

## Candidates' Performance

### Paper 1

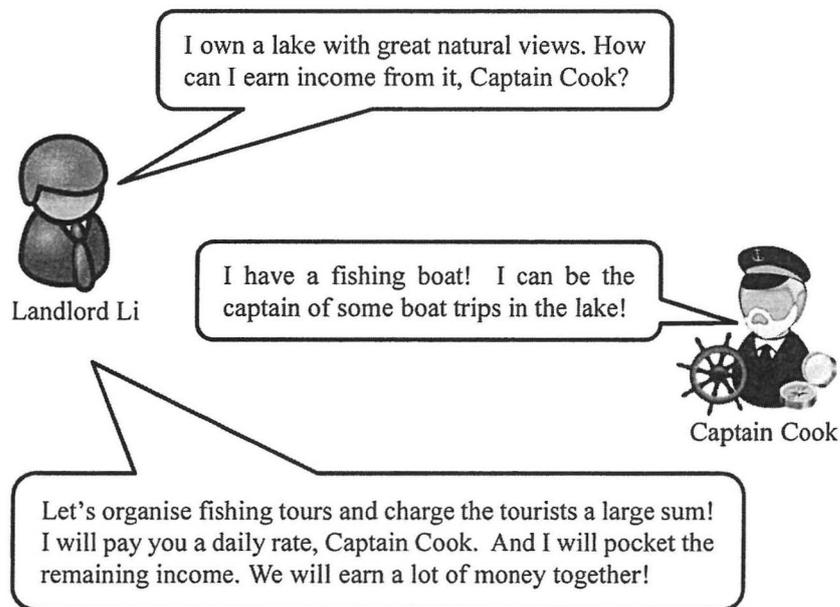
Candidates' overall performance was good. The mean score of this paper was 28 out of 45. The following questions deserve special attention.

Q.5 If a public limited company in Hong Kong gets listed on the stock exchange,

- A. it will face a higher profits tax rate. (7%)
- B. it can no longer keep its accounting information confidential. (42%)
- \*C. its shareholders will enjoy higher liquidity of their assets. (40%)
- D. it will enjoy economies of scale. (11%)

Many candidates mistakenly picked option B. This suggests that they did not realise that a public limited company is required to submit its financial information to the Companies Registry, so that its financial information is accessible to the public whether it is listed on the stock exchange or not. The difference that 'listing' makes is that the company's shareholders can trade their stocks for cash on the stock market. Therefore, option C is the key.

Q.6 Refer to the following dialogue.



Given the return of land is rent, the return of labour is wage, the return of capital is interest while the return of entrepreneur is profit. The income earned by Captain Cook consists of \_\_\_\_\_ while the remaining income earned by Landlord Li consists of \_\_\_\_\_.

- A. wage.....profit (51%)
- B. interest .....rent and profit (3%)
- C. wage and interest.....rent (4%)
- \*D. wage and interest .....rent and profit (42%)

This question is about factors of production and their corresponding incomes. A person may perform more than one role in the production process and may thus earn more than one kind of income. As a land owner and an entrepreneur, Landlord Li receives both rental and profit incomes. As a provider of both capital and labour services, Captain Cook earns interest and wage incomes respectively.

Q.25 Which of the following should be deducted from the gross domestic product of Hong Kong to calculate the gross national income of Hong Kong?

- \*A. the fee paid by a Hong Kong football club to a Japanese football team for an exhibition match in Hong Kong (53%)
- B. the rent earned by a Hong Kong property developer from its residential property in Japan (10%)
- C. the capital gain earned by a Japanese insurance corporation from its financial investment in Hong Kong (27%)
- D. the dividend paid by a listed company in Japan to a Hong Kong resident (10%)

This question is about factor incomes from/to abroad. Most candidates correctly ruled out options B and D. Since factor incomes were earned by local residents from abroad in both cases, they should be added to (rather than deducted from) Hong Kong's GDP to calculate its GNI. Most capable candidates also managed to rule out option C, realising that capital gains are not considered as factor income. Option A is the best answer, as it describes a situation that might be conceived as a resident producing unit of Hong Kong employing which pays 'wages' to foreigners as a labour input in the production of the football match. Statistics shows that this question effectively discriminates able candidates from weaker ones.<sup>1</sup>

Q.33 Which of the following will increase the actual banking multiplier?

- A. The public tends to hold more cash. (22%)
- \*B. The use of credit card becomes more popular. (36%)
- C. The central bank increases the required reserve ratio. (18%)
- D. The interest rate of bank deposit decreases. (24%)

Most capable candidates were able to rule out options A, C, and D, which would all cause a reduction in actual deposits and reserves and tend to narrow the scope of credit creation. Option B implies that there is a drop in the public's willingness to hold cash, resulting in a larger quantity of deposits and reserves in the banking system. The banking multiplier would attain its maximal effect (i.e., actual deposits = maximum possible amount of deposits) when the following standard assumptions are satisfied—i.e., absence of cash leakage and of excess reserves held by banks. The further the actual economy deviates from these assumptions, the weaker the multiplier effect. If people use credit cards (or e-payments) to settle transactions more often, they need not hold too much cash in their pockets (i.e., less cash leakage). Instead, they would keep a larger amount of deposits in their banks and withdraw deposits less often. As banks expect such change in deposit-withdrawal behaviour, they need not hold a lot of reserves (i.e., less excess reserves); they can safely make more/bigger loans. Under this situation, when the standard assumptions are more or less satisfied, the actual banking multiplier would likely be close to its maximum possible level.<sup>2</sup>

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<sup>1</sup> In standard textbooks, the classification of 'income paid abroad' focuses on the identity of the recipient (i.e., whether the sum of money is paid to a foreign, rather than domestic, resident) and the nature of income (i.e., whether the sum is viewed as factor income). Instead of classifying the fee mentioned in option A as such (i.e., as NIA), one may argue that this fee should better be treated as 'import of services'. In authentic contexts, the correct way to classify the fee is determined by the precise terms specified in the contract between the HK football club and the Japanese football team. Such complications in the accounting treatment of BOP involved in the actual arrangements of business activities are not the intention of this exam assessment. Students are not expected to look into such details in answering this question.

<sup>2</sup> It is not advisable to use a mathematical approach to tackle this question because it would be very difficult to calculate the change in the amount of actual deposits due to the change in cash leakage (i.e., cash-deposit ratio) and to the change in the banks' tendency to hold excess reserves (i.e., actual reserve ratio) in this context. As a side note, the manipulation of cash-deposit ratio in the analysis of credit creation is not required in the Curriculum.

Paper 2

Section A

Q. number	Performance in General
1	Satisfactory. The majority of candidates correctly pointed out that a free good is necessarily free-of-charge and supported their stand by some features of a free good. However, some candidates just recited the definition of free good without relating their arguments to the question, thus failing to obtain the full score for this question.
2(a)	Satisfactory. Some candidates failed to give a proper explanation for the type of expansion they named.
2(b)	Good. A few candidates listed some motives which did not suit the expansion in this case, e.g., increasing market share.
2(c)	Good. Instead of providing reasons for the declining average cost, some candidates simply listed additional motives behind the expansion. A few thought that the question was asking about increasing average cost and gave irrelevant answers.
3(a)	Excellent.
3(b)	Good. A few candidates did not read the question carefully and included 'increase in unemployment rate' in their answers.
3(c)	Good. Some candidates regarded an increase in welfare payment as a loss to society.
4(a)	Good. A few candidates had problems in rounding off the inflation figures.
4(b)	Satisfactory. Some candidates failed to explain the difference between CPI and GDP deflator from a single perspective. Instead, they merely stated one feature of CPI and another feature of GDP deflator without pointing out the difference.
4(c)	Satisfactory. Most candidates wrote the correct quantity equation, but only a few got full marks. The following lists some of the mistakes found in their answers: <ul style="list-style-type: none"> <li>-failing to define the variables M, V, P, and Y;</li> <li>-failing to realise that classical QTM assumes that V and Y are constant;</li> <li>-failing to mention that inflation is a continuous and sustained increase in the price level;</li> <li>-mis-thinking that open market purchase of government bonds would result in a fall in the money supply.</li> </ul>
5(a)	Good. Many candidates were able to point out that holding cash implies forgoing the option to earn interest income from various means of financial investment, such as bank deposits or bonds. Weaker candidates could only state the definition of opportunity cost without elaborating on the kind of investment return people have to give up while holding cash. Some simply put down the term 'interest' without explanation.
5(b)	Satisfactory. The majority of candidates were able to compare cash and the supermarket coupon from the perspective of 'functions of money' or 'features of good money'. A common problem was the inaccuracy or imprecision in using such terminology as general acceptability, divisibility, durability, medium of exchange, and store of value, resulting in vague or inconsistent answers.
6	Satisfactory. Some candidates failed to realise that the market adjustment operates via a leftward shift in the SRAS curve to restore output to its full-employment level. Instead, they shifted either AD or LRAS. A few candidates left out the reason behind the SRAS adjustment, i.e., a rise in production cost due to excess demand in the factor market.
7(a)	Good. In determining the direction of trade, a few candidates mistakenly compared the unit cost of cars with that of toys in a given country. Some missed out the unit in their calculations. Others did not state explicitly that country B enjoys comparative advantage in producing and exporting toys because it has a lower opportunity cost in producing toys than country A.

Q. number	Performance in General
7(b)	Satisfactory. Some candidates overlooked the keywords 'the cost is equally shared by both countries' in the question and thus got the wrong answer.
8(a)	Excellent.
8(b)(i)	Good. Many candidates demonstrated understanding of how the monetary base would change in the case of cash withdrawal.
8(b)(ii)	Good. Most candidates calculated the required reserve ratio correctly. However, some made the following mistakes: <ul style="list-style-type: none"> <li>- neglecting the word 'change' and calculating only the new level of money supply;</li> <li>- failing to state verbally that there was a 'drop' in money supply OR failing to give a 'negative' figure as their numerical answer;</li> <li>- omitting the unit (i.e., \$ million) in their answers.</li> </ul>

### Section B

Q. number	Performance in General
9(a)	Good. The only problem was that a minority of candidates misspelled the term 'oligopoly' or created a term like 'oligopoly competition'.
9(b)	Satisfactory. Most candidates demonstrated understanding of the AS-AD model and correctly presented the case in a proper diagram. In their verbal explanation, many candidates were able to point out that a rise in tourist spending would lead to an increase in net export, but only some clearly stated that there was an increase in the export of services. Common errors included: <ul style="list-style-type: none"> <li>-misconceiving an increase in tourist expenditure as a rise in consumption expenditure;</li> <li>-mistaking the expense on infrastructure development for an increase in government expenditure or an increase in labour supply;</li> <li>-failing to elaborate on how the case would lead to an increase in LRAS;</li> <li>-mislabelling the horizontal axis as price or \$.</li> </ul>
9(c)	Satisfactory. Some candidates merely stated the advantages of issuing shares without mentioning in what ways it is better than obtaining bank loans as a means of raising capital. Some erroneously thought that issuing shares could help Ocean Park raise capital more easily or raise more capital than bank loans. Others mis-read the question and focused on the difference between shares and bonds.
9(d)	Fair. Many candidates were able to identify the source of discrepancy, but not everyone could provide a clear explanation. For instance, some candidates merely provided the terms 'inventory' or 'imports' without mentioning that these goods are not produced in the current period or not produced by domestic firms.
10(a)(i)	Satisfactory. Common mistakes included <ul style="list-style-type: none"> <li>- missing the word 'balance' in their discussion of trade/current account balance;</li> <li>- mixing up the 'balance of goods and services' with 'balance of current account'.</li> </ul>
10(a)(ii)	Satisfactory. Most candidates were able to point out that there are other sub-accounts within the current account. One common mistake was the confusion between 'current transfer' and 'transfer payment'.

Q. number	Performance in General
10(b)(i)(ii)	<p>Satisfactory. Most candidates correctly stated one such condition, but a few candidates missed some important steps in their verbal explanation or made some errors in their diagrams. Common mistakes are listed below:</p> <ul style="list-style-type: none"> <li>- mis-matching perfectly elastic demand with a vertical demand curve OR perfectly inelastic supply with a horizontal supply curve;</li> <li>- failing to mention that the after-tax market price would stay unchanged, so that the consumers would bear no tariff burden;</li> <li>- failing to identify correctly the after-tax market price and/or the per-unit price the sellers can receive net-of-tax, and thus to indicate correctly the tariff revenue.</li> </ul>
10(c)	<p>Good. One common error was to wrongly include the tariff revenue in the after-tariff producers' surplus and mis-labelling the latter area as <math>bcd</math>.</p>
10(d)	<p>Satisfactory. The majority of candidates correctly suggested the advantage and disadvantage from the viewpoint of the US government. However, some erroneously thought that tariff would lead to a rise in import prices while quota would not, OR that tariff might lead to retaliation from other countries while quota would not.</p>
11(a)	<p>Good. A few candidates simply provided a sentence or two without saying whether it was an advantage or disadvantage.</p>
11(b)	<p>Good. Most candidates were able to illustrate the traffic-jam situation using a supply-demand diagram, but only some got full credits. Common mistakes/omissions included:</p> <ul style="list-style-type: none"> <li>- failing to state that 'the price is set below its equilibrium (market-clearing) level' in their verbal elaboration;</li> <li>- drawing an upward-sloping, rather than vertical, supply curve;</li> <li>- stating imprecisely that shortage corresponds to the situation where demand is bigger than supply (rather than 'the quantity demanded is bigger than the quantity supplied at the given price/toll');</li> <li>- referring to a case of an increase in demand (not mentioned in the given information) as the cause of shortage in their diagrams.</li> </ul>
11(c)(i)	<p>Fair. Some candidates did not mention that other drivers using the tunnel are adversely affected, or that they are not compensated for these adverse effects. Others failed to use the information from source C to support their answers, e.g., they cited air pollution as an example of external cost.</p>
11(c)(ii)	<p>Fair. Only some of the candidates were able to pinpoint the gist of the inefficiency in this case— i.e., <math>MSC &gt; MSB</math> and over-use of the tunnel. Instead, some wrongly explained inefficiency by comparing marginal private cost with marginal private benefit, or claimed that <math>MSC &gt; MSB</math> would result in under-production.</p>
11(d)	<p>Excellent.</p>
11(e)	<p>Satisfactory. The following are some general comments.</p> <ul style="list-style-type: none"> <li>- Many candidates were able to organise their arguments on behalf of different stakeholders in separate paragraphs, and present them in an orderly way.</li> <li>- A few candidates provided a list of the effects of both proposals, which was not required.</li> <li>- While considering the preference of a given stakeholder, some candidates sometimes included discussion of some other stakeholders, to the detriment of the clarity of their answers.</li> <li>- Some weaker candidates just copied data from the sources without analysing them before concluding which proposal is preferred by which stakeholder.</li> </ul> <p>Comments on sub-questions are listed below:</p> <p><u>For the owners of the WHC company</u></p> <p>Some candidates failed to realise that WHC is a private firm so the original price it sets should be profit-maximising. Others failed to use more precise terms, such as a change in the demand for WHC service or competitive demand, in their elaborations. Instead, they described the situation loosely as a change in the usage of the 2 tunnels upon toll adjustments under the 2 proposals.</p>

Q. number	Performance in General
	<p><u>For income inequality</u> Quite a number of candidates were able to provide proper reasons to support their choice between Proposal I and Proposal II. But some of their explanations were incomprehensive. For example, some candidates argued for Proposal I on the grounds that the toll raise would only affect the rich, without mentioning that most rich people drive private cars while the poor commute by public transport. Others argued for Proposal II on the ground that the toll cut would relieve the poor's burden, without mentioning that the percentage drop in toll (as a regressive tax) for the low-income group is bigger than that for the high-income group.</p> <p><u>For government revenue and/or expenditure</u> Some candidates were able to give concise and precise explanations to demonstrate their in-depth understanding of public finance. In discussing the effects of externality or the difficulty in negotiation with WHC about the toll adjustment, however, some merely referred to the information in Source C or Source F without addressing the gist of the question.</p> <p><u>Other stakeholders</u> Most candidates tried hard to identify a group of stakeholders and to deduce their stand as a group by examining the effects of the two proposals on such a group. One common problem was that they simply named their chosen group vaguely as 'people,' or 'citizens,' or 'drivers,' making it difficult to analyse precisely the effects of the two proposals on different members of the group separately and then to aggregate the effects across these members to reach a conclusion for the group as a whole. For those who picked a better-defined group of stakeholders (e.g., taxi drivers, or environmentalists), their discussion sometimes neglected the fact that both proposals can reduce the traffic jam, so alleviation of traffic congestion cannot be used to support one proposal against another.</p>
11(f)	Satisfactory. A few candidates did not read the question carefully, and stated taxation on cross harbour tunnels or toll adjustment as their answers.

## Section C

Q. number	Popularity	Performance in General
12(a)	58%	Satisfactory. Some candidates wrongly drew an upward-sloping marginal cost curve. Others did not state the profit-maximising condition in their verbal elaboration, or simply stated 'marginal benefit = marginal cost' as the condition.
12(b)		Poor. Many candidates did not realise that the imposition of a lump-sum tax would not affect marginal cost or marginal revenue.
12(c)		Good. Most candidates were able to apply their knowledge of price discrimination in answering this question. Many of them correctly identified the higher cost of electricity production in the rural area as a proper explanation for (non-discriminatory) differential pricing.
12(d)(i)		Excellent.
12(d)(ii)		Satisfactory. Some candidates wrongly stated the harm such anti-competitive behaviour would inflict upon the consumers, instead of ABC Company. Others wrongly conceived that the company had violated the law and would thus be punished.
13(a)		42%
13(b)	Satisfactory. Some candidates did not realise that country A would not specialise completely in producing one single good. Others had difficulty in explaining how they could find the production point of country A in part (ii).	
13(c)(i)	Satisfactory. A few candidates misread the question and thought that the productivity of both Good X and Good Y doubled simultaneously. Others did not support their answer with a proper calculation of the new opportunity cost.	
13(c)(ii)	Fair. One common mistake was to use GNI, instead of per capita GNI, to explain the AI-effect on economic development. Overlooking the difference between economic growth and economic development, some candidates focused their discussion narrowly on per capita GNI and ignored the other two aspects of HDI (i.e., education and health).	
13(c)(iii)	Good. Candidates should be reminded that, while increases in the quantity/quality of capital goods or in the quality of labour would help boost economic growth via an increase in GNI, any factor contributing to an increase in the population only may not lead to an increase in per capita GNI (despite its positive effect on GNI).	

#### General comments and recommendations

1. Some candidates failed to demonstrate 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 lacked 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.
3. Some candidates had difficulty in presenting their answers in a clear and precise way. Candidates should equip themselves with better language abilities as well as graphical skills, and make sure that their handwriting is legible.
4. Some candidates did not read the questions carefully. Candidates should devote special attention to the assumptions and conditions laid down in the questions to avoid giving irrelevant answers.
5. Some candidates did not seem to be well-informed about current economic issues in the real world. Candidates should pay more attention to economic news.

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- South China Morning Post    Pay gap: Hong Kong women earn more than men before 20 but only half when they turn 60  
<https://www.scmp.com/business/companies/article/2149404/pay-gap-hong-kong-women-earn-more-men-20-only-half-when-they-turn>
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<https://www.censtatd.gov.hk/hkstat/sub/so30.jsp>
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- Transport Department    5.3 Cross Harbour Vehicular Trips  
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