

**CAMBRIDGE INTERNATIONAL EXAMINATIONS**  
**General Certificate of Education Advanced Level**

**ECONOMICS**

**9708/3**

**PAPER 3 Multiple Choice (Extension)**

**OCTOBER/NOVEMBER 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.

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**This question paper consists of 12 printed pages.**



- 1 New technology makes it possible to produce more of a good at every given price.

What effect will this have on equilibrium price and output in a competitive industry?

	price	output
<b>A</b>	decrease	decrease
<b>B</b>	decrease	increase
<b>C</b>	increase	decrease
<b>D</b>	increase	increase

- 2 The table shows the marginal utility that a consumer obtains from consuming successive units of good X.

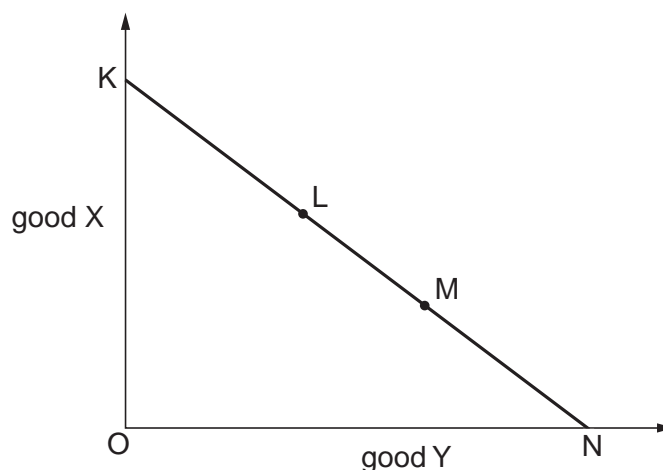
quantity (units)	mu (units of utility)
1	10
2	18
3	24
4	28
5	30
6	31

The price of good X is \$4.

What additional information is needed to determine the quantity of X that the consumer will purchase?

- A** the consumer's income elasticity of demand for good X
- B** the consumer's price elasticity of demand for good X
- C** the marginal utility of money to the consumer
- D** the marginal utility that the consumer obtains from substitute goods

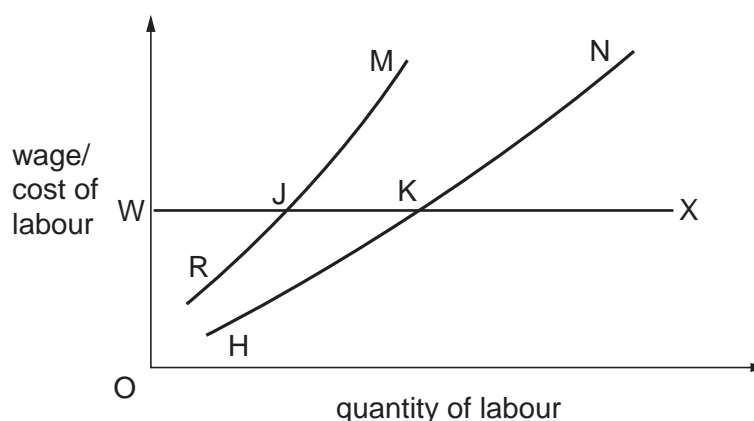
- 3 In the diagram, KN is a budget line showing the different combinations of two normal goods, X and Y, that a consumer is able to purchase. A consumer initially chooses point L on the budget line.



In a subsequent period, the consumer chooses the combination of X and Y shown by point M.

What could explain this change?

- A a change in the consumer's preferences
  - B an increase in the consumer's income and an increase in the price of Y
  - C a reduction in the consumer's income
  - D a reduction in the consumer's income and a reduction in the price of X
- 4 In the diagram, HN is the initial supply of labour curve faced by a firm, and RM is its initial marginal cost of labour curve.



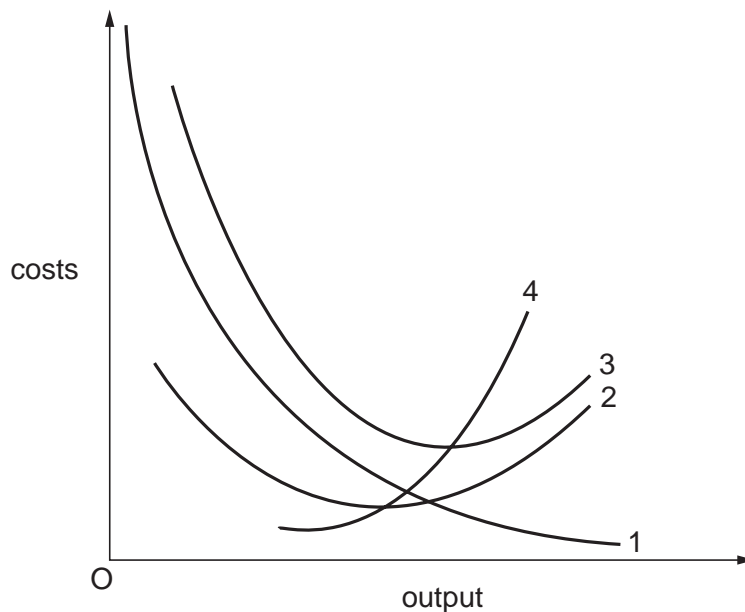
What will be the firm's new labour supply curve, if the workers join a trade union and achieve a union negotiated wage, OW?

- A RJX
- B HKX
- C WJM
- D WKN

- 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 offsetting a substitution effect
  - C an income effect reinforcing a substitution effect
  - D a zero income effect
- 6 Which of the following is a financial economy of scale?
- A less risk due to diversification
  - B lower costs in raising capital
  - C lower costs of marketing
  - D lower variable costs of production
- 7 The diagram shows the short-run cost curves of a firm.

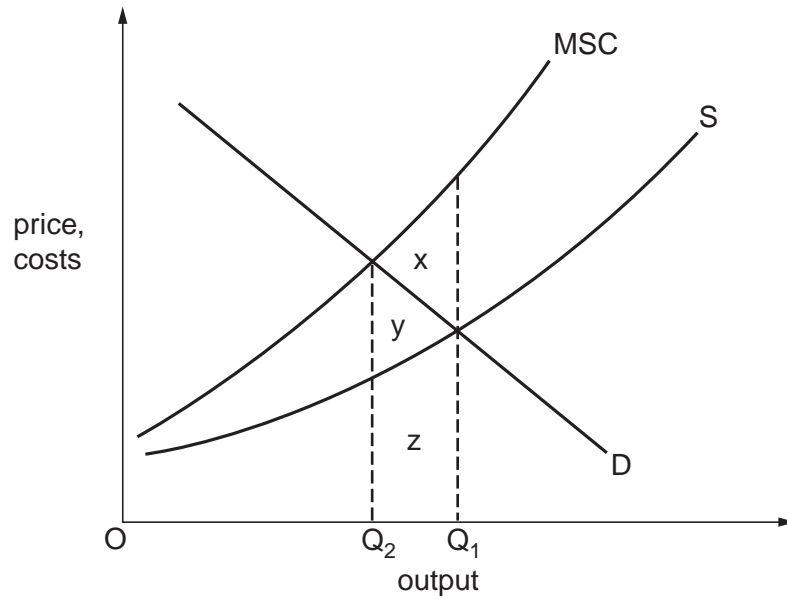


Which statement is correct?

- A Curve 1 is the average fixed cost curve.
- B Curve 2 is the marginal cost curve.
- C Curve 3 is the average variable cost curve.
- D Curve 4 is the average total cost curve.

- 8 In which of the following market situations will a firm take account of the reactions of its competitors before deciding to cut its price?
- A monopoly
  - B monopolistic competition
  - C oligopoly
  - D perfect competition
- 9 If a profit-maximising company believes that the market price of a good will not be affected by its own output, it will
- 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.
- 10 Which of the following items would **not** appear in a firm's financial accounts but would be included in an economist's calculation of the cost 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
- 11 When is allocative efficiency achieved in an economy?
- A when nobody can become better off without somebody else becoming worse off
  - B when the economy is operating at its natural rate of unemployment
  - C when the level of social costs is minimised
  - D when the rate of economic growth is maximised

- 12 The diagram shows the supply and demand curves for a good. The curve labelled MSC shows the marginal social cost of producing the good.



Which area measures the net welfare gain to society from reducing output from  $OQ_1$  to  $OQ_2$ ?

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

- 13 The table shows the marginal tax rates paid by a country's taxpayers at different levels of income.

income	tax rate
first \$4000	zero
\$4001 – \$20 000	20%
above \$20 000	40%

Which of the following correctly describes this tax?

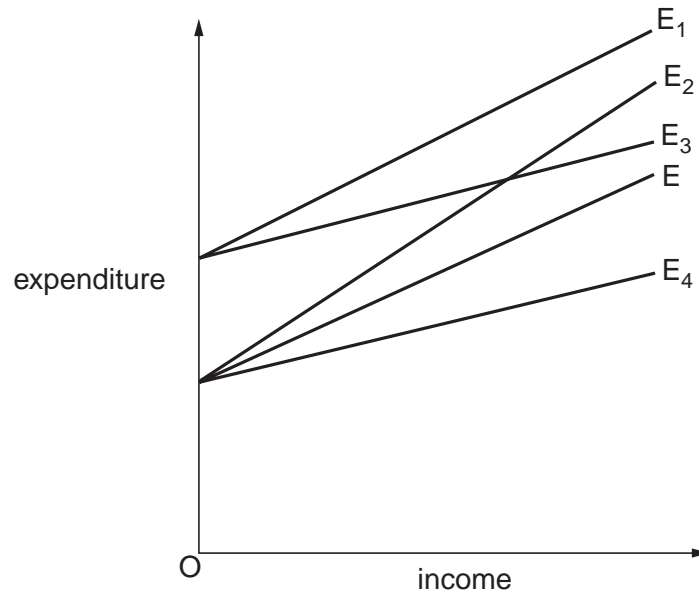
- A** It is regressive over the entire range of income.  
**B** It is proportional over the income range \$4001 – \$20 000.  
**C** It is proportional over the range of income above \$20 000.  
**D** It is progressive over the range of income above \$4000.

- 14 Assuming that all indexes have 1990 as 100, the national income figures for 2000 at 1990 prices may be obtained by multiplying 2000 national income at current prices by
- A  $\frac{\text{the index for 2000 prices}}{\text{the index for 1990 prices}}$
  - B  $\frac{\text{the index for 2000 prices}}{\text{the index for 1990 output}}$
  - C  $\frac{\text{the index for 1990 output}}{\text{the index for 2000 output}}$
  - D  $\frac{\text{the index for 1990 prices}}{\text{the index for 2000 prices}}$
- 15 During a year, a country's national income in money terms increased by 6%, prices increased by 4% and total population increased by 2%.

What was the approximate change in real income per head?

- A a decrease of 2%
- B nil
- C an increase of 2%
- D an increase of 4%

- 16 The diagram shows a number of expenditure functions. The original expenditure function is shown by E.

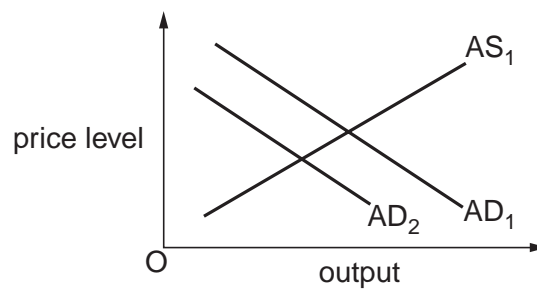


The government announces an increase in government expenditure on goods and services and increases the standard rate of income tax.

Which line shows the new expenditure function resulting from these changes?

- A**  $E_1$       **B**  $E_2$       **C**  $E_3$       **D**  $E_4$

- 17 In the diagram  $AD_1$  and  $AS_1$  are an economy's initial aggregate demand and aggregate supply curves.

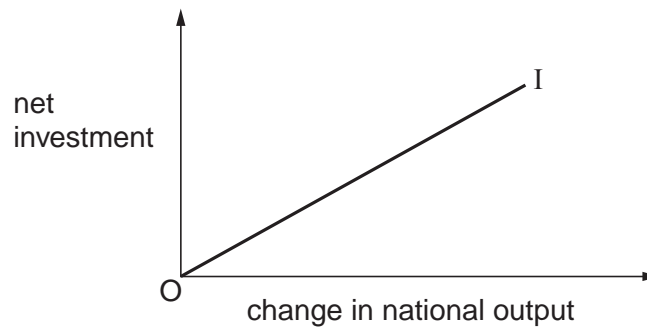


What will cause the aggregate demand curve to shift to  $AD_2$ ?

- A** a depreciation of the currency  
**B** an increase in the price level  
**C** an increase in the real wage  
**D** a reduction in the money supply



- 18 One of the reasons why a country's aggregate demand curve slopes downwards is that a fall in the average price level
- A leads to an increase in interest rates.
  - B reduces the real value of money balances.
  - C makes the country's goods cheaper relative to foreign goods.
  - D leads to the expectation of further price falls.
- 19 In the diagram, the curve I depicts the accelerator relationship between net investment and the change in national output.



What does the slope of the curve measure?

- A the capital-output ratio
  - B the marginal propensity to invest
  - C the marginal propensity to save
  - D the multiplier
- 20 In a closed economy, the full employment level of income is \$90 million,  $C = \frac{2}{3}Y$  and  $I = \$ (40 - 3r)$  million, where  $C$  = consumption,  $Y$  = income,  $I$  = investment and  $r$  = the rate of interest.

If planned government expenditure is \$20 million, what rate of interest would be required for there to be full employment?

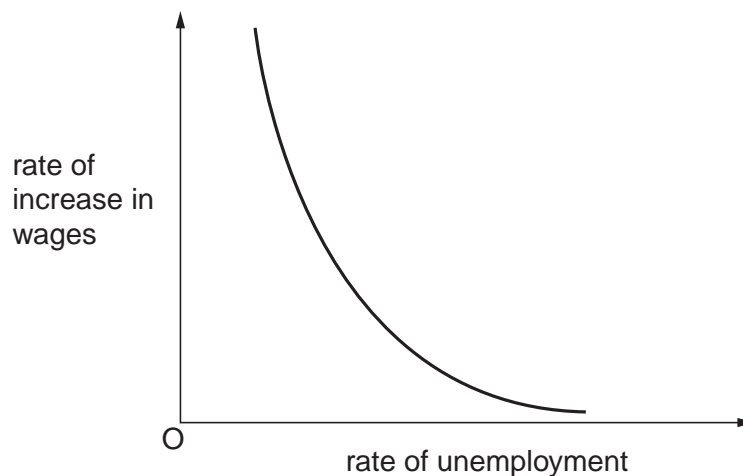
- A 10% per annum
- B 12% per annum
- C 14% per annum
- D 16% per annum

- 21** A 6% increase in the money supply leads to a 4% increase in the level of money income.

What can be deduced from this?

- A** There has been an increase in interest rates.
  - B** There has been a decrease in the level of output.
  - C** There has been a decrease in the velocity of circulation.
  - D** The price level has increased by 2%.
- 22** What would result in a reduction in the volume of bank deposits?
- A** an increase in the public's desire to hold cash
  - B** an increase in government expenditure financed by borrowing from the central bank
  - C** a reduction in the proportion of their deposits that banks hold in cash
  - D** an open market purchase of securities by the central bank
- 23** If a country has a surplus in its balance of payments, all else being equal, what is likely to happen to its money supply?
- A** It will fall, because more of its goods were purchased by foreign consumers than by consumers at home.
  - B** It will remain unchanged, because its exports are bought with foreign currency.
  - C** It will remain unchanged, because the surplus is automatically offset by a loan for the deficit countries.
  - D** It will rise, because the foreign currency received for exports will be exchanged for domestic currency.
- 24** In a closed economy with no government the full employment level of output is \$25 million, the actual level of output is \$20 million, and the marginal propensity to consume is  $\frac{4}{5}$ . What is the size of the deflationary gap?
- A** \$1 million      **B** \$4 million      **C** \$5 million      **D** \$16 million
- 25** Which of the following is likely to intensify a recession following an initial fall in aggregate demand?
- A** Unemployment benefits increase as the level of activity falls.
  - B** The yield from income tax falls as incomes fall.
  - C** Firms maintain a constant ratio of stocks to sales.
  - D** Interest rates fall as the demand for money falls.

- 26** What would explain why the prices of the primary commodities produced by less developed countries fluctuate widely from year to year?
- A** the development of artificial substitutes for natural products
  - B** the introduction of more capital-intensive methods of production by mineral producers
  - C** inelasticity of both the supply and demand for these products
  - D** improvements in agricultural productivity
- 27** Which of the following policies is specifically designed to reduce the level of structural unemployment?
- A** a reduction in interest rates
  - B** a reduction in the level of direct taxation
  - C** the provision of retraining schemes
  - D** an increase in the level of state benefit paid to the unemployed
- 28** The diagram shows the relationship between the rate of increase in wages and the rate of unemployment.



Which of the following would be likely to cause the curve in the diagram to shift upwards and to the right?

- A** a reduction in regional differences in unemployment rates
- B** a reduction in the proportion of the workforce belonging to trade unions
- C** an increase in the unemployment rate
- D** the expectation of a higher rate of inflation

- 29 Which of the following is most likely to lead to an increase in a developing country's long-run rate of growth of income per head?
- A a higher birth rate
  - B a higher saving ratio
  - C the imposition of import controls
  - D an increase in government spending on defence
- 30 Which of the following is **not** an automatic stabiliser?
- A income tax
  - B profits tax
  - C state retirement pension
  - D unemployment benefit