

**ECONOMICS
HIGHER LEVEL
PAPER 1**

Thursday 6 November 2003 (afternoon)

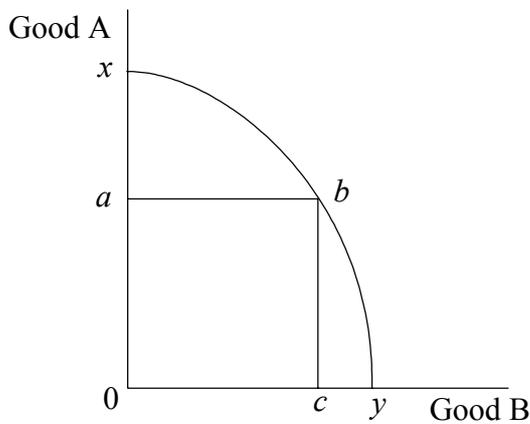
1 hour

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. The basic economic problem is
 - A. whether to produce consumption or investment goods.
 - B. how to distribute income equally.
 - C. what goods to produce, how to produce them and how to allocate them.
 - D. how to enable the market system to produce with the greatest efficiency.

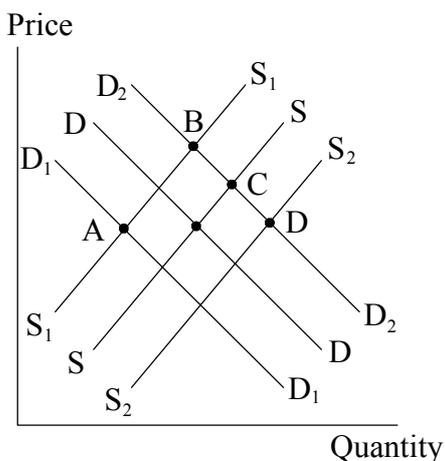
2. The diagram below shows a production possibility curve or frontier for an economy.



What is the opportunity cost of increasing output from $0c$ to $0y$?

- A. Quantity ax of Good A
 - B. Quantity $0a$ of Good A
 - C. Quantity $0c$ of Good B
 - D. Area $0abc$ of Goods A and B
3. In a particular market, if supply increases when demand remains the same, equilibrium price
 - A. rises and equilibrium quantity decreases.
 - B. rises and equilibrium quantity increases.
 - C. falls and equilibrium quantity decreases.
 - D. falls and equilibrium quantity increases.

4. The following diagram represents the market for ice cream.



Initial equilibrium is at the point where S crosses D. Where would the new equilibrium be following an increase in the price of sugar (an ingredient) and a period of hot weather?

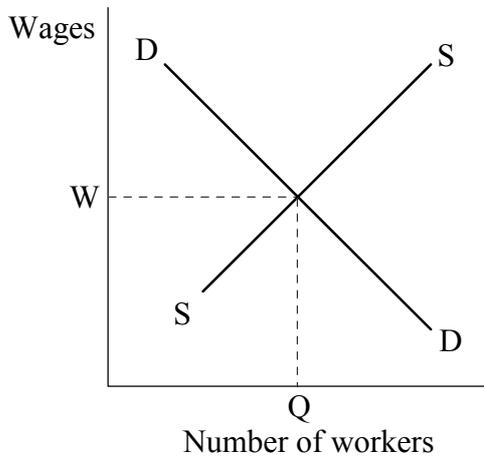
- A. A
 - B. B
 - C. C
 - D. D
5. The following table shows the market for a good.

Price	Quantity demanded	Quantity supplied
50	100	220
40	120	180
30	140	140
20	160	100
10	180	60

A government decision to impose a maximum price of 40 would

- A. leave the equilibrium quantity unchanged and raise the equilibrium price.
- B. create excess supply of 60 units.
- C. reduce the equilibrium price and create excess demand.
- D. leave the equilibrium price unchanged.

6. The following diagram shows the market for labour.



If the government imposed a minimum wage that was greater than W , the following would result:

- I. a decrease in the number of workers seeking employment in the industry.
- II. an increase in the wages of workers.
- III. a decrease in the number of workers in employment.

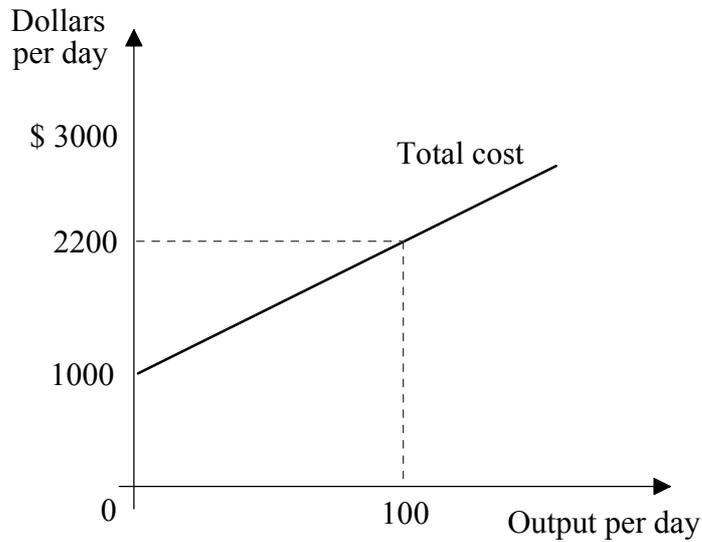
- A. I only
- B. I and II
- C. II and III
- D. I, II and III

7. A good or service consumed by one person can also be consumed by others at no extra cost. This good or service is a

- A. Veblen good.
- B. inferior good.
- C. normal good.
- D. public good.

8. Which **one** of the following is true of a command economy?
- A. Unemployment increases following periods of inflation.
 - B. The signalling function of price plays little part in resource allocation.
 - C. Wage levels are the same in all occupations.
 - D. The value of the currency is determined by supply and demand.
9. The price elasticity of demand for a good is defined as the
- A. lack of responsiveness of price to a change in quantity demanded.
 - B. degree of responsiveness of quantity demanded to a change in price.
 - C. extent of responsiveness of price to a change in income.
 - D. amount of responsiveness of quantity demanded to a change in price of another good.
10. A bookshop wants to increase the quantity of textbooks sold by 5 %. The price elasticity of demand for textbooks is -4 . The bookshop should
- A. raise the price of textbooks by 0.4 %.
 - B. lower the price of textbooks by 0.8 %.
 - C. lower the price of textbooks by 1.25 %.
 - D. lower the price of textbooks by 2 %.
11. At a price of \$1.00 per kilogram, the same amount was spent on bananas as when the price was \$0.80. Which **one** of the following statements can be applied to the banana market?
- A. Demand is inelastic.
 - B. Demand is perfectly elastic.
 - C. Demand is unit elastic.
 - D. Demand is infinitely elastic.

12. Study the following diagram.



At 100 units of output per day average variable cost is

- A. \$10.
 - B. \$12.
 - C. \$22.
 - D. \$1200.
13. A farmer buys several new tractors. All other factor inputs remain the same. Additions to output resulting from this investment decline. This is an example of
- A. the law of diminishing marginal returns.
 - B. diseconomies of scale.
 - C. the principle of diminishing marginal utility.
 - D. constant returns to scale.

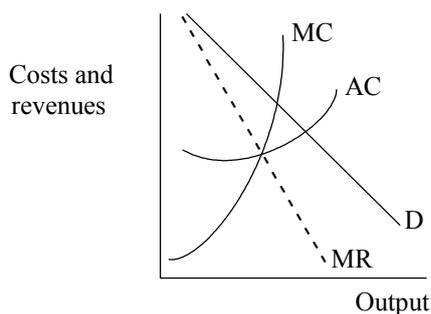
14. In a perfectly competitive market, a farmer is producing and selling 2000 bananas per week, at a price of 1 500 pesos each. The accountant has reported the following cost information relating to an output of 2000 bananas per week:

Total fixed cost	800 000 pesos
Total variable cost	2 000 000 pesos
Marginal cost	1 500 pesos

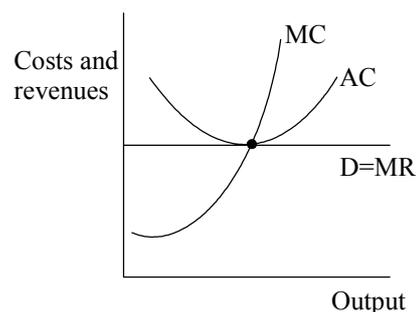
What should the farmer do in order to maximize profits in the short run?

- A. Maintain output at the present level.
 - B. Increase output.
 - C. Decrease output.
 - D. Increase price and leave output constant.
15. Which **one** of the following represents the long-term equilibrium of a firm in perfect competition?

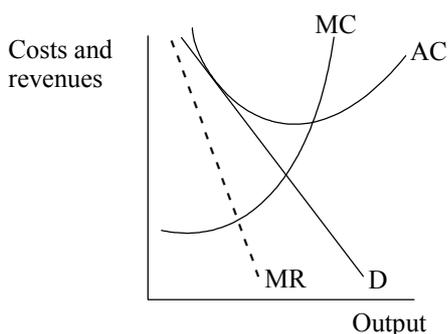
A.



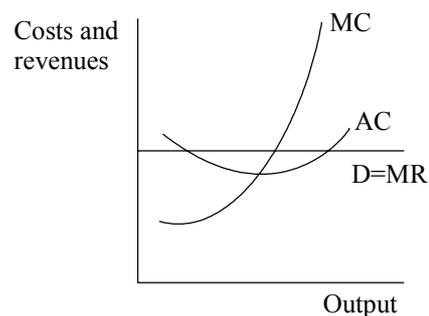
B.



C.

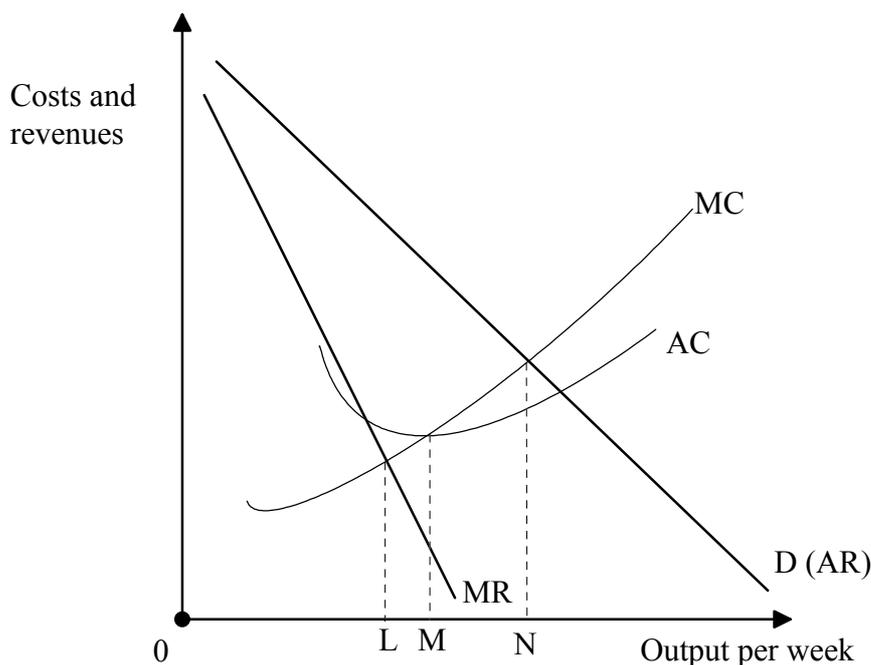


D.



- A. A
- B. B
- C. C
- D. D

16. The following diagram represents different levels of output of a monopolist.



Which of the following is/are correct?

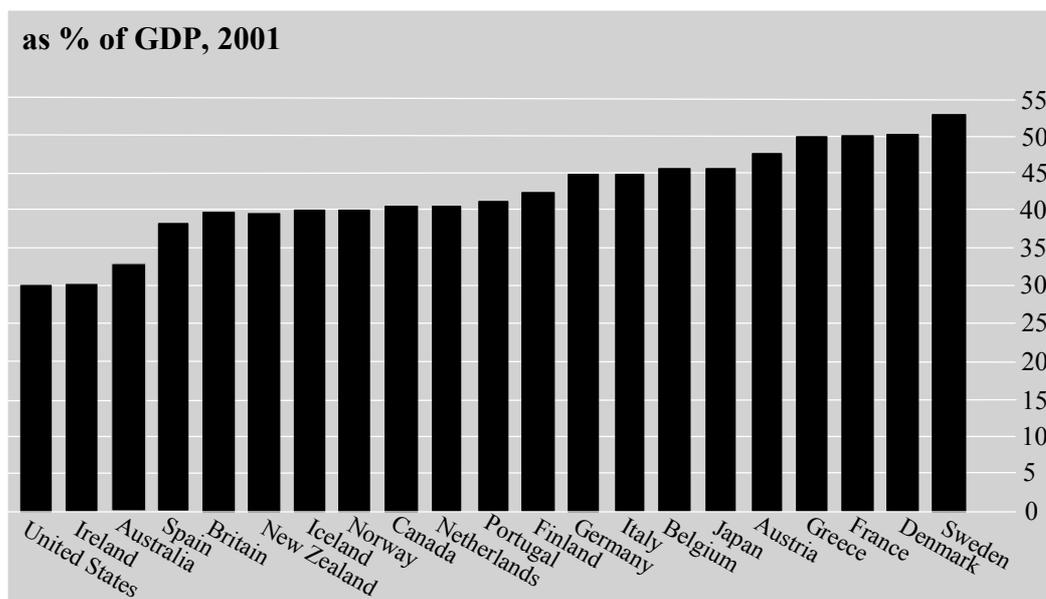
- I. Output 0L is the profit maximising output.
- II. Output 0M represents productive efficiency.
- III. Output 0N represents allocative efficiency.

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

17. To convert Gross National Product at market prices into Net National Product at factor cost, it is necessary to

- A. subtract depreciation and indirect taxes and add subsidies.
- B. add net property income from abroad and add depreciation.
- C. subtract factor costs and subsidies and add indirect taxes.
- D. add fixed capital expenditure by government and subtract depreciation.

18. Refer to the following bar chart concerning government spending.

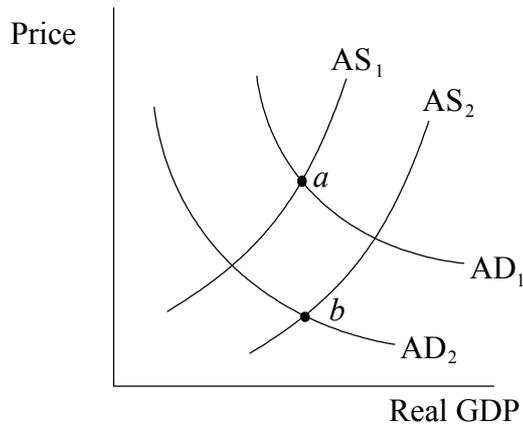


[Source: OECD adapted from *The Economist*, 4 August 2001, p.82]

Which **one** of the following conclusions can be made from this data?

- A. The Irish and US governments spent the lowest amounts.
 - B. The Belgian and Japanese governments spent approximately the same amount.
 - C. Public spending in Japan was roughly 46 % of GDP.
 - D. The amount of public spending in Austria was higher than in Germany.
19. In a closed economy with no government, by how much would investment need to rise to produce an increase in incomes of \$ 6 bn if the marginal propensity to consume is 0.8?
- A. \$ 4.8 bn.
 - B. \$ 0.8 bn.
 - C. \$ 1.2 bn.
 - D. \$ 5.2 bn.

20. Study the following AD/AS diagram.



Initial equilibrium is at point *a*. Which combination of events will move the equilibrium position to point *b*?

- A. Deregulation of industry and lower taxes.
- B. An increase in taxes and stricter environmental laws.
- C. Increased education and training and an increase in direct taxes.
- D. A reduction in interest rates and a programme of privatization.

21. Examine each of the following diagrams in which aggregate demand increases from AD_1 to AD_2 .

DIAGRAM A

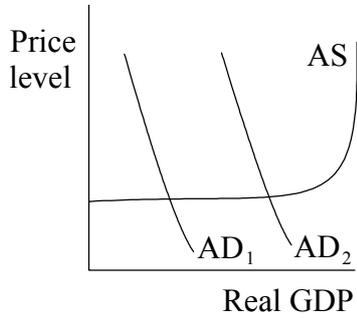


DIAGRAM B

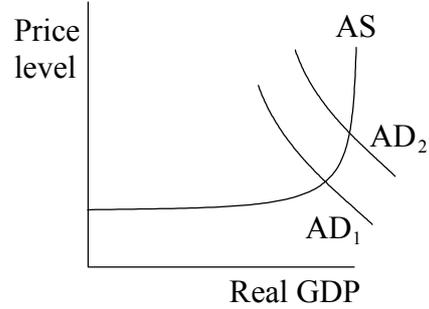


DIAGRAM C

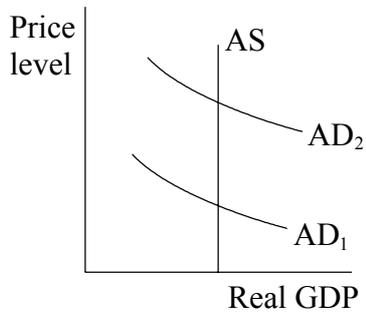
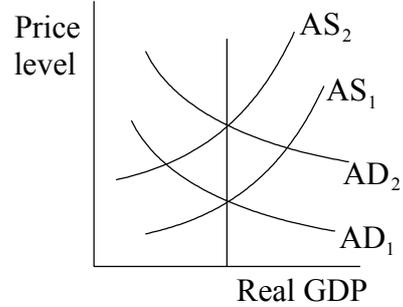


DIAGRAM D



Which **one** of the diagrams best illustrates the success of a government policy to reduce unemployment?

- A. Diagram A
- B. Diagram B
- C. Diagram C
- D. Diagram D

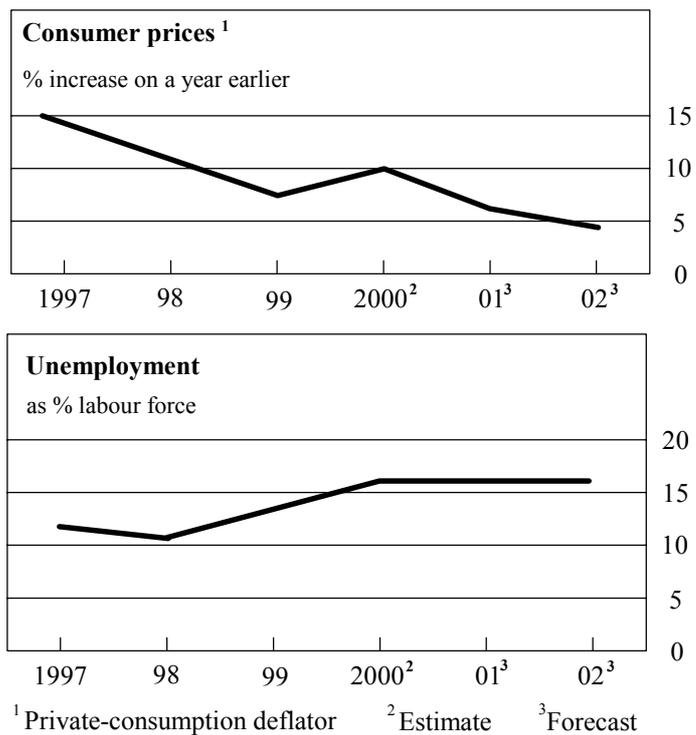
22. An expansionary fiscal policy requires which **one** of the following combinations of policies?

	Government spending	Taxes
A.	Increase	Increase
B.	Increase	Decrease
C.	Decrease	Decrease
D.	Decrease	Increase

23. The multiplier effect of using a budget deficit to stimulate an economy is limited by

- A. net property income from abroad.
- B. the marginal propensity to export.
- C. an increase in transfer payments.
- D. the “crowding out” effect on private sector investment.

24. Consider the following data about unemployment and inflation in the Polish economy.

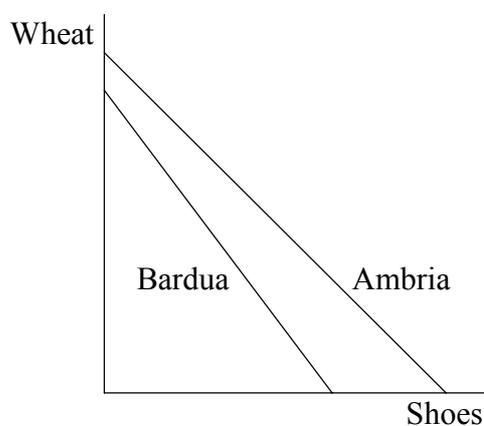


[Source: *The Economist*, 21 April 2001, p.110]

The relationship between unemployment and inflation described by the Phillips Curve is **best** illustrated between the years

- A. 1997–1998.
- B. 1998–1999.
- C. 1999–2000.
- D. 2000–2001.

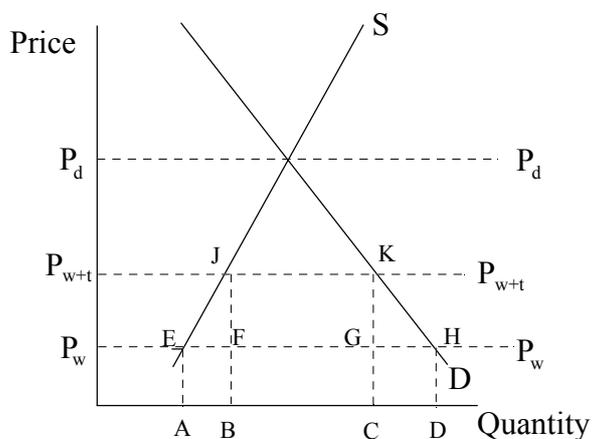
25. The diagram below shows the production possibility curves for two countries, Ambria and Bardua, which both produce wheat and shoes.



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

- A. Bardua has an absolute disadvantage in the production of shoes, but not wheat.
- B. Ambria has a comparative advantage in the production of both shoes and wheat.
- C. Ambria has a comparative advantage in the production of shoes.
- D. Bardua should not produce any wheat at all.

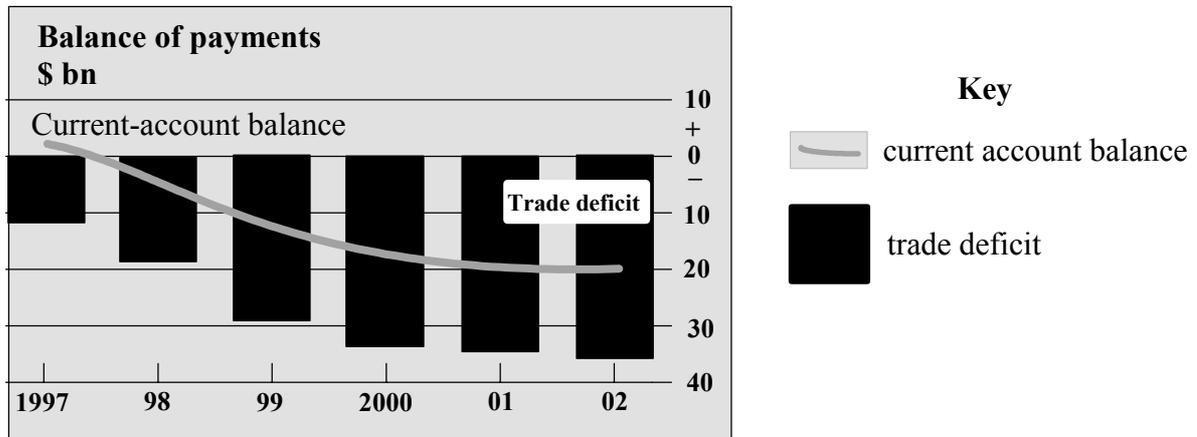
26. In the diagram below, P_d is the domestic price of a good before trade, P_w is the price if there is free trade, and P_{w+t} is the price when a tariff is imposed.



Which **one** of the following statements is **not** correct?

- A. Imports under free trade are AD.
 - B. As a result of the tariff, imports fall by $AB + CD$.
 - C. Government revenue is shown by the area EJKH.
 - D. Domestic consumers are likely to suffer as a result of the tariff.
27. Country X wishes to achieve the benefits of economic integration with other countries but does not wish to sacrifice sovereignty over its economic policies. Which **one** of the following should it join?
- A. A common currency
 - B. A free trade area
 - C. A customs union
 - D. A common market

28. The bar chart below refers to Spain's balance of payments' account.



[Source: OECD adapted from *The Economist*, 30 June 2001, p.98]

From the data, it can be concluded that over the period shown

- A. Spain's trade deficit decreased.
 - B. there were net capital outflows from Spain.
 - C. Spain's trade in services was in surplus.
 - D. Spain's current account balance decreased.
29. Which **one** of the following is an item on the Austrian balance of payments current account?
- A. Increased capital spending by OPEC on its head offices in Austria.
 - B. The purchase of shares of a German firm by an Austrian resident.
 - C. The payment of interest to an Austrian bank by a foreign company.
 - D. A soft loan from the Austrian government to a developing country for a water project.

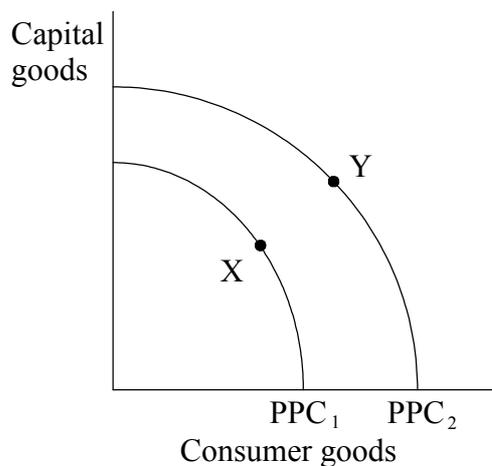
30. From the data given below, calculate the value of a country's invisible balance (balance in services).

Visible balance (balance in goods)	+ 200
Current balance	+ 600
Capital balance (transaction in external assets and liabilities)	- 600
Change in reserves of foreign currency	zero

- A. - 200
- B. zero
- C. + 400
- D. + 800
31. Other things being equal, if the Singaporean dollar declines against other countries, then all of the following are likely to rise **except**
- A. the quantity of Singaporean exports.
- B. tourism in Singapore.
- C. the Singaporean price level.
- D. the price of Singaporean exports, measured in foreign currencies.
32. Which **one** of the following policy combinations would be favoured by a monetarist/ neoclassical economist to help reduce a deficit on the current account of the balance of payments?

	Money supply	Interest rate	Exchange rate	Trade barriers
A.	Decrease	Decrease	Fixed	Increase
B.	Decrease	Increase	Floating	Decrease
C.	Increase	Decrease	Fixed	Increase
D.	Increase	Increase	Floating	Decrease

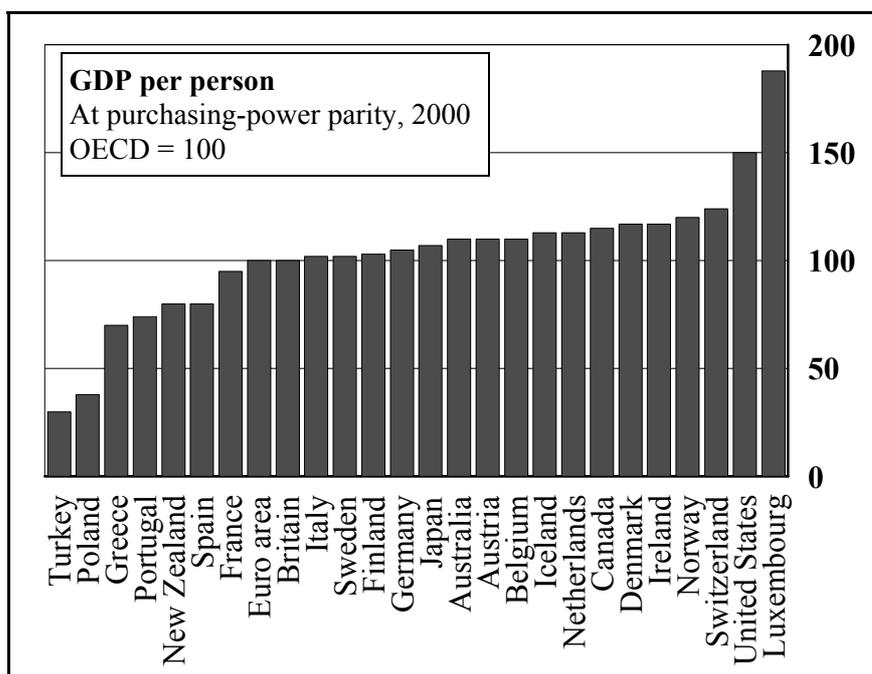
33. Study the diagram below.



A movement from point X on the production possibilities curve PPC_1 to point Y on the production possibilities curve PPC_2 is consistent with the idea of

- I. an increase in the country's GDP.
 - II. an increase in the country's standard of living.
 - III. a reduction in income inequality in the country.
- A. I only
 - B. I and II
 - C. II and III
 - D. I, II and III

34. Study the data in the table below.



[Source: OECD]

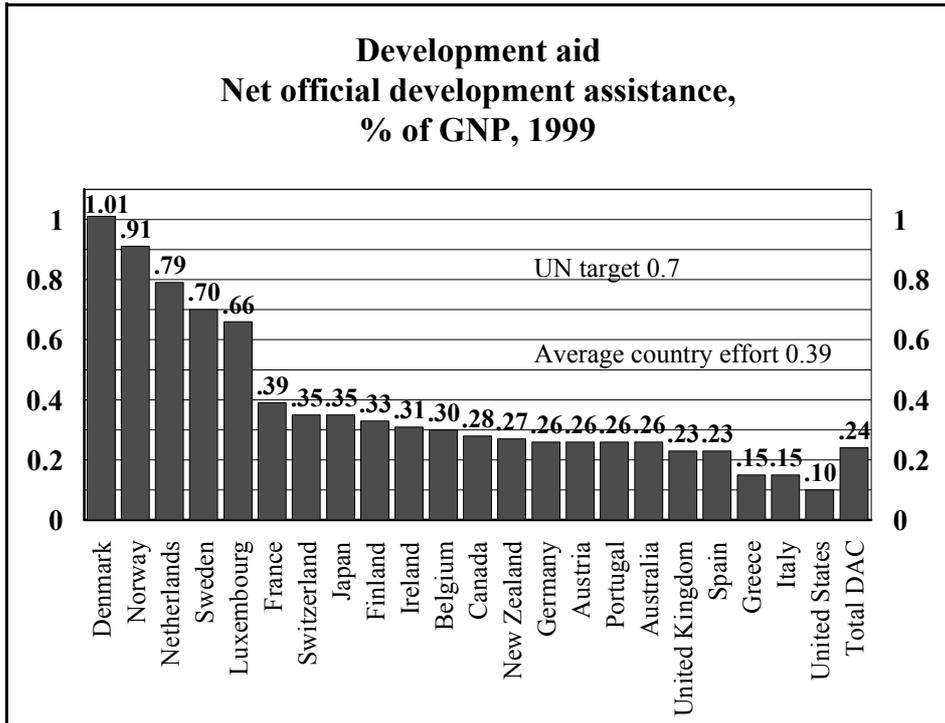
Which **one** of the following statements is correct?

- A. GDP per person at purchasing power parity makes allowance for short term fluctuations in the nominal exchange rate.
- B. GDP per person in the USA is 150 % higher than that in Britain.
- C. Luxembourg has the highest GDP of the countries shown in the chart.
- D. Turkey is the country with the slowest rate of economic growth.

35. Living a long and healthy life, being knowledgeable and enjoying a decent standard of living are goals which are best represented by which one of the following concepts?

- A. Sustainable development
- B. Economic growth
- C. Human development
- D. Sectoral change

36.



[Source: OECD]

From the data in the table it can be concluded that

- A. the total amount of official aid given by the countries shown in the chart fell in 1999.
 - B. the USA is the smallest aid contributor in percentage terms but the largest in absolute terms.
 - C. Luxembourg contributes twice the amount of aid that Finland does.
 - D. only four countries met the UN target for aid.
37. A major difference between commodity agreements and cartels is that a commodity agreement, unlike a cartel,
- A. includes consumers as well as producers of the product.
 - B. is a voluntary agreement rather than a legal agreement.
 - C. does not attempt to control prices by setting production quotas.
 - D. seeks to maximise the producer's total revenue rather than their total profit.

- 38.** Which of the following is/are part of an IMF approved development strategy?
- I. Freely floating exchange rates
 - II. Cuts in government subsidies to help balance the government's budget
 - III. Making income (direct) taxes more progressive so as to reduce income inequality
- A. I only
 - B. I and II
 - C. II and III
 - D. I, II and III
- 39.** Outward-orientated growth strategies are characterized by
- A. government intervention through long term economic planning.
 - B. import substitution and protection of infant industries.
 - C. export-led growth and free interaction of market forces.
 - D. the formation of cartels and buffer stocks through international commodity agreements.
- 40.** The concept of “sustainable development” has been much discussed in recent years because of a realization that
- A. the debt repayments of LDCs cannot be sustained at their present level.
 - B. the exchange rates of LDCs are more unstable than those of MDCs.
 - C. technological change has allowed for the market mechanism to operate in a more efficient manner.
 - D. present MDC production and consumption patterns cannot be enjoyed by all the world's population.
-