



**ECONOMICS  
HIGHER LEVEL  
PAPER 1**

Tuesday 9 November 2004 (afternoon)

1 hour

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**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.

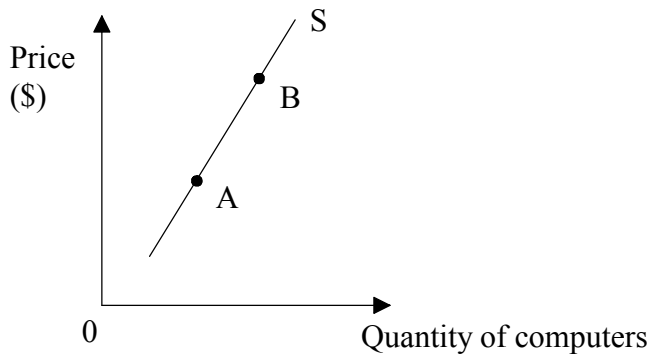
1. Which **one** of the following can be described as a normative statement?

- A. The natural rate of unemployment is 4 %.
- B. Unemployment has fallen in the last year.
- C. Unemployment is too high.
- D. The level of inflation has increased in the last year.

2. To an economist, a free good is best described as

- A. a good which has no opportunity cost.
- B. a good which is available at no cost to a consumer.
- C. a good which has a negative opportunity cost.
- D. a good or service provided by the government.

3. The graph below illustrates the supply of computers in Canada.

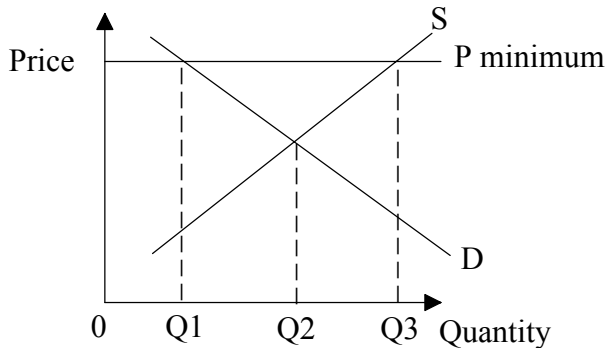


A movement from A to B may be caused by which **one** of the following?

- A. A fall in the price of machinery used to make computers.
- B. An increase in incomes.
- C. Increased subsidies to computer manufacturers.
- D. Improved technology in the computer industry.

4. When there is a fall in the price of a good,
- A. the income effect is always positive.
  - B. the substitution effect is always positive.
  - C. the income effect is zero.
  - D. the substitution effect is zero.

5. The following diagram illustrates the market for wheat in a country.



The imposition of a minimum price for wheat at “P minimum” is likely to lead to

- A. a shortage of wheat equal to Q1Q3.
  - B. an increase in the quantity of wheat demanded of Q2Q3.
  - C. an over-supply of wheat of Q1Q3.
  - D. a fall in the quantity of wheat supplied of Q2Q3.
6. Which **one** of the following combinations best applies to a public good?

	<b>Rivalrous</b>	<b>Excludable</b>
A.	Yes	Yes
B.	Yes	No
C.	No	Yes
D.	No	No

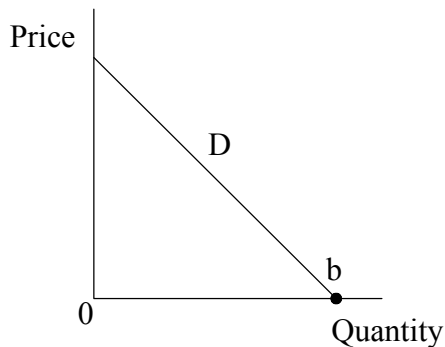
7. The socially efficient level of output is at which **one** of the following levels?

	<b>Output</b>	<b>Marginal social cost</b>	<b>Marginal private benefit</b>	<b>External benefit</b>
A.	30	200	150	20
B.	40	220	170	30
C.	50	240	190	50
D.	60	260	210	70

8. A country moving from a centrally planned system to a market system is likely to experience which **one** of the following?

- A. A fall in unemployment
- B. An increase in inflation
- C. More equitable distribution of income
- D. An increase in the exchange rate of its currency

9. Study the following demand curve for good X.

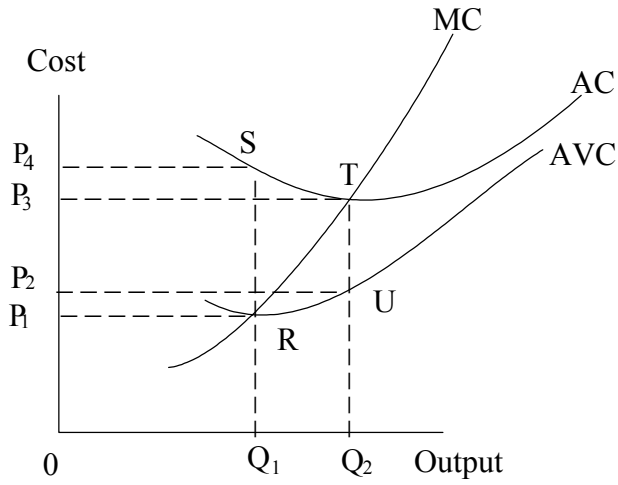


At point b price elasticity of demand will be

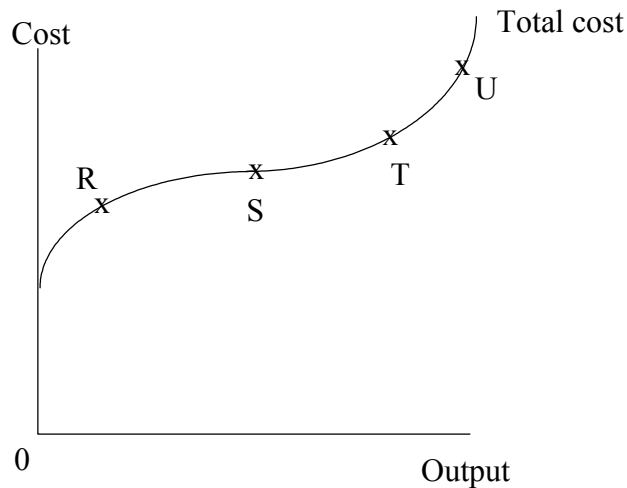
- A. unitary.
- B. zero.
- C. infinity.
- D. variable.

10. An increase in the price of petrol of 5 % results in the fall of the quantity of cars sold of 10 %. This suggests that
- A. the price elasticity of demand for petrol is 2.
  - B. the price elasticity of demand for cars is 2.
  - C. the cross elasticity of demand between petrol and cars is 0.2.
  - D. the cross elasticity of demand between petrol and cars is negative.
11. A Giffen good is
- A. a good with positive income elasticity.
  - B. a good with negative income elasticity.
  - C. an inferior good where the income effect of a price change is greater than the substitution effect of the price change.
  - D. an inferior good where the income effect of a price change is smaller than the substitution effect of the price change.
12. A perfectly competitive firm, which is maximizing its profit, is selling each unit of output at \$6 and its total revenue is \$600. Given a fixed cost of \$100 and an average variable cost of \$3 per unit of output, the firm is
- A. making an economic (supernormal) profit of \$200.
  - B. having an economic loss of \$200.
  - C. earning normal profit only.
  - D. attaining productive efficiency.

13. Refer to the following diagram. What would be the loss to the firm if it produced at the shut down output?



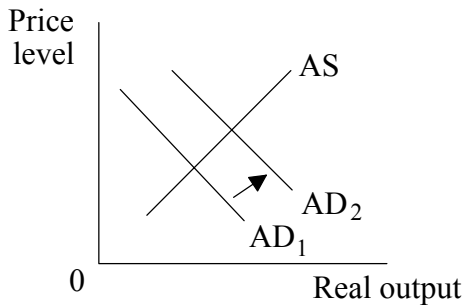
- A.  $P_1P_4SR$
  - B.  $0P_4SQ_1$
  - C.  $0P_3TQ_2$
  - D.  $P_2P_3TU$
14. Refer to the following diagram. At which point does the law of diminishing returns begin to operate?



- A. R
- B. S
- C. T
- D. U

15. Which **one** of the following statements can be made about a perfectly competitive firm?
- A. Economic profits (abnormal) exist in the long run.
  - B. Productive and allocative efficiency cannot exist in the long run.
  - C. The demand curve is the same as the market demand curve.
  - D. Its total revenue curve is a straight line.
16. Which **one** of the following policies would a government be least likely to use to regulate private monopolies?
- A. Subsidies
  - B. Price controls
  - C. Output restrictions
  - D. Anti-trust laws
17. Net national product is equal to
- A. gross national product minus depreciation.
  - B. the total value of all goods and services produced in the country in a year.
  - C. gross national product minus indirect taxes plus subsidies.
  - D. gross domestic product plus net property income from abroad.

18.



Which **one** of the following could cause the shift from  $AD_1$  to  $AD_2$ ?

- A. An increase in income tax.
  - B. An increase in the external balance.
  - C. An increase in the interest rate.
  - D. An increase in productivity.
19. In an economy with a marginal propensity to withdraw equal to 0.2 and equilibrium income equal to \$200 million, find the new level of income if there is an increase in investment expenditure of \$2 million.
- The new equilibrium level of income is
- A. \$200 million.
  - B. \$202 million.
  - C. \$210 million.
  - D. \$202.5 million.
20. The accelerator principle helps to explain why
- A. income will increase due to an increase in government expenditure.
  - B. import payments fluctuate with national income.
  - C. output and employment in capital goods industries fluctuate more than in consumer goods industries.
  - D. an economy will accelerate with an increase in saving.



21. Which of the following policies would be most appropriate in controlling cost-push inflation?
- A. Reducing income tax.
  - B. Removing price ceiling on food.
  - C. Increasing money supply.
  - D. Increasing labour productivity.

22. Referring to Figure 1, the movement from A → B → C → D → E corresponds to which movement on Figure 2?

Figure 1

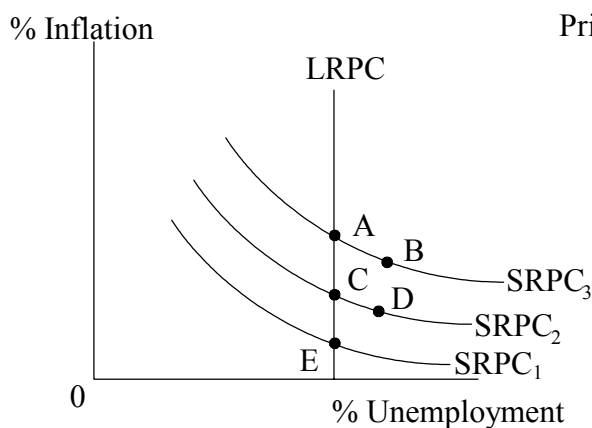
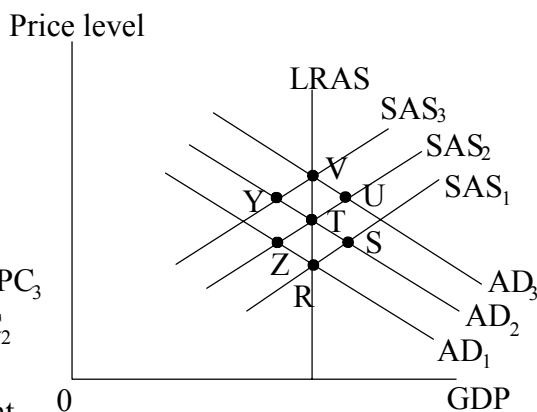
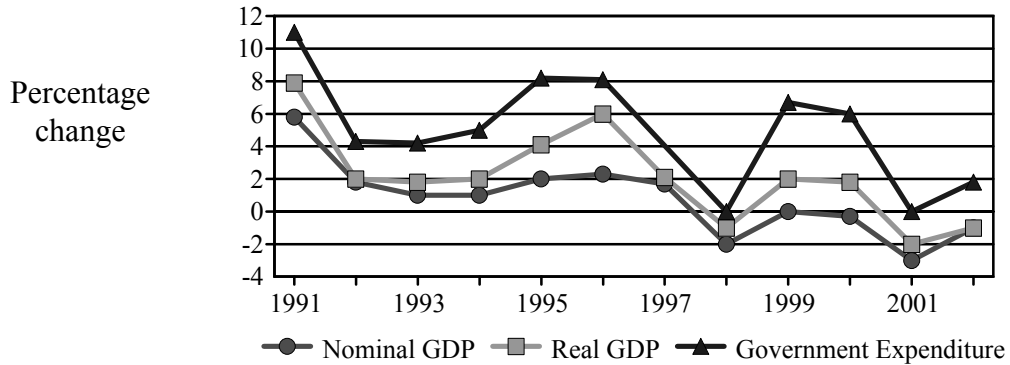


Figure 2



- A. R → Z → T → Y → V
- B. V → Y → T → Z → R
- C. V → U → T → S → R
- D. R → S → T → U → V

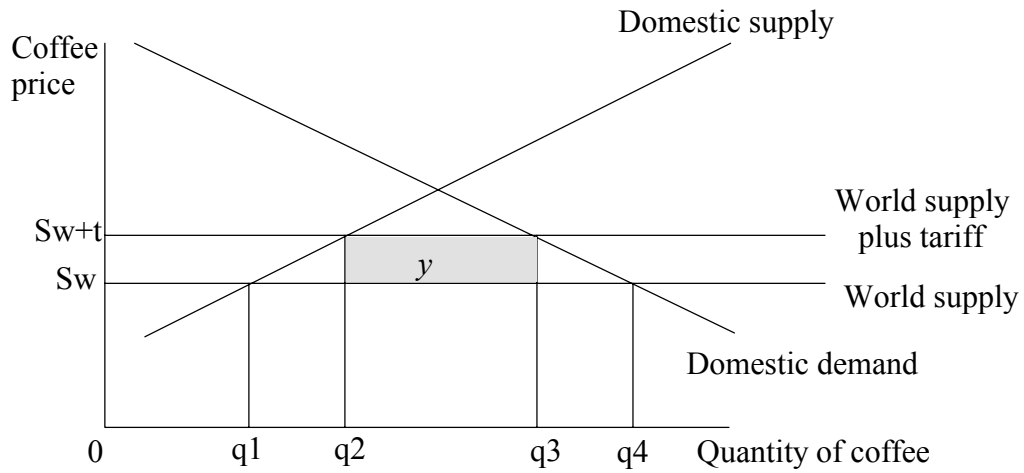
23. The graph below shows the annual growth rates of government expenditure, nominal and real GDP of Japan.



Which of the following can be concluded from the graph?

- A. Japanese government was using contractionary policies during 1990s.
  - B. The difference in nominal and real GDP growth rates can be explained by the changes in government expenditure.
  - C. Japan was experiencing deflation in most of the years throughout the period.
  - D. There was a continuous decline in the living standard of the Japanese economy throughout the period.
24. “Crowding out” can best be defined as
- A. a fall in private sector investment as a result of increased government borrowing.
  - B. the effect of a multinational company entering a less developed country.
  - C. an increase in unemployment as a result of excessive trade union power.
  - D. a fall in interest rates leading to greater demand for investment funds.
25. The law of comparative advantage depends on the existence of
- A. similar opportunity costs in the production of different goods in the same country.
  - B. different opportunity costs in the production of the same goods in different countries.
  - C. similar opportunity costs in the production of different goods in the same countries.
  - D. lower opportunity costs in the production of all goods in one country.

26. The following diagram shows country X, introducing a tariff on imports of coffee.



Rectangle  $y$  shows the value of

- A. improved living standards in country X.
  - B. tariff revenues to the government of country X.
  - C. production gained from world producers by domestic producers.
  - D. environmental or green gain.
27. A teacher from a school in the USA attends a conference in Costa Rica. When she pays her hotel bill this will show in the US balance of payment as
- A. an invisible export.
  - B. a visible export.
  - C. a capital transaction
  - D. an invisible import.

- 28.** The value of the euro is likely to rise against the US dollar if
- A. interest rates are higher in the USA than in the euro-zone countries.
  - B. the USA has a trade surplus with the euro-zone countries.
  - C. interest rates rise in the euro-zone countries.
  - D. productivity is greater in the US economy than in the euro-zone countries.
- 29.** Trade diversion is said to take place when
- A. a trade agreement is signed between two countries and they agree to eliminate all barriers to trade between themselves.
  - B. a union is formed between countries, where the member countries act as a single market, with free movement of labour and capital.
  - C. a customs union leads to greater specialization according to comparative advantage and thus a shift in production from higher-cost to lower-cost sources.
  - D. a customs union changes consumption from goods produced at a lower cost outside the union to goods produced at a higher cost within the union.
- 30.** The J-curve effect shows that
- A. any surplus on the balance of payments overall must, at some time, be followed by corresponding deficits.
  - B. there tends to be regular fluctuations between deficit and surplus on the balance of payments.
  - C. following measures to cure a balance of payments deficit, such as devaluation, there tends to be an immediate further deterioration in the balance before a recovery takes place.
  - D. Japanese trade surpluses have an adverse effect upon the balance of payments accounts of their trading partners.

31. The following table shows the indices of import and export prices for country X.

Year	2002	2004
Index of export prices	90	102
Index of import prices	100	110

From the data it can be concluded that

- A. country X has a trade surplus.
  - B. country X has a trade deficit.
  - C. there has been a deterioration in the terms of trade.
  - D. there has been an improvement in the terms of trade.
32. Which **one** of the following statements is true concerning exchange rates and the terms of trade?
- A. Devaluation improves the terms of trade.
  - B. Governments will seek to balance the terms of trade to keep exchange rates stable.
  - C. Improvements in the terms of trade can be caused by currency appreciation.
  - D. Revaluation causes deterioration in the terms of trade.
33. Which **one** of the following statements about economic growth and development is true?
- A. Economic growth always leads to economic development.
  - B. IMF structural adjustment policies are well known for contributing to both growth and development in LDCs.
  - C. Economic development is possible without economic growth.
  - D. The majority of LDCs have achieved higher rates of economic development than economic growth.

34. Economic growth in LDCs is usually accompanied by
- A. “crowding out”.
  - B. an increase in employment in secondary industry.
  - C. greater income equality.
  - D. a fall in inflation.
35. The Human Development Index includes which combination of indicators?
- A. GDP per capita at PPP, daily calorie supply and life expectancy.
  - B. Life expectancy, literacy/secondary school enrolment and GDP per capita at PPP.
  - C. Growth in GDP per capita at PPP, life expectancy and infant mortality.
  - D. GDP per capita at PPP, secondary school enrolment and infant mortality.

36.

<b>Country Rankings in the World</b>		
	<b>GDP per capita at PPP</b>	<b>HDI</b>
Country A	37	42
Country B	38	35

Using the information in the table above which **one** of the following statements is likely to be true?

- A. GDP per capita at PPP is the best indicator of economic development.
- B. Country B has higher illiteracy than Country A.
- C. Country A has invested more in human capital than Country B.
- D. The average citizen of Country B has a better standard of living than the average citizen of Country A.

37. Investment in education in developing countries is extremely important because
- A. the external benefits of education are less than the external costs.
  - B. education is a public good.
  - C. education is a merit good.
  - D. education is a free good.
38. Which **one** of the following is a reason for a country to provide tied aid to a less developed country (LDC)?
- A. To increase the international competitiveness of the LDC.
  - B. To give the LDC increased choice in the goods it can buy.
  - C. To increase the exports of the donor country.
  - D. To reduce the debt service ratio of the LDC.
39. Import Substitution can best be described as a strategy to
- A. replace imports from high cost countries with imports from low cost countries.
  - B. use tariffs and other forms of trade barriers to replace imports with domestic goods.
  - C. use export revenues to replace imported agricultural products with imported manufactured goods.
  - D. use tax incentives to attract multinational investment to replace inefficient domestic manufacturing.

40. The terms of trade for a country dependent on its coffee export revenues and imports of manufactured goods deteriorate when
- A. the price of coffee increases and the prices of imported manufactures fall.
  - B. the price of coffee falls and the price of imported manufactures rise.
  - C. it imports more than it exports.
  - D. it exports more than it imports.
-