Candidates' Performance

Paper 1

Candidates' performance was generally good. The mean score of this paper is 29 out of 45. The following questions deserve special attention.

Q1. A famous football team, Manchester United, visited Hong Kong for a friendly match. The day before the match, the team found the pitch in the Hong Kong Stadium had been damaged by prolonged rain and it considered cancelling the match. The opportunity cost for Manchester United to continue playing in such a poor pitch would _____ because _____.

*A.	increase ..... there was a higher chance for the players to get injured	(32%)
B.	increase ..... the team was likely to have poor performance	(4%)
C.	remain unchanged .....the expense on the visit to Hong Kong had already been paid	(23%)
D.	remain unchanged ..... the players spent the same amount of time in Hong Kong	(41%)

This question examines the concept of opportunity cost. Many candidates overlooked ManU's concern about the higher probability of its players getting injured if they played on the poor (rather than a normal) pitch, which would cost them higher medical expenses and may increase their chances of losing in subsequent games in the Premier League and the UEFA Champions League. These extra costs (net of the penalty due to breach of contract) could be avoided if they chose not to play.

Q28. The Old Age Living Allowance (長者生活津貼) introduced by the Hong Kong government increases the _____ in GDP and results in a _____ shift of the aggregate demand curve.

A.	government consumption expenditure ..... rightward	(46%)
B.	government consumption expenditure ..... leftward	(5%)
*C.	private consumption expenditure ..... rightward	(48%)
D.	private consumption expenditure ..... leftward	(1%)

This question examines the effect of an exogenous change in government policy on the aggregate demand curve and consumption expenditure. Many candidates mistook the welfare payment to the elderly for government expenditure. The old age living allowance is actually a transfer payment (rather than government expenditure), and would only affect aggregate demand indirectly via an increase in disposable income and thus the consumption of the elderly.

Q34. Deflationary (output) gap

A.	will be widened when there is a depreciation of the domestic currency.	(9%)
B.	will be eliminated by a rightward shift of the aggregate demand curve when the market adjusts from short run equilibrium to long run equilibrium.	(31%)
*C.	will result in a downward pressure on the prices of inputs.	(42%)
D.	will exist if the aggregate demand falls short of the short run aggregate supply.	(18%)

This question is about the deflationary (output) gap. Some candidates did not understand the adjustment mechanism from the short run equilibrium to the long run equilibrium. Many mistakenly thought that aggregate demand would adjust to close the gap in the long run--ignoring the fact that the excess supply of goods and factor inputs under the deflationary gap would exert downward pressure on prices and cause a leftward shift in the aggregate supply curve over time.

43. Which of the following is included in the calculation of the balance of Hong Kong's current account?

A. A mainland investor purchases a house in Hong Kong. (39%)
B. A Hong Kong investor buys shares issued by a mainland listed company. (11%)
C. A mainland resident buys an air ticket to Hong Kong from a mainland airline. (12%)
*D. A Hong Kong resident buys a life insurance policy from a mainland insurance company. (38%)

This question tests candidates' knowledge about the balance of payments. The purchase of a house in HK by a mainlander would be recorded in the capital and financial account, but many candidates erroneously thought that it should be included in the current account. The purchase of life insurance policy is a kind of financial service, and would thus be included in the service component of the current account.

44. The following table shows the data about Country A.

	Petroleum (unit)		Rubber (unit)
Total output with no international trade	60	and	90
Total output with specialization and international trade	0	and	210
Total consumption with international trade	90	and	120

Which of the following statements about Country A is correct?

A. Country A has both absolute advantage and comparative advantage in producing rubber. (10%)
B. The gain from trade of exporting 1 unit of rubber is 1 unit of petroleum. (20%)
C. The opportunity cost of producing 1 unit of rubber(R) is 2/3 units of petroleum(P) and the terms of trade is 1R=3/4 P. (31%)
*D. Country A can benefit from trading with Country B, whose opportunity cost of producing 1 unit of rubber is 2 units of petroleum. (39%)

The question involves selection and manipulation of relevant numbers from the trade table. Many candidates failed to keep track of the meaning of different numbers and to figure out the correct volumes of the country's exports and imports. In particular, it had exported 90(=210-120) units of rubber in exchange for 90 units of petroleum. Thus, the terms of trade is given by 1R=1P, rather than the ratio of total consumption of the two goods (1R=3/4P).

Paper 2

Section A

Q. number	Performance in General
1(a)	Excellent. Only a few candidates were confused about the meaning of the word "necessarily" in the question.
1(b)	Good. Some candidates failed to consider the possibility of an increase in the value of third options in affecting the highest-value option forgone. In their explanations, candidates sometimes confused the concept of "cost" with "value".
2(a)	Excellent. A minority of candidates erroneously thought that the question was about types of production.
2(b)	Fair. Most candidates realized that they should not give examples of fixed cost in their answers. But many of them chose to provide examples of variable factors, such as electricity and part-time workers, instead of variable cost. Among those who were able to give a correct example, some did not explain how cost varies with output.
2(c)	Good. However, a few candidates used inaccurate terms like "monopolistic" or "competitive monopoly" in their answers.
3	Satisfactory. Most candidates showed adequate understanding of the concept of price floor, but provided incomplete analysis. Common mistakes included: – not using the diagram to answer the question; – mistaking P_a for an effective price floor; and – confusing the concepts of the two adjectives, "effective" and "efficient."
4(a)	Good. A majority of candidates got the correct answer, though some failed to support the type of expansion with good reasons. Instead of expressing their answers explicitly in terms of the previous stage of production, they merely copied from the stem to argue that Tai Fok Institute is a backward expansion because it "provides professional training for chefs and managers for Chinese restaurants."
4(b)	Good. Many candidates related the case to the motives they suggested.
5(a)	Excellent.
5(b)	Fair. Many candidates failed to define the two price indices clearly and to provide proper comparisons between them.
5(ci)	Good. Most candidates were able to demonstrate understanding of the purchasing power of money.
5(cii)	Fair. Half of the candidates did not make good use of the given data to illustrate their answers. They either ignored the given rates of return and of inflation or failed to differentiate between the "expected" and "actual" rates.
6(a)	Poor. Many candidates did not understand the source principle. Some of them wrongly stated Karen's work location or residency in their explanation.
6(b)	Excellent.
7(a)	Satisfactory. Most candidates were able to explain the effects of contractionary fiscal policy using the AS-AD model. However, some candidates failed to provide a complete analysis; they simply rushed to the conclusion without elaborating on the process of changes in the macro variables.

Q. number	Performance in General
7(b)	Fair. While many candidates were able to state correctly the advantage(s) and disadvantage(s) of the alternative policy, some important steps were omitted in their reasoning, such as how a change in the interest rate (induced by monetary expansion) would affect output and the price level.
8(a)	Excellent.
8(b)	Good. Some candidates failed to express their answers in terms of "gain per unit of export". A few candidates committed careless computational mistakes. In their calculations and answers, candidates are advised NOT to use fractions and decimals at the same time.

Section B

Q. number	Performance in General
9(a)(b)	Good. Many candidates indicated accurately the prices, quantities, and tax burdens before and after tax on a supply-demand diagram. There was a technical problem in graphical presentation, however, that candidates should be aware of—the shading or using different colours to represent the tax burdens and the change in consumer surplus were sometimes hardly visible on the markers' computer screens. Candidates are thus advised to label the (3 or 4) corners of the relevant areas for these objects. A few candidates wrongly assumed inelastic demand and ignored the role of the demand and supply elasticities.
9(c)	Fair. Most candidates were able to state the law of demand correctly, although some omitted the clause "other factors being constant." Some weaker candidates stated the law inaccurately, such as "a rise in quantity demanded results in a rise in price," or "a rise in price results in an increase in demand." Regarding the concept of "relative" price, quite a few candidates failed to mention that the relative price had been altered by the per unit tax. The stronger candidates managed to express it in the form of "the relative price of large-bottle soft drink in terms of small-bottle ones," or illustrated their answers mathematically.
10(a)(i)	Good. Most candidates were able to foresee a reduction in labour supply, leading to a reduction in tax revenue in the future. A few candidates attributed this to the "rising old dependency ratio and thus more elderly in the future", However, this constituted an incomplete answer.
10(a)(ii)	Satisfactory. Most candidates stated correctly that both the welfare and public health expenditure would increase, but were unable to provide a clear explanation. For example, many candidates failed to point out the greater need of public health by the elderly.
10(b)	Good.
10(c)	Good. Some candidates only gave "limited company" as their answer. This was inaccurate.
10(d)	Good. The majority of candidates were able to explain the difference between the two types of ownership. However, a small number of them had either confused the concepts of limited liability and legal entity or omitted the comparison altogether.

Q. number	Performance in General
10(e)	Satisfactory. Common mistakes included failure to: – distinguish between the stock market and the product market; – observe that the rise in the stock price was the result of an increase in the demand for stocks; – note that an increase in future demand for the product could lead to high future profits and dividend payouts.
11(a)	Fair. Most candidates were able to point out that the demand for Japanese automobiles would increase as a result of the JPY-depreciation. But some candidates overlooked the condition that "the JPY-price of Japanese automobiles is constant" and wrongly drew a diagram that showed a rise in the JPY-price. Some other candidates mislabelled the Y-axis as "HKD-price of Japanese automobiles" and wrongly based their analysis on the price-elasticity of demand.
11(b)	Good.
12(a)	Good. However, a minority of candidates failed to show a good understanding of the concept of monetary base.
12(b)	Satisfactory. The following contains a list of common mistakes: – confusing the open market purchase with an open market sale; – confusing the credit creation with a credit contraction; and – confusing central-bank purchase of bonds from commercial banks with similar purchase from the general public.
12(c)	Good. The majority of candidates were able to draw a well-labelled diagram and to explain clearly the policy effects. Some common mistakes included: – a failure to realize the question is about short-run effects, thus wasting effort on irrelevant long-run analysis; – mis-labelling the vertical axis of the AD-AS diagram as money or price (instead of the price level); and – a failure to provide a step-by-step analysis of how a change in the money supply would affect AD (e.g., omitting the step that shows how a drop in the interest rate would follow from an increase in money supply).

Section C

Q. number	Popularity	Performance in General
13(a)	57%	Good. The most common mistake was a failure to label the diagram properly using the notations provided by the question. Some candidates argued incorrectly that a price searcher would produce at the mid-point of its demand curve, while a minority of them stated the profit-maximizing condition as "marginal cost = marginal benefit," rather than "marginal cost = marginal revenue."
13(b)		Fair. Some candidates wrongly shifted the marginal cost or supply curve to the right. Others failed to use the correct symbols to label the diagram.

Q. number	Popularity	Performance in General
13(c)		Satisfactory. A few candidates failed to clarify the following: Given that the per-unit cost of production was the same, customers buying different amounts of beef would end up paying different prices (per unit) on average.
13(d)(i)(ii)		Good. Many candidates were able to "name" the anti-competitive behaviour. However, a minority of them did not explain properly how the behaviour restricted competition.
13(e)		Excellent.
14(a)	43%	Fair. Many candidates were able to point out that the opportunity cost of production was constant, but only some further explained the reason behind this.
14(b) (i)(ii)		Good. Most candidates were able to compute and compare the opportunity costs of producing Good X (in terms of Good Y) for Countries A and B and to draw a conclusion in terms of comparative advantage. However, some candidates failed to compare production costs for the same amount of resources for the two countries. They therefore arrived at a wrong conclusion about absolute advantage.
14(c)(i)(ii) (iii)		Satisfactory. A common mistake was that candidates failed to draw the consumption possibility curve and/or to locate the consumption point.
14(d)		Satisfactory. Some candidates did not quite understand the concept of human capital and gave irrelevant answers as a result.

General comments and recommendations

1. Some candidates lack a thorough understanding of basic economic concepts and principles, especially when applying them to solve hypothetical or real-life problems. Candidates should strengthen their analytical skills instead of simply regurgitating concepts and theories.

2. Some candidates fail to read the questions carefully. Candidates should devote special attention to the assumptions and conditions laid down in the questions to avoid giving incorrect or irrelevant answers.

3. Some candidates have difficulty in presenting their answers in a precise way. Candidates should equip themselves with better language abilities as well as graphical skills.

4. Some candidates lack an awareness of current economic issues in our society. Candidates should pay more attention to economic news.

5. Some candidates lack skills to extract information from tables and graphs as well as to draw well-labelled diagrams. Candidates should pay special attention to the headings, labels, and axes as they are essential to our understanding of the data presented therein.