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UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS
General Certificate of Education Advanced Level

ECONOMICS **9708/03**

Paper 3 Multiple Choice (Extension)

October/November 2004

1 hour

Additional Materials: Multiple Choice Answer Sheet
Soft clean eraser
Soft pencil (type B or HB is recommended)

READ THESE INSTRUCTIONS FIRST

Write in soft pencil.
Do not use staples, paper clips, highlighters, glue or correction fluid.
Write your name, Centre number and candidate number on the answer sheet in the spaces provided unless this has been done for you.

There are **thirty** questions on 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 the instructions on the answer sheet very carefully.

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.

This document consists of **10** printed pages and **2** blank pages.

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1 A firm is operating in a perfectly competitive market.

What would ensure that it is both productively and allocatively efficient?

A It is in long-run equilibrium.

B It is maximising total revenue.

C It is producing where marginal revenue is equal to marginal cost.

D Long-run average costs are falling and sales are rising.

2 A consumer allocates his expenditure between three goods, X, Y and Z.

The table shows the prices of goods and the consumer's marginal utilities.

good	X	Y	Z
price ($)	20	15	10
marginal utility (units)	40	30	15

How should the consumer's expenditure be reallocated in order to maximise his utility?

	X	Y	Z
A	more	more	less
B	more	less	more
C	less	more	less
D	less	less	more

3 What explains the slope of an individual's demand curve for a normal good?

A market imperfections

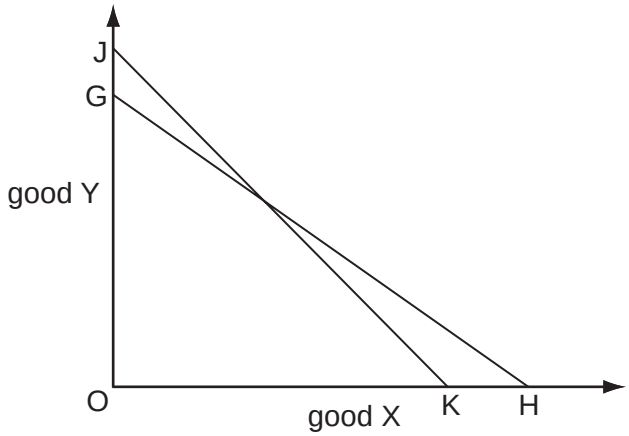
B the law of variable proportions

C diminishing returns

D diminishing marginal utility

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4 In the diagram a consumer's initial budget line is JK.



Assuming no change in the price of X, what could explain a shift in the consumer's budget line to GH?

	price of good Y	consumer's money income
A	decrease	decrease
B	decrease	increase
C	increase	decrease
D	increase	increase

5 Which statement explains why in the short run labour is subject to the law of diminishing returns?

A As additional workers are hired, output decreases.

B As employment increases, the capital-labour ratio falls.

C As employment increases, wage rates will have to be increased.

D As output expands, sooner or later diseconomies of scale will set in.

6 What will cause the demand curve for labour to shift to the right?

A a fall in the money wage rate

B a rise in real wages

C an increase in immigration

D an increase in labour productivity

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7 A worker responds to an increase in his hourly wage rate by reducing the number of hours he works per week.

What would explain this?

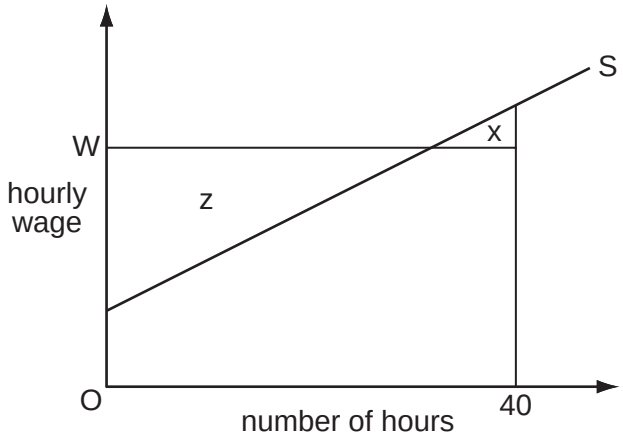
A The income effect of the wage rate increase outweighs the substitution effect.

B The opportunity cost of leisure has increased.

C The worker prefers leisure to work.

D The worker's supply of labour is wage inelastic.

8 The diagram shows an individual worker's supply curve of labour.



The hourly wage is OW and the worker is required to work a standard 40-hour week.

Which area measures the difference between the total amount the worker is paid per week and the minimum amount he would be willing to accept?

A x **B** z **C** x + z **D** z – x

9 A firm's long-run production function describes the relationship between

A the firm's output and the quantities of factor inputs employed.

B the firm's long-run average cost of production and the level of output.

C the firm's long-run average cost of production and the quantities of factor inputs employed.

D the prices of factor inputs and the quantities of factor inputs employed.

10 What is marginal cost?

A the difference between the total cost of producing *n* and *n*-1 units of output

B the difference between the average variable cost of producing *n* units and *n*-1 units of output

C the difference between the average total cost of producing *n* units and *n*-1 units of output

D the average variable cost of producing one more unit

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11 To maximise total revenue, up to which point should a monopolist increase output?

A where marginal revenue equals average revenue

B where marginal revenue is maximised

C where marginal revenue is zero

D where price elasticity of demand is zero

12 A monopolist finds that at his current level of output, marginal revenue is $2.00 and marginal cost is $2.50.

In order to increase his current level of profits, which strategy should the monopolist adopt?

	price	output
A	decrease	unchanged
B	decrease	increase
C	increase	decrease
D	increase	unchanged

13 A perfectly competitive firm is currently producing at a level of output where its marginal cost is above its average total cost but below the market price.

What would be the effect on price and output if the firm were to maximise its profit?

	effect on output	effect on price
A	decrease	increase
B	decrease	unchanged
C	increase	decrease
D	increase	unchanged

14 In which way does monopolistic competition differ from perfect competition?

A Average revenue exceeds average cost in long-run equilibrium.

B Barriers exist to the entry of new firms.

C Marginal revenue exceeds marginal cost in long-run equilibrium.

D Products are differentiated.

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15 A discriminating monopolist, faced with two demand curves of differing elasticity, will equate the combined marginal cost of production with

A marginal revenue in each market.

B average revenue in each market.

C the difference between the marginal revenues in the two markets.

D the difference between the average revenues in the two markets.

16 What might prevent an economy in which all firms are required to equate price and marginal cost from achieving allocative efficiency?

A differences in preferences between consumers

B divergences between private and social costs

C inequalities of income and wealth

D product differentiation

17 A good gives rise to external benefits and is produced under conditions of imperfect competition.

Which statement must be true?

A Consumers of the good are paying too low a price.

B Firms producing the good will make a loss.

C Output of the good is below the socially optimum level.

D Social costs of production exceed private costs.

18 Which of the following will directly result in an increase in China's Gross National Product?

A increased wages earned in a Malaysian-owned factory in China

B increased imports of goods and services

C increased outflows of net property income

D increased taxes on domestic expenditure

19 A country's GDP declines but the welfare of its population rises.

What could explain this?

A a fall in leisure time

B a fall in the size of the subsistence sector

C a rise in positive externalities

D a rise in the size of the population

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20 The accelerator principle refers to a relationship between investment and

A the level of GDP.

B changes in GDP.

C the level of interest rates.

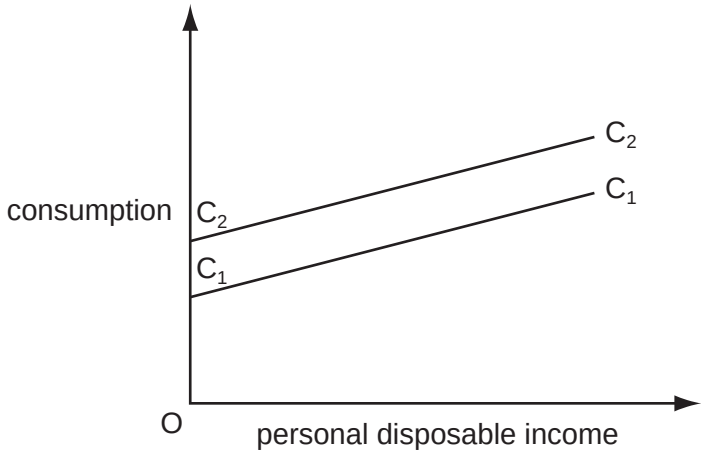
D changes in interest rates.

21 In a closed economy, households pay \$0.40 in tax on every \$1 increase in their gross income, and spend $^5/_6$ of every increase in their disposable income.

What is the value of the multiplier?

A 2 **B** $2^1/_2$ **C** 3 **D** 6

22 A country's initial consumption function is C_1C_1.



What will cause the consumption function to shift from C_1C_1 to C_2C_2?

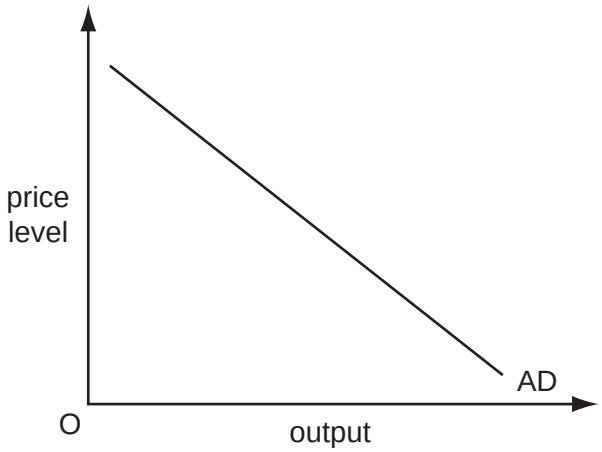
A an increase in wealth

B an increase in interest rates

C an increase in personal disposable income

D an increase in the expected future rates of income tax

23 The diagram shows an economy's aggregate demand curve.



What is held constant when drawing an AD curve?

A the exchange rate

B the money supply

C the rate of interest

D the price level

24 Assuming a constant income velocity of circulation of money, if real output grows by 5 %, and the money supply grows by 2 %, what will be the approximate change in the price level?

A –3 % **B** +2 % **C** +3 % **D** +7 %

25 What would cause an increase in the transactions demand for money?

A an increase in the rate of interest

B an increase in nominal national income

C a fall in the price of bonds

D an increase in unemployment

26 In the long run, productive potential in an economy grows at an average rate of 3 % per year. In a particular year actual growth is zero because of a fall in domestic consumption.

What is likely to occur?

A an increase in the rate of inflation

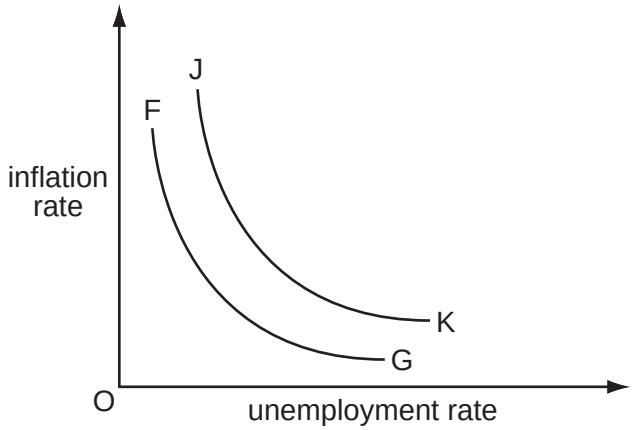
B an increase in the trade deficit

C an increase in unemployment

D a reduction in the government budget deficit

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27 The diagram shows the relationship between the rate of inflation and the rate of unemployment.



What would cause the curve FG to shift to JK?

A a decrease in government expenditure

B a fall in the level of employment

C an increase in the rate of change of wages

D the expectation of an increase in inflation

28 Why might a rise in domestic interest rates improve a country's balance of payments on current account?

A Domestic firms will become more competitive.

B It will result in a fall in the exchange rate.

C It will result in a reduction in spending.

D There will be an inflow of short-term capital.

29 Without any change in government policy, what will be the effect of an economic recession on tax revenue and on government expenditure?

	tax revenue	government expenditure
A	decrease	decrease
B	decrease	increase
C	increase	increase
D	increase	decrease

30 An economy has a low level of unemployment. The government increases its expenditure.

Which method of financing the additional expenditure is most likely to cause inflation?

A an increase in borrowing from the Central Bank

B an increase in income taxes

C an increase in sales of state assets to the non-bank public

D an issue of bonds to the non-bank public

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