UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS
General Certificate of Education Advanced Level

ECONOMICS **9708/03**

Paper 3 Multiple Choice (Extension)

October/November 2005

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 **11** printed pages and **1** blank page.

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1 What will happen if a firm is subsidised by an amount equivalent to the external benefits that it confers on the rest of society?

A Resource allocation will be improved.

B The firm will produce less.

C There will be a misallocation of resources.

D There will be no effect upon production.

2 The table shows the total utility that an individual derives from consuming different quantities of a good.

quantity of good (units)	total utility (units)
1	20
2	36
3	50
4	62
5	72
6	80

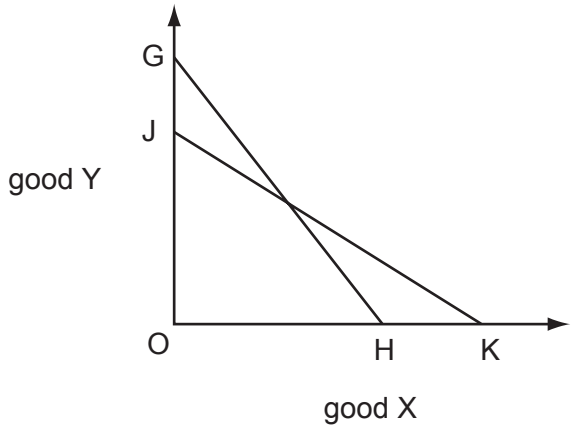
The individual's marginal utility of money is $1 = 2 units of utility.

What is the maximum quantity of the good that the individual will buy when its price is $6?

A 2 units **B** 3 units **C** 4 units **D** 5 units

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3 In the diagram a consumer's budget line shifts from GH to JK.



What **must** be true?

A The prices of both goods have changed.

B There has been no change in the consumer's real income.

C There has been no change in the consumer's money income.

D The price of good Y has increased relative to the price of good X.

4 The table shows the output of chairs at a factory when different numbers of workers are employed.

number of workers	0	1	2	3	4	5
number of chairs produced	0	7	17	29	38	42

Diminishing marginal returns to labour will set in when

A the second worker is employed.

B the third worker is employed.

C the fourth worker is employed.

D the fifth worker is employed.

5 What could cause a perfectly competitive firm's marginal revenue product of labour curve to shift to the right?

A an increase in wages

B a higher rate of sales tax

C an increase in labour supply

D a rise in the price of the final product

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6 What is likely to be the direction of the income and substitution effects of a wage rate increase on the number of hours workers will choose to work?

	income effect	substitution effect
A	decrease	decrease
B	decrease	increase
C	increase	decrease
D	increase	increase

7 A trade union seeks to increase the wages that a firm pays to its workers while at the same time preserving jobs.

What will strengthen the union's negotiating position?

A Capital and labour are perfect substitutes.

B The firm operates in a competitive market.

C The demand for the good produced by the firm is price-inelastic.

D The supply of labour to the firm is perfectly elastic.

8 The table below shows the relationship between total output and total costs of a firm given constant factor prices and fixed factor proportions.

output	costs ($)
100	80
200	180
300	300
400	440
500	600

It follows that, over this range of output, the firm experiences

A decreasing returns for output between 100 and 300 and increasing returns for output larger than 300.

B increasing returns for output between 100 and 300 and decreasing returns for output larger than 300.

C decreasing returns throughout.

D increasing returns throughout.

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9 Which item would **not** appear in a firm's financial accounts but would be included in an economist's calculation of the costs incurred by the firm?

A interest on bank loans used to purchase assets that have no alternative uses

B interest forgone on finance provided by the firm's owner

C depreciation

D rent

10 As a firm expands, what is **most** likely to prevent its long run average costs falling?

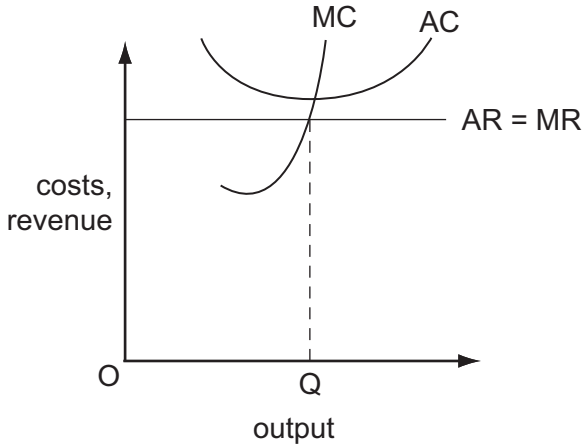
A increased interest rates on borrowing

B increased labour specialisation

C increased labour supervision costs

D substitution of capital for labour

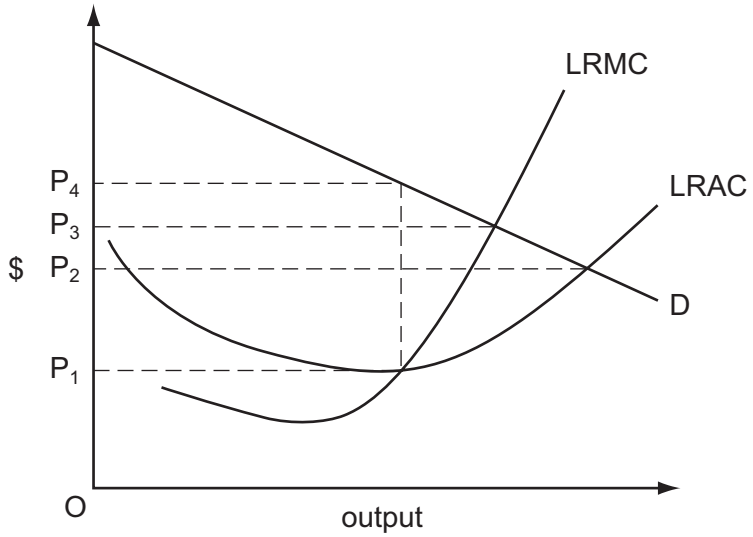
11 The diagram shows the position of a firm in a perfectly competitive industry.



What describes the position of the firm and the industry at output OQ?

	firm	industry
A	disequilibrium	disequilibrium
B	disequilibrium	equilibrium
C	equilibrium	disequilibrium
D	equilibrium	equilibrium

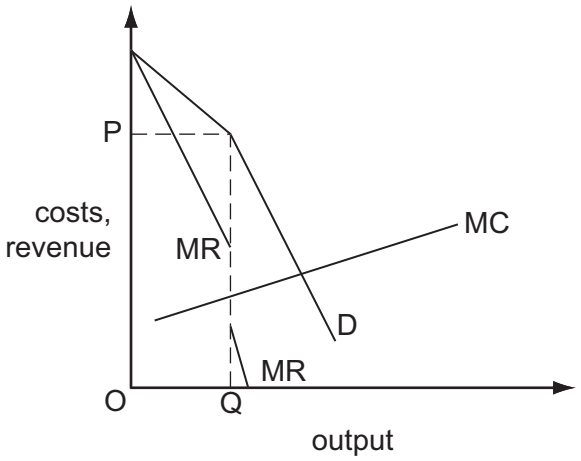
12 The diagram shows the demand curve and the long-run cost curves of a firm that operates in a perfectly contestable market.



Which price will the firm charge for its product?

A OP_1 **B** OP_2 **C** OP_3 **D** OP_4

13 The diagram shows a firm's cost and revenue curves.



Which features are associated with the situation shown in the diagram?

A economies of scale and allocative efficiency

B interdependence and allocative efficiency

C price rigidity and economies of scale

D price rigidity and interdependence

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14 The value of government benefits that households are able to claim currently depends on their level of income.

What would reduce the extent of the resulting poverty trap?

A a campaign to encourage more households to apply for the benefits to which they are entitled

B an increase in the level of government benefits

C a reduction in the rate at which benefits are withdrawn as a household's income increases

D the targeting of benefits on those in greatest need

15 Which area of skill possessed by the managers of government-owned enterprises in a planned economy is **less** relevant when industries are privatised?

A financial management

B marketing

C production targeting

D stock quality and control

16 Over a given period, money income in an economy increased by 8 %. Over the same period, prices rose on average by 6 %.

What can be deduced from this?

A Real income decreased by 2 %.

B The income velocity of circulation decreased by 2 %.

C The money supply increased by 14 %.

D The volume of output increased by 2 %.

17 According to monetarist theory, when will an increase in the money supply leave the level of output unchanged?

A when the increase in the money supply was not anticipated

B when the exchange rate is flexible

C when the liquidity trap is operative

D when there is an immediate adjustment to expectations about future price levels

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18 According to the accelerator theory, what determines this year's net investment?

A last year's consumption

B last year's output

C the change in last year's output

D the change in last year's investment

19 What is the value of the multiplier in an economy with no government where the marginal propensity to save is $\frac{1}{6}$, and the marginal propensity to import is $\frac{1}{3}$?

A $\frac{1}{2}$ **B** $1\frac{1}{2}$ **C** 2 **D** 3

20 An aggregate demand curve slopes downwards from left to right.

One reason for this is that a reduction in the average price level will lead to

A an increase in the real value of money balances.

B an increase in interest rates.

C a decline in the country's international competitiveness.

D the expectation of further price falls.

21 A government uses real personal disposable income as a measure of the standard of living.

What does this measure **not** take into account?

A the distribution of income

B the level of national income

C the size of the population

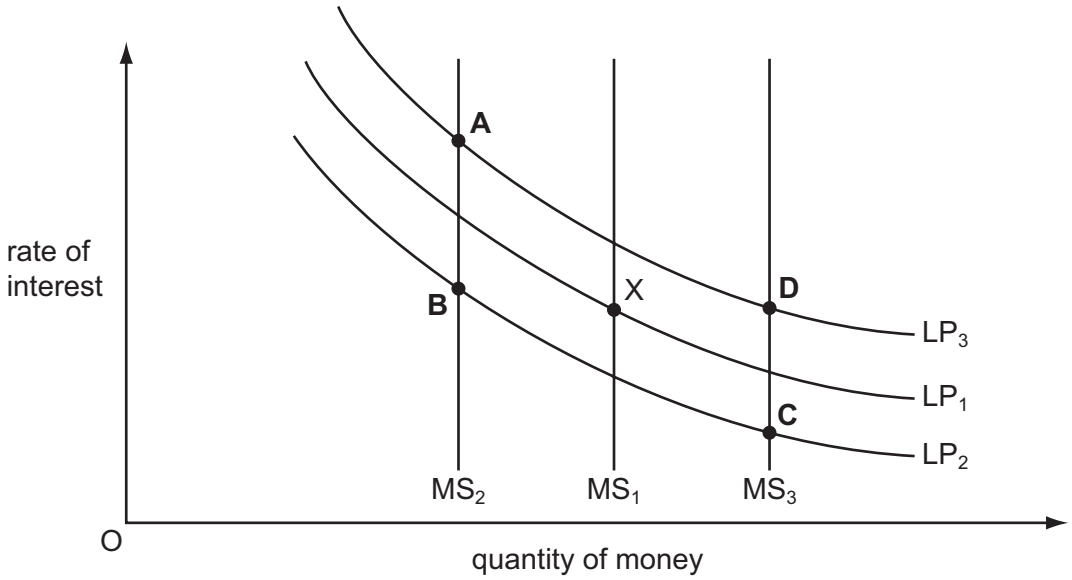
D the average price level

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22 The diagram shows three different levels of the supply of money (MS) and three different demand for money curves (LP). The initial equilibrium is at point X.

There is an increase in the level of money income and at the same time there is a contraction in bank credit.

Which point could be the new equilibrium point?



23 What is likely to increase GDP per worker in a developing economy?

A a decrease in the numbers engaged in subsistence agriculture

B a decrease in the numbers engaged in manufacturing

C an increase in the employment rate

D an increase in the population of working age

24 In an economy the long-run rate of growth of potential output is 2.5%.

What **must** happen in the short run if actual output grows at 5%?

A an increase in employment

B an increase in the rate of inflation

C a deterioration in the balance of trade

D an increase in labour productivity

25 All else remaining unchanged, which measure would be most likely to increase the natural rate of unemployment?

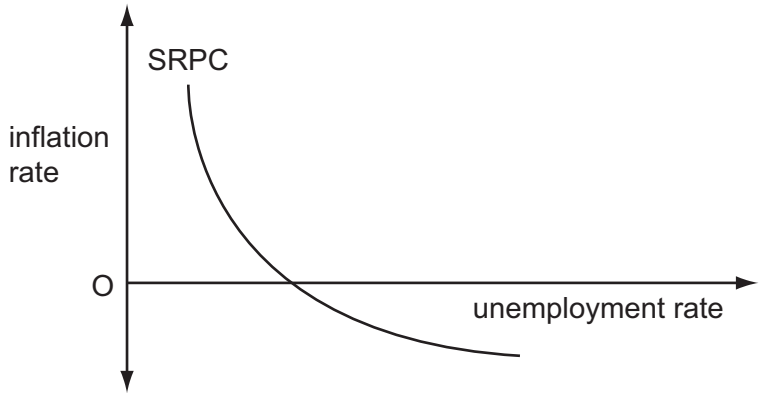
A an increase in expenditure on education and training

B an increase in the rate of unemployment benefits

C a reduction in the government's budget deficit

D a reduction in the general level of interest rates

26 The diagram shows an economy's short-run Phillips curve.



What is assumed to remain constant when drawing this curve?

A the average price level

B the money supply

C the exchange rate

D the natural rate of unemployment

27 The economy of a country is simultaneously experiencing a balance of payments deficit, a budget deficit, demand inflation and unemployment. The government decides to cut personal income taxes.

What does this suggest is its main macroeconomic objective?

A to improve the balance of payments position

B to reduce the budget deficit

C to reduce the level of unemployment

D to reduce the rate of inflation

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28 A developing economy attracts additional foreign direct investment.

What is likely to be the effect on its visible trade balance and on its invisibles balance?

	visible trade balance	invisibles balance
A	improve	improve
B	improve	worsen
C	worsen	improve
D	worsen	worsen

29 How do automatic stabilisers work?

A by reducing government deficits in times of recession

B by reducing fluctuations in disposable income

C by reducing fluctuations in the exchange rate

D by increasing the size of the investment multiplier

30 Which government policy will increase aggregate demand?

A raising indirect taxation

B reducing the budget surplus

C removing import quotas

D removing subsidies

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