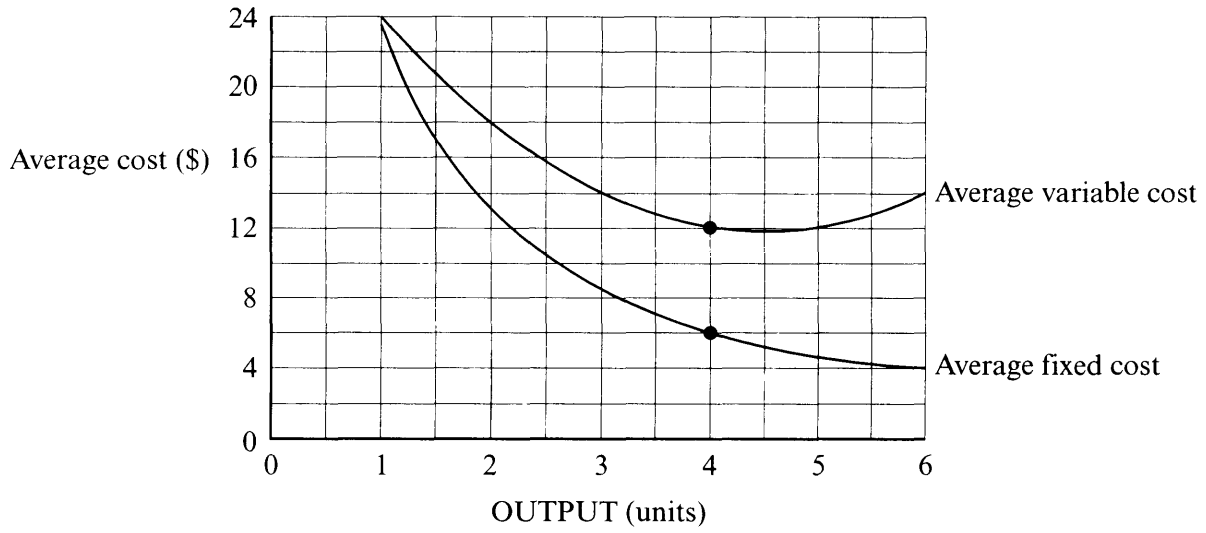
10. If the price elasticity of demand for a commodity is equal to one, a reduction in its price will lead to an increase in

- A. the seller's marginal revenue.
- B. the seller's total revenue.
- C. expenditure on substitutes.
- D. quantity demanded.

11. Which **one** of the following diagrams (A, B, C or D) illustrates the effect on the price and sales of petrol of an increase in an ad valorem tax?



12. The following diagram illustrates the costs of production of a firm.



The total cost of producing 4 units is

- A. \$12.
- B. \$24.
- C. \$48.
- D. \$72.

13. Company X is operating in long run equilibrium, and the following data is known about its cost and revenue structure.

$$\text{Marginal costs} = \$400$$

$$\text{Average costs} = \$500$$

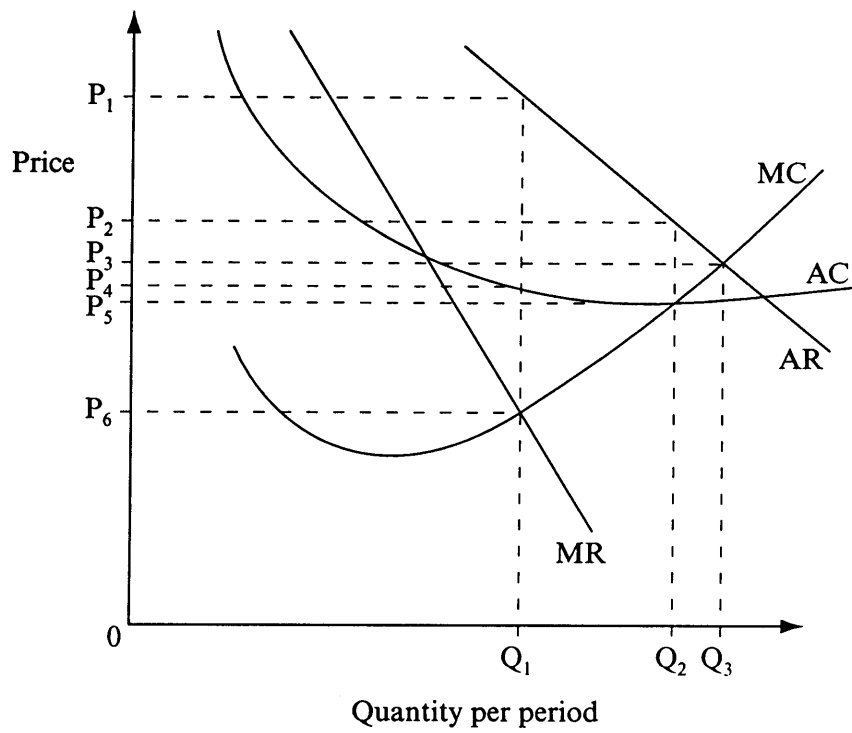
$$\text{Marginal revenue} = \$400$$

$$\text{Average revenue} = \$500$$

Company X could be operating under each of the following market conditions **except**

- A. oligopoly.
- B. monopolistic competition.
- C. monopoly.
- D. perfect competition.

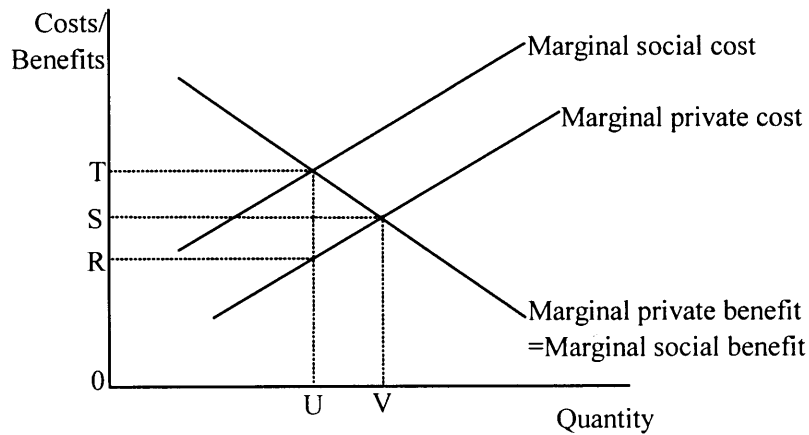
14. The diagram below represents a firm operating under conditions of monopoly.



The supernormal (economic) profits earned by this firm will be equal to $0Q_1$ multiplied by the difference between $0P_1$ and

- A. $0P_3$.
- B. $0P_4$.
- C. $0P_5$.
- D. $0P_6$.

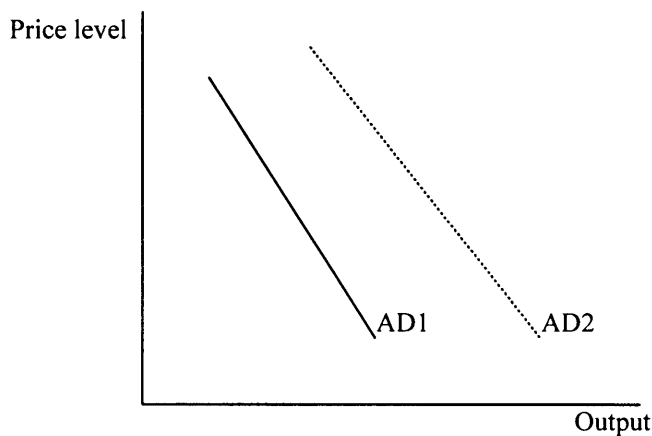
15. The diagram below indicates the market for a product which generates negative externalities.



To achieve an optimum allocation of resources from society's point of view requires

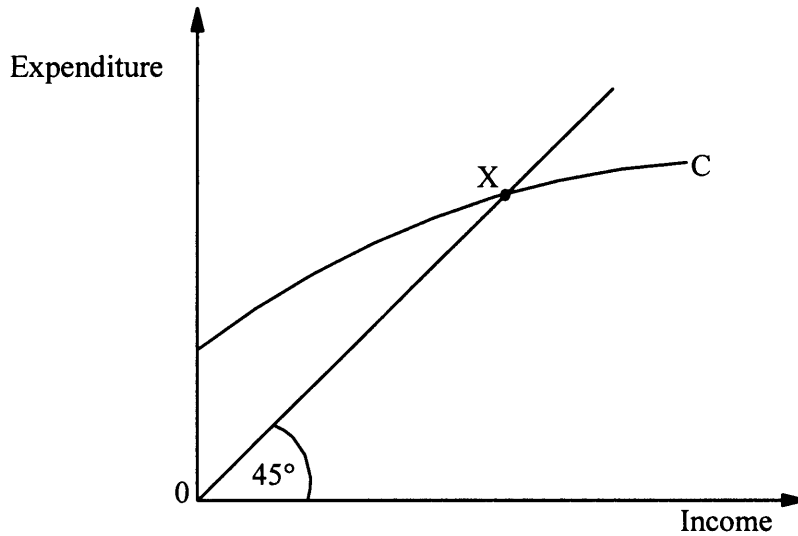
- A. a subsidy of RT and quantity of 0V.
 - B. a subsidy of RT and quantity of 0U.
 - C. a tax of ST and quantity of 0V.
 - D. a tax of RT and quantity of 0U.
16. Which **one** of the following is a necessary condition for a firm to practise price discrimination between two markets?
- A. Costs of production in each market must be different.
 - B. Consumers must be aware of price differences between the two markets.
 - C. Price elasticities of demand must be different in each market.
 - D. There must be no barriers between the markets.

17. Which **one** of the following represents a withdrawal from the circular flow of income?
- A. Private funding for a national arts centre
 - B. The extension, by the government, of the existing highway network
 - C. The commissioning of a domestic firm of consultant engineers by a foreign oil company to investigate suspected structural defects in some pipelines
 - D. The purchase by a domestic department store of designer clothes produced abroad
18. 'The total value of all the output produced within a country's geographical boundaries over a period of time.' This is a definition of
- A. Gross Domestic Product at market prices.
 - B. Net Domestic Product at factor cost.
 - C. Gross National Product at market prices.
 - D. Gross Domestic Fixed Capital Formation.
19. The diagram below shows two aggregate demand curves.



- Which **one** of the following is most likely to have caused the shift from AD1 to AD2?
- A. A reduction in interest rates
 - B. An increase in taxes
 - C. Lower government spending
 - D. Increased unemployment

20. In the diagram below, C is a consumption function.



Which **one** of the following statements is correct?

- A. The average propensity to consume is zero at point X.
 - B. The marginal propensity to consume rises as GNP rises.
 - C. The average propensity to save is equal to 1 at point X.
 - D. The marginal propensity to save rises as GNP rises.
21. The monetary policy being pursued by most governments is aimed at achieving higher levels of
- I. price stability.
 - II. government borrowing.
 - III. income equality.
- A. I only
 - B. I and II only
 - C. II and III only
 - D. I, II and III

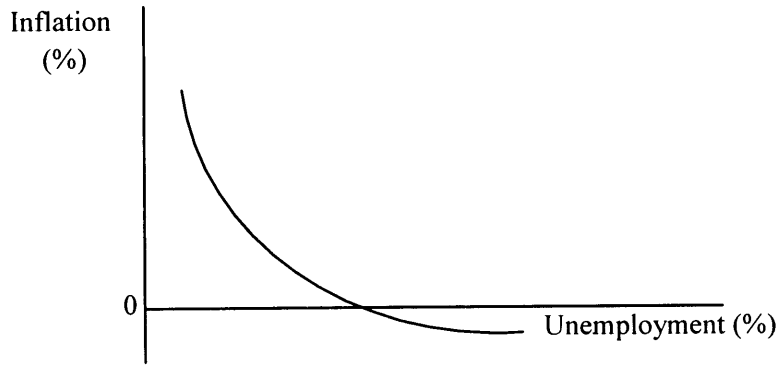
22. Using index numbers, the table below shows money wages and the price level in a certain economy.

	Money Wages	Price Level
Year 1	100	100
Year 2	120	110

From this information we can conclude that there has been an increase in real wages of

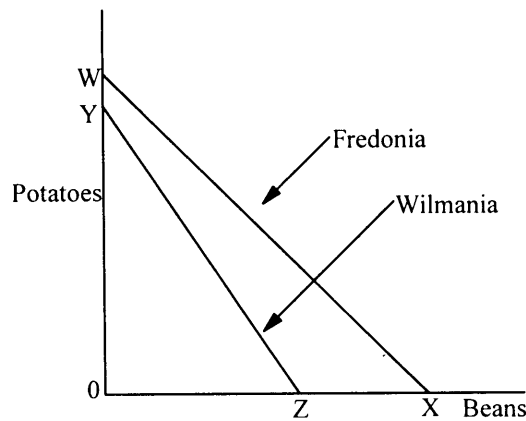
- A. just over 120%.
 - B. exactly 20%.
 - C. exactly 19%.
 - D. just over 9%.
23. A government wishes to reduce aggregate demand by increasing interest rates. This will have the effect of reducing
- A. industrial costs.
 - B. disposable income.
 - C. the external value of the domestic currency.
 - D. the propensity to save.

24. The diagram below shows a Phillips curve.



A diagram like this is generally used to show that

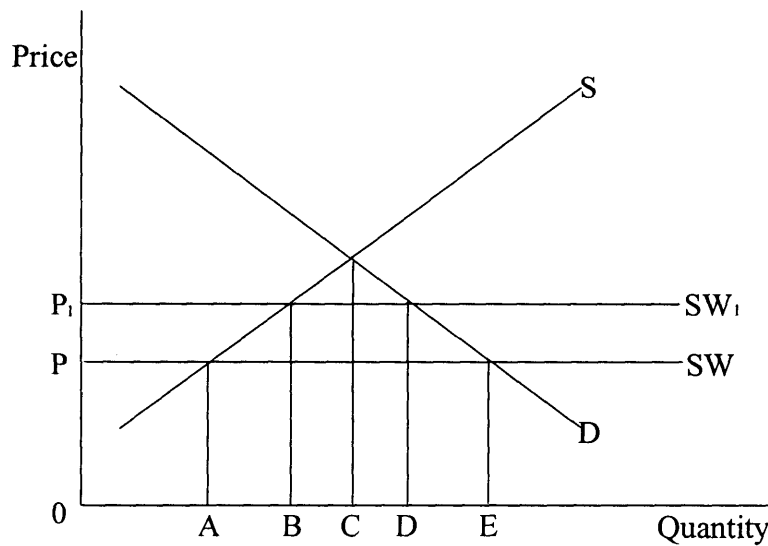
- A. it is impossible to reduce unemployment in the long run.
 - B. there is a 'trade-off' between inflation and unemployment in the short run.
 - C. unemployment may be negative, but inflation is always positive.
 - D. higher levels of unemployment result in higher levels of inflation.
25. In the diagram below WX is the production possibility frontier of one country, Fredonia, and YZ is the production possibility frontier for another, Wilmania.



According to international trade theory

- A. Wilmania has an absolute advantage in both potatoes and beans.
- B. Wilmania should export potatoes.
- C. Fredonia should export potatoes.
- D. no trade should take place.

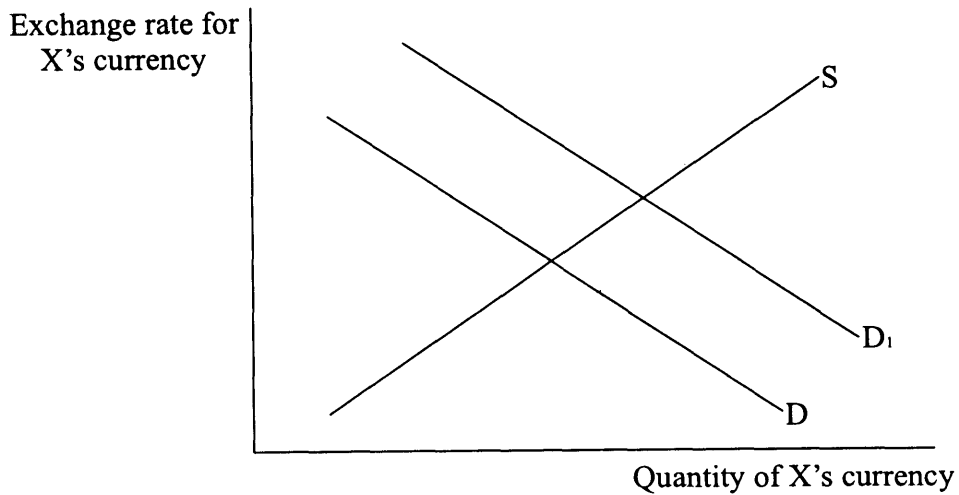
26. The diagram below shows the market for a good whose demand is met by both domestic production and world production at the world price P.



Subsequently, the country imposes a tariff on imports of the good, causing the domestic price to increase to OP_1 . The diagram shows that

- I. imports fall from AE to BD.
 - II. domestic demand increases from 0A to 0B.
 - III. domestic supply falls from 0E to 0D.
- A. I only
 - B. I and II only
 - C. II and III only
 - D. I, II and III
27. Which **one** of the following transactions would be recorded in the balance of payments accounts as a positive item for Alba, but a negative item for Bayona?
- A. An oil company from Alba develops an oil field in Bayona.
 - B. Oil executives from Alba stay in hotels in Bayona.
 - C. Petrol (gasoline) from a refinery in Alba is sold in Bayona.
 - D. Petrol (gasoline) from Alba is taxed by the Bayona government.

28. The diagram below shows the demand for and supply of the currency of Country X in international money markets.

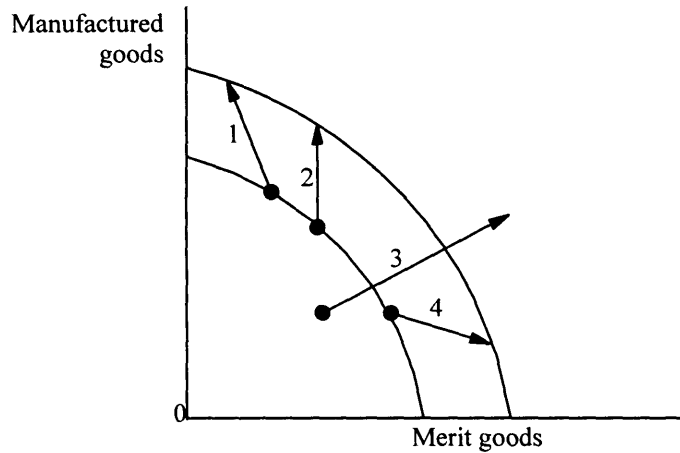


Other things being equal, a shift from D to D₁ would be the result of

- A. a deficit in the current account of the balance of payments of Country X.
 - B. an increase in Country X's inflation.
 - C. an inflow of foreign investment into Country X.
 - D. a reduction in Country X's interest rates.
29. A country could offset a downward movement in its exchange rate by
- A. the sale of domestic currency by the Central Bank.
 - B. increasing interest rates.
 - C. increasing its foreign exchange reserves.
 - D. reducing import taxes.

30. A loaf of bread costs 4 Gondomar pesos in Gondomar, and 5 Monforte dollars in Monforte. If bread is typical of all other goods, the idea of 'purchasing power parity' suggests that 1 Gondomar peso will exchange for how many Monforte dollars?
- A. 0.8
 - B. 1.0
 - C. 1.25
 - D. 4.5
31. Participation by a group of countries in a common currency means that for an individual country
- I. the possibility of restoring competitiveness by means of devaluation would be lost.
 - II. control over monetary policy would be lost.
 - III. foreign exchange dealing costs would be eliminated for trade within the zone of the currency.
- A. I only
 - B. I and II only
 - C. II and III only
 - D. I, II and III
32. A deterioration in the terms of trade means
- A. a fall in the average price of exports relative to the average price of imports.
 - B. a fall in the average price of raw materials relative to the average price of manufactured goods.
 - C. a higher volume of imports relative to the volume of exports.
 - D. a fall in the average price of imports relative to the average price of exports.

33. The following diagram shows two production possibility frontiers for the same country at different points in time.



- Which **one** of the four lines shows that growth **and** development have occurred over time?
- A. 1
 - B. 2
 - C. 3
 - D. 4
34. A major difference between the Human Development Index (HDI) and the Human Poverty Index (HPI) is that the HDI
- A. measures progress towards target indicator levels, the HPI measures relative deprivation.
 - B. reflects income inequality, the HPI measures income equality.
 - C. is more accurate for high and middle income countries, the HPI is more accurate for low income countries.
 - D. measures relative poverty, the HPI measures absolute poverty.

35. How might a Less Developed Country best try to prevent ‘capital flight’?
- A. Remove controls on the movement of capital between countries.
 - B. Allow the exchange rate to depreciate.
 - C. Lower domestic interest rates.
 - D. Build up investor confidence in local capital markets.
36. The government of a Less Developed Country awards scholarships for able students to study Economics at university. This represents
- A. capital broadening.
 - B. investment in social capital.
 - C. investment in human capital.
 - D. social returns to scale.
37. Multilateral aid is best defined as aid which
- A. is used for many different purposes in the country which receives the aid.
 - B. comes from a non-governmental organisation.
 - C. is used to both widen and deepen capital-labour ratios.
 - D. comes indirectly from several donor countries through a body such as the United Nations.
38. Which **one** of the following is **least** likely to contribute to a worsening of the debt problems of many Less Developed Countries?
- A. Loans made with variable rates of interest
 - B. An appreciation of the dollar against debtor countries’ currencies
 - C. A worsening of the terms of trade for debtor countries
 - D. The adoption of IMF Structural Adjustment Programmes

39. Less Developed Countries (LDCs) are more open to environmental exploitation than More Developed Countries (MDCs) because
- A. ownership rights are less well established in LDCs than in MDCs.
 - B. the MDCs have exhausted their factor endowment.
 - C. market failure is less in the early stages of development.
 - D. wages are lower in LDCs.
40. Sustainable development is concerned with development which
- A. meets the needs of the present and future generations.
 - B. sustains existing growth and consumption patterns.
 - C. favours 'appropriate technology' methods of production.
 - D. promotes agricultural growth so as to sustain food production.
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