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UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS
General Certificate of Education Advanced Level

ECONOMICS **9708/03**

Paper 3 Multiple Choice (Supplement)

October/November 2006

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 An economy is operating at a point on its production possibility curve.

What is true about the way the economy's resources are being used at this point?

	allocatively efficient	productively efficient	socially desirable
A	possibly	yes	yes
B	yes	possibly	possibly
C	possibly	yes	possibly
D	yes	possibly	yes

2 The diagram shows the marginal utility that an individual derives from a good at different levels of consumption.



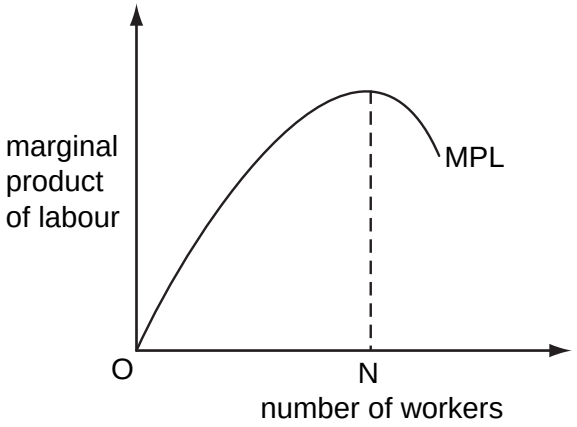
The utility he derives from the last $ he spends on every good is 2 units.

Assuming the marginal utility of money is constant, which quantity will he purchase if the price of the good is $20?

A 4 units **B** 5 units **C** 6 units **D** 7 units

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3 The diagram shows the marginal product of labour curve (MPL) for a firm.



Labour is the only variable factor and the firm pays its workers the market wage.

At the level of employment ON, which statement is correct?

A The firm is maximising its output.

B The firm is minimising its total costs.

C The firm is minimising its wage bill.

D The firm is minimising its marginal cost of production.

4 A firm working in perfect competition sells its product for $1. The table gives the average physical product with different numbers of workers.

number of workers	average physical product
1	20
2	18
3	16
4	14

Which wage rise would cause the firm to employ two instead of three workers?

A $8 to $10 **B** $10 to $14 **C** $14 to $18 **D** $16 to $18

5 An individual works 40 hours per week when the wage rate is $7 per hour. When the wage rate is increased to $9 per hour, the individual works 36 hours per week.

What explains the change in the number of hours worked?

A a negative income elasticity of demand for leisure

B an income effect outweighing a substitution effect

C an income effect reinforcing a substitution effect

D a zero income effect

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6 If a firm experiences an increase in its fixed costs, how will its average variable cost and its marginal cost be affected?

	average variable cost	marginal cost
A	rise	rise
B	rise	no change
C	no change	rise
D	no change	no change

7 Which of the following is an example of an external diseconomy?

A difficulties in co-ordinating activities in a large organisation

B difficulties in motivating workers in a large organisation

C higher transport costs as a firm's market expands

D increased traffic congestion as industries expand

8 Which small firms are most likely to survive for only a relatively short period?

A those producing components for large firms

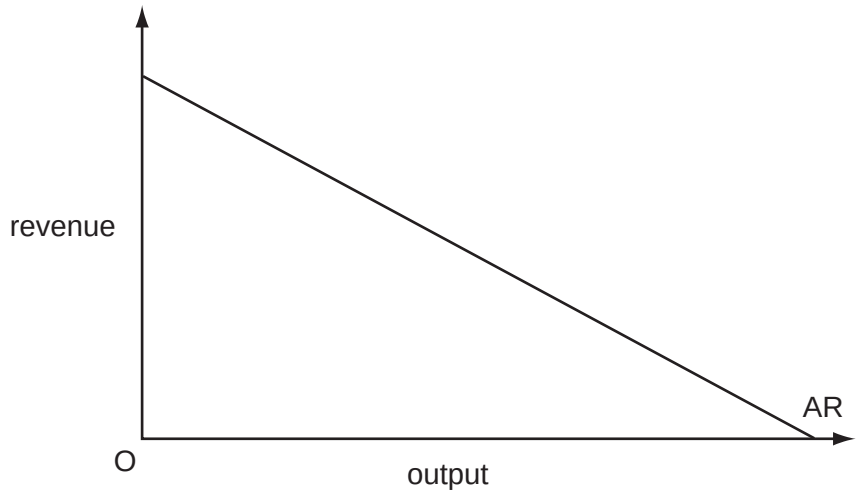
B those producing specialised products for small markets

C those engaged in activities with low start-up costs

D those engaged in activities that require flexibility in meeting customer requirements

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9 The diagram shows a firm's average revenue curve.



What can be deduced from the average revenue curve about the firm's total revenue as it increases output?

A It will rise continuously.

B It will fall continuously.

C It will rise initially then fall.

D It will fall initially then rise.

10 A firm decides to aim to maximise sales revenue rather than profits.

What is likely to be one of the consequences of this decision?

A an increase in the price of the firm's product

B a reduction in the price of the firm's shares

C a reduction in the firm's market share

D a reduction in the number employed by the firm

11 Which assumption is essential for a market to be contestable?

A The market is supplied by a large number of firms.

B Firms are free to enter and leave the market.

C Firms cannot earn abnormal profits in the short run.

D Firms produce differentiated goods.

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12 A firm wishes to acquire some of the consumer surplus its customers currently enjoy.

How might it achieve this?

A by charging a price that maximises revenue

B by introducing price discrimination

C by reducing operating costs

D by taking advantage of economies of scale

13 The price that a firm obtains for its product is not affected by the volume of goods that it produces.

What should it do to maximise profits?

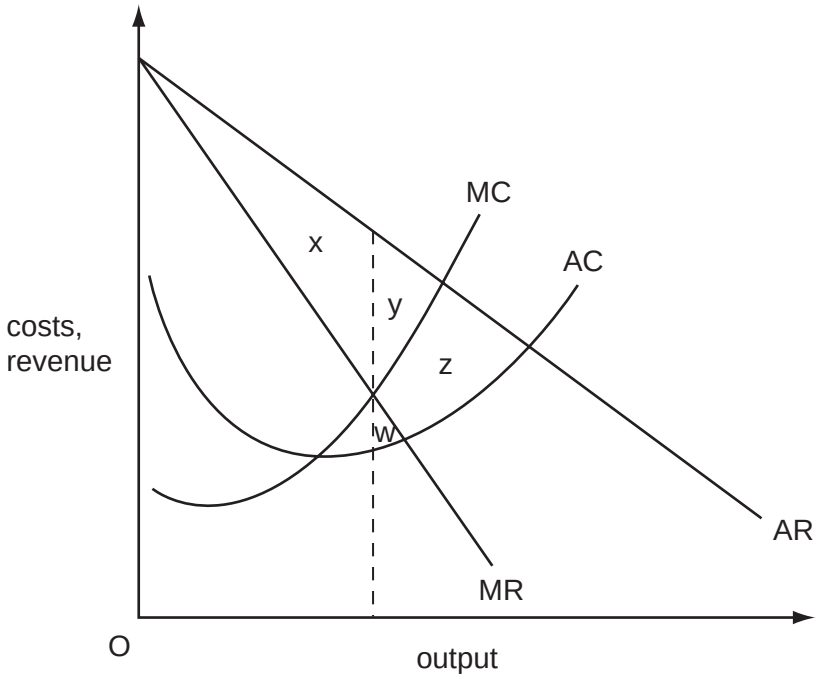
A produce until marginal cost equals price

B produce until average cost equals price

C produce until marginal revenue is zero

D sell as much as it can produce

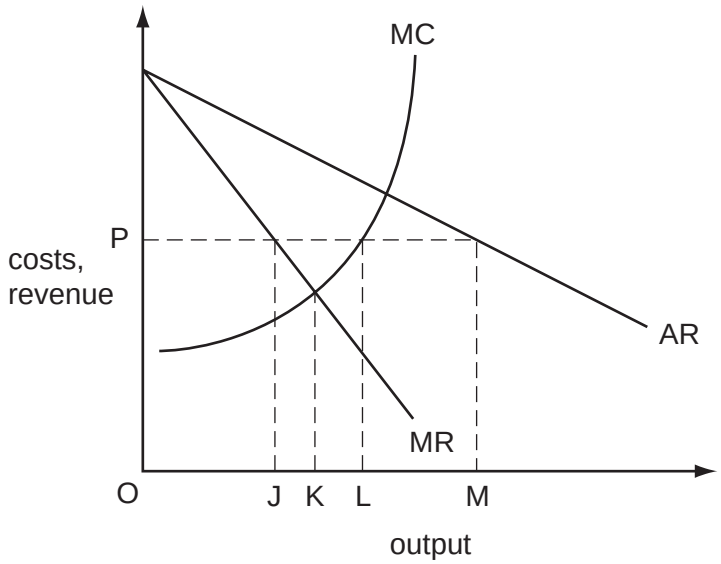
14 The diagram shows the cost and revenue curves of a profit-maximising monopolist.



Which area measures the deadweight loss arising from the exercise of monopoly power?

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

15 The diagram shows the initial cost and revenue curves of a monopoly supplier.



What will be the firm's profit-maximising level of output if the government fixes the price at OP?

A OJ **B** OK **C** OL **D** OM

16 Over a given period, the nominal value of a country's national income increased by 20 % and the rate of inflation was 10 %.

Which statement is correct?

A There was an increase in the volume of output.

B There was an increase in the income velocity of circulation.

C There was a reduction in the demand for money.

D The country's money supply increased by 10 %.

17 The table shows data on a country's gross national product at market prices and on domestic spending.

	year 1 ($m)	year 2 ($m)	year 3 ($m)
GNP at market prices	400	480	560
private consumption	200	260	300
government consumption	120	120	140
gross investment	90	80	130

In which of these years will the country be faced with a deficit on the current account of the balance of payments?

	year 1	year 2	year 3
A	✓	✗	✗
B	✗	✓	✓
C	✓	✗	✓
D	✗	✓	✗

18 Which statement is consistent with a Keynesian view of the workings of the macroeconomy?

A Recessions can result from fluctuations in private investment expenditure.

B Interest rates move to ensure continuous equality between savings and investment plans.

C Money wages in the economy in the short run are perfectly flexible.

D There is no short-run trade off between inflation and unemployment.

19 What would explain why an economy's short-run aggregate supply curve is upward sloping?

A a constant price level

B constant money wages

C diseconomies of scale

D economies of scale

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20 The national income is initially in equilibrium.

If there were a **decrease** in exports, which change of equivalent value would restore national income to its initial equilibrium level?

A an increase in investment

B an increase in saving

C a reduction in government expenditure on goods and services

D a reduction in taxation

21 In a closed economy with no government C = 30 + 0.8 Y and I = 50, where C is consumption, Y is income and I is investment.

What is the equilibrium level of income?

A 64 **B** 80 **C** 250 **D** 400

22 According to Keynesian theory, what would cause individuals to want to hold more idle money balances?

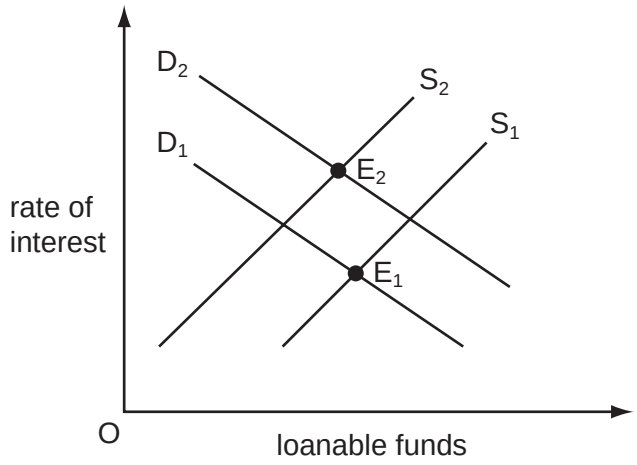
A an increase in bond prices

B an increase in the rate of interest

C an increase in the rate of inflation

D an increase in the level of output

23 The diagram shows the market for loanable funds.



Which changes could cause the equilibrium to move from E_1 to E_2?

A an increase in bank lending and a depletion of natural resources

B an increase in the propensity to save and the discovery of new mineral deposits

C advances in technology and a reduction in the propensity to save

D a decline in business confidence and a decrease in bank lending

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24 Which of the following are characteristics of most developing economies?

	high government debt: GDP ratio	a high average propensity to save
A	✗	✗
B	✗	✓
C	✓	✓
D	✓	✗

25 What would cause an expansionary fiscal policy to be relatively ineffective?

A a low marginal propensity to import

B a fixed exchange rate

C a fixed money supply

D large-scale unemployment of resources

26 An economy has unemployed resources and a flexible exchange rate. It lowers interest rates below the level prevailing in other countries.

What will be the likely effect on the level of domestic demand for goods and services and on the demand for the country's exports?

	domestic demand	export demand
A	increase	increase
B	increase	decrease
C	decrease	decrease
D	decrease	increase

27 In an economy the proportion of the working age population in employment increases from 70 % to 80 %.

What is likely to be the effect on labour productivity and on GDP per head?

	labour productivity	GDP per head
A	increase	increase
B	increase	decrease
C	decrease	increase
D	decrease	decrease

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28 What would be most likely to result in an increase in an economy's long-run rate of growth of potential output?

A an appreciation of the currency

B an increase in interest rates

C an increase in the government's budget deficit

D an increase in the level of private investment

29 An economy with a floating exchange rate is in recession and at the same time has a deficit on the current account of its balance of payments.

Which policy combination would be most likely to help with both of these problems?

	interest rates	tax rates
A	decrease	unchanged
B	decrease	increase
C	increase	unchanged
D	increase	increase

30 What does a government need to do to maintain a balanced budget?

A allow automatic stabilisers to work

B keep tax rates and benefit rates unchanged

C raise taxes in a slump and lower taxes in a boom

D aim to keep output close to the full employment level

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