

ECONOMICS PAPER 2
Question-Answer Book

10:15 am – 12:45 pm (2 hours 30 minutes)
This paper must be answered in English

INSTRUCTIONS

- (1) After the announcement of the start of the examination, you should first write your Candidate Number in the space provided on Page 1 and stick barcode labels in the spaces provided on Pages 1, 3, 5, 7, 9 and 11.
- (2) This paper consists of two sections, A and B. Answer ALL questions in sections A and B.
- (3) Write your answers in the spaces provided in this Question-Answer Book. Do not write in the margins. Answers written in the margins will not be marked.
- (4) Supplementary answer sheets will be supplied on request. Write your Candidate Number, mark the question number box and stick a barcode label on each sheet, and fasten them with string INSIDE this book.
- (5) No extra time will be given to candidates for sticking on the barcode labels or filling in the question number boxes after the 'Time is up' announcement.

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Candidate Number



Section A (50 marks)

1. The table below shows the distribution of market share in the telecommunications industry in Hong Kong in 2023.

	Market Share
Hong Kong Telecommunications (stock code: 6823)	55%
Hong Kong Broadband Network	35%
Others	10%

- (a) (i) Name the type of business ownership of Hong Kong Telecommunications. (1 mark)
- (ii) Suppose Hong Kong Telecommunications plans to raise capital for expansion. From the viewpoint of the owners of the company, state **ONE** advantage and **ONE** disadvantage of issuing shares over bonds. (2 marks)
- (b) What was the type of market structure of the above telecommunications market in 2023? List **TWO** features of this type of market structure that distinguish it from all the other types of market structure. (3 marks)
- (c) Unlike Hong Kong, City A has only one telecommunications company. Suggest **ONE** possible source of monopoly power for the telecommunications company in City A. (1 mark)

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2. Many industrial activities emit carbon dioxide, intensifying global warming and potentially bringing hazards to all human beings.

- (a) In terms of externality, explain why the emission of carbon dioxide by industrial activities may result in economic inefficiency. (4 marks)

A system of carbon credits is introduced by the governments in some countries. Carbon credits are permits for emitting carbon dioxide. Producers must purchase carbon credits from the government in order to engage in production activities that emit carbon dioxide.

- (b) Explain how the introduction of the system of carbon credits may improve economic efficiency. (2 marks)

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3. Since 2020, the government of an economy has imposed an effective quota on the production of automobiles. From 2022 to 2023, a strong economic growth was recorded in the economy.

Suppose automobiles are normal goods. How would the deadweight loss in the market of automobiles in the economy be affected by the economic growth in the above period? Explain with the aid of a diagram.

(6 marks)

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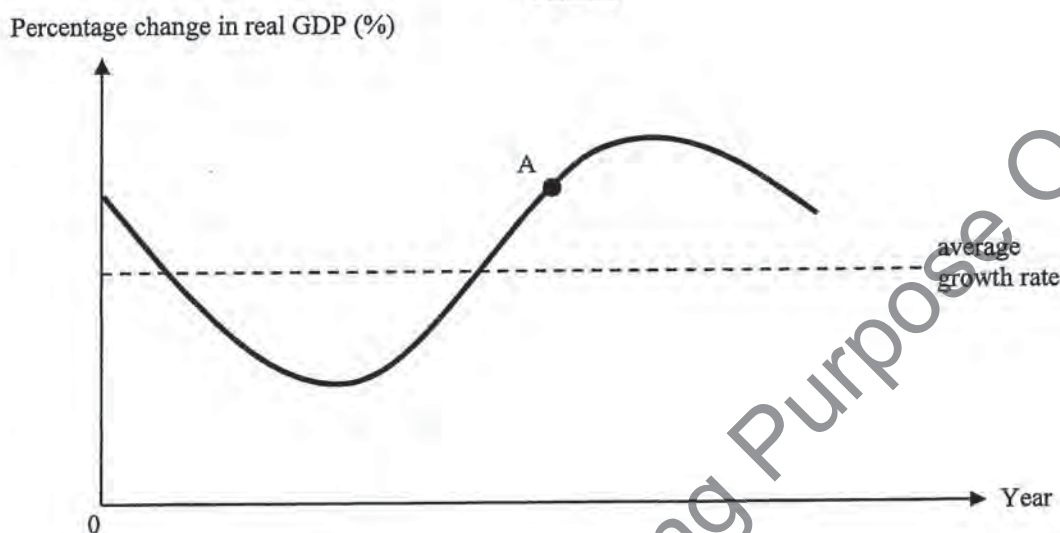
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4. Figure 1 shows the percentage change in real gross domestic product (GDP) of an economy.

Figure 1



- (a) Identify the phase of business cycle that point A is in. (1 mark)
- (b) Apart from the change in real GDP, list TWO economic phenomena which would generally occur at point A. (2 marks)

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5. Refer to the following statistical information of an economy.

Year	Nominal GDP (\$ million)	Year-on-year percentage change in implicit price deflator of GDP
2022	2 850 000	+3.8%
2023	2 800 000	+0.7%

- (a) Based on the above information, how did the real output of the economy change from 2022 to 2023? Explain your answer. (2 marks)
- (b) 'As the nominal GDP in 2023 decreased, the general living standard in the economy deteriorated during that period.' Suggest **TWO** reasons why this statement may be incorrect. (2 marks)
- (c) Suppose people did not expect any change in the general price level in 2023. A tenant signed a rental contract with a landlord in 2022 for a fixed monthly rental over a 3-year contractual period. Who, the tenant or the landlord, would gain when the above change in the general price level occurred in 2023? Explain. (2 marks)

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6. Refer to the following conversation between two villagers in a barter economy.

Villager A: I want to exchange my beans for your pork.

Villager B: But what I want now is rice.

- (a) A problem that hinders exchanges in a barter economy is revealed in the above situation. Identify the problem. (1 mark)
- (b) (i) What is money? (1 mark)
- (ii) Explain how the use of money can facilitate exchanges. (2 marks)

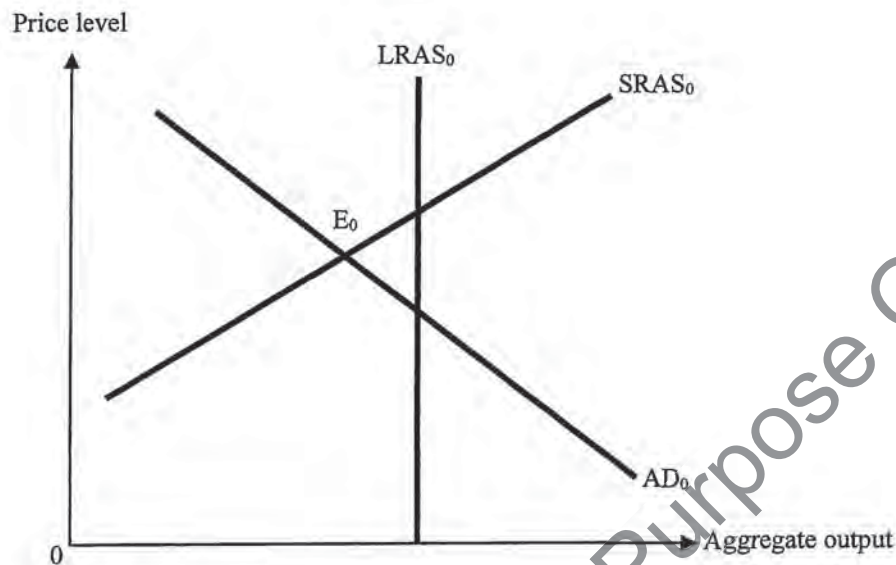
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7. Figure 2 shows the aggregate demand (AD), short run aggregate supply (SRAS) and long run aggregate supply (LRAS) curves of an economy.

Figure 2



- (a) Give **ONE** reason to explain why the aggregate demand curve is downward sloping. (3 marks)
- (b) Suppose the economy initially operates at E_0 . With the aid of Figure 2, explain how the market adjustment mechanism can restore the aggregate output to the full-employment output level in the long run. (5 marks)

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8. Suppose in an economy, the public increases their cash holding by withdrawing bank deposits. Immediately after the withdrawal, the banking system of the economy faces a reserve shortage of \$100 million.

The following table shows the balance sheet of the banking system immediately after the withdrawal.

Assets (\$ million)		Liabilities (\$ million)	
Reserves	600	Deposits	3 500
Loans	2 900		

- (a) Find the required reserve ratio. (1 mark)
- (b) Suppose the required reserve ratio is reduced by 5 percentage points. Calculate the maximum possible change in deposits after deposit creation/contraction. Show your workings. (3 marks)

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9. The table below shows the total output of Country X and Country Y. Each country allocates 25% of its resources to produce bread and 75% of its resources to produce clothing.

	Bread (units)		Clothing (units)
Country X	100	AND	75
Country Y	80	AND	240

- (a) Explain whether Country X has an absolute advantage in the production of bread. (2 marks)
- (b) Suppose Country X and Country Y trade at an exchange ratio of 10 units of bread to 7 units of clothing. Calculate the gain from trade for the bread-exporting country from exporting 30 units of bread. Show your workings. (4 marks)

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Section B (70 marks)

10. The government of City B actively promotes the development of tourism industry.

Suppose some airlines in City B hold promotion campaigns that a total of 20 000 flight tickets to City B are given out for free.

- (a) Explain whether the free flight tickets are
- (i) free goods. (2 marks)
 - (ii) public goods. (3 marks)
- (b) To which type of production do airlines belong? Explain your answer. (2 marks)

Following the promotion effort of the government, many people travel to City B. As a result, flight ticket price is doubled, while the quantity transacted of flight tickets changes by 50%.

- (c) Based on the above information, what can we conclude about the price elasticity of demand and/or supply of flight tickets? Explain. (3 marks)
- (d) To further stimulate the tourism industry, the government of City B abolishes the lump-sum fuel surcharge on flight tickets. Explain how the average flight distance would be affected. (3 marks)

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11. Ann is the owner of a coffee shop in Hong Kong.

- (a) Ann is recruiting a new barista to prepare beverages for customers in her coffee shop. She is considering the following two wage payment methods.

Wage Payment Method A	Wage Payment Method B
- \$14 000 per month	- \$15 000 per month
- The barista is allowed to receive tips from customers	- The barista is NOT allowed to receive tips from customers

From the viewpoint of the barista, state **ONE** advantage and **ONE** disadvantage of wage payment method A over wage payment method B. (2 marks)

- (b) The landlord of Ann's coffee shop premises raised the monthly rental from \$70 000 to \$85 000. Ann said, 'Despite the increase in the monthly rental, the quantity of daily output of my coffee shop remains unchanged.'
Explain Ann's output decision with reference to the profit-maximising condition under perfect competition. (3 marks)
- (c) Ann invited a famous barista from Japan to provide a workshop for her customers. The barista received a remuneration of \$30 000 from Ann's coffee shop and stayed in Hong Kong for a week. Explain how this \$30 000 would affect Hong Kong's net factor income from abroad. (3 marks)
- (d) Suppose more and more Mainland visitors consume at Ann's coffee shop. Thus, Ann purchases more coffee beans from Brazil to cater for the increased business. Explain why these transactions may increase the current account balance of Hong Kong's balance of payments. (3 marks)
- (e) Ann has been operating her business in the form of a sole proprietorship. Give **TWO** economic reasons why she does not choose to change the form of business ownership of her coffee shop to a partnership. (2 marks)
- (f) After opening several new coffee shops, Ann found that the average cost of production of her business had decreased. Give **TWO** reasons for the above change in average cost. (2 marks)

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12. Since the 2010s, the government of Saudi Arabia has been actively promoting football development.

- (a) Suppose a football club in Saudi Arabia constructs a large football stadium there. With the aid of a diagram, explain how Saudi Arabia's aggregate output in the short run will be affected during the construction period of the stadium. (5 marks)

Some football clubs in Saudi Arabia have established their own football academies to train young players.

- (b) Suppose some unemployed youngsters stopped seeking jobs and enrolled in the full-time training programmes of these football academies. Explain how the unemployment rate in Saudi Arabia would be affected. (4 marks)
- (c) Ahmed, an unemployed youngster in Saudi Arabia, is considering whether he should stop seeking jobs and enrol in a full-time training programme of a football academy. His order of preference is as follows:

First option:	to enrol in a training programme of Football Academy A
Second option:	to enrol in a training programme of Football Academy B
Third option:	to continue seeking jobs

Suppose Football Academy B offers a scholarship to Ahmed. Explain whether the opportunity cost for Ahmed to continue seeking jobs would necessarily remain unchanged. (3 marks)

- (d) Neymar is a famous Brazilian footballer. He has been recruited by a football club in Saudi Arabia recently. Suppose he is required to pay an income tax of 20% on his taxable income to the Government of Saudi Arabia. Explain whether the income tax paid by Neymar is
- (i) a direct tax or an indirect tax. (2 marks)
- (ii) progressive, proportional or regressive. (2 marks)

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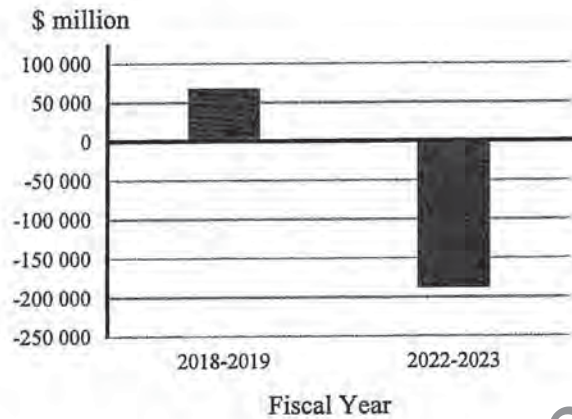
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13. Hong Kong experienced an economic downturn because of the Covid-19 pandemic. It still faces various challenges on its path to resumption of normalcy after the pandemic.

Source A: Fiscal balance of the Hong Kong Government



Source B: Exchange rate of US dollar (USD) to Renminbi (RMB) before and after the pandemic

Date	Exchange Rate
1 April 2019	USD 1 = RMB 6.71
1 November 2023	USD 1 = RMB 7.32

Source C: News extract about the catering industry in Hong Kong in 2023

According to a representative of the catering industry in Hong Kong, local restaurants are unable to recruit enough waiters even though they are offering wages that are more than 50% above the statutory minimum.

Source D: Wage rates of waiters in Hong Kong in 2023

Statutory minimum wage rate	\$40 per hour
Average wage rate of waiters	\$62.4 per hour

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Source E: Some data and views on the Hong Kong economy

A banker 	Influenced by the contractionary monetary policy in the US, the interest rate in Hong Kong rose drastically from mostly below 2% in 2018 to over 5% by the end of 2023.
An economist 	The inflation rate in the Mainland remained lower than that in Hong Kong throughout 2023. Negative growth in the general price level was recorded in October and November in the Mainland.
A government official 	Reviving the night-time economy is essential in facilitating the economic recovery in the short term, whereas innovation and technology development is a significant engine for driving high-quality economic growth in the medium-to-long term.

- (a) Refer to Source A. How may an economic downturn affect the fiscal balance of the Hong Kong Government? Explain your answer with reference to the possible effects of an economic downturn on the government's revenue and expenditure. (4 marks)
- (b) Refer to Source B. Under the Linked Exchange Rate System of Hong Kong, how would the change in the exchange rate shown in Source B affect the number of Hong Kong residents visiting the Mainland during the period? Explain your answer. (3 marks)
- (c) Refer to Sources C and D.
- Illustrate the economic phenomenon revealed by Source C with a supply-demand diagram.
 - With the aid of the same diagram in (c)(i), explain whether the minimum wage was effective in the labour market of waiters in 2023. (5 marks)

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

- (d) Suppose there are two suggestions to stimulate Hong Kong's economic recovery and growth:

Suggestions	Objectives
I. Importing a large number of low-skilled workers for the catering industry and organising more night-time events to attract citizens and tourists to stay out at night for leisure	To facilitate the revival of the catering industry by boosting their revenue
II. Providing tax deductions for firms' expenses on innovation and technology projects to attract local and foreign investors to invest in the innovation and technology industry in Hong Kong	To enhance labour productivity and potential output

With reference to the above sources and your own knowledge in Economics, discuss

- how each of the above two suggestions may achieve its objective, and
- some possible factors that may limit the effectiveness of the two suggestions in achieving their corresponding objective. (Hint: You may consider some macroeconomic variables shown in the above sources, e.g. the exchange rate and the interest rate.)

(14 marks)

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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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