

Marking Schemes

Paper 1

Question No.	Key	Question No.	Key
1.	C (90%)	26.	A (52%)
2.	C (53%)	27.	B (76%)
3.	D (82%)	28.	C (76%)
4.	D (44%)	29.	D (60%)
5.	D (88%)	30.	A (69%)
6.	A (84%)	31.	B (36%)
7.	B (65%)	32.	A (61%)
8.	D (55%)	33.	C (43%)
9.	C (57%)	34.	C (85%)
10.	B (87%)	35.	A (57%)
11.	C (75%)	36.	C (64%)
12.	A (88%)	37.	B (66%)
13.	A (46%)	38.	B (68%)
14.	C (59%)	39.	D (51%)
15.	B (84%)	40.	B (45%)
16.	B (64%)	41.	B (48%)
17.	D (62%)	42.	C (57%)
18.	C (47%)	43.	B (65%)
19.	D (70%)	44.	A (69%)
20.	A (68%)	45.	D (40%)
21.	D (91%)		
22.	C (73%)		
23.	D (47%)		
24.	A (69%)		
25.	A (40%)		

Note: Figures in brackets indicate the percentages of candidates choosing the correct answers.

Section A

1. (a) No. The value of the highest-valued option forgone (i.e., the first option) would drop. **Marks**
(2)
- (b) No. The working time in South Korea may be quite long, so that the first option would become less preferred. (3)

2. (a) (i) From the viewpoint of the employees:
possibility of getting higher income with more effort and/or better service **Marks**
(2)
- (ii) From the viewpoint of the employer:
lower cost of monitoring the performance of the waiters and/or higher incentives for the waiters to work harder and provide higher-quality service to the customers (2)

- (b) Reasons:
- The firm may have become too large in scale, so managerial efficiency starts declining.
 - The firm may have large outstanding loans, so the marginal cost of further borrowing increases.
 - The market may have saturated, leading to a rise in the marketing cost.
 - Any other relevant point
- [Mark the FIRST TWO reasons only.]
- } @2
max: 4

3. Oligopoly. **Marks**
(1)

- Features:
- several dominant firms
 - entry barrier
 - interdependent pricing strategies
 - imperfect market information
 - Any other relevant point
- [Mark the FIRST TWO features only.]
- } @1
max: 2

4. (a) Positive externality. Restaurants in remote areas enjoy benefits from increased business due to the game developer's choice of hotspots locations without paying the developer. So external benefit exists and marginal social benefit is greater than marginal social cost. The number of existing hotspots near the restaurants is lower than that required by the efficiency level. **Marks**
(3)

- (b) The restaurants may pay the game developer to increase the hotspots nearby. (2)

Or

The game developer may charge the restaurants for placing more hotspots near them. **or**
(2)

5. Functions of money:

- Store of value:
As the value of the local currency drops in terms of foreign currency, its purchasing power in terms of the quantity of foreign goods and services would also fall.
 - Standard of deferred payment:
As the value of the currency becomes highly volatile, the contracting cost of specifying future payments in terms of this currency would increase.
 - Medium of exchange:
Some multinational firms may refuse to accept the currency if its value fluctuates too much.
- [Mark the FIRST TWO functions only.]

Marks

} @2
max: 4

6. (a) Fluctuation in consumption is smaller than that of income. Sales-tax revenue generated from consumption would fall less than income-tax revenue generated from income, thus stabilizing total government revenue, during economic downturn. **Marks**
(2)

Or

Introduction of a general sales tax broadens the tax base, so that the tax revenue collected would fluctuate less. **or**
(2)

- (b) Standard tax rate of salaries tax / profits tax / property tax as every taxpayer has to pay the tax amount in the same proportion to these different sources (salaries/profits/property) of his income. (2)
[Mark the FIRST point only.]

Marks

7. (a) (i) Uncertain. Without knowing the total amount of resources of both countries, the productivity (output per unit of resource) for food and computer cannot be determined. (2)

- (ii) Total producible outputs in the two countries when they utilize all of their resources in producing either food or computer:

	Food	Computers
Country A	200	100
Country B	200	200

The opportunity cost of producing 1 unit of computer in Country A: (1)

$$= 200/100 = 2 \text{ units of food}$$

The opportunity cost of producing 1 unit of computer in Country B: (1)

$$= 200/200 = 1 \text{ unit of food}$$

Country B has a lower opportunity cost in producing computers, so it will produce and export computers. (1)

- (b) Terms of Trade (TOT) = $7/4 = 1.75$ F per unit of C (1)

Per unit gain for Country B = $1.75 - 1 = 0.75$ F (1)

Total gain = $0.75 \times 16 = 12$ F (1)

Marks

8. (a) $RRR = (\$1000 - \$250) / \$3000 = 0.25$ (1)

- (b) The change in deposits = $\$250 \times \frac{1}{0.25} = \1000 (2)

- | | Marks |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------|
| 9. (a) Depression / trough | (1) |
| (b) A reduction in interest rate would result in a rise in investment and/or consumption. Aggregate demand would thus increase, and so would aggregate output as well. | (3) |
| (c) Consistent.
When interest rate dropped in 2009, GDP growth rate increased and unemployment rate dropped. | (1)
(3) |
| <p>[Alternatively, it may be argued that the data is not consistent with the answer in (b)—as the US actually cut its interest rate in 2008, but GDP growth was still negative and the unemployment rate was still rising in 2009.]¹</p> | |
| (d) Subsidizing research and development / importation of labour / investment in infrastructures could increase potential output or production capacity of the economy as a whole in the long run, and thus shift LRAS rightward.
[Mark the FIRST policy only.] | (2) |

¹ The long and variable time lag of monetary policy is not required.

Section B

10. (a) – Shares of a listed company are freely transferrable while shares of a private limited company are not.
 – A listed company is required to disclose its accounting information to the public while a private limited company is not.
 – A listed company can issue shares and bonds to the general public while a private limited company cannot.
 [Mark the FIRST TWO points only.]

Marks } @1
 } max: 2

- (b) Arguments supporting the suggestion:
 – Government will have a better control of the train fare, and it can freely reduce the fare to relieve the burden of the passengers
 – If MTR is fully owned and supported by the government, that would make it easier for MTR to get loans to fund its operation or investment.
 [Mark the FIRST point only.]

} @2
 } max: 2

- Arguments opposing the suggestion:
 – It may lower the efficiency of MTR's management and reduce its sensitivity to market (price) signals.
 – The money involved in the purchase of MTR is substantial. The government may have better alternative uses of the money, such as education and medical services.
 [Mark the FIRST point only.]

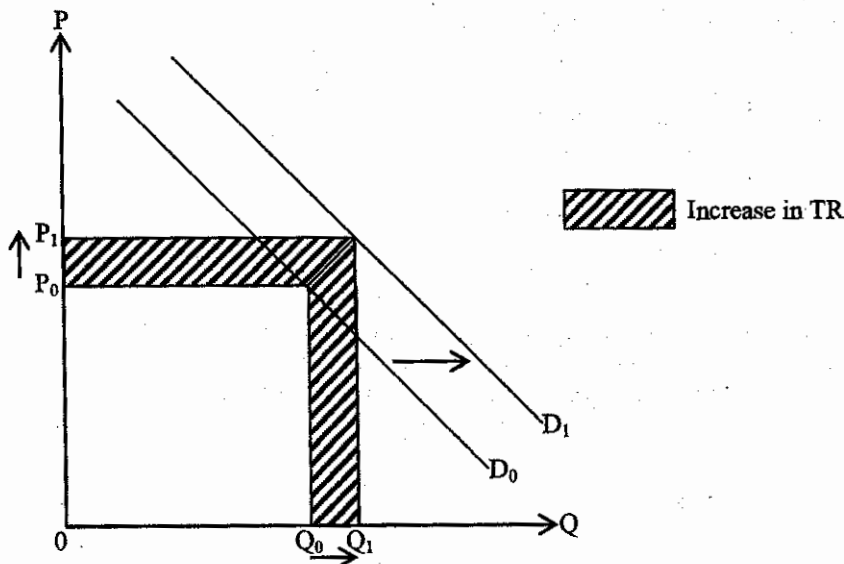
} @2
 } max: 2

- (c) No.
Verbal elaboration:
 – There was a rise in demand.
 – Both the price and the quantity transacted have increased.
 – Total revenue has increased.

(1)
 (2)
 (2)
 (1) } max: 7

- Illustrate in the diagram:
 – Rightward shift in the demand curve
 – Higher Price and Quantity
 – Higher Total Revenue

(1)
 (1)
 (1) }

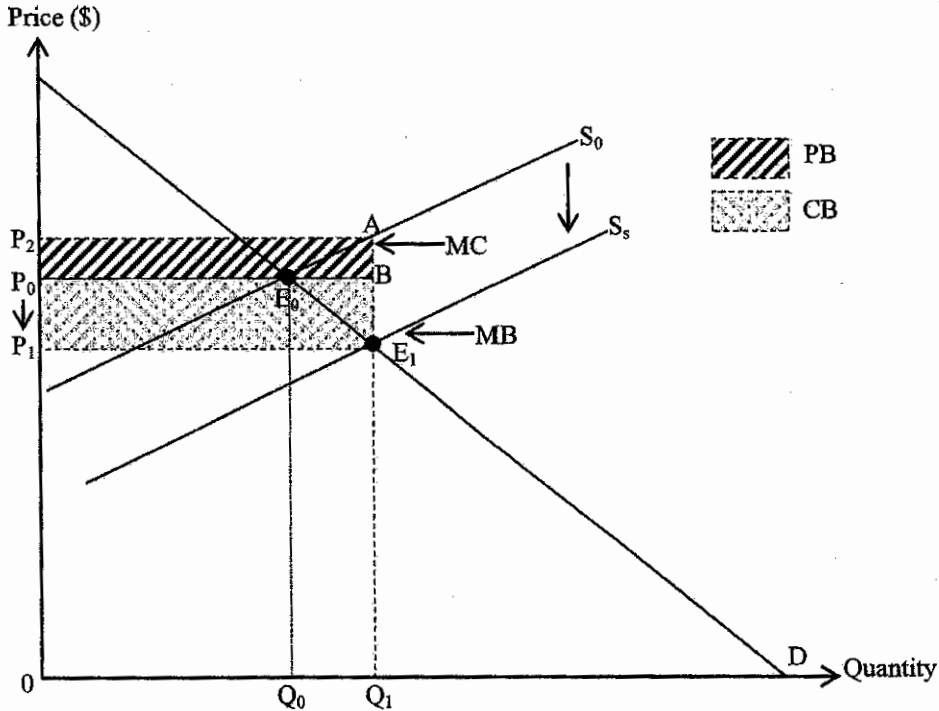


11. (a) Verbal elaboration:

The condition is that the elasticity of demand for education services is lower than the elasticity of supply. (2)

Illustrate in the diagram:

- Parallel downward shift of supply curve due to the per unit subsidy (1)
- Correct position of New Price (P_1) (1)
- Correct position of New Quantity (Q_1) (1)
- Correct position of producer benefit and consumer benefit (1)
- Consumer benefit > producer benefit (1)



(b) Verbal elaboration:

At Q_1 , marginal cost is larger than marginal benefit. (1)

Illustrate in the diagram:

- Correct position of marginal benefit (1)
- Correct position of marginal cost (1)

(c) Yes. Subsidizing education is a measure to equalize opportunities, so the poor will not be deprived of university education due to financial constraint. Education could also raise their future income, thus reducing income inequality over generations. (3)

Marks
(3)

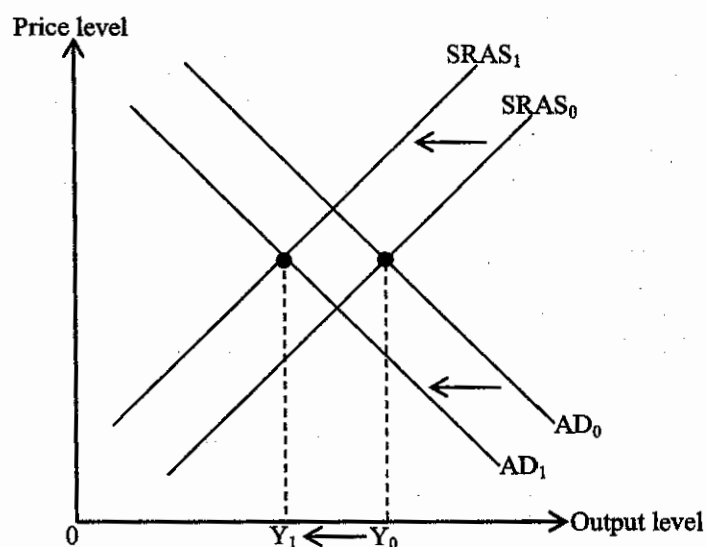
12. (a) The geographical mobility of low-skilled workers from the EU would be lowered—because the visa requirement would increase the cost for those EU workers to go to work in the UK.

(b) Verbal elaboration:

- The new visa requirement would increase labour cost for the British firm owners, resulting in a drop in SRAS. (2)
- Political uncertainty would result in a drop in investment from the global investors and thus a fall in AD. (2)
- Aggregate output would thus drop. (1)

Illustrate in the diagram:

- leftward shift of AD curve (1)
- leftward shift of SRAS curve (1)
- lower output (1)



(c) Components of current account:

- Invisible trade: the increase in cost of travel would result in a fall in the number of British citizens visiting the EU and hence the import of services.
- Factor income (primary income): with fewer British workers working in the EU, there would be a drop in total wage payment to such workers.
- Unilateral transfer (secondary income): with fewer workers working in the EU, there would be a drop in their remittance back to Britain.

} @2
max: 4

	Marks
13. (a) (i) Tertiary production.	(1)
(ii) GDP would rise, as charges for the service of the elderly care centre is regarded as consumption expenditure by Mr Chan on final goods and services.	(2)
(b) (i) <u>Proposal A's effect</u> on aggregate output: An increase in salaries tax would reduce AD via a drop in disposable (after-tax) income and thus consumption. As a result, aggregate output would fall. [An increase in salaries tax may also reduce SRAS by creating a disincentive effect on labor.]	(4)
<u>Proposal B's effect</u> on aggregate output: There would be no extra effect on aggregate output as a component of AD/AS does not change.	(2)
(ii) <u>Proposal A's effect</u> on income distribution: Salaries tax payers (higher-income group) would pay more taxes while non-tax payers (lower-income group) would not be affected. <u>Or</u> High-income tax payers pay more, low-income tax payers pay less.	(2)
The after-tax income inequality would thus be reduced.	(1)
<u>Proposal B's effect</u> on income distribution: – There will be no extra effect on current tax payers, so the income inequality is unaffected. – Reduction of fiscal reserves may result in a tax increase in the future, so future tax payers (mainly the younger portion of the population) may have to pay more taxes, thus <i>increasing income inequality between generations</i> .	(2)
	(2)
	} max: 2
(iii) <u>Proposal A's effect</u> on other variables: – Price level would drop as AD drops (while there is no such an effect generated by proposal B). – Unemployment may increase as AD drops (while there is no such an effect generated by proposal B). – Any other relevant point	} @2 max: 2
<u>Proposal B's effect</u> on other variables: – A worsening of the government's budgetary position (due to a drain on fiscal reserves) may imply tax increase in the future. (No such effect arises under proposal A.) – Business confidence may be weakened. Expecting tax increases in the future (due to the problem of fiscal sustainability), which would reduce their after-tax profits, business firms may choose to cut down their investment. (No such effect arises under proposal A.) – Any other relevant point	} @2 max: 2

Note: The maximum marks for part (b) is 10.

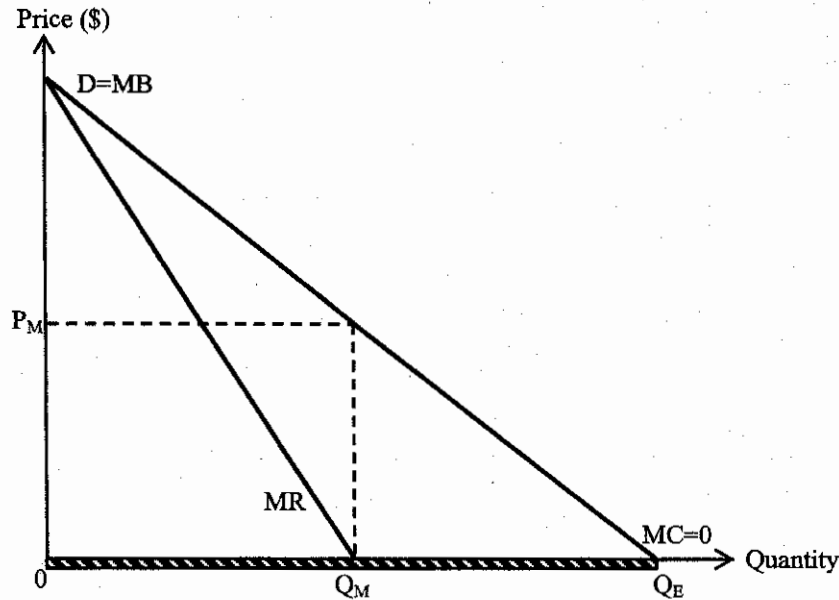
Section C

Marks

14. (a) (i) Illustrated in the diagram:

- Correct position of MR
- Correct position of Q_M
- Correct position of P_M

(1)
(1)
(1)



Verbal elaboration:

HK ONLINE would produce at a quantity where $MR = MC = 0$.

(1)

(ii) - Correct position of Q_E

(1)

(b) (i) Yes.

Different consumers (new and existing customers) are charged different prices for the same services produced under the same cost.

(3)

(ii) No.

A lower price is charged for the internet service because, when combined with TV service, its marginal cost of production (including, administration cost, marketing cost, installation cost, etc.) would be lowered.

(3)

(c) (i) Market sharing / market allocation.

(1)

Motives:

- Firms would face less competition within their assigned markets.
- They can raise prices and make more profit in their own assigned markets.
- By focusing on their assigned markets alone, firms can lower their marketing cost.

[Mark the FIRST TWO motives only.]

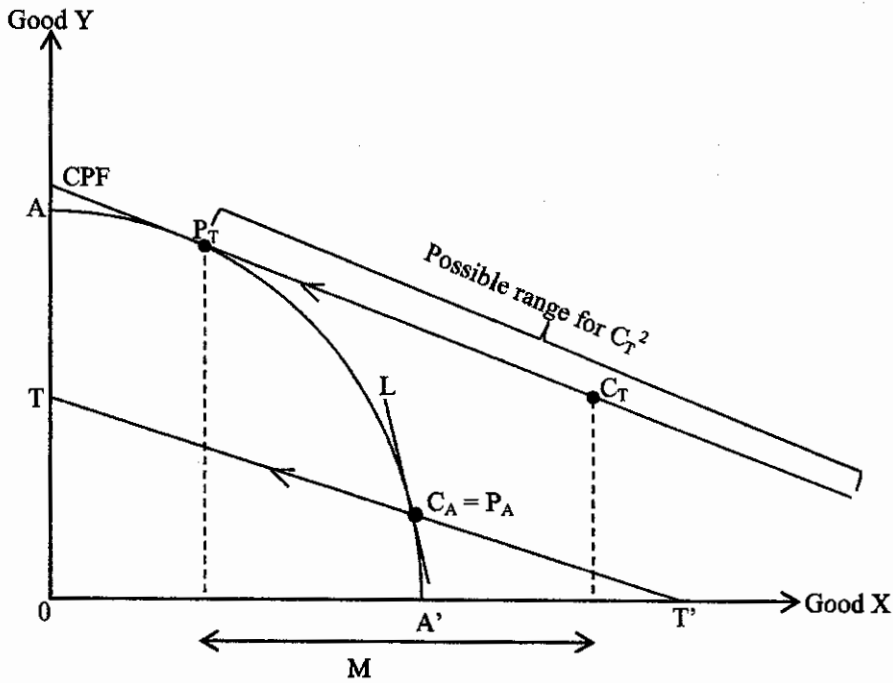
} @1
max: 2

(ii) The first conduct rule. Because this is a case of an anti-competitive agreement.

(2)

15.

Marks



- (a) (i) Illustrated in the diagram:
 correct position of $C_A = P_A$ production point P_A (1)

Verbal elaboration:
 Without trade, Country A can only consume its own production. (1)

- (ii) Illustrated in the diagram:
 Correct position of the straight line (L) (1)

Verbal elaboration:

- Slope of L is the marginal cost of Good X. (1)
- L is steeper than TT' . (1)

That means marginal cost of producing Good X is higher than the world price of Good X. (1)

So Country A did not have a comparative advantage in producing Good X. (1)

} max: 3

² Knowledge of convex indifference curves is not required.

	Marks
(b) (i) <u>Illustrated in the diagram:</u>	
– Correct position of P_T	(1)
– Correct position of CPF	(1)
<u>Verbal elaboration:</u>	
– Country A would produce at P_T where TOT = domestic marginal cost of production.	(1)
(ii) <u>Illustrated in the diagram:</u>	
– Correct position of C_T	(1)
<u>Verbal elaboration:</u>	
– Country A can consume at a point which is unattainable from local production before trade.	(1)
(iii) <u>Illustrated in the diagram:</u>	
– Correct position of M	(1)
(c) (i) – enhance economic growth (as shown by higher levels or positive rates of growth) of per-capita real GDP because	(1)
external trade could increase aggregate demand (through exports) and hence real GDP.	(1)
(ii) – no change in economic development (as reflected by the same level of HDI) because	(1)
more people may leave school earlier in order to take part in trading activities, thus decreasing the average number of years of schooling, while GDP rises as a result of trade.	(1)
<u>Or</u>	<u>or</u>
pollution (as a by-product) may become more serious as production is increased after trade /	(1)
new disease or virus brought in by foreigners may shorten the life expectancy at birth of the local people.	