2.2.1 Compulsory Part

	Topic	Key Points
A	Basic Economic Concepts	Economics as a social science
		Scarcity, choice and opportunity cost (i) The source of economic problems: scarcity • Unlimited wants and limited resources • Free and economic goods (ii) Choice and opportunity cost • Economic decisions involving choices among alternatives • Concept of cost in economics • Interest as the cost of earlier availability of resources
		The three basic economic problems (i) What to produce? How to produce? For whom to produce? (ii) How society tackles the basic economic problems • By society's customs and traditions • By government decisions • By the market mechanism (N.B. Illustrations by examples only. All theories on types of economic systems NOT required) (iii)Private property rights and its importance in a market economy
		Specialization and exchange • Exchange as a condition for specialization Circular flow of economic activities (i) Consumption of households and production of firms (ii) The relationship among production, income and expenditure
		Positive and normative statements • Distinction between positive statements and normative statements

	Topic	Key Points
B	Firms and Production	Ownership of firms (N.B. Firm as a unit that makes decisions regarding the employment of factors of production and the production of goods and services) (i) Forms of ownership • Public ownership • Private ownership: sole proprietorship, partnership and limited company (N.B. Classification of partnership NOT required) (ii) Limited and unlimited liability (iii)Shares and bonds as sources of capital (N.B. Classification of shares and bonds NOT required)
		Types/stages of production • Primary, secondary and tertiary production and their inter-relationship
		Types of goods and services produced (i) Producer and consumer goods (ii) Private and public goods (N.B. Modelling regarding public goods NOT required)
		Division of labour (i) Types: simple, complex and regional (ii) Advantages and disadvantages (iii)Limitations

	Topic	Key Points
		Factors of production (i) Human resources • Labour: supply, productivity, mobility and different methods of wage payments • Entrepreneurship: risk-bearing and decision-making (ii) Natural resources • Land: supply (iii) Man-made resources • Capital: accumulation and depreciation (iv) The features of (i) to (iii) in Hong Kong
		Production and costs in the short run and long run (i) Definition of short run and long run • In terms of fixed and variable factors of production (ii) Law of diminishing marginal returns • Illustration by total product, average product and marginal product schedules only (iii) Cost of production • Fixed and variable costs • Total, marginal and average cost of production (N.B. General relationship between total, marginal and average cost curves NOT required. Relationship between short run and long run cost curves NOT required) (iv) Economies and diseconomies of scale • Internal economies and diseconomies of scale • External economies and diseconomies of scale (N.B. Economies and diseconomies of scale illustrated by average cost. Further classification of internal and external economies and diseconomies of scale NOT required) (v) Expansion and integration of firms • Types: vertical, horizontal, lateral and conglomerate • Motives

	Topic	Key Points
		The objectives of firms: (i) Profit maximization with given prices and marginal cost schedule • Meaning of profit as the difference between total revenue and total cost • Profit maximizing choice of output for individual firms with given prices and marginal cost schedule • The marginal cost schedule as the supply schedule of individual firms (N.B. Long run supply NOT required) (ii) Other objectives: market share, provision of non-profit making services, corporate social responsibility, etc
C	Market and Price	Law of Demand
		Individual demand (i) Factors affecting individual demand (ii) Complements and substitutes, superior and inferior goods (N.B. Giffen goods NOT required) (iii) Individual demand schedule and importance of the *ceteris paribus* assumption (iv) Difference between change in quantity demanded and change in demand
		Market demand (i) Horizontal summation of individual demand curves (ii) Factors affecting market demand
		Individual supply (i) Factors affecting individual supply (ii) Individual supply schedule and importance of the *ceteris paribus* assumption (iii) Difference between change in quantity supplied and change in supply

	Topic	Key Points
		Market supply (i) Horizontal summation of individual supply curves (ii) Factors affecting market supply
		Interaction between demand, supply and price (i) Definition of equilibrium: no tendency to change (ii) Equilibrium price and quantity (iii) Effects of change in demand and/or change in supply on equilibrium price and quantity
		Consumer and producer surplus (i) Marginal benefit to consumers, willingness to pay, consumer surplus, demand curve and their relationship (ii) Marginal cost of firms, minimum supply-price, producer surplus, supply curve and their relationship (iii) Illustrate consumer surplus and producer surplus in a demand-supply diagram (N.B. Concepts of utility, marginal rate of substitution, and indifference curves NOT required)
		Functions of prices (i) Rationing function: existing supplies are distributed to users with highest value (ii) Allocative function: • Demand is derived from marginal benefit, and supply is derived from marginal cost; the interaction between demand and supply then determines price and resources allocation • Changes in relative prices and resource deployment (N.B. Graphical analysis NOT required)
		Price elasticity of demand (i) Arc elasticity (N.B. Point elasticity, cross elasticity and income elasticity NOT required) (ii) Relationship between price elasticity and total revenue (iii) Factors affecting price elasticity of demand