



Province of the
EASTERN CAPE
EDUCATION

ECONOMICS P1
COMMON TEST - JUNE 2014
MEMORANDUM

**NATIONAL
SENIOR CERTIFICATE**

GRADE 12

MARKS : 150

TIME : 1½ Hours

This memorandum consists of 12 pages

SECTION A**QUESTION 1****1.1 Choose the answer and write only the letter (A – C) next to the question number.**

1.1.1	A✓✓	fiscal		
1.1.2	C✓✓	injection		
1.1.3	B✓✓	direct investment		
1.1.4	C✓✓	trough		
1.1.5	A✓✓	lagging		
1.1.6	C✓✓	free rider		
1.1.7	A✓✓	deregulation		
1.1.8	B✓✓	current	(8 x 2)	(16)

1.2 Choose a description from COLUMN B that matches an item in COLUMN A.

1.2.1	G✓			
1.2.2	E✓			
1.2.3	H✓			
1.2.4	A✓			
1.2.5	B✓			
1.2.6	D✓			
1.2.7	C✓			
1.2.8	F✓		(8 x 1)	(8)

1.3 Give the economic term/concept for each of the following descriptions.

1.3.1	public goods✓			
1.3.2	devaluation ✓			
1.3.3	comparative advantage✓			
1.3.4	rent-seeking✓			
1.3.5	moving averages✓			
1.3.6	GDP deflator✓	(6 x 1)		(6)

SECTION A: [30]

SECTION B**QUESTION 2 (CIRCULAR FLOW)****2.1 Answer the following questions appropriately****2.1.1 Name TWO flows found in the circular flow model.**

- * Real flow✓
- * Money flow✓ (2)

2.1.2 Explain how the problem of double counting can be avoided when calculating GDP.

Subtract the value of input costs from the gross value added✓✓ / Do not include the value of intermediate goods in the calculations ✓✓

2.2 Study the diagram below and answer the questions that follow.

- 2.2.1 tax payment✓✓ (2)
 - 2.2.2 savings✓✓/leakage✓✓ (2)
 - 2.2.3 $GDE = C + I + G$ ✓✓✓ (3)
 - 2.2.4 Open economy✓ because of the existence of the foreign sector✓✓ (3)
- [10]**

2.3 Study the table below and answer the questions that follow.

- 2.3.1 South Africa Reserve Bank✓✓/SARB✓✓ (2)
 - 2.3.2 Gross domestic product @ market prices✓✓ (2)
 - 2.3.3 It is the direct subsidy paid by government to firms that produce✓✓ exportable products in order to reduce their production costs. (2)
 - 2.3.4 $R2\ 631\ 227✓ + R50\ 009 - R10\ 732✓ = R2\ 670\ 504✓✓$ (4)
- [10]**

2.4 Distinguish between a factor market and a product market.

Factor market: It is the market where factors of production are sold and bought✓✓. Businesses purchase factors of production from the households through the factor market✓✓.

The factor market is further subdivided into:

- the labour market ✓✓
- capital market ✓✓
- land market✓✓

Product market: This is the market where goods and services are bought and sold✓✓. Businesses produce and sell goods to households, government and foreign sector✓✓. Those goods and services are sold through the product market or goods market✓✓.
(Max 4 for each market)

Any 4 x 2 (8)

2.5 With the aid of a formula explain the multiplier concept.

The multiplier describes a situation where a change in spending eg investment ultimately changes output and income by more than the initial change in investment income ✓✓

- * To show this we need to know the value of the marginal propensity to consume (mpc) and the injection✓✓
- * The formula for the multiplier is: $k = \frac{1}{(1 - MPC)}$ ✓✓
- * Suppose MPC = 0.75 and the injection is R10 000
- * Multiplier = $1 \div (1 - 0.75)$ ✓✓ = 4✓✓
- * The change in aggregate income will be $4 \times 10\,000 = R40\,000$ ✓✓
- * The bigger the MPC, the bigger the multiplier ✓✓

(Any 4 x 2)

Note: Learner may use an MPC and injection different to the one used in the memo.

(8)
[40]

QUESTION 3 (BUSINESS CYCLES)**3.1 Answer the following questions appropriately.****3.1.1 Name TWO broad categories of causes of business cycles.**

- * Exogenous causes✓
- * Endogenous causes✓ (2 x 1) (2)

3.1.2 Why the length of the business cycle important in the forecasting of business cycles .

- * The length of a cycle tells us how long did the cycle last✓✓
- * A long cycle tells us that the underlying causes of that cycle were very strong and a short cycle tells us the causes were weak✓✓
- * The length of a cycle can be used to predict the length of another cycle✓✓
(Any 1 x 2) (2)

3.2 Study the graph below and answer the questions that follow.

3.2.1 1st quarter 2009✓✓ or 09/1✓✓ (2)

3.2.2 5.0%✓✓□ (2)

3.2.3 3✓✓/Any answer between 3 & 3.5%✓✓ (2)

3.2.4 Policies government could have implemented in 2009.

- Reduce taxation✓✓
- Increase government spending✓✓
- Implement expansionary fiscal policies✓✓
- Increase money supply✓✓
- Reduce interest rates✓✓ (Any 2 x 2) (4)

3.3 Study the graph below and answer the questions that follow

3.3.1 P_d ✓✓ (2)

3.3.2 Q_1 ✓✓ (2)

3.3.3 Why is the WS curve horizontal?

- * There are numerous sellers from all over the world that can increase supply at the same price. ✓✓ (2)

3.3.4 Impact of opening up trade

- * Decrease in domestic price from P_d to P_w ✓✓
- * Increase in supply to Q_1 ✓✓
- * Improvement in standard of living of residents✓✓
(Any 2 x 2) (4)

3.4 Compare and contrast the expansion period and the contraction period of a business cycle.

Expansion period:

- * It is a period which represents an increase in economic activity✓✓.
- * It consists of the recovery phase and the prosperity phase✓✓□
- * Expansion ends when it reaches the peak✓✓
- * The further away the peak is from the trend line, the stronger were the underlying causes of expansion✓✓

Any 2 x 2

Contraction period:

- * It is a period when economic activity decreases✓✓
 - * It consists of the recession and depression phases✓✓
 - * It ends with the trough✓✓
 - * The further away the trough is from the trend line, the stronger were the underlying causes of contraction✓✓
- (Any relevant answer:

Any 2 x 2
(8)

3.5 Advise the Minister of Finance of the how he can use tariffs to reduce unnecessary imports.

- * There are two kinds of tariffs he can use to reduce imports✓✓
- * **Ad valorem**✓: He can impose a certain percentage on the value of imported goods.✓✓
Example: He can charge a tariff of 10% on the value of all imported goods✓✓
- * **Specific tariff**✓: He can impose a certain amount on all imported goods based on quantity or weight✓✓.
Example R100 is added to every item that is imported✓✓
- * The tariff increases the price of the goods and makes them expensive for consumers to buy✓✓.
- * Producers may then decide to produce those goods locally instead of importing them✓✓.

Any 4 x 2 (8)

[40]**TOTAL FOR SECTION B: [80]**

SECTION C

Answer **ONE** question from this section.

QUESTION 4

“One of the functions of government is to provide communities with basic services. However, there are certain challenges it is faced with when performing this task.”

- Discuss the problems of public sector provisioning. (30)
- Use the Laffer curve to explain the incentive to work. (10)

INTRODUCTION

(Any other relevant introduction)

(Max. 2)

BODY**1 Accountability ✓**

Government is required to give an explanation of its decisions, actions and expenditures over a period of time ✓✓

Economic accountability ✓: Government must implement correct economic policies and ensure that the resources of the nation are used correctly. ✓✓

- * **Financial accountability** ✓: State funds are controlled by the Treasury. ✓✓ Strict procedures must be followed when expropriating government funds. ✓✓
The **Treasury Committee** ✓ must ensure that expropriation procedures are followed and to ensure that state funds are used appropriately. ✓✓ Government's accounting books must be audited to prevent fraud and corruption. ✓✓
- * **Political accountability** ✓: Ministers are responsible for their departments ✓✓. They must account to Parliament for their actions ✓✓. Ministers must ensure that their departments are run within the rules and policies of government ✓✓. Each department is headed by the Director General ✓✓ whose duty is to ensure that the department is run efficiently on the daily basis ✓✓.
- * **Portfolio committees** ✓: Portfolio Committees are responsible for monitoring their respective departments ✓✓. They report to Parliament. ✓✓

2. Assessing needs ✓

Government must ensure that citizens are able to satisfy their basic needs✓✓.
It must use various social security systems in order to improve the welfare of its citizens✓✓.
However, it must first assess the needs of its people to determine who qualifies for state assistance✓✓. A number of institutions are used to collect information including census statistics provided by Statistics South Africa, hospitals, schools etc. ✓✓

3. Efficiency ✓

Government should provide public goods in the most efficient manner✓✓. Public goods should be provided in such a way that the Pareto efficiency is achieved✓✓ Instruments that can be used to measure efficiency:

- * **Bureaucracy**✓: . While government officials must follow rules and procedures, that should not compromise efficiency ✓✓
- * **Incompetence**✓: Government officials should get the necessary education and training in order to perform their functions efficiently ✓✓
- * **Corruption**✓: Government is faced with a problem of corruption among its officials ✓✓. Officials have a tendency of misusing their position in government to enrich themselves✓✓. Strict policies should be put in place to prevent fraud and corruption. ✓✓

4. Pricing policy ✓

In the private sector motive of the entrepreneur is to make the maximum profit✓✓.
The aim of government provisioning is achieve social, economic and political objectives✓✓.
It is therefore not guided by profit maximisation but by social responsibility. ✓✓
Public goods are non-excludable and non-rival in nature✓✓.
Non-excludable goods benefit every citizen without paying for them✓✓ e.g. street light, defence✓.
Non-rival goods are goods that do diminish as a person consumes them✓✓ e.g. street lights✓. Private sector is not prepared to provide such goods✓✓ and must therefore be provided by government✓✓.

Government may use various pricing systems:

- * **Free-of-charge services**✓: Services such as defence, police etc. are provided free of charge ✓✓.
- * **User-charges**✓: . A person is charged for using a service ✓✓ e.g. toll fees ✓.
- * **Economic reasons**✓ such as services like water and electricity ✓✓ that have a zero price political
- * **Direct and indirect subsidies**✓. Direct subsidies are used to cover part of the costs ✓✓ (e.g.) urban bus service and an indirect subsidy is used to write off accumulated losses or deficits ✓✓
- * **Standing charges**✓ called availability charges (eg.) water and electricity ✓✓ standing charges goes to meet fixed costs and the price per unit consumed covers variable costs ✓✓
- * **Price discrimination**✓ different users have different needs for a good ✓✓ (e.g.) commercial and manufacturing businesses pay higher rates than households ✓

5. **Parastatals** ✓ state-owned enterprises ✓✓ that either render a service or when an existing enterprise is nationalised ✓✓ They focus on making a profit and maximizing cost at the expense of the needs of some groups ✓✓ (e.g.) Iscor ✓✓ SABC, SAA, Spoornet ✓✓
6. **Privatisation** ✓ refers to the process whereby state-owned enterprises and state-owned assets are handed over or sold to the private individuals ✓✓ Nationalisation is the process whereby the state takes control and ownership of privately owned assets and private enterprises ✓✓. It includes contracting of services, Public-Private Partnerships, deregulation, increasing competitiveness ✓✓
- Max 8 marks for headings (1mark each)** (Discussion max 26)

ADDITIONAL PART

Use the Laffer curve to explain the incentive to work.

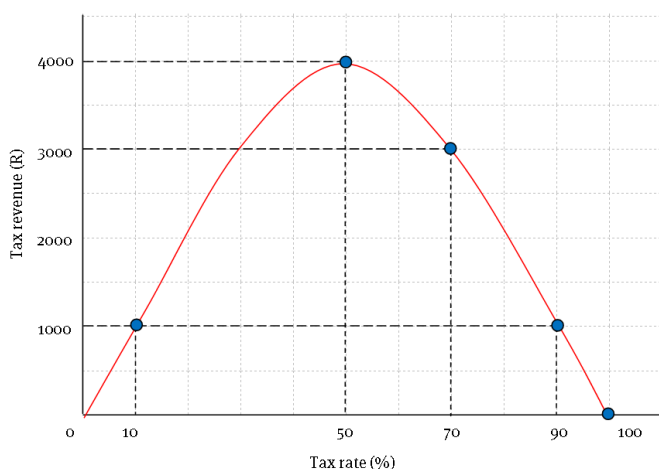


FIGURE 1.16 The Laffer curve

Fiscal policy impacts the labour market by encouraging or discouraging productivity ✓✓. A very high tax rate reduces people's willingness to work ✓✓. If people know that they will be charged more tax if they earn more, they will be discouraged to exert themselves more ✓✓. This reduces both the productivity and the total tax revenue ✓✓.

The Laffer curve is a graph which shows the relationship between government revenue raised through taxation and the tax rate ✓✓. On the graph above, if the tax rate is 0%, the revenue that the government collects is zero ✓✓. As the tax rate increases from 0% to 10%, the tax revenue increases to R1000 ✓✓. A further increase of the tax rate to 50% yields a tax return of R4000 ✓✓. This is the maximum ✓✓ tax rate that can be charged because a further increase in the tax rate after this point causes a decline in total tax revenue ✓✓. If the tax rate increases to 80%, many people get discouraged and work less or even stop working ✓✓. At 100% tax rate, no one is working ✓✓.

Mark allocation for additional part

Graph: 2 for shape, 2 for scale =	4
Discussion	6
Total	10

(Body max)

CONCLUSION

(36)

(Any relevant conclusion)

(2)
[40]

QUESTION 5

“In the spirit of globalisation, it is essential that countries of the world interact with one another on an on-going basis.”

- Discuss the supply reasons for international trade. (30)
- Briefly advise the Minister of Trade and Industry how he can use exchange rates to correct the balance of payments disequilibrium. (10)

INTRODUCTION

(Any suitable introduction)

Eg. Definition of international trade.

(2)

SUPPLY REASONS

a) Natural resources: ✓

- Natural resources are unevenly distributed over the face of the earth. ✓✓
- Countries that lack certain resources will have to get them from countries that have an abundant supply. ✓✓
- South Africa's gold and diamond resources, for example, have given us an advantage in producing gold and diamonds and have enabled us to produce these goods more cheaply. ✓✓
- We therefore export gold and diamonds, but import crude oil, for example. ✓

b) Climatic conditions: ✓

- Differences in climatic conditions between countries make it possible for some countries to produce certain goods at lower prices than other countries. ✓✓
- Example, climatic conditions in Brazil make it possible for Brazilian farmers to produce coffee beans at a lower price than other countries. They therefore, export coffee to the rest of the world. ✓✓
- South Africa exports meat to Europe and imports wood from Scandinavia. ✓✓

c) Labour resources: ✓

- The quantity, quality and cost of labour also differ between countries. ✓✓
- Countries that have skilled labour have high productivity rates and are able to produce certain goods at a lower price than other countries. ✓✓
- In Malaysia, the supply of labour is very high, but the cost of labour is low. This enables Malaysia to produce certain goods that have labour intensive production, at comparatively lower prices ✓✓.

d) Technology: ✓

- Some countries have access to technological resources that enable them to produce certain goods at lower prices. ✓✓
- Production processes, the availability of equipment and machinery influence the supply of goods and these contribute to cost differences between countries. ✓✓

e) Specialisation/Mass production✓

- Some countries specialize in the production of goods and services and are able to produce certain goods at lower prices than other countries. ✓✓
- Example, Japan has specialized in the production of certain electronic equipment. They are able to mass produce electronic goods and sell them at lower prices than other countries. ✓✓

f) Capital ✓ is not always easily obtained in every country. Developed countries usually enjoy an advantage over underdeveloped countries ✓✓. Due to lack of capital, countries cannot produce all products they wish to produce ✓. Underdeveloped countries must import certain goods from developed countries. ✓✓

g) Cost differences (opportunity cost) ✓ Goods and services can be produced at a lower cost in one country than another ✓ Countries find it profitable to trade with each other if they have different opportunity cost structures ✓✓

h) Absolute advantage and comparative advantage ✓. A country that enjoys absolute advantage must produce and export the goods in which it has absolute advantage to other countries. ✓✓ (26)

Max 8 marks for headings (1mark each)

ADDITIONAL PART

Briefly advise the Minister of Trade and Industry how he can use exchange rates to correct the balance of payments disequilibrium.

The Minister can use one or more of three ways to manipulate the exchange rates.

a) Fixed exchange rate system: ✓

- This means that the value of a currency is fixed or pegged. ✓✓
- The government can fix the exchange rate at a certain level and ensures that the exchange rate remains at that level. ✓✓
- The government can buy and sell foreign exchange to maintain the exchange rate at the level it has set. ✓✓
- If there is a deficit the government will sell foreign exchange to maintain its level. ✓✓

(b) Managed floating exchange rate system:

- The exchange rate is allowed to fluctuate between certain limits (set by government) as demand and supply change. ✓✓
- Government intervenes only when the exchange rate moves outside the set limits.
- They do this by buying and selling foreign exchange. ✓✓
- This form of intervention is usually managed by the Reserve bank.
- If there is an increase in the demand for foreign exchange, the authorities must dig into their reserves and supply the required amount of foreign exchange. ✓✓
- This prevents the domestic currency from depreciating. ✓✓
- To prevent the domestic currency from appreciating the authorities must buy back the excess supply of foreign exchange and add it to their reserves. ✓✓

(10)

CONCLUSION

(Any relevant conclusion)

(2)

TOTAL FOR SECTION C [40]

GRAND TOTAL 150