

FORM TP 2006196



TEST CODE **02116020**

MAY/JUNE 2006

**CARIBBEAN EXAMINATIONS COUNCIL
ADVANCED PROFICIENCY EXAMINATION**

ECONOMICS

UNIT 1 – PAPER 02

2½ hours

25 MAY 2006 (a.m.)

INSTRUCTIONS TO CANDIDATES

1. This paper consists of **THREE** sections.
2. Each section consists of **TWO** questions. Candidates **MUST** answer **THREE** questions, **ONE** from **EACH** section.
3. Answers for **ALL** questions must be written in the answer booklet provided.
4. Candidates may use silent non-programmable calculators.

SECTION I

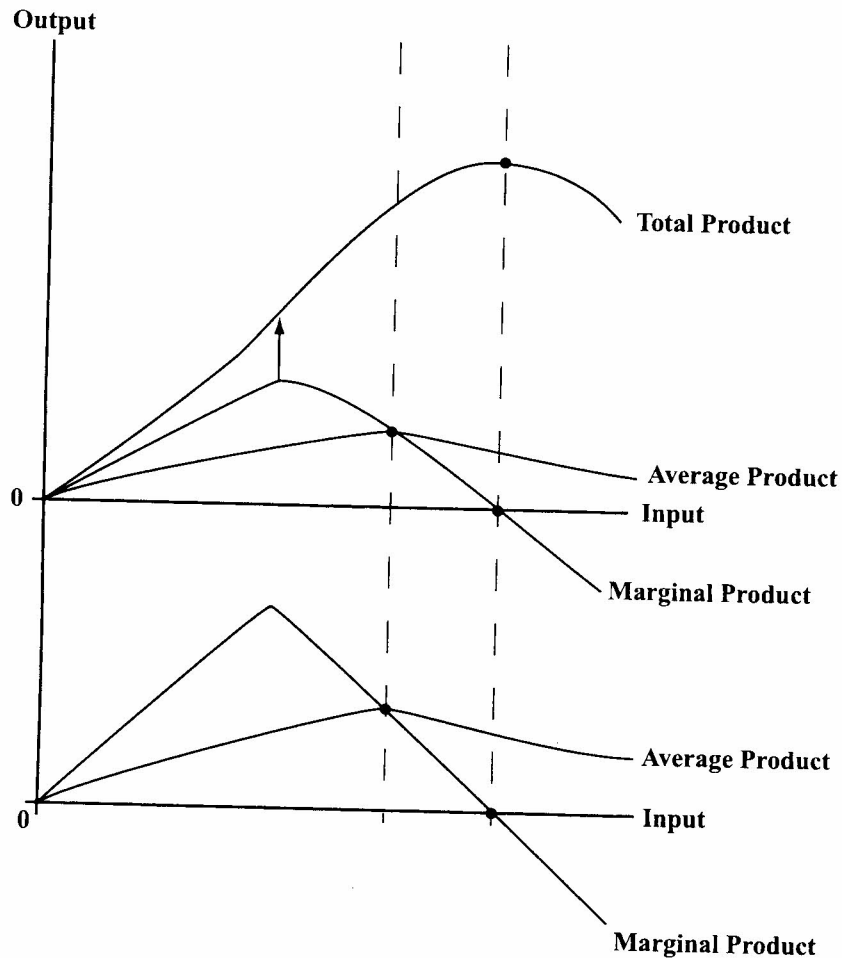
Answer ONE question from this section.

1. (a) Define the following terms:
- (i) Equilibrium price [2 marks]
 - (ii) Pareto efficiency [2 marks]
 - (iii) Price ceiling [2 marks]
- (b) Discuss FOUR main factors that influence EACH of the following:
- (i) The demand for beef [12 marks]
 - (ii) The supply of beef [12 marks]
- (c) A government imposes a ceiling on the price of milk in order to increase the quantity of milk consumed by low-income families. Using your knowledge of how the market operates, explain
- (i) why all low-income families may not be able to increase their consumption of milk [6 marks]
 - (ii) how consumers and producers will react to the new situation [4 marks]
 - (iii) what the Government might do to maintain the legal price [3 marks]
 - (iv) what the Government might do to ensure that the low-income families benefit from the pricing policy. [3 marks]
- (d) Identify ONE advantage and ONE disadvantage of the free market allocation of resources. [4 marks]

Total 50 marks

2. (a) (i) Define the term 'production function'. [2 marks]
- (ii) State where EACH of the three stages of production begins and ends. [9 marks]
- (iii) With the aid of the diagram on page 3, explain why production tends to occur in Stage TWO of the production stages and not in Stage ONE or Stage THREE.

GO ON TO THE NEXT PAGE



[9 marks]

(b) Explain the law of diminishing returns.

[6 marks]

(c) Explain the following concepts:

- (i) Constant returns to scale
- (ii) Increasing returns to scale
- (iii) Decreasing returns to scale
- (iv) Economies of scale

[8 marks]

(d) (i) Discuss ONE reason for economies of scale and ONE reason for diseconomies of scale.

[8 marks]

(ii) Explain how economies and diseconomies of scale influence the shape of the long-run average cost curve of a firm.

[8 marks]

Total 50 marks

SECTION II

Answer ONE question from this section.

3. (a) Define the term 'market structure'. [2 marks]
- (b) State FOUR assumptions on which perfect competition is based. [8 marks]
- (c) (i) State THREE types of market structures, other than perfect competition, and give an example of EACH. [6 marks]
- (ii) Explain how EACH of the types you mentioned in (c) (i) above differs from perfect competition. [6 marks]
- (d) An industry's long-run average cost is falling even after demand is met. Describe the type of market structure that this industry is likely to represent. [6 marks]
- (e) In a perfectly competitive industry, firms are making positive economic profit (above the normal profit).
- (i) Draw a diagram showing this situation. Label the axes, the cost and revenue curves, and indicate the profit made by firms. [16 marks]
- (ii) Explain what will happen to profit, the number of firms and output in the long-run. [6 marks]

Total 50 marks

4. (a) Explain and give an example of EACH of the following terms.
- (i) Public goods [5 marks]
- (ii) Externalities [5 marks]
- (iii) Asymmetric information [4 marks]
- (b) Explain how EACH of the concepts listed in 4 (a) above causes a market to fail. [21 marks]
- (c) Explain how EACH of the following government measures can correct market failure:
- (i) Taxation [5 marks]
- (ii) Subsidies [5 marks]
- (iii) Regulation [5 marks]

Total 50 marks

GO ON TO THE NEXT PAGE

SECTION III

Answer ONE question from this section.

5. (a) Define EACH of the four broad types of resources: land, labour, capital (including human capital) and entrepreneurship. State the role EACH plays in the production process. [12 marks]

- (b) Consider the following data on AURO INC.

Units of Labour	Output per Week	Marginal Product	Marginal Revenue	Marginal Revenue Product	Marginal Factor or Resource Cost
1	14				
2	26				
3	36				
4	44				
5	50				
6	54				

Assume perfect competition in the labour and output markets. The wage rate is \$18 and the price of the output is \$3.

- (i) Complete the table in your answer booklet. [12 marks]
- (ii) State the number of units of labour that AURO INC employs. [4 marks]
- (c) (i) Draw a backward-bending supply curve of labour and identify the region where the income effect exceeds the substitution effect. [6 marks]
- (ii) Explain why part of the curve has a negative slope. [4 marks]
- (d) Give FOUR reasons why wages differ. [12 marks]

Total 50 marks

GO ON TO THE NEXT PAGE

6. (a) (i) Explain the term 'poverty line'. [4 marks]
- (ii) Use the concept of poverty line to distinguish between persons who are 'absolutely poor' and persons who are 'relatively poor'. [6 marks]
- (b) Explain how THREE of the following factors contribute to poverty:
- (i) Non-ownership of resources, especially human capital
- (ii) Unemployment
- (iii) Large family size
- (iv) Single parent, female-headed family
- (v) Discrimination [18 marks]
- (c) (i) Discuss the term 'welfare programme'. [4 marks]
- (ii) Discuss THREE areas from among health, education, housing, and employment in which the government of your country supports programmes aimed at poverty reduction. [18 marks]

Total 50 marks

END OF TEST