

## PRACTICE PAPER ECONOMICS PAPER 1

(1 hour)

This paper must be answered in English

### INSTRUCTIONS

1. Read carefully the instructions on the Answer Sheet. After the announcement of the start of the examination, you should first stick a barcode label and insert the information required in the spaces provided. No extra time will be given for sticking on the barcode label after the 'Time is up' announcement.
2. When told to open this book, you should check that all the questions are there. Look for the words '**END OF PAPER**' after the last question.
3. All questions carry equal marks.
4. **ANSWER ALL QUESTIONS.** You are advised to use an HB pencil to mark all the answers on the Answer Sheet, so that wrong marks can be completely erased with a clean rubber. You must mark the answers clearly; otherwise you will lose marks if the answers cannot be captured.
5. You should mark only **ONE** answer for each question. If you mark more than one answer, you will receive **NO MARKS** for that question.
6. No marks will be deducted for wrong answers.

There are 40 questions in this paper. Choose the **BEST** answer for each question.

1. In the absence of scarcity,
  - (1) there will be no discrimination.
  - (2) there will be no market price.
  - (3) there will be no goods.
  - A. (1) and (2) only
  - B. (1) and (3) only
  - C. (2) and (3) only
  - D. (1), (2) and (3)
  
2. Mr. Chan spent \$5 000 on buying a new mobile phone which can be sold for \$7 000 in the second-hand market. Mr. Chan's cost of keeping the mobile phone is \_\_\_\_\_.
  - A. \$0
  - B. \$2 000
  - C. \$5 000
  - D. \$7 000
  
3. Which of the following statements about interest are correct?
  - (1) Interest is a premium received for postponing current consumption.
  - (2) An interest rate does not exist in a barter economy.
  - (3) A fall in the interest rate increases present consumption.
  - A. (1) and (2) only
  - B. (1) and (3) only
  - C. (2) and (3) only
  - D. (1), (2) and (3)
  
4. Which of the following descriptions about the relationship between the three types of production is correct?
  - A. Primary production provides raw materials for the other types of production.
  - B. Secondary production does not rely on tertiary production to produce finished goods.
  - C. Tertiary production relies only on primary production.
  - D. The three types of production are independent, and tertiary production is the most important.

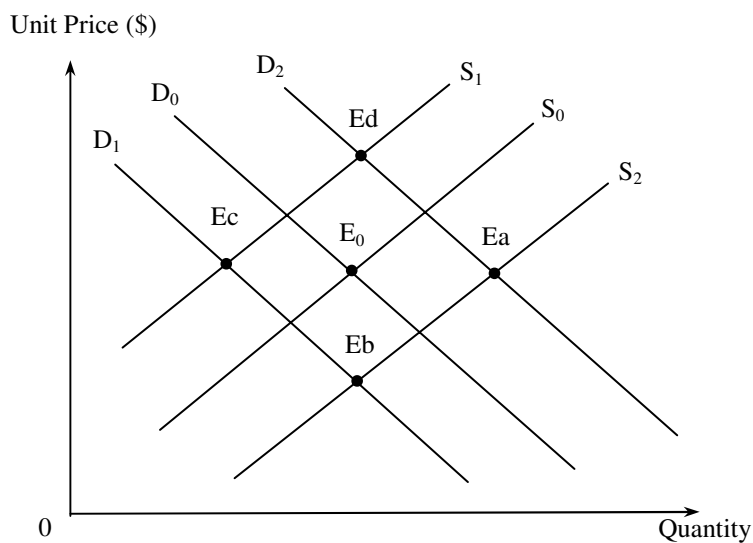
5. The following table shows the monthly production of a firm with two inputs, machines and labour.

Machines (Units)	Labour (Units)	Total product (Units)
2	5	10
3	5	20
4	5	32
5	5	42
6	5	X

If the law of diminishing marginal returns applies to the firm, X

- A. must be smaller than 42.
  - B. must be greater than 42.
  - C. can be equal to 42.
  - D. is equal to 52.
6. A worker is paid by the quantity he produced instead of receiving a monthly salary. Which of the following statements is INCORRECT?
- A. The worker tends to produce more output.
  - B. The quality of the output tends to be lower.
  - C. The cost of monitoring the worker regarding shirking will be lower.
  - D. The income of the worker will increase.
7. Tommy and David have turned their firm from a partnership into a private limited company. Which of the following statements is correct?
- A. They have a higher incentive to work as the profits tax rate is lower.
  - B. The firm can still exist even if one of the owners goes bankrupt.
  - C. The size of the firm will increase.
  - D. The financial conditions of the firm have to be disclosed to the public.
8. An increase in tobacco duty will lead to
- A. a rise in government tax revenue from cigarettes.
  - B. a rise in smokers' total expenditure on cigarettes.
  - C. a fall in the total market value of cigarettes.
  - D. a fall in cigarette retailers' total revenue net of tax.
9. Suppose there is political unrest in the countries exporting crude oil. As a result, there is a 30% increase in the price of gasoline and a 15% change in the quantity transacted of gasoline. We can conclude that
- A. the demand for gasoline is elastic.
  - B. the demand for gasoline is inelastic.
  - C. the supply of gasoline is elastic.
  - D. the supply of gasoline is inelastic.

10. In the following diagram,  $E_0$  is the initial equilibrium of the market for printed books in Hong Kong.



Suppose there is a trend to read electronic books and there is a rise in the price of printing paper. The new equilibrium point in the diagram will be \_\_\_\_\_.

- A. Ea
  - B. Eb
  - C. Ec
  - D. Ed
11. Refer to the following demand and supply schedules of good X.

Unit price (\$)	20	18	16	14	12	10
Quantity demanded (units)	500	550	600	650	700	750
Quantity supplied (units)	800	750	700	650	600	550

If the government lowers the quota from 700 units to 550 units,

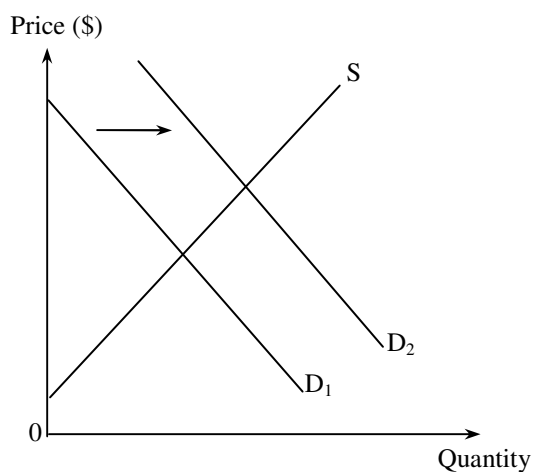
- A. the market price will drop by \$2.
- B. the market price will rise by \$2.
- C. the market price will rise by \$4.
- D. the market price will rise by \$6.

12. The following table shows the total cost schedule of a price-taking firm which has a fixed cost equal to \$20.

Quantity (units)	Total cost (\$)
1	40
2	65
3	95
4	130
5	170

Suppose the market price is \$35. At the profit-maximizing output level, the firm's profit and total producer surplus are \_\_\_\_\_ and \_\_\_\_\_ respectively.

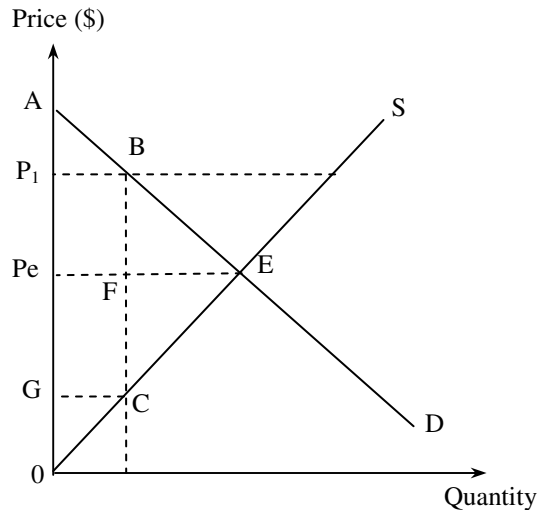
- A. \$10 ... \$10  
 B. \$10 ... \$30  
 C. \$30 ... \$10  
 D. \$30 ... \$30
13. Which of the following is INCONSISTENT with the law of demand?
- A. An imposition of an import quota on garments will lead to an improvement in the average quality of imported garments.  
 B. People who live in remote areas tend to buy better seats at concerts held in the town centre.  
 C. An increase in unemployment allowance raises the unemployment rate.  
 D. If an additional lump-sum charge is imposed per taxi trip, the number of short-distance trips will fall by a smaller percentage than the number of long-distance trips.
14. The following diagram shows the demand and supply curves of good X in a perfectly competitive market.



There is a shift in the demand curve for good X from  $D_1$  to  $D_2$ . As a result,

- A. firms enjoy more producer surplus.  
 B. the marginal cost of producing the last unit decreases.  
 C. the supply of good X increases.  
 D. consumers enjoy less consumer surplus.

15. The following diagram shows the demand and supply curves of good X in a perfectly competitive market.



Suppose a price floor is set at  $P_1$ . As a result,

- A. the deadweight loss is equal to area BEF.
  - B. the producer surplus is equal to area  $P_1BCO$ .
  - C. the consumer surplus is equal to area AEPe.
  - D. the total social surplus is equal to area  $P_1BCG$ .
16. Which of the following are features of a perfectly competitive market?
- (1) The marginal revenue of each firm equals the market price.
  - (2) The sellers and buyers have perfect market information.
  - (3) The marginal cost schedule of a firm is the same as its supply schedule.
- A. (1) and (2) only
  - B. (1) and (3) only
  - C. (2) and (3) only
  - D. (1), (2) and (3)
17. Economic efficiency is attained when
- (1) total benefits to consumers are maximized.
  - (2) all potential gains are fully captured.
  - (3) marginal social benefits are equal to marginal social costs.
- A. (1) and (2) only
  - B. (1) and (3) only
  - C. (2) and (3) only
  - D. (1), (2) and (3)

18. The following table shows the Gini coefficient of Economy A from Year 1 to Year 4.

Year	Gini coefficient
1	0.534
2	0.563
3	0.609
4	0.614

Based on the above information, which of the following statements is/are correct?

- (1) The income of high-income households increases while the income of low-income households decreases.
- (2) The income distribution becomes more uneven.
- (3) The general living standard declines.

- A. (1) only
- B. (2) only
- C. (3) only
- D. (1), (2) and (3)

19. Which of the following is the most likely effect of an effective minimum wage law?

- A. Income distribution will become more even.
- B. Total wage earnings of workers will rise.
- C. The employed population will increase.
- D. Non-price competition will emerge.

20. The following table shows the statistical data of an economy.

Gross Domestic Product (GDP) components	Million (\$)
Private consumption expenditure	400
Government consumption expenditure	250
Net domestic fixed capital formation	300
Decrease in stock	70
Subsidies	120
Capital consumption allowance	50
Net exports	300
Net income from abroad	80
Direct tax	100

The GDP at factor cost is \$\_\_\_\_\_ million.

- A. 1 250
- B. 1 270
- C. 1 350
- D. 1 490

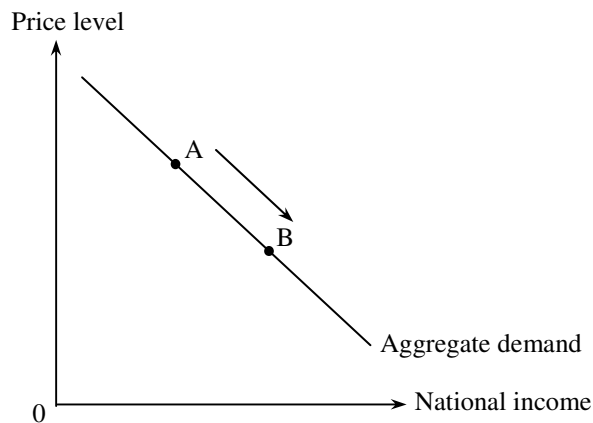
21. If the value of the net external factor income flow (i.e. the net income from abroad) of an economy is negative, it implies that
- the capital inflow to the economy is greater than the capital outflow from it.
  - the gross investment of the economy is smaller than the net investment.
  - the gross national product of the economy is less than the GDP.
  - the value of imports of the economy is greater than that of exports.

22. Over a given period, the GDP at current market prices of an economy increases by 15% and the rate of inflation decreases from 10% to 5%.

Based on the above information, the real GDP \_\_\_\_\_ and the general price level \_\_\_\_\_.

- increases ... rises
- increases ... falls
- decreases ... rises
- decreases ... falls

23. Refer to the following diagram.



Which of the following will cause a movement along the aggregate demand curve from point A to point B?

- a drop in price level
- a decrease in the interest rate
- a reduction in salaries tax
- a depreciation of domestic currency

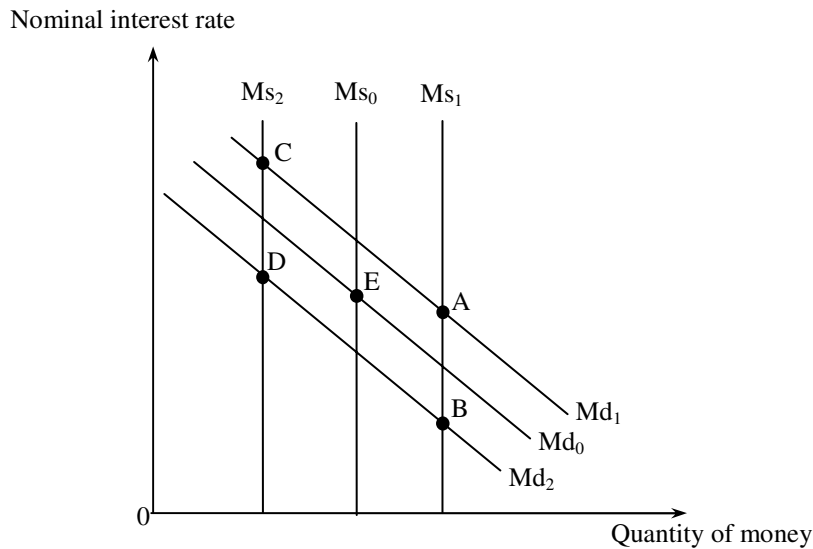
24. A large number of oil fields have to be closed because of serious oil spill accidents. In the short run, the aggregate supply of an oil-importing country will \_\_\_\_\_ and its price level will \_\_\_\_\_.

- increase ... rise
- increase ... fall
- decrease ... rise
- decrease ... fall



25. Which of the following can explain a leftward shift of the money demand curve?
- a rise in the interest rate
  - an increase in income of households
  - a more widespread use of Octopus cards
  - an increase in the required reserve ratio

26. The diagram below shows the money demand and money supply curves of an economy. The original equilibrium point is at E.



Suppose national income increases and the government carries out an open market purchase of bonds. The new equilibrium point will be at \_\_\_\_\_.

- A
  - B
  - C
  - D
27. Suppose the balance sheet of a banking system is as follows.

Assets(\$)		Liabilities(\$)	
Reserves	150	Deposits	500
Loans	350		

The amount of excess reserves in the banking system is \$50. Now, a customer withdraws \$50 from his bank account. If the banking system is fully loaned up, the maximum amount of loans in the banking system is \_\_\_\_\_.

- \$350
- \$400
- \$450
- \$500

28. If Mr. Chan withdraws HK\$500 000 from his account in a deposit-taking company and remits the sum to his relatives in Canada, Hong Kong's money supply M2 will \_\_\_\_\_ and M3 will \_\_\_\_\_.
- A. decrease ... decrease
  - B. remain unchanged ... remain unchanged
  - C. decrease ... remain unchanged
  - D. remain unchanged ... decrease
29. An asset which can be readily converted into cash at short notice without making a loss is regarded as a \_\_\_\_\_ asset.
- A. portable
  - B. durable
  - C. divisible
  - D. liquid
30. The real value of money decreases when the \_\_\_\_\_ is rising.
- A. deflation rate
  - B. general price level
  - C. money demand
  - D. nominal interest rate
31. Which of the following people will lose when unexpected inflation occurs?
- A. an individual holding time deposits in a bank
  - B. a holder of government bonds with interest rates adjusted according to the inflation rate
  - C. a flat owner repaying a fixed-rate mortgage loan
  - D. a billionaire keeping all his wealth in the form of gold
32. Which of the following can help narrow a deflationary (output) gap?
- A. an increase in the required reserve ratio
  - B. a sale of bonds by the central bank in the market
  - C. an increase in government expenditure
  - D. the abolishment of a tariff on imports
33. Which of the following statements about the classical quantity theory of money is INCORRECT?
- A. Both the velocity of circulation of money and the real output are assumed to be constant.
  - B. Any change in money supply will lead to the same proportional change in nominal output.
  - C. Deflation will occur when there is a continuous fall in money supply.
  - D. Any change in price level will lead to the same proportional change in money supply.

34. An increase in \_\_\_\_\_ may offset the effect of an expansionary monetary policy on national income.
- (1) people's desire to hold money as an asset
  - (2) people's desire to save
  - (3) transfer payments
- A. (1) and (2) only
  - B. (1) and (3) only
  - C. (2) and (3) only
  - D. (1), (2) and (3)
35. When the nominal interest rate is higher than the real interest rate, the expected inflation rate must be \_\_\_\_\_.
- A. positive
  - B. negative
  - C. rising
  - D. falling
36. Which of the following is a direct and proportional tax in Hong Kong?
- A. hotel accommodation tax
  - B. profits tax
  - C. salaries tax
  - D. general rates
37. The Inland Revenue Department will inform every salaries tax payer of the amount of tax payable either by mail or by the etax account. This practice is in line with the \_\_\_\_\_ principle of taxation put forward by Adam Smith.
- A. equity
  - B. certainty
  - C. convenience
  - D. economy
38. If a small open economy reduces the tariff on an imported good,
- A. both domestic production and consumption of the good will increase.
  - B. both tariff revenue and import volume will decrease.
  - C. the consumer surplus will increase while the producer surplus will decrease.
  - D. the world price of the good will fall while the total social surplus will increase.

39. Assume both Country A and Country B produce and consume Good X and Good Y only. If Country A can produce a unit of Good X with less resources than Country B,

- (1) Country A has an absolute advantage in producing Good X.
- (2) Country A has a comparative advantage in producing Good X.
- (3) Country B has an absolute advantage in producing Good Y.
- (4) Country B has a comparative advantage in producing Good Y.

- A. (1) only
- B. (1) and (2) only
- C. (2) and (4) only
- D. (1), (2), (3) and (4)

40. The following table shows the output per unit of resources in Country A and Country B.

	Tablet computers (Units)	Mobile phones (Units)
Country A	8	12
Country B	10	30

If Country A exports 10 units of tablet computers to Country B in exchange for 25 units of mobile phones, the total gains from trade of Country A will be \_\_\_\_\_unit(s) of mobile phones.

- A. 1
- B. 5
- C. 6.667
- D. 10

**END OF PAPER**