



Province of the
EASTERN CAPE
EDUCATION

ECONOMICS P2
COMMON TEST - JUNE 2014

MEMORANDUM

**NATIONAL
SENIOR CERTIFICATE**

GRADE 12

MARKS : 150

TIME : 1½ Hours

This memorandum consists of 10 pages

SECTION A (COMPULSORY)**QUESTION 1****1.1 Multiple choice items**

- 1.1.1 B price-maker.✓✓
- 1.1.2 A zero economic.✓✓
- 1.1.3 C oligopoly.✓✓
- 1.1.4 B economic✓✓
- 1.1.5 C average✓✓
- 1.1.6 B free.✓✓
- 1.1.7 C both rival and excludable.✓✓
- 1.1.8 A unique.✓✓

(8 x 2) (16)

1.2 Choose from columns

- 1.2.1 D✓
- 1.2.2 F✓
- 1.2.3 G✓
- 1.2.4 B✓
- 1.2.5 A✓
- 1.2.6 C✓
- 1.2.7 H✓
- 1.2.8 E✓

(8 x 1) (8)

1.3 Concepts

- 1.3.1 social benefits✓
- 1.3.2 industry✓
- 1.3.3 equilibrium price✓
- 1.3.4 breakeven point✓
- 1.3.5 patent✓
- 1.3.6 variable costs

(6 x 1) (6)

[30]

SECTION B**QUESTION 2****2.1 Answer the following questions appropriately.****2.1.1 Name two kinds of collusion that characterize oligopolies.**

- * overt / explicit collusion✓
- * tacit / implicit collusion✓ (2 x 1) (2)

2.1.2 Why is Eskom regarded as a natural monopoly?

- High development costs prevent others from entering the market and therefore the government supplies the product through Eskom ✓✓
- It costs billions of rands to build and maintain power stations and therefore there are no other suppliers. Government plays a key role ✓✓ (1 x 2) (2)

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

2.2.1 R70✓✓ (2)

2.2.2 A✓✓ (2)

2.2.3 Due to negative slope of demand curve the additional units are bought at lower prices.✓✓ (2)

2.2.4 $(R70 \times 4 = R280) - (R50 \times 4 = 200)✓ = R80✓✓$ OR (4)
 $(R70 - R50 = R20) \times 4✓✓ = R80✓✓$ [10]

2.3 Study the cartoon below and answer the questions that follow

2.3.1 SANRAL/South African National Road Agency Limited✓✓ (2)

2.3.2 Message portrayed by the cartoon.

- * Govt. failure/public sector failure✓✓
- * Confusion caused by mixed messages✓✓
- * Frustration ✓✓
- * Lack of CBA✓✓
- * Any relevant answer

Any 1 x 2 = (2)

2.3.3

- * the cost of construction was very high✓✓
- * the price to the final consumer is high✓✓
- * road-users/consumers/tax payers were not adequately consulted✓✓
- * the effects of the e-tolls on people was not considered✓✓
- * the billing system of the e-tolls is inaccurate✓✓
- * e-tolls are being forced on road-users✓✓

Any 3 x 2 = (6)

(Accept any relevant answer even those that say CBA was taken into account if valid reasons are given.)

[10]

2.4 Outline the ways in which government regulations can create barriers to entry in the monopoly market.

- * **Licences** ✓✓: Government limits entry by requiring businesses to obtain a licence before they enter the market ✓✓.
- * **Patents** ✓✓: Entry is blocked by granting exclusive rights to one firm to operate in the market ✓✓.
- * **Copyrights** ✓✓: The issue of copyrights restricts entry into the market and creates a monopoly ✓✓. (Max 8)
Any 4 x 2 (8)

2.5 How can merit and demerit goods be regarded as a cause of market failure.

- * **Merit goods** ✓✓: These are goods that are desirable in society ✓✓ but the market does not produce them in large quantities ✓✓. Examples are schools, hospitals ✓. Most people cannot afford them because the price is high ✓✓. As a result their provision is taken over by government ✓✓.
- * **Demerit goods** ✓✓: These are goods that are harmful to society ✓✓. The market produces them in large quantities ✓✓ and their price is very low ✓✓. Examples: alcohol, cigarettes ✓. Any relevant answer
(Max: Merit = 4; Demerit = 4)
Any 4 x 2 (8)

[40]**QUESTION 3****3.1 Answer the following questions appropriately.****3.1.1 Name TWO kind of businesses that are monopolistically competitive.**

- Supermarkets
 - Restaurants
 - Fast food outlets
 - Chemists
 - Clothing stores
- (Any relevant answer) (2 x 1) (2)
- Accept examples of businesses in the above categories eg. Spar, OK, Pick & Pay. (supermarkets)**

3.1.2 Explain the concept “*product differentiation*”.

Product differentiation is a strategy whereby the product is made distinct to others. ✓✓ (Any close definition.) (2)

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

- 3.2.1 oligopoly ✓✓ (2)
- 3.2.2 duopoly ✓✓ (2)

- 3.2.3 Use of non-price competition✓✓ e.g.
- Embark on rigorous advertising and marketing campaigns ✓✓
 - Offer loyalty rewards ✓✓
 - Offer after-sales service ✓✓
 - Provide efficient mobile phone service ✓✓
 - Door-to-door sales✓✓
 - Any relevant answer

Any 3 x 2 = (6)

3.3 Study the cartoon below and answer the questions that follow

- 3.3.1 They met to discuss the construction of stadiums/ They colluded✓✓ (2)
- 3.3.2 Collusion can destroy the companies involved✓✓/
Govt. is always on the lookout for price fixing tendencies✓✓ (2)
(Any relevant answer)
- 3.3.3 They can take the matter to the Competition Appeal Court✓✓ (2)
- 3.3.4 There are three competition institutions:
- * **Competition Commission:** It investigates allegations of collusion✓✓
 - * **Competition Tribunal:** It adjudicates cases of anti-competition✓✓
 - * **Competition Appeal Court:** It reconsiders decisions taken by the Tribunal if referred by the aggrieved party✓✓ (4)

3.4 Briefly compare monopoly with perfect competition.

Profit✓✓: The economic profit made in the perfect market is gradually reduced as more firms enter the market✓✓. In the long term the perfect competition makes a normal profit while the monopoly makes the economic profit✓✓. The monopolist makes economic profit both in the short run and the long run.✓✓

Price✓✓: Monopoly charges a higher price than the perfect market.✓✓

Output✓✓: The output produced by the monopolist is lower than the output produced by the perfect market✓✓. If the monopolist increases the output it would depress the price✓✓. Therefore to keep his price he limits the output✓✓.

Efficiency✓✓: The monopolist does not produce at the lowest possible cost✓✓. As a result the community does not get the best deal from the monopolist✓✓.

Any 4 x 2 (8)

3.5 Explain why it is difficult for the oligopolists to compete with the price.

- * It is difficult for oligopolists to fix the price because collusion is illegal✓✓.
- * If they agree to increase the price, other firms may cheat and not change their prices✓✓
- * They must consider the reaction of oligopolists if they change the price✓✓
- * Those that increased the price will lose customers✓✓
- * The quantity sold will decrease✓✓ and the firm will make less profit than before✓✓
- * If they decide to reduce the price, the percentage increase in the quantity is less than the percentage drop in the price✓✓
- * In both cases it is not worthwhile compete with the price✓✓
- * Max 4 for the graph if the learner included the kinked demand curve

Any 4 x 2 (8)
(40)

TOTAL FOR SECTION B: [80]

SECTION C**QUESTION 4**

“Perfect competition is an ideal market structure to which all economies aspire”.

- Discuss the characteristics of a perfect market in detail. (26)
- With the aid of a graph explain why marginal revenue must be equal to marginal cost for profits to be maximised. (10)

Introduction

Any relevant introduction (2)

Body**Number of buyers and sellers✓**

- There are many buyers and sellers✓✓
- Buyers and sellers are so many that no individual buyer or seller can influence the price✓✓
- Each seller or producer has a small market share.✓✓

Control over price✓

- Because the market share is so small, it is impossible for each seller to influence the market price.✓✓
- The price is determined by the interaction of demand and supply✓✓ in the market.
- Each seller is a **price taker** ✓✓
- If the producer tries to increase the price above the market price, customers will buy from another seller.✓✓
- If he charges a price less than the market price, he will run out of stock✓✓

Freedom of entry and exit✓

- Anyone who wants to enter the market is free to do so.✓✓
- Likewise he is free to leave the market any time.✓✓
- There are no restrictions to entry or exit✓✓

Nature of the product✓

- The product is 100% identical✓✓ or homogeneous✓✓.
- Because the product is identical there is no reason for the customer to prefer one seller to the other.✓✓
- He can buy from any seller and still get the same quality product✓✓ at the same price✓✓

Perfect information✓

- All buyers and sellers have complete knowledge of the market conditions✓✓.
- Buyers and sellers have full knowledge about the price✓✓, the availability of the product✓✓, the quality✓✓
- There is no barrier to the knowledge of market conditions.✓✓

Profit✓

- Sellers in the perfect competition make a normal profit.✓✓
- In the beginning they can make an economic profit✓✓ but it attracts other sellers to enter the market✓✓
- The entry of other sellers increases supply and reduces the profit to normal profit✓✓
- There is no one seller that can influence the price.✓✓

No collusion✓

- Collusions happen when sellers or buyers enter into agreements to limit competition in order to influence market price.✓✓
- Collusion can only happen where there are few sellers and buyers✓✓
- In the perfect market sellers act independently of each other✓✓
- As a result they cannot get into agreements that may influence the price✓✓

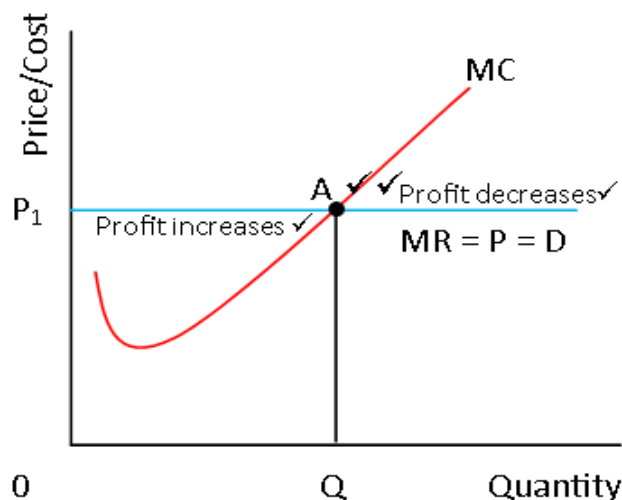
No government intervention✓

- There is no government intervention that can affect buyers or sellers✓✓
- (Any other relevant point)

(26)

Note :Max 8 marks for headings - 1 mark each**ADDITIONAL PART**

- **With the aid of a graph explain why marginal revenue must be equal to marginal cost for profits to be maximised.**
 - * Marginal revenue (MR) is the additional revenue the producer gets by producing one more unit✓✓
 - * The individual producer must produce at a point where marginal revenue is equal to marginal cost ($MR=MC$)✓✓
 - * The profit maximizing point in the graph is A✓✓
 - * In a perfect market the price (P) is the same as MR and the demand (D)✓✓.



- * If the firm is producing a quantity between 0 and Q_1 , MR runs above MC✓✓
- * It is worthwhile for the firm to increase output because at this stage more profits can be obtained by producing more output✓✓.
- * The maximum profit is obtained at point A where $MR = MC$ ✓✓.
- * At any point to the left of A, profit is increasing✓✓.
- * At any point beyond A, MC lies above MR and that reduces profits✓✓.
- * A prudent entrepreneur will not produce beyond A✓✓.
- * Therefore the optimum point of production A where $MR = MC$ ✓✓
- * This point is called the profit maximisation point.✓✓

(Graph 4; Discussion 6)

(10)

Conclusion

(2)

(40)

QUESTION 5

“No matter how perfect the market economy may seem to be, however, it has its own flaws”.

- Discuss the various causes of market failure. (30)
- Explain with the aid of a graph why the government uses price ceilings to correct market failures. (10)

Introduction

(Any relevant introduction) (2)

Body:**1. Existence of externalities✓**

Externalities are the costs and benefits that are not included in the market price. Negative externalities results in goods being overproduced. For example, if a business pollutes the air, people living in surrounding areas may experience health problems✓✓. The community will have a burden of increased health care✓✓ which is not paid for by the firm responsible for pollution. Society desires less of that good✓✓ In the case of positive externalities the market under produces this good . ✓✓

2. Existence of public goods✓

Public goods are consumed by the community as a whole✓✓. It is impossible to exclude some consumers from using the product✓✓. As a result of this non-exclusivity, the private sector is usually unwilling to provide these public goods✓✓. Public goods then have to be provided by government✓✓.

3. Imperfect information✓✓

One condition of perfect competition is that all buyers and sellers should have perfect knowledge of the market conditions✓✓. In reality households and firms do not have access to that kind of knowledge✓✓. This constitutes a condition of market failure✓✓.

4. Imperfect distribution of income and wealth✓

The free market system tends to generate an unequal distribution of income across the population✓✓. The income of consumers determines their access to consumer goods and services✓✓. The higher the income, the more goods and services a consumer can purchase✓✓. The inequality of income and wealth causes people to live unequal standards✓✓.

5. Imperfect competition✓

Competition is often impaired by power struggle in market economies✓✓. Imperfect competition restricts output and raise prices✓✓. They prevent new businesses to enter, prevent full adjustment to changes in demand✓✓. Modern market does not allow for price negotiations✓✓. Advertising promotes producer sovereignty and sway consumers to buy certain products✓✓.

6. Immobility of factors of production✓

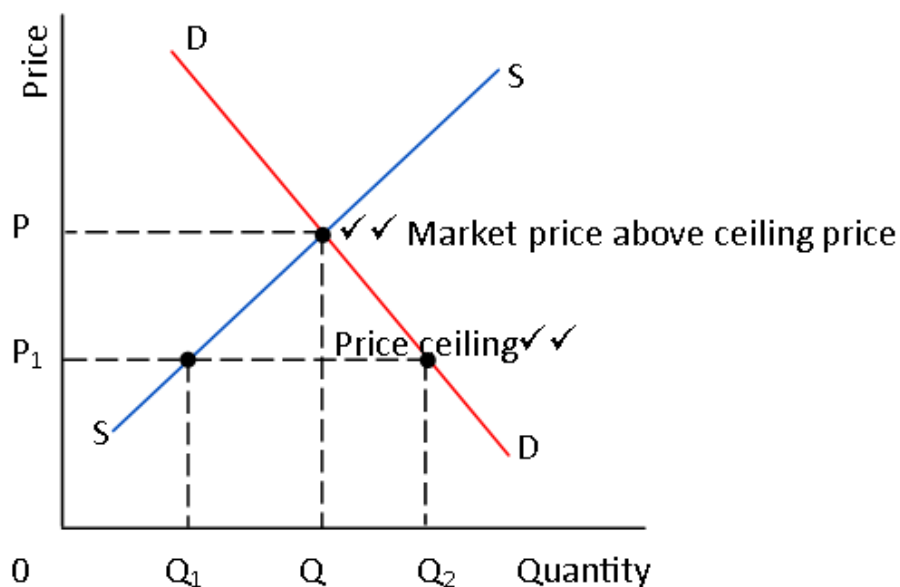
Most markets do not adjust rapidly to changes in supply and demand because resources are not freely mobile✓✓. Labour✓✓ takes time to move occupationally and geographically✓✓. Physical infrastructure like telephone lines takes time to move from one location to another. ✓✓

Max (26)

Note :Max 8 marks for headings - 1 mark each

ADDITIONAL PART

Explain with the aid of a graph why the government uses price ceilings to correct market failures.



- A price ceiling is when the government imposes a maximum price that the producer must charge✓✓.
 - The ceiling price must be below the market price✓✓
 - The aim of a price ceiling is to make the product affordable to a large number of people✓✓
 - The market price in the graph is P✓✓ and the quantity bought and sold is Q✓✓
 - The ceiling price is fixed at P_1 ✓✓ where the quantity supplied is Q_1 ✓✓
 - At this price the quantity demanded is Q_2 ✓✓
 - The product is now accessible to a large number of people than before✓✓
- (Graph 4, Discussion 6) (10)

Conclusion:

Any suitable conclusion

(2)
TOTAL FOR SECTION C: [40]

TOTAL MARKS: 150