

MARKER CODE



Student Personal Identification Number

Solomon Islands National Form Six Certificate 2018

ECONOMICS

QUESTION AND ANSWER BOOKLET

FRIDAY 9th NOVEMBER 9:00 AM

TIME: 3 Hours Plus 10 Minutes
Reading Time.

1. This paper is divided into FIVE (5) sections. Answer **ALL** five sections.

	<u>Marks</u>	<u>Suggested time</u>
Section A. Basic Economic Concepts	52 marks	48 minutes
Section B. Money	33 marks	30 minutes
Section C. International Trade and Payments	39 marks	36 minutes
Section D. Economic Functions of Government	45 marks	42 minutes
Section E. Economic Development	<u>31 marks</u>	<u>24 minutes</u>
TOTAL	200 marks	180 minutes

1. **Answer all questions** in the spaces provided in this booklet.
2. **Write your Student Personal Identification Number (SPIN)** on the top right hand corner of this page and on the fold-out flap on the last page.
3. If you require more paper, ask the supervisor for extra sheets. Write your SPIN on additional sheets used and tie them inside this booklet at the appropriate space.
4. Check that this booklet contains pages **2– 34** in the correct order and that none of these pages is blank.
5. Do NOT use correction fluid.
6. Mobile phones are NOT allowed in the Examination room.

YOU MUST HAND THIS BOOKLET TO THE SUPERVISOR AT THE END OF THE EXAMINATION.

TOTAL MARKS

200

SECTION A: BASIC ECONOMICS CONCEPTS

(52 MARKS)

Part 1: Multiple Choice Questions (5 marks)

Circle the letter of your chosen answer.

1. Economics is fundamentally concerned with the;
 - A. financial aspects of everyday life.
 - B. scarcity of resources in relation to wants.
 - C. free working of market forces in an economy.
 - D. production and distribution of material goods.

2. What is scarcity?
 - A. When an unlimited amount of goods and services are available to meet limited wants and needs.
 - B. When a limited amount of goods and services are available to meet unlimited wants and needs.
 - C. When a limited amount of goods and services are available to meet limited wants and needs.
 - D. When an unlimited amount of goods and services are available to meet unlimited wants and needs.

3. Which of the following statements best define **opportunity cost**?
 - A. Price of a commodity.
 - B. Sacrifice of any alternative.
 - C. Loss suffered by missing a bargain.
 - D. Sacrifice of the next most desired alternative.

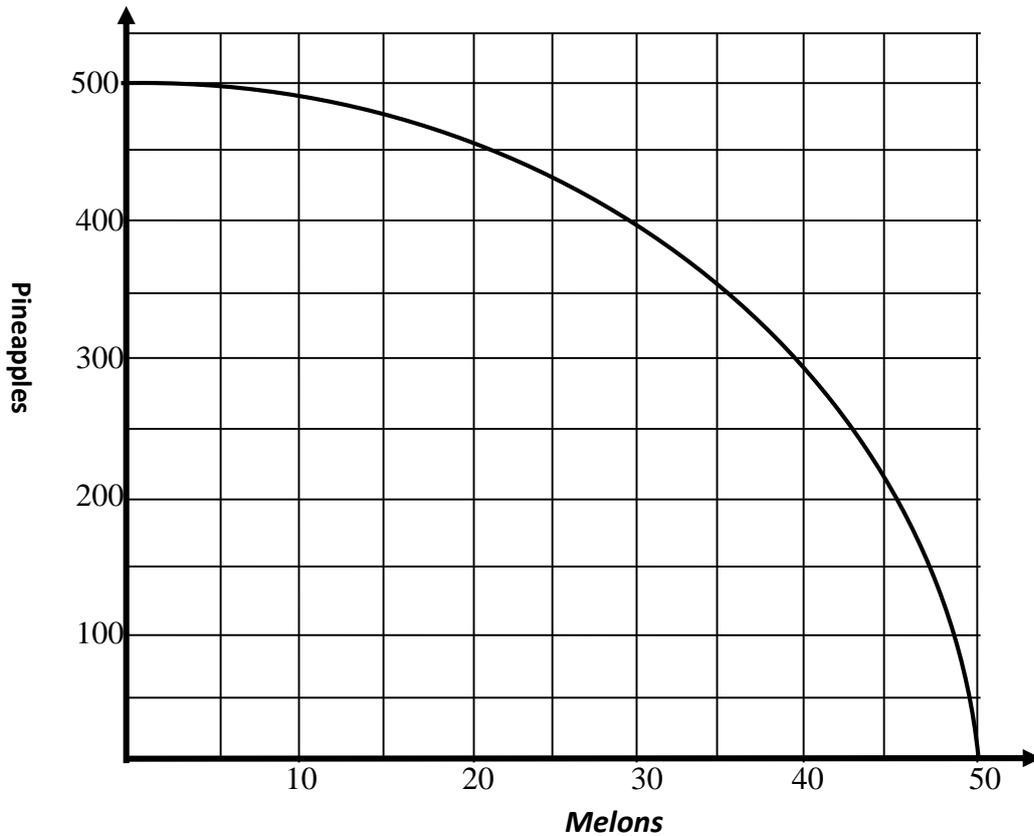
4. In which of the following market models is the individual seller of a product a **price taker**?
 - A. Oligopoly.
 - B. Monopoly.
 - C. Perfect competition.
 - D. Monopolistic competition.

5. Which of the following statements is TRUE about **labour markets**?
 - A. Households are the only buyers.
 - B. Households are considered sellers.
 - C. When businesses are called sellers.
 - D. Both businesses and households are buyers.

Part 2: Short Answer Questions (7 marks)

6. Production Possibility Curve

Use the graph below to answer questions (a) and (b).



(a) On the graph, placed (2 marks)

- (i) "X" as the area illustrating *under-utilisation of resources*.
- (ii) "Y" as the area that is *unattainable* with the current resources and technology.

(b) (i) How does the production possibility curve illustrate scarcity?

(2 marks)

(ii) What is the **opportunity cost** of increasing pineapple production from 400 to 500 pineapples?

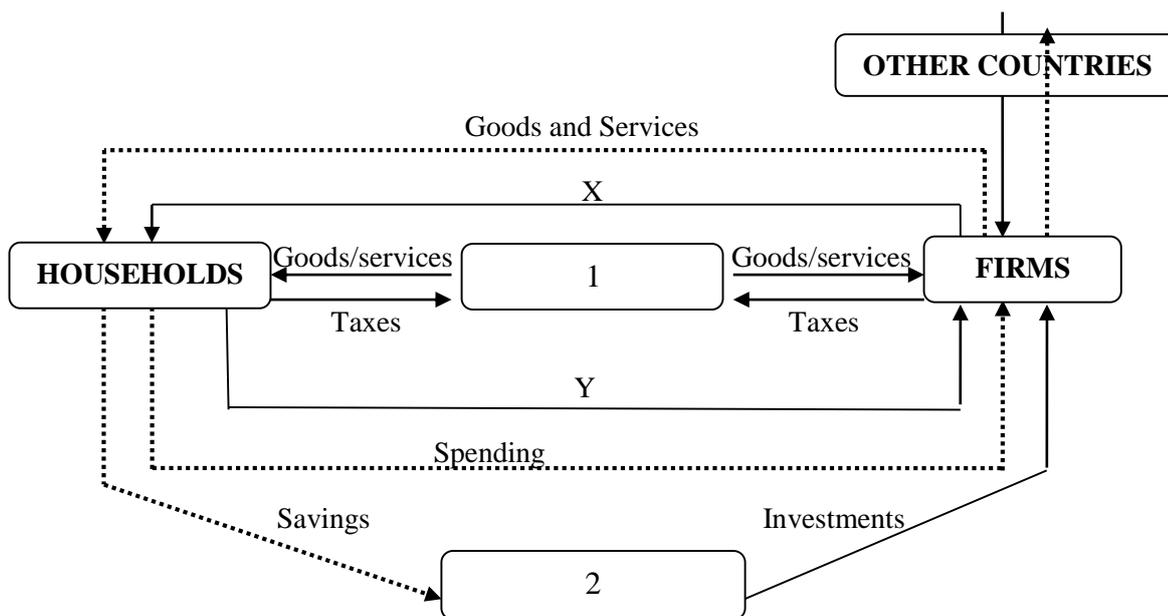
(1 mark)

(iii) Explain the relationship between scarcity, choice, and opportunity cost.

(2 marks)

7. Five-sector Circular Model (10 marks)

Study the diagram below and answer the questions on it.



(a) Name the sectors labelled 1 and 2 in the diagram.

1. _____

2. _____

(2 marks)

(b) Label the flows marked X and Y.

X _____

Y _____

(2 marks)

(c) When households purchased goods and services from firms, the associated demand is known as derived demand. Write **True** or **False** in the space below.

(1 mark)

(d) State the THREE (3) **injections** in an economy.

(i) _____

(ii) _____

(iii) _____

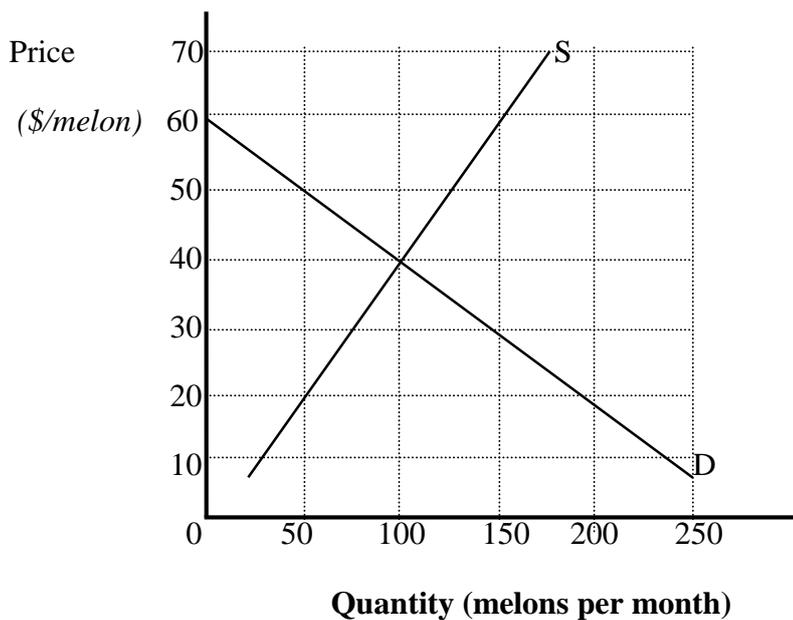
(3 marks)

(e) Explain the **interdependence** relationship between households and firms.

(2 marks)

8. Demand –Supply Curve Model (6 marks)

The figure below illustrates the market for melons in Tulagi.



(a) At the price of \$50.00, what situation exists in the market?

(1 mark)

(b) If the producer wish to sell 150 melons, what price must they charge?

(1 mark)

(c) How much revenue would the producers receive at the equilibrium price?

(1 mark)

(d) (i) Which of the curves would a government subsidy shift and state the direction of the shift.

(2 marks)

(ii) How would this shift affect the equilibrium price and quantity?

(1 mark)

9. Components of Aggregate Demand (5 marks)

Study the extract and answer the questions (a, b and c) below.

Keynesian economists believe that a change in total spending (including consumption, investment and government spending and spending on imports) has a multiplied impact on income. They also believe that we can calculate the extent of the resulting change in income using the multiplier.

[Adapted from OBE for FET]

(a) Write down the **aggregate demand** equation.

(1 mark)

(b) Describe the economic relationship depicted by the aggregate demand equation.

(2 marks)

(c) How does an increase in government spending affect aggregate demand?

(2 marks)

10. Market Structure (4 marks)

(a) How is perfect competition different from Monopolistic competition?

(2 marks)

b) Explain who is a **price maker**?

(2 marks)

11. Nominal and Real GDP (9 marks)

Study the data given in the table below and answer questions (a) to (e).

Good	2008		2011	
	Price	Qty	Price	Quantity
CDs	\$15	1000	\$30	1,300
Tapes	\$5	2000	\$10	2,600

(a) Distinguish between real **GDP** and **nominal GDP**.

(2 marks)

(b) Calculate the Nominal GDP for 2008 and 2011.

(2 marks)

(c) Calculate Real GDP for 2008 and 2011.

(2 marks)

(d) What is the percentage increase in real GDP?

(1 mark)

(e) Why is nominal GDP not a good measure of national output?

(2 marks)

12. GDP and Value-Added (6 marks)

Below is a table which summarises the process by which a packet of wheat flakes is produced and sold to a consumer as a final good.

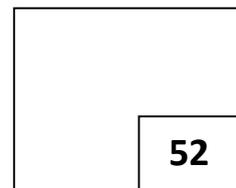
Stage	Producer	Price received \$	Value Added \$
1	Farmer sells wheat to miller	0.60	
2	Miller sells husked wheat to breakfast cereal maker	1.00	
3	Breakfast cereal maker sells wheat flakes to grocer	2.00	
4	Grocer sells wheat flakes to consumer	2.50	

(a) Complete the last column of the above table by calculating the **value added** at each of the FOUR (4) stages of production. (4 marks)

(b) Why does GDP equal aggregate income?

(2 marks)

Section A: P1 & P2



SECTION B: MONEY

(33 MARKS)

Part 1. Multiple Choice Questions (5 marks)

Circle the letter of your chosen answer.

1. Modern money or fiat money has;
 - A. a lot of intrinsic value.
 - B. no intrinsic value.
 - C. no intrinsic value but is guaranteed by the government.
 - D. guarantee by the government and central bank but is not true money.

2. In Solomon Islands M_1 consists of;
 - A. notes and coins in circulation.
 - B. term deposits in the commercial banks.
 - C. notes and coins in circulation plus term deposits.
 - D. notes and coins in circulation plus demand deposits.

3. Use the equation of **exchange** to solve this problem: $P = \$4$, $Q = \$1m$ and $V = 4$. What is the value of GDP?
 - A. \$1 million
 - B. \$2 million
 - C. \$4 million
 - D. \$6 million

4. A **commodity** money is a money that has;
 - A. a primary value in being a commodity.
 - B. been borrowed from the bank as a loan.
 - C. an external way of paying for goods or services.
 - D. an alternative use as an economic good or commodity.

5. Which of the following events will lead to **an increase** in the demand for money?
 - A. A decrease in the price level.
 - B. An increase in the interest rate.
 - C. An increase in the supply of money.
 - D. An increase in the level of aggregate output.

Part 2: Short Answer Questions

6. Functions of money (2 marks)

List any TWO (2) functions of money.

(i) _____

(ii) _____

(2 marks)

7. Inflation Rate (5 marks)

Use the table to answer the questions (a), (b) & (c) below.

Year	CPI	% change
1990	130.7	
1991	136.2	

(a) Define **inflation rate**.

(1 mark)

(b) Calculate the **inflation rate** for 1991.

(2 marks)

(c) How does an increase in the **rate of inflation** affect the purchasing power of the people?

(2 marks)

8. Causes and Effects of Inflation (7 marks)

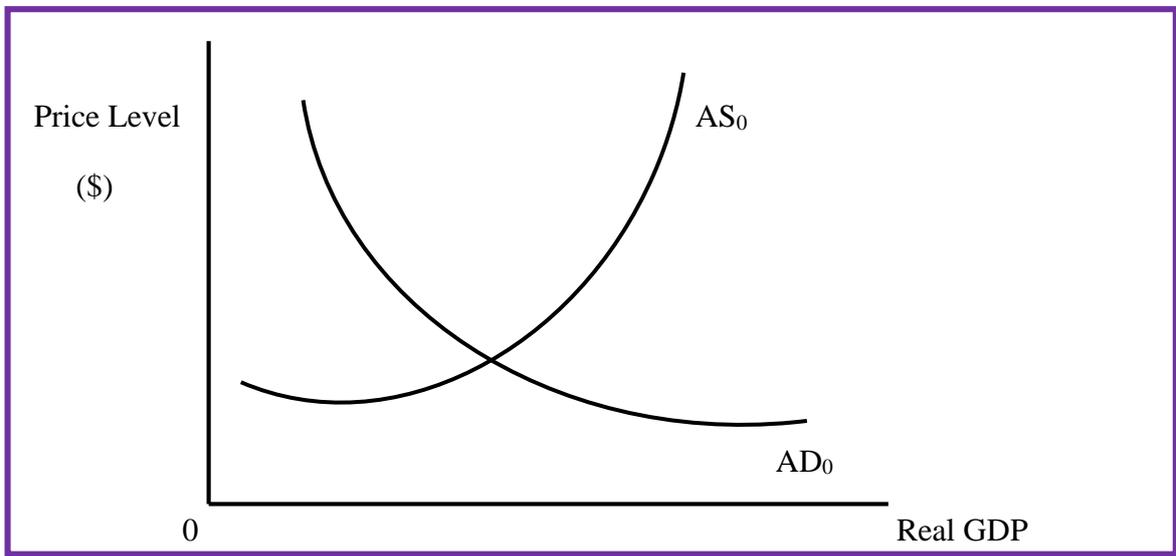
- (a) (i) Identify each of the following as either 'cost-push inflation' or 'demand-pull inflation' by putting a tick (✓) under the two blank columns. The first one has been done for you.

Statement	Cost-push	Demand- pull
(i) A depreciation in the exchange rate pushes up raw material prices and therefore causes inflation.	✓	
(ii) The impact of tax cuts is to cause inflation.		
(iii) Rising confidence in the economy boosts retail sales and has the effect of causing inflation.		

(2 marks)

- (ii) Use the Aggregate Supply (AS) and Aggregate Demand (AD) model below to show the effect of petrol price increases on the price level. Fully label the change.

Aggregate Supply and Aggregate Demand Model



(3 marks)

- (b) If high inflation is caused by demand-pull, describe a government fiscal policy that can be used to address this economic problem.

(2 marks)

9. Causes of Changes in Money Supply (5 marks)

(a) The table shows TWO (2) economic events which can cause money supply to either increase or decrease. In the right hand column, state whether the event will increase or decrease money supply.

EVENT	EFFECT ON MONEY SUPPLY
(i) The public withdraws less notes and coins than they use.	
(ii) Commercial Banks increase their lending to the public.	

(2 marks)

(b) Explain how the money supply will be affected if the government sells securities to the public.

(3 marks)

10. Equation of exchange (2 marks)

Use the equation of exchange to answer question below.

Given $P = \$10$, $Q = 6000$ million, and $V = 2$ and $M = \$300$ million.

According to the quantity theory of money, what effect will an increase in money supply has on the price level, assuming that velocity and quantity remain constant?

(2 marks)

11. Commercial Bank Balance Sheet (7 marks)

Consider the following balance sheet of Westpac Bank and answer the questions (a), (b) & (c). The reserve ratio (rr) is 10%.

Westpac Bank Balance sheet

Assets		Liabilities	
Cash reserves	\$100	Deposits	\$1,000
Loans	\$900		
Total	\$1,000	Total	\$1,000

(a) What is the purpose of **cash reserves**?

(1 mark)

(b) Assume that Joana borrowed \$900.00 from this Bank and bought a second-hand car with this loan. The former owner of the car, Karen deposits the proceeds from the sale into her account at Westpac Bank. Draw the Westpac Bank's new balance sheet for this new deposit.

(4 marks)

- (c) In May 2000, at the height of the ethnic tension, the Banks in Solomon Islands had experienced a '**run on the banks**'. Explain what is meant by this phrase?

(2 marks)

Section B: P1 & P2

33

Part 1. Multiple Choice Questions (5 marks)

Circle the letter of your chosen answer.

1. A **Depreciation** of Solomon Islands dollar relative to other currencies implies a/an;
 - A. increase in the price of Solomon Islands dollar in terms of other currencies.
 - B. decrease in the price of Solomon Islands dollar in terms of our own currency.
 - C. decrease in the price of Solomon Islands dollar in terms of other currencies.
 - D. increase in the price of Solomon Islands dollar in terms of our own currency.

2. A country that can produce more of a good or service than another country with the same amount of inputs is said to have a /an;
 - A. output advantage.
 - B. absolute advantage.
 - C. production advantage.
 - D. comparative advantage.

3. **Terms of trade** for a country are the ratio of _____ to _____
 - A. export prices, import prices.
 - B. its currency, other currencies.
 - C. the value of exports, the value of imports.
 - D. its opportunity costs, world opportunity costs.

4. The term **tariff**, as used in international trade, refers to a;
 - A. tax on imports.
 - B. tax on exports.
 - C. limit on the quantity of exports.
 - D. limit on the quantity of imports.

5. If net exports are **positive**, which of the following is false?
 - A. Net capital outflow is positive.
 - B. There is a balance of trade deficit.
 - C. Domestic output exceeds domestic spending.
 - D. Domestic saving exceeds domestic investment.

Part 2: Short Answer Questions

6. Absolute and Comparative Advantage (8 marks)

Sololand and Zealand, two hypothetical economies, has the following production output using 1 unit of labour.

Commodity	Sololand	Zealand
Copra (tonnes)	10	2
Sheep	1	12

(a) Which country has **absolute advantage** in sheep production?

_____ (1 mark)

(b) (i) Calculate the **opportunity cost** of producing 1 sheep in Sololand and Zealand?

_____ (3 marks)

(c) State which country has the **comparative advantage** in the production of sheep and why?

(i) Country _____ (1 mark)

(ii) Why? _____ (2 marks)

(d) Would you agree that the increase in the production of sheep imply specialisation?

_____ (1 mark)

7. Trade Balance (4 marks)

The table below gives the visible exports (in units) and imports (in units) of a country.

Exports			Imports	
Year	Price per Unit	No. Of Units	Price per Unit	No. Of Units
2008	\$150	4000	\$230	8000
2011	\$180	4000	\$250	8000

(a) Calculate the **total export revenue** for 2008.

(2 marks)

(b) Calculate the **Balance of trade** for 2008.

(2 marks)

8. Trade Protectionism (6 marks)

(a) The '**infant industry**' argument is probably the most economically sound argument in favour of protectionism.

(i) Explain what **infant industry protection** argument is.

(2 marks)

(ii) Explain ONE (1) possible argument **against** infant industry protection.

(2 marks)

(b) Why does **export-led** growth appear to work better than import substitution?

(2 marks)

9. Recording of Balance of Payments Transactions (4 marks)

(a) Given here are TWO (2) trade transactions, identify whether each transaction has a 'positive' or 'negative' effect on a country's Balance of Payment accounts by placing a tick (✓) in the last two columns. *An example has been done for you.*

Transaction	Positive	Negative
(i) Any sale of goods or services abroad	✓	
(ii) Any earnings on an investment in a foreign country		
(iii) Any purchase of goods or services abroad		

(2 marks)

(b) Explain how a **positive Balance of Payment** will affect foreign reserves.

(2 marks)

10. Currency Devaluation and Unemployment (4 marks)

In 2007 the Solomon Islands currency was devalued by 25% due to the Asian financial crises.

Evaluate the **positive** impact of the devaluation of the Solomon Islands currency on the level of unemployment in Solomon Islands.

(4 marks)

11. Exchange Rate (8 marks)

(a) What is the difference between a **fixed exchange rate** and a **flexible exchange rate**?

(2 marks)

(b) The **money supply** is normally affected under the flexible exchange rate. True or False.

(1 mark)

(c) **Given below are the exchange rates between Solomon Islands and four (4) of its major trading partners. The exchange rates are as at 1st of July 2017 and are expressed per \$1.00 SBD.**

USD = 0.1273
AUD = 0.1653
NZD = 0.1810
JPY = 15.5903

Use these exchange rates to convert the following;

(i) Foreign currency amount into **Solomon Islands currency**:
(Show your working out).

AUD \$230:

ANS: _____

(2 marks)

- (ii) Solomon Islands dollar into the **US currency**:
(Show your working out).

SBD\$1,000:

ANS: _____

(2 marks)

- (d) With reference to the Exchange rates on page 20, if the Solomon Islands currency now cost AUD 0.1735, this is called an **appreciation** of the Solomon Islands currency. True or false

(1 mark)

Section C: P1 & P2

39

SECTION D: ECONOMIC FUNCTIONS OF GOVERNMENT

(45 MARKS)

Part 1. Multiple Choice Questions (5 Marks)

Circle the letter of your chosen answer.

1. Name the THREE (3) types of **taxes**.
 - A. Regressive, retaining, proposed.
 - B. Regressive, proportional, probable.
 - C. Proportional, proposed, regressive.
 - D. Progressive, proportional, regressive.

2. The word "**Laissez Faire**" means the;
 - A. philosophy that individuals should not interfere with activity.
 - B. philosophy that government should not interfere with business activity.
 - C. law stating that government can at any time interfere with business activity.
 - D. law stating that government cannot at any time interfere with business activity.

3. An decrease in the demand for money is caused by a/an;
 - A. increase in the price level.
 - B. decrease in the interest rate.
 - C. decrease in the supply of money.
 - D. decrease in the level of total output.

4. To finance major **capital expenditure** in Solomon Islands, the government usually;
 - A. borrows externally.
 - B. prints more money.
 - C. uses taxation revenue.
 - D. uses profits from public enterprises.

5. Where a tax can be shifted, the incidence depends on;
 - A. how many producers.
 - B. the elasticity of demand and supply.
 - C. who is legally obliged to pay the tax.
 - D. whether there is perfect or imperfect information.

Part 2: Short Answer Questions

6. Budget Deficit (8 marks)

Read the extract and answer the questions (a) – (d) below.

DO DEFICITS MATTER?

Why do deficits cause anxiety? What happens when a government cannot cover its spending with taxes? If you spend more than you earn, you have a deficit, and to cover your deficit, you have to borrow. But when you borrow you must pay interest on your debt. Just like you, if a government or a nation has a deficit, it must borrow. And it must pay interest on its debts.

Whether borrowing and paying out huge amount of interest is a good idea or not it depends on what the borrowed funds are used for.

Adapted from *Macroeconomics* by McTaggart et al. (2010)

(a) What is the difference between a **budget deficit** and **debt**?

(2 marks)

(b) **Budget deficit** is an example of which type of fiscal policy?

(1 mark)

(c) Why is borrowing undesirable?

(2 marks)

(d) Name any THREE (3) sources of government revenue.

(i) _____

(ii) _____

(iii) _____

(3 marks)

7. Public Good (4 marks)

It is estimated that the Blue Devil Engineers will use almost \$10 million of worth of Solomon Islands development budget funds to reconstruct the Mataniko river bank buffer to withstand heavy flash flood.

(a) Explain why flood control would be considered a **public good**.

(2 marks)

(b) Explain how public goods are funded.

(2 marks)

8. Roles of the government (4 marks)

Explain the following roles of the government.

(i) Distributive role:

(2 marks)

(ii) Regulatory role:

(2 marks)

9. Tax System (4 marks)

Identify any FOUR (4) of the key features of a **good tax system**.

1. _____
 2. _____
 3. _____
 4. _____
- (4 marks)

10. Wage control (8 marks)

In 2010 the minimum wage for unskilled labour in Solomon Islands was increased from \$1.50 to \$4.00. This is an example of a price floor.

(a) Define the economic concept of a **price floor**.

(1 mark)

(b) Describe what a **minimum wage** is.

(2 marks)

(c) Explain how this minimum wage policy will affect the unskilled labour market.

(2 marks)

(d) State any THREE (3) disadvantages of a **government wage control policy**.

- (i) _____
 - (ii) _____
 - (iii) _____
- (3 marks)

11. Foreign Trade and Foreign Aid (4 marks)

In this global economy, foreign trade and foreign aid are very important to developing nation like Solomon Islands.

(a) Differentiate between **foreign trade** and **foreign aid**.

(2 marks)

(b) Explain how **foreign trade** can help Solomon Islands develop?

(2 marks)

12. Economic Growth Policies (8 marks)

Economic growth is an objective of government economic policy because it is one of the keys to higher standards of living and working conditions, greater life expectancy and a better life.

(a) (i) Explain what **monetary policy** is.

(2 marks)

(ii) Describe how an **expansionary monetary policy** works.

(2 marks)

(b) (i) Explain what **fiscal policy** is.

(2 marks)

(ii) Describe how an **expansionary fiscal policy** would reduce unemployment in the domestic economy.

(2 marks)

Section D: P1 & P2

45

SECTION E: ECONOMIC DEVELOPMENT

(31 MARKS)

Part 1. Multiple Choice Questions (5 marks)

Circle the letter of your best chosen answer.

1. The economic characteristic of underdeveloped countries includes a;
 - A. low life expectancy.
 - B. very high illiteracy rate.
 - C. lack of social overhead capital.
 - D. persistent balance of payments surplus.

2. An example of a **transfer payment** is;
 - A. rent.
 - B. profit.
 - C. government purchases.
 - D. unemployment benefits.

3. **Economic growth** is depicted by a;
 - A. shift in the production possibilities frontier outward.
 - B. movement from inside the curve toward the curve.
 - C. no changes in the production possibilities frontier.
 - D. shift in the production possibilities frontier inward.

4. **Sustainable economic development** refers to the type of development that;
 - A. ensures a balanced development of all productive sectors in the economy.
 - B. lays emphasis on the use of scarce resources of developing countries.
 - C. creates attainable financial and environmental goals for future generation.
 - D. incurs minimum financial and environmental burden on future generation.

5. The **infant mortality rate** would be very high in;
 - A. developed countries.
 - B. less developed countries.
 - C. least developed countries.
 - D. newly industrialised countries.

Part 2. Short Answer Questions

6. Economic growth and Economic development (8 marks)

(a) Describe **Economic development**.

(2 marks)

(b) State any THREE (3) benefits of **Economic growth** to a nation.

1. _____

2. _____

3. _____

(3 marks)

(c) Identify any THREE (3) major sources of **Economic growth**.

1. _____

2. _____

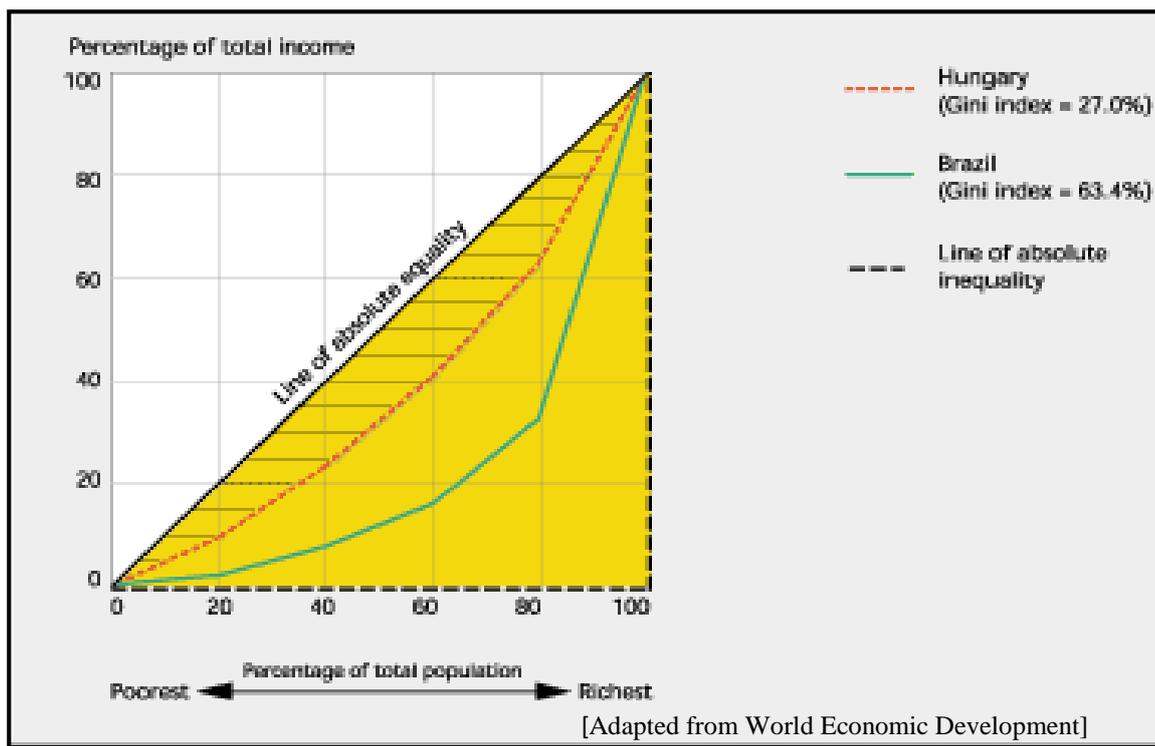
3. _____

(3 marks)

7. Income Inequality (3 marks)

Study the graph given below and answer questions (a) and (b).

Lorenz Curves and Gini indexes for Brazil and Hungary



(a) State which country has a high level of **income inequality**.

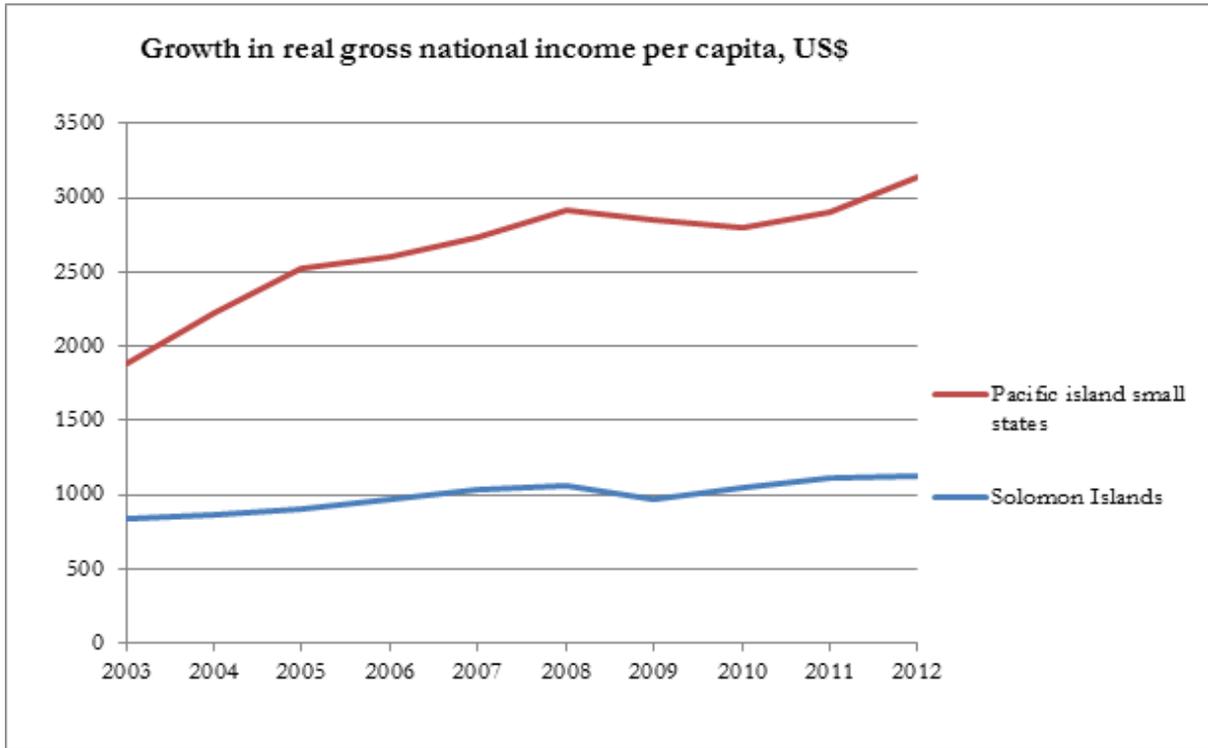
(1 mark)

(b) Explain what the line of **absolute equality** represent.

(2 marks)

8. Real Gross National Income Per Capita (4 marks)

Consider the graph below to answer questions (a) and (b).



Source: World Development Indicators, Atlas method.

(a) Describe the trend in the growth of real gross income per capita of Solomon Islands over the ten years period.

(2 marks)

(b) What is the importance of an increase in **real gross income per capita** to a nation?

(2 marks)

9. Development programmes (4 marks)

Many developing countries aim to achieve development through development programmes.

(a) Identify any TWO (2) main sources of financing development programmes.

(i) _____

(ii) _____

(2 marks)

(b) Explain an argument **against** foreign investment in developing countries like Solomon Islands.

(2 marks)

10. Measures to Increase Development (3 marks)

Identify THREE (3) ways through which the government can encourage **economic growth** in Solomon Islands.

1. _____

2. _____

3. _____

(3 marks)

11. Economic Issues of Unsustainable development (4 marks)

Read the extract below and answer questions (a) to (c).

Box 3: Logging in Solomon Islands

Deforestation in Solomon Islands provides a good example of a failure to adequately consider environmental costs. Logging for export started in 1961, and has accelerated over the past few years. Half the viable (non-steep-sloped) resource has now been logged, with extraction rates having almost doubled between 1991 and 1992. At current rates, harvesting cannot be sustained for more than eight years and the cessation of logging is likely to reproduce a significant drop in national income and output. A recent economic assessment by the Asian Development Bank estimates sustainable annual yields at 270,000m³, yet logging licences have been granted for up to 1.4 million m³ per annum. Reforestation will take 30 to 40 years in those areas that have been carefully logged. There has been widespread disregard of environmental protection controls with the results that reforestation may take anything from 45 to 200 years. Significant under-reporting of volumes and values has eroded the returns to Solomon Islands in the form of royalties and export taxes. No significant environmental analysis has been used as an input into decisions about logging in Solomon Islands, despite available evidence from other parts of the world which high-lights that costs, in similar circumstances, can be substantial.

Source: UNDP 1994

(a) What is the main **economic issue** highlighted in this article?

(1 mark)

(b) If the trend in the use of Solomon Islands natural resources as highlighted in this article continues, what will happen to its **national income**?

(1 mark)

(c) Describe any ONE (1) role the Solomon Islands government can play to address the environmental issue in the article above.

(2 marks)

ECONOMICS 2018

Student Personal Identification Number

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FOR MARKER USE ONLY

SECTION	EXAM MARKS	MARKER	SCRIPT CHECKER
A	52		
B	33		
C	39		
D	45		
E	31		
TOTAL	200		
Marker / Checker Initials			