

## ECONOMICS

### EXAMINATION OBJECTIVES

The following objectives of the examination are to test whether the candidates have acquired a basic understanding of economics – with special emphasis on Hong Kong conditions and problems :

1. to test candidates' knowledge and understanding of fundamental economic concepts,
2. to test candidates' ability to apply such concepts to explain real world situations,
3. to test candidates' ability to understand and interpret economic information presented in various forms,
4. to test candidates' acquisition of some of the basic tools of economic analysis,
5. to test candidates' skill in analyzing simple economic problems,
6. to test candidates' ability to integrate various economic concepts contained in the syllabus, and
7. to test candidates' ability to present ideas clearly, and in a well-reasoned manner, illustrating answers with simple diagrams and examples.

### THE EXAMINATION

Two papers will be set. No choice will be allowed in both papers.

Paper 1 (1½ hours) (60%) will consist of two sections. Section A (27%) will consist of short questions. Section B (33%) may consist of three or four structured questions.

Paper 2 (1 hour) (40%) will consist of multiple-choice questions.

### THE SYLLABUS

In the following syllabus, candidates should be able to illustrate general principles with relevant examples from Hong Kong.

*Syllabus Topics**Explanatory Notes*

## 1. THE BASIC ECONOMIC PROBLEMS

1.1 The source of economic problems:  
scarcity

- (i) unlimited wants and limited resources
- (ii) free and economic goods

1.2 Choice and opportunity cost

- (i) economic decisions involving choices among alternatives
- (ii) concept of cost in economics

1.3 The three basic economic problems:  
What ? How ? For whom ?1.4 How society tackles the three basic  
economic problems

- (i) by society's customs and traditions
- (ii) by government decisions
- (iii) by the market mechanism

(N.B. Illustrations by examples only. All theories on types of economic systems NOT required)

## 2. DEMAND, SUPPLY AND PRICE

2.1 Individual demand

- (i) factors affecting individual demand
- (ii) complements and substitutes, superior and inferior goods  
(N.B. Giffen goods NOT required)
- (iii) individual demand schedule and importance of the ceteris paribus assumption
- (iv) difference between change in quantity demanded and change in demand

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2.2 Market demand

2.3 Price elasticity of demand

2.4 Individual supply

2.5 Market supply

2.6 Price elasticity of supply

2.7 Interaction between demand, supply and price

*Explanatory Notes*

- (i) horizontal summation of individual demand curves
- (ii) factors affecting market demand

- (i) arc elasticity  
(N.B. Point elasticity, cross elasticity and income elasticity NOT required)
- (ii) relationship between price elasticity and total revenue
- (iii) factors affecting price elasticity of demand

- (i) factors affecting individual supply
- (ii) individual supply schedule and importance of the ceteris paribus assumption
- (iii) difference between change in quantity supplied and change in supply

- (i) horizontal summation of individual supply curves
- (ii) factors affecting market supply

- (i) arc elasticity  
(N.B. Point elasticity and cross elasticity NOT required)
- (ii) factors affecting price elasticity of supply

- (i) definition of equilibrium : no tendency to change
- (ii) equilibrium price, effects of change in demand and/or change in supply on equilibrium price

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## 2.8 Market intervention

graphical illustration of price ceiling, price floor, quota, unit tax and unit subsidy and their impact on price and quantity

I Price intervention : price ceiling and price floor

II Quantity intervention : quota

illustration by a kinked supply curve

III Unit tax and unit subsidy

determination of the share of the tax burden/subsidy between producers and consumers

## 3. PRODUCTION

## 3.1 Definition

## 3.2 Types/stages of production

primary, secondary and tertiary production and their inter-relationship

## 3.3 Types of goods and services produced

- (i) producer goods
- (ii) consumer goods
- (iii) services

## 3.4 Division of labour : types, advantages, disadvantages, limitations

simple, complex and regional

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## 3.5 Factors of production

## I Definition

## II Classification

## III Nature and functions

- (i) human resources : labour, entrepreneurship
- (ii) natural resources : land
- (iii) man-made resources/aids to further production : capital

- (i) labour : factors affecting its quantity, productivity, mobility; different types of wage payment
- (ii) entrepreneurship : risk-bearing and decision-making
- (iii) land : supply and mobility
- (iv) capital : forms and depreciation
- (v) the features of (i) to (iv) in Hong Kong

## 3.6 Production in the short-run and the long-run

## I Definition of short-run and long-run

## II Law of diminishing returns

in terms of fixed and variable factors of production

Illustration by total product, average product and marginal product schedules only

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III Economies and diseconomies of scale

4. UNITS OF PRODUCTION (THE FIRM)

4.1 Definition of a firm

4.2 Forms of control and ownership

*Explanatory Notes*

- (i) economies of scale : technical, managerial, financial, marketing, risk diversification, and research and development  
(N.B. Sources of technical economies of scale NOT required)
- (ii) diseconomies of scale : managerial, financial and marketing

Economies and diseconomies of scale illustrated by average cost only

A unit that makes decisions regarding the employment of factors of production and the production of goods and services

- (i) public ownership as ownership by government or its agencies with the right to own, control, use and dispose of property - to be illustrated by examples only
  - (ii) private ownership :
    - sole proprietorship
    - partnership
    - company
    - types of shares and bonds
- } their features, advantages and disadvantages

(N.B. A comparison of the advantages and disadvantages of public and private ownership NOT required. Documentation involved in setting up business units NOT required)

- (iii) separation of ownership from control in a limited company

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4.3 Integration : types and motives

5. MARKET STRUCTURE

5.1 Definition of market

5.2 Perfect competition; imperfect competition : monopoly, oligopoly and monopolistic competition

6. NATIONAL INCOME

6.1 Meaning of national income

6.2 Circular flow of economic activities

*Explanatory Notes*

vertical, horizontal, lateral and conglomerate integration

(i) general features

- number of sellers
- number of buyers
- nature of product
- ease of entry
- availability of information

(ii) different ways in which a monopoly can be formed

The four different forms of market structure are theoretical constructs. Actual examples may only be approximations of the above constructs

national income as a general term for aggregates like Gross Domestic Product (GDP) and Gross National Product (GNP)

the relationship among production, income and expenditure

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## 6.3 Gross Domestic Product (GDP)

## 6.4 Gross National Product (GNP)

## 6.5 Uses and limitations of national income statistics as an indicator of economic welfare and for international comparison

## 6.6 Factors affecting national income

*Explanatory Notes*

(i) the three approaches to measure GDP : production approach (value-added approach), income approach and expenditure approach  
(N.B. Components of GDP compiled under the income approach NOT required)

(ii) GDP at current and constant market prices

(iii) GDP at factor cost

(iv) GDP per capita; growth rate of GDP

(N.B. Other measures related to GDP NOT required)

GNP as GDP plus net income from abroad

(N.B. Other measures related to GNP NOT required)

(i) demand side : consumption, investment, government expenditure, exports and imports

(ii) supply side : capital, labour, entrepreneurship, land and technology

(N.B. Multiplier and determination of national income NOT required.  
Graphical analysis NOT required)



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6.7 Business cycles, unemployment and changes in the general price level

*Explanatory Notes*

(i) business cycles : a description of the recurrent fluctuations in GDP around a secular trend

(N.B. Theories of business cycles NOT required)

(ii) unemployment

- meaning of unemployment
- unemployment rate as measured in terms of the percentage of unemployed persons in the labour force
- brief introduction to underemployment
- cost of unemployment

(N.B. Various types of unemployment NOT required)

(iii) changes in the general price level

- definitions of inflation and deflation
- measurement by Consumer Price Index and implicit price deflator of GDP
- redistributive effects

(N.B. Construction of CPI and implicit price deflator of GDP NOT required)

*Syllabus Topics**Explanatory Notes*

## 7. MONEY AND BANKING

## 7.1 Nature and functions of money

- (i) definition
- (ii) different forms of money
  - commodity money
  - paper money : convertible and inconvertible
  - deposit money

## 7.2 Banks : functions and services

- (i) commercial banks and central bank
  - (ii) licensed banks, restricted licence banks and deposit-taking companies in Hong Kong
  - (iii) how central banking functions are performed in Hong Kong
- (N.B. Tools of monetary policy NOT required)

## 7.3 Money supply

- (i) definitions of money supply in Hong Kong
- (ii) credit creation and the banking multiplier

## 7.4 Hong Kong as a financial centre

- (i) factors contributing to its development as a financial centre
- (ii) effects on the Hong Kong economy

## 8. PUBLIC FINANCE

## 8.1 Government revenue

- (i) sources of government revenue in Hong Kong
  - direct tax
  - indirect tax
  - other revenue

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- (ii) principles of taxation
  - (iii) classification of taxes according to various criteria
  - (iv) effects of taxation on individuals and firms
- 8.2 Public expenditure
- (i) public expenditure as a proportion of GDP and its trend
  - (ii) public expenditure by function and its trend
  - (iii) socio-economic implications of such trends
- 8.3 Government budget
- (i) definition of budget; surplus budget, deficit budget and balanced budget
  - (ii) major proposals in the current budget speech
- (N.B. Mechanism of fiscal policy NOT required)
9. INTERNATIONAL TRADE
- 9.1 Absolute advantage, comparative advantage and gains from trade
- 9.2 Balance of payments
- brief introduction to the balance of payments account
- current account
    - main components of the current account : goods, services, income and current transfers
    - (N.B. Sub-classification of these components NOT required)
  - capital and financial account
    - (N.B. Sub-classification of this account NOT required)

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## 9.3 Exchange rate

## 9.4 Trade barriers

## I Types

## II Effects on price, output and employment

## 9.5 Hong Kong's international trade

## I Principle of comparative advantage as applied to Hong Kong

## II Importance of trade to Hong Kong's economy

## III Trade barriers faced by Hong Kong and attempts to overcome them

*Explanatory Notes*

- (i) meaning of exchange rate  
(N.B. Graphical illustration NOT required)
- (ii) effect of a change in the exchange rate on import price and export price
- (iii) brief introduction to the linked exchange rate system in Hong Kong  
(N.B. Mechanism of maintaining the linked exchange rate NOT required)

using the pattern of trade in Hong Kong to illustrate the principle

- (i) trade promotion
- (ii) the role of the HKSAR Government