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Section A (44 marks)

1. (a) Mary was the major shareholder of a private limited company which operated a restaurant chain. She planned to change the form of business ownership to a listed company. List **ONE** advantage and **ONE** disadvantage of the change. (2 marks)
- (b) After opening some new restaurants, Mary found that the average ^{Ac 9} cost of production of her company had increased. Explain the change in average cost with **ONE** reason. (2 marks)

a) Advantage: The firm can have wider source of capital as it can sell bonds and shares to the general public.

Disadvantage: The existing shareholders' control over the company may be diluted when general public could buy shares of the company.

b) The company experiences internal diseconomies of scale. When firm expands and become too large, a lot of communication and management problems may arise. Solving these problem turns cost so that the cost of production may increase.

2. There are two kinds of food deliverers: 'riders' delivering food by self-provided motorbikes and 'walkers' delivering food on foot. Why do 'riders' usually have a higher income per order than 'walkers'? Suggest **ONE** demand-side factor and **ONE** supply-side factor to explain your answer. (4 marks)

Riders usually could deliver food faster than walkers, as they use motorbikes for delivery services. If more customers are willing and able to have delivering food more faster, demand for riders increases, so that price and quantity transacted of delivery services by riders increase, and their income would higher than walkers.

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As riders have to self-supplied producer goods, such as their motorcycles. The cost of production of delivery services provided by riders is higher, so that the supply of riders may decrease, price of order for riders is higher than that of the walkers.

3. Refer to the following data about Country A.

Year	2019	2020
Per capita disposable income	\$15 000	\$20 000
Gini coefficient (based on household income)	0.51	0.56
Gini coefficient (based on household disposable income)	0.51	0.44

- (a) State **TWO** reasons to explain why the increase in per capita disposable income may lead to an over-estimation of the improvement in living standard of Country A. (2 marks)
- (b) Based on household disposable income, did income inequality of Country A improve or worsen in 2020? Suggest **ONE** policy which may have caused such a change. (2 marks)

a) As calculation of per capita disposable income did not take people's leisure time into account. If people work a longer hour and have fewer leisure time, there may be an increase in per capita disposable income. As the calculation of per capita disposable income did not include the change in general price level. If the general price level increases, the cost of living increases. the living standard of country A may not improve a lot.

★: overstate the improvement in living standard.

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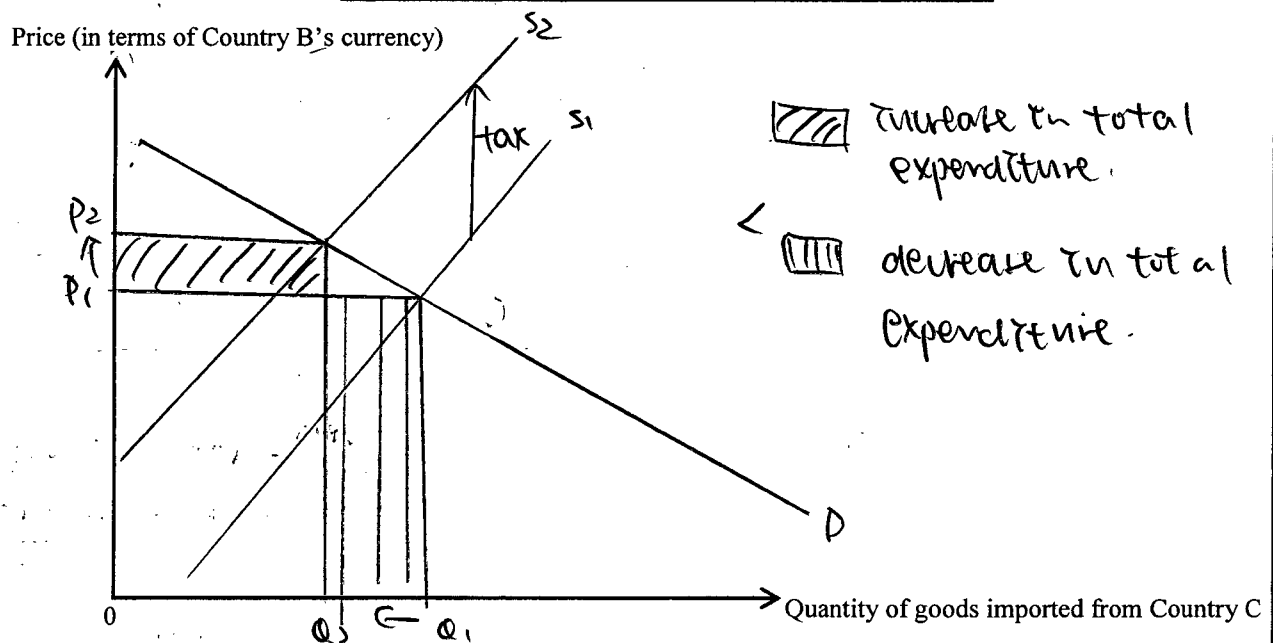
b) The income inequality improve as the Gini coefficient base on household disposable income reduces from 0.51 to 0.44 in 2020. (more transfer payment, such as cash, The government provide \uparrow to low-income group, so that the disposable income of low income group increase while that of high-income remains unchanged.

4. Country B and Country C are two large open economies. Facing a huge visible trade deficit, Country B imposes a per-unit tariff on goods imported from Country C. Suppose Country B's demand for goods imported from Country C is elastic.

$$\frac{\Delta Q}{\Delta P} > 1$$

- (a) With the aid of Figure 1, explain how the tariff would affect the total expenditure of Country B on goods imported from Country C. (6 marks)
- (b) "Devaluation of a country's currency against its trading partners' may have the same effect on imports as a tariff." Use Country B as an example to justify this statement. (2 marks)
- (c) Apart from the effect on the country's visible trade balance, explain ONE other effect of devaluation on its balance of payments. (2 marks)

Figure 1: Goods imported from Country C by Country B



a) After the imposition of tariff, the price (in terms of country B currency) of import increases and quantity imported decreases. If the demand for import from Country C is elastic, the decrease in quantity demanded is greater (percentage) than percentage

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$$\frac{QdI}{Pp} > 1$$

Increase in price. The total expenditure of Country B on goods imported from country C (in terms of country B's currency) decreases.

b) When the government of Country B devaluation its currency against the currency of Country C, the price of import from country C in terms of Country B's currency increases, and quantity demanded decrease. As the demand for goods imported from country C is elastic, percentage decrease in quantity demanded is greater than percentage increase in price. The total expenditure in terms of country B's currency on imports decrease.

c) The invisible trade balance improves, as the cost of travelling to Country C (in terms of country B's currency) increase, demand for travelling to Country C decrease. The total import value of services of Country B decreases, improving the balance of invisible trade and balance of payment.

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5. Country D introduced a short-term capital gains tax (STCGT) on property market.

Capital gains (\$)	STCGT rate (%)
10 000 or below	8
10 001 to 50 000	16
50 001 to 100 000	24
100 001 or above	32

STCGT is a tax on capital gains from the sale of a property held for less than 1 year.

A spokesman of the tax department said that a new computer system had been developed for STCGT. Although the system cost more than 1 billion dollars, it allowed tax payers to check and pay the amount of STCGT online easily.

- (a) Evaluate the new tax in terms of TWO principles of taxation put forward by Adam Smith. (4 marks)
- (b) 'The introduction of STCGT would not relieve the problem of rising property prices.' Explain whether this is a positive statement or a normative statement. (2 marks)

a) The new tax system is in line with 'convenient' principle. As taxpayers could check and pay the amount of STCGT online easily which is convenient to taxpayers.

The new tax system does not in line with 'equity' principle. As the Capital gain tax payment is not in proportion to taxpayers' taxable income. The new tax rate increases when taxable income increases.

b) Positive statement.

As the statement could be further refutable by (fact or the) evidence, such as comparing the property price before and after the introduction of the tax.

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$$10 - 5 = 5$$

$$8 \quad -210 \\ MV = PY$$

6. (a) 'Deflation will occur if the amount of goods and services produced is growing faster than money supply.' Explain this statement in terms of the quantity theory of money. (4 marks)
- (b) 'If deflation is expected, the real interest rate will be higher than the nominal interest rate.' Why? (2 marks)

a) Quantity theory of money stated that $MV = PY$, where
 M = money supply, V = velocity of circulation of money,
 P = price level, Y = real output.

It's assumed that V is constant in short run.

When M growing slower than the amount of goods and services, which is Y , a sustained increase in M would lead to a sustained decrease in P by a smaller percentage.

b) Nominal interest rate = expected inflation rate + real interest rate

If deflation is expected, expected inflation rate is negative, so that real interest rate will be higher than nominal interest rate.

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7. In a two-country-two-good model, the outputs per unit of resources of both countries are as follows.

	Rice (units)		Toys (units)
Country E	10	OR	20
Country F	5	OR	15

$$1R \geq T$$

$$1R \leq T$$

- (a) Assume the terms of trade are that 1 unit of rice can be exchanged for 2 units of toys. Calculate the gains from trade of EACH country when trading 1 unit of rice. Show your workings. (4 marks)
- (b) With reference to your answer in part (a), defend the following statement. 'There is still a basis for trade even if a country has no absolute advantage in producing any goods.' (2 marks)

a) Opportunity cost of producing 1 unit of rice

in Country E: $20/10 = 2$ unit of toys

in Country F: $15/5 = 3$ unit of toys

per-unit gain of trading 1 unit of rice

in Country E: $2.2 - 2 = 0.2$ unit of toys

in Country F: $3 - 2.2 = 0.8$ unit of toys

b) Country F has the absolute advantage in producing both rice and toys as it can produce more unit of rice and toys than country E using the same amount of resources.

Therefore, country F has no absolute advantage in produce rice and toys. However,

specialization based on the Comparative advantage, which stated that if each country specialised in producing goods in which they have a lower opportunity cost.

Under the world price, both country E and F could gain, so that trade can be occurred.

from trade

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$$0.25 = \frac{1600}{R - Ex} \quad m = \frac{R - Ex}{D}$$

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

Assets (\$ million)		Liabilities (\$ million)	
Reserves	1 000	Deposits	4 000
Loans	3 000		

The public initially holds \$1 000 million cash and the banks are fully loaned up.

- (a) Calculate the required reserve ratio. (1 mark)
- (b) Suppose the public only wants to hold \$400 million cash and deposits the remaining cash into the banks. Calculate the maximum change in money supply. Show your workings. (3 marks)

a) Required reserve ratio = $\frac{1000}{4000} \times 100\%$
 $= 25\%$

b) Max. possible deposit = $\frac{1600 \text{ m}}{25\%} = 6400 \text{ million}$

Max. change in money supply
 $= \text{Max change in cash held by public} + \text{Max change in deposit}$
 $= \$(-600 + 6400 - 4000) \text{ m}$
 $= -\$800 \text{ m}$

END OF SECTION A

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Section B (60 marks)

9. The Mainland government introduced the Targeted Poverty Alleviation Campaign (精準扶貧政策) in 2014. After analysing the situations of people living in poverty, the government officials came up with tailor-made measures. The following are two examples of the campaign.

Example 1	A village in Yunnan province has beautiful natural landscape. The government of Yunnan province promoted the village to <u>attract more travellers</u> . Apart from farming, the villagers also set up <u>hostels to serve travellers</u> in order to earn more income.
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(a) Refer to Example 1.

- (i) In which types of production did the villagers engage after the introduction of the campaign? Explain. (4 marks)
- (ii) Explain how labour mobility of the villagers would be affected. (3 marks)

Example 2	The government <u>provided funding</u> and <u>invited private firms to develop</u> hydroelectric power plants in six provinces (such as Hubei and Jiangxi). Such development would help improve transportation, irrigation and flood prevention in the rural villages in these provinces.
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- (b) Refer to Example 2. With the aid of a diagram, explain how aggregate output in these six provinces would be affected in the long run. (8 marks)

ai) Tertiary production.

As the villagers started to provide service to the tourist, such as accommodation service.

Secondary production.

The villagers started to convert raw materials into semi-finished or finished goods, such as setting up hotels ready for travellers.

aii) Occupational mobility increase.

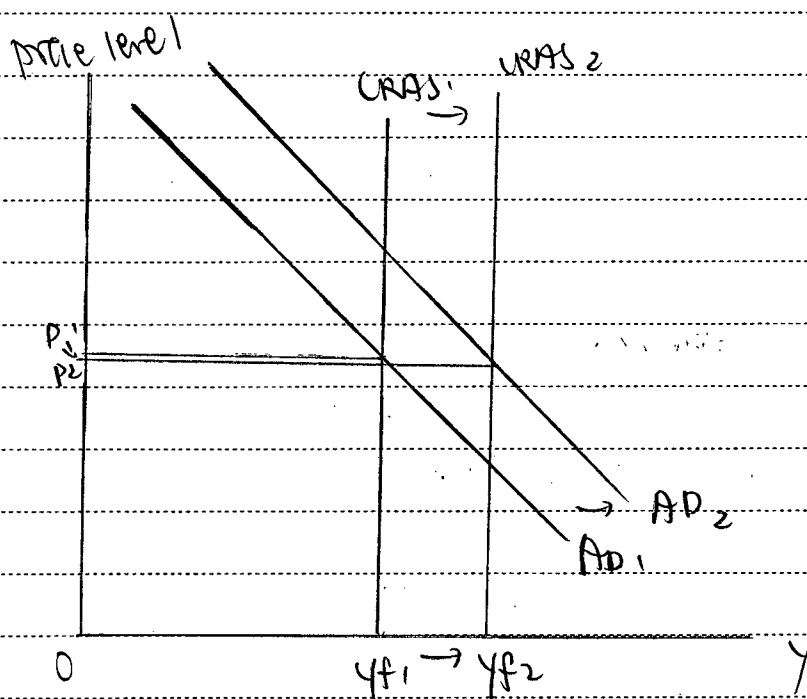
As the campaign provide more job opportunity for the villagers. The villagers would more willing to change her occupation into tourism-related industry in order to earn more income.

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b) The development of hydroelectric power lead to improvement of technology and increases the physical capital. The production capacity increases the long run Aggregate supply increase and potential output level increases. Government funding also increases the government expenditure, aggregate demand would increase, and output level increases.



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10. The Olympic Games attract billions of international television viewers to watch the competitions among thousands of top athletes.

- (a) Some restaurants in shopping malls find their businesses increase sharply when the malls broadcast Olympic events. Explain how the broadcast of Olympic events may result in divergence between private and social benefits. (3 marks)
- (b) Suppose the divergence in part (a) does exist. How can market mechanism help reduce this divergence? (2 marks)

Athletes compete in the Olympic Games with their support teams consisting of sport psychologists, physical therapists, nutritionists, etc.

- (c) Which economic principle is illustrated in the above practice? State TWO reasons why such a practice can increase labour productivity. (3 marks)

Some professional athletes receive a monthly salary and share a proportion of the prize money whenever they win in competitions.

- (d) Instead of paying the athletes a monthly rate only, explain why some employers of professional athletes use the above wage payment arrangement. (2 marks)

Whenever an athlete wins a gold medal in a certain sport, there will be the following phenomena: more people will start learning the sport. As a result, there will soon be long queues registering for courses in the sport.

- (e) With the aid of a demand-supply diagram, explain the above phenomena. (5 marks)

Professional athletes usually start their full-time training before graduating from secondary school and have to give up their studies.

- (f) Will the opportunity cost of being a professional athlete be affected if the average income of professional athletes increases? Explain. (2 marks)

a) There is positive externality.

The external benefit is the increase in sales revenue of some restaurants when they broadcast Olympic as more customers are attracted to watch the Olympic events. No compensation is paid from these restaurants to Olympic Company.

The marginal social benefit is greater than marginal private benefit.

b) The restaurants can pay to the Olympic Company

Answers written in the margins will not be marked.

for external benefit produced. This can internalise the external benefit into marginal private benefit, so that marginal private benefit increases towards the marginal social benefit to reduce their divergence.

c) Division of labour.

Choosing the best people to do the job could improve the production efficiency, so that the average labour productivity increases.

Saving time in moving around different location and changing tools as the workers in support teams only have to focus on specific task of work, so that they can work efficiently, increases the average labour productivity.

d) For employers, they can reduce cost of supervision athletes' performances. As the athletes have higher incentive to win the prize to get a higher paid.

~~For athletes, they can earn more by performing better to win the prize and receive higher salary.~~

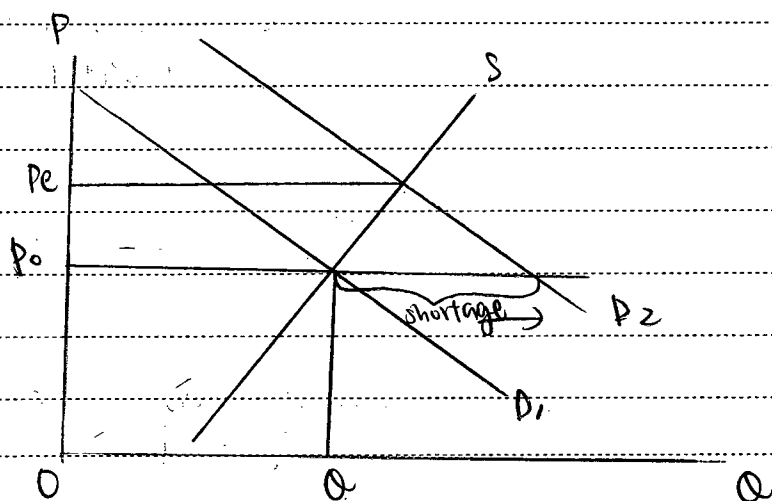
e) When athletes win a gold medal in certain sport, demand for the certain sport courses increases.

The price of course than ^{become} below the equilibrium price, quantity demanded is greater than quantity supplied. there's shortage. People have to use non-price competition, such as queuing, to get the the courses.

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f) The opportunity cost of being professional athletes is the value of continuous study in school forgone. If the average income of professional athletes increases, the value of the chosen option increases, and the value of the highest-valued option forgone remains unchanged. The opportunity cost of being athlete remains unchanged.

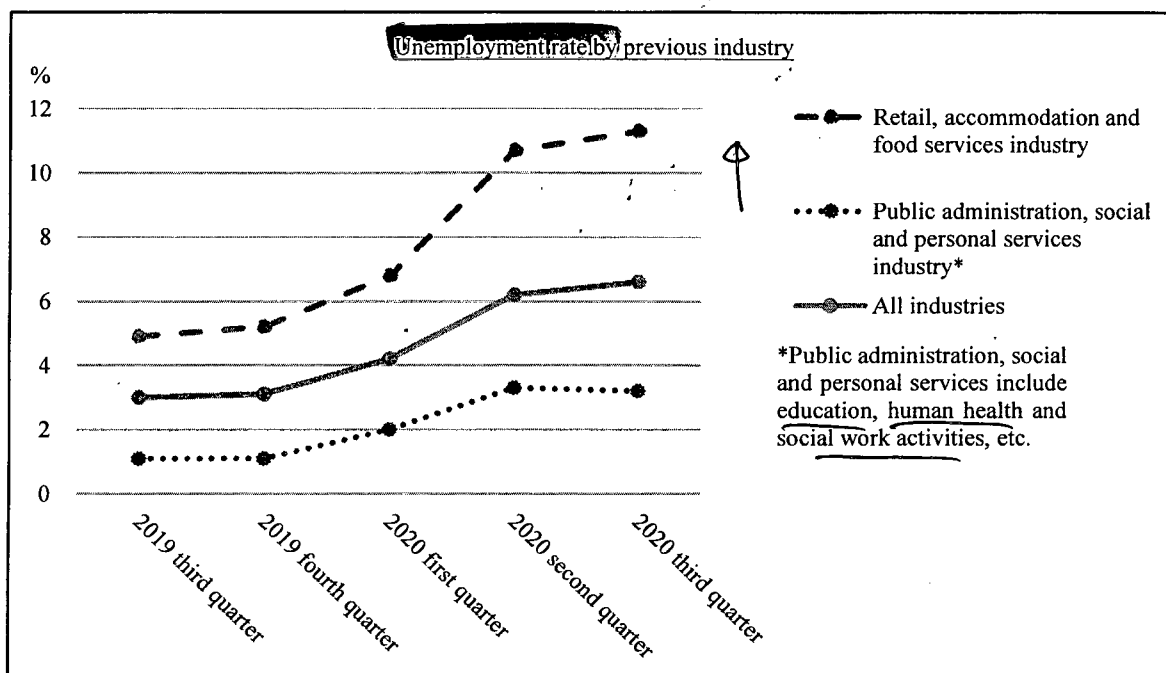
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 professional

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11. The Government launched the Consumption Voucher Scheme in 2021 to relieve the impact of COVID-19 on the Hong Kong economy.





Source A: Statistical data about unemployment rate in Hong Kong



Source B: An extract of information about the Consumption Voucher Scheme

All Hong Kong permanent residents and new arrivals aged 18 or above, who comply with the 'residing in Hong Kong' requirement, could register to receive electronic consumption vouchers with a total value of \$5,000 by instalments.

Source C: Information about the four designated stored value facilities to receive the \$5 000 consumption vouchers by instalments

	AlipayHK	Octopus	Tap & Go	WeChat Pay HK
	 AlipayHK	 八達通 Octopus		 WeChat Pay®
Public transportation with the above payment facilities installed	MTR, bus, mini bus and ferry	MTR, bus, mini bus and ferry	Bus and mini bus	None
Promotions to consumption voucher users	5 e-coupons	First 2 million registered customers enjoy \$18 of stored value	\$50 awarded when using virtual Tap & Go Unionpay card for the first transaction with an amount equal to or larger than \$50	e-coupons




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Source D: Some reminders for the Consumption Voucher Scheme

- Consumption vouchers cannot be used in transactions such as payments to the government (e.g. tax), public utilities (e.g. electricity charges), purchase of financial products (e.g. insurance), and direct purchase from merchants located outside Hong Kong.
- There are deadlines for using consumption vouchers.

Source E: Some views on the Consumption Voucher Scheme in Hong Kong

<p>A housewife</p> 	<p>I have spent more than \$5 000 as there are e-coupons from the stored value facility provider. A lot of promotions in large retail chains and malls have also tempted me to consume!</p>
<p>A former chef in a restaurant</p> 	<p>I have been laid off and have stayed home for months. No one knows when the travellers would be back. I hope that the Consumption Voucher Scheme will bring more local people to spend on food and beverage and the whole industry can survive the pandemic. Otherwise, many workers will be forced to leave the industry.</p>
<p>A doctor working in a public hospital</p> 	<p>Resources should be allocated to the medical sector, instead of giving everyone an equal amount under the Consumption Voucher Scheme. The public hospitals lacked space, manpower and equipment even before the pandemic. Start building new hospitals earlier so that more lives could be saved.</p>

(a) Refer to Source A.

(i) In which phase of business cycle the Hong Kong economy most likely was? Apart from the change in unemployment rate, list ONE other economic phenomenon of this phase. (2 marks)

45
unemployment

(ii) Why did the unemployment rate of retail, accommodation and food services industry increase faster than that of public administration, social and personal services industry during the pandemic? (2 marks)

(b) Refer to Source B. Would the \$5,000 distributed under the Consumption Voucher Scheme be included in the calculation of government consumption expenditure? Explain your answer. (2 marks)

(c) Based on the information given in Source C, explain with TWO reasons why the market of stored value facilities in Hong Kong is NOT perfectly competitive. (4 marks)

(d) Refer to Source D. Some citizens claimed, 'I would rather receive \$5,000 cash instead of consumption vouchers.' In terms of functions of money, explain such a claim with TWO reasons. (4 marks)

Answers written in the margins will not be marked.

For part (e), candidates are required to present their answers in essay form. Criteria for marking will include use of sources and economic theories, relevant content, logical presentation and clarity of expression.

- (e) Suppose the Government plans to spend another sum of money to **cope with the pandemic**. The following are two suggestions.

Scheme C	Distribute the sum of money using the same mechanism as the existing Consumption Voucher Scheme .
Scheme H	Spend the sum of money on building new hospitals and hiring additional medical staff .

With reference to the above sources and your own knowledge in Economics, discuss which scheme **the Government** will prefer in order to achieve **EACH** of the following policy objectives respectively.

Objective 1: to relieve **unemployment** in an industry severely affected by the pandemic

Objective 2: to increase average labour productivity $\frac{Q}{L}$

Objective 3: to increase aggregate output (in the short run and/or in the long run)

(14 marks)

[Use a separate paragraph for comparing the effects of the two schemes under each policy objective.]

a) **Recession**

The general price level is decreasing.
The real GDP is decreasing.

a) As the business of retail, accommodation and food services are heavily hit under the pandemic and the social distancing policies. The owners tend to lay off more workers when their business greatly suffered. On the other hand, most public social and personal services could still be continued, such as education, so that they suffer less. Therefore the unemployment rate in retail, food services is higher.

b) **No**

As \$5000 provided by government is only ~~transfer~~ transfer payment with no production involved. It should not be included in government consumption expenditure.

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Answers written in the margins will not be marked.

c) There's Imperfect Information.

Neither sellers nor customers know all the market information about the market of stored-valued facilities, such as their quality and future development.

There's heterogeneous products.

The stored value services provided by different stored valued facilities are different from buyers' point of view, as they provided different promotions for using the electrical voucher.

d) The Consumption ^{voucher} could not perform the 'store of value' of money. People could not store their purchasing power for future consumption in the form of electrical vouchers, as they have maturity date for use.

The Consumption voucher is not generally accepted as a medium of exchange. Consumption voucher cannot acts as a medium for facilities people buying and selling all goods and services, as they could only be used in specific shop, which accept the voucher for their payment.

e) For objective 1:

Scheme C can increase the disposable income of the general public. As the Consumption voucher could only be used in consumption, not for storage of purchasing power, the private consumption expenditure would increase and the demand for food, retail services increases. This creates the

derived demand for workers, so that more labour could be hired and the unemployment problem would be relieved.

Scheme H would ^{not} have effect on relieving unemployment in an industry severely suffered. The construction of hospital provide job opportunity for the unemployed population, but in long run, the unemployment in suffered industry still could not be solved.

Overall, government would prefer Scheme C to achieve object, as it could effectively stimulated the business of the affected industries and provide more job opportunity for the unemployed.

For objective 2:

Scheme C may not improve the average labour productivity. The provision of consumption voucher increases the demand for retail and food services. The labour supply may increase as shops tends to hire more workers and workers have longer hours for work to earn an income. However, if the future prospects and rewards of the job is uncertain and workers are affected by the pandemic, their health risk increases, they may not be productive and the average labour productivity may not improved.

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Scheme H could improve average labour productivity. When the government build up new hospital and hire additional medical staff, the shorter time for seek patient to receive medical services and this safeguard the public health. With better health condition, workers could perform better and produce goods more efficiently, so that the average labour productivity can be improved.

< ★ p.24

For Objective 3

Scheme C Could Increases the output level in short run. The Consumption vouchers is transfer payment, which increases the disposable income of the household. As people could not store their purchasing power in form of consumption vouchers, their consumption expenditure would increase effectively. Aggregate demand increases and the output level increases.

Scheme C may not improved the long run aggregate output as the consumption voucher is one-time payment.

Scheme H Could improve the aggregate output in short run. As government tend to build new hospital and hire additional medical staff, the labour force would increases and the short run aggregate supply would increases. The output level

Increases in short run.

Scheme H could also increase the potential output in long run. As the infrastructure of building new hospital could increase the physical capital and the production capacity. The long run aggregate supply increases and the full employment output level increases.

Overall, the government would prefer Scheme H to achieve objective 3 as it can effectively increase the output level in both short run and long run.

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END OF PAPER

Sources of materials used in this paper will be acknowledged in the *HKDSE Question Papers* booklet published by the Hong Kong Examinations and Assessment Authority at a later stage.

Answers written in the margins will not be marked.

Supplementary Answer Sheet

Question No. 11

Overall, the government would prefer Scheme H as it could effectively increase the average labour productivity by providing more medical services for the public and improve their health condition, as well as their productivity.

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Section A (44 marks)

1. (a) Mary was the major shareholder of a private limited company which operated a restaurant chain. She planned to change the form of business ownership to a listed company. List **ONE** advantage and **ONE** disadvantage of the change. (2 marks)
- (b) After opening some new restaurants, Mary found that the average cost of production of her company had increased. Explain the change in average cost with **ONE** reason. (2 marks)

1. (a) Disadvantage: Her control over the company may be weakened, the risk of the company being taken over will increase.

Advantage: The company can issue share to the public and trade share in a stock exchange to raise more capital. The source of capital will be wider.

1. (b) Mary suffer from diseconomies of scale. Because Mary may have a huge outstanding loan, thus the interest may increase if she borrow more money from the banks. The borrowing cost increase leading to an increase in average cost of production.

2. There are two kinds of food deliverers: 'riders' delivering food by self-provided motorbikes and 'walkers' delivering food on foot. Why do 'riders' usually have a higher income per order than 'walkers'? Suggest **ONE** demand-side factor and **ONE** supply-side factor to explain your answer. (4 marks)

Demand-side: Riders' speed of delivering food is faster than walkers. Riders provide better service than walkers. So the demand for riders is higher than the demand for walkers. Thus the income per order is higher than walkers.

Answers written in the margins will not be marked.

Supply-side: Riders need to have a self-provided motorbikes, but walkers do not need. Thus, the requirement of being a riders is more than being a walker. Thus, the supply of rider is lower than the supply of walker. It leads to a higher income per order of rider than walker.

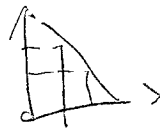
3. Refer to the following data about Country A.

Year	2019	2020
Per capita disposable income	\$15 000	\$20 000
Gini coefficient (based on household income)	0.51	0.56
Gini coefficient (based on household disposable income)	0.51	0.44

- (a) State **TWO** reasons to explain why the increase in per capita disposable income may lead to an over-estimation of the improvement in living standard of Country A. (2 marks)
- (b) Based on household disposable income, did income inequality of Country A improve or worsen in 2020? Suggest **ONE** policy which may have caused such a change. (2 marks)

3(a) First, the crime rate of the country may be very high, which lower the living standard. But per capita disposable income cannot reflect the crime rate.

Second, the price level of the country may increase sharply. A high inflation rate may make people cannot afford daily necessities, which may lower the living standard. But per capita disposable income cannot reflect the price level.



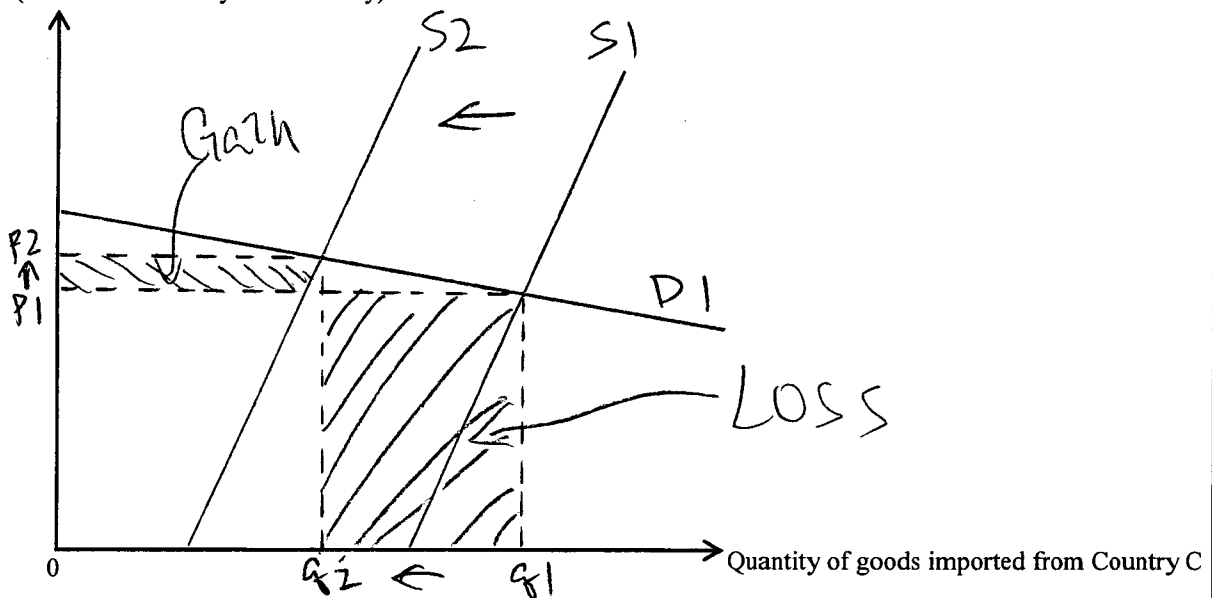
3. (b) The income inequality has improved in 2020. Increasing the unemployment benefit, can improve income inequality. It will let the income of unemployment population increase, which is lower-income group, while the income of higher-income group won't be affected. The income gap is narrowed.

4. Country B and Country C are two large open economies. Facing a huge visible trade deficit, Country B imposes a per-unit tariff on goods imported from Country C. Suppose Country B's demand for goods imported from Country C is elastic.

- With the aid of Figure 1, explain how the tariff would affect the total expenditure of Country B on goods imported from Country C. (6 marks)
- "Devaluation of a country's currency against its trading partners' may have the same effect on imports as tariff." Use Country B as an example to justify this statement. (2 marks)
- Apart from the effect on the country's visible trade balance, explain ONE other effect of devaluation on its balance of payments. (2 marks)

Figure 1: Goods imported from Country C by Country B

Price (in terms of Country B's currency)



4. (a) When the tariff is imposed, the supply will decrease, the price will increase, quantity transacted will decrease. As the demand is elastic, the percentage decrease in quantity transacted is larger than the percentage increase in price. The gain in total

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4(a) expenditure is smaller than the loss in total expenditure. Thus, the total expenditure will decrease.

4.(b) Devaluation will lead to an increase in the price of imported good in terms of Country B's currency. The quantity demanded will thus decrease. As Country B's demand is elastic. The percentage increase in the price is smaller than the percentage decrease in the quantity demanded. The gain in total expenditure will be smaller than the loss. The total expenditure will thus decrease, which is same as the effect of tariff.

4-(c) The invisible trade balance will increase. As devaluation occurs, the price of the product and service in the country will be lower in terms of other countries' currencies. So the cost of foreigners visiting the devaluation country will be lower. More foreigners will travel to the country. Thus the export of service increases, leading to an increase in invisible trade balance.

5. Country D introduced a short-term capital gains tax (STCGT) on property market.

Capital gains (\$)	STCGT rate (%)
10 000 or below	8
10 001 to 50 000	16
50 001 to 100 000	24
100 001 or above	32

STCGT is a tax on capital gains from the sale of a property held for less than 1 year.

A spokesman of the tax department said that a new computer system had been developed for STCGT. Although the system cost more than 1 billion dollars, it allowed tax payers to check and pay the amount of STCGT online easily.

- (a) Evaluate the new tax in terms of **TWO** principles of taxation put forward by Adam Smith. (4 marks)
- (b) 'The introduction of STCGT would not relieve the problem of rising property prices.' Explain whether this is a positive statement or a normative statement. (2 marks)

5.(a) It does not consistent to the economy principle.
Because the government need to pay over
1 billion dollars to build up the tax system.
It may higher than the tax revenue. Thus,
It is not economy.

It is consistent to the convenient principle.
As the system allow tax payers to check
and pay the amount of STCGT online easily.
Therefore, it is convenient to the taxpayers.

5.(b) It is a positive statement.
Because it is refutable by facts and
it does not involve value judgement.

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6. (a) 'Deflation will occur if the amount of goods and services produced is growing faster than money supply.' Explain this statement in terms of the quantity theory of money. (4 marks)

(b) 'If deflation is expected, the real interest rate will be higher than the nominal interest rate.' Why? (2 marks)

6.(a) Let M be money supply, V be the velocity of money circulation, P be the price level, Y be the real output.

Quantity theory of money states that $MV = PY$, where V is a constant.

So, percentage change in $M = \text{percentage change in } P + \text{percentage change in } Y$

When the percentage increase in Y is higher than the percentage increase in M , there is a percentage decrease in P .

Thus, deflation occurs.

6 (b) Because,

Nominal interest rate = Expected real interest rate + Expected inflation rate

Thus, when deflation is expected, the expected inflation rate will be negative. Thus the real interest rate will be higher than the nominal interest rate.

7. In a two-country-two-good model, the outputs per unit of resources of both countries are as follows.

	Rice (units)		Toys (units)
Country E	10	OR	20
Country F	5	OR	15

- (a) Assume the terms of trade are that 1 unit of rice can be exchanged for 2.2 units of toys. Calculate the gains from trade of **EACH** country when trading 1 unit of rice. Show your workings. (4 marks)
- (b) With reference to your answer in part (a), defend the following statement. 'There is still a basis for trade even if a country has no absolute advantage in producing any goods.' (2 marks)

7.(a) Opportunity cost of Country E producing 1 unit of rice = $20 \div 10 = 2$ Toys

Opportunity cost of country F producing 1 unit of rice = $15 \div 5 = 3$ Toys

\therefore Because the opportunity cost of Country E producing rice is lower, so Country E gains the comparative advantage, Country E will export rice.

The gain from trade of Country E = $2.2 - 2 = 0.2$ Toys

The gain from trade of Country F = $3 - 2.2 = 0.8$ Toys

7.(b) Country F has no absolute advantage in producing any goods, but Country F can still gain from trade with reference to the answer in part (a). Thus, Country F and E can still mutually benefit from trade, thus there is still a basis for trade.

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0.25

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

Assets (\$ million)		Liabilities (\$ million)	
Reserves	1 000	Deposits	4 000
Loans	3 000		

The public initially holds \$1 000 million cash and the banks are fully loaned up.

- (a) Calculate the required reserve ratio. (1 mark)
- (b) Suppose the public only wants to hold \$400 million cash and deposits the remaining cash into the banks. Calculate the maximum change in money supply. Show your workings. (3 marks)

8(a) Required reserve ratio = $1000 \div 4000$
 $= 0.25$

8(b) The initial money supply = $4000 + 1000$
 $= \$5000 \text{ million}$

Maximum amount of new money supply
 $= \frac{1000 + 600}{0.25} + 400$
 $= \$6800 \text{ million}$

The maximum change in money supply
 $= 6800 - 5000$
 $= \$1800 \text{ million}$

\therefore The money supply will maximally increase by \$1800 million.

END OF SECTION A

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Section B (60 marks)

9. The Mainland government introduced the Targeted Poverty Alleviation Campaign (精準扶貧政策) in 2014. After analysing the situations of people living in poverty, the government officials came up with tailor-made measures. The following are two examples of the campaign.

Example 1	A village in Yunnan province has beautiful natural landscape. The government of Yunnan province promoted the village to attract more travellers. Apart from farming, the villagers also set up hostels to serve travellers in order to earn more income.
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- (a) Refer to Example 1.
- (i) In which types of production did the villagers engage after the introduction of the campaign? Explain. (4 marks)
- (ii) Explain how labour mobility of the villagers would be affected. (3 marks)

Example 2	The government provided funding and invited private firms to develop hydroelectric power plants in six provinces (such as Hubei and Jiangxi). Such development would help improve transportation, irrigation and flood prevention in the rural villages in these provinces.
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- (b) Refer to Example 2. With the aid of a diagram, explain how aggregate output in these six provinces would be affected in the long run. (8 marks)

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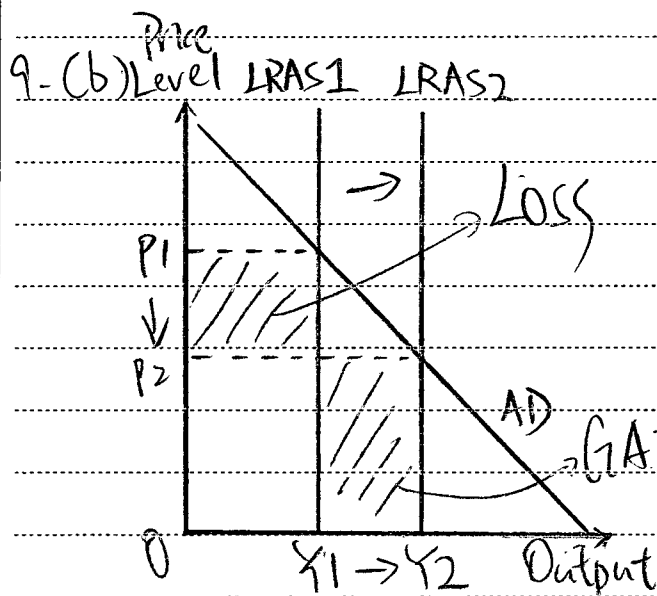
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9(a)(i) They engage in primary production and tertiary production.
Because farming is a production of raw materials, such as cottons, so it is primary production.
Hostels is providing services to consumers, so it is tertiary production.

9(a)(ii) Villagers' geographical mobility will increase, when they earn more income, they will be able to afford the transportation cost to travel to other places, so they are able to work in different places.
Villagers' occupational mobility will increase because the travelling industries is developed.

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9. (a)(ii) In the village, villagers have more types of job to choose. so their occupational mobility increase. *different*



After the measure, the transportation and flood prevention will improve, leading to an increase in the production capacity, thus the full employment level increase, the long run aggregate demand will increase. the price level will decrease in long run, the aggregate output will decrease in long run.

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10. The Olympic Games attract billions of international television viewers to watch the competitions among thousands of top athletes.

- (a) Some restaurants in shopping malls find their businesses increase sharply when the malls broadcast Olympic events. Explain how the broadcast of Olympic events may result in a divergence between private and social benefits. (3 marks)
- (b) Suppose the divergence in part (a) does exist. How can market mechanism help reduce this divergence? (2 marks)

Athletes compete in the Olympic Games with their support teams consisting of sport psychologists, physical therapists, nutritionists, etc.

- (c) Which economic principle is illustrated in the above practice? State **TWO** reasons why such a practice can increase labour productivity. (3 marks)

Some professional athletes receive a monthly salary and share a proportion of the prize money whenever they win in competitions.

- (d) Instead of paying the athletes a monthly rate only, explain why some employers of professional athletes use the above wage payment arrangement. (2 marks)

Whenever an athlete wins a gold medal in a certain sport, there will be the following phenomena: more people will start learning the sport. As a result, there will soon be long queues registering for courses in the sport.

- (e) With the aid of a demand-supply diagram, explain the above phenomena. (5 marks)

Professional athletes usually start their full-time training before graduating from secondary school and have to give up their studies.

- (f) Will the opportunity cost of being a professional athlete be affected if the average income of professional athletes increases? Explain. (2 marks)

10.(a) A Positive externality occurs, the broadcast attract more people to visit the shopping malls, People may dine in the restaurant in the mall, so the broadcast benefit the restaurants, but the restaurants didn't pay or compensate the malls. External benefit exist, the marginal social benefit is higher than the marginal private benefit, so it result in a divergence between private and social benefits.

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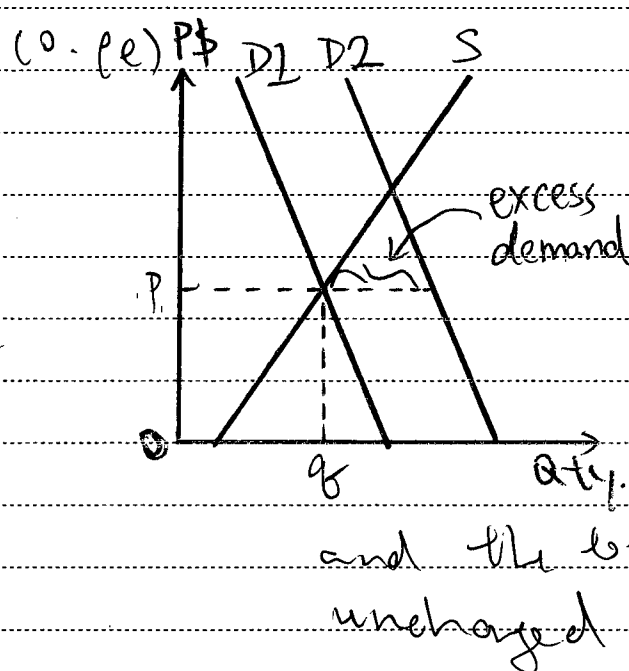
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10. (b) As the broadcast can benefit the restaurant, so there is an excess demand in the broadcast, so the restaurant may pay the mall to do more broadcasting, so that the marginal private benefit will increase, and the divergence between private and social cost narrowed.

10. (c) Division of labour,

Reasons : 1. Practice makes perfect
2. Save the time for training

10. (d) Because the income of the athletes will increase, if they won prize. Thus, the athletes' incentive to training will be higher than only giving a monthly rate. Thus the cost of supervision is lower. So employers will use this arrangement.



The demand for the courses will increase. But the price has not increased yet, leading to an excess demand for the course, and the quantity transacted and the total revenue is remain unchanged.

10.(f) No.

Because opportunity cost is the value of the highest-valued option forgone. However, the average income of professional athletes increases only affect the value of chosen option. It doesn't affect the value of the highest-valued option forgone, thus it won't affect the opportunity cost.

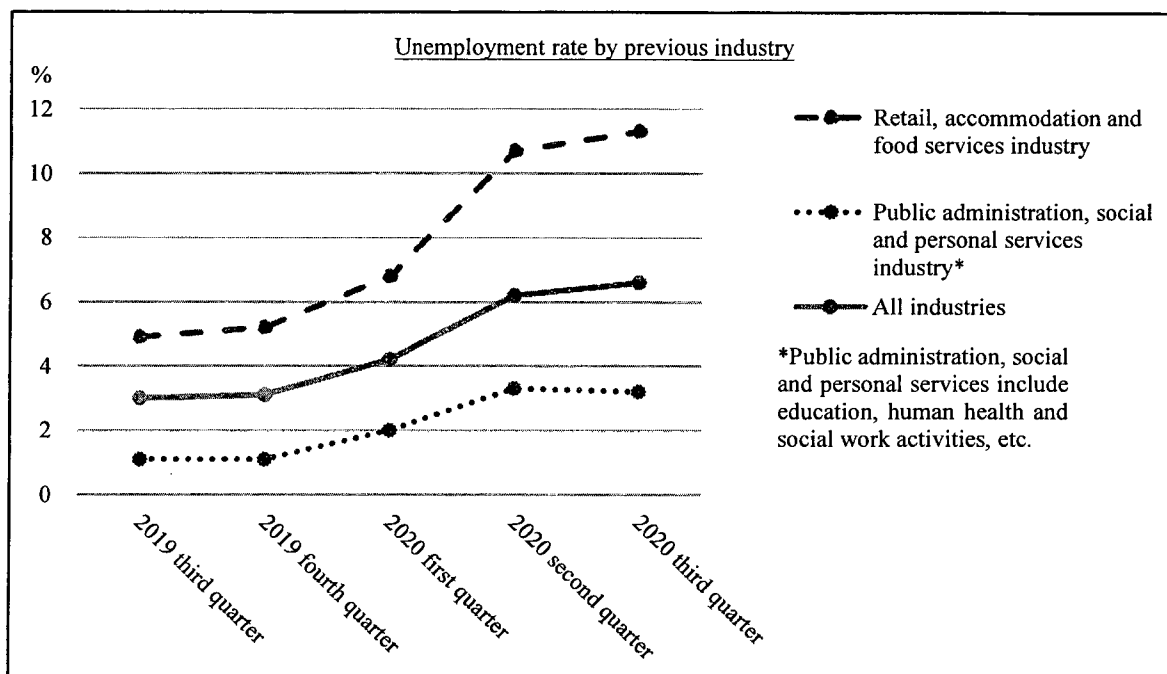
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11. The Government launched the Consumption Voucher Scheme in 2021 to relieve the impact of COVID-19 on the Hong Kong economy.





Source A: Statistical data about unemployment rate in Hong Kong



Source B: An extract of information about the Consumption Voucher Scheme

All Hong Kong permanent residents and new arrivals aged 18 or above, who comply with the 'residing in Hong Kong' requirement, could register to receive electronic consumption vouchers with a total value of \$5 000 by instalments.

Source C: Information about the four designated stored value facilities to receive the \$5 000 consumption vouchers by instalments

	AlipayHK	Octopus	Tap & Go	WeChat Pay HK
	 AlipayHK	 八達通 Octopus		 WeChat Pay [®]
Public transportation with the above payment facilities installed	MTR, bus, mini bus and ferry	MTR, bus, mini bus and ferry	Bus and mini bus	None
Promotions to consumption voucher users	5 e-coupons	First 2 million registered customers enjoy \$18 of stored value	\$50 awarded when using virtual Tap & Go Unionpay card for the first transaction with an amount equal to or larger than \$50	e-coupons




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Source D: Some reminders for the Consumption Voucher Scheme

- Consumption vouchers cannot be used in transactions such as payments to the government (e.g. tax), public utilities (e.g. electricity charges), purchase of financial products (e.g. insurance), and direct purchase from merchants located outside Hong Kong.
- There are deadlines for using consumption vouchers.

Source E: Some views on the Consumption Voucher Scheme in Hong Kong

<p>A housewife</p> 	<p>I have spent more than \$5 000 as there are e-coupons from the stored value facility provider. A lot of promotions in large retail chains and malls have also tempted me to consume!</p> <p>AD ↑ PCE ↑</p>
<p>A former chef in a restaurant</p> 	<p>I have been laid off and have stayed home for months. No one knows when the travellers would be back. I hope that the Consumption Voucher Scheme will bring more local people to spend on food and beverage and the whole industry can survive the pandemic. Otherwise, many workers will be forced to leave the industry.</p> <p>Output ↑ employment ↓</p>
<p>A doctor working in a public hospital</p> 	<p>Resources should be allocated to the medical sector, instead of giving everyone an equal amount under the Consumption Voucher Scheme. The public hospitals lacked space, manpower and equipment even before the pandemic. Start building new hospitals earlier so that more lives could be saved.</p>

- (a) Refer to Source A.
- In which phase of business cycle the Hong Kong economy most likely was? Apart from the change in unemployment rate, list **ONE** other economic phenomenon of this phase. (2 marks)
 - Why did the unemployment rate of retail, accommodation and food services industry increase faster than that of public administration, social and personal services industry during the pandemic? (2 marks)
- (b) Refer to Source B. Would the \$5 000 distributed under the Consumption Voucher Scheme be included in the calculation of government consumption expenditure? Explain your answer. (2 marks)
- (c) Based on the information given in Source C, explain with **TWO** reasons why the market of stored value facilities in Hong Kong is **NOT** perfectly competitive. (4 marks)
- (d) Refer to Source D. Some citizens claimed, 'I would rather receive \$5 000 cash instead of consumption vouchers.' In terms of functions of money, explain such a claim with **TWO** reasons. (4 marks)

For part (e), candidates are required to present their answers in essay form. Criteria for marking will include use of sources and economic theories, relevant content, logical presentation and clarity of expression.

- (e) Suppose the Government plans to spend another sum of money to cope with the pandemic. The following are two suggestions.

Scheme C	Distribute the sum of money using the same mechanism as the existing Consumption Voucher Scheme.
Scheme H	Spend the sum of money on building new hospitals and hiring additional medical staff.

With reference to the above sources and your own knowledge in Economics, discuss which scheme the Government will prefer in order to achieve **EACH** of the following policy objectives respectively.

Objective 1: to relieve unemployment in an industry severely affected by the pandemic

Objective 2: to increase average labour productivity

Objective 3: to increase aggregate output (in the short run and/or in the long run)

(14 marks)

[Use a separate paragraph for comparing the effects of the two schemes under each policy objective.]

11. (a)(i) Recession.

The aggregate output decreases.

11. (a)(ii) Because public administration, social and personal services is more necessary than retail, accommodation and food services in people's daily lives. Thus, the pandemic's effect on the former is less than the latter.

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11. (b) No, because the \$5000 is only a transfer of wealth, it does not involve current consumption, so it would not include in the calculation of government consumption expenditure.

11. (c) Reason 1: They provide heterogeneous product and services. Their products and service is differentiated.

Reason 2: It involves non-price competition, as the facilitates launch different promotion to consumption voucher users to compete with each other.

11. (d) Reason 1: The vouchers' function of medium of exchange is weaker than money. Because it is not generally accepted, it can't be use to purchase from merchants located outside Hong Kong, of financial products, etc.

Reason 2: The vouchers' function of store of value is weaker than money. As there are deadlines for using consumption vouchers, the value of the vouchers will decrease sharply after the deadline, so it cannot store and keep values as long as money.

11.(e) Objective 1

Scheme C can relieve unemployment in an industry severely affected by the pandemic. When more consumption voucher is given to the residents, the private consumption expenditure will increase and hence the aggregate output. An increase in aggregate output will lead to an increase in input. Thus, the demand for labour will increase. More people can be able to get a job. The unemployment rate will decrease. Thus, Scheme C can achieve objective 1.

Scheme H cannot relieve unemployment in an industry severely affected by the pandemic. Although it can relieve the excess demand on medical service, it has no extra effect on other industries that severely affected by the pandemic, such as catering industry.

In short, Scheme C can achieve objective 1, while Scheme H cannot.

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11.(e) Objective 2

Scheme C can increase the average labour productivity. When the consumption voucher's amount increase, the improvement in the welfare measure can lead to an increase in working incentive. It will result in an increase in average labour productivity.

Scheme H can increase the average labour productivity. When more new hospital is built and additional medical staff is hired, it can relieve the excess demand for medical service. More people can get medical support. People's health condition will be improved. Their ability on working will also improved. Therefore, the average labour productivity will increase.

In short, both Scheme C and Scheme H can achieve Objective 2.

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11. (e) Objective 3

Scheme C can increase the aggregate output in the short run. When more consumption voucher is given to the residents, the private consumption expenditure will increase. It will result in an increase in aggregate demand. Then, the aggregate output in the short run will increase.

Scheme 1-1 can increase the aggregate output in both the long run and short run. When the money is spending on hiring medical staff and building hospital, government expenditure will increase.

Thus, the aggregate demand will increase and hence the aggregate output in short run. Apart from that, it will improve the medical system by relieving the excess demand for medical service. It will attract more imported labour to work in Hong Kong. It will increase the labour force and hence the full employment level in the long run. Thus, the long run aggregate supply will increase, which leads to an increase in long run aggregate output.

In short, both Scheme C and

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11.(c) Scheme H can achieve Objective 3.

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END OF PAPER

Sources of materials used in this paper will be acknowledged in the *HKDSE Question Papers* booklet published by the Hong Kong Examinations and Assessment Authority at a later stage.

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Supplementary Answer Sheet

Question No. _____

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