

Candidates' Performance

Paper 1

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

Q.13 Which of the following is **INCONSISTENT** with the law of demand?

- *A. The abolishment of per unit import tariff on garment results in a rise in the quality of imported garments. (46%)
- B. Live fishes sold in a market near the fish farm have a higher price than frozen fishes sold in a faraway market. (12%)
- C. The ratio of high-quality white wine sold to total white wine sold remains unchanged when the government imposes an ad valorem tax on white wine. (32%)
- D. Developers tend to build higher-quality housing units on a piece of land with a good view. (10%)

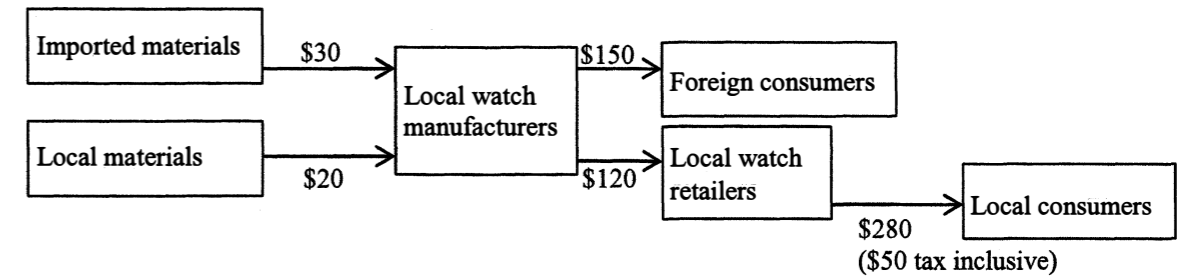
An ad valorem tax is a percent tax on the price of a good that reduces its supply and its quantity transacted in the market. But unlike a per-unit tax, such a tax does not alter the relative price of the high-quality good in terms of the low-quality one. Other things being equal, the quantities sold of both high-quality and low-quality white wine would decrease by the same proportion and the ratio of the former to the total amount of white wine sold would remain constant.

Q.18 Suppose the government imposed an effective rent control on living units. Which of the following would **LEAST** likely occur?

- A. There would be a shortage of living units. (10%)
- B. Black market would emerge. (32%)
- *C. Poor people would be able to rent a living unit more easily. (47%)
- D. Landlords would have a lower incentive to renovate their living units for rent. (11%)

Under an effective price ceiling, there would exist a shortage of (excess demand for) living units. This would likely result in a black market (not necessarily in the physical sense), where illegal contracts involving higher-than-controlled rental or contracts involving side benefits to the landlord may exist. Candidates may have erroneously thought that the price control would help the poor get more resources: As price competition was weakened, other forms of non-price competition would be used to determine the resource allocation. This may or may not be beneficial to the poor.

Q.25 The following diagram shows a production chain of watches in an economy:



The contribution of the local watch manufacturers to the economy's GDP at market prices is _____.

- *A. \$220 (40%)
- B. \$240 (11%)
- C. \$350 (16%)
- D. \$400 (33%)

Some candidates mis-interpreted the question and thus mis-calculated the contribution of the whole production chain of watches, probably by recalling answers to similar questions from past papers. Candidates are advised to read the question carefully.

Q.31. The following table shows the balance sheet of a banking system.

Assets (\$)		Liabilities (\$)	
Reserves	300	Deposits	900
Loans	600		

Suppose the public does not hold cash and the required reserve ratio is reduced to 25%. After deposit creation, the amount of loans in the banking system is \$750. Which of the following statements about the banking system is correct?

- A. The money supply increases by \$300. (31%)
- *B. The actual banking multiplier is 3.5. (36%)
- C. The deposits increase by \$600. (11%)
- D. Bank reserves are \$450. (22%)

This question does not assume that banks do not hold excess reserves. As the banking system might not be fully loaned up, the required reserve ratio could be used to calculate the maximum possible amount of deposits (and the corresponding money supply), but not the actual one. On the other hand, the amount of loans could be used to deduce the actual amount of deposits and the actual banking multiplier as reserves in the banking system should be constant.

Paper 2

Section A

Q. number	Performance in General
1	Fair. A common mistake made was that some candidates misunderstood the question as asking about the cost of working in a firm located in South Korea. Some weaker candidates mis-stated that the cost of the 2 nd option would be the 3 rd option. Most of those who understood the gist of the questions performed well in part (a) and correctly pointed out that the reason for a drop in cost is the drop in value of the 1 st option. In part (b), many candidates said that the value of the 2 nd option would drop. This deserved partial credit. Some candidates with a strong understanding of the concept of opportunity cost were able to provide proper reasons why the value of the 1 st option may drop (or why the value of the 3 rd option may even rise so that it is more preferred) to explain why the cost did not necessarily remain unchanged.
2(a)	Excellent. A minority of candidates confused the viewpoints of the employees and the employer.
2(b)	Fair. Many candidates were unable to differentiate between the concepts of total cost and average cost, so their answers only explained why (total) cost increases when output increases. Better candidates correctly stated the type of diseconomies of scale. However some failed to elaborate clearly and accurately. Weaker candidates were under the misapprehension that this was an example of economies (rather than diseconomies) of scale.
3	Good. A small number of candidates had difficulty in accurately spelling the term "oligopoly".
4(a)	Satisfactory. Most candidates demonstrated that they understood that there were positive externalities involved. However, many mistakenly thought that the existence of external benefits was due to a lack of compensation to the gamers, rather than to the game developer. Some candidates mistook it as a case of over-production instead of under-production, while others failed to apply the concept of marginal social benefits/costs in their answers.
4(b)	Fair. Most candidates who demonstrated that they understood that it was a case of positive externality in part (a) correctly pointed out that the restaurants should pay compensation to the game developer. However, some of them mistakenly thought that the gamers should be paid. A minority of candidates talked about how the government could intervene (e.g., by providing a subsidy to the game developer). This was irrelevant to the question.
5	Good. Many candidates were aware of how an unstable and depreciating currency would dampen the store-of-value and standard-of-deferred-payment functions of money. A small number of candidates provided irrelevant answers, such as the functions of price or the features of good money.
6(a)	Fair. Many candidates were able to point out that general sales tax revenue is more stable than income tax revenue, but some failed to explain the reason, i.e., consumption is less volatile than income over the business cycle.
6(b)	Satisfactory. A common mistake was to state salaries tax as the answer without specifying the standard tax rate.
7(a)	Excellent. A minority of candidates mistakenly thought that both countries have the same amount of resources and thus reached the wrong conclusion in part (i). A few candidates lost marks in part (b) as they failed to show the correct calculation of the opportunity costs of production in the two countries.
7(b)	Good. Some candidates were not aware of the difference between per-unit gain from trade and total gain from trade.

Q. number	Performance in General
8(a)	Excellent.
8(b)	Excellent. A minority of candidates overlooked the key word "change" in the deposits and thus failed to reach the correct answer.
9(a)	Good. The only problem was the inaccuracy in spelling.
9(b)	Good. A majority of candidates correctly deduced the effect of a reduction in the interest rate on consumption and/or investment and thus aggregate demand and output. A small number of candidates argued that there was an increase in SRAS without providing a concrete elaboration.
9(c)	Fair. Common errors made by those who failed to get the correct answer included: <ul style="list-style-type: none"> - confusing the two sets of data shown in Figure 2; - mis-interpreting the word "consistent"; - mis-quoting the data in Figure 2, e.g., referring to unemployment and GDP instead of unemployment rate and GDP growth rate in their answers.
9(d)	Good. Most candidates were able to suggest relevant policy to boost output. A minority of candidates wrongly argued that policies stimulating aggregate demand could help increase LRAS.

Section B

Q. number	Performance in General
10(a)	Good.
10(b)	Satisfactory. Most candidates managed to provide sound arguments for and against the suggestion for the government to wholly own MTRC. The following is a list of mistakes and omissions: <ul style="list-style-type: none"> - failure to assess the suggestion from the perspective of society; - mis-labelling arguments "for" the suggestion under the heading of arguments "against", or vice versa; - failure to support arguments with proper elaboration in economic terms, e.g., they mentioned that the government could adopt policies to benefit consumers after taking over MTRC or that the government could resolve market failure, but they were unable to substantiate their arguments.
10(c)	Fair. Many candidates failed to realise that both price and quantity transacted had increased. They simply recalled the definition of inelastic demand and tried to match the data with the definition without taking account of the increase in total passengers boarding. Some candidates were able to give a nice interpretation of the figures and were aware of the increase in both price and quantity transacted, which contradicts the negative relation between price and quantity demanded in the case of inelastic demand. The better candidates identified an increase in demand as the reason and illustrate the case in a well-labelled diagram.
11(a)	Good. Most candidates were able to indicate correctly the shift of supply as a result of education subsidy, but only some managed to provide a comprehensive illustration to account for the difference in shares of subsidy benefit by pointing out that supply is more elastic than demand. Some candidates were under the misapprehension that elastic supply or inelastic demand alone was sufficient for the students to enjoy a larger share of subsidy benefit than the private universities. Others wrongly compared consumer surplus and producer surplus, instead of consumer share and producer share of the subsidy benefit.

Q. number	Performance in General
11(b)	Satisfactory. Some candidates were able to indicate clearly, either in the diagram or in their verbal elaboration, that marginal cost exceeded marginal benefit at the after-subsidy equilibrium quantity. Some others committed the following mistakes: <ul style="list-style-type: none"> – believing that the after-subsidy supply curve is the marginal cost curve and wrongly concluding that the after-subsidy equilibrium was efficient; – mis-labelling the area of deadweight loss at a wrong location.
11(c)	Good. Most candidates were able to explain the effect of subsidising education on equalising opportunities and/or equalising future income. Some candidates failed to emphasise that the impact of the policy fell mainly on the low-income group.
12(a)	Good. Many candidates were able to explain how Brexit would lower the geographical mobility of low-skilled workers from the EU. A small number of candidates missed the term “geographical”, and a few failed to accurately state the direction of the effect.
12(b)	Satisfactory. Most candidates made a good attempt to analyse the effect on aggregate output by using appropriate tools. The following problems were identified: <ul style="list-style-type: none"> – failure to relate the change of AD to the global investors’ view and the change in SRAS to the British firm owners’ view; – mislabelling of the y-axis as \$, SRAS as S, AS curves as D, AD curves as SRAD; – failure to indicate correctly the new equilibrium price level and aggregate output at the intersection of the new SRAS and AD curves; – mistaking quantity transacted for aggregate output.
12(c)	Fair. Similar to the questions in the past, some candidates were not familiar with the components of the current account in the BOP, and failed to provide clear and accurate answers as a result. Some candidates did not start their analysis from the standpoint of Britain, and thus got the direction of invisible trade and factor income wrong. Another common mistake was to consider labour services offered by British citizens in EU countries as visible trade. Some weaker candidates mistook transfer payment for current transfer and the invisible account for invisible trade account.
13(a)(i)	Good. Most candidates were able to identify the type of production in question, but some of them failed to spell the word “tertiary” correctly.
13(a)(ii)	Good. Most candidates were able to point out that GDP would rise. A few candidates wrongly regarded \$30000 as a transfer payment and concluded that there would not be any change in HK’s GDP.
13(b)	Satisfactory. Most candidates were able to apply economic concepts and theories correctly to identify the effects of the two proposals. Their performance in this particular question has shown improvement when compared to similar questions last year. The following contains a list of mistakes for both parts that deserve attention: <ul style="list-style-type: none"> – failure to focus their analysis on the proposals to finance the scheme, but devoting much of their effort to elaborate on the effects of the transfer payment instead; – poor organisation of answers, without clear indication as to which of their arguments refers to which proposal. <p>Part (i): The performance was good in answers related to proposal A. The performance was poor in answers related to proposal B. Many candidates did not realise that no extra tax would be charged, so that there would be no extra effect on aggregate output. In their answers, many candidates tried to explain the effect of transfer payment on aggregate output, which is not what the question is asking.</p>

Q. number	Performance in General
	<p>Part (ii): The performance was good in answers related to proposal A. Many candidates had a good understanding of the concept of income inequality, and were able to reach their conclusions by examining the effect of the change in the tax structure on the high-income group and the low-income group respectively.</p> <p>The performance was poor in answers related to proposal B. Most candidates focused on the transfer payment and reach an irrelevant conclusion. A minority of candidates made use of their knowledge outside of the textbook on this topic and explained that future generations may be worse off.</p> <p>Part (iii): The performance was fair. Many of those candidates who attempted to analyse an economic variable other than output and income distribution gave a correct answer with appropriate reasons, such as a decreasing price level for a drop in AD and a rising unemployment for a drop in AD, etc.</p>

Section C

Q. number	Popularity	Performance in General
14(a)(i)(ii)	57%	Fair. Some candidates ignored the important information of zero marginal cost, and therefore gave a wrong answer. Some others wrongly labelled the marginal cost curve as a supply curve. Some mis-used Q_E to represent the equilibrium output instead of efficient output. In their verbal elaboration, some candidates mistakenly stated the profit-maximising condition as $MB=MC$, $MB=MR$ or MC =marginal return.
14(b)(i)		Good. Most candidates were able to define price discrimination correctly, but not all of them could explain how the definition is related to the cases given. In part (i), a common mistake was to view the lower price offered to new customers as a strategy to attract these new customers rather than price discrimination. A few candidates inaccurately used the terms “first-degree / second-degree / third-degree price discrimination” in their answers, thus showing poor understanding of the concepts of price discrimination.
14(b)(ii)		Fair. Even though many candidates were able to see that it is not a case of price discrimination, some of them put too much emphasis on the different services involved in their answers. They failed to explain their answers in terms of the lower cost involved when subscribing to two kinds of services.
14(c)(i)(ii)		Good. Most candidates identified the type of anti-competitive behaviour and correctly stated that it violated the first conduct rule. However, some candidates failed to provide a clear explanation and to use the keyword “agreement”.
15(a)(i)	43%	Excellent. Most candidates were able to indicate the correct position of C_A and give a proper explanation.
15(a)(ii)		Satisfactory. Some candidates failed to draw a line tangent to P_A and were thus unable to show the opportunity cost of producing Good X correctly.
15(b)(i)(ii)(iii)		Fair. Mistakes in the graphical illustrations included: <ul style="list-style-type: none"> - failure to draw a CPF parallel to TT'; - wrong labelling of the tangency point between AA' and CPF as the consumption point C_T; - mis-representation of the volume of imports as the gap between P_A and C_T, or between P_A and P_T, or confusing volume of imports with that of exports. Mistakes in the verbal explanations include: <ul style="list-style-type: none"> - failure to use the equilibrium condition $MC=TOT$ to determine the production point; - failure to match the explanation of the post-trade better-off Country A with the correct consumption point C_T.
15(c)(i)(ii)		Satisfactory. In part (i), many candidates correctly used the per-capita real GDP data to conclude that trade could enhance economic growth, but only some were able to provide proper, trade-related reasons. In part (ii), a small number of candidates wrongly drew on the data of 1990 and 2000. Among candidates who were able to give the correct standpoint, only some managed to provide logical reasons to explain why the HDI would remain unchanged despite of a rise in per-capita real GDP.

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 do not always read the questions carefully. Candidates should devote special attention to the assumptions and conditions laid down in the questions to avoid giving 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 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.