**SECTION A: MULTIPLE CHOICE QUESTIONS**

1. An expansionary fiscal policy increases aggregate demand by :

(A) Reducing the interest rate.

**(B) Increasing autonomous spending.**

(C) Lowering the demand for money.

(D) Increasing the money supply.

2. Individuals *A* and *B* can both produce good *X*. We say that *A* has a comparative advantage in the production of good *X* if

(A) *A* has a higher opportunity cost of producing X than B.

(B) *A* can produce *X* using newer technology than *B*.

(C) *A* can produce more units of *X* in a given time period than *B*

**(D) *A* has a lower opportunity cost of producing *X* than *B*.**

*Questions 3 is* based on the chart 1 below, which gives a firm’s total cost of producing different levels of output.

|  |  |
| --- | --- |
| Output | Total Cost |
| 0 | 130 |
| 1 | 200 |
| 2 | 250 |
| 3 | 280 |
| 4 | 320 |
| 5 | 430 |
| 6 | 600 |

**Chart 1**

3. The marginal cost of producing the fourth unit of output is

(A) MK 40

(B) MK110

(C) MK190

(D) MK320

4. The development of money as a medium of exchange has facilitated the expansion of trade because

(A) holding money increases people's income.

(B) no other mediums of exchange are available.

**(C) money eliminates the "double coincidence of wants" problem.**

(D) holding money increases people's wealth.

5. As the interest rate falls, people hold \_\_\_\_\_\_\_\_ money instead of bonds because the opportunity cost of holding money has \_\_\_\_\_\_\_\_.

**(A) more; fallen**

(B) more; risen

(C) less; fallen

(D) less; risen

6. An example of a contractionary monetary policy is

**(A) an increase in the required reserve ratio.**

(B) a reduction in the taxes banks pay on their profits.

(C) a decrease in the discount rate.

(D) the Fed buying government securities in the open market.

***Refer to the information provided in Figure 2 below to answer the three questions that follow.***



**Figure 2**

7. Refer to Figure 2. An aggregate demand shift from *AD*2 to *AD*0 can be caused by

(A) an increase in the price level.

(B) a decrease in the price level.

(C) a decrease in money supply.

**(D) a decrease in taxes.**

8. Refer to Figure 2. An aggregate demand shift from *AD*1 to *AD*0 can be caused by

(A) an increase in the price level.

(B) a decrease in the price level.

**(C) a decrease in government spending.**

(D) an increase in money supply.

9. The depletion of fish stocks in Lake Malawi with an accompanying unemployment, will lead

to a

A) movement from the existing production possibilities frontier to a point inside the

production possibilities frontier.

B) shift inward of the existing production possibilities frontier.

**C) shift inward of the existing production possibilities frontier plus a movement to a**

**point inside the new production possibilities frontier.**

D) movement along the existing production possibilities frontier to a point of less fish

production.

***Refer to the information provided in Figure 3 below to answer the three questions that follow.***



**Figure 3**

10. Refer to Figure 3. Cost-push inflation occurs if

(A) the aggregate supply curve shifts from *AS*1 to *AS*0.

(B) the economy moves from Point *A* to Point *B* on aggregate supply curve *AS*1.

**(C) the aggregate supply curve shifts from *AS*1 to *AS*2.**

(D) the economy moves from Point *A* to Point *C* on the aggregate supply curve *AS*1.

11. If the increase in the price of one good decreases the demand for another, then the two goods are

(A) Inferior goods

**(B) Complementary goods**

(C) Substitute goods

(D) Normal goods

12. Expansionary monetary policy

(A) tends to lead to an appreciation of a nation's currency.

(B) usually has no effect on a currency's exchange value.

(C) tends to lead to a depreciation of the currencies of other nations.

**(D) tends to lead to a depreciation of a nation's currency.**

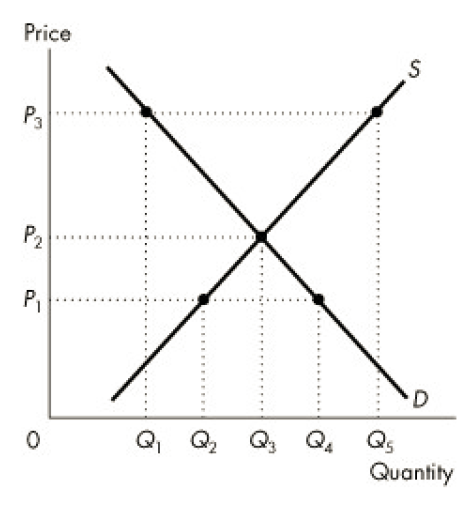
13. A bank has excess reserves to lend but is unable to find anyone to borrow the money. This will \_\_\_\_\_\_\_\_\_\_ the size of the money multiplier.

**(A) reduce**

(B) increase

(C) have no effect on

(D) double



14. At price P3 in the figure above

(A) this market is in equilibrium.

(B) there is a shortage in the amount of *Q*5 - *Q*1.

(C) there is a tendency for the price to rise.

(D) **there is a surplus in the amount of *Q*5 - *Q*1.**

15 If the CPI was 128 at the end of 2011 and 136 and the end of 2012, what was the inflation

rate in 2012?

(A) 4.2 percent

(B) 5.9 percent

**(C) 6.25 percent**

(D) 8 percent

16. Macroeconomics is concerned with

(A) Only long-run trends in economic activity.

(B) Only short-run fluctuations in the business cycle.

**(C) Both long-run trends and short-term fluctuations in economic activity.**

(D) Only with changes in the overall price level.

17. If one firm in a perfectly competitive industry experiences a technological breakthrough that lowers only that firm’s cost of production, which of the following correctly describes the effect on this firm’s price, quantity, and profit?

|  |  |  |  |
| --- | --- | --- | --- |
|  | Price | Quantity | Profit |
| A. | decrease | decrease | decrease |
| B. | decrease | increase | increase |
| C | no change | decrease | increase |
| **D** | **no change** | **increase** | **increase** |

18. Which of the following is accurate?

(A) When the price level decreases, the value of money decreases.

**(B) When the price level decreases, the value of money increases.**

(C) When the price level decreases, the value of money remains the same.

(D) None of the above.

19. If the demand for potatoes increases whenever a person’s income increases, then potatoes are an example of

(A) an inferior good

(B) a Giffen good

**(C) a normal good**

(D) a public good

20. The multiplier in an open economy is -------------------- than in a closed economy because, as income level increases, ----------------------.

(A) Greater, there is a wider market available

**(B) Smaller, some of the increase will be used to buy imports**

(C) Greater, exports become more attractive to foreigners

(D) Smaller, consumers buy goods that had previously been sent abroad.

**SECTION B:**

**QUESTION 2**

1. Define the term globalization **(4 marks)**

Globalization is a process of **interaction** and **integration** among the people, companies, and governments of different nations, a process **driven by** [**international trade**](http://www.globalization101.org/category/issues-in-depth/trade/)and [**investment**](http://www.globalization101.org/category/issues-in-depth/investment/)and aided by [**information technology**](http://www.globalization101.org/category/issues-in-depth/technology/). This process has effects on the [**environment**](http://www.globalization101.org/category/issues-in-depth/environment/)**,** on [**culture**](http://www.globalization101.org/category/issues-in-depth/culture/)**,** on political systems, on [**economic development**](http://www.globalization101.org/category/issues-in-depth/development/)and prosperity, and on [**human physical well-being**](http://www.globalization101.org/category/issues-in-depth/health/) in societies around the world.

1. Discuss which factors might increase a country’s Terms of Trade and which factors

might decrease its Terms of Trade. (10 marks)

**The following might lead to an increase in the Terms of Trade: A rise in the level of domestic inflation; an increase in importing countries exchange rate; changes in the conditions of demand which might lead to an increase in export prices; or changes in the conditions of supply for example the introduction of new technology in producing goods imported may lead to a fall in import prices.**

**The following might lead to a decrease in the Terms of Trade: A fall in the domestic price level; a fall in the importing countries exchange rate; changes in the conditions of demand which might lead to an increase in the price of imported goods, for example if the price of imported oil rises significantly the Terms of Trade of the importing country will deteriorate; there might be changes in the conditions of supply which make exports cheaper.**

1. Explain the difference between absolute advantage and comparative advantage in international trade. **(6 marks)**

**Advantages: Firms might benefit from**

Economies of specialization

Economies of scale

Easier access to raw materials

Access to cheap raw materials

Access to large markets

**Disadvantages: Firms might suffer from**

Cheap overseas imports

A fall in demand for their products

Unfair competition due to ‘dumping’

Unfair competition from ‘cheap labour’ economies

Infant/small industry firms find it more difficult to survive

**(Total 20 marks)**

**QUESTION 3**

One of the Chief Executive Officers has asked you to advise his Business Development Managers about the income elasticity of demand. Using examples where necessary,

**(a)** Explain and provide a formula to measure income elasticity of demand. **(5 marks)**

**Income elasticity of demand measures the responsiveness of demand for a good in relation to a change in income.**



**(b)** Explain how income elasticity of demand can be used to show the difference between

**normal** goods and **inferior** goods. **(5 marks)**

**The demand for a normal good will increase when income increases. Therefore the income elasticity of demand will be positive for a normal good.**

**The demand for an inferior good will decrease when income increases. Therefore the income elasticity of demand will be negative for inferior goods.**

**(c)** Explain how the concept of income elasticity of demand might be useful to a business.

**(10 marks)**

**Firms will want to know the income elasticity of demand for their product and whether it is a normal good. Some types of goods, typically luxury goods, have an income elastic demand and, therefore, can expect a significant rise in sales revenue when incomes are rising and vice-versa when incomes are falling. Also when income elasticity is positive, the demand for this type of good will rise when incomes are rising.**

**Some firms produce goods with a low income elasticity, for example goods which are seen to be necessities. Such firms are then less likely to be negatively affected by an economic recession. In addition, some firms produce goods which have a negative income elasticity of demand. These can be described as inferior goods. Inferior goods can expect an increase in demand in a recession and this enables firms to plan accordingly.**

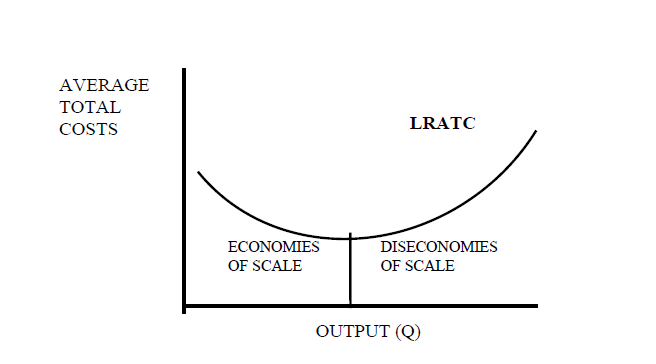
**(Total 15 marks)**

**QUESTION 4**

**(a)** Define the term ‘internal economies of scale’. **(4 marks)**

**Internal economies of scale are attained when a firm grows and this leads to a lower unit cost of production.**

**(b)** Draw a long run average total cost curve and label the parts of the curve which reflecting the respective economic returns **(8 marks)**



**(c)** Explain **two** types of economy of scale which a business could experience as it grows in size. **(8 marks)**

**Answers could refer to any two of the following economies: commercial/marketing economies; technical economies; financial economies; risk economies; managerial economies**.

**(Total 15 marks)**

**Question 34**

You are an Executive at the Institute of Bankers which is organizing a workshop for all its member banks. During the workshop the CEO has asked you to outline to the member banks **three** functions of a commercial (retail) bank, and explain the importance of these three functions to a business.

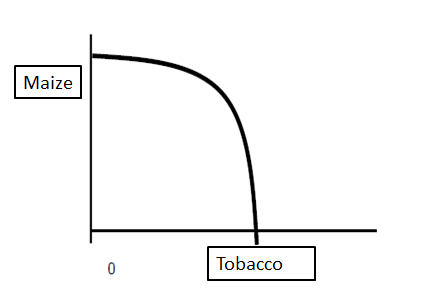
**(20 marks)**

**Functions might include:**

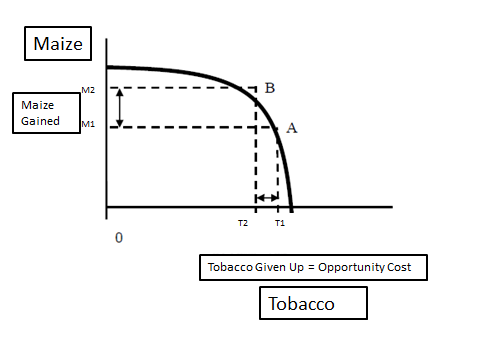
* **Provision of loans – to provide short term working capital and long term direct**
* **investment; mortgage loans; overdraft facilities; corporate loans.**
* **Provides methods of safekeeping including savings and deposits accounts which**
* **allow value of funds to grow;**
* **Provides methods of payments which include: cheques; standing orders; electronic**
* **funds transfer; debit/credit cards.**
* **Provides business advice and advice on taxation and financial matters and supplies**
* **foreign currency.**
* **Any other relevant function which might be beneficial to a business.**

**QUESTION 5**

1. Explain with the aid of a diagram, the Production Possibility Frontier for a country producing two alternative goods; maize and tobacco. **(5 marks)**



1. Use the Production Possibility Frontier to illustrate the opportunity cost for the country to produce maize. **(5 marks)**



**If production moves from point A on the production possibility frontier to point B, the extra maize gained will be a movement from M1 to M2 and the number of units of tobacco given up will be a movement from T1 to T2. Therefore the opportunity cost of is the value of the tobacco units given up (i.e. T1 tp T2.**

**Note that the notations on quantities of maize nd tobacco are illustrative notations and candidates may choose any notations of their choice.**

1. Explain why the country would be inefficient if it operated at a point within its Production Possibility Frontier and identify some strategies that a firm might adopt to enable it to operate on the production possibility frontier. **(10 marks)**

**The country would be inefficient because the firm is not using all its resources to maximise output**

**The country could increase labour productivity by introducing financial incentives**

**The country could attempt to reduce any existing negative working practices**

**The country could introduce new working shift patterns**

**The country might provide better working conditions**

**The country might provide additional training for its workforce**

**The country might use existing machinery more efficiently**

**(Total 20 marks)**