1. The natural rate of unemployment in an economy is 5%. What will happen if a government persists in trying to achieve a target rate of unemployment of 3% by expansionary monetary policy?
   I. **an accelerating rate of inflation**
   II. a diminishing rate of inflation
   III. a high but constant rate of inflation
   IV. a negative rate of inflation
   V. none of the above

2. In a closed economy, the marginal propensity to save is 0.4 and the marginal propensity to pay taxes is also 0.1. These values are constant and do not vary with the level of income. What will be the increase in national income if there is an injection of 100 million into the circular flow?
   I. 1000 million
   II. 500 million
   III. **200 million**
   IV. 100 million
   V. 50 million

3. Other things being equal, what is most likely to be reduced by falling labour productivity
   I. the balance of trade deficit
   II. **the internal value of money**
   III. the level of unemployment
   IV. the rate of domestic inflation
   V. none of the above

4. The table shows a country's consumer prices index (CPI) for March and April 2018.

	CPI
March 2018	151.3
April 2018	148.6

   Which statement correctly describes what happened between these two months?

   I. There was a decrease in the annual rate of inflation.
   II. There was a decrease in real interest rates.
   III. **There was an increase in the purchasing power of money.**
   IV. There was an increase in the standard of living.
   V. None of the above

5. A country has a deficit on the current account of its balance of payments. What might help the country to reduce its deficit?
   I. a decrease in its rate of income tax
   II. a decrease in its tariffs
   III. an increase in its level of employment
   IV. <u>an increase in its subsidies to exporters</u>
   V. none of the above

6. What will be the immediate effect of a devaluation of an economy's foreign exchange rate?
   I. The price of imported goods in the domestic currency will fall.
   II. <u>The price of imported goods in the domestic currency will rise.</u>
   III. The price of imported goods in the foreign currency will fall.
   IV. The price of imported goods in the foreign currency will rise.
   V. None of the above

7. A country replaces a floating exchange rate system with a managed floating exchange rate system. Which statement is correct?
   I. <u>Its central bank would have to intervene more frequently in the foreign exchange market.</u>
   II. Its central bank would need to hold fewer foreign currency reserves.
   III. The value of its currency would be determined by its major trading partners.
   IV. The value of its currency would be determined by the value of the US dollar.
   V. None of the above

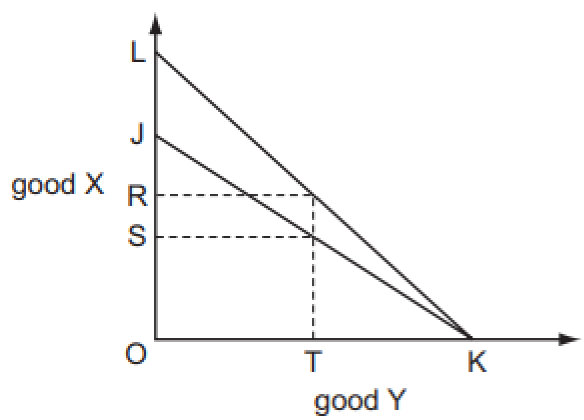
8. A country's terms of trade changed from 100 to 95. What is most likely to have caused this change?
   I. <u>a depreciation of the country's currency</u>
   II. a reduction in import tariffs
   III. a rise in the price of exported goods
   IV. an improvement in the balance of trade
   V. none of the above

9. In 2020 it was reported that there were concerns when a government kept interest rates very low despite a threat of inflation. Why might the government's policy have caused concern at this time?
   I. <u>Low interest rates encourage increased consumer spending.</u>
   II. Low interest rates lead to increased spending on capital equipment.
   III. Low interest rates mean exports will increase.
   IV. Low interest rates will cause an increase in the exchange rate.
   V. None of the above

10. Legal reforms to reduce the power of trade unions have reduced inflationary pressures in many countries. Of which policy is this an example?
    I. monetary policy
    II. demand side policy
    III. fiscal policy
    IV. <u>supply side policy</u>
    V. none of the above

11. What is the most likely aim of a government that increases the level of tariffs on imported manufactured goods?
    I. a fall in interest rates
    II. a fall in the exchange rate
    III. <u>a rise in domestic employment</u>
    IV. a rise in the general price level
    V. none of the above

12. In the diagram, JK is a country's production possibility curve. LK is its trading possibility curve which shows possible combinations of good X and good Y after specialising in the product in which it has comparative advantage, and then trading this product.



The country consumes OR of good X and OT of good Y.

Which quantities of goods X and Y does it produce?

	Good X	Good Y
I	JS	OT
II	OS	OT
III	RS	TK
<u>IV</u>	**<u>zero</u>**	**<u>OK</u>**
V	OT	zero

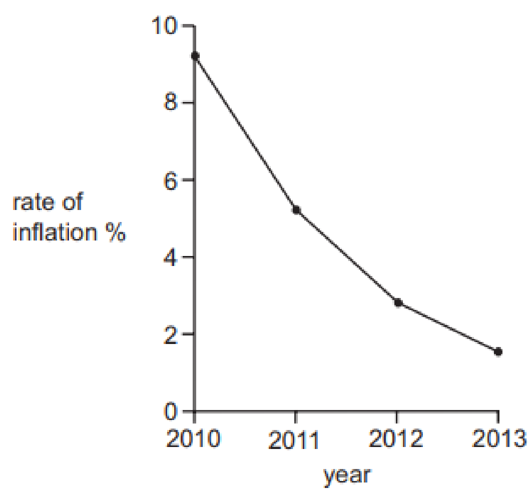
13. A country's terms of trade increased from the base year value of 100 to 120 in the following year. What changes in export prices and import prices would have caused this?

	export prices	import prices
I	decreased 10%	increased 10%
II	increased 10%	decreased 10%
III	**increased 20%**	**unchanged**
IV	unchanged	decreased 20%
V	increased 20%	decreased 20%

14. In 2020 the US$ exchanged for 181.6 Sri Lankan Rupee. In 2021 the US$ exchanged for 176.1 Sri Lankan Rupee.
What would be expected to rise for the United States (US) as a result of this change?
    I. the level of unemployment
    II. the price of US exports sold in Sri Lanka
    III. the rate of imported inflation
    IV. the volume of imports
    V. none of the above

15. When is a balance of trade deficit likely to be considered a particularly difficult problem for a country?
    I. when the imported goods are identical to domestic products
    II. when the imported goods are items of capital equipment
    III. when the imported goods are the raw material for exports
    IV. when the imported goods are to cover a temporary shortage
    V. None of the above

16. The diagram shows the annual rate of inflation in a country between 2010 and 2013.



Which statement about the period 2010 to 2013 is correct?
    I. The cost of living fell.
    II. The price level rose.
    III. The Retail Prices Index fell.
    IV. The value of money rose.
    V. None of the above

17. What will be the probable effect of an increase in indirect taxes on demand-pull inflation and on cost-push inflation?

	demand-pull inflation	cost-push inflation
I	increase	increase
II	increase	decrease
III	decrease	decrease
IV	**decrease**	**increase**
V	Unchanged	decrease

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

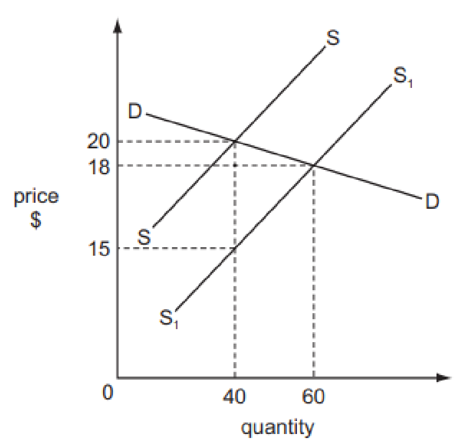
income	tax rate
first $4000	zero
$4001 - $20 000	20 %
above $20 000	40 %

What correctly describes this tax?

I. It is regressive over the entire range of income.
II. It is proportional over the income range $4001 - $20000.
III. It is proportional over the range of income above $20000.
IV. It is progressive over the range of income above $4000
V. None of the above

19. A tax on a product is removed causing supply to increase from SS to S1S1 as shown in the diagram
What effect does the move have on government tax revenue and consumer expenditure?

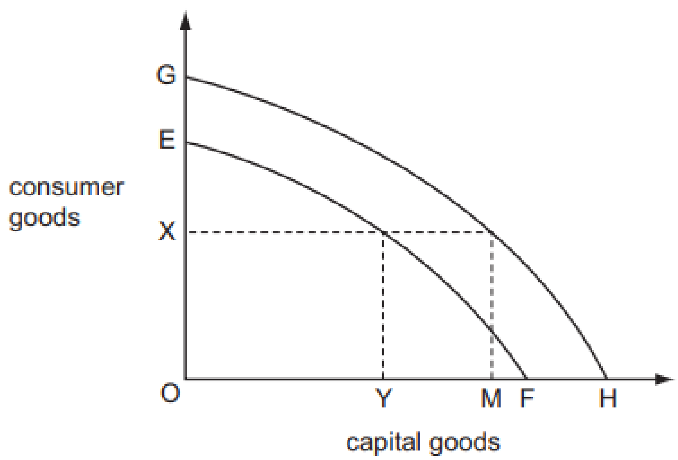
	tax revenue	consumer expenditure
I	reduce by $80	increase by $280
II	reduce by $80	increase by $480
III	reduce by $200	increase by $280
IV	reduce by $200	increase by $480
V	increase by $280	reduce by $80



20. Which type of government intervention runs the risk of causing shortages?
    I. <u>maximum price controls</u>
    II. specific indirect taxes
    III. subsidies paid to some producers
    IV. taxes on company profits
    V. none of the above

21. The price elasticity of demand for a product is unitary for all price ranges. What will be the effect of an increase in its price?
    I. <u>an equal proportionate decrease in the amount demanded</u>
    II. an equal proportionate decrease in expenditure on the product
    III. an increase in the product's percentage of total consumer expenditure
    IV. no change in the amount of the product demanded
    V. none of the above

22. The diagram shows two production possibility curves (EF and GH), before and after technological progress has taken place.



After technological progress has taken place, what is the opportunity cost in capital goods of producing OX consumer goods?

I. <u>MH</u>
II. OH
III. OM
IV. YF
V. YH

23. In an economy, the marginal propensity to consume of the unemployed is higher than that of taxpayers. The government increases expenditure on unemployment benefits by $10 million. What will the government need to do if it wishes to keep aggregate demand unchanged?

I. raise taxation by less than $10 million
II. <u>raise taxation by more than $10 million</u>

III. raise taxation by $10 million
IV. leave taxes unchanged
V. none of the above

24. 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
I	decrease	decrease
II	**decrease**	**increase**
III	increase	increase
IV	increase	decrease
V	increase	unchanged

25. Other things being equal, what is likely to result from an increase in interest rates in a country?

I. a capital outflow from the country
II. a depreciation of the country's currency
III. a decrease in consumption
IV. an increase in investment
V. None of the above

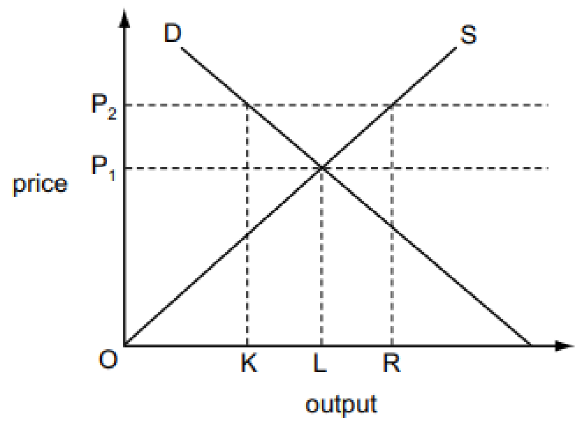
26. According to monetarist theory, what will be the short-run effect on the level of output and on the price level of an unanticipated increase in the money supply?

	effect on output	effect on the price level
I	**increase**	**increase**
II	increase	no change
III	no change	increase
IV	no change	no change
V	decrease	increase

27. The diagram shows the market supply and demand curves for corn.

    What should a government do if it is to maintain a minimum price of OP2?

    I. <u>buy quantity KR</u>
    II. buy quantity LR
    III. sell quantity KL
    IV. sell quantity OL
    V. None of the above



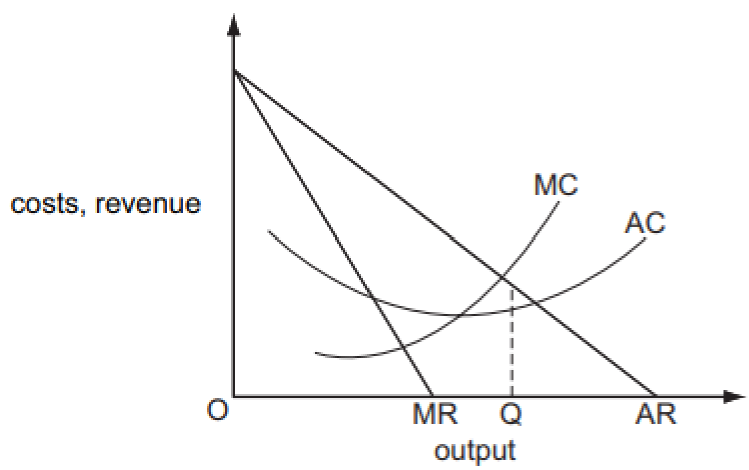
28. A country has a floating exchange rate and an independent central bank with the power to set interest rates.
    The inflation rate is currently stable at the central bank's target rate of 5%. What is likely to happen to interest rates and to the exchange rate if the bank's target rate was reduced to 2%?

	interest rates	exchange rate
I	decrease	depreciate
II	decrease	appreciate
III	increase	depreciate
<u>IV</u>	**<u>increase</u>**	**<u>appreciate</u>**
V	decrease	unchanged

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

    What could explain why the firm produces output OQ?

I. **<u>It is operating in a contestable market.</u>**
II. It is operating in a perfectly competitive market.
III. It is seeking to maximise profits.
IV. It is seeking to maximise sales revenue.
V. None of the above



30. All firms in an economy produce at levels of output where price and marginal private cost are equal. Why might this not be sufficient to ensure that allocative efficiency is achieved?
    I. a small number of buyers and sellers
    II. differences in consumers' preferences
    III. product differentiation
    IV. <u>the presence of externalities</u>
    V. All of the above

31. The schedule shows the short-run marginal cost of producing good X

units of X	1	2	3	4	5
marginal cost ($)	50	40	20	20	60

Given that the total fixed cost is $10, what level of output minimises average total cost?

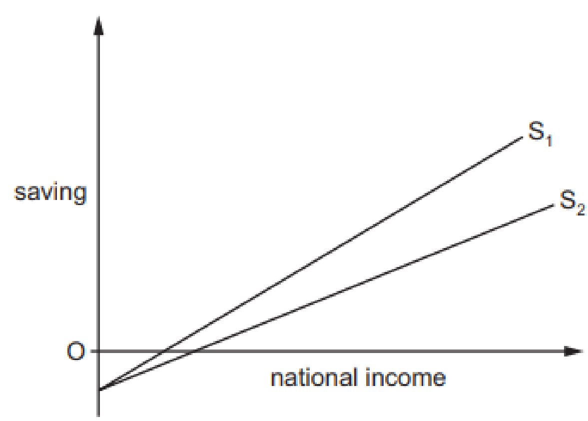
    I. 1 units
    II. 2 units
    III. <u>3 units</u>
    IV. 4 units
    V. 5 units

32. What must result from a rise in the supply of money, if the income velocity of circulation remains unchanged?
    I. a fall in unemployment
    II. a rise in the volume of output
    III. a rise in the general level of prices
    IV. <u>a rise in the money value of national income</u>
    V. None of the above

33. In the diagram, S1 is an economy's initial saving function.

If the saving function shifts to S2, what effect will this have on the marginal propensity to consume and on the multiplier?

	marginal propensity to consume	multiplier
I	decreases	decreases
II	decreases	increases
III	increases	decreases
<u>IV</u>	**<u>increases</u>**	**<u>increases</u>**
V	unchanged	Unchanged



34. In an economy, the volume of output rises by 2% in a year, while the quantity of money rises by 5%. If the velocity of circulation of money remains the same, what will be the approximate increases in the price level and the money value of national income?

	increase in price level	increase in money value of national income
I	2%	5%
II	2%	7%
III	**3%**	**5%**
IV	3%	7%
V	5%	7%

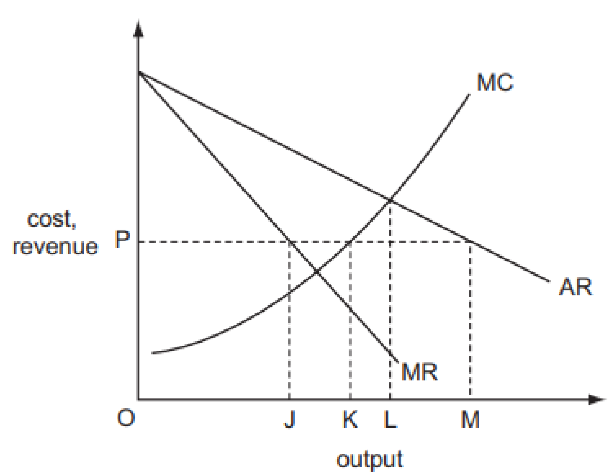
35. Between 2019 and 2020 a country's national output fell by 2%. Over the same period its unemployment rate decreased from 6% to 4%. What could explain this?
    I. There was a decrease in labour productivity.
    II. There was a fall in the rate of inflation.
    III. There was an increase in the long-term potential rate of growth.
    IV. There was an increase in the size of the labour force.
    V. None of the above

36. In an economy operating below full employment, which combination of changes will definitely result in an increase in national income?
    I. a fall in the rate of taxation together with a rise in the saving rate
    II. a rise in government expenditure together with a fall in the propensity to import
    III. a rise in investment expenditure together with a rise in the rate of taxation
    IV. a rise in the propensity to save together with a rise in exports
    V. None of the above

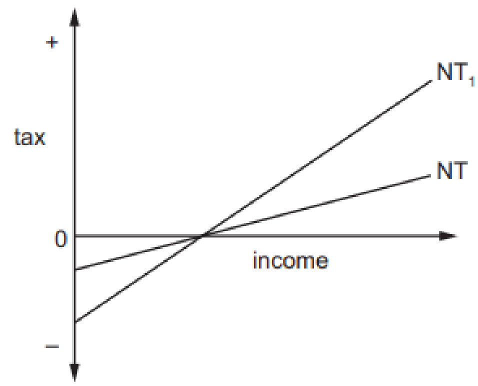
37. The diagram shows the initial cost and revenue curves of a profit-maximising monopolist.

What output will the firm produce if the government fixes the price at OP?

I. OJ
II. OK
III. OL
IV. OM
V. None of the above



38. A country has a negative income tax. In the diagram, the curve NT shows the country's initial tax schedule.



What could cause the tax schedule to shift to NT1?

I. <u>a higher marginal tax rate</u>
II. a more equal distribution of income
III. an increase in household disposable income
IV. an increase in the marginal propensity to consume
V. none of the above

39. Over one year the money income in an economy increased by 6%. In the same period prices rose by 4%.
What can be concluded from this?
I. Real incomes decreased by 2%.
II. The velocity of circulation decreased by 2%.
III. The money supply increased by 10%.
IV. <u>The volume of output increased by 2%.</u>
V. None of the above

40. What is likely to be the effect on interest rates and the supply of money of a purchase of government securities by a central bank?

	interest rates	money supply
I	increase	increase
II	increase	decrease
III	decrease	decrease
<u>IV</u>	**<u>decrease</u>**	**<u>increase</u>**
V	increase	Unchanged