



**ECONOMICS
HIGHER LEVEL
PAPER 1**

Wednesday 7 November 2001 (afternoon)

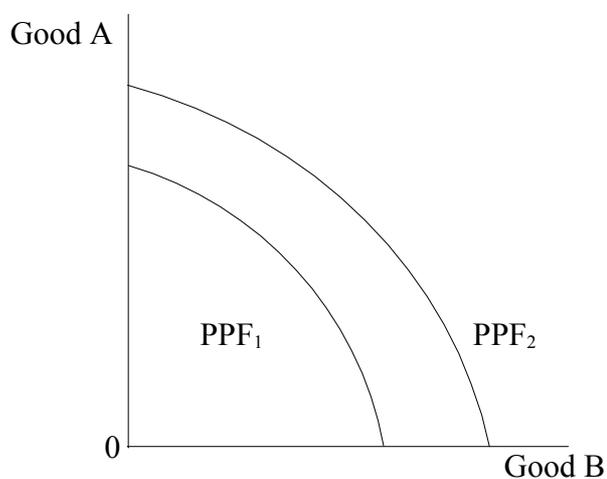
1 hour

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. In a free market economy, the most important determinant of resource allocation is the
 - A. government.
 - B. entrepreneur.
 - C. price mechanism.
 - D. exchange rate.

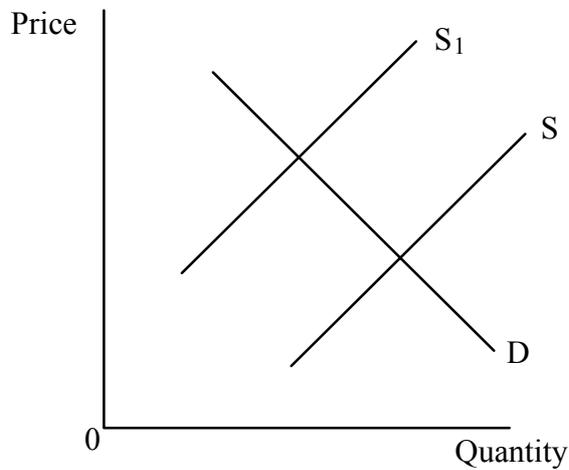
2. The following diagram shows two production possibility frontiers (PPF) for an economy which can produce two goods.



- A shift from PPF₁ to PPF₂ is caused by
- A. an increase in aggregate demand.
 - B. price increases for both good A and good B.
 - C. an increase in the productivity of labour.
 - D. recovery from a recession.

3. A major distinction between an economic good and a free good is that a free good
- A. is provided by the government.
 - B. is always a public good.
 - C. has the same price as an inferior good.
 - D. has no opportunity cost.

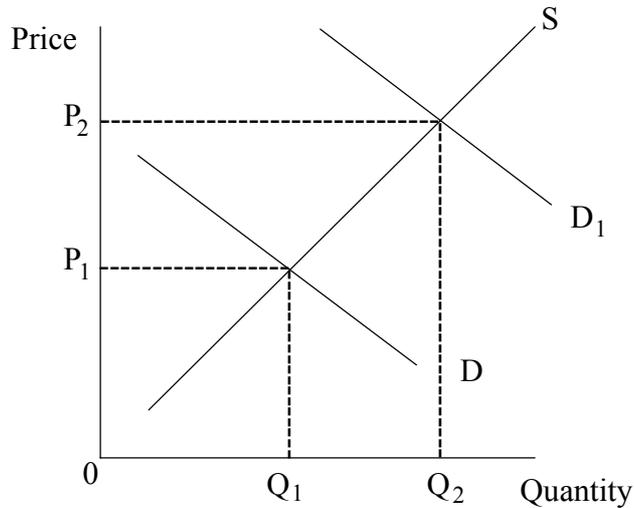
4. The diagram below shows the demand and supply for tennis balls.



Which **one** of the following could explain the shift in the supply curve from S to S₁?

- A. An increase in the price of a complement
- B. A decrease in the level of a government subsidy for tennis ball producers
- C. An improvement in the technology for making tennis balls
- D. A decrease in the cost of producing tennis balls

5. The diagram below shows the demand and supply for a good.



Which **one** of the following could explain the rise in price from P_1 to P_2 ?

- A. A fall in consumer incomes
- B. A rise in the cost of producing the good
- C. A fall in the price of a complementary good
- D. A fall in the price of a substitute good

6. The table below shows a demand and supply schedule.

Price in dollars	Quantity demanded	Quantity supplied
20	100	200
18	120	170
16	140	140
14	160	110
12	180	80
10	200	50

A government decision to impose a minimum price of 12 dollars would result in

- A. excess demand of 100.
- B. excess supply of 100.
- C. a fall in the equilibrium price to 12 dollars.
- D. no change in the equilibrium price or quantity.

7. Other things being equal, the existence of a negative externality is likely to be associated with
- A. underproduction.
 - B. overproduction.
 - C. under-consumption.
 - D. overpricing.
8. During the 1990s several countries, mainly in Eastern Europe, made the transition from a planned economy to a market economy. The economies experienced all of the following problems **except**
- A. fluctuating growth rates.
 - B. rising unemployment.
 - C. disruption of consumption and production patterns.
 - D. falling prices.
9. Which **one** of the following best describes a tradable permit?
- A. A means of creating a market in externalities
 - B. A non tariff import restriction
 - C. A licence issued to producers in command economies
 - D. An indicator of the band in which a fixed exchange rate is allowed to fluctuate
10. A value of -2 for income elasticity of demand for a good means that
- A. any 1 % increase in income leads to a 2 % increase in quantity demanded.
 - B. any 1 % increase in income leads to a $\frac{1}{2}$ % increase in quantity demanded.
 - C. any 1 % decrease in income leads to a 2 % increase in quantity demanded.
 - D. the good would be classified as a normal good.

11. A business in a more developed country believes that its product has a price elasticity of demand of -0.1 per year. It has an income elasticity of demand of $+0.1$ per year and a price elasticity of supply of 0 per year.

The business is most likely to be in which **one** of the following industries?

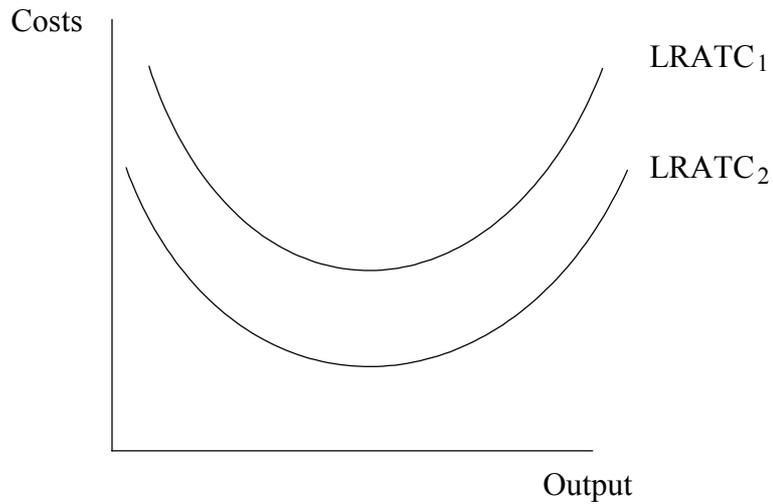
- A. Computer manufacturing
 - B. Farming
 - C. Car manufacturing
 - D. Foreign exchange dealing
12. A profit maximising firm believes that the demand for its product is price elastic. It also believes that it will get increasing returns to the variable factor if it increases output. In these circumstances it should
- A. reduce price and increase output.
 - B. reduce price and decrease output.
 - C. increase price and increase output.
 - D. increase price and decrease output.
13. The table below shows total cost at various levels of output.

Output	Total Cost
0	60
10	300
20	500
30	600
40	1000
50	1500

Average fixed cost at the productively efficient level of output is

- A. 2.
- B. 20.
- C. 60.
- D. 600.

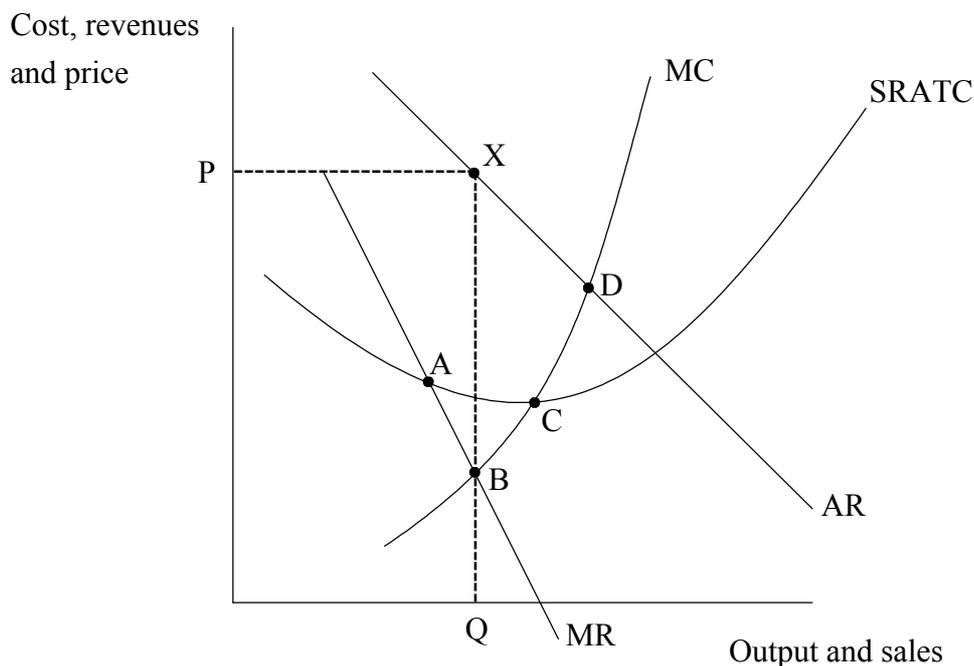
14. This question relates to the diagram below.



A shift in the long run average total cost curve from LRATC₁ to LRATC₂ would be due to

- A. increasing returns to scale.
- B. increasing returns to the variable factor of production.
- C. increased short run production costs.
- D. a technological breakthrough.

15. This question relates to the diagram below.



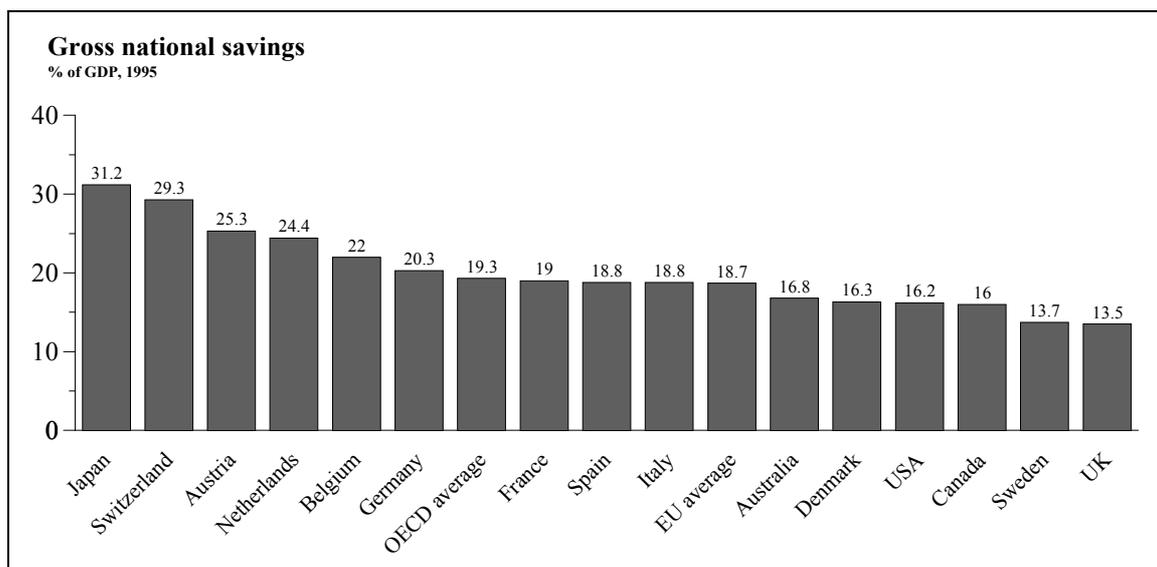
Point X represents the profit maximising level of price and output of a monopoly firm. Other things remaining equal, if this firm were to become perfectly competitive the new equilibrium level of price and output would be given by point

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

16. Price discrimination can best be defined as

- A. charging different consumers different prices for the same product for reasons not associated with variations in costs.
- B. charging different consumers different prices for the same product at different times of the day.
- C. charging public sector firms a different price from private sector firms.
- D. producers taking advantage of differences in costs in different markets to charge different prices.

17. Examine the graph below and answer the question which follows.



From the information provided in the graph it may be concluded that of the countries listed

- A. Spain and Italy have similar GDP per capita.
- B. the UK is the most likely to achieve economic growth.
- C. Japan is likely to have the highest rate of inflation.
- D. Japan is likely to have the highest rate of investment.

18. The figures below provide the national income statistics for a given economy.

GDP	\$6847 billion
Consumption	\$5528 billion
Government spending	\$942 billion
Investment	\$529 billion

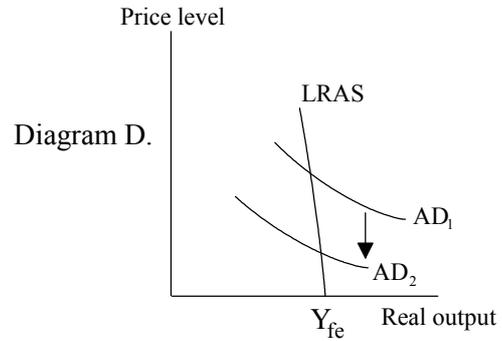
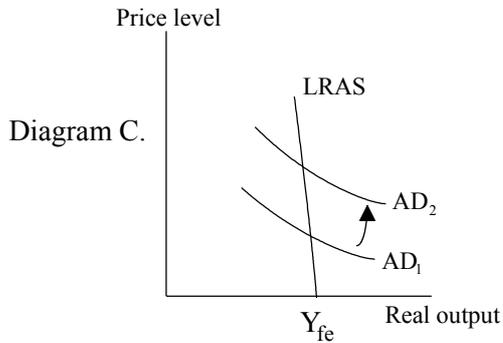
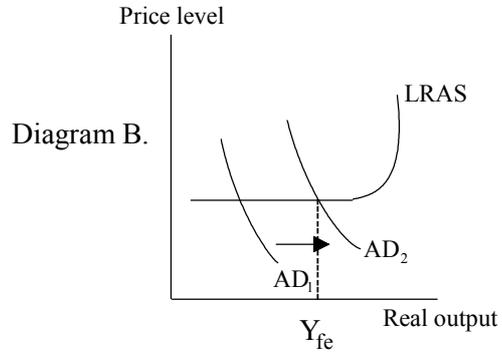
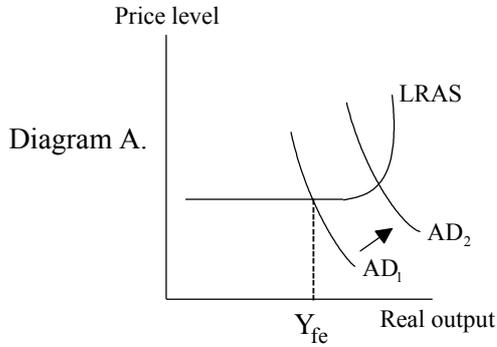
Given the amounts above, net exports are

- A. - \$319 billion.
- B. - \$152 billion.
- C. \$6999 billion.
- D. \$413 billion.

19. The question below refers to the following headline in a national newspaper:

“Increased unemployment rate prompts talk of an interest rate cut.”

If the Central Bank were to cut the interest rate as suggested by the headline, which diagram best illustrates the present situation and desired outcome?



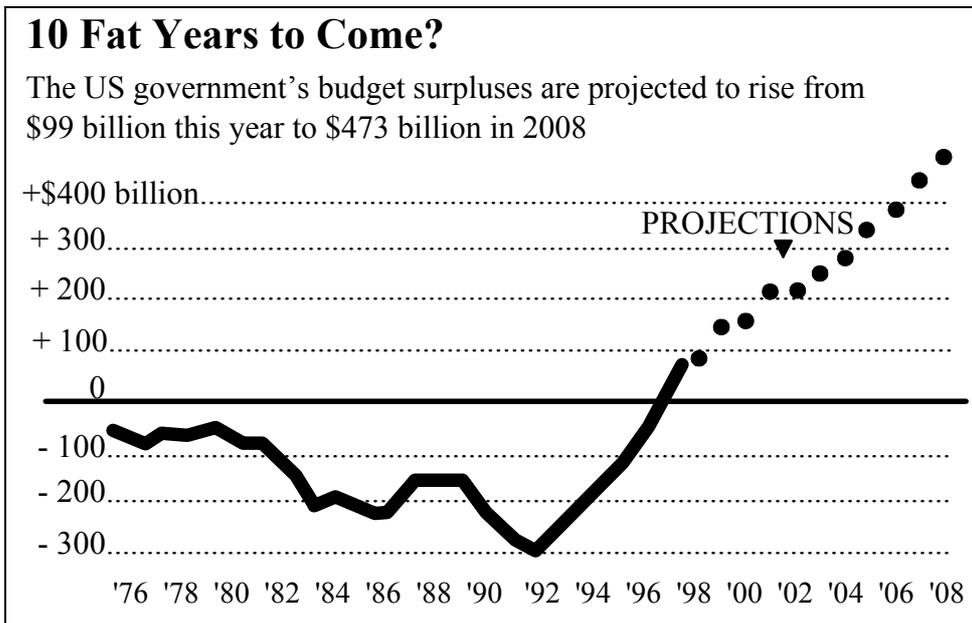
Note: Y_{fe} equals the full employment level of income.

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

20. The value of the multiplier will fall if there is a fall in

- A. investment.
- B. the marginal propensity to consume.
- C. the marginal propensity to import.
- D. national income.

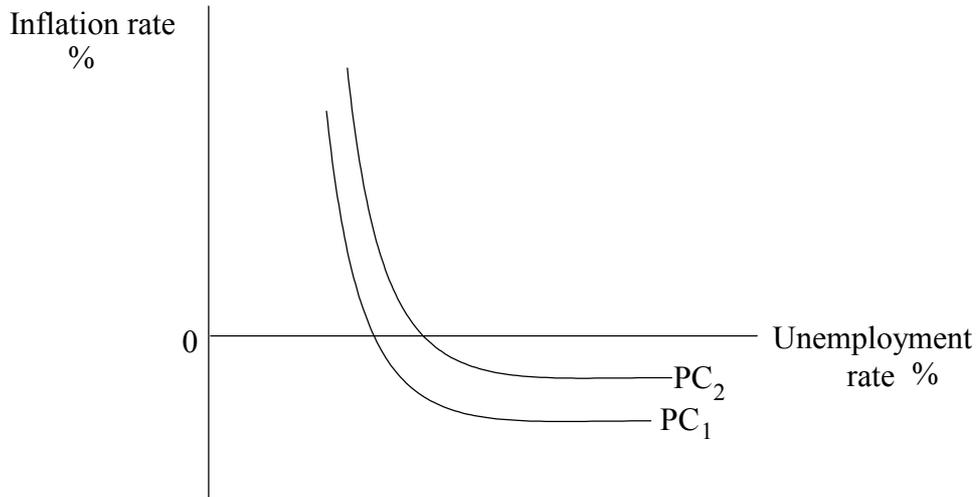
21. The graph below shows the United States government budget from 1976, projected to 2008.



Which **one** of the following conclusions can be drawn from the graph?

- A. The US budget surplus in 1984 was approximately \$200 billion.
 - B. In 1992, the difference between US exports and imports reached its highest value.
 - C. It was forecast that in 1999 there would be no national debt.
 - D. In 1998 government revenues exceeded government spending.
22. What type of unemployment best describes workers in the automobile industry who are still unemployed two years after their factory closed down?
- A. Frictional unemployment
 - B. Structural unemployment
 - C. Seasonal unemployment
 - D. Cyclical unemployment

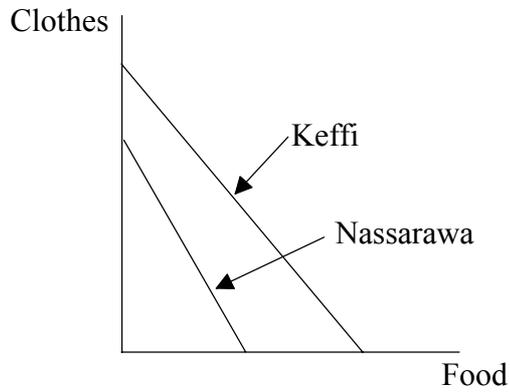
23. This question relates to the Phillips curve diagram below.



A shift in the Phillips curve from PC₁ to PC₂ is most likely to have been caused by an increase in

- A. government spending.
 - B. investment.
 - C. minimum wages.
 - D. taxation.
24. Crowding out occurs when
- A. overvalued currencies force uncompetitive exporters out of business.
 - B. increased private investment in an economy at full employment causes a reduction in consumption spending.
 - C. a budget surplus is used to finance the renationalisation of utilities.
 - D. increased government demand for funds causes an increase in interest rates and a fall in private investment.

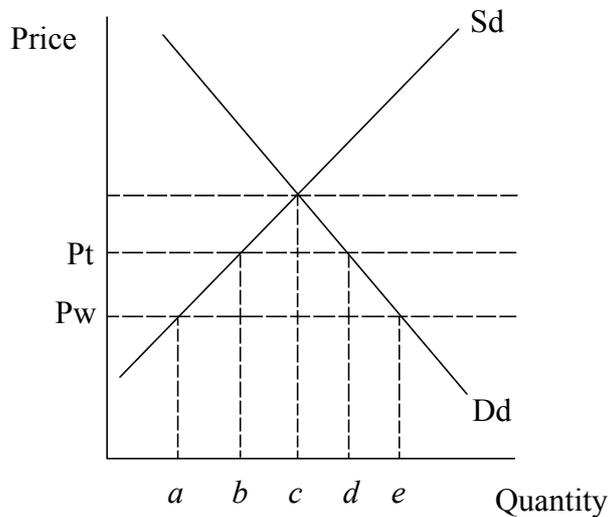
25. The diagram below shows the production possibility frontiers for two countries, Keffi and Nassarawa, which both make clothes and food.



From the diagram it may be concluded that

- A. Nassarawa has a lower rate of inflation than Keffi.
- B. Nassarawa has a comparative advantage in producing clothes.
- C. Keffi has an absolute advantage only in the production of food.
- D. Keffi has a comparative advantage in both food and clothes.

26. The graph below shows the domestic supply (Sd) and domestic demand (Dd) for widgets in Platonia. Pw represents the world price for widgets. Pt is the price following the imposition of a tariff.



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

- A. With free trade, Platonia will import *bd* widgets.
 - B. In moving from free trade to trade with a tariff, there has been an overall increase in efficiency.
 - C. As a result of the tariff, there is a decrease in the supply of widgets made in Platonia.
 - D. As a result of the tariff, imports fall from *ae* to *bd*.
27. Which **one** of the following is an item on the Canadian Balance of Payments current account?
- A. The purchase of shares in a Japanese firm by a Canadian resident
 - B. The purchase of a Canadian firm by a foreign multinational company
 - C. The payment of interest by a Canadian bank to a foreign depositor
 - D. The payment of a loan to the Canadian government from the IMF

28. The question below refers to the following headline:

“Britain’s trade deficit widened to £2.18 billion in November from £1.64 billion in October as imports surged.”

Which **one** of the following was **most** likely to have caused the situation described in the headline?

- A. A fall in the exchange rate of the British pound
- B. An increase in British interest rates
- C. An improved balance of trade
- D. A rise in the exchange rate of the British pound

29. If the Japanese Yen declines against other currencies, then all of the following are likely to rise **except**

- A. Japanese output.
- B. the price level in Japan.
- C. the price of Japanese exports in terms of other countries.
- D. the volume of Japanese goods sold in other countries.

30. Which **one** of the following is the best explanation for the ‘J-curve’ effect following the depreciation of a currency?

- A. The demand for exports is very price elastic in the short run.
- B. Consumers and producers react very quickly to the increased prices of imported goods.
- C. Over a period of time, demand for both exports and imports tends to become more price elastic.
- D. Fluctuating exchange rates lead to an automatic adjustment in the balance of payments.

31. If the price elasticity of demand for Swedish exports is -0.4 and the elasticity of demand for imports is -0.3 then, other things being equal, a devaluation of the Swedish Krona will lead to
- A. a fall in Swedish export revenues.
 - B. an improvement in the Swedish terms of trade.
 - C. a fall in the level of unemployment in Sweden.
 - D. an improvement in the visible trade balance.

32. The following data shows a country's export and import prices.

	Index of export prices	Index of import prices
1996	100	100
1997	120	140
1998	130	130
1999	150	140

The terms of trade for this country

- A. rose between 1996 and 1997 and then fell.
- B. fell between 1996 and 1997 and then rose.
- C. fell between 1996 and 1998 and then rose.
- D. rose continuously over the whole period.

33. The following table shows the percentage of national income distributed over five segments of the population in four different less developed countries.

Country	lowest 20 %	second 20 %	third 20 %	fourth 20 %	highest 20 %
Brazil	2.1	4.9	8.9	16.8	67.5
Sri Lanka	8.9	13.1	16.9	21.7	39.3
Guatemala	2.1	5.8	10.5	18.6	63.0
Hong Kong	5.4	10.8	15.2	21.6	47.0

Which **one** of these four countries has the most unequal income distribution?

- A. Brazil
 - B. Sri Lanka
 - C. Guatemala
 - D. Hong Kong
34. Migration takes place in a less developed country from the countryside (where food is produced) to the town, yet there is no reduction in the country's domestic food supply. This is because rural farms
- A. were experiencing negative marginal returns to labour.
 - B. were experiencing diseconomies of scale.
 - C. were not paying money wages.
 - D. now provide less food to their remaining workers.

35. The following data gives values of GNP per capita in US dollars and the Human Development Index (HDI) for particular countries for a particular year.

	GNP per capita	HDI value
Country A	28,740	0.943
Country B	25,820	0.941
Country C	20,710	0.932
Country D	19,290	0.960

Which **one** of the following statements is consistent with the data?

- A. The citizens of Country A have the highest living standards.
 - B. Country D is the least developed of the four countries.
 - C. Life expectancy and adult literacy are highest in Country D.
 - D. Country A has the fastest economic growth rate.
36. A country experiences long run economic growth resulting in a large taxable capacity. The government wishes to further increase the country's level of economic development. Which **one** of the following policies should it pursue?
- A. Leave all wealth and income in private hands and wait for 'trickle-down'.
 - B. Tax and spend heavily on defence.
 - C. Tax and spend on merit goods which improve human capital.
 - D. Borrow from abroad to pay for improved administrative efficiency.
37. Which **one** of the following is **not** a common view of the effect of foreign aid?
- A. Aid helps fill the foreign exchange 'gap' which makes it difficult for developing countries to finance necessary imports of capital.
 - B. Aid can contribute to the transfer of necessary skills and technologies.
 - C. Food aid has alleviated famine in several drought stricken areas.
 - D. Most aid has been directed to rural projects, stimulating valuable employment opportunities.

- 38.** As a country experiences economic growth
- I. there will necessarily be greater equality of income.
 - II. employment tends to shift from primary to secondary to tertiary industry.
 - III. real GNP increases.
- A. I only
 - B. I and II
 - C. II and III
 - D. I, II and III
- 39.** A Sub-Saharan less developed country (LDC) with a narrow range of non-oil exports managed to increase its exports by volume during the 1990s. Nevertheless, it found difficulty in paying for necessary imports. A development economist might argue that this was a result of
- A. an adverse shift in the LDC's terms of trade.
 - B. the growth of protectionism.
 - C. international debt reduction.
 - D. capital flight.
- 40.** The government of a country finds that the use of non-renewable resources is unavoidable. If it still wishes to pursue a policy of sustainable development, the government should
- A. deplete the country's non-renewable resources without polluting the environment.
 - B. reduce the rate of economic growth to ease pressure on aggregate demand.
 - C. exploit non-renewable resources more slowly than the rate of growth of renewable resources.
 - D. depreciate the stock of natural capital.
-