

CAMBRIDGE INTERNATIONAL EXAMINATIONS
General Certificate of Education Advanced Subsidiary Level
and Advanced Level

ECONOMICS

9708/1

PAPER 1 Multiple Choice (Core)

OCTOBER/NOVEMBER SESSION 2002

1 hour

Additional materials:

Multiple Choice answer sheet

Soft clean eraser

Soft pencil (type B or HB is recommended)

TIME 1 hour

INSTRUCTIONS TO CANDIDATES

Do not open this booklet until you are told to do so.

Write your name, Centre number and candidate number on the answer sheet in the spaces provided unless this has already been done for you.

There are **thirty** questions in this paper. Answer **all** questions. For each question there are four possible answers, **A, B, C** and **D**. Choose the **one** you consider correct and record your choice in **soft pencil** on the separate answer sheet.

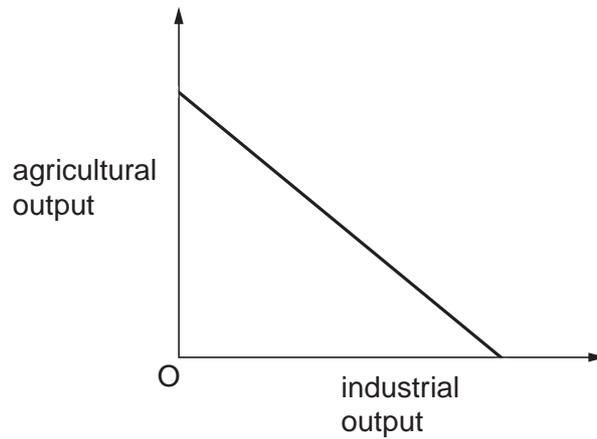
Read very carefully the instructions on the answer sheet.

INFORMATION FOR CANDIDATES

Each correct answer will score one mark. A mark will not be deducted for a wrong answer.

Any rough working should be done in this booklet.

- 1 The diagram shows an economy's production possibility curve.



Why does the curve slope downwards?

- A** Agriculture and industry are subject to decreasing returns to scale.
- B** Agriculture and industry are subject to increasing returns to scale.
- C** Resources are shared equally between industrial and agricultural production.
- D** Total resources available to the economy are limited.
- 2 Which of the following statements about trade unions is normative?
- A** Since trade unions exist to safeguard the interests of their members, they deserve the legal protection of the state.
- B** In countries where trade unions are strong, income distribution is more equal.
- C** Uneven trade union membership has resulted in a widening of the wage gap between different industries.
- D** In industries where trade unions are powerful, technical progress tends to be much slower.
- 3 Given a rate of interest of 10% per year, what is the opportunity cost to an individual of saving an additional \$100 in year 1?
- A** an increase in consumption of \$110 in year 2
- B** an increase in consumption of \$10 in year 2
- C** consumption of \$100 in year 1
- D** consumption of \$110 in year 1

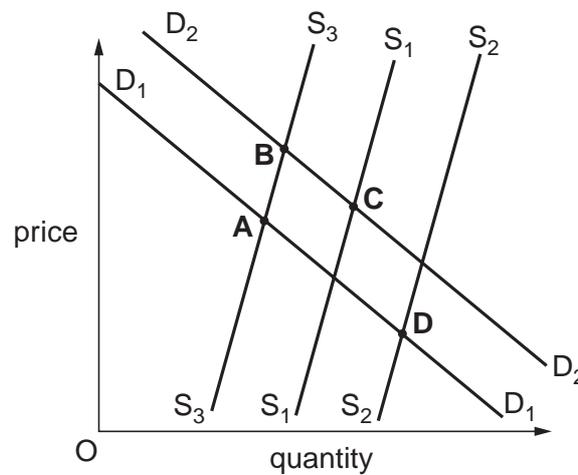
- 4 In the diagram LM is the production possibility curve of a country that has a comparative advantage in the production of good Y.



What might enable the country to consume the quantities of X and Y indicated by point R?

- A increased specialisation in the production of good X
 - B international trade
 - C a reduction in unemployment
 - D increased specialisation in the production of good Y
- 5 In the diagram, S_1 and D_1 are the initial supply and demand curves for tea.

Which point could represent the equilibrium position in the tea market following a failure in the coffee harvest of a major coffee producer?



- 6 A manufacturer progressively reduces the price of his product in an attempt to increase total revenue.

The table shows the outcome of this policy.

price (\$)	total revenue 000's (\$)
10	750
9	750
8	750

What is the price elasticity of demand for the product?

- A perfectly inelastic
 B relatively inelastic
 C perfectly elastic
 D unitary
- 7 A product is an inferior good with no close substitutes. It is also a complement to product X.

Which product matches the description of this product?

product	price elasticity of demand	income elasticity of demand	cross elasticity of demand with respect to the price of X
A	-2	+2	+1
B	-2	+2	-1
C	-0.5	-2	+1
D	-0.5	-2	-1

- 8 Which of the following combinations is most likely to result in the demand for a product being highly price elastic?

	number of close substitutes	% of income spent on product
A	large	large
B	large	small
C	small	large
D	small	small

- 9 Goods X and Y are complements.

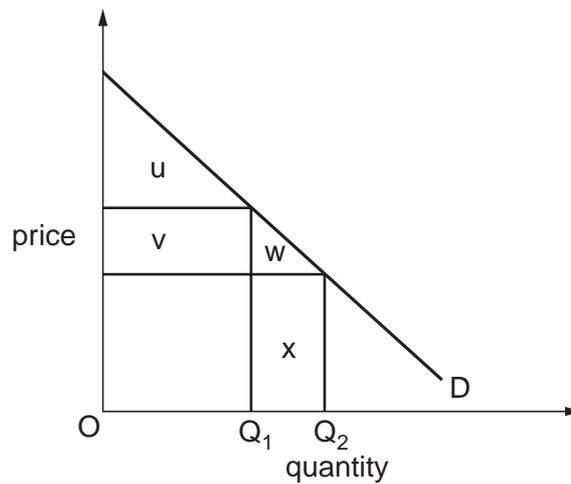
What will be the effect on the equilibrium price and quantity of good X of an increase in the price of good Y?

	<i>equilibrium price of X</i>	<i>equilibrium quantity of X</i>
A	decrease	decrease
B	decrease	increase
C	increase	decrease
D	increase	increase

- 10 What would cause a movement along an industry's supply curve?

- A** a change in the price of raw materials
- B** a change in the price of a substitute good
- C** an improvement in technology
- D** the imposition of a sales tax on the industry's product

- 11 In the diagram D is the demand curve for a commodity.

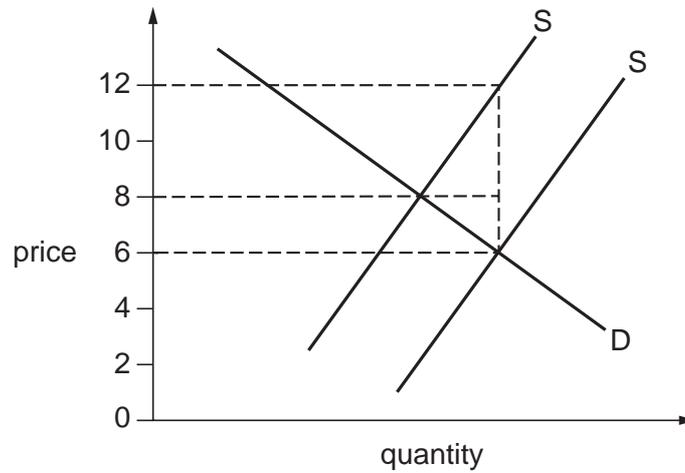


The quantity initially supplied is OQ_1 .

Which area measures the total additional amount consumers would be willing to pay for an increase equal to Q_1Q_2 in the quantity supplied?

- A** $u + v + w$
- B** w
- C** $w + x$
- D** v

- 12 The diagram shows the demand and supply curves of a commodity before and after a tax is removed.



What was the tax per unit of output and what is the price after the removal of the tax?

	tax per unit (\$)	price after the removal of the tax (\$)
A	6	6
B	6	8
C	4	6
D	4	8

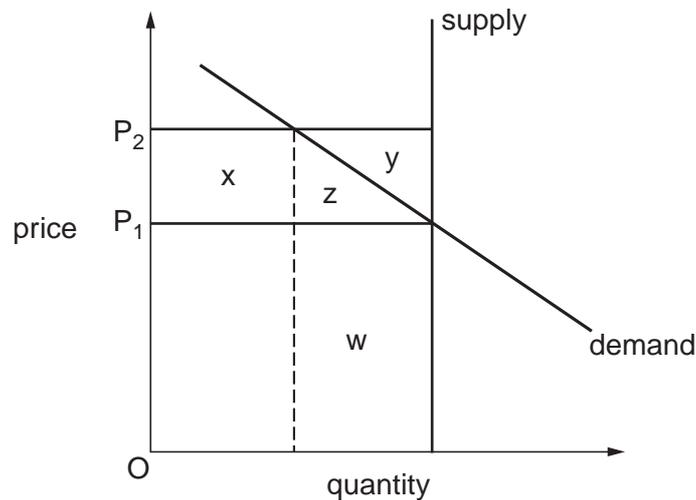
- 13 A manufacturer's ability to increase his output in the short run will be greater
- A** if labour is immobile.
 - B** if the product is perishable.
 - C** if there is spare capacity.
 - D** if unemployment is low.
- 14 Jones's well-being not only depends on the amounts of goods and services he himself consumes but is also directly affected by the amount of good X consumed by Smith. What does this illustrate?
- A** an externality
 - B** cross-elasticity of demand
 - C** joint demand
 - D** substitute goods

- 15 An Environment Agency requires companies to introduce more expensive but environmentally friendly and cleaner methods of production.

What effect will this have on the private, external and social costs of production?

	private costs	external costs	social costs
A	increase	decrease	decrease
B	increase	decrease	uncertain
C	decrease	increase	uncertain
D	decrease	increase	decrease

- 16 The diagram shows the market supply and demand curves for a particular agricultural product. The government allows the market price paid by consumers to be freely determined by demand and supply, but guarantees producers a price of OP_2 .



Which area in the diagram represents the total subsidy payments made by the government to producers?

- A** $w + y + z$
B $y + z$
C x
D $x + y + z$

17 Non-rivalry is a characteristic of which type of good?

- A an inferior good
- B a merit good
- C a private good
- D a public good

18 The table refers to a particular country.

<i>year</i>	<i>index of import prices (1995 = 100)</i>	<i>index of export prices (1995 = 100)</i>
1992	48.1	57.0
1996	122.4	120.8

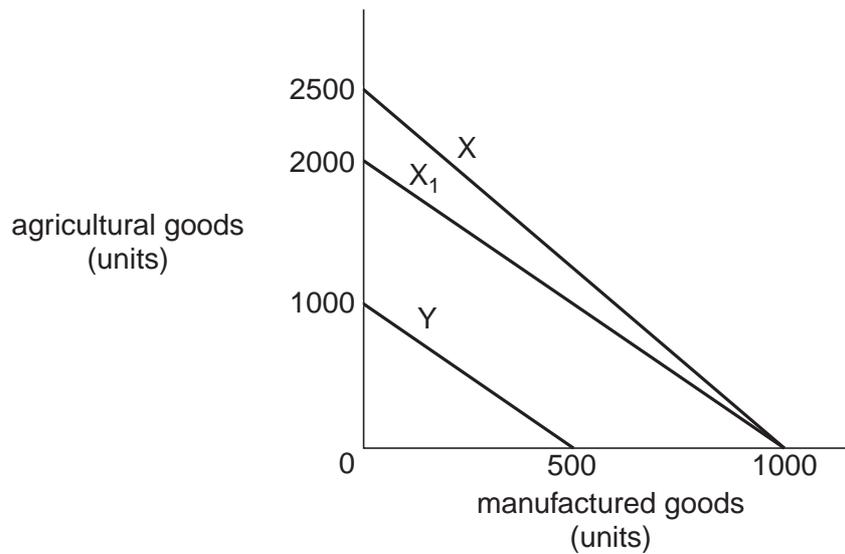
Which of the following statements about the period 1992 to 1996 is correct?

- A The balance of trade improved.
 - B The balance of payments worsened.
 - C The terms of trade worsened.
 - D The exchange rate appreciated.
- 19 Why might the establishment of a customs union lower economic welfare?
- A The exchange rate is realigned.
 - B Labour mobility is increased.
 - C Trade is created.
 - D Trade is diverted.
- 20 A developing country imposes a tariff to protect a new domestic industry.

Which argument would provide an acceptable economic case for this?

- A It is believed that the industry will always need government assistance to compete internationally.
- B It is believed that the industry will compete effectively when it achieves economies of scale.
- C The country wishes to reduce the rate of inflation.
- D The country wishes to lower its terms of trade.

- 21 The diagram represents the production possibilities of two economies X and Y.



As a result of soil erosion in economy X, the production possibility curve shifts from X to X₁.

According to the law of comparative advantage, what should country Y do following this change?

- A cease to trade with country X
 - B export agricultural goods to country X
 - C export manufactured goods to country X
 - D import both agricultural and manufactured goods from country X
- 22 What is likely to improve the visible trade balance of Mauritius but to worsen its invisible balance?
- A A Mauritian company sets up a subsidiary company in France.
 - B A US company builds a factory in the Mauritius to serve the African market.
 - C The Mauritian government removes import controls on semi-manufactured goods.
 - D The Mauritian government increases interest rates with a view to strengthening the exchange rate of the Mauritian rupee.
- 23 In an economy real national output increases more rapidly than the increase in employment.

What could account for this?

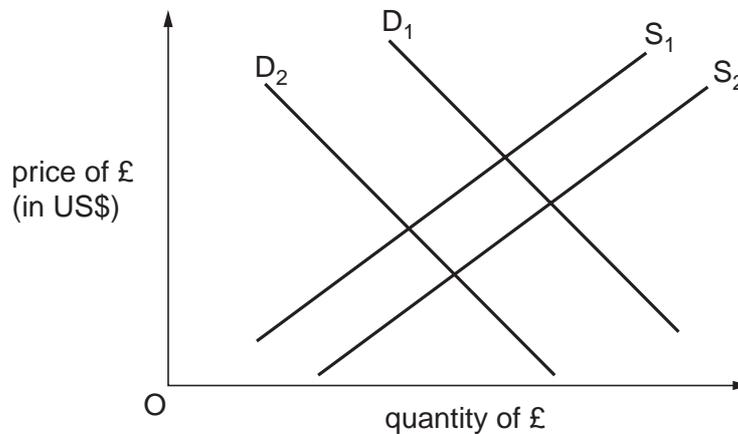
- A a decrease in the general price level
- B an improvement in the country's terms of trade
- C an increase in the size of the labour force
- D an increase in labour productivity

- 24 The table shows information about a country whose consumers spend their income on three commodities, *P*, *Q* and *R*.

<i>commodity</i>	<i>index of prices in year 1</i>	<i>index of prices in year 2</i>	<i>consumers' expenditure in year 1</i>
P	100	160	\$100 million
Q	100	80	\$300 million
R	100	100	\$100 million

Between year 1 and year 2 how has the general level of prices changed?

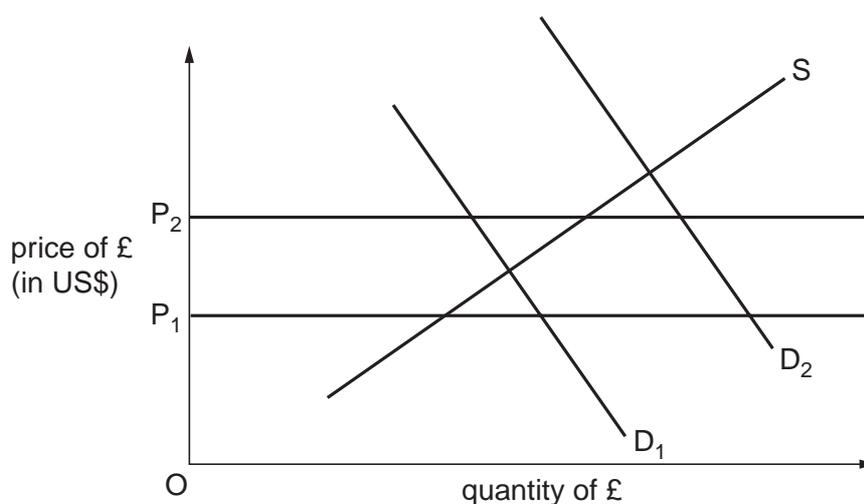
- A It has risen by 40%.
 B It has risen by 10%.
 C It has remained the same.
 D It has fallen by 5%.
- 25 In the diagram D_1 and S_1 are the initial demand and supply curves of the UK pound (£) on the foreign exchange markets.



What will cause the demand curve to shift to D_2 and the supply curve to S_2 ?

- A an appreciation of the pound
 B an increase in the price level in the US
 C an increase in incomes in the US
 D a decrease in UK interest rates

- 26 A representative basket of goods costs \$2500 in the United States. The same basket costs £2000 in the UK. What can be deduced from this?
- A The £ sterling is 25% over-valued.
 - B The £ sterling is 20% under-valued.
 - C The purchasing power parity exchange rate of the £ sterling is \$0.80 to the £.
 - D The purchasing power parity exchange rate of the £ sterling is \$1.25 to the £.
- 27 The British monetary authorities are committed to maintaining the exchange rate of the UK £ against the US dollar between P_1 and P_2 on the diagram.



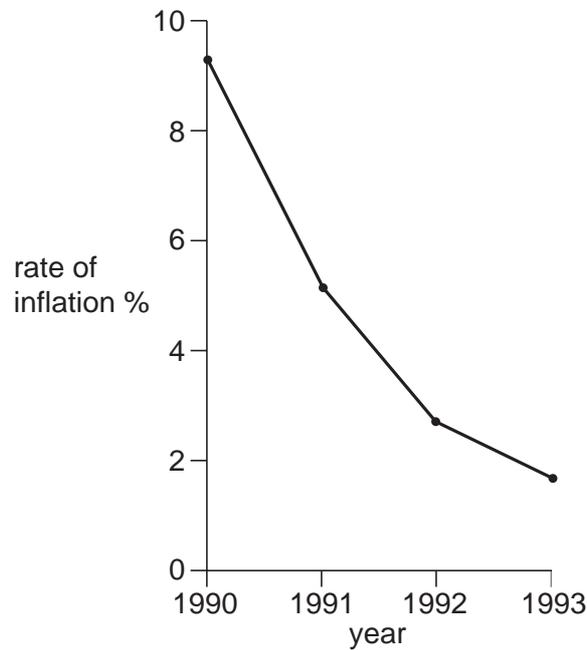
What might they do if demand changes from D_1 to D_2 ?

- A impose controls on UK investment overseas
 - B increase interest rates
 - C sell \$ out of foreign exchange reserves
 - D sell £ on the foreign exchange markets
- 28 What do the weights used to calculate a country's trade-weighted exchange rate reflect?
- A the relative importance of different goods in a country's balance of trade
 - B the relative size of a country's trade with different countries
 - C the relative importance of trade as a percentage of a country's GDP
 - D the relative size of a country's trade as a percentage of world trade

- 29 Which of the following combinations of changes indicates that a country is operating under a floating exchange rate?

	nominal exchange rate	foreign currency reserves
A	depreciates by 20%	decreases by \$1 billion
B	depreciates by 20%	unchanged
C	unchanged	unchanged
D	unchanged	decreases by \$1 billion

- 30 The diagram shows the annual rate of inflation in the UK between 1990 and 1993.



Which statement is true of the period 1990 to 1993?

- A** The cost of living fell.
- B** The price level rose.
- C** The retail price index fell.
- D** The value of money rose.