

7.3 Output profit and loss

7.3.1 Revenue

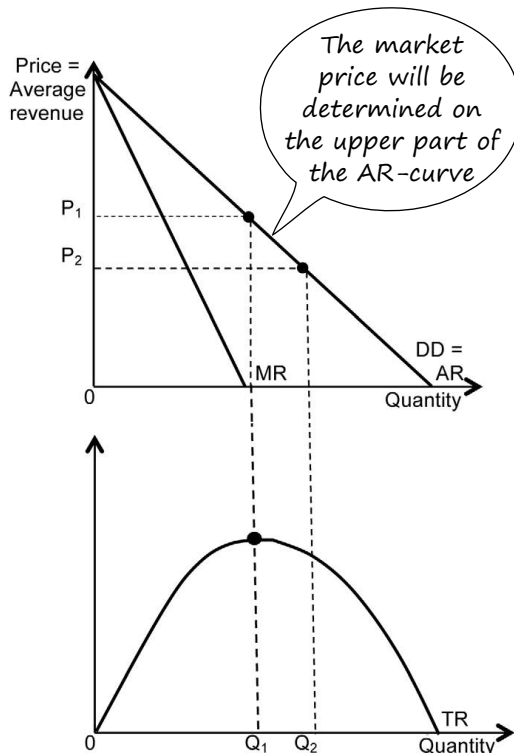


Figure 7.1 Revenue curves of the individual producer

- The **demand curve** for a monopolist is the market demand curve and slopes downwards from left to right (DD/AR). See the top graph in **Figure 7.1**.
- Any point on the curve is an indication of the **quantity** of the product to be sold and the **price** at which trade takes place.
- Any price-quantity combination on the demand curve is also its average revenue (AR) curve.
- The average revenue from each product is calculated by dividing the total revenue by the quantity = the price. See the bottom graph in **Figure 7.1** (left).
- The **marginal revenue** (MR) curve runs below the **demand curve** (AR) – it always intersects the horizontal axis at a point halfway between the origin and the point of intersection of the demand curve (AR).
- The monopolist will try to **fix the price above the centre of the demand curve**, because only then will his total revenue increase. See **Figure 7.1**. Note how at Q_1 total revenue is at its highest. Q_1 intersects the demand curve of the top graph above the centre of the curve.

7.3.2 Economic profit in the short term



Step 1: Draw your two axes

First, draw your TWO axes: Price (vertical) and Quantity (horizontal) – remember, they meet at the origin (0). Everything counts for marks – do not leave out anything. Now go to step 2.



Figure 7.2



Step 2:

The two revenue

curves start on the price axis and move down to meet the **quantity axis**. Draw these axes now. Then go to step 3.

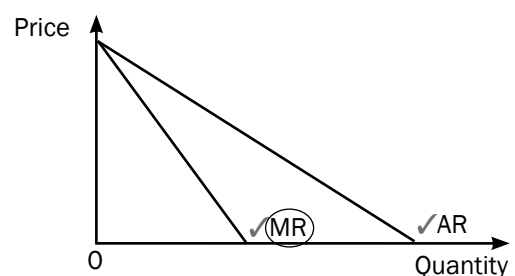


Figure 7.3



It is easy to draw a graph – **YOU MUST JUST KNOW HOW.**

Practise makes perfect.



Step 3:

This MC curve intersects the AC curve **at the minimum point of the AC curve**.

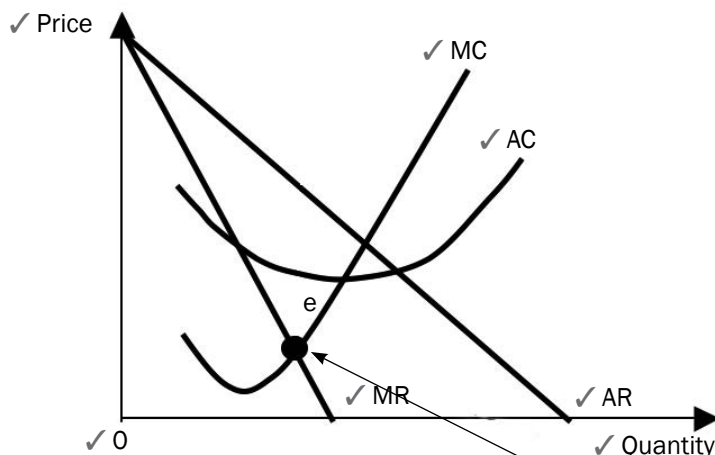


Figure 7.4



Step 4:

The most important point on the graph is where **MC = MR** (look for the dot •). At this point: equilibrium/maximum profit/profit maximisation is reached (all the

same point).



Step 5:

This **dot** is extended upwards and downwards. Your **cost** occurs where it meets the AC curve, and your **market price** occurs where it meets the AR curve (demand curve). Remember, a monopoly company will determine the price.

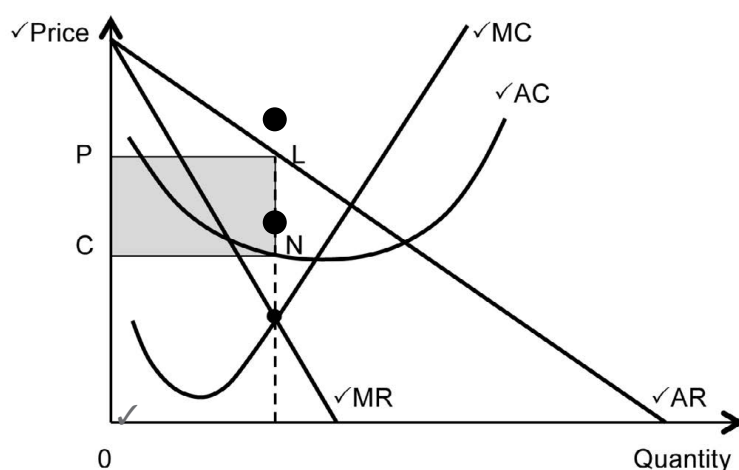


Figure 7.5

Notice how the marginal cost curve is in the shape of a tick.



Practise drawing steps 1 to 5. Draw these over and over until you do not make any mistakes. In this way you will be able to draw the economic profit made by a monopoly.



The graph below shows the economic profit made by a monopoly:

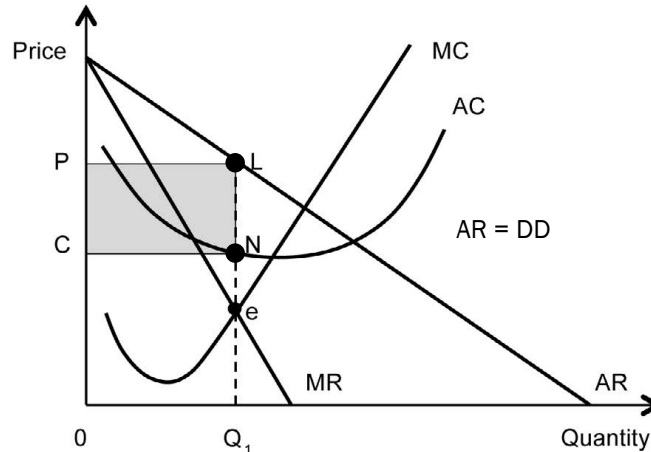


Figure 7.6: The economic profit made by a monopoly

- The cost structure of the monopoly is the same as that of competitive businesses.
- Determine the point where $MC = MR$, the point where the production cost of the last unit is equal to the revenue it earns (point e) – profit-maximising production quantity of Q_1 on the horizontal axis.
- To determine the price at which Q_1 is sold, move vertically upwards from e to L on the demand curve. The market price is therefore determined at P.
- Total revenue is greater than the short-term total costs. The monopolist makes a profit (due to demand and cost of production).

7.3.3 Economic loss in the short term

When you draw the economic loss for the monopolist, the graph stays the same, EXCEPT the AC curve moves to the right - up, and totally misses the AR (demand) curve (see Figure 7.7).

Remember: To draw the economic loss, you find the market price (OP) where the dotted line meets AR. Then extend the line further to meet the AC curve – THAT indicates your cost (OC).

The **total income** = Price (OP) \times Quantity (OQ) = the area OPNQ

The **total cost** = Cost (OC) \times Quantity (OQ) = the area OCLQ.

Economic loss = income – cost

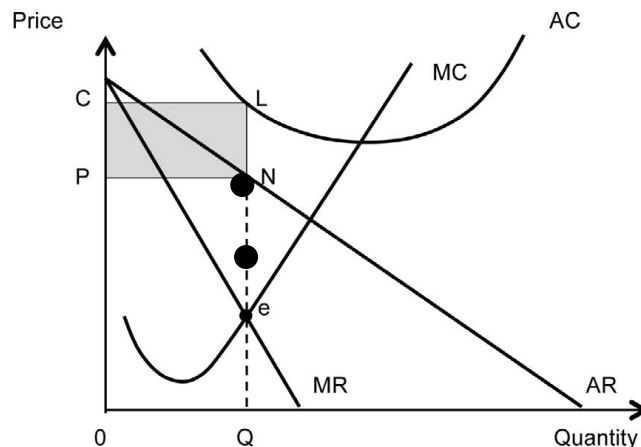


Figure 7.7: The economic loss of the monopoly

Practise drawing the economic loss of the monopoly over and over again until you do not make any mistakes.

Learn the following THREE bullets as a description for the economic loss of a monopoly:

- The monopoly suffers short-term losses when the AC curve lies above the demand curve (DD).
- Equilibrium is reached where $MR = MC$ (a loss-minimising situation).
- The monopoly will produce a quantity Q and sell at price P . The total costs are the area $OCLQ$; the total revenue is the area $OPNQ$. The loss will be that part that is shaded (the area $PCLN$).

7.3.4 Comparison of a monopoly and a perfect market

Monopoly	Perfect market
1. Downward sloping DD curve MR curve lies below the DD curve	Horizontal DD curve MR curve same as DD curve
2. Price setter (maker)	Price-taker
3. Individual business is the industry	Individual businesses add up to make the industry
4. Consumer buys less if the selling price is high (and vice versa)	Business can't choose its price and if it sells at a different price it loses out
5. Monopolist produces a lower output at higher prices and in so doing produces at sub-efficient quantities. It does not produce at the minimum point of the LAC curve	Larger output and lower prices. Economically efficient quantities produced. Produces on the lowest point on the AC curve
6. Producer and consumer surpluses are smaller	Surpluses bigger
7. Products differentiated – unique – no close substitutes	Product are homogenous
8. Long-term: can make economic profit	Only normal profit in the long-term



7.4 Oligopolies

An oligopoly exists when a small number of large companies are able to influence the supply of a product or service to a market. By controlling the supply of the product or service on the market, oligopolies aim to keep its prices and profits high. Oil companies are one of the best examples of an oligopoly. A special type of this market form is a duopoly – an industry with only two producers.

7.4.1 Characteristics of oligopolies

- There is **limited competition**. Only a few suppliers manufacture the same product.
- Products may be **homogenous or differentiated**.

- This market is characterised by **mutual dependence**. The decision of one company will influence and will be influenced by the decisions of the other companies.
- Oligopolies can **frequently change their prices** in order to increase their market share. However this can result in a price war.
- Extensive use is made **non-price measures** to increase market share e.g. advertising, efficient service or product differentiation.
- Producers have **considerable control over the price** of their products although not as much as in a monopoly.
- If oligopolies operate as a cartel, firms have an **absolute cost advantage** over the rest of the competitors in the industry. **Abnormal high profits** may be a result of joint decisions in an oligopoly.
- **Entry** is not easy in an oligopolistic market. This is due to brand loyalty and it also requires a large capital outlay.

7.4.2 Kinked demand curve for the oligopolist

- One theory devised by an American economist, Paul Sweezy, can be used to determine the oligopolist's demand curve.
- An oligopolist faces a kinked demand curve. This demand curve consists of two sections.
- The top section, the section that relates to high prices is a very elastic slope (i.e. demand is very sensitive to a price change.)
- The bottom section, the section that relates to lower prices is very inelastic (i.e. demand is not sensitive to a price change).
- To understand the demand curve of an oligopolist, view the graph below.

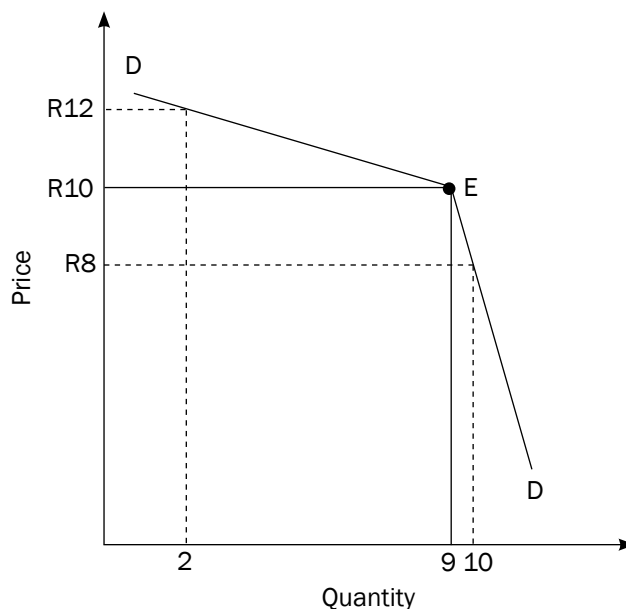


Figure 7.8: The kinked demand curve of the oligopolist

- Suppose the oligopolist is selling at the original/present price of R10 and 9 units of output are sold. Total revenue is $R10 \times 9 = R90$
- If the firm tries to increase profit by increasing the price by R2 to R12, quantity demanded would fall to 2 units and total revenue would decrease to R24 ($R12 \times 2$).
- If the firm tries to increase profit by reducing the price by R2 to R8

and increasing its total sales, total revenue would be R80.

- The oligopolist is therefore faced with a difficult decision because in both instances it will not benefit.
- Increasing the price of goods or reducing the price to increase sales will not lead to greater revenue earned.

7.4.3 Non-price competition

- Oligopoly firms are reluctant to change prices because a price war will drive prices down and profits will be eliminated.
- They make use of non-price measures to attract customers and increase their market share.
- An important aspect of non-price competition is **to build brand loyalty, product recognition and product differentiation**.
- This is done by means of advertising and marketing. As a result, oligopoly firms tend to spend a substantial amount of money on this.

Other forms of non-price competition include:

- extended shopping and business hours
- doing business over the internet
- after-sales services
- offering additional services
- loyalty rewards for customers
- door-to-door deliveries

Examples of firms that use kinds of non-price strategies are those in petrol retailing such as Shell, BP and Caltex and in the banking sector such as ABSA, FNB etc.

7.4.4 Collusion

Collusion takes place when rival firms cooperate by raising prices and by restricting production in order to maximise their profits. When there is a formal agreement between firms to collude it is called a **cartel**. A cartel is a group of producers whose goal is to form a collective monopoly in order to fix prices and limit supply and competition.

In general, cartels are economically unstable because there is a great incentive for members not to stick to the agreement, to cheat by cutting prices illegally and to sell more than the quotas set by the cartel. Although there is an incentive to collude there is also an incentive to compete. This has caused many cartels to be unsuccessful in the long term. Some well known cartels are the Organisation of Petroleum Exporting Countries (OPEC) and De Beers diamonds in South Africa.

Overt/Formal collusion e.g. cartels are generally forbidden by law in most countries. However, they continue to exist nationally and internationally.

Sometimes in an oligopoly market, a dominant firm will increase the price of a product in the hope that its rivals will see this as a signal to do the same. This is referred to as **price leadership** and is an example of a **tacit collusion**.

7.5 Monopolistic competition

7.5.1 Characteristics of monopolistic competition

- The **products are differentiated**. Products are similar but not identical. They are similar in that they satisfy the same need of the consumer. There may be differences in packaging but the product is the same. e.g. sugar and salt.
- Differentiated products create opportunities for **non-price competition** e.g. advertising.
- Monopolistic competition displays a **hybrid structure**. It is a combination of competition and a monopoly.
- There **are many sellers**. This indicates the element of competition.
- **Entry** into the market is **easy**.
- Businesses have **little control over the price** of the product. Each business sells at its own price since a single price cannot be determined for the differentiated product because a range of prices could apply.
- **Information** for buyers and sellers is **incomplete**.
- **Collusion is not possible** under monopolistic competition.
- Restaurants, plumbers, lawyers, insurance brokers, hairdressers, funeral parlours and estate agents are all examples of monopolistic competitors.

7.5.2 Non-price competition

- Differentiated products create opportunities for **non-price competition** i.e. competition is not based on prices but rather on factors relating to the product's uniqueness.
- Advertising campaigns and further product differentiation are powerful forms of non-price competition.
- The greater the product differentiation the less price elastic the demand for the product will be.
- Large sums of money are spent on research, development and advertising to build a loyal consumer group.
- Therefore **brands** play a significant role in determining customer loyalty where a consumer may choose one producer over another. Large chain stores e.g. Checkers, Spar etc. have their own brands for some products. Most of these products are exactly the same as known brands.

7.5.3 Prices and production levels in the short-term and long-term

- The demand curve for a monopolistic competitor is similar to that of a monopolist.
- Short term equilibrium (economic profit and economic loss) corresponds with a monopoly, but the demand curve is more price elastic (flatter) due to good substitutes.

See non-price competition for oligopolies on page 109. Some forms are similar for monopolistic competition. Make sure you can draw the graphs for the monopolistic competitor.



- Long-term equilibrium is characterised by normal profit, due to the ease of entry and exit into the market (similar to a perfect market). The economic profit made in the short-term attracts more businesses to enter the market.

7.5.4 Comparison of monopolistic competition with perfect competition

- Both firms make normal profit in the long run. Therefore there is no difference in the long-run between the perfect market and the monopolistic market as far as profit is concerned.
- The equilibrium price is higher than in a perfect market. The consumer therefore pays less in the perfect market and more in the monopolistic market.
- The monopolistic competitor does not produce at the minimum of the LAC whereas the perfect competitor does. He is less efficient.
- The perfect competitor produces more at a lower price while the monopolistic competitor produces less at a higher price.

7.6 Summary of market structures

	Firm	Perfect Competition	Monopolistic Competition	Oligopoly	Monopoly
A	Number of firms	Many	Large numbers	Very few	One
B	Entry into market	Completely free/unrestricted	Free/Unrestricted	Free but not easy Varies from free to restricted	Restricted or completely blocked
C	Nature of product	Homogenous/Identical	Differentiated	Homogenous/Differentiated	Unique (with no substitute)
D	Demand Curve	Horizontal – firm price taker	Downward sloping but relatively elastic	Downward sloping Kinked (relatively inelastic and elastic)	Downward sloping (INELASTIC) Equals the market demand curve
E	Market information (Knowledge of market conditions)	Perfect knowledge i.e. Complete	Incomplete	Incomplete	Perfect knowledge i.e. Complete
F	Control over market price	No control Price taker	Limited/some control	Substantial control but not price setters	Complete control Price setter/makers
G	Profit/Loss	Short-run = economic profit/loss Long-run = Normal profit	Short-run = economic profit/loss Long-run = Normal profit	Economic profit in the long-run	Economic profit in short-run and long-run

H	Decision-making	Decision has no influence on others	Influenced by other competitors	Influenced by other competitors	Independent
I	Examples	Fresh produce	Restaurants	Petrol, Oil	Water & electricity supply (Eskom)
J	Collusion	Not possible	Not possible	Possible	Not relevant
K	Technical efficiency	Yes	Close	Possible	Possible
L	Allocative efficiency	Yes	Close	No	No



Activity 2

Complete the following table by filling in the missing information:

Characteristics	Perfect market	Monopolistic competition	Oligopoly	Monopoly
	So many competitors that a single business cannot influence the market price		So few competitors that each business takes the actions of the others into account	
Market entry	Completely free	Free		
			Downward sloping	
Long-term economic profit			Positive	
Seller market power				
Control over price		Some control		Considerably more than oligopoly
Examples		Fast-food outlets		Eskom

[20]

Answer to activity 2

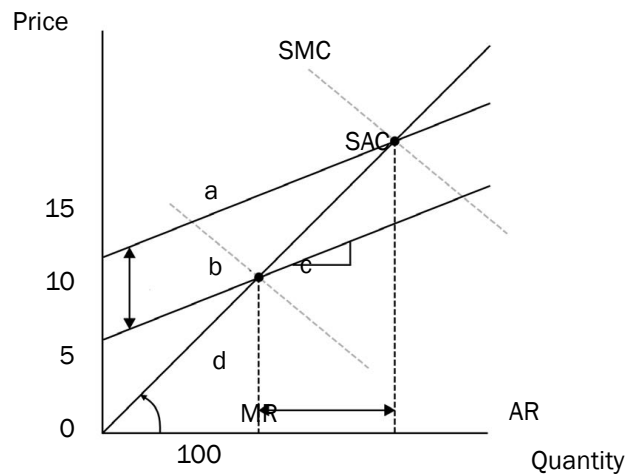
Characteristics	Perfect market	Monopolistic competition	Oligopoly	Monopoly
Number of businesses✓	So many competitors that a single business cannot influence the market price	A very large number✓	So few competitors that each business takes the actions of the others into account	One business✓
Market entry	Completely free	Free	Free to restricted✓	Blocked✓
Demand curve✓	Slopes from left to right✓	Downward sloping✓	Downward sloping	Downward sloping = market demand✓
Long term economic profit	Normal profit✓	Normal profit✓	Positive	Positive✓
Seller market power	None, price-taker✓	Some✓	A whole lot✓	Many (price-maker)✓
Control over price	None✓	Few	Considerable✓	Considerably more than oligopoly
Examples	Gold and oil✓	Fast-food outlets	Petrol and oil✓	Eskom

[20]



Activity 3

Study the following graph and answer the questions that follow:



1. Define the term imperfect market. (2)
2. Motivate why the above graph indicates short-term equilibrium. (4)
3. Which point on the graph indicates profit maximisation? (2)
4. Calculate the economic profit. (6)

[14]

Answers to activity 3

1. An imperfect market occurs where the market price is not a pure reflection of the scarcity of that product. ✓✓ (2)
2. The firm is producing where $SMC = MR$ and is therefore in equilibrium in the short term. ✓✓✓✓ (4)
The slope of the curves indicates a short run. ✓✓
3. d where $MR = MC$ ✓✓ (2)
4. Income = Price (15) × Quantity (100) ✓
= R1 500 ✓
Cost = Cost (10) × Quantity (100) ✓
= R1 000 ✓
Economic profit = Income (R1 500) – Cost (R1 000)
= R500 ✓✓ (6)


[14]



The reasons for and consequences of market failures

Markets can fail for many reasons. The reasons for, and consequences of, **market failure** are explained in this Topic.

Overview

TOPIC	CONTENT	SCOPE AND DEPTH OF EXAMINABLE CONTENT
8. Dynamics of markets: Market failures	<p>Explain the reasons for and consequences of market failures, reflecting on the cost-benefit analysis</p> <ul style="list-style-type: none"> • The causes of market failures <ul style="list-style-type: none"> – Externalities <ul style="list-style-type: none"> – Private cost – Private benefits – Social cost – Social benefits – Missing markets <ul style="list-style-type: none"> – Community goods – Collective goods – Public goods – Merit and demerit goods – Imperfect competition – Lack of information <ul style="list-style-type: none"> – Consumers – Workers – Entrepreneurs – Immobility of factors of production <ul style="list-style-type: none"> – Labour – Physical Capital – Technological change – Imperfect distribution of income and wealth • Consequences of market failures <ul style="list-style-type: none"> – Inefficiencies (Refer to Pareto efficiency) <ul style="list-style-type: none"> – Productive inefficiency – Allocative inefficiency – Externalities <ul style="list-style-type: none"> – Negative externalities – Positive externalities – State Intervention – Rules and regulations <ul style="list-style-type: none"> – Direct control – Imperfect markets – Minimum wages – Maximum prices – Minimum prices 	<ul style="list-style-type: none"> • Discuss the causes of market failures in detail <p>HOT QUESTION: Draw a fully labelled graph to demonstrate the basic elements of the concept externalities</p> <p>HOT QUESTION: Why do governments produce goods and services themselves?</p> <div data-bbox="954 869 1423 1003">  <p>It is important to explain how these causes relate to market failure.</p> </div> <ul style="list-style-type: none"> • Discuss the consequences of market failure in detail • Illustrate productive and allocative inefficiency with the aid of a production possibility curve (refer to Pareto efficiency) <p>HOT QUESTION: Draw two graphs to demonstrate negative and positive elements in the concept “externalities”</p> <ul style="list-style-type: none"> • Illustrate with the aid of graphs

	<ul style="list-style-type: none"> – Taxes and Subsidies <ul style="list-style-type: none"> – The price mechanism – Subsidies on goods and services – Redistribution of wealth – Government involvement in production <ul style="list-style-type: none"> • Cost-benefit analysis <ul style="list-style-type: none"> – Description/Definition – Reasons for a CBA – Applications/examples in South Africa 	<ul style="list-style-type: none"> • Define/explain the concept • Briefly discuss the rationale/reasons • Emphasise and highlight good practical examples • Apply by graphical or numerical illustration <p>HOT QUESTION: Present a case for the use of CBA in practice</p>
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8.1 Key concepts

These definitions will help you understand the meaning of key Economics concepts that are used in this study guide. Understand these concepts well.

TERM	DEFINITION
Allocative Inefficiency	When resources are not allocated in the right proportions and the product mix does not match consumers' tastes. It is possible to reallocate resources to make one person better off while not making someone else worse off
Allocative/Pareto Efficiency	Occurs when resources cannot be readjusted to make one consumer better off without making another consumer worse off. There is zero opportunity cost
Black market	An illegal market in which illegal goods are bought and sold or illegal prices are charged
Cost-Benefit Analysis	An analysis done by government which weighs the costs and benefits of a project to determine whether it should be carried out
Demerit Goods	Goods that are seen to be socially harmful e.g. cigarettes, gambling
Externalities	Costs or benefits to third parties which are not included in the market price of a good
Market Failure	When the forces of demand and supply fail to allocate resources efficiently
Maximum Price/ Price Ceiling	A price set below the equilibrium price/market price to make goods affordable
Merit Goods	Goods that are so beneficial to society that every individual should consume them irrespective of their income e.g. health care, education
Minimum Price/ Price Floor	A price set above the equilibrium price/market price to allow producers to make a fair profit
Minimum Wage	A wage rate set by the government, below which no employer can pay their workers. It is set above the equilibrium wage rate
Negative Externalities	A cost to a third party which is not included in a market price of a good. It is a difference between social cost and private cost. E.g. the harmful effect of a product e.g. pollution
Non-Excludable Goods	Goods whereby individuals can benefit even if they do not pay for it e.g. the television or the police force
Non-Rival Goods	Goods when consumed by one person will not reduce the consumption by another individual e.g. street lights
Positive Externalities	The benefit gained by a third party which is not included in the market price
Private Benefit	The gain a consumer gets from the use of a goods or the gain a producer gets from the sale of a product. E.g. The joy gained by a consumer from driving a car
Private Cost	The actual cost paid by a consumer when a good is purchased. E.g. R150 000 for a car
Producer Subsidies	A cash allowance given to a producer to lower the cost of production and allow more goods to be supplied at a lower price
Productive/ Technical Inefficiency	When resources are not used appropriately to produce the maximum number of goods at the lowest cost and best quality
Public Works Programme	A government initiative aimed at reducing poverty by creating temporary jobs in areas of infrastructure and other areas
SABS – South African Bureau Of Standards	An institute that monitors the quality of goods in South Africa
Social Benefit	The benefit gained by society from the use of a good or service. E.g. taxpayers pay for the maintenance of roads, society will benefit from fewer accidents. It is calculated by adding the private benefit and external benefit
Social Cost	The cost of a good or service which is paid by society. It is calculated by adding the private cost and external cost. E.g. the air pollution caused by cars, will affect people's health bills

8.2 The reasons for market failures

There are many reasons for **market failure**. These include:

8.2.1 Externalities

Externalities are costs not included in the pricing of goods/services, and consequently there is a difference between the **private costs/benefits** and the **social costs/benefits** of production.

- **Private costs:** the cost of producing the good or service which translates into the prices that consumers pay. Also called internal costs.
- **Private benefits:** Internal benefits that accrue to those who produce goods and buy these goods, e.g. producing a bicycle (for producer) and using the bicycle (consumer).
- **Social costs:** these are total costs incurred by society as a whole. For example the social cost of electricity includes the cost of capital, labour, inputs and the cost of the externalities such as dirty water and air. Social cost = private costs plus external costs.
- **Social benefits:** this includes the total benefit experienced by society as a whole. For example, municipalities provide clean water to society which results in fewer illnesses. Social benefits = private benefits plus external benefits.

Negative externalities are things like pollution, tobacco smoking and alcohol abuse. The costs of negative externalities are paid by society rather than by the producers. For example, Styvesant produces cigarettes, many illnesses are related to smoking. The treatment for these illnesses is paid for by society.

Positive externalities are the positive effects of products to third parties which are not paid for.

Negative externalities are often over-produced while positive externalities are under-produced. This leads to market failure.

8.2.2 Missing markets

Markets are incomplete because they cannot meet the demand for certain goods.

Public goods (community and collective goods) are in high demand but are not supplied by the market because of the low profit gained from them and the high cost of capital needed to supply them. Since private producers cannot withhold these goods for non-payment, they are reluctant to provide these goods. The government thus provides these goods and services.

Public goods

This includes community and collective goods and has two features:

- **Non-rivalry:** Consumption by one person does not reduce consumption by another individual, e.g. a lighthouse.
- **Non-excludability:** Consumption can't be confined to those who pay for it (free riders can use them), e.g. radio and television.



Learn these six reasons for market failure.

When you buy a product in a polystyrene container, this gives rise to a negative externality – pollution! This is a form of market failure.



In addition

- **Social benefits outstrip private benefits:** e.g. health care and education.
- **Non-rejectability:** Individuals are not able to abstain from consumption, e.g. street lighting.
- **Continuous consumption.** E.g. traffic lights.

Community goods

These are goods such as, defence, police services, prison services, street lighting, flood control, storm water drainage and lighthouses.

Collective goods

These are goods such as parks, beach facilities, streets. Markets are incomplete and cannot meet the demand for all goods. Government provides public goods, which consist of:

Merit and demerit goods

- **Merit goods:** These are highly desirable for general welfare, but not highly rated by the market, e.g. health care, education and safety. If people had to pay the market price for them, very little would be consumed. The market fails because the market produces less than the desired quantity.
- **Demerit goods:** These are over-consumed goods, e.g. cigarettes, alcohol and drugs. Thus more of the good is produced than is socially desirable. The government bans or reduces consumption of these products through taxation, and provides information to the population on their harmful effects.

8.2.3 Imperfect competition

- Competition in market economies is limited by the power of certain producers to **prevent** new businesses from entering the market. This is imperfect competition.
- Barriers to entry are created because of advertising, a lack of capital and the controlling of resources.
- The imperfect market doesn't allow for price negotiations.
- Advertising is used to promote producer sovereignty (dominance), which encourages consumers to buy existing products and allows producers to delay new products from entering the market until it is in their own interest (e.g. businesses have had the technology to produce long-life light bulbs for many years but have chosen not to launch them in the market).

8.2.4 Lack of information

Consumers, workers and entrepreneurs do not have the necessary information to make rational decisions. This results in resources not being allocated efficiently.

- **Consumers:** To maximise their benefits, consumers need detailed information about goods and services. Although technology offers this to the consumer, they obviously do not have perfect information.
- **Workers:** Are often unaware of job opportunities.
- **Entrepreneurs:** Lack of information on costs, availability and



productivity of factors of production impacts their effectiveness.

8.2.5 Immobility of factors of production

- Labour takes time to move from one area to another.
- The supply of skilled labour cannot be increased because of the time it takes to be trained or educated.
- Physical capital, like factory buildings or infrastructure such as telephone lines cannot be reallocated easily.
- Structural changes like a change from producing plastic packets to paper packets or shifting from labour-intensive production to computer based production requires a change in labourers' skills, employment and work patterns. This takes time to change.

8.2.6 Imperfect distribution of income and wealth

- **Income distribution:** The market system is neutral on issues of income distribution.
- **Discrimination:** Distorts earnings for women and minority groups, disabled persons and people subject to illness and incapacity.
- The market produces goods and services only for those who can afford it.
- This leads to some people having too many goods while others have too few goods.
- The difference in income occurs because there is a difference in market power, unequal educational opportunities, discrimination and inheritance.



8.3 Consequences/effects of market failures



Learn these four consequences of market failure.

8.3.1 Inefficiencies

Two kinds of inefficiencies are possible:

1. Productive inefficiency/Technical inefficiency

When resources are not used appropriately to produce the maximum number of goods at the lowest cost and best quality.

2. Allocative inefficiency

Allocative inefficiency means that the types/quantities of goods or services produced are not what is best for consumers.

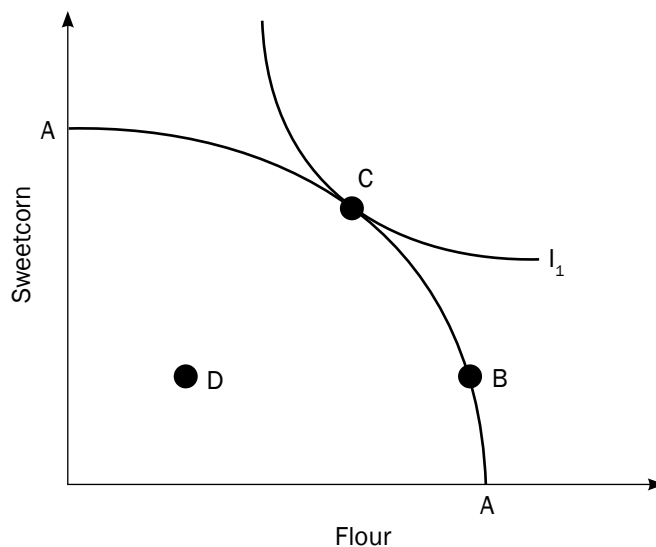


Figure 8.1: Inefficiencies can be described using a production possibility curve

- The Production possibility curve (AA), above, shows a combination of goods that can be produced using all the available resources.
- Any point on the curve shows a combination of goods where resources will be used efficiently.
- Therefore any point on the curve indicates Productive/Technical efficiency.
- The indifference curve (I_1) shows a combination of two goods which gives the consumer the same level of satisfaction. However, if production takes place at point B on the curve, but the demand for goods is actually represented by point C, Allocative inefficiency will occur where the tastes of consumers are not met.
- Any point to the left of the curve such as D, indicates that some resources are unused. If this occurs some customers may be deprived of goods. This depicts Allocative and Productive inefficiency.



8.3.2 Externalities (spill-over effects)

Negative externalities

Negative externalities bear a private cost, the cost of producing the actual product and a social cost, a cost suffered by society.

If the social cost of a good were added to the private cost of a good, the final price would be pushed up and fewer goods would be supplied. This is depicted in Figure 8.2 below.

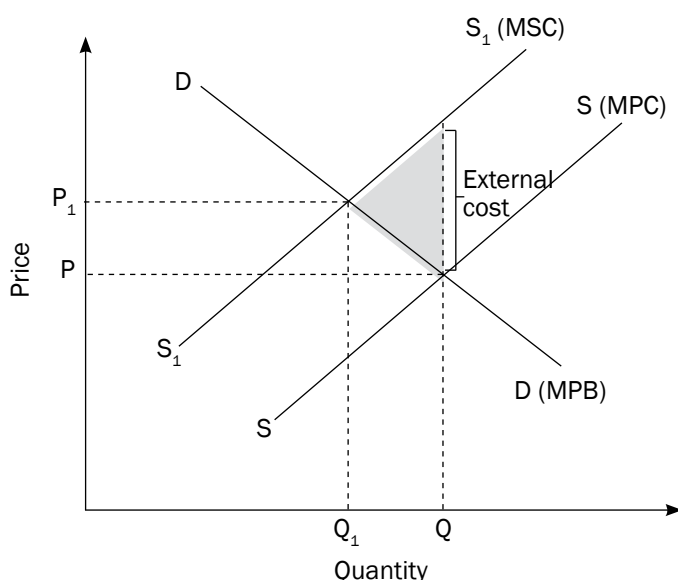


Figure 8.2 Negative externalities

From the graph it can be seen:

- The demand for the cigarettes is represented by DD.
- The supply of the product, which is also the marginal private cost (MPC) of the industry, is represented by SS.
- As a result of the pollution, the marginal social cost (MSC) is greater than MPC.
- If the market is left to its own devices, a quantity Q will be produced at price P.
- This is a socially inefficient solution.
- Social efficiency requires that MSC be equal to the price of the product.
- This occurs at price P_1 and quantity Q_1 .
- Fewer goods should be produced at a higher price.
- The shaded angle represents the negative externality (welfare loss) to society.

The government has used three methods to reduce negative externalities:

- The government has carried out **campaigns** in order to change/persuade people from causing negative externalities.
- **Levying taxes** on goods that cause negative externalities. E.g. Taxes are levied on cigarettes and alcohol.
- **Passing laws and regulations** to prevent activities that cause negative externalities. E.g. Tobacco companies are not allowed to advertise. There are laws that regulate the amount of air pollution and waste.

Positive externalities

If people acknowledged the social benefit of a good, they would demand more of that good. The price of such a good would therefore increase. This is depicted in the Figure 8.3 below.

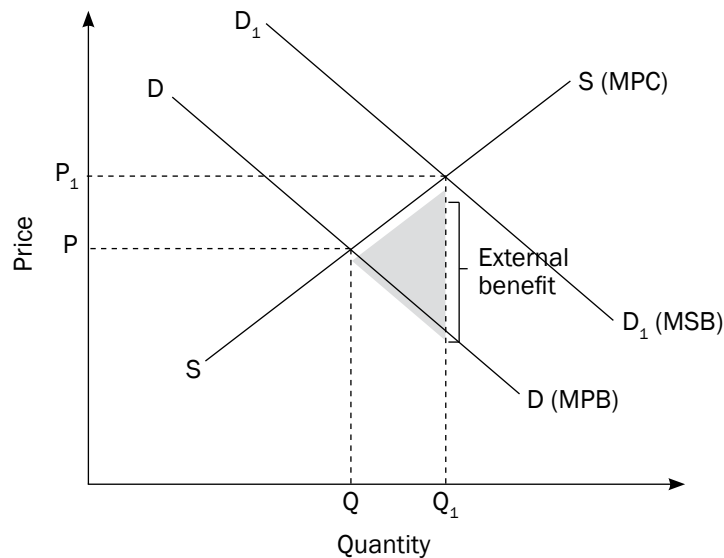


Figure 8.3 Positive externalities

From the graph it can be seen:

- The supply of education, which is also the marginal social cost, is represented by SS.
- The demand for school education, which is also the marginal private benefit (MPB) of the industry, is represented by DD. The cost of school fees is P and the quantity demanded and supplied is Q.
- If the cost of school fees is P, most learners will not be able to afford it.
- The demand curve D_1D_1 also represents the marginal social benefit (MSB), that is, the level of education that should be demanded.
- As a result of the benefits of education, MSB is greater than MPB.
- If the market is left to its own devices, a quantity Q will be produced at price P.
- There would be social inefficiency in the market since not enough education is being demanded.
- However, if social benefits are acknowledged, a quantity Q_1 will be produced at price P_1 .
- More education would be demanded, this will lead to social efficiency.
- The shaded angle represents the positive externality (the welfare gain) to society.

The government encourages positive externalities by:

- Advertising on the radio or television.
- Providing education, health care and other services at a low cost or free.
- Providing consumer subsidies.
- Consumer subsidies lower the cost of a good and encourage its usage.

8.3.3 Government intervention

Rules and regulations

a) Direct controls

The government can pass laws or use existing legislative framework to control businesses that generate negative externalities.

b) Imperfect markets

Firms in an imperfect market supply a limited quantity of goods and services at a very high price.

The government uses its laws on competition to prevent exorbitant prices charged by firms, to ensure entry to the market is free, prevent harmful collusion and encourage foreign competition which helps keep prices of goods low.

c) Establishing minimum wages

- When the government enforces a minimum wage, it means workers have to be paid a certain wage amount and not anything less than this.
- The Figure 8.4 below shows that if the wage rate is set at W , the corresponding demand and supply of labour will be Q .
- If a minimum wage of W_1 is set, the demand for labour will decrease from Q to Q_1 . Some people may become unemployed due to the introduction of a minimum wage.
- However, the quantity of labour supplied will increase from Q to Q_2 .
- More people will offer their labour because of the higher wage.

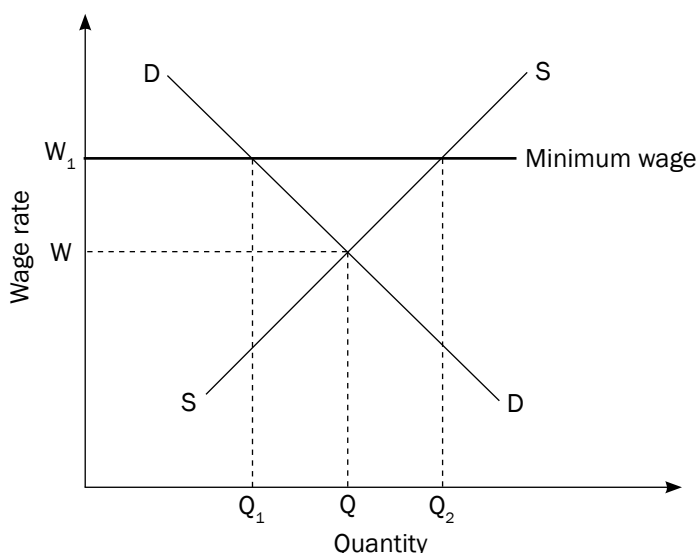


Figure 8.4 Establishing minimum wages

d) Setting maximum prices/price ceilings

- The government sets a **maximum price ceiling** below the market **price** to make goods more affordable.
- Maximum prices allow the **poor greater access to certain goods and services**.

- A maximum price is set on goods such as basic foods, housing and transport.
- In South Africa the price of petrol, diesel fuel and paraffin are controlled at their maximum prices.

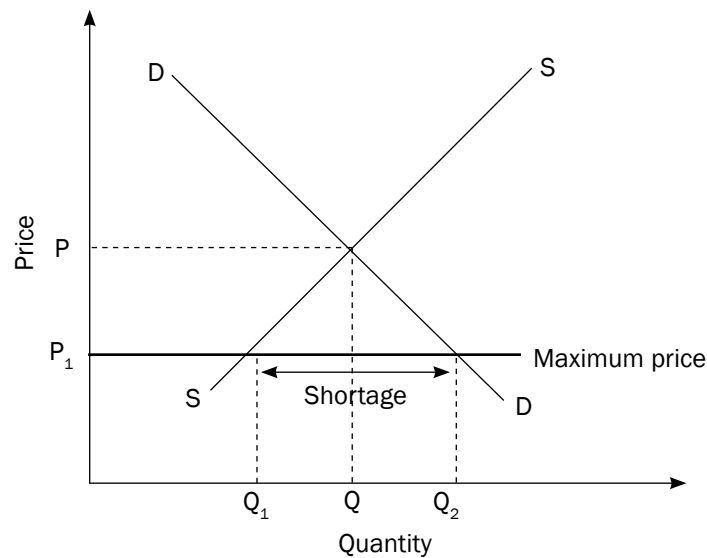


Figure 8.5 Setting maximum prices

- Initially the market equilibrium price is P and equilibrium quantity is Q .
- The government intervenes and passes a law that milk cannot be sold for more than P_1 .
- The effect of this maximum price is that quantity supplied decreases to Q_1 and quantity demanded increases to Q_2 .
- There is a shortage of milk equal to the difference between Q_1 and Q_2 .
- A shortage creates a problem of how to allocate milk to consumers.
- Black markets often develop where people can obtain milk. A black market is an illegal market in which either illegal goods are bought and sold or illegal prices are charged.
- Maximum prices may cause a shortage of goods but they do improve the welfare of some consumers since goods can be purchased at lower prices.

e) Setting minimum prices/price floors

- The government sets a **minimum price** at some point above the **market price**.
- This is done to **enable producers to make a comfortable profit** and thus encourages them to **supply important essential goods**.

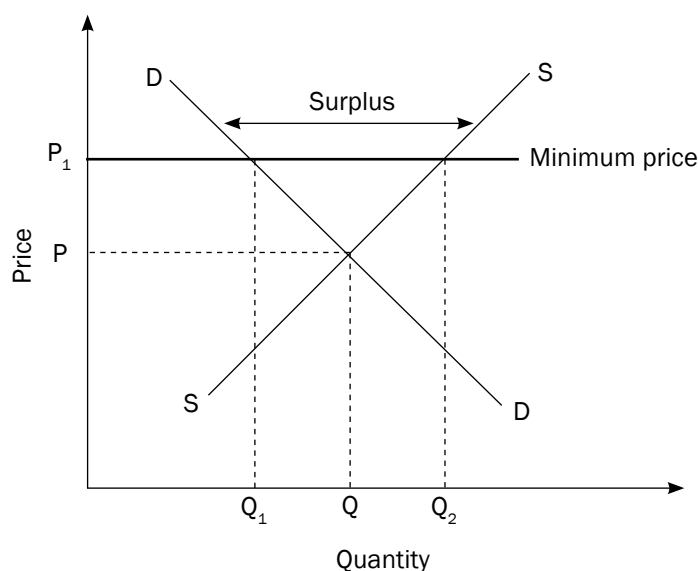


Figure 8.6 Setting minimum prices

- Consider the market for wheat.
- The market equilibrium price is P and the equilibrium quantity is Q .
- If the government sets a minimum price at P_1 , farmers will be earn greater profits and supply more wheat. Quantity supplied will therefore increase to Q_2 .
- However, quantity demanded will decrease to Q_1 .
- There would be a surplus of wheat equal to the difference between Q_2 and Q_1 .
- A surplus means the government will have to buy the extra wheat and dump it locally or abroad.
- Although minimum prices may cause a surplus they do encourage the supply of important food stuffs.

f) Taxes and subsidies

Levying of taxes

Governments intervene in the market by levying taxes to recover the external cost. These taxes will increase the price and will result in a decrease in production. This could help to reduce a negative externality such as pollution.

Providing Producer Subsidies

- The government provides subsidies to producers in order to encourage them to increase the production of goods. Supply increases.
- Producer subsidies are often given to suppliers of agricultural products such as milk, wheat and maize.
- Subsidies lower the cost of producing goods and thus the market price of these goods is lowered.

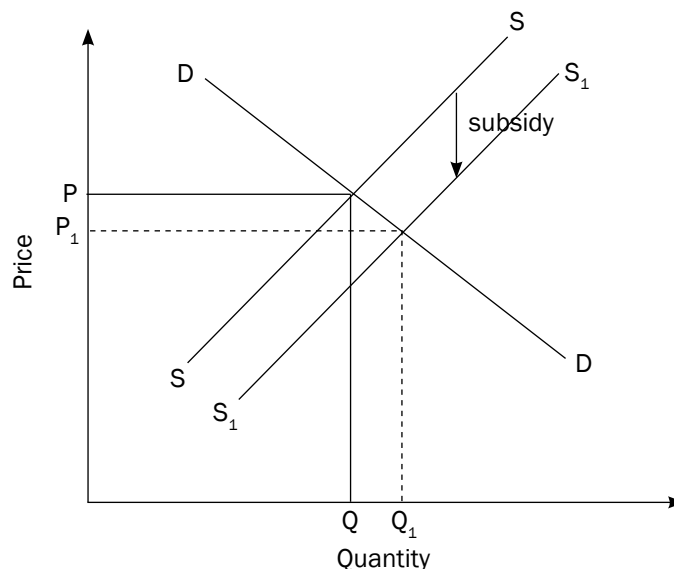


Figure 8.7 Taxes and subsidies

For example, if we look at Figure 8.7:

- The market price of rice is P and the corresponding quantity is Q .
- If the government subsidises the production of rice, the market price will decrease to P_1 with corresponding quantity Q_1 .
- The lower price, P_1 , allows the poor to purchase more rice.

g) Redistribution of wealth

- Traditional methods e.g. the levying of various taxes and the provision of free services, services in kind and cash benefits to the poor.
- Implementing Redress methods e.g. the use of law to enforce redistribution. It includes BEE, affirmative action, empowerment, land restitution, land redistribution and property subsidies (for RDP houses).

The government can use other ways to improve income distribution and overcome market failure:

- Transfers income directly to the poor e.g. child support grants, unemployment benefits etc.
- Provides goods free of charge e.g. community goods, education etc.
- Implements employment creation programmes e.g. public works programme.
- Subsidising merit goods e.g. subsidising arts and cultural events.
- Imposes taxes and laws on demerit goods to discourage consumption.
- Uses fiscal and monetary policy to achieve macroeconomic stability.
- Makes sure that consumers are informed about products through legislation. The South African Bureau of Standards (SABS) checks consumer goods in South Africa.
- Tries to prevent misleading advertising. (Advertising Standards Authority)

8.4 Cost-benefit analysis (CBA)

8.4.1 Description

In both private and public sectors project evaluations are done in terms of cost and benefits. In the **private sector** feasibility studies are done which also provides for legal aspects relating to externalities. Expected private costs and benefits are taken into account.

In the **public sector** a Cost Benefit Analysis is done which takes into account expected social costs and social benefits of providing such goods and services.



Learn these three points about cost benefit analysis.

8.4.2 Reasons for cost benefit analysis

- Market signals e.g. price help to allocate resources through demand and supply.
- Goods supplied by the government such as roads, bridges etc. are provided free.
- With the absence of market signals, decisions on the desirability of a project may be subjective.
- Objective criteria may be required to ensure economic efficiency in resource allocation.
- CBA brings greater objectivity to decision making.
- This is done by identifying all the relevant benefits and costs of a project so that an informed decision can be made.

8.4.3 Applying the CBA (an example)

CBA is usually applied to projects where it is expected there will be a significant difference in private and social costs and benefits.

Imagine the Gautrain project, a rail service that connects Hatfield in Tshwane with Johannesburg and the OR Tambo International Airport.

Private costs would include: <ul style="list-style-type: none"> • The cost of land. • The cost of building materials and equipment. • Transport costs. • Labour costs. • Overhead costs etc. 	Private benefits would include: <ul style="list-style-type: none"> • Train fares. • Subsidies from government. • Money from allowing companies to advertise.
External costs would include: <ul style="list-style-type: none"> • Pollution. • Destruction of plants, animals and insects. • Resettlement for people whose homes were expropriated. • Increased traffic in certain areas and blockages of certain driving routes. 	External benefits would include: <ul style="list-style-type: none"> • Employment and income. • Opportunities for new businesses. • Time saved because of the high speed of the train. • Fewer accidents and less traffic. • Less strain on medical facilities.

Once all benefits and costs were determined it was eventually decided that the idea of the Gautrain would benefit society more than harm it. Planning for the Gautrain started in 2000 but building only started in 2006.



Activity 1

Study Figure 8.8 and answer the questions that follow.

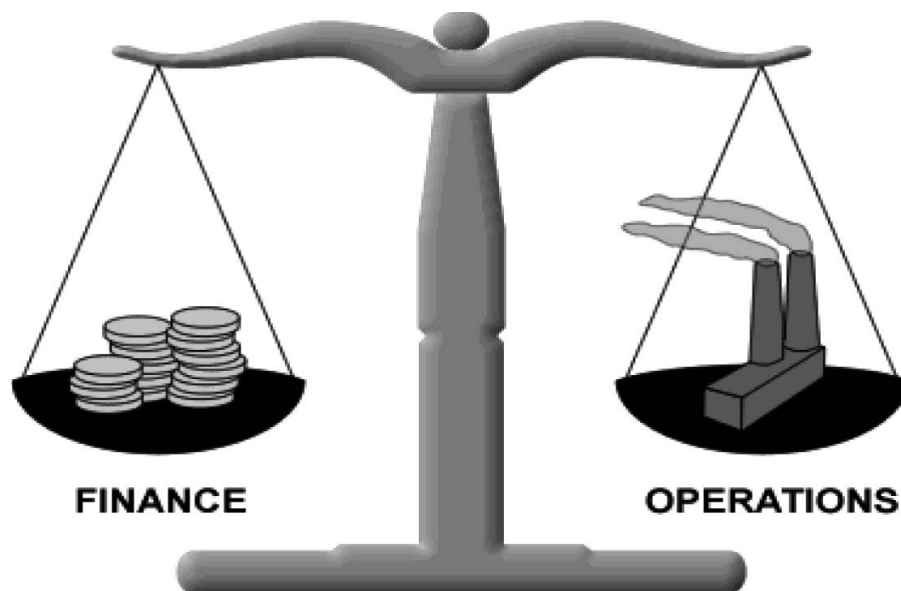


Figure 8.8

1. What economic technique for enumerating and evaluating is depicted in the illustration? (2)
 2. Give TWO recent examples of potential 'operations' in South Africa that will fit into the illustration. (2)
 3. List ONE social benefit of each of the above projects. (4)
- [8]**

Answers to activity 1

1. Cost benefit analysis ✓✓ (2)
2. Gautrain ✓ Coega ✓ (2)
Any other relevant fact.
3. Gautrain: Better infrastructure ✓✓ More effective transport ✓✓
Coega: Job creation ✓✓ / increased standard of living ✓✓ Any other relevant fact. (any 2 × 2) (4)

[8]



Activity 2

Distinguish between merit and demerit goods.

[8]

Answer to activity 2

- Taxation, subsidies and legislation are used to control merit and demerit goods. ✓✓
- **Merit goods:** higher consumption of goods is regarded as good for society ✓✓ government makes use of subsidies ✓✓ (distribute condoms). ✓✓
- **Demerit goods:** government imposes taxes to discourage consumption ✓✓ (cigarettes). ✓✓

[8]



Activity 3

Discuss the features of collective goods.

[8]

Answer to activity 3

- **Non-rivalry:** ✓✓ Consumption by one person does not reduce consumption by another individual ✓✓ e.g. a lighthouse ✓✓
- **Non-excludability:** ✓✓ Consumption can't be confined to those who pay for it (free riders can use it) ✓✓ e.g. radio and television ✓✓

[8]



Activity 4

Discuss the distribution of wealth and income as a consequence of market failure.

[8]

Answer to activity 4

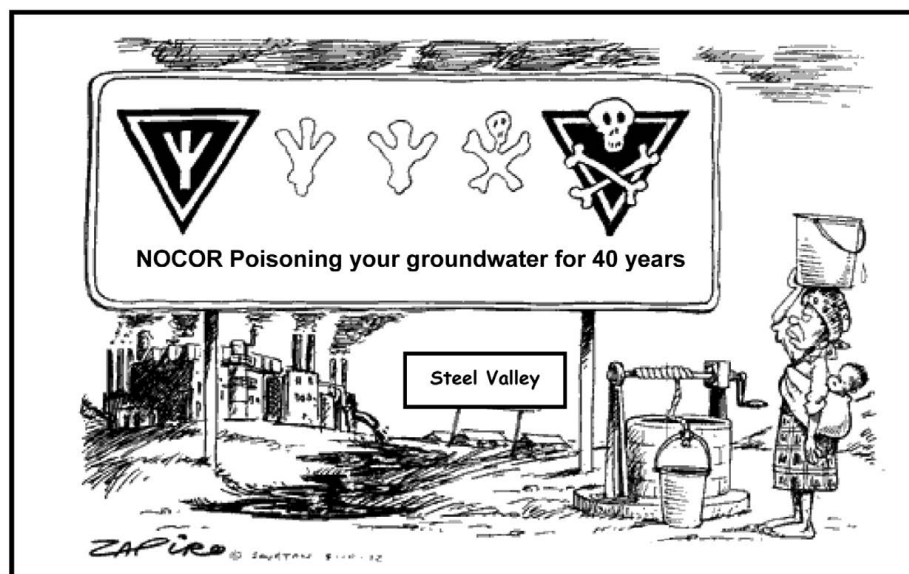
- Through the national budget and taxation ✓✓
- Change the distribution of income by: ✓✓ Subsidies, transferring payments to poor households, providing goods and services free of charge, implementing job creation programmes ✓✓
- Regulatory measures: ✓✓ Land reform, labour legislation, preferential access to government procurement contracts, black economic empowerment policies ✓✓

[8]



Activity 5

Study the following illustration and answer the questions that follow:



1. Identify the negative externality depicted in the illustration. (2)
2. List TWO measures that can be applied by government to reduce this externality. (2)
3. What is the liability of the factory in this regard? (2)
4. What effect will this have on consumer prices? (2)

[8]

Answers to activity 5

1. Pollution ✓✓
2. Legal actions ✓ and taxes ✓ (any 1)
3. To reduce the pollution ✓✓
4. Consumer prices will increase ✓✓

[8]



Economic growth and economic development

Overview

TOPIC	CONTENT	SCOPE AND DEPTH OF EXAMINABLE CONTENT
9. Economic growth & Development	<p>Compare South African growth and development policies in terms of international benchmarks, also highlight the North/South divide</p> <ul style="list-style-type: none"> • Background <ul style="list-style-type: none"> – Economic growth – Economic development • The demand-side Approach <ul style="list-style-type: none"> – Growth and Development <ul style="list-style-type: none"> – Monetary policy – Fiscal policy – South Africa's Approach <ul style="list-style-type: none"> – Monetary policy <ul style="list-style-type: none"> Interest rate changes Open market transactions Moral suasion – Fiscal Policy <ul style="list-style-type: none"> Progressive personal income tax Wealth tax Cash benefits Natura benefits Other redistribution Land restitution and redistribution Subsidies on property • The supply-side Approach <ul style="list-style-type: none"> – Creation of growth <ul style="list-style-type: none"> – Aggregate supply and demand – South Africa's approach <ul style="list-style-type: none"> – Efficiency and effectiveness of markets – Business efficiency – The cost of doing business 	<ul style="list-style-type: none"> • Distinguish between growth and development • Distinguish between government policies, strategies and initiatives • Discuss the demand-side approach in detail • Focus on discretionary changes in monetary and fiscal policies with the aim of changing the level of aggregate demand and therefore output (Real GDP) • Analyse SA's approach in terms of its monetary policy • Focus on: the SARB which is responsible for the implementation of the policy. Its primary goal is to protect the value of our currency • Analyse South Africa's approach in terms of fiscal policy • Focus on: the budgetary process, the purpose of fiscal policy to stimulate macroeconomic growth and employment and to ensure a desirable redistribution of income • Discuss the supply-side approach in detail <p>HOT QUESTION: Critically analyse the use of demand and supply-side policies in South Africa</p>

	<ul style="list-style-type: none"> • Evaluate the approaches of the growth and development policies used in South Africa <ul style="list-style-type: none"> – Growth and Development Policies <ul style="list-style-type: none"> – Reconstruction and Development policy (RDP) – Growth Employment and Redistribution Programme (GEAR) – National Skills Development Strategy (NSDS) – Accelerated and Shared Growth Initiative for South Africa (ASGISA) – Joint Initiative on Priority Skills Acquisition (JIPSA) – Expanded Public Works Programme (EPWP) – The New Growth Path (NGP) – National Development Plan (NDP) – Small Business Development Promotion Programme – Black Economic Empowerment Programmes • The North/South divide <ul style="list-style-type: none"> – Unequal standards of living <ul style="list-style-type: none"> – Per capita income – Life expectancy – Education – Challenges of Globalisation <ul style="list-style-type: none"> – Poverty – Growth – Trade – Environment <ul style="list-style-type: none"> – Countries in the North – Countries in the South 	<ul style="list-style-type: none"> • Discuss South Africa's growth and development policies in detail • Appraise South Africa's growth and development policies • Evaluate (benchmark) elements of South Africa's growth and development policies from given data <p>HOT QUESTION: Analyse South Africa's Growth and Development Plan (GDP) in terms of growth and development objectives</p> <ul style="list-style-type: none"> • Compare the standard of living between North/South countries • Explain the positive/negative impact of globalisation on developing countries • Explain the negative environmental effects as a result of the economic activities in both North and South
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9.1 Key concepts

These definitions will help you understand the meaning of key Economics concepts that are used in this study guide. Understand these concepts well.

Use mobile notes to help you learn these key concepts. See page xiv in the introduction for more.



Term	Definition
Accelerated and Shared Growth initiative for South Africa (ASGISA)	An initiative to promote development strategies, e.g. infrastructure and skills development
Broad Based Black economic empowerment (BBBEE)	Has the goal of the sustainable (able to continue) distribution of wealth across as broad a spectrum of South African society as possible, especially the most vulnerable such as women, mainly through ownership and management of business enterprises
Black economic empowerment (BEE)	An earlier policy similar to BBBEE, with the aims of distributing wealth to and developing skills in black citizens in post-apartheid South Africa
Development Bank of Southern Africa (DBSA)	Promotes development in the Southern African region by financing important development projects
demand-side approach	The focus is on attempts to increase aggregate demand in an economy. Fiscal and monetary policy can be used
economic development	The process by which the standard of living improves
economic development policy	A policy that involves the interaction of economic, social and human development
economic growth	An increase in the productive capacity of an economy over time. It is a change in the real GDP
economic growth policy	A policy that helps to increase the annual total production or income in the economy
Growth, employment and redistribution (Gear)	A strategy to promote economic growth, increase employment and redistribute income
Globalisation	The worldwide interaction of economies with trade as an important element
Integrated Manufacturing Strategy (IMS)	A strategy to strengthen institutional capacity to deliver services that will facilitate development
Joint initiative on Priority Skills acquisition (JIPSA)	An initiative to aid the development of urgently needed skills to facilitate job creation
Life expectancy	Expresses in number of years how long a child born today is expected to live
National Growth Path (NGP)	Initiatives to stimulate economic growth
North-South divide	Refers to the developed countries in the Northern hemisphere and the developing countries in the Southern hemisphere

Public and Private Sector Partnerships (PPP)	These are contracts between a public sector institution/municipality and a private business, in which the design, financing, building and operation of public sector projects is managed by the private business
Reconstruction and Development Programme (RDP)	A development policy to improve service delivery to the poor and create an environment for human development
South African Reserve Bank (SARB)	Central bank of South Africa with the main goal to maintain price stability, thereby promoting balanced and sustainable growth
Small, Medium and Micro Enterprises (SMMEs)	A small business that has a small share of the market place; operates independent of larger enterprises; employs few people; and is managed directly by owners
Supply-side approach	Policies aimed at increasing the aggregate supply

Learn the difference between growth and development initiatives.

9.2 Economic growth and economic development

The difference between economic growth and economic development

Economic growth	Economic development
<ul style="list-style-type: none"> • Increase in a country's real gross domestic product • It is measured by the increase in the production of goods and services over time 	<ul style="list-style-type: none"> • Increase in a country's real gross domestic product per capita over time • A process that concentrates on peoples' standards of living, self-respect and freedom of choice • Growth should lead to development

9.3 Demand-side approach

9.3.1 Growth and Development

A **demand-side** approach includes discretionary changes in monetary and fiscal policies with the aim of changing the level of *aggregate demand*.

Monetary policy is driven by the South African Reserve Bank (SARB). It aims to stabilise prices by managing inflation.

Fiscal policy is driven by the Department of Finance. It aims to facilitate government, political and economic objectives.

A demand-side approach to economic growth and development does not only depend on fiscal and monetary policy. It is dependent on all components of aggregate demand, that is, C, I, X and G.

hint

When you prepare for the exam, memorise CONCEPTS FIRST!

9.3.2 South African approach

The South African approach uses both monetary and fiscal measures to influence aggregate demand in the economy.

Monetary policy

The South African Reserve Bank (SARB) as the central bank in South Africa formulates the monetary policy. They use the following instruments:

- **Interest rate changes**
It is used to influence credit creation by making credit more expensive or cheaper. The exchange rate is stabilised by encouraging inflow or outflows.
- **Open market transactions**
To restrict credit the SARB sells securities. When banks buy these securities money flows from banks to the SARB. The banks have less money to lend and cannot extend as much credit as before. To encourage credit creation the SARB buys securities. Money flows into the banking system.
- **Moral suasion**
The SARB consults with banks to act in a responsible manner based on the prevailing economic conditions.
- **Cash Reserve Requirements**
Banks are required to hold a certain minimum cash reserve in the central bank. Banks have a limited amount to give out as credit.

Fiscal policy

South Africa's fiscal policy is put into practice through the budgetary process. The main purpose of fiscal policy is to stimulate macroeconomic growth and employment, and ensure redistribution of wealth.

The following instruments are used:

- **Progressive personal income tax**
Higher income earners are taxed at higher tax rates. These taxes are used to finance social development. The poor benefit more than those with higher incomes.
- **Wealth taxes**
Properties are levied (taxed) according to their market values. Transfer duties are paid when properties are bought. Securities (shares and bonds) are taxed when traded. Capital gains tax is levied on gains on the sale of capital goods (e.g. properties, shares). Estate duties are paid on the estates of the deceased. These taxes are used to finance development expenditures which benefit the poor more often.
- **Cash benefits**
Old age pensions, disability grants, child support and unemployment insurance are cash grants. These are also known as social security payments.
- **Benefits in kind (natura benefits)**
These include the provision of healthcare, education, school meals, protection etc. When user fees are charged, poor or low income earners pay less or nothing. Limited quantities of free electricity and water are provided.

- **Other redistribution**
Public works programmes, e.g. the Strategic Integrated Projects (SIP) provides employment subsidies and other cash and financial benefits such as training, financing and export incentives.
- **Land restitution and land redistribution**
Land restitution is the return of land to those that have lost it due to discriminatory laws in the past. Land redistribution focuses on land for residential (town) and production (farm) for previously disadvantaged groups. The money for these programmes is provided in the main budget.
- **Subsidies on properties**
It helps people to acquire ownership of fixed residential properties. E.g. government's housing subsidy scheme provides funding to all people earning less than R3 500 per month.

9.4 The supply-side approach

9.4.1 Creation of growth

A supply-side approach includes anything that can influence the aggregate supply of goods and services, with the focus on microeconomic components, e.g. competition and potential output.

Government intervention aims to facilitate the smooth operation of markets in order to stimulate growth and development.

9.4.2 South African approach

The South African approach aims at improving the **effectiveness** and **efficiency** of markets. This requires:

- Markets to operate more equitably and inclusively: More blacks must be accommodated in the mainstream economy if it is to work efficiently.
- **Business efficiency:** Taxes must be collected efficiently, capital formation must increase, human resources must be supported to improve, and free advisory services must be made available so that business efficiency improves.
- **The cost of doing business** must be lowered: transport, communication and energy costs must decrease.

9.5 Evaluation of the South African approaches used in South Africa

9.5.1 Growth and development policies

Growth	Development
<p>Macroeconomic policies</p> <p>These include measures to achieve the following macroeconomic objectives:</p> <ol style="list-style-type: none"> 1. Higher economic growth 2. High levels of employment 3. Price stability 4. Exchange rate stability 5. Economic equity <p>Increased economic growth leads to more tax revenue which can be used to provide more social goods and services with the aim of achieving economic development.</p> <p>All the above measures should be evaluated in terms of international benchmarks.</p>	<p>Development policies</p> <p>These include measures aimed at achieving industrial, agricultural and human development:</p> <ol style="list-style-type: none"> 1. Microeconomic initiatives <ul style="list-style-type: none"> • Facilitating increased competition, opening up resource markets, enabling land-use and environmental policy. 2. Social care <ul style="list-style-type: none"> • Social welfare and security and poverty alleviation • Policies to redress past inequalities, including Employment Equity and BEE/BBBEE • Affirmative action • Land redistribution and restitution 3. Macroeconomic characteristics and desired outcomes: <ul style="list-style-type: none"> • Standard of living low – increase the per capita income. • Unemployment high – create more employment, e.g. public sector work programme. • Productivity low – improve the level of knowledge, skills and motivation, e.g. JIPSA.

At certain periods, the South African government has focused its initiatives on economic growth, while at other points, policy emphasis has shifted to economic development (see Figure 1 below).

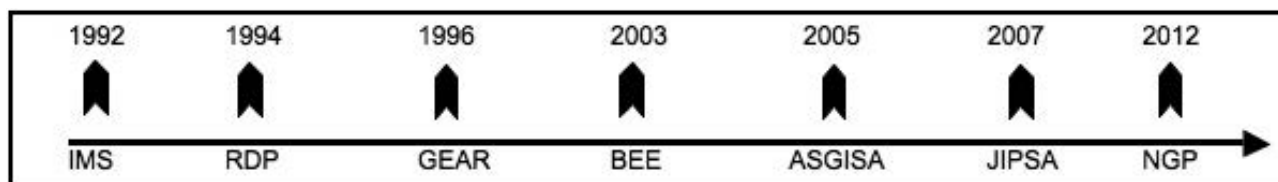


Figure 9.1 Growth and development policies

The main growth and development policies are:

1. Reconstruction and Development Programme (RDP)

The main strategy was to alleviate poverty and address the inequalities and shortfalls in social services by focusing on job creation, welfare, housing, transport, land reform, healthcare, education, training, water and sanitation.

Evaluation thus far:

- Meeting basic needs: government creates an increased demand for goods and services. The expanded public works programmes were mostly labour intensive. This helped alleviate unemployment and poverty slightly.

- Some social achievements: building houses, providing clean water, electrification, land reform, and healthcare.
- Real GDP growth erratic since 1994, unemployment in formal sector increased.
- Key objectives of poverty reduction and improved service delivery hardly successful.

2. Growth, Employment and Redistribution (GEAR)

The main strategy was to strengthen economic development, redistribute income and create socio-economic opportunities for the poor.

Evaluation thus far:

- Mixed outcomes.
- Brought greater financial discipline and macroeconomic stability.
- Real reduction in fiscal deficit (less than 3% in terms of international benchmarks).
- Inflation has dropped mostly to within inflation targets.
- Foreign exchange reserves increased in most regards.
- Failure to create sustainable job opportunities.
- Failure to redistribute wealth more evenly.

3. Accelerated and Shared Growth Initiative for South Africa (ASGISA)

Its objective is to co-ordinate government initiative to create economic development:

The key elements are:

- Halve unemployment and poverty by 2014.
- Accelerate economic growth to an average of 6% between 2010 and 2014.

Evaluation thus far:

- Growth in infrastructure investment, especially in the public sector.
- Employment growth has lagged behind economic growth – reason real wage increases are higher than productivity.
- The second economic strategy helped slightly to reduce unemployment through the Expanded public Works Programme.
- Poor economic growth and high unemployment for the youth.

4. Joint Initiative on Priority Skills Acquisitions (JIPSA)

It is the skills development arm of ASGISA. Focus is on skills development, especially through the SETAS.

5. Expanded Public Works Programme (EPWP)

It is a nationwide government intervention to create employment using labour-intensive methods, and to give people skills they can use to find jobs when their work in the EPWP is done.

6. The New Growth Path (NGP)

Its aim is to enhance growth, create employment and create greater equity.

The strategy is to identify key sectors as “job drivers” and promote and support industries and sectors that can drive job creation.

Focus is to:

- Create 5 million jobs by 2020, reducing unemployment from 25% to 15%.

7. National Development Plan (NDP)

It sets out to expand economic opportunities through investment in infrastructure, more innovation, private investment and entrepreneurship.

8. Small Business Development Promotion Programme (SBDPP)

It was designed to deliver support and services to small, medium and micro enterprises.

- Department of Trade and Industry (DTI), Industrial Development Corporation (IDC) and the National Small Business Act offer these services.
- Laws are revised to help change power imbalances.

9. Black Economic Empowerment Programmes (BEE)

The Black Empowerment Act and Employment Equity Act were designed to assist in the transformation and redress of previously disadvantaged groups. Measures are implemented to ensure redress and affirmative action in the workplace and business environment.

9.6 The North/South divide

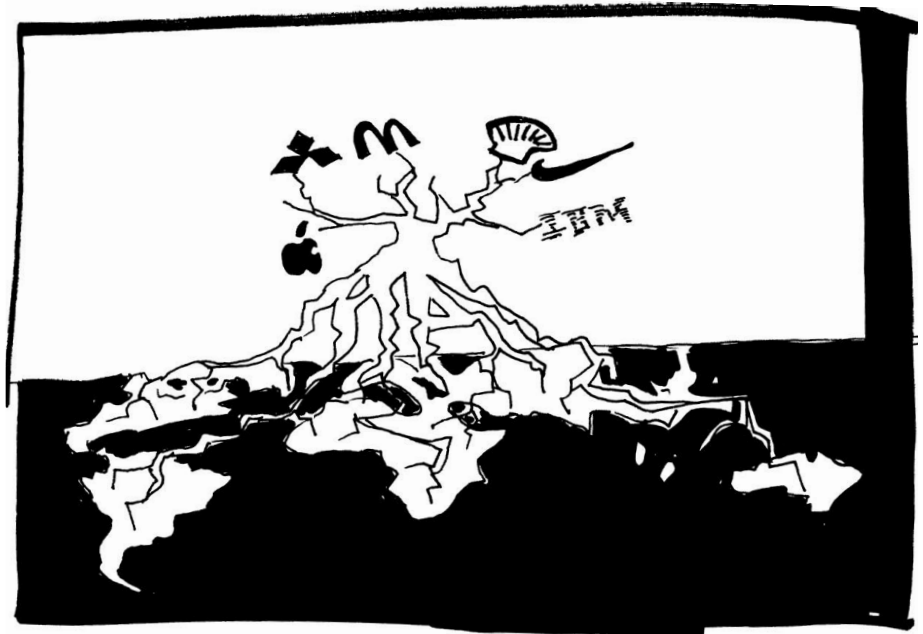
The table below shows different ways to distinguish between developed countries (in the North) and developing countries (in the South).

	North (developed)	South (developing)
Standard of living: <ul style="list-style-type: none"> • Real GDP per capita • Life expectancy • Education: Literacy level 	<ul style="list-style-type: none"> • High • 75 years • High 	<ul style="list-style-type: none"> • Low • 48 years • Low
Globalisation inequalities: <ul style="list-style-type: none"> • Poverty level • Economic growth • Production and trade 	<ul style="list-style-type: none"> • Low • High • Manufacturing goods • Receive subsidies 	<ul style="list-style-type: none"> • High • Low • Raw material • Agriculture/mining without subsidies
Environment: <ul style="list-style-type: none"> • Mass production and consumption damages the ozone layer, caused by pollution and toxic waste 	<ul style="list-style-type: none"> • Mainly responsible for damaging the ozone layer 	<ul style="list-style-type: none"> • Affects developing countries more negatively
Sustainable development: <ul style="list-style-type: none"> • The pattern of development that permits future generations to live as well as the current generation 	<ul style="list-style-type: none"> • Practices used in production are more in favour of sustainable development 	<ul style="list-style-type: none"> • Production practices do not promote sustainable development



Activity 1

Study the cartoon below and answer the questions that follow:



1. What is the message behind the cartoon? (2)
 2. List any TWO countries involved in this phenomenon. (2)
 3. List any TWO products displayed in the cartoon. (4)
- [8]

Answers to activity 1

1. Globalisation ✓✓ (2)
 2. USA ✓ and Japan ✓ (2)
 3. Motor vehicles ✓✓ and fuel ✓✓ (4)
- [8]



Activity 2

Study the cartoon below and answer the questions that follow:



1. What is the message behind the cartoon? (2)
 2. What is the main objective of Broad-Based Black Economic Empowerment? (2)
- [4]

Answers to activity 2

1. The people are dissatisfied about the way the government is handling Black Economic Empowerment (corruption and nepotism). ✓✓ (2)
 2. To advantage the previously disadvantaged section of the population. ✓✓ (2)
- [4]



Activity 3

Distinguish between economic growth and economic development.

[8]

Answer to activity 3

Economic growth	Economic development
<ul style="list-style-type: none"> A process by which the productive capacity of the economy increases over time. ✓✓ Leads to rising levels of national output and income. ✓✓ Is an increase in real gross domestic product (GDP). ✓✓ 	<ul style="list-style-type: none"> A process that concentrates on people's standard of living, self-respect and freedom of choice. ✓✓ Growth should lead to development. ✓✓ The ultimate aim of economic policy is an improved standard of living of the population per capita by means of economic growth and development. ✓✓

(any 2 × 2) × 2 [8]



Activity 4

Explain unequal standards of living as a characteristic of the North/South divide.

[6]

Answer to activity 4

- The real per capita income in developing countries is low compared to developed countries, ✓ e.g. 87% of the world's total income is produced by 15% of the world's population ✓
- Life expectancy in developing countries is as low ✓ as 47 years compared to a life expectancy of over 80 years in a country like Sweden ✓
- Low levels of education ✓ the adult literacy rate determines the effectiveness of education ✓

[6]



South Africa's industrial policies and their suitability in terms of international best practice

Overview

TOPIC	CONTENT	SCOPE AND DEPTH OF EXAMINABLE CONTENT
10. Economic growth and development: Industrial development policies	<p>Justify South Africa's industrial development policies and their suitability in terms of international best practice</p> <ul style="list-style-type: none"> • Industrial development in South Africa <ul style="list-style-type: none"> – Industrial Development Policies <ul style="list-style-type: none"> – National Industrial Policy Framework (NIPF) – Industrial Policy Action Plans (IPAP) – Industrial development Strategies <ul style="list-style-type: none"> – National Research and Development Strategy (NRDS) – Integrated Manufacturing Strategy (IMS) – Focus of these Policies and Actions <ul style="list-style-type: none"> – Targeted industries, sectors and regions – Sectors with potential – Special Economic Zones – Southern Africa 	<ul style="list-style-type: none"> • Define/explain the concept • Briefly discuss the reasons for industrial development • Justify South Africa's Industrial Development Policies • Briefly explain South Africa's Industrial Development Strategies

	<ul style="list-style-type: none"> • Regional Development <ul style="list-style-type: none"> – Aims – Regional development in South Africa – International best practice for regional development • South Africa's endeavours <ul style="list-style-type: none"> – Spatial Development Initiatives (SDIs) – Industrial Development Zones (IDZs) – Special Economic Zones (SEZs) – Corridors – Strategic Integrated Projects (SIPs) – Infrastructure Plan • Incentives to encourage industrial development <ul style="list-style-type: none"> – Small Businesses Support Program – SEDA Technology Program (STP) – Skills Support Program (SSP) – Critical Infrastructure Facilities (CIP) – Custom Free Incentives – Foreign Investment Incentives – Strategic Investment Program – Services to Business Processes • Appropriateness of South Africa's industrial policies <ul style="list-style-type: none"> – Success factors – External Limitations – Internal Limitations • Appropriateness of South Africa's regional development policies • Small business development • The appropriateness of Black Economic Empowerment in the SA economy <ul style="list-style-type: none"> – Best practice for regional development <ul style="list-style-type: none"> – Benchmarks criteria: <ul style="list-style-type: none"> – Free Market orientation – Competitiveness – Sustainability – Good governance – Provisioning of resources – Investment of social capital – Integration – Partnerships 	<ul style="list-style-type: none"> • Define/explain the concept • Briefly discuss regional development • Briefly discuss Spatial Development Initiatives (SDIs) in South Africa • Briefly discuss Industrial Development Zones (IDZs) in South Africa • Briefly discuss Special Economic Zones (SEZs) in South Africa • Briefly discuss corridors in South Africa • Critically discuss the incentives used by the SA government to improve industrial development • Briefly discuss the appropriateness of SA endeavours • Evaluate the appropriateness of the South African industrial development strategies in terms of international benchmark criteria
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10.1 Key Concepts

These definitions will help you understand the meaning of key Economics concepts that are used in this study guide. Understand these concepts well.

Use mobile notes to help you learn these key concepts. Find out more about mobile notes on page xiv in the introduction.



Term	Definition
Black Business Supplier Development Programme (BBSdP)	An incentive for black businesses consisting of an 80% cash grant to help increase the number of cash suppliers
Critical Infrastructure Programme (CIP)	Offers cash grants for projects that require new, expanded or improved infrastructure
Department of Trade and Industry (DTI)	Provides a competitive, socially responsible environment for investment, trade and enterprise development. It helps broaden participation in the economy to strengthen economic development; and it promotes structural transformation of the economy
Foreign Investment Grant (FIG)	Offers cash grants for foreign investors who invest in new manufacturing businesses in South Africa
General agreement on tariffs and trade (GATT)	A multilateral agreement regulating international trade. Its purpose is to reduce tariffs and other trade barriers
Industrial Development Corporation (IDC)	Set up by government to promote economic growth and industrial development in South Africa and Africa. It promotes entrepreneurship by building competitive industries and enterprises based on sound business principles
Industrial Development Zone (IDZ)	These are purpose-built industrial estates that are physically enclosed and linked to an international port or airport e.g. Coega. Businesses are encouraged to open in IDZs by being offered improved tax rates or incentives
Integrated Manufacturing Strategy (IMS)	A strategy to strengthen institutional capacity to deliver services that will facilitate development
industrial development	Refers to policies that are aimed at the encouragement of industrial investment and greater industrial efficiency
Regional industrial development	Refers to policies that are aimed at increasing the economic livelihood of specific areas or geographical regions
Southern African Development Community (SADC)	An inter-governmental organisation whose goal is to further socio-economic cooperation and integration, as well as political and security cooperation among 15 Southern African states
Spatial Development Initiatives (SDI)	Initiated to attract infrastructure and business investments to neglected and underdeveloped areas, e.g. Maputo Corridor
Small and Medium Enterprise Development Programme (SMedP)	A programme that offers grants paid to local and foreign manufacturers starting new businesses
Skills Support Programme (SSP)	A cash incentive granted for skills development

10.2 Industrial development policies in South Africa

10.2.1 Industrial development policies

Reasons for industrial development

- Exploit the world economy to trade and acquire knowledge.
- Maintain macroeconomic stability.
- Achieve high rates of savings and investment.
- Establish large scale manufacturing, agricultural, mining and services production.
- Diversification of the economy.
- Develop domestic manufacturing capacity to increase exports.
- Create jobs.
- Develop and maintain appropriate incentives to attract investors.
- Contribute to the industrial development of the African continent.

National Industrial Policy Framework (NIPF)

- Is the industrialisation policy of the Department of Trade and Industry.
- Aims:
 1. To make the economy more diverse so that exports can increase.
 2. To make industrialisation more intensive in the long run.
 3. To promote the development of labour-intensive industries.
 4. Greater participation by disadvantaged groups and development of marginalised areas.
 5. Increase potential for large scale production.

Industrial Policy Action Plans (IPAP)

- As part of the NIPF, the DTI developed a revised three-year rolling action plan each year with a ten year outlook.

First Industrial Policy Action Plan (IPAP-1), 2007	Second Industrial Policy Action Plan (IPAP-2), 2011	Third Industrial Policy Action Plan (IPAP-3), 2012
Establish a new support programme for the clothing and textile industry	Increase the availability of financing for industrial development	Launch manufacturing Competitiveness Enhancement Programmes
Provide a programme to assist the motor industry	Improve the procurement policy under BBBEE policy	Develop special economic zones including IDZs
Strengthening the Competitions Act Increase energy savings	Strengthening the trade policy	Provide government support for regional economic development
Make business management more efficient and increase job creation	Reduce anti-competitive practices	Encourage integration of South Africa into Southern African region

10.2.2 Industrial development strategies

- National Research and Development Strategy (NRDS)
- Integrated Manufacturing Strategy
 - The IMS focus on improving competitiveness in manufacturing by looking at a range of factors, such as input prices, improving infrastructure, technology and innovation, skills and effective regulation.

Focus of these policies and actions

- Targeted industries, sectors and regions
- Sectors with potential
- Special Economic Zone (SEZ)
- Southern Africa

10.3 Regional development

10.3.1 Aims

- Reduce unequal development of economic activities within the country
- To stimulate development in poorer areas
- To implement and coordinate the implementation of national and regional industrial policies
- To prevent new imbalances from emerging

10.3.2 Regional development in South Africa

- An estimated 80% of the country's GDP is produced in four industrialised areas, namely:
 - Johannesburg-Pretoria-Tshwane
 - Durban-Pinetown
 - Cape Town metropole
 - Port Elizabeth-Coega-Uitenhage
- Reasons for the uneven geographical economic development
 - Unequal spending on regional development
 - Uneven distribution of economic resources, such as natural resources and skilled workforce
- The regional development policy aims to promote a more even spread of industries so that capital and labour can be directed towards under-developed areas.
- Regional development is currently based on the Spatial Development Initiatives (SDIs), Special Economic Zones (including IDZs and corridors)
- The Integrated Manufacturing Strategy (IMS) was implemented by the DTI to assist industries to grow by identifying certain cross cutting issues and competitive input sectors. The cross cutting issues are technology, human resource development, access to finance and infrastructure. The competitive input sectors are transport, telecommunications and energy.
- Strategic Integrated Projects (SIPs) are being implemented to uplift economic and social infrastructure projects across the country. There are currently 17 identified SIPs.

10.3.3 International best practice for regional development

These are the best international practices for regional industrial development policies:

Best practice	Description
Good governance	Regional development strategies should be managed effectively and free of corruption. Democratic decision-making, transparency, financial management and control.
Integration	An integrated approach, ensuring that the benefits of one region spill over to other industries and areas.
Partnerships	Partnerships should be built between central government, local authorities, civil society, special interest groups, NGOs and the private sector.
Provision of resources	Sufficient resources should be provided in resource-poor areas, e.g. infrastructure, human resources.
Competitiveness	Industries or business established as a result of regional policies should be competitive and not need ongoing financial aid from government.
Development of people, for people, by people	Regional development concerns people, and aims to serve the people of the region. Training, education, improving productivity and providing essential goods and services to raise the standards of living in regions. People should be involved.
Development from below	Concentrate on issues at grass roots level where most urgent human needs exist. It starts by dealing with poverty.
Total development as a multi-dimensional process	Treat development from a global perspective covering all human life, including the interaction of special forces in a community, e.g. education, health, nutrition.

10.4 South Africa's endeavours

10.4.1 Spatial Development Initiatives (SDIs)

SDI is a policy to promote sustainable industrial development in areas where poverty and unemployment are at their highest. It can be defined as a link between important economic hubs and regions in a country. The main objective is to stimulate economic growth and employment in those regions.

These are the main SDIs and their economic focus:

SDI	Economic area
KwaZulu-Natal SDI	Industrial
Wild Coast SDI	Agri-tourism
Fish River SDI	Industrial
West Coast Investment Initiative	Industrials and agri-processing
Coast to coast Corridor	Transport and Tourism
Platinum SDI	Mining and agri-tourism
Phalaborwa SDI	Industrial and agri-tourism
Gauteng Special Economic Zone	Information technology, telecommunications
Maputo Development Corridor	Industrial and agri-processing
Lubombo SDI	Agri-tourism
Richards Bay Initiative	Mining, industrial and agri-processing

Financial incentives for SDIs:

- Duty-free incentives – duty-free import of raw materials or intermediate goods.
- Small and Medium Enterprise Development Programme (support operations).
- Skills support programme – tax-free grants for skills development.
- Critical infrastructure programme – cash grant to build or expand physical infrastructure.
- Foreign investment grants – cash grant to foreign companies that want to invest in new manufacturing businesses.

10.4.2 Industrial Development Zones (IDZ)

A purpose built industrial estate linked to an airport or seaport with export as the main objective (it will be incorporated into the SEZ in future).

These are the current IDZs in SA:

- Coega – Steel and auto components
- OR Tambo International Airport – high tech industries
- East London – vehicles
- Richards Bay – metals
- Saldanha Bay – steel

10.4.3 Special Economic Zones (SEZ)

Geographically demarcated area where specific economic activities have been identified to be developed. These areas may enjoy incentives such as tax relief and support systems to promote industrial development.

It creates a basis for a broader range of industrial parks and provides economic infrastructure to enable the effective clustering of value-adding and employment-enhancing manufacturers.

10.4.4 Corridors

A corridor is a track of land that forms a passageway allowing access from one area to another and is developed as part of regional development (also forms part of an SDI).

10.4.5 Strategic Integrated Projects (SIPs)

Integration of economic and social infrastructure projects in the country. There are currently 17 designated projects identified. The Strategic Integrated Projects main objective is to identify and implement projects to achieve the provisioning of infrastructure.

10.4.6 Infrastructure plan

The focus is on assessing infrastructure gaps and needs in terms of population growth. The main focus is on water, electricity, roads, sanitation and communication.

10.5 Incentives to encourage industrial development

10.5.1 Small Business Support Program

- This programme is designed for small businesses with assets of R100 million or less.
- This incentive consists of a tax free cash grant for investment in industries.
- Grants were available to new and expanding businesses.
- Grants are given for three years after which the company is expected to become self-sustaining.

10.5.2 Seda Technology Program (STP)

- STP was created as part of government's national strategy of consolidating and rationalising small enterprise support interventions across the different government departments and government agencies, within the overall objective of improving the delivery of small business support services to entrepreneurs and small enterprises.

10.5.3 Skills Development Programme (SSP)

- This a cash incentive to encourage greater investment in skills training and to introduce new, advanced skills to the SA labour force.
- A maximum of 50% of a company's trading costs are covered.

10.5.4 Critical Infrastructure Programme (CIP)

- It is a cost sharing grant for projects designed to improve infrastructure in SA.
- It covers a qualifying development cost between 10% and 30% towards the total development cost.
- It becomes available on completion of the project.
- It extends to both the public sector (e.g. municipalities) and private sector (companies).
- It is deemed “critical” if the investment had not taken place or would not work optimally without the infrastructure.

10.5.5 Custom free incentives

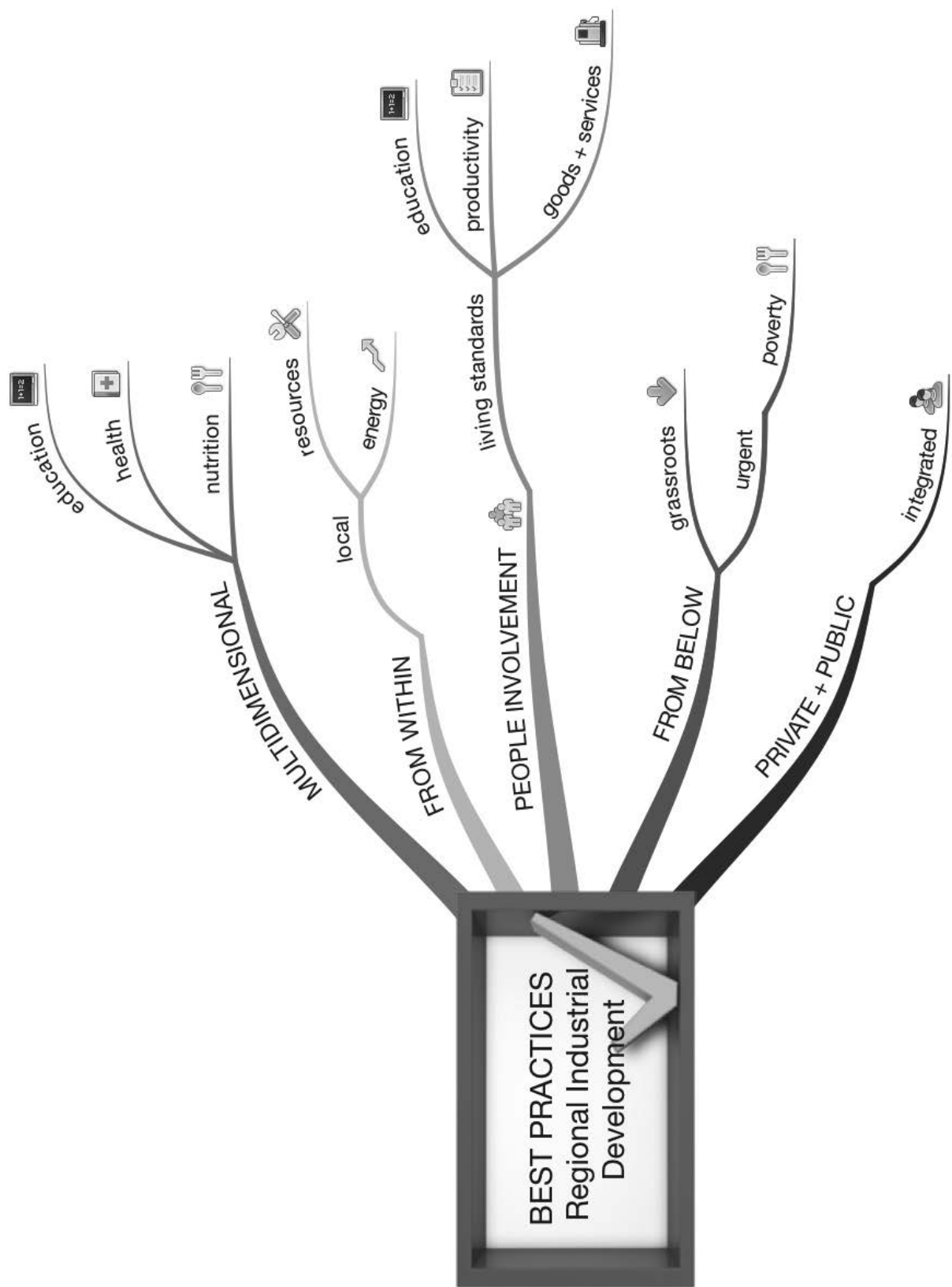
- These incentives are aimed at export orientated manufacturing businesses that operate in the IDZs and SEZs.
- Duty-free imports on intermediate products that will be used in the IDZ to produce other final goods.

10.5.6 Foreign investment incentives

- It is a cash incentive to assist foreign investors who want to invest in new manufacturing businesses in SA.
- It covers the cost of relocating new machinery and equipment from abroad.
- It becomes available to any registered company who would like to operate in the manufacturing sector.
- It also covers up to 15% of the costs of new machinery and equipment to a certain value.
- Strategic Investment Programme.

10.5.7 Services to business processes

- The BPS aims to attract investment and create employment in South Africa through off-shore activities.
- A base incentive as a tax exempt grant is paid over three years for each offshore job created and maintained.
- A graduated bonus incentive is paid as follows:
 - 20% bonus for more than 4 000 but less than 8 000 offshore jobs paid once off in a year in which the bonus is reached;
 - 30% bonus for more than 8 000 offshore jobs paid once off in the year in which the bonus level is reached.



10.6 Appropriateness of South Africa's industrial policies

10.6.1 Success factors

- **GEAR** did not do enough to promote development and an increase in economic growth did not occur.
- **Asgisa** policy was not successful in the main aim of reducing unemployment and increasing skills.
- The **New Growth Path** has not seen any decrease in the number of people who are unemployed.
- **The National Industrial Policy Framework** is an appropriate policy within best practice, but is hindered by an unemployment problem.
- **SDIs** the growth rate is lower than expected despite the huge amount spent on improvement on infrastructure in the SDIs. The main aim of creating employment has not been achieved.
- **IDZs** – growth has been very slow. The incentives offered were not attractive enough. Investors have not been attracted to Gauteng and Saldanha Bay as expected. Coega and Richards Bay have been more successful.
- **Regional development** is still uneven, concentrated mainly in the four metropolitan areas.
- **Workers** still have to move where employment is.
- **Small business development** – specific government programmes were successful. The promotion of entrepreneurship (amongst women and youth) have been reasonably successful. Improved access to finance and capital, information and advice have been reasonably successful.

10.6.2 External limitations

- **Global recession** had a severe negative effect on the manufacturing industry.
- **An unstable exchange rate** resulted in slow economic growth and development in the industrial sectors.

10.6.3 Internal limitations

- **Huge increase in electricity and logistic costs** – these price hikes affected smaller businesses and many more were forced into bankruptcy.
- **Skill shortages** – slow progress in addressing this need.
- **Infrastructure** – backlogs in expenditure at all government levels.
- **Restructural scale** – government sectoral programme to restructure the industrial economy was not of a significant scale for the structural scale envisaged.
- **Neglect of larger firms** – much emphasis has been placed on smaller firms and larger firms were neglected.
- **Uncompetitive behaviour of firms** – competition policy needs to be strengthened to counter high levels of industry concentration and anti-competitive behaviour.
- **Poor industrial financing** – insufficient financing to meet South Africa's investment and industrialisation challenges.

10.7 Appropriateness of South Africa's regional development policies

The **regional policy** is underpinned by most important international best practice principles: job creation, human development and macro- and microeconomic development. It focuses on:

- **Workers-to-the-work:** The priority is on employment creation. Workers have to move to where employment is.
- **Work-to-workers:** This is internationally regarded as the policy most likely to affect long-term problems of structural unemployment (unemployment resulting from a mismatch between demand in the labour market, and the skills and locations of workers).

10.8 Small business development policies

- The Department of Trade and Industry has various programmes in place to support SMMEs.
- The creation of employment for structurally unemployed people.
- Focus is on incentives for small businesses.
- Providing easier access to capital, information, business advice.
- Promotion of entrepreneurial development among women and the youth.

10.9 The appropriateness of black economic empowerment in the South African economy

- This strategy is in line with the empowerment of indigenous people in the development in developing countries. It is in line with the UN and World Bank development initiative of indigenous people in a country.
- Benchmark criteria.



Activity 1

Study the logos in **Figure 10.1** and answer the questions that follow:

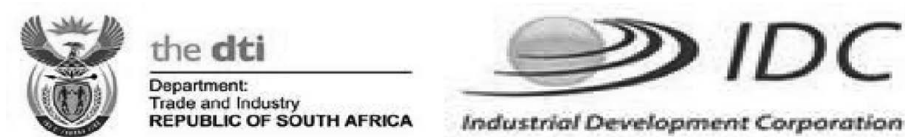


Figure 10.1: Logos

1. What government bodies do the acronyms in the logos stand for? (2)
 2. Define the concept industrial development. (2)
 3. Describe in your own words the important role of these institutions. (2)
- [6]

Answers to activity 1

1. DTI – Department of Trade and Industry✓
IDC – Industrial Development Corporation✓ (2)
 2. Refers to policies that are aimed at the encouragement of industrial investment and greater industrial efficiency. ✓✓ (2)
 3. They promote industrial development in underdeveloped regions.✓✓ (2)
- [6]



Activity 2

Discuss any TWO international best practices in terms of regional development. [8]

Answers to activity 2

1. **Total development as a multidimensional process** ✓✓ This is from a global development perspective. It includes all dimensions of human living, including the interaction of social forces in a community, e.g. education, health, nutrition.✓✓
 2. **Development from within** ✓✓ This is endogenous or independent development. In the past development programmes were forced upon regions. Now regions strive for independence with development assistance from outside included in their strategies. Local physical resources, human resources and energy are utilised.✓✓
- [8]



Activity 3

Explain the rationale of industrial development highlighting the past and present approaches. [8]

Answers to activity 3

1. **Past: Manufacturing development ✓✓** is a method to advance economic development. It is financed by foreign loans, aid and generous financial and other incentives received by businesses. ✓✓
2. **Present: Emphasis has shifted to industrial development ✓✓** – services and agricultural activities – focus on role for SMMEs – policies continue to exist – aim to export, employ and raise standard of living. ✓✓

[8]



Activity 4

Study **Figure 10.2** and answer the questions that follow:

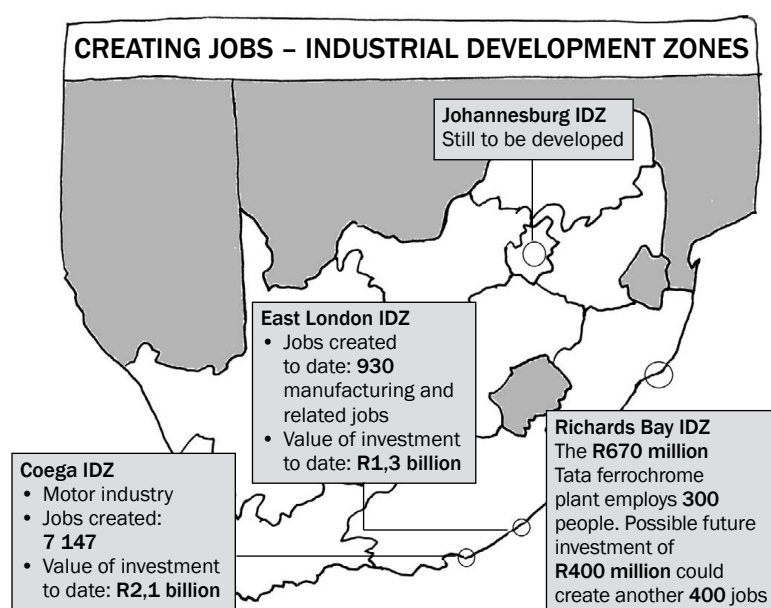


Figure 10.2: Creating jobs. Industrial development zones

1. Define the concept IDZ. (2)
2. List any TWO IDZ 's from the map. (2)
3. Mention the industry involved in TWO of the above mentioned IDZ's. (2)
4. Discuss an incentive applied to businesses within the IDZ. (4)

[10]

Answers to activity 4

1. Industrial Development Zones are purpose-built industrial estates that are physically enclosed and linked to an international port or airport. ✓✓ (2)
2. Johannesburg, ✓ Richards Bay, ✓ East London ✓ and Coega ✓ (any 2) (2)
3. Coega = motor industry ✓ and Richards Bay = metal industry ✓ (2)
4. No duties are paid on imported goods. ✓✓
Designed to encourage domestic and foreign businesses to open in an IDZ and produce goods and services for export. ✓✓ (4)

[10]



South Africa's economic and social indicators

Economic and social indicators are useful tools to determine a country's well-being. There are many economic and social indicators, including production, employment, education and demographic indicators.

Overview

TOPIC	CONTENT	SCOPE AND DEPTH OF EXAMINABLE CONTENT
11. Economics: basic concepts and quantitative elements: Economic and social performance indicators	Analyse South Africa's economic and social performance indicators and their uses <ul style="list-style-type: none"> • The Performance of an Economy <ul style="list-style-type: none"> – Performance – Comparisons – Specifications – Purposes • Economic Indicators: <ul style="list-style-type: none"> – Inflation Rate <ul style="list-style-type: none"> – Production prices (PPI) – Consumer prices (CPI) – Foreign Trade <ul style="list-style-type: none"> – Terms of trade – The exchange rate – Employment <ul style="list-style-type: none"> – Economically Active Population (EAP) – Employment rate – Unemployment rate – Productivity <ul style="list-style-type: none"> – Labour productivity – Remuneration per worker – Interest Rates <ul style="list-style-type: none"> – Repo Rate 	<ul style="list-style-type: none"> • Define/explain the relevant concepts • Broadly outline the performance of an economy <p>HOT QUESTION: Propose five considerations when assessing the performance of an economy</p> <ul style="list-style-type: none"> • Analyse the economic indicators in detail

	<ul style="list-style-type: none"> - Money Supply <ul style="list-style-type: none"> - M1 - M2 - M3 • Social Indicators: <ul style="list-style-type: none"> - Demographics <ul style="list-style-type: none"> - Population growth - Life expectancy - Nutrition and Health <ul style="list-style-type: none"> - Nutrition <ul style="list-style-type: none"> - Malnutrition - Obesity - Health <ul style="list-style-type: none"> - Infant mortality - Under 5 mortality - Spending on health - Access to clean water - Access to sanitation - Education <ul style="list-style-type: none"> - Percentage public sector spending - Percentage enrolment in Secondary Schools - Services <ul style="list-style-type: none"> - Electricity - Refuse/Garbage removal - Water supply - Sanitation - Housing and Urbanisation <ul style="list-style-type: none"> - Housing <ul style="list-style-type: none"> - Number of houses completed - Urbanisation <ul style="list-style-type: none"> - Natural growth in population - Migration - Founding of new towns • International Comparisons <ul style="list-style-type: none"> - Globalisation - International standardisation - Aid and support - Comparison and forecasting 	<ul style="list-style-type: none"> • Analyse the social indicators in detail <p>HOT QUESTION: Identify five social indicators that are used for international benchmarking and give an analysis of their importance</p>
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11.1 Key concepts

These definitions will help you understand the meaning of key Economics concepts that are used in this study guide. Understand these concepts well.

Term	Definition
Consumer Price Index (CPI)	Measures changes over time in the prices of an average market 'basket' of consumer goods and services purchased by households
Economically active Population (EAP)	All persons of either sex between the ages of 15 and 65 who supply labour for productive activities
International Monetary Fund (IMF)	An organisation working to promote employment, exchange rate stability, and international trade and economic cooperation by making financial resources available to member countries to meet their balance of payments needs
System of National accounts (SNa)	Techniques which include double-entry accounting, for measuring the economic activity of a nation
United Nations Children's Fund (UNICEF)	An international body working for the development of children's rights, and their survival and protection
World Bank	The international bank established to promote economic recovery and development

Use mobile notes to help you learn these key concepts. Learn more about mobile notes on page xiv in the introduction.



11.2 The performance of an economy

When we assess the economy, there are a few things that should be considered:

- **Performance**
Economic indicators are used to establish the state of the economy. An economic indicator is a statistic (data) that shows the behaviour of one or other variable.
- **Comparisons**
Changing statistics (data) inform us of changes in the economy. By comparing these changes we can determine whether there is a growth or slowdown in the economy.
- **Specifications**
To be meaningful, indicators have to be compiled in terms of their rules of compilation.
- **Purposes**
Indicators are compiled for specific purposes. Example, the CPI is calculated to show increases in consumer prices and reflect the cost of living.

11.3 Economic indicators

11.3.1 Price change indicators

Price increases occur either because of scarcities of a product or changes in consumer preferences. Price increases over long periods of time are known as inflation.

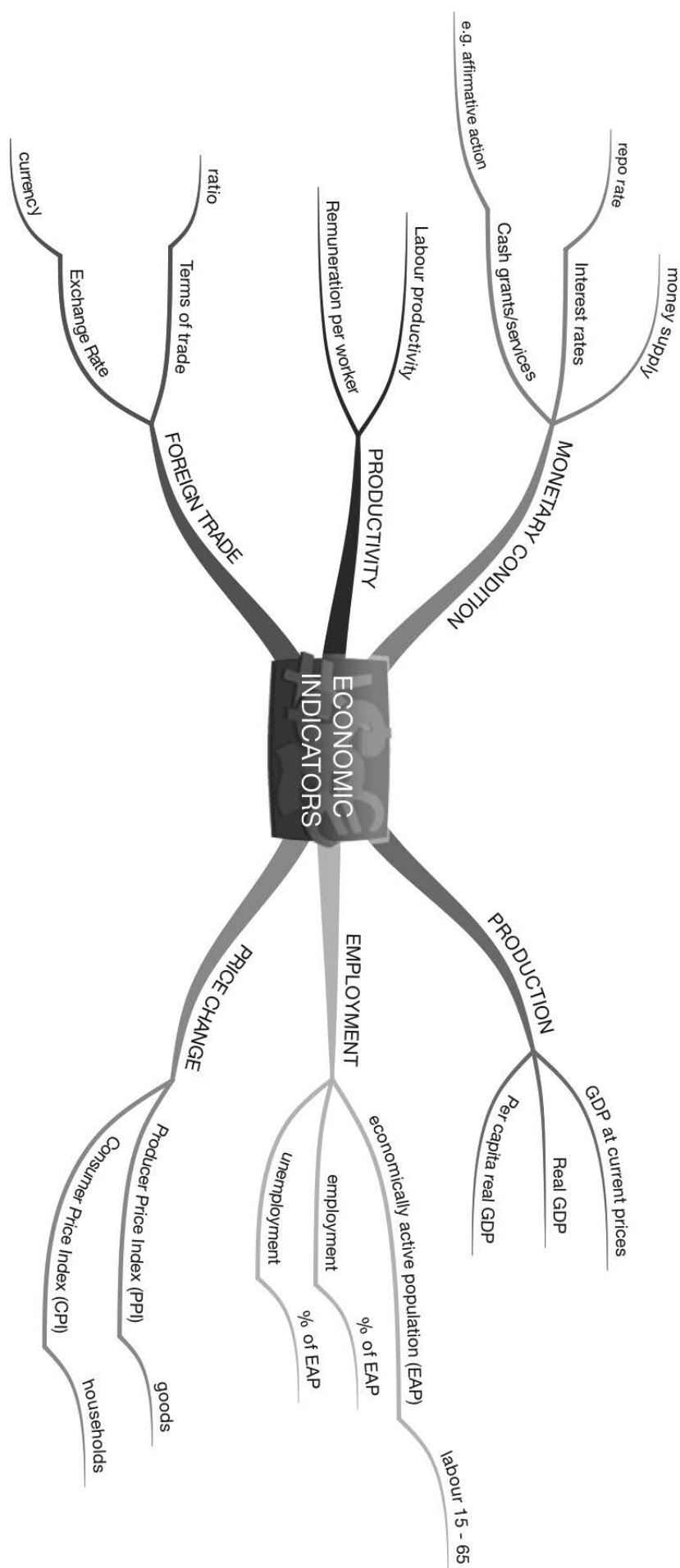
There are two key price change indicators:

- **Producer Price index (PPI):** This is the indicator used to measure an increase or decrease over time in the prices of goods produced locally when they leave the factory floor; and an increase or decrease in the price of imported goods.
- **Consumer Price index (CPI):** Weights are obtained from the expenditure of households and show changes in the purchasing power of the rand. This is the official index used in inflation targeting.

11.3.2 Foreign trade indicators

International trade is important in a globalised world. Exports stimulate employment and imports widen the choice of consumers.

- **Terms of trade:** The ratio of export and import prices. If the ratio deteriorates (gets worse), a greater volume of exports must be produced that may cause a spill-over effect into the balance of payments.
- **Exchange rate:** The value of one country's currency in relation to another country's currency.



11.3.3 Employment indicators

- **The economically active population (EAP):** The labour force between 15 – 65 years of age.
- **Employment:** The number of employed persons as a percentage of the economically active population (EAP), e.g. 73.5% in South Africa.
- **Unemployment:** The unemployed (who are actively looking for work) as a percentage of the economically active population.

11.3.4 Productivity indicators

Labour productivity is watched very closely, particularly in relation to real wage increases.

- **Labour productivity:** This is measured by dividing the real GDP by the number of workers employed.
- **Remuneration per worker:** If productivity increases are lower than the real wage increases, inflationary pressures will occur.

11.3.5 Interest rates

Interest is the charge made for borrowing money.

- **Repo rate** is one of the most important interest rate indicators. It is the rate at which the SARB lends money to banks.

11.3.6 Money supply

The supply of money is controlled by the SARB. The money is classified in three categories.

- **M1:** notes and coins in circulation and demand deposits of the domestic private sector at banks.
- **M2:** M1 plus other short term and medium term deposits of the domestic private sector at banks.
- **M3:** M2 plus long term deposits of the domestic private sector at banks.

11.4 Social indicators

Social indicators are concerned with people. They monitor identifiable and definable issues related to human well-being over a period of time.

11.4.1 Demographics

The size of the population is important for infrastructure and social programmes.

- **Population growth:** The population numbered 46.8 million in 2005. Growth is slowing down. Measuring population growth is important for delivering social services and for identifying the size of the tax base (the total number of people paying taxes).
- **Life expectancy:** South Africa's life expectancy rate is down from 62,8 years to 47 years.

11.4.2 Nutrition and Health

The standard of living of the population is related to the quality of nutrition and health:

Nutrition

- **Child malnutrition:** Malnutrition is expressed in two ways – weight for age (under weight) and height for age (dwarfism). The proportion of underweight children is the most important indicator of malnutrition.
- **Overweight children:** there is an association between obesity of children and other diseases.

Health

- **Infant mortality:** The number of children that will die before one year of age is one way of measuring the health of a population.
- **Under-five mortality:** the number of children that will die before the age of 5 years.
- **Health expenditure:** the amount of health expenditure as a percentage of GDP.
- **Access to safe drinking water:** the percentage of a population that has reasonable access to safe drinking water.
- **Access to sanitation facilities:** the percentage of a population with at least adequate sanitation facilities that can prevent human, animal and insect contact.

11.4.3 Education

The standard of living is related to the level of education. Education is a key social indicator:

- **Public expenditure:** The percentage of the national budget that is directed towards education.
- **Secondary enrolment:** This shows the percentage of an age group attending high school.
- **Primary completion:** The percentage of an age group that has completed primary education is an indicator of the efficiency of the education system.
- **Youth literacy rate:** The percentage of the 15–24 age group that are literate.

11.4.4 Services

A number of services that are vital to enhance people's lifestyle and level of economic and social development:

- Electricity
- Refuse removal
- Water supply
- Sanitation

11.4.5 Housing and urbanisation

The standard of living of the population is related to the quality of their housing and services:

Housing

- **Housing:** Many South African citizens are poor and cannot afford property. The government supplies housing subsidies and the private sector provides housing loans.

Urbanisation

The level of **urbanisation** is one of the indicators of a country's social development. It is measured by:

- Natural growth of the urban population
- Migration
- Establishment of new towns



Learn these four points that are used by international organisations to measure a country's level of economic and social development.

11.5 International comparisons

International comparisons are the key means of measuring a country's economic and social development.

11.5.1 Globalisation

- **International trade:** Payments are affected by the exchange rate.
- **Internationalisation:** Branch offices in foreign countries monitor indicators to publish financial reports in a single currency and pay dividends in different currencies.

11.5.2 International standardisation

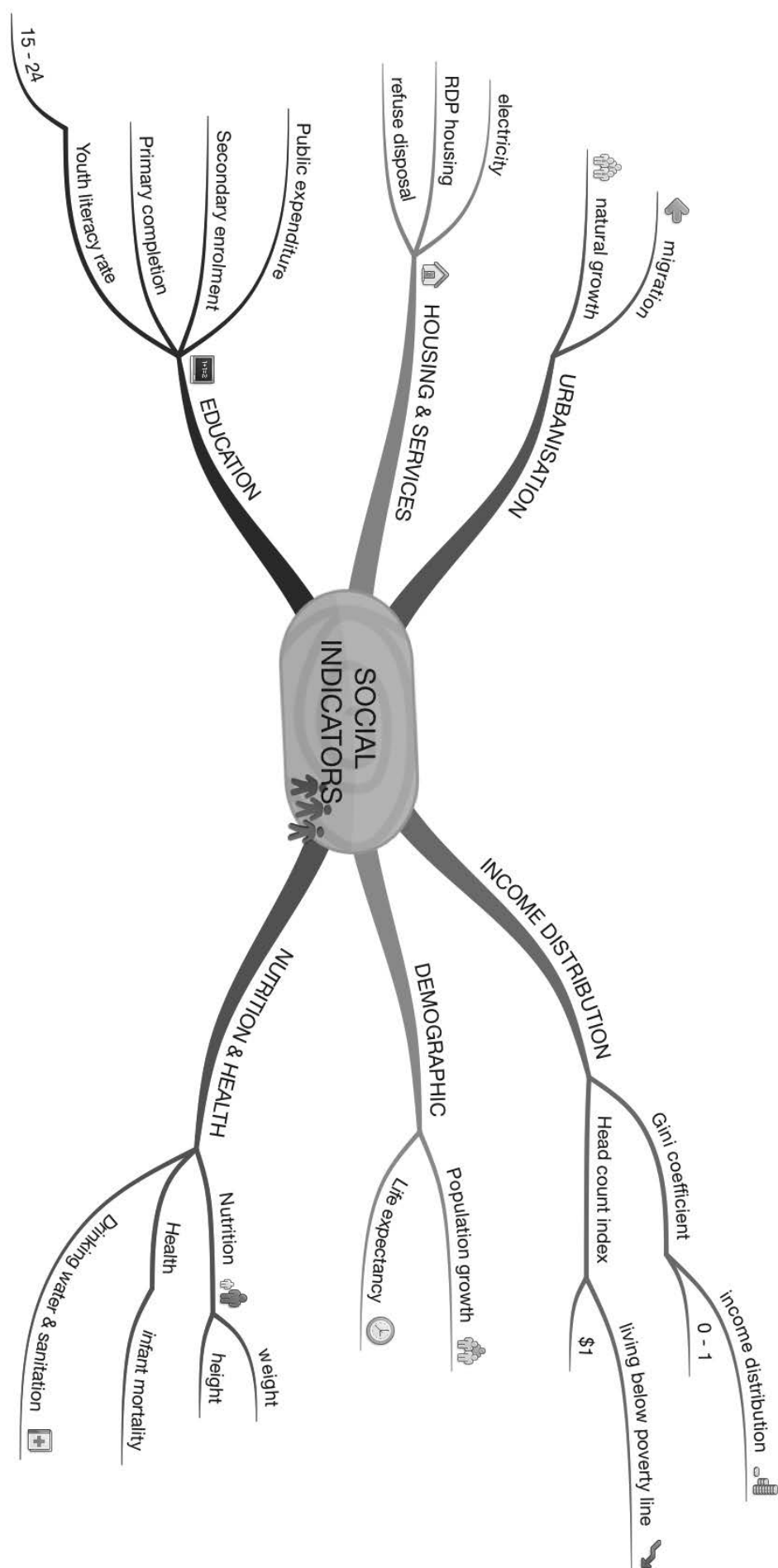
- Economic and social indicators are useful. International organisations, like the World Bank and the IMF, are very specific in determining, utilising and applying these indicators.
- Benefits from organisations cannot be measured if indicators are not available, e.g. bridging finance from the IMF, World Bank and the UN.

11.5.3 Aid and support

- Foreign countries, governments, international institutions and NGOs are globally involved in providing financial aid.
- A country needs indicators, including domestic income, production and expenditure, poverty, education and health data, to receive aid and to measure the impact of this aid.
- Human rights (children's rights), environment (pollution) and governance (corruption) indicators might also be requested by aid organisations.

11.5.4 Comparison and forecasting

- Capital markets are liberated through globalisation.
- Capital moves where it receives the best returns.
- Publications for global players give indicator values for the 3 previous and 3 future years to spot underlying trends.





Activity 1

Choose the correct word between brackets:

1. The key rate of interest in SA is the (repo/exchange) rate. (2)
2. The growth performance of a country is measured in terms of the (per capita real GDP/increase in the real GDP). (2)
3. The economically active population is the labour force between 15 and (55/65) years of age. (2)
4. The index used to determine the prices of inputs is called the (consumer/producer) price index. (2)
5. Social indicators are concerned with people, such as education and (corruption/health). (2)

[10]

Answers to activity 1

1. Repo rate ✓✓ (2)
2. Increase in the real GDP ✓✓ (2)
3. 65 ✓✓ (2)
4. Producer ✓✓ (2)
5. Health ✓✓ (2)

[10]



Activity 2

Give **ONE** answer for each of the following:

1. An international bank established to promote economic recovery and development (2)
2. Used to establish the performance of the economy in terms of basic economic objectives of growth, price stability, exchange rate stability and full employment (2)
3. It is depicted in the Lorenz curve and shows the distribution of income (2)
4. The price of one country's currency in terms of another country's currency (2)
5. Ratio of export and import prices (2)

[10]

Answers to activity 2

1. World Bank ✓✓ (2)
2. Economic indicator ✓✓ (2)
3. Gini coefficient ✓✓ (2)
4. Exchange rate ✓✓ (2)
5. Terms of trade ✓✓ (2)

[10]



Activity 3

Distinguish in tabular form between the Consumer Price Index and the Producer Price Index. (2 × 4) [8]

Answers to activity 3

PPI	CPI
<p>Producer Price Index: an index that assesses the impact of changes ✓ in the relative prices of production inputs ✓</p> <ul style="list-style-type: none"> • Relates to the cost of production ✓ • Basket consists of goods only ✓✓ • Capital and intermediate goods are included ✓✓ • Prices exclude VAT ✓✓ • Interest rates are excluded ✓✓ • Prices of imported goods are shown explicitly ✓✓ 	<p>Consumer Price Index: an index that measures the price ✓ of a fixed basket of consumer goods and services ✓</p> <ul style="list-style-type: none"> • Relates to the cost of living ✓ • Basket consists of consumer goods and services ✓✓ • Capital and intermediate goods are excluded ✓✓ • Prices include VAT ✓✓ • Interest rates are taken into account ✓✓ • Prices of imported goods are not shown ✓✓

[8]



Keep going!

12 Chapter

Inflation

Inflation occurs when there is a sustained and significant increase in the general price level over a period of time. At the same time, there is a decline in the buying power of money, i.e. the general price level increases more than the general increase in wages or salaries.

Overview

TOPIC	CONTENT	SCOPE AND DEPTH OF EXAMINABLE CONTENT
12 Economic Issues of the day: Inflation	<p>Analyse and investigate inflation and the policies used to combat it</p> <p>Inflation</p> <ul style="list-style-type: none"> • Definition • Measuring Inflation <ul style="list-style-type: none"> – Indexes (CPI/PPI) – Weighting (Basket of goods and services) – Inflation Rate (Calculations) • Types and Characteristics of Inflation <ul style="list-style-type: none"> – Consumer Inflation <ul style="list-style-type: none"> – Headline Inflation – Core Inflation – Administered Prices Inflation – Producer Inflation – All inclusive Inflation – Hyperinflation – Stagflation – Comparison of inflation rates • Causes and consequences of inflation <ul style="list-style-type: none"> – Demand-pull inflation <ul style="list-style-type: none"> – Monetarists explanation – Causes of demand inflation <ul style="list-style-type: none"> – Increase in household consumption – Decline in saving – Tax reduction – Access to credit – Investors expenditure – Government expenditure – Export services 	<ul style="list-style-type: none"> • Define/explain the concept • Examine ways to measure inflation • Define/explain the different types of inflation • Distinguish between the different types of inflation • Briefly discuss demand-pull inflation • Analyse the causes of demand-pull inflation

	<ul style="list-style-type: none"> - Cost-push Inflation <ul style="list-style-type: none"> - Causes of cost-push inflation <ul style="list-style-type: none"> - Wages - Key inputs - Exchange rate depreciation - Profit margins - Productivity - Natural disasters - Consequences of Inflation, on <ul style="list-style-type: none"> - Debtors/Creditors - Wage and salary earners - Investors and savers - Taxpayers - Industrial peace - Expectancy and Inflation <ul style="list-style-type: none"> • The inflation problem in South Africa • Measures to Combat Inflation <ul style="list-style-type: none"> - Demand-pull inflation <ul style="list-style-type: none"> - Monetary policy - Fiscal policy - Cost-Push Inflation <ul style="list-style-type: none"> - Productivity - Competition 	<ul style="list-style-type: none"> • Briefly discuss cost-push inflation • Analyse the causes of cost-push inflation <ul style="list-style-type: none"> • Examine in detail the consequences of inflation <ul style="list-style-type: none"> • Broadly outline the inflation problem in South Africa • Examine the measures to combat inflation in detail • Use the following information to calculate the CPI for September 20... <p>HOT QUESTION: What effects does inflation have on the current account of the South African BoP?</p>
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12.1 Key concepts

These definitions will help you understand the meaning of key Economics concepts that are used in this study guide. Understand these concepts well.

Term	Definition
Administered prices	Prices set or controlled by government
Core inflation	Excludes items from the CPI basket that are highly volatile or prices affected by government policy
Cost-push inflation	Occurs when there is an increase in the general price level caused by an increase in the cost of production
Consumer Price Index (CPI)	An index that measures the price of a fixed basket of consumer goods and services <ul style="list-style-type: none"> • Relates to the cost of living • The basket consists of consumer goods and services • Capital and intermediate goods are excluded • Prices include VAT • Interest rates are taken into account • Prices of imported goods are not shown
Demand-pull inflation	Occurs when the aggregate demand for goods and services exceeds the aggregate supply of goods and services
Headline inflation	Unadjusted CPI figures
Hyperinflation	An inflation rate above 50%. People lose confidence in the value of money and start bartering goods and services
Inflation	A sustained and significant increase in the general price level over a period of time; and a simultaneous (at the same time) decline in the buying power of money
Inflation targeting	Forms part of monetary policy and is managed by the Reserve Bank to keep inflation within the range as set by the Minister of Finance (between 3% and 6%)
Monetary Policy Committee (MPC)	Consists of the Governor of the Reserve Bank, 3 deputy governors and another 3 members. Their main purpose is to determine an interest rate that will be consistent with meeting the inflation target
Producer Price Index (PPI)	Assesses the impact of changes in the relative weighting of production inputs: <ul style="list-style-type: none"> • Pertains to the cost of production • The basket consists of goods only • Capital and intermediate goods are included • Prices exclude VAT • Interest rates are excluded • Prices of imported goods are shown explicitly
Stagflation	Low growth, high unemployment and high inflation rates occur simultaneously

Monetary Policy in South Africa is formulated and implemented by SARB within an inflation targeting framework. SARB works closely with Treasury, but it has operational independence.



12.2 Measuring inflation (define, explain, examine)

Price indexes are used to measure the changes in the general price level. The following are important concepts related to measuring inflation:

1. **Indexes:** A price index is compiled by using the prices of a representative range of goods and services which are recorded on a regular basis.

2. **Weighting:** The difference in the importance of items in an index is solved through a weighted index which reflects the relative importance of each item.
3. **Inflation rate:** The inflation rate is determined by using changes in the CPI and/or PPI index. The figures for each month are compared to the corresponding month in the previous year.
4. **Inflation targeting:** Forms part of monetary policy set by government and is managed by the Reserve Bank to keep inflation within the range as set by the Minister of Finance (between 3% and 6%). The aim of inflation targeting is to keep the inflation rate at low and more stable levels.

The main way in which inflation is measure are:
Changes in CPI; Changes in PPI; Changes in implicit GDP deflator



12.3 Types and characteristics of inflation

There are two main types of inflation – demand-pull inflation and cost-push inflation. Their characteristics are explained below:

12.3.1 Consumer inflation

- **Headline inflation:** it is measured by the CPI and is calculated for urban areas only. It represents the cost of a shopping basket of goods and services of a typical SA household. Stats SA identifies 1 500 different consumer goods/services, assigns a weight to each, decides on a base year, on formula and on the collection of prices. The unadjusted CPI rate is known as headline inflation.
- **Core inflation:** it is published by Stats SA and excludes items from the CPI basket with highly volatile prices and those affected by government intervention and policy, e.g. fresh and frozen meat and fish, vegetables, interest rates on mortgage bonds, VAT and assessment rates.
- **Administered prices:** the prices are set by government or controlled by government through appointed authorities. Price changes must remain within the inflation target prescribed by the Minister of Finance.

12.3.2 Producer inflation

PPI is used to measure the prices of domestically produced goods. It also shows domestic output. When the rand depreciates it will first be reflected in the PPI.

Differences between CPI and PPI:

CPI:

- Pertains to cost of living
- Basket consists of consumer goods and services
- Capital and intermediate goods are excluded
- Prices include VAT
- Interest rates are taken into account
- Prices of imported goods are not shown

PPI:

- Pertains to cost of production.
- Basket consists of goods only.
- Capital and intermediate goods are included.
- Prices exclude VAT.
- Interest rates are excluded.
- Prices of imported goods are shown explicitly.

12.3.3 All-inclusive inflation

- Economists check what happened to prices of all final goods and services produced in a particular year.
- Use the calculated implicit GDP deflator.
- GDP figures at current and constant prices are used as published in the national accounts.
- GDP at constant prices measures economic growth and measures inflation.
- Measures the inflation rate for economy as a whole.
- Implicit GDP deflator is the ratio of GDP at current prices to GDP at constant prices.
- To determine inflation: $\frac{\text{GDP deflator for next year}}{\text{GDP deflator for previous year}} \times 100$.

12.3.4 Hyperinflation

- Very high rate of inflation (more than 50%).
- Price levels rise so rapidly that people lose confidence in the value of money.
- Becomes difficult for the economy to operate.
- People resort to goods as medium of exchange – barter.

12.3.5 Stagflation

A low growth rate, high unemployment and high inflation rate.

12.3.6 Comparison of inflation rates

- Annual inflation rates of CPI, PPI and GDP deflation are provided.
- For policy purposes and forecasting all these indexes as well as other implicit deflators are considered.
- For the consumer the CPI is by far the most important indicator because it relates to their cost of living and the interest rate policy of the Reserve Bank.

12.4 The causes of inflation

12.4.1 Demand-pull inflation

Demand-pull inflation occurs when aggregate demand in an economy outpaces (is faster than) aggregate supply, even though gross domestic product rises and unemployment falls. Effectively, too much money is spent chasing too few goods. Generally, an increase in the supply of demanded goods will reverse the inflationary trend. Some of the characteristics of demand-pull inflation are:

- Aggregate demand rises more than aggregate supply, causing an increase in the general price level.
- **Groups that are responsible:** Consumers, businesses and government.
- **Foreigners' contribution:** They further increase the demand for our goods and services through an increase in exports.
- **Relative increase in aggregate demand's components:** C (consumption spending), I (investment spending), G (government spending), M (cost of imports).
- **Decline savings:** if savings habits are changed and consumers start spending their current and accumulated savings, growth in aggregate demand can outstrip growth in aggregate supply

Note that demand inflation is the same thing as demand-pull inflation. Cost inflation is the same thing as cost-push inflation.



- **Tax reduction:** If personal income tax is reduced more money is available for private consumption expenditure.
- **Access to credit:** Greater availability of consumer credit (credit cards) and cheaper credit – credit multiplier kicks in and more credit is created.

- Figure 12.1 illustrates an increase in aggregate demand from AD_1 to AD_2 and a single aggregate supply AS_1 . As the aggregate demand increases, the price level and production output will also increase until full employment is reached. The initial increase in demand will have a positive influence on production, employment and income, but when full capacity is reached further increases in demand will lead to price increases.

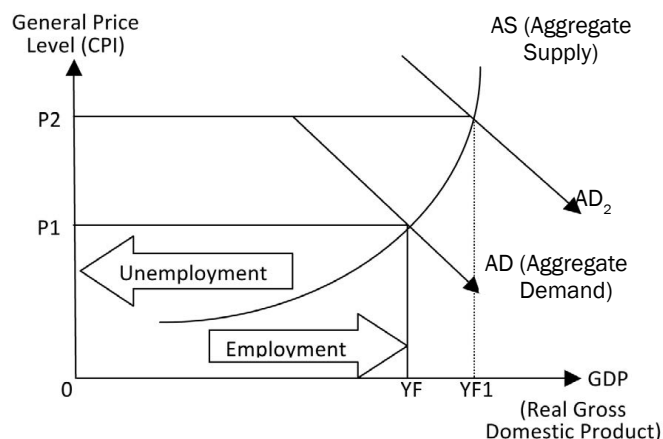


Figure 12.1: The inflationary process

Causes of demand-pull inflation

There are many causes of demand-pull inflation.

Some of these are:

- **Increase in household consumption:** due to easily available credit, a reduction in taxes and less savings.
- **Investors expenditure:** may lead to higher profit expectations of businesses. They will invest more, this might lead to an increase in the demand for goods and services.
- **Government expenditure:** an increase in government spending leads to an increase in prices. More money comes into circulation due to an increase in spending on infrastructure, consumption spending and social spending.
- **Export earnings:** the growth in foreign countries might create an increased demand for locally produced goods without an increase in production.
- **The Monetarist explanation:** According to the monetarists sustained high rates of growth in the money supply cause high inflation, while low rates of growth cause low inflation. They base their view on the quantity theory of money ($MV = PT$). They make three basic assumptions: the velocity of circulation of money is stable; the quantity of money is exogenously determined by monetary authorities and real output is determined by the quantity and quality of various factors of production.

12.4.2 Cost-push inflation

Cost-push inflation is caused by an increase in the cost of goods or services that are very important to the economy, and for which no alternatives exist. Examples can be spikes in the oil price due to war, huge price rises in essential food products due to drought, or excessive increases in the cost of labour due to control of industries by trade unions. Some of the characteristics of cost-push inflation are:

- **An increase in labour costs:** Aggressive trade union negotiations push the price of labour up above the increase in productivity.
- **Producers increase profits:** Prices rise more than the rise in production costs.
- The state imposes a **higher VAT rate**.



- **Expensive imported products** (intermediate goods) cause an increase in the prices of locally finished goods.
- **Lower productivity but the same remuneration:** The cost of production increases.
- **Natural disasters:** Floods or droughts increase the cost of production.
- Increased total costs on the supply side.

Causes of cost-push inflation

- **Wages:** an increase in wages constitutes 50% of GVA at basic prices and is one of the major causes of cost-push inflation.
- **Key inputs:** When the prices of key input goods that are imported, increase, domestic cost of production increases especially in the manufacturing sector.
- **Exchange rate depreciation:** The depreciation in the rand will lead to more expensive imports.
- **Profit margins:** When businesses increase their profit margins, their cost of production and prices consumers must pay, will also increase.
- **Productivity:** Less productive factors of production will lead to increased cost per unit.
- **Natural disasters:** Prices will increase due to weather changes such as droughts, floods and global warming.

Expectancy and inflation

The inflationary process is triggered by demand pull and cost push inflation. The role of inflationary expectations:

- during inflation consumers expect prices to rise and start to buy more goods
- labour unions wish to protect their members' income against erosion of purchasing power caused by inflation
- expectation that wages will rise encourages some businesses to increase prices in advance.

SUMMARY: Fiscal policy makes use of **tax increases** and **spending cuts** to combat inflation.

12.5 The consequences of inflation

- **Debtors/Creditors:** debtors benefit because they receive money with a high purchasing power and repay their debt with money with low purchasing power. Creditors on the other hand suffer.
- **Wage and salary earners:** people with a fixed income will be able to purchase less as prices are rising.
- **Investors and savers:** Assets with a fixed nominal value have a fixed return and lower purchasing power as prices increase. Real value of savings decreases.
- **Tax payers:** In South Africa income is taxed on a progressive system. We experience a bracket creep, resulting from inflation and progressive income tax and the government benefits.
- **Disruption of industrial peace:** Wage bargaining is accompanied by strikes and mass action.

12.6 Measures to combat inflation

Policy makers can use various policy measures to fight inflation when it gets too high. Three types of policy measures are highlighted.

12.6.1 Fiscal measures

Fiscal measures are measures taken by the Minister of Finance regarding taxation and expenditure. Examples of measures that can be taken include:

- An increase in **direct taxation** (personal income tax) which will help to decrease demand.
- An increase in **indirect taxation** (VAT) causes spending to decrease because goods become more expensive.
- A **loan levy**. Reduces the disposable income of consumers.
- **The state cuts back on expenditure** by cancelling government projects like roads, hospitals and schools.
- **The country's finance budget deficit is non-inflationary** (the government uses loans from the non-banking sector to limit inflation).
- **The state imposes surcharges** on imported goods. This increases the price of these imported goods, resulting in many people being unable to afford to buy these goods.

SUMMARY: Monetary policy involves **reducing money supply** to combat inflation.

12.6.2 Monetary measures

The South African Reserve Bank (SARB) and the government apply certain monetary measures to curb inflation:

- The SARB **adjusts the quantity of money to the needs of the economy**, (e.g. through open-market policy, thus maintaining a fine balance) between the supply of goods and services and money supply.
- The SARB **curbs inflation** caused by excess demand by reducing the money supply.
- The **bank rate** of the central bank (SARB) affects the interest rates in the economy (repo rate). The bank rate can be raised to encourage savings.
- Excessive credit can be reduced by **restricting the granting of credit** by banks.
- The SARB can apply **moral pressure** (moral suasion) on financial institutions to be more careful when granting credit.

12.6.3 Other measures

Additional measures that can be taken to combat inflation include:

- **Increase productivity:** This is a long-term measure generated through improved education and training which allows more people to be employed and ensures they are more productive.
- **Price control:** By fixing the price of certain essential goods, the government assures they remain affordable.
- **Wage policy:** The government takes a decision to break the inflationary spiral of increased wages and prices by keeping the increase in wages below or at the level of inflation.
- **Stricter conditions for consumer credit:** The government makes it harder for consumers to get credit in order to restrict their spending.
- **Encourage personal savings:** The government implements measures to encourage savings, e.g. by cutting taxes on savings. The imbalance between demand and supply is corrected by increased savings, as people save more and spend less.
- **Import controls** are relaxed.
- **Floating exchange rate:** Prices are automatically adjusted to international conditions.
- **Indexation:** A policy of linking prices of items such as wages, pensions and mortgage bond interest rates to price indices to eliminate the effects of inflation.

Use the following word acronyms to help you remember these additional measures to combat inflation:

W – Wage
I – Import
P – Productivity
E – Exchange rate

S – Savings
C – Credit
I – Indexation
P – Price



Activity 1

Study Figure 12.2 below and answer the questions that follow:

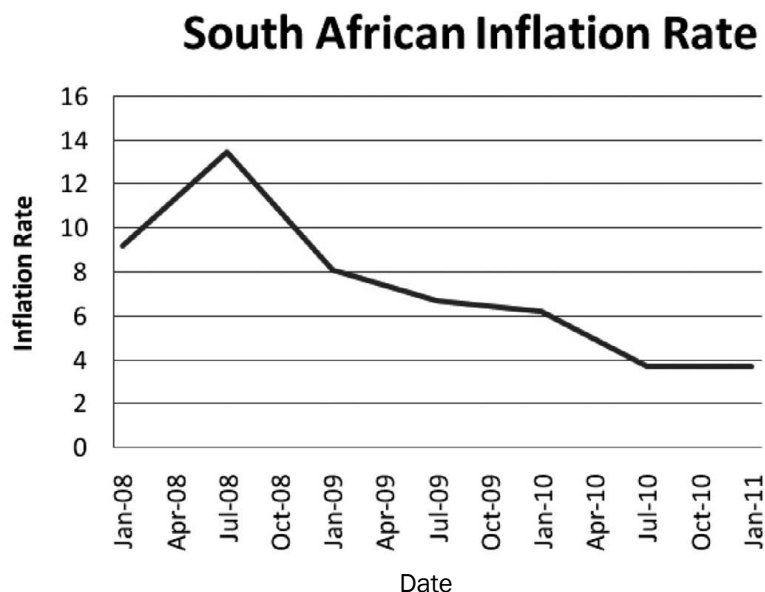


Figure 12.2 South Africa's inflation rate

1. Define the concept inflation. (2)
2. When did the inflation rate peak? (2)
3. Do we adhere to the inflation target set by government from July 2010–Jan 2011? Supply figures. (4)
4. Explain what you would do to lower the inflation rate in our country? (4)
5. Which institutions in South Africa make inflation figures available? (2)
6. What, according to you, caused the double figures in April–July 2008? (4)
7. Why are these figures in the graph not a reflection of hyperinflation? (4)

[22]

Answers to activity 1


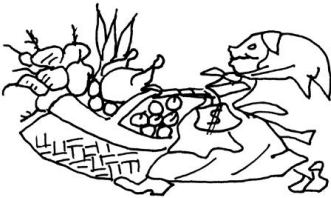


1. A sustained and significant increase in the general price level over a period of time. ✓✓ (2)
2. July 2008 ✓✓ (2)
3. Yes ✓✓ Inflation target between 3 – 6 % ✓✓ (4)
4. Apply monetary (repo rate) ✓✓ and fiscal policies (tax increases) ✓✓ (4)
5. SARB and Stats SA ✓✓ (2)
6. Excessive consumer spending. ✓✓ Due to the capital expenditure by the state for the Soccer World Cup ✓✓ (4)
7. Hyperinflation starts at 50% ✓✓✓✓ (4)

[22]



Activity 2

Study the cartoon below and answer the questions that follow:

	
<p>Before inflation - she goes to the market carrying her money in her HANDBAG</p>	<p>And brings her groceries home in a BASKET</p>
	
<p>After inflation - she carries her MONEY in a basket, and.....</p>	<p>Brings her groceries home in her HANDBAG</p>

1. What is the message behind the cartoon? (2)
 2. What is happening to the purchasing power of the money? (2)
 3. In which country is this woman a consumer? Motivate your answer. (4)
- [8]

Answers to activity 2

1. Due to inflation, the consumer can buy less for the same amount ✓✓ (2)
 2. Declining ✓✓ (2)
 3. USA ✓✓ She is carrying US Dollars (\$) in her basket ✓✓ (4)
- [8]



Activity 3

Name any THREE fiscal measures to control inflation. (3 × 2) [6]

Answers to activity 3

Increase direct taxation (personal income tax) if inflation is due to excess demand ✓✓

- Increase indirect taxation (VAT) ✓✓
 - A loan levy is introduced ✓✓
 - The state cuts back on expenditure ✓✓
 - The finance budget deficit is non-inflationary ✓✓
 - Impose surcharges on imported goods ✓✓
- (any 3) (3 × 2)

[6]



Tourism

Tourism is travel for the purpose of leisure, recreation or business. Local tourists travel to different places in their own country. **Inbound tourists** come to South Africa from other countries. South African tourists who travel overseas are known as **outbound tourists**. South Africa is a popular tourist destination because of its beauty, wildlife, good weather and its interesting political history.

Overview

TOPIC	CONTENT	CONTENT DETAILS FOR TEACHING, LEARNING AND ASSESSMENT PURPOSES
13. Tourism and Economic Redress: Environmental sustainability	<p>Debate the economic importance of tourism to South Africa and suggest policies to promote it, also refer to the importance of indigenous knowledge systems (IKS)</p> <p>Tourism:</p> <ul style="list-style-type: none"> • Definition • Types of tourism • Measuring tourism <p>• Reasons for its Growth</p> <ul style="list-style-type: none"> – International – Domestically <p>• The Effects of Tourism on:</p> <ul style="list-style-type: none"> – GDP – Employment – Poverty – Externalities – Environment – Investment <p>• The Benefits of Tourism for:</p> <ul style="list-style-type: none"> – Households – Businesses – State – Infrastructure Development <p>• South Africa's profile (indigenous knowledge systems)</p> <ul style="list-style-type: none"> – South Africa's Profile – Aim with visits – Local Destinations – Local Tourists – Indigenous Knowledge <p>• Policy Suggestions – Department of Tourism</p> <ul style="list-style-type: none"> – Marketing, infrastructure, education and training and environmental management 	<ul style="list-style-type: none"> • Define/explain the relevant concepts • Broadly outline the types of tourism • Broadly outline the measuring of tourism <ul style="list-style-type: none"> • Examine the reasons for growth in the tourism industry in detail <ul style="list-style-type: none"> • Examine the effects of tourism in detail <ul style="list-style-type: none"> • Examine the benefits of tourism on: Households, Businesses, Government and Infrastructure development <ul style="list-style-type: none"> • Broadly outline the tourism profile of South Africa <ul style="list-style-type: none"> • Broadly outline the Department of Tourism's policy suggestions • Briefly analyse the relationship between tourism and indigenous knowledge within the South African context

Use mobile notes to help you learn these key concepts. Learn more about mobile notes on page xiv in the introduction.



13.1 Key concepts

These definitions will help you understand the meaning of key Economics concepts that are used in this study guide. Understand these concepts well. Use mobile notes to help you remember them.

Term	Definition
Domestic tourist	South African citizens travelling within the borders of South Africa
Department of Tourism	Ensures and accelerates (speeds up) the delivery of tourism benefits
Foreign tourist	Visits a foreign country as a destination
Inbound tourist	Tourists from other countries (foreign tourists) who stay for more than one day
Outbound tourist	South African citizens travelling abroad. They have the same effect as imports on the balance of payments
Tourism	Activities of people travelling to and staying in places outside their usual environment for no more than one year for leisure, business and other purposes. It does not relate to any work done for money in the place visited
Transit tourist	Tourists travelling through South Africa using air, road, rail and sea transport to get to another destination

13.2 Definition of tourism

Tourists travel to foreign countries for holidays, business, conferences and to discover more about other countries. **Tourism** allows people to experience the world. Tourism can be defined as activities of people travelling to places outside their usual environment for less than one year for business, leisure or other purposes without any remuneration.

An activity is seen as tourism if it fits in with the following criteria:

- There is a purpose for the visit or activity.
- There is no remuneration (money) earned in the place visited.
- A minimum length of stay is one night.
- A maximum length of stay is one year.
- There is a travelling distance of more than 160 km from the tourist's home environment.

13.3 The purposes (types) of tourism

- **Leisure and recreation:** Tourists come to South Africa on holiday, to play sport, to visit friends, and to see the tourist attractions
- **Cultural tourism:** Tourists come to visit museums and art galleries, e.g. Robben Island and the Apartheid Museum.
- **Ecotourism:** Tourists visit undisturbed natural areas, e.g. the Richtersveld Cultural and Botanical Landscape, the Cape Floral Region Protected Areas and the Kruger National Park.
- **Business and professional:** Tourists visit for business meetings and conferences.
- **Other:** For studies, or medical reasons.



Leisure and recreation



Cultural tourism



Ecotourism



Business and professional

13.4 Measuring tourism

Tourism consists of different activities that should comply with the following:

- There should be a purpose for the visit e.g. camping, business or studies.
- No remuneration should be earned at the tourist destination.
- A minimum length of stay should be one night.
- The maximum length of stay should not exceed one year.
- The travelling distance should exceed 160 km from a person's residence.

13.5 Reasons for growth

The rapid growth in the tourism industry has resulted in a steady change in the standard of living as well as people's lifestyles. Tourism is much more evident in the developed than developing countries, although tourism is increasing faster in the developing countries. Local tourism is booming since South Africa is becoming more attractive as tourist destination.

Reasons for the growth of the tourism industry are:

- Increased disposable income.
- Less working hours so more time to travel.
- An awareness of leisure and recreation.
- Improved transport, communication and accommodation facilities.
- Increased advertising and promotion.
- Enjoying the benefits of holidays and travel.
- Easily obtainable foreign exchange.
- **International:** tourism is much more evident in the developed than developing world, but tourism is growing faster in developing countries, e.g. 4.6% growth from 2010 to 2011.
- **Locally:**
 - **Foreign arrivals:** foreign tourists who visit the country as their destination.
 - Those who are stopping over, are called transit tourists or same-day travellers.
 - **Foreign tourists:** come for the experience – visit friends, game farms, enjoy the different cultures, heritage spots or sports activities and events.
 - **Domestic tourism:** South Africans are free to travel locally (domestic tourists) or abroad (outbound tourists). Outbound tourists have the same effect on the Balance of Payments as imports.

Use the acronym PIGEEE to help you remember the 6 effects of tourism:

P – Poverty

I – Infrastructure

G – GDP

E – Employment

E – Environment

E – Externalities

13.6 The effects of tourism

Tourism has a significant effect on the economy and the country as a whole. The following **6 areas** are greatly affected by tourism:

13.6.1 Employment

- Tourism employs 7% of South Africa's workforce (approximately 1,12 million people).
- Tourism is the largest provider of jobs because it:
 - Is labour intensive.
 - Employs many different kinds of skills, e.g. tourist guides, hotel staff.
 - Provides immediate employment.
 - Provides entrepreneurial opportunities.
- Tourism is the largest earner of foreign exchange because:
 - Foreign tourists pay for services in foreign exchange.
 - Foreign tourists usually spend more than local tourists.

13.6.2 Gross domestic product (GDP)

- Tourism has the biggest impact on the services industry.
- Indirect contribution: Tourism is a service-based industry. It is responsible for 65% of the GDP in developed economies and 40% of the GDP in developing countries.
- Direct contribution: Tourism contributes 7,9 % of GDP in South Africa (compared to 12% worldwide).

13.6.3 Poverty

Poverty is most evident in rural areas due to a lack of job opportunities. Tourism can alleviate (ease) poverty in the following ways:

- Tourism is a fast and effective mechanism for distributing resources to rural areas to develop them as tourist sites.
- Many prime tourist attractions are located in rural areas.
- Tourist developments in rural areas increase the number of available jobs in areas where there aren't many jobs.
- Tourism promotes a balanced and sustainable form of development. People are able to earn a living in their home areas, resulting in a reduction in urbanisation and a more balanced population distribution.

13.6.4 Externalities

Externalities are costs and benefits that result from a specific activity. Tourism results in both:

Positive externalities:

- Tourism attracts large amounts of revenue.
- Tourism leads to an improvement in infrastructure development.
- Tourism can stimulate employment indirectly.
- Tourism can help conserve cultural and natural assets and alleviate poverty, but needs to be carefully planned.

Negative externalities:

- Tourism can cause environmental damage if not managed correctly.
- Tourism can result in a lot of waste and damage to sensitive tourist sites.
- The infrastructure at tourist sites can come under pressure to cater for increased tourist numbers.
- Tourism can lead to increased prices for locals.

13.6.5 The environment

Tourism can create environmental stress. It can result in:

- Permanent restructuring of the landscape, e.g. construction work on highways.
- Additional waste products, e.g. biological (sewage) and non-biological (litter) waste.
- Direct environmental stress, e.g. the loss of wildlife species due to safari hunting.
- Effects on population dynamics, e.g. migration and changes in population density in response to the needs of tourist sites.

13.6.6 Investment

Tourist destinations require adequate physical (hotel rooms), economic (ATMs) and basic (water and electricity) services infrastructure. This includes:

- Transport infrastructure, e.g. improved roads are needed to access tourist sites.
- Communication infrastructure, e.g. hotels need telephone lines to take bookings at tourist sites.
- Energy infrastructure, e.g. tourists need electricity at tourist sites.
- Basic services, e.g. clean water and refuse removal.

Use this mnemonic to help you remember the 4 benefits of tourism:

H – Households – HOT

B – Businesses – BEACHES

I – Infrastructure – IN

G – Government – GEORGE

13.7 The benefits of tourism

South Africa benefits from tourism through the growth in the gross domestic product (GDP), employment and infrastructure development. An additional benefit is that spending by foreign tourists results in an increase in foreign exchange earnings, which has a similar impact on the GDP to an increase in exports.

13.7.1 Households

Tourism benefits a household's prosperity (wealth) in three ways:

- **More people earn salaries and wages** because of additional job opportunities.
- **Infrastructure** built for tourists is available both for tourists and local people's use.
- **Skills:** A variety of skills is required in the tourism industry.

13.7.2 Businesses

Tourism has many benefits for the business sector:

- The economic and basic services infrastructure required for tourism is provided by the public sector.
- Tourism needs superstructure, which consists of businesses that provide accommodation, transport, built attractions, retailing and recreation services.
- Superstructure is normally supplied by the private sector, and the building and running of the superstructure make profits.
- Public and private sector partnerships (PPPs) are used to develop tourist destinations.
- Other work opportunities become available for the previously disadvantaged. These include:
 - Employment opportunities in entertainment, laundry and transportation.
 - Business opportunities in car rental, arts, craft and curio sales.

13.7.3 Government

The main benefit to government is in the levying (charging) of taxes. This has two purposes:

- **To recover external costs:** To compensate the host community for providing infrastructure.
- **To raise revenue:** Tourists are seen as part of the overall tax base (e.g. airport departure taxes and hotel tourism levies increase the amount of taxes collected).

13.7.4 Infrastructure development

South Africa benefits from tourism because all infrastructure built to support tourism becomes an asset to the country.

As a result:

- Residents and visitors enjoy adequate and well-maintained physical and basic services infrastructure.
- The Department of Transport prioritises economic infrastructure. Spatial Development Initiatives and economic corridors focus on tourism, and public and private sector partnerships (PPPs) are used for the development of infrastructure.

- Tourists require social infrastructure – ambulances, medical clinics, police protection services and information services – that becomes a national asset.

13.8 A South African tourism profile

1. Aim with visits: most foreign tourists visit South Africa for vacation (94.3%) and business (2%). The major attractions are the coast, wildlife and scenery.
2. Local destinations: Destinations link all aspects of tourism – demand, supply, transport, accommodation and marketing. The success of tourism is determined by the variety of destinations as well as the geographical distribution of tourist destinations.
3. Local tourists: There has been a steady growth in the number of South Africans travelling domestically.
4. Indigenous knowledge
 - Tourists want to understand the indigenous (local) culture, history and environment.
 - Tourists seek authentic (genuine) and unique destinations. They want to see how local people live and work.
 - The Khoi San are among the world's oldest people, and their way of life is of interest to many foreign tourists.

World heritage sites:

- Mapungubwe (Limpopo)
- Vredefort Dome (Free State and North West)
- Sterkfontein caves
- Robben Island
- Richtersveld Cultural and Botanical Landscape

Environmental World Heritage Sites:

- iSimangiliso Wetland Park (ecosystems)
- Cape Fynbos Region
- uKhahlamba Drakensberg Park

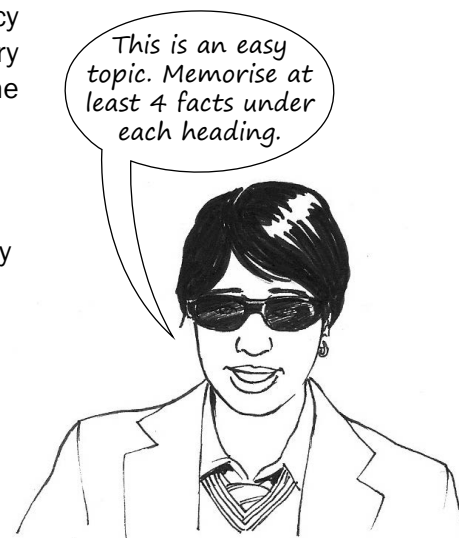
13.9 Tourism policy suggestions

The **Department of Tourism** leads and directs tourism policy. The starting point for policy on tourism is the **White Paper on Tourism**. Tourism policy is also supported and directed by the **Tourism Forum**, which is an advisory body to the **Minister of Tourism**. Some tourism policy initiatives include the following:

13.9.1 Marketing

SA Tourism was created to promote tourism internationally and nationally

- **Nationally:** SA Tourism persuades South African citizens to travel in their own country.
- **Internationally:** Marketing initiatives try to ensure South Africa is selected as a tourist destination. Foreigners visit our country for the following reasons:
 - Value for money
 - The world in one country



- South Africa's political miracle
- The climate
- Safety
- The friendliness of South Africa's people
- The cleanliness and tranquility (peace) of our tourist destinations

13.9.2 Directing tourists' spatial distribution

Three approaches are followed to distribute tourists effectively to the many tourist sites:

- **Create representative bodies:** Tourist-based industries are linked to form representative bodies. Tourists can then easily access knowledge about all tourist destinations.
- **Improve marketing:** Tourists receive accurate product descriptions and information about competitive prices. Less well-known destinations are aggressively marketed.
- **Improve supporting services:** The standards of transport, accommodation and other amenities (facilities and services) are world class.

13.9.3 Taxation

Growth in tourism results in increased tourist taxes. Guidelines for levying taxes are:

- **Equity:** Taxes must be fair, e.g. taxes on air tickets.
- **Efficiency:** Nature and game reserves charge entry taxes to regulate tourist flows.
- **Simplicity:** A flat tax rate is used to ensure taxes are easy to pay and administer.

13.9.4 Infrastructure

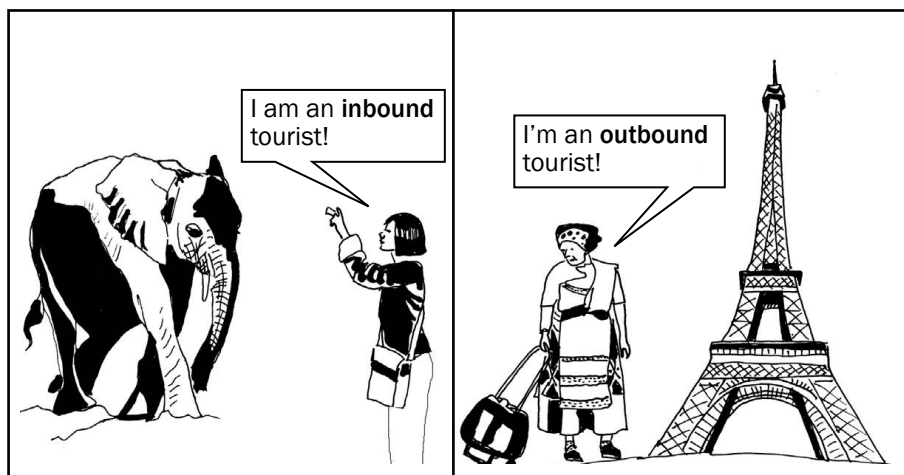
Tourism requires economic infrastructure (roads), social infrastructure (ambulances) and basic services (clean water):

- Infrastructure is maintained for the benefit of domestic and foreign tourists, as well as local citizens.
- The basic considerations are:
 - More infrastructure is required, e.g. water supplies.
 - Existing infrastructure must be upgraded, e.g. upgrade dirt roads to tarred roads.
 - Use new technology to extend the infrastructure, e.g. build the Gautrain.



Activity 1

Study the diagram below and answer the questions that follow:



1. Define the concept tourism. (4)
 2. Explain the difference between an inbound and an outbound tourist. (4)
 3. List any THREE World Heritage Sites in South Africa. (3)
 4. Discuss the effect of tourism on infrastructure. (4 × 2) (8)
- [19]

Answers to activity 1

1. Activities of people travelling to and staying in places ✓ outside of their usual environment for no more than one consecutive year ✓ for leisure, business and other purposes. ✓ It does not relate to any work done for money in the place visited. ✓ (4)

2.

Inbound tourist	Tourists from other countries ✓ who stay for more than one day ✓ are inbound tourists (foreign tourists).
Outbound tourist	South African citizens travelling abroad ✓ have the same effect as imports on the balance of payments. ✓

(4)

3. Mapungubwe in Limpopo ✓ Vredefort Dome (meteorite) in North West ✓ Sterkfontein caves (Mrs Ples and Cradle of Humankind) ✓ Robben Island ✓ (any 3) (3)

4. Tourism requires economic infrastructure (roads), social infrastructure (ambulances) and basic services (clean water). ✓ This infrastructure needs to be maintained for local citizens, domestic and foreign tourists. ✓

Basic considerations for infrastructure development are:

- More infrastructure (e.g. water) ✓✓
- Upgrading (e.g. upgrade dirt roads to tarred roads) ✓✓
- New technology (e.g. transport) ✓✓

(8)

[19]

**Activity 2**

Choose the correct answer from the following alternatives:

Tourism is _____ intensive.

- A. Labour
- B. Capital
- C. Risk

[2]

Answer to activity 2

A. Labour ✓✓

[2]

**Activity 3**

Choose the correct answer from the following alternatives:

Tourism benefits the household through _____ .

- A. Lower incomes
- B. Lower productivity
- C. More infrastructure

[2]

Answer to activity 3

C. More infrastructure ✓✓

[2]



Keep going!

Environmental sustainability

Environmental sustainability relates to the ability of the environment to survive its use for economic activity. The environment is not an unlimited resource and it is important that we sustain the environment so that it can be used by future generations.

Overview

TOPIC	CONTENT	CONTENT DETAILS FOR TEACHING, LEARNING AND ASSESSMENT PURPOSES
14. Basic economic problem: Environmental sustainability	<p>Analyse environmental sustainability and investigate recent international agreements in this regard, for example, the Rio de Janeiro and Johannesburg summits</p> <ul style="list-style-type: none"> • The State of the Environment <ul style="list-style-type: none"> – Pollution <ul style="list-style-type: none"> – Definition – Types – Erosion, deforestation and climate change – Conservation – Preservation • Measures to Ensure Sustainability <ul style="list-style-type: none"> – Using the market <ul style="list-style-type: none"> – The market does not take care of social costs and benefits – The market fails because of specific reasons – The mechanism of market and social costs and benefits 	<ul style="list-style-type: none"> • Define/explain the relevant concepts • Briefly discuss the state of environment • Examine the measures to ensure sustainability in detail <p>HOT QUESTION: How effective are the South African government's interventions with regard to environmental sustainability? Motivate your response!</p>

	<ul style="list-style-type: none"> - Government Interventions <ul style="list-style-type: none"> - Give property rights - Pay for environmental use - Levying of environmental tax - Pay for environmental subsidies - Issuing of marketable permits - Public sector control <ul style="list-style-type: none"> - Command and control - Voluntary agreements - Education - International <ul style="list-style-type: none"> - Sustaining biodiversity - Chemical waste - Hazardous waste - Climate change policy – adaptation and mitigation - Loss in indigenous knowledge • Major International Agreements <ul style="list-style-type: none"> - Rio de Janeiro summit (UNCED) - Johannesburg summit (WSSD) - Rio + 20 summit - Kyoto-protocol - Millennium Development Goals - United Nations Framework Convention on Climate Change (COP 17) 	<ul style="list-style-type: none"> • Distinguish between the concepts, protocol and agreement • Briefly discuss the major protocols in terms of the following: <ul style="list-style-type: none"> - Name of the agreement - Environmental issue to be addressed by the agreement/protocol - Envisaged outcome of the agreement/protocol
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14.1 Key concepts

These definitions will help you understand the meaning of key Economics concepts that are used in this study guide. Understand these concepts well. Use mobile notes to help you study them.

Terms	Definitions
Command and Control (CAC)	The direct regulation of an industry or activity through laws that state what is allowed and what is illegal
Conservation	Seeks creative continuity of the environment, while ensuring that environmental change considers the quality of life for both present and future generations
Environmental sustainability	The ability of the environment to survive its use for economic activity. It refers to meeting the needs of the present generation without compromising the needs of future generations
Pollution	Emissions which flow into the natural environment from human activity, and which are beyond the capacity of the environment to absorb
Preservation	To keep resources that are non-renewable intact, e.g. ecological systems, heritage sites
The United Nations Conference on Environment and Development (UNCED)	UNCED was held in 1992 and is known as the Earth Summit. The goal of UNCED was to create strategies to stop and reverse the effects of environmental degradation (damage), and to support international efforts to promote sustainable development in all countries



14.2 The state of the environment

The **state of the environment** is very important for environmental sustainability. If the environment is damaged, it will become more difficult to sustain life on earth. The environment can be damaged by excessive (too much) mining; by farming without allowing the soil to recover; by excess fishing without allowing the fishing stocks to build up again; and by not controlling the release of pollution.

14.2.1 Pollution

Pollution relates to the introduction of contaminants (poisons) that damage the natural environment. Pollution can come from chemical substances released by factories, as well as from household and business waste and rubbish. Pollution policy is difficult to apply in practice. The following are 3 ways of dealing with pollution:

- **Technology and control:** New technology is cleaner and has less impact on the environment. The government controls pollution by limiting the use of older technologies that pollute the environment.
- **Marginal decisions:** These are decisions made by government on what acceptable levels of pollution are. If the government is too tolerant, or makes its decisions in the interest of expanding business rather than sustaining the environment, then pollution levels can rise to the point where they damage the environment.
- **Self-interest:** For example, keeping a beach litter-free. People use dustbins on the beach because they want to use a beach that is clean.

14.2.2 Conservation

Conservation relates to the preservation (looking after) of natural resources to ensure they are not completely used up and disappear from the environment. Conservation is necessary due to pollution and the over-utilisation (using too much) of resources:

The conservation of stocks (resources):

- Conservation is needed when stocks are utilised (used) more than they can reproduce to replace what has been used.
- This leads to a search for substitutes.
- Conservation policies help to conserve renewable stocks (e.g. trees) and non-renewable stocks (e.g. fossil fuels).

Maintaining renewable stocks:

- A **market economy** has an interest in conservation as it helps maintain renewable stocks, e.g. timber and fishing. Conservation is achieved through the force of demand and supply which helps to sustain these kinds of industries.
- **Direct controls:** The government maintains the stock levels of environmental resources through the issuing of permits and quotas. For example, the government sets quotas for fishing to stop catches being so large that they exceed (are bigger than) the growth of the fish population. It also sets quotas for cutting down trees to ensure deforestation does not exceed the rate of renewal.

14.2.3 Preservation

Preservation is linked to conservation. It is about preserving existing assets to ensure they do not get used in a way that is destructive to the environment.

- **Private property:** A game reserve may be sold to a businessman to be used for farming. But the government can intervene and stop the sale because they recognise the importance to the environment of preserving game reserves.
- **Preservation requires compromise** (give and take): Farmers may develop their river mouth as a holiday resort. If this is not controlled, and too many other farmers do the same, the entire ecosystem will be damaged, and animal and plant life will be negatively affected.
- **Government policy:** Government intervenes to preserve environmental assets by:
 - Buying, confiscating, expropriating (taking ownership) or nationalising resources, e.g. indigenous forests.
 - Subsidising key resources, e.g. privately owned ecosystems.

14.2.4 Externalities

Externalities imply costs and benefits that were not planned for.

- The extra costs and benefits of externalities are not factors when the state of the environment is assessed.
- Goods that have negative externalities such as air and water pollution are generally oversupplied in the market.
- When businesses are expected to bear the cost of equipment to reduce pollution, it could have a positive externality on others. Businesses tend to spend little on pollution abatement equipment due to its limited marginal private benefit. The major role of government, regarding the environment, is to correct inefficiencies arising from externalities.

14.3 Measures to ensure sustainability

It is important for governments to take steps to ensure **sustainability**. Sometimes, businesses are driven by self-interest, and they see nothing wrong with using all available resources if they can make a profit from them. There are 5 controlling mechanisms to ensure sustainability:

14.3.1 The market

Use this mnemonic to help you remember the 5 controlling mechanisms

M – Market – Make
I – Intervention – It
C – Control – Count
M – Measures – More
A – Agreements – Always

The market is driven by self-interest. The market considers the environment as an asset to be used for its own benefit. Sustainability is achieved in the free market only to the extent that **resource prices** rise as they become scarce (less available), and through the development of **environment-friendly technology**.

There is a **social interest** in using the environment, not only to the direct producer/consumer, but also to people in general, now and in the future. This means we all have an interest in preserving the environment.

Reasons why the market fails to ensure sustainability:

- The market sees the environment as a common resource.
- **Externalities** such as air pollution caused by factories cannot be stopped without restrictive policies.
- **Lack of knowledge**: Businesses cause damage without realising it, e.g. companies making aerosol cans (such as spray-on deodorants) and did not know the damaging effect they had on the ozone layer.
- **Carelessness**: People continue with harmful practices and leave future generations to worry about the consequences.

Optimum market decisions

- Market mechanisms have failed when market forces fail to produce the desired result of environmental sustainability.
- All costs and benefits are not captured in the market price. The future cost of the resource disappearing is not often considered.

14.3.2 Public sector intervention

Public sector intervention aims to achieve social efficiency. This occurs through:

Granting property rights:

- **The conservationist effect**: People care for things that belong to them.
- To prevent fauna and flora species from becoming extinct, people are granted property rights if they agree to preserve the flora and fauna.
- Property rights can be expanded to common goods such as clean air.
- The **Kyoto Protocol** is an international agreement whereby developed countries pay developing countries for their right to pollute.

Charging for the use of the environment:

- **Price the environment**: The government levies fees for waste produced and dumped in the environment.
- In South Africa, local authorities levy charges on rubbish collection and sewage disposal.

- The best results are achieved when charges are proportional (related to) to waste produced.

Environmental taxes:

- Environmental taxes are taxes imposed on the output of goods that generate external environmental costs (pollution). These are called **green taxes**.
- **Carbon dioxide emissions** from wineries and vehicle tyres are taxed. The tax rate is equal to the marginal external cost.

Environmental subsidies:

- Subsidies are granted to businesses to reduce environmental damage, e.g. the government subsidises new technology that saves energy, such as energy-saving light bulbs or solar geysers.

Marketable permits:

- The government gives each business a licence to pollute to a certain degree.
- Businesses sell their licences to other businesses.
- In South Africa, marketable permits are granted by the **Department of Minerals and Energy**.

14.3.3 Public sector control

When government environmental policies don't produce positive results, the government takes direct control through **Command and Control (CAC)** systems:

Command and Control (CAC):

- The government enforces **policy** by setting maximum levels of the emission of pollution.
- Most developed countries have **regulations** that control air and water pollution.

There are **3 approaches** in CAC systems:

- **Quantity standards:** These focus on the amount of pollution emitted.
- **Quality standards:** These focus on the environmental impact of the pollution emitted.
- **Social impact standards:** These focus on the effect on people of the pollution emitted.

Voluntary agreements:

- The government concludes **agreements** with businesses on a voluntary basis to cut pollution.

Education:

- Education is used to try to change **people's attitudes** towards the environment.
- Innovative approaches have been tried in the developing world to educate people, e.g. setting up community wildlife reserves.

14.3.4 International measures

Environmental problems are global problems. For example, pollution from motor vehicles and the greenhouse effect have an impact on the entire world. Polluted air and water moves from one country to another, and if the ocean is polluted in America, it can affect beaches in Australia. **International measures** have been implemented to deal with the following 5 environmental problems:

Biodiversity loss:

- If species become **extinct** (die out completely), this cannot be reversed.
- Modern techniques such as **gene transplants** can limit the loss of species.
- **The Convention on International Trade in Endangered Species (CITES)** sets many policies to deal with species loss.

Chemical waste:

- Chemical waste is toxic (it has a negative effect on living beings and can cause infertility or death).
- Chemical waste needs to be carefully managed to ensure it does not seep into the ground water.
- The **Stockholm Protocol** is a United Nations agreement to limit chemical waste.

Hazardous waste:

- Hazardous waste is highly toxic. It has a slow decomposition rate (it stays poisonous for a very long time).
- The most hazardous (dangerous) waste is radioactive waste from nuclear power.
- The **Basel Convention** is an international agreement to manage nuclear waste. South Africa is a signatory to the agreement.

Climate change:

- Global warming primarily causes climate change.
- Climate change can be reversed through widespread international co-operation, e.g. sharing weather information and weather patterns; agreeing to limit pollution; and banning chemical products such as greenhouse gases that damage the ozone layer.
- The **Kyoto Protocol** of 1997 is an international agreement to limit the production of greenhouse gases, because voluntary reductions of carbon dioxide levels did not succeed.

Loss of indigenous knowledge:

- Indigenous people have a lot of knowledge about the natural environment, which they use to make a living.
- Indigenous people traditionally used organic methods and natural processes.
- As indigenous people lose their habitats or are urbanised, this knowledge is disappearing and is being lost to the world forever.
- **Local capacity-building** is very important for the environmental sustainability of indigenous people, i.e. finding a way for them to earn a living in their traditional environment.

14.3.5 Major international agreements

Since the 1990's the United Nations has convened various meetings with all countries worldwide on issues affecting them. They should take responsibility for the management of these issues.

- **Rio de Janeiro summit (UNCED):** This summit took place in 1992 with the objective of sustainable development. Envisaged outcomes included: environmental protection as an integral part of development, cooperation to conserve, protect and restore the health of the ecosystem, prevent environmental degradation where the polluter should bear the cost of pollution and assess the environmental impact.
- **Johannesburg summit (WSSD):** Hosted in 2002 in Johannesburg on Sustainable Development. Envisaged outcome of the programme includes: poverty eradication, changing unsustainable patterns of consumption, globalisation, health and the environment.
- **Rio +20 summit:** Also known as the United Nations Conference on Sustainable Development took place in Brazil. The main issue was sustainable growth and poverty eradication without damaging the environment. It was agreed that a green economy would be one of the tools for sustainable development. Sustainable development goals covering economic, social and environmental aspects will replace the MDG from 2013.
- **Kyoto-protocol:** This conference held in 1997 in Kyoto, established legally binding obligations whereby industrialised countries agreed to reduce their emission of six greenhouse gases.
- **Millennium Development Goals:** Communities depend on healthy ecosystems to survive and prosper. Some of the MDGs are: eradication of extreme poverty and hunger, achieve universal primary education, gender equality, reducing child mortality rates, improve maternal health, combat HIV/Aids and other diseases and create a global partnership for development.
- **United Nations Framework Convention on Climate Change (COP 17):** The 17th Conference of the Parties was held in Durban where the following decisions were taken:
 - Commitment to the Kyoto Protocol and reducing pollution by greenhouse gases.
 - A Green Climate Fund to help developing countries to establish cleaner sources of energy and to adapt to climate change.
 - An Adaptation committee of 16 members to report to COP 18 on the improvement of the ability of the poorest and most vulnerable countries to adapt to climate change, better protection and help against losses and damage related to climate change.



The Kyoto conference was held in Japan in 1997 and focused specifically on climate change. It resulted in the Kyoto Protocol which attempted to get the developed countries to commit to reducing their emission of greenhouse gases.



Activity 1

Study the following sign and answer the questions that follow:

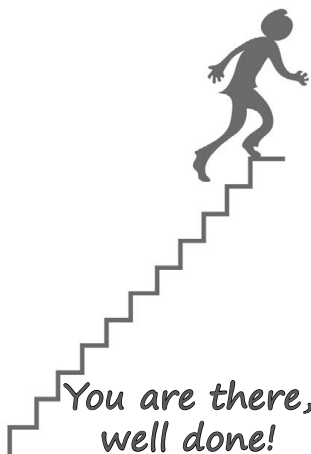


Warning
Chemical waste

1. What environmental hazard is depicted in the above logo? (1)
 2. Explain in your own words how the above can threaten the environment. (3)
 3. Name an international protocol which addresses this hazard. (2)
- [6]

Answers to activity 1

1. Chemical waste ✓ (1)
 2. Pollution of water resources which can be very harmful to humans ✓ plants and animals ✓ (3)
 3. The Stockholm Protocol ✓✓ (2)
- [6]



Appendix: Exemplar exam papers

The 2014 Economics exams have a new format in line with CAPS. The Department of Basic Education has offered an example of Economics Paper 1 and Paper 2 with marking memoranda.


Use this exam paper and marking memorandum to help you prepare for your exams:

1. Answer the questions in the exam. **Time yourself** so you complete it within 1½ hours (which is the time you will have in the real exam).
2. Treat each one as a ‘real’ exam by making sure you have all the materials you need (pens, pencils, eraser, protractor and calculator).
3. This exercise is meant to test your knowledge – so **don’t cheat yourself** by looking up the answers provided in the marking memoranda before you’ve finished each exam.
4. Use the memoranda to **check whether or not your answers are correct**. Note where you have got answers wrong – these are the sections of the curriculum that you need to do more work on. Go back to your textbooks and to the relevant sections of this study guide, and **spend time learning** the sections for which you got the lowest marks.
5. And remember: success depends on **practise, practise, practise, and then more practice!** Repeat this exercise as often as you can so that you fly in your year-end exams!

INSTRUCTIONS AND INFORMATION

1. Answer FOUR questions as follows in the ANSWER BOOK:
SECTION A: COMPULSORY
SECTION B: Answer TWO of the three questions.
SECTION C: Answer ONE of the two questions.
2. Answer only the required number of questions. Answers in excess of the required number will NOT be marked.
3. Number the answers correctly according to the numbering system used in this question paper.
4. Write the question number above each answer.
5. Read the questions carefully.
6. Start EACH question on a NEW page.
7. Leave 2–3 lines between subsections of questions.
8. Answer the questions in full sentences and ensure that the format, content and context of your responses comply with the cognitive requirements of the questions.
9. Use only black or blue ink.
10. You may use a non-programmable pocket calculator.
11. Write neatly and legibly.

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basic education
Department:
Basic Education
REPUBLIC OF SOUTH AFRICA

**NATIONAL
SENIOR CERTIFICATE**

GRADE 12

ECONOMICS P1
EXEMPLAR 2014

MARKS: 150
TIME: 1½ hours

This question paper consists of 12 pages.

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DBE/2014

Economics/P1

30 MARKS – 15 MINUTES

SECTION A (COMPULSORY)

QUESTION 1

1.1

Various options are provided as possible answers to the following questions. Choose the answer and write only the letter (A–C) next to the question number (1.1.1–1.1.8) in the ANSWER BOOK.

1.1.1

The money market is a market for ... term savings and loans.

A

short-

B

short- and long-

C

long-

1.1.2

Consumption of fixed capital is used to calculate the gross value added at ...

A

basic prices.

B

market prices.

C

factor cost.

1.1.3

During an economic recession ...

A

unemployment will increase.

B

production increases.

C

spending increases.

1.1.4

The new economic paradigm is embedded in ... side policies.

A

demand-

B

supply-

C

demand-and-supply-

1.1.5

According to the UN classification, South Africa's HDI ranking is categorised as a ... level.

A

low

B

middle

C

high

1.1.6

Economic growth is measured in terms of ...

A

real GDP.

B

real GDP per capita.

C

nominal GDP.

1.1.7

The ratio of export prices and import prices is known as the ...

A

terms of trade.

B

exchange rate.

C

balance of payments.

1.1.8

An example of an economic indicator is ...

A

labour productivity.

B

life expectancy.

C

housing.

1.2

Choose a description from COLUMN B that matches an item in COLUMN A. Write only the letter (A–J) next to the question number (1.2.1–1.2.8) in the ANSWER BOOK.

COLUMN A

1.2.1

Capital Transfer Account

1.2.2

Depreciation

1.2.3

Free floating

1.2.4

Tariffs

1.2.5

Regional development

1.2.6

Prime rate

1.2.7

Globalisation

1.2.8

Deregulation

COLUMN B

A

the weakening of a currency as result of market forces

B

policies aimed at increasing the economic livelihood of a specific area

C

the interest rate which banks charge on loans to preferential clients

D

world-wide interfacing with trade as the major element

E

the removal of unnecessary laws that inhibit the free operation of markets

F

subaccount in the balance of payments

G

a protection measure against unfair foreign competition

H

exchange rate system

I

the interest rate at which the Reserve Bank charges commercial banks

J

subaccount in the current account

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Economics/P1

30 MARKS – 15 MINUTES

SECTION A (COMPULSORY)

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SECTION B

Answer TWO of the three questions in this section in the ANSWER BOOK.

QUESTION 2: MACROECONOMICS 40 MARKS – 20 MINUTES

- 2.1 Answer the following questions.
- 2.1.1 Give TWO examples of injections into the economy. (2 x 1) (2)
- 2.1.2 What effect will an increase in the value of the rand against the US dollar have on imports from the USA? (1 x 2) (2)
- 2.2 Study the table below and answer the questions that follow.

EXTRACT FROM NATIONAL ACCOUNTS OF SOUTH AFRICA AT CURRENT PRICES	
R million	2012
Gross domestic product (GDP) at market prices	3 155 195
Primary income from the rest of the world	48 501
Primary income to the rest of the world	A
Gross national product (GNP) at market prices	3 085 188

[Source: SARB Quarterly Bulletin, March 2013]

- 2.2.1 Define the concept *gross domestic product*. (2)
- 2.2.2 Calculate the value of A in the table. (2)
- 2.2.3 Give an example of a primary income from the rest of the world. (2)
- 2.2.4 Explain the difference between *current prices* and *constant prices*. (4)

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- 1.3 Give ONE term for each of the following descriptions. Write only the term next to the question number (1.3.1–1.3.6) in the ANSWER BOOK.
- 1.3.1 A small initial change in spending produces a proportionately larger increase in national income
- 1.3.2 The sale of state-owned enterprises to the private sector
- 1.3.3 Goods used as inputs to produce other goods and services
- 1.3.4 An increase in the capacity of the population to produce more goods and services
- 1.3.5 It consists of people between the ages of 15 and 60/65 who are willing to work for an income
- 1.3.6 Return of land to their original owners after confiscation by the government (6 x 1) (6)
- TOTAL SECTION A: 30

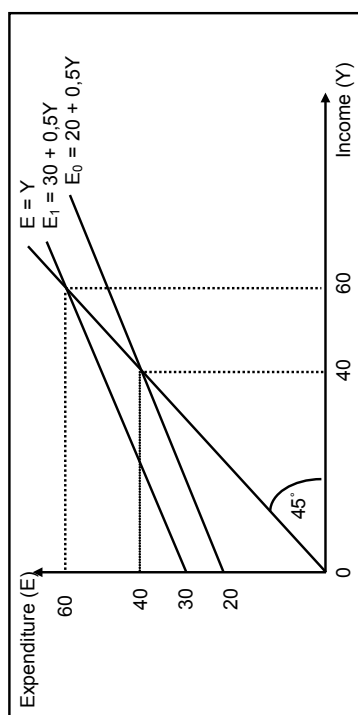
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- 2.3 Study the graph below that depicts a simplified two-sector economy (where $E = C + I$) and answer the questions that follow.



- 2.3.1 Identify ONE participant in the economy above. (2)
- 2.3.2 What does the line $E = Y$ represent? (2)
- 2.3.3 Calculate the multiplier using the following formula:

$$k = \frac{1}{1 - \text{mpg}}$$

The marginal propensity to consume (mpc) = 0.8.
(Show ALL calculations.)

- 2.3.4 What is the relationship between the *marginal propensity to consume* (mpc) and the *multiplier*? (2)
- 2.4 Explain the new economic paradigm. (4 x 2) (8)
- 2.5 Argue ONE case in favour of free trade and ONE case against protectionism. (2 x 4) (8)
- [40]**

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QUESTION 3: ECONOMIC PURSUITS

40 MARKS: 20 MINUTES

- 3.1 Answer the following questions.
- 3.1.1 State TWO fiscal policy measures that can be implemented to redistribute wealth in South Africa. (2 x 1) (2)
- 3.1.2 What effect will import restrictions have on the local textile industry in South Africa? (1 x 2) (2)
- 3.2 Study the extract below and answer the questions that follow.

INDUSTRIAL POLICY ACTION PLAN

The Industrial Policy Action Plan (IPAP) is located in the vision of the National Development Plan and forms one of the fundamental cornerstones of the New Growth Path Framework. IPAP is predicated to bring about significant structural change to the South African economy. The existing growth path is led by the consumption-driven sectors, which are growing twice as fast as the manufacturing sectors. The economy is import intensive, especially with respect to value-added products. Stronger domestic growth in the manufacturing sector is imperative. High structural unemployment is a constant, oscillating between 22,5% and 25% if the strict definition is used.

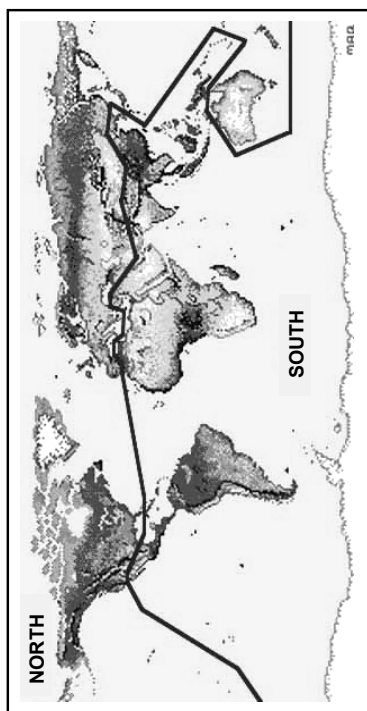
[Adapted from www.bdlive.co.za]

- 3.2.1 Identify the main objective of the IPAP. (2)
- 3.2.2 How will the above objective be achieved? (4)
- 3.2.3 Explain how unemployment will be addressed by the New Growth Path Framework. (4)

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- 3.3 Study the map below and answer the questions that follow.



- 3.3.1 What is indicated by the solid line in the map above? (2)
- 3.3.2 Name TWO countries that make up the G8 grouping of countries in the North. (2)
- 3.3.3 Briefly comment on the trade relations between the countries in the North and South. (6)
- 3.4 Briefly explain the integrated manufacturing strategy in South Africa. (4 x 2) (8)
- 3.5 How can the repo rate be used to stimulate aggregate demand? (4 x 2) (8)

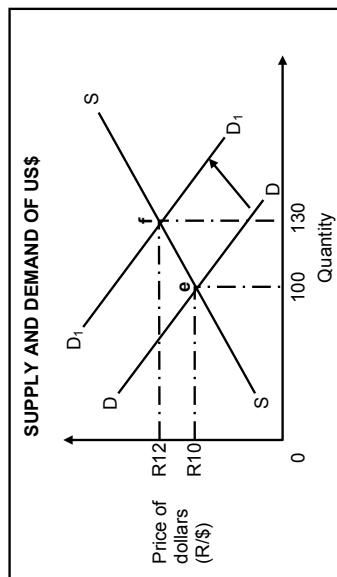
[40]

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QUESTION 4: MACROECONOMICS AND ECONOMIC PURSUITS
40 MARKS – 20 MINUTES

- 4.1 Answer the following questions.
- 4.1.1 Name TWO problems of public sector provisioning. (2 x 1) (2)
- 4.1.2 What effect will low labour productivity have on inflation? (1 x 2) (2)
- 4.2 Study the graph below and answer the questions that follow.



- 4.2.1 At what point on the graph does the equilibrium for foreign exchange originally occur? (2)
- 4.2.2 What happens to the value of the rand when DD shifts to D_1 ? Motivate your answer. (4)
- 4.2.3 How can the Central Bank of South Africa intervene in the market to influence the exchange rate? (4)

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- 4.3 Study the extract below and answer the questions that follow.

SPECIAL ECONOMIC ZONES TO EMPLOY REGIONAL STRENGTHS	
<p>The announcement that 10 potential special economic zones have been identified in conjunction with the provinces could be a game-changer for South African manufacturers. Such zones are intended to bring mainstream economic activity to poor and isolated parts of South Africa by leveraging the commercial potential of the particular regions.</p> <p>This will include industry clustering, or targeted development. Upington, in the Northern Cape, is a natural home for solar energy research and development. Saldanha Bay will service the growing oil and gas industry on Africa's west coast, while expanding iron ore exports.</p> <p>The Department of Trade and Industry is devising a draft of regulations that will see the country's industrial development zones (IDZs) in Richards Bay, East London and Coega, near Port Elizabeth, taken into a new special economic zones framework. This envisages zones including free ports, free trade zones, and sector development zones.</p> <p>A special corporate tax rate of 15% is proposed, well below the 28% currently applied. There was, however, a concern that the incentive would cause dislocation and would have 'distorting effects' on the economy.</p> <p>[Source: www.bdlive.co.za]</p>	

- 4.3.1 Define the concept *IDZ*. (2)
- 4.3.2 Identify TWO new proposed economic regions. (2)
- 4.3.3 What is the main difference between an *IDZ* and an *SEZ*? (2)
- 4.3.4 What, in your opinion, would be the 'distorting effects' on the economy? (4)
- 4.4 Explain *leading* and *lagging business cycle indicators*. (2 x 4) (8)
- 4.5 Explain the TWO social indicators used for children under the age of five. (2 x 4) (8)
- TOTAL SECTION B: 80** [40]

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SECTION C

Answer only ONE of the two questions in this section in the ANSWER BOOK.

STRUCTURE OF THE ESSAY:	
Introduction	MARK ALLOCATION:
Body:	Max. 2
Main part: Discuss in detail/in-depth discussion/Examine/ Critically discuss/Analyse/Compare/Evaluate/Distinguish/ Explain/Assess/Debate	Max. 26
Additional part: Give own opinion/Critically discuss/Evaluate/ Critically evaluate/Draw a graph and explain/Use the graph given and explain/Complete the given graph/Calculate/Deduce/ Compare/Explain/Distinguish/Interpret/Briefly debate	Max. 10
Conclusion	Max. 2
TOTAL	40

QUESTION 5: MACROECONOMICS

40 MARKS – 35 MINUTES

International trade is the backbone of our modern commercial world as producers in various nations try to profit from an expanded market, rather than be limited to selling within their own borders.

- Discuss export promotion as part of South Africa's international trade policy. (26 marks)
 - In your opinion, how successful is South Africa with the implementing of the above policy? Motivate your answer. (10 marks)
- [40]**

QUESTION 6: ECONOMIC PURSUITS


40 MARKS – 35 MINUTES

Supply-side policies focus on the ability of markets to supply enough goods and services to meet aggregate demand.

- Discuss this statement by focusing on effectiveness and efficiency of markets in the South African context. (26 marks)
 - In your opinion, how successful is the South African government in providing for the basic needs of the poor? (10 marks)
- [40]**

TOTAL SECTION C: 40
GRAND TOTAL: 150

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basic education
Department:
Basic Education
REPUBLIC OF SOUTH AFRICA

NATIONAL
SENIOR CERTIFICATE

GRADE 12

ECONOMICS P1
EXEMPLAR 2014
MEMORANDUM

MARKS: 150

This memorandum consists of 13 pages.

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SECTION A (COMPULSORY)

QUESTION 1

1.1 MULTIPLE-CHOICE QUESTIONS

- 1.1.1 A short ✓✓
 - 1.1.2 C factor cost ✓✓
 - 1.1.3 A unemployment will increase ✓✓
 - 1.1.4 C demand and supply ✓✓
 - 1.1.5 B middle ✓✓
 - 1.1.6 A real GDP ✓✓
 - 1.1.7 C terms of trade ✓✓
 - 1.1.8 A labour productivity ✓✓
- (8 x 2) (16)

1.2 MATCHING ITEMS

- 1.2.1 F subaccount in the balance of payment ✓
 - 1.2.2 A the weakening of a currency as result of market forces ✓
 - 1.2.3 H exchange rate system ✓
 - 1.2.4 G a protection measure against unfair international competition ✓
 - 1.2.5 B policies aimed at increasing the economic livelihood of a specific area ✓
 - 1.2.6 C the interest rate which banks charge on loans to preferential clients ✓
 - 1.2.7 D world-wide interfacing with trade as the major element ✓
 - 1.2.8 E the removal of unnecessary laws that inhibit the free operation of markets ✓
- (8 x 1) (8)

1.3 IDENTIFY THE CONCEPT

- 1.3.1 Multiplier effect ✓
 - 1.3.2 Privatisation ✓
 - 1.3.3 Capital goods ✓
 - 1.3.4 Economic development ✓
 - 1.3.5 Economically Active Population ✓
 - 1.3.6 Land restitution ✓
- (6 x 1) (6)

TOTAL SECTION A: 30

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Economics/P1	3	NSC – Grade 12 Exemplar – Memorandum	DBE/2014	Economics/P1	4	NSC – Grade 12 Exemplar – Memorandum	DBE/2014
SECTION B							
Answer TWO of the three questions in this section in the ANSWER BOOK.							
QUESTION 2							
2.1	2.1.1	<ul style="list-style-type: none">Government spending ✓Investments ✓Exports ✓	Any (2 x 1)	2.5	<ul style="list-style-type: none">Argument in favour of free trade: ✓✓<ul style="list-style-type: none">The free trade argument is persuasive. ✓✓ If each nation does what it does best, everyone will enjoy lower prices and higher levels of output. ✓✓Free trade leads to greater world production ✓✓ of traded goods, leading to an increase in economic welfare. ✓✓Free trade allows countries to specialise ✓✓ in economic activities in which they have a comparative advantage (economies of scale). ✓✓Free trade leads to mutual gains ✓✓ from international trade to all countries. ✓✓When there is free trade, more efficient distribution of resources ✓✓ is possible because each country specialises in its most effective production. ✓✓Free trade offers consumers greater choice. ✓✓ It allows consumers the choice of what to buy globally and not just from what is available locally. ✓✓Any 1 argument (2 x 2) (4)	Any 1 argument (2 x 2) (4)	
	2.1.2	Imports will increase ✓✓	(1 x 2)				
	2.2.1	The final value of goods and services produced within the borders of a country in one year. ✓✓					
	2.2.2	R87 593 million ✓✓					
	2.2.3	RSA citizen working and earning money in the UK. ✓✓					
	2.2.4	Current prices – (Nominal) Does not take into account changes in the general price level ✓✓					
		Constant prices – (Real) Where the change in the general price levels were taken into account ✓✓	(4)				
2.3	2.3.1	Households/Consumers ✓ Business sector/Firms/Producers ✓	(2)				
	2.3.2	It shows all the possible levels of expenditure and output ✓ at which the economy is in equilibrium ✓	(2)				
	2.3.3	$k = \frac{1}{(1 - 0.8)}$ $= \frac{1}{0.2}$ $= 5 \checkmark \checkmark$	(4)				
	2.3.4	The bigger the mpc, the bigger the multiplier (and vice versa) ✓✓	(2)				
2.4		<ul style="list-style-type: none">Theories by the Monetarists (Friedman) and Keynesians (Keynes) extreme and only true under specific circumstances ✓✓Under real circumstances, government pursues economic growth irrespective of inherently stable or unstable market. ✓✓Therefore governments aren't extreme, but transparent and follow pragmatic policies ✓✓The root of the new economic paradigm is embedded in the prevention of unstable conditions that will lead to contractions ✓✓According to the new economic paradigm it is possible for output to rise over extended periods of time without being hampered by supply constraints and inflationary pressuresEmbedded in demand-side and supply-side policies ✓✓	(Any 4 x 2) (8)				
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Economics/P1	NSC – Grade 12 Exemplar – Memorandum	DBE/2014	Economics/P1	NSC – Grade 12 Exemplar – Memorandum	DBE/2014
QUESTION 3					
3.1			3.4		
3.1.1	<ul style="list-style-type: none"> Progressive personal income tax ✓ Wealth taxes ✓ Cash benefits - grants ✓ Benefits in kind – food parcels/user fee charge/school meals ✓ Land reform programmes – land restitution and land redistribution ✓ Property subsidies ✓ Youth wage subsidies ✓ 	(Any 2 x 1)	<ul style="list-style-type: none"> The main focus was on developing the global competitiveness of the SA manufacturing enterprises (implemented by the DTI) ✓ ✓ It is a strategy that applies to all processes that transforms natural products into manufactured products ✓ ✓ It involve cross cutting issues such as technology, human resource development, access to finance and infrastructure ✓ ✓ It also concentrate on key input sectors like transport, telecommunications and energy ✓ ✓ The IMS prioritise certain growth sectors like tourism, agriculture, information technology and cultural industries ✓ ✓ 	(4 x 2)	
3.1.2	<ul style="list-style-type: none"> Increased sales of locally produced clothing ✓ ✓ Expansion of local industries ✓ ✓ Increased employment ✓ ✓ (Accept any relevant answer)	(Any 1 x 2)	3.5	<ul style="list-style-type: none"> The SARB is using interest rates to manipulate the market ✓ ✓ The repo rate is the key interest rate. This is the rate at which the SARB lends money to banks for short periods of time ✓ ✓ The SARB will lower the interest rate if it wants to stimulate the demand for credit. ✓ ✓ Many people will be encouraged to buy more at lower interest rates. ✓ ✓ This will lead to a higher demand for goods and services ✓ ✓ 	(8)
3.2	<ul style="list-style-type: none"> IPAP is predicated on the need to bring about significant structural change to the South Africa economy. ✓ ✓ 	(2)			
3.2.1					
3.2.2	<ul style="list-style-type: none"> Stronger domestic growth in the manufacturing sector. ✓ ✓ High employment levels ✓ ✓ 	(4)			
3.2.3	<ul style="list-style-type: none"> Creation of employment. ✓ ✓ NGP envisage the creation of 5 million new jobs by 2020. ✓ ✓ 	(4)			
3.3	<ul style="list-style-type: none"> North/South divide or developed/developing countries ✓ ✓ 	(2)			
3.3.1					
3.3.2	<ul style="list-style-type: none"> USA, Canada, UK, France, Germany, Japan, Italy, Russia (2 x 1)	(2)			
3.3.3	Developing countries: mainly export raw to developed countries and import manufactured products from developed countries. ✓ ✓ Developed countries: continue to subsidise production of their agricultural goods, making it difficult for developing countries to compete, ✓ ✓ while insisting that developing countries eliminate their tariffs on manufactured goods. ✓ ✓ Most developing countries have very little foreign trade. ✓ ✓	(6)			

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QUESTION 4									
4.1	4.1.1	Accountability/Efficiency/Assessing needs/Pricing policy/Parastatals/Privateisation ✓✓ (Any 1 x 2)	(2)	4.4	Leading: • Give consumers, businesses and the state a glimpse of the direction in which the economy might be heading. ✓✓ ▪ When these indicators rise, the level of economic activities will also rise a few months later. ✓✓ ▪ Examples of leading indicators are job advertising space; inventory; and sales. ✓✓ (Any 2 x 2)	(4)			
4.2	4.2.1	Low productivity – low production – negative effect on the aggregate supply of goods and services – same/or growing aggregate demand = rapid increase in general price level ✓✓ (demand inflation) Point, e ✓✓ (1 x 2)	(2)		Lagging: • Lagging indicators won't change direction until after the business cycle has changed its direction. ✓✓ • Examples of these indicators are hours worked in construction and total of commercial vehicles sold. ✓✓ (Any 2 x 2)	(4)			
	4.2.2	The value of the rand depreciates ✓✓ As a result of the increase in the demand for dollars, the value of the rand decreases from R10 for one dollar to R12 for one dollar ✓✓	(4)	4.5	Infant mortality rates ✓✓ – the number of children younger than one year old who die in a year per 1 000 births during that year. In 2010 in SA it was 34 per thousand ✓✓ Under five mortality rates ✓✓ – the number of children under five years old who die per 1 000 live births during that year. In SA it was 50 per thousand. ✓✓ (Any 2 x 2)	(4)			
4.3	4.3.1	An IDZ is a purpose-built industrial estate which is closed off and situated in a specific area. ✓	(2)	[40]					
	4.3.2	Upington, in the Northern Cape, is a natural home for solar energy research and development. ✓✓ Saldanha Bay will service the growing oil and gas industry on Africa's west coast, while expanding iron ore exports. ✓✓	(2)	TOTAL SECTION B:					
	4.3.3	SEZ's currently get a special incentive, which is not applicable to the IDZ. A blanket corporate tax rate of 15%, well below the 28% currently applied. ✓✓	(2)	80					
	4.3.4	IDZ is located in a smaller area linked directly to a port, whereby an SEZ covers a wider area. The plan is to incorporate the IDZ into an SEZ. ✓✓ Distorting effects – the current IDZ does not benefit from the special tax incentive scheme. ✓✓ The concern is that companies within the IDZ will close their operations and move over to the SEZ's to enjoy this incentive. ✓✓ This could mean dislocations and movement to other areas. ✓✓ Valuable investments will be lost in the area withdrawn. This will cause distortions in the production and output for that region. ✓✓	(4)						

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Methods of export promotion✓

- Incentives: The government supplies information on export markets, research on new markets, concessions on transport charges, export credit, etc. in order to stimulate exports. ✓✓
- Subsidies: These include direct and indirect subsidies: ✓✓
 - Direct subsidies: Cash payments to exporters. ✓✓
 - Indirect subsidies: Refunds on import tariffs and general tax rebates. ✓✓
- Trade neutrality: Subsidies equal in size to import duties are paid. ✓✓
Neutrality can be achieved through trade liberalisation. ✓✓

Advantages of export promotion✓

- There are no limitations to size of scale since the market is very large. ✓✓
- Production is based on cost and efficiency. ✓✓
- There is increased domestic production. ✓✓
- Exchange rates would be realistic. ✓✓

Disadvantages of export promotion✓

- The real cost of production is reduced by subsidies and incentives. ✓✓
- The lack of competition because of incentives and subsidies forces competitors out of the market. ✓✓
- Export promotion results in increased tariffs and quotas by powerful overseas competitors. ✓✓
- Export promotion results in the protection of labour-intensive industries by developed countries. ✓✓ (Max 26)

NOTE: A maximum of 8 x 1 marks will be allocated for headings.

ADDITIONAL PART

The candidate can offer a positive or a negative argument.

Positive/Negative ✓✓
Arguments ✓✓ ✓✓
Substantial evidence ✓✓ ✓✓
(Accept any other relevant answer) (Max. 10)

Conclusion

Any relevant conclusion. (Max. 2)

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SECTION C

Answer only ONE of the two questions in this section in the ANSWER BOOK

STRUCTURE OF ESSAY:		MARK ALLOCATION:
Introduction		Max. 2
Body:		
Main part: Discuss in detail/In-depth discussion/Examine/Critically discuss/Analyse/Compare/Evaluate/Distinguish/Explain/Assess/Debate		Max. 26
Additional part: Give own opinion/Critically discuss/Evaluate/Critically evaluate/Draw a graph and explain/Use the graph given and explain/Complete the given graph/Calculate/Deduce/Compare/Explain/Distinguish/Interpret/Briefly debate		Max. 10
Conclusion		Max. 2
TOTAL		40

QUESTION 5: MACROECONOMICS 40 MARKS – 30MINUTES

International trade is the backbone of our modern commercial world as producers in various nations try to profit from an expanded market, rather than be limited to selling within their own borders.

- Discuss export promotion as part of South Africa's international trade policy. (26 marks)
- In your opinion, how successful is South Africa with the implementing of the above policy? Motivate your answer. (10 marks)

[40]

Introduction

Incentives or mechanisms to encourage domestic manufacturers to increase the exports of goods and services to foreign countries ✓✓ (Max. 2)
(Any other relevant definition of export promotion)

Body

MAIN PART

Reasons for export promotion✓

- The country achieves significant export-led economic growth. ✓✓
- Export promotion enlarges the production capacity of the country. ✓✓
- Export markets are much bigger than local markets. ✓✓
- More workers will be employed. ✓✓
- Prices will be reduced. ✓✓

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Economics/P1	11	NSC – Grade 12 Exemplar – Memorandum	DBE/2014
QUESTION 6: ECONOMIC PURSUITS			
40 MARKS – 30 MINUTES			
Supply-side policies focus on the ability of markets to supply enough goods and services to meet aggregate demand.			
<ul style="list-style-type: none">Discuss this statement by focusing on effectiveness and efficiency of markets in the South African context. (26 marks)In your opinion, how successful is the South African government in providing in the basic needs of the poor? (10 marks)			
Introduction			
The stimulation of supply means to increase the output, in terms of goods and services. ✓✓			
(Any other relevant definition)			
Body			
MAIN PART:			
There are various factors that promote the efficiency and effectiveness of resources:			
<ul style="list-style-type: none">Education and training✓<ul style="list-style-type: none">The Sectoral Education and Training Authorities (SETA's) have been created to promote and facilitate work-related training for the different sectors of the economy. ✓✓The increase in the number of skilled workers will improve the productivity levels of workers. This will lead to an increase in output. ✓✓Fiscal policy✓<ul style="list-style-type: none">High tax rates discourage individuals, leading them to work less and businesses to invest less. ✓✓In South Africa the tax rates for individuals and businesses have been systematically reduced. Tax incentives give industries an area to operate at lower costs. These additional funds can be used to increase production. ✓✓Individuals get tax rebates. ✓✓This will increase the disposable income levels of individuals. This will stimulate the demand for consumer goods and services. ✓✓Competition✓<ul style="list-style-type: none">The promotion of competition services as an incentive for new businesses to enter the market. ✓✓The Competition Act is aimed at limiting the number of monopolies formed and reducing or eliminating the powers of monopolies. ✓✓In addition, the many barriers of international trade have been lifted over the years. ✓✓			
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Economics/P1	12	NSC – Grade 12 Exemplar – Memorandum	DBE/2014
<ul style="list-style-type: none">Deregulations✓<ul style="list-style-type: none">The deregulation of regulated industries provide for greater competition in the market. ✓✓Many unnecessary laws and other barriers to competition in SA have been removed, although there are still some regulations, especially the informal sector that has to be revised. ✓✓Labour legislation✓<ul style="list-style-type: none">In South Africa, the Labour Relations Act, the Employment Equity Act and the Basic Conditions of Employment Act provide a fair and equitable working environment. ✓✓Such a workplace atmosphere will motivate workers to not only improve the quality of their work but also strive towards self-development. ✓✓Small, medium and micro enterprises✓<ul style="list-style-type: none">In South Africa, the government encourages the establishment of SMMEs through various financing and support structures. ✓✓Institutions such as Khula, the National Empowerment Fund, the Industrial Development Corporations and Business Partners are in partnership with national government. ✓✓There are also free advisory centres available to provide information on topics such as managing and running SMMEs ✓✓Broad-Based Black Economic Empowerment Act (BBBEE) ✓<ul style="list-style-type: none">BBBEE is the economic empowerment of all black people, especially women, workers, youth, the disabled and people living in rural areas. ✓✓It is aimed at addressing historical imbalances of the past, through increasing the number of black people that can own, control and control the country's economy and decreasing income inequalities. ✓✓Research and Development✓<ul style="list-style-type: none">An R&D strategy has been implemented by the government to improve national competitiveness. ✓✓The R&D Strategy has three pillars: innovation; science, engineering and technology (SET), human resources and transformation; creating an effective government system. ✓✓Examples are the CSIR and Mintek ✓✓Privatisation✓<ul style="list-style-type: none">Many publicly owned businesses have been privatised or partly privatised. ✓✓Privatisation is essential in promoting competition in the market place. ✓✓It is also proven that private companies are more effective and efficient than state-owned businesses. ✓✓Examples are Telkom, Iscor, ✓✓			
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Economics/P1

13

NSC – Grade 12 Exemplar – Memorandum

DBE/2014

•

Infrastructure ✓

-

A well-developed infrastructure is the backbone of a growing economy. South Africa has one of the better-developed infrastructure in Southern Africa. ✓✓

-

Transport: The South African transport network consists of highways, railways and ports. ✓✓

-

Energy: Currently Eskom generates 95% of electricity in South Africa. It is one of the world's ten largest electricity suppliers in the world. It also exports to other countries. ✓✓

-

Telecommunications: this is one of the fastest growing sectors in the SA economy. It offers fixed-line, wireless and satellite communication and has the most developed network on the African continent. ✓✓

•

Cost of doing business✓

-

It refers to cost of doing business, such as transport, communication and energy costs.✓✓

-

Other costs involve water, sanitation, vehicle and registration and labour markets. ✓✓

(Max 26)

NOTE:

A maximum of 8 x 1 marks will be allocated for headings.

ADDITIONAL PART:

In your opinion, is the South African government successful in meeting the basic needs of the poor? Motivate your response.

Yes/No✓✓

Almost 26% is regarded as absolutely poor in terms of international benchmark poverty line (\$1,25 per day)

(1)

Social security grants: old age pensions, child support grants, disability grants.✓✓

(2)

Benefits in kind: free quota water (6 000 litres per household) and electricity (20 kWh) per household, school-feeding schemes.✓✓

(3)

Housing: RDP houses✓✓

(4)

Sanitation: Access to clean water, energy, sewerage system✓✓

(5)

Primary healthcare: poor receive free hospitalisation and medicine. From certain income levels fees are staggered. Immunisation for all children is free. ✓✓

(6)

Education: no-fee schools✓✓

(Candidates must mention some of these basic needs and how it affects the poor)

(Max.10)

Conclusion

Any relevant conclusion ✓✓

(Max. 2)

TOTAL SECTION C:

40

GRAND TOTAL

150



basic education

Department:
Basic Education
REPUBLIC OF SOUTH AFRICA

**NATIONAL
SENIOR CERTIFICATE**

GRADE 12

**ECONOMICS P2
EXEMPLAR 2014**

MARKS: 150

TIME: 1½ hours

This question paper consists of 12 pages.

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INSTRUCTIONS AND INFORMATION

1. Answer FOUR questions as follows in the ANSWER BOOK:
SECTION A: COMPULSORY
SECTION B: Answer TWO of the three questions.
SECTION C: Answer ONE of the two questions.
2. Answer only the required number of questions. Answers in excess of the required number will NOT be marked.
3. Number the answers correctly according to the numbering system used in this question paper.
4. Write the question number above each answer.
5. Read the questions carefully.
6. Start EACH question on a NEW page.
7. Leave 2–3 lines between subsections of questions.
8. Answer the questions in full sentences and ensure that the format, content and context of your responses comply with the cognitive requirements of the questions.
9. Use only black or blue ink.
10. You may use a non-programmable pocket calculator.
11. Write neatly and legibly.

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Economics/P2	5	NSC – Grade 12 Exemplar	DBE/2014
1.3	Give ONE term for each of the following descriptions. Write only the term next to the question number (1.3.1–1.3.6) in the ANSWER BOOK.		
1.3.1	A market structure dominated by a small number of large firms		
1.3.2	Prices that are set below equilibrium price in the market and which allow the poor greater access to goods and services		
1.3.3	The additional cost incurred when production is increased by one more unit		
1.3.4	Seeks creative continuity of the environment, while ensuring that environmental change considers the quality of life of both present and future generations		
1.3.5	The cost of a basket of consumer goods and services of an average South African household		
1.3.6	A general increase in prices caused by increases in factor input costs		
TOTAL SECTION A:			30

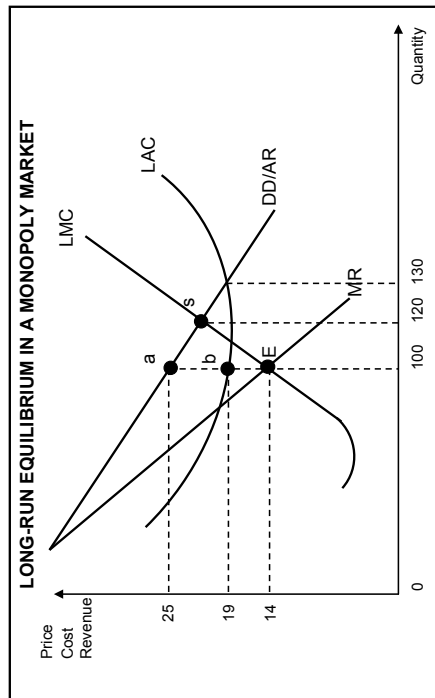
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Economics/P2	6	NSC – Grade 12 Exemplar	DBE/2014
SECTION B			
Answer any TWO of the three questions in this section in the ANSWER BOOK.			
QUESTION 2: MICROECONOMICS		40 MARKS – 20 MINUTES	
2.1	Answer the following questions.		
2.1.1	Name TWO redress methods used by the government to improve income distribution.	(2 x 1)	(2)
2.1.2	Explain how price leadership can result in consumers paying higher prices in an oligopoly market.	(1 x 2)	(2)
2.2	Study the graph below and answer the questions that follow.		

LONG-RUN EQUILIBRIUM IN A MONOPOLY MARKET

The graph illustrates the long-run equilibrium in a monopoly market. The vertical axis represents Price, Cost, and Revenue, while the horizontal axis represents Quantity. The Demand curve is downward-sloping, and the Marginal Revenue curve is steeper and also downward-sloping. The Marginal Cost (LMC) curve is upward-sloping. The Long-Run Average Cost (LAC) curve is also upward-sloping but flatter than the LMC curve. The equilibrium point 'a' is determined by the intersection of the Marginal Revenue and Marginal Cost curves. A dashed line from point 'a' to the vertical axis indicates the price, and a dashed line from point 'a' to the horizontal axis indicates the quantity. The value '25' is marked on the vertical axis.



- | | | |
|-------|---|-----|
| 2.2.1 | Define the concept <i>long run</i> as used in economics. | (2) |
| 2.2.2 | Identify the optimum production level. | (2) |
| 2.2.3 | Explain why the marginal revenue (MR) curve will always lie below the demand curve (DD) in this type of market. | (2) |
| 2.2.4 | Calculate the profit or loss of this monopolist. Show ALL calculations. | (4) |

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- 2.3 Study the article below and answer the questions that follow

COMMISSION CRACKS GLASS CARTEL

Six firms active in the manufacturing and distribution of glass products for the building and construction industry have been found to be involved in a cartel by a Competition Commission investigation.

In its latest ruling on anti-competitive practices in the building and construction industry, the commission alleged that National Glass, Northern Hardware & Glass, Furman and Glass, McCoy's Glass, AF-FSL Glass and Glass South Africa were involved in price fixing, market allocation and the fixing of trading conditions through various arrangements and agreements.

The investigation into cartel activity in the glass industry was initiated in February 2010 based on information received in June 2009. AF-FSL Glass was granted conditional leniency from prosecution.

[Adapted from *Business Report*, 9 April 2013]

- 2.3.1 Define the term *cartel*. (2)
- 2.3.2 Which market structure is depicted in the above article? (1)
- 2.3.3 What prompted the Competition Commission to investigate anti-competitive behaviour in the glass industry? (2)
- 2.3.4 Explain how the glass cartel's behaviour can affect the economy negatively. (4)
- 2.3.5 Name the institution that the glass companies can approach if they are not happy with the fine imposed on them. (1)
- 2.4 Explain the reasons why cost-benefit analysis is used in practice. (8)
- 2.5 How can non-price strategies assist firms to increase their market share? (8)
- [40]**

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QUESTION 3: CONTEMPORARY ECONOMIC ISSUES 40 MARKS – 20 MINUTES

- 3.1 Answer the following questions.
- 3.1.1 Give TWO examples of places or events that form part of cultural tourism. (2)
- 3.1.2 How will a sound political climate lead to an increase in tourist figures? (1 x 2) (2)
- 3.2 Study the cartoon below and answer the questions that follow.



[Source: *Internet Globalisation*, 22 February 2013]

- 3.2.1 What is the meaning of the *greenhouse effect*? (2)
- 3.2.2 Why is it necessary to prevent global warming at all times? (2)
- 3.2.3 Name ONE international convention/protocol against global warming. (2)
- 3.2.4 Explain how the market fails to protect the environment. (4)

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- 3.3 Study the table below and answer the questions that follow.

EXPECTED GDP: R51,1 billion		
Tourist group	Volume of local tourism market (number of trips)	Value of local market (%)
Visits to family and friends	32	37,2
Holiday makers	8,1	44,5
Religion	5,3	4
Business	3,8	12,8
Medical reasons	0,8	14

[Fictitious figures]

- 3.3.1 Which tourist group contributed most (%) to the local economy? (2)
- 3.3.2 Determine the percentage contribution to the gross domestic product by people visiting friends and family. (2)
- 3.3.3 Why do you think that tourist figures increased locally after 1994? (2 x 2) (4)
- 3.3.4 How can tourism eradicate poverty in South Africa? (2 x 1) (2)
- 3.4 Discuss taxation as a fiscal measure to combat inflation. (4 x 2) (8)
- 3.5 Discuss why the loss of indigenous knowledge requires international measures. (4 x 2) (8) **[40]**

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QUESTION 4: MICROECONOMICS & CONTEMPORARY ECONOMIC ISSUES
40 MARKS – 20 MINUTES

- 4.1 Answer the following questions.
- 4.1.1 Name TWO characteristics of monopolistic competition. (2 x 1) (2)
- 4.1.2 What is the value of the production price index (PPI) as an inflation indicator? (1 x 2) (2)
- 4.2 Study the extract below and answer the questions that follow.

TIME RIFE FOR SMART TRANSPORT

Motorists will have to reconsider their transport options in the light of current petrol price hikes. According to Findalift.co.za many motorists drive to work causing millions of empty seats daily. Registering with Findalift will bring you into contact with people traveling the same route on a daily basis. Sharing the total cost of travelling 25 km daily will save you more than R6 500 every year – four people per vehicle will bring this saving up to R10 000. The Universities of Cape Town and Stellenbosch have already registered their students and employees to lower their travel costs.

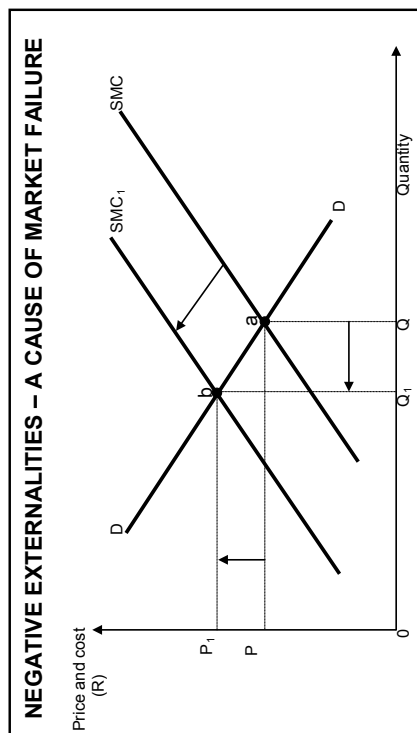
[Adapted from *Beeld*, March 2013]

- 4.2.1 Define the concept *inflation*. (2)
- 4.2.2 Explain the influence Findalift might have on consumer consumption expenditure. (4)
- 4.2.3 What impact will reduced petrol costs have on savings and investment in general? (4)

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- 4.3 Study the graph below and answer the questions that follow.



- 4.3.1 Define the concept *market failure*. (2)
- 4.3.2 Give ONE example of a negative externality. (1)
- 4.3.3 Which curve indicates the social cost to society? (1)
- 4.3.4 Explain how negative externalities can lead to market failure by using the data given in the above graph. (6)
- 4.4 Explain inefficiency in the economy as a consequence of market failure. (4 x 2) (8)
- 4.5 What are the effects of taxes and subsidies on the South African economy? (4 x 2) (8)

[40]

TOTAL SECTION B: 80

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SECTION C

Answer any ONE of the two questions in this section in the ANSWER BOOK.

Your answer will be assessed as follows:

STRUCTURE OF THE ESSAY:		MARK ALLOCATION:
Introduction		Max. 2
Body: Main part: Discuss in detail/in-depth discussion/Examine/Critically discuss/Analyse/Compare/Evaluate/Distinguish/Explain/Assess/Debate		Max. 26
Additional part: Give own opinion/Critically discuss/Evaluate/Critically evaluate/Draw a graph and explain/Use the graph given and explain/Complete the given graph/Calculate/Deduce/Compare/Explain/Distinguish/Interpret/Briefly debate		Max. 10
Conclusion		Max. 2
TOTAL		40

QUESTION 5: MACROECONOMICS 40 MARKS – 35 MINUTES

Markets are broadly categorised into perfect and imperfect markets. However, in reality very few examples of perfect markets exist.

- Examine the conditions of a perfect market in detail. (26 marks)
- Draw a clearly labelled graph to show economic profit for an individual producer in the market. (10 marks)

[40]

QUESTION 6: CONTEMPORARY ECONOMIC ISSUES 40 MARKS – 35 MINUTES

Tourism is one of the fastest growing industries worldwide.

- Critically discuss the effects of tourism. (28 marks)
- Evaluate how tourism benefits the households in your community by using appropriate examples. (10 marks)

[40]

TOTAL SECTION C: 40
GRAND TOTAL: 150

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SECTION A (COMPULSORY)

QUESTION 1

1.1 MULTIPLE-CHOICE QUESTIONS

- 1.1.1 A (MC = AVC) ✓✓
 - 1.1.2 C (regulated) ✓✓
 - 1.1.3 C (implicit) ✓✓
 - 1.1.4 A (artificial) ✓✓
 - 1.1.5 B (demand-pull inflation) ✓✓
 - 1.1.6 A (labour) ✓✓
 - 1.1.7 B (eco) ✓✓
 - 1.1.8 B (fiscal) ✓✓
- (8 x 2) (16)

1.2 MATCHING ITEMS

- 1.2.1 B (items that have highly volatile prices are excluded from the CPI basket) ✓
 - 1.2.2 A (price increases combined with high unemployment) ✓
 - 1.2.3 H (occurs due to global warming) ✓
 - 1.2.4 I (the flow of residual emissions exceeds the natural environment's capacity to absorb them) ✓
 - 1.2.5 E (two industries that dominate a particular market) ✓
 - 1.2.6 C (when it is impossible to increase the welfare of one without decreasing the welfare of another) ✓
 - 1.2.7 D (often under-produced by the market e.g. education) ✓
 - 1.2.8 G (average revenue = average costs) ✓
- (8 x 1) (8)

1.3 IDENTIFY THE CONCEPT

- 1.3.1 Oligopoly ✓
 - 1.3.2 Maximum prices ✓
 - 1.3.3 Marginal cost ✓
 - 1.3.4 Conservation ✓
 - 1.3.5 Consumer Price Index ✓
 - 1.3.6 Cost push inflation ✓
- (6 x 1) (6)

TOTAL SECTION A: 30

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Department:
Basic Education
REPUBLIC OF SOUTH AFRICA

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SENIOR CERTIFICATE

GRADE 12

ECONOMICS P2
EXEMPLAR 2014
MEMORANDUM

MARKS: 150

This memorandum consists of 14 pages.

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Economics/P2	NSC – Grade 12 Exemplar – Memorandum 3	DBE/2014	Economics/P2	NSC – Grade 12 Exemplar – Memorandum 4	DBE/2014
SECTION B					
Answer TWO of the three questions from this section in the ANSWER BOOK.					
QUESTION 2: MACROECONOMICS					
2.1	2.1.1	<ul style="list-style-type: none"> BEE✓ affirmative action✓ land restitution✓ land redistribution ✓ property subsidies (for RDP houses) ✓ 	2.4	<ul style="list-style-type: none"> Market signals, e.g. price helps to allocate resources through demand and supply. ✓✓ Goods supplied by the government such as roads, bridges etc. are provided free. ✓✓ With the absence of market signals, decisions on the desirability of a project may be subjective. ✓✓ Objective criteria may be required to ensure economic efficiency in resource allocation. ✓✓ CBA brings greater objectivity to decision making. ✓✓ This is done by identifying all the relevant benefits and costs of a project where an informed decision can be made✓✓ 	(8)
2.2	2.2.1	The long run is the period of production where all factors can change. The time is long enough for variable and fixed factors to change✓✓	2.5	<ul style="list-style-type: none"> An important aspect of non-price competition is to build brand loyalty, ✓ product recognition✓ and product differentiation. ✓ This is done by means of advertising and marketing. As a result, firms tend to spend a substantial amount of money on this. ✓✓ Other forms of non-price competition include: <ul style="list-style-type: none"> extended shopping and business hours✓✓ doing business over the internet✓✓ after-sales services✓✓ loyalty rewards for customers✓✓ In-store competitions✓✓ door-to-door deliveries✓✓ 	(8) [40]
	2.2.2	100✓		(Any 4 x 2)	
	2.2.3	The negative sloping demand curve means that more goods are sold at low prices✓, hence additional revenue will decrease as more goods are sold. ✓			
2.2.4		Unit profit: $25 - 19 = 6$ ✓✓ Total profit: $6 \times 100 = R600$ ✓✓ OR TR – TC ✓ $(25 \times 100) - (19 \times 100) = R600$ ✓			
2.3	2.3.1	A cartel is a group of producers working together to form a monopoly by fixing prices. ✓✓			
	2.3.2	Oligopoly✓			
	2.3.3	They received information when AF-FSL Glass had applied for leniency for their part in collusive behaviour. ✓✓			
	2.3.4	<ul style="list-style-type: none"> Consumers will pay higher prices. ✓✓ Competition will be eliminated which could result in poor quality goods. ✓✓ Supply will be reduced which will affect employment 			
	2.3.5	Competition Appeal Court✓			
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Economics/P2	5	NSC – Grade 12 Exemplar – Memorandum	DBE/DBE/2014	Economics/P2	6	NSC – Grade 12 Exemplar – Memorandum	DBE/2014
QUESTION 3: CONTEMPORARY ECONOMIC ISSUES							
3.1	3.1.1	<ul style="list-style-type: none">• Museums ✓• Art galleries ✓• Archaeological sites ✓• Festivals ✓• Sports events ✓ Any other relevant fact		3.4	<ul style="list-style-type: none">• Direct taxation increased ✓✓ less money available for consumption expenditure by consumers ✓✓• Indirect taxation increased ✓✓ as part of a restrictive fiscal policy government can reduce its spending or increase taxation e.g. sins tax (2 x 4) (8)		
	3.1.2	<ul style="list-style-type: none">• Where government intervenes to preserve environmental assets more tourists will visit a country ✓✓• Better control and management of e.g. indigenous forests will maximize a country's income over the long run ✓✓ Any other relevant fact	(2)	3.5	<ul style="list-style-type: none">• Today's tourists seek authenticity and uniqueness at destinations ✓✓• They want to understand the indigenous culture, history and environment and how local people live and work ✓✓• Of importance is the World Heritage Sites, e.g. Mapungubwe, Vredefort Dome, Sterkfontein Caves and Robben Island ✓✓• Environmental World Heritage Sites represent the extreme of our indigenous environmental uniqueness, e.g. iSimangaliso Wetland Park (4 x 2) (8) [40]		
3.2	3.2.1	Pollutants contribute to a layer or blanket in the atmosphere that traps heat ✓✓	(2)				
	3.2.2	There is a steady increase in the average temperature of the earth's near-surface air and oceans that influences all economic sectors like agriculture and transport negatively ✓✓	(2)				
	3.2.3	<ul style="list-style-type: none">• Kyoto protocol ✓✓• Montreal protocol ✓✓ Any other acceptable answer	(1 x 2) (2)				
	3.2.4	<ul style="list-style-type: none">• The environment is a common resource ✓✓ many parts of the environment are not privately owned e.g. the sea• Externalities ✓✓ when people pollute the environment costs are borne by others• Lack of knowledge ✓✓ people cause damage without realizing it• Carelessness ✓✓ people continue with harmful practices and leave future generations to worry about the consequences	(4)				
3.3	3.3.1	Holiday makers with a 44,5 % share ✓✓	(2)				
	3.3.2	$\frac{51,1 \times 37,2}{100} = 19\% \checkmark \checkmark / 19\% \checkmark \checkmark$	(2)				
	3.3.3	<ul style="list-style-type: none">• Safety ✓✓• Increased media coverage ✓✓• Interest in politics ✓✓• Interest in sport ✓✓• Improved infrastructure ✓✓	(2 x 2) (4)				
	3.3.4	<ul style="list-style-type: none">• Job creation – jobs can be provided immediately ✓✓• Entrepreneurial opportunities ✓✓• Tourism allows rural people to share in the benefits of tourism development ✓✓ Any other relevant fact	(2)				
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SECTION C

Answer ONE question from this section in the ANSWER BOOK.

STRUCTURE OF ESSAY:		MARK ALLOCATION:
Introduction		Max. 2
Body:		
• Main part: Discuss/Distinguish/Differentiate/Explain/Analyse /Evaluate/Assess		Max. 26
• Additional part: Use/Draw/Sketch a graph/diagram .../ Deduce .../Outline/Briefly explain/Expand on .../Your own opinion		Max. 10
Conclusion		Max. 2
TOTAL		40

QUESTION 5: MACROECONOMICS 40 MARKS – 25 MINUTES

Markets are broadly categorised into perfect and imperfect markets. However, in reality very few examples of perfect markets exist.

- Examine the conditions of a perfect market in detail. (26 marks)
- Draw a clearly labelled graph to show economic profit for an individual producer in the market. (10 marks)

[40]

Introduction

It is a market structure with a large number of participants who are price-takers.

✓ The price is determined by the market demand and supply. This market is most efficient in the allocation of resources ✓✓

Max (2)

BODY:

Characteristics:

- a) **Products must be homogenous (i.e. identical).** ✓
- Products must be identical. There should be no differences in style, design and quality. ✓✓
 - In this way products compete solely on the basis of price and can be purchased anywhere. ✓✓
 - If products differ, sellers can persuade buyers to buy their more expensive products by grading them. ✓✓ E.g. The markets for maize and coal consist of homogenous products which are graded. Grade 1 fetches a higher price than other grades.

- b) **There should be a large number of buyers and sellers.** ✓

- It should not be possible for one buyer or seller to influence the price.
- When there are many sellers the share of each seller to the market is so small that the seller cannot influence the price. ✓✓
- Sellers are price-takers, they accept the prevailing market price. If they increase prices above the market price, they will lose customers. ✓✓.

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- c) **No preferential treatment/discrimination**✓

- Collusion occurs when buyers and sellers make an agreement to limit competition. In a perfect market no collusion takes place. ✓✓
- Buyers and sellers base their actions solely on price, homogenous product fetch the same price and therefore no preference is shown for buying from or selling to any particular person. ✓✓

- d) **Free competition/Unregulated market:** ✓

- Buyers must be free to buy whatever they want from any firm and in any quantity. ✓✓
- Sellers must be free to sell what, how much and where they wish. ✓✓
- They should be no state interference and no price control. ✓✓
- Buyers should not form groups to obtain lower prices nor should sellers combine to enforce higher prices. ✓✓

- e) **Efficient transport and communication**✓

- Efficient transport ensures that products are made available everywhere. ✓✓
- In this way changes in demand and supply in one part of the market will influence the price in the entire market. ✓✓
- Efficient communication keeps buyers and sellers informed about market conditions. ✓✓

- f) **All participants must have perfect knowledge of market conditions.** ✓

- All buyers and sellers must be fully aware of what is happening in any part of the market. ✓✓
- Technology has increased competition as information is easily obtained via the Internet. ✓✓

- g) **Freedom of entry/exit:** ✓ There is complete freedom of entry and exit, that is to say the market is fully accessible. ✓✓ Buyers and sellers are completely free to enter or to leave the market. Entry should not be subject to any restrictions in the form of legal, financial, technological or other barriers that curtail the freedom of movement of buyers and sellers. ✓✓

- h) **Mobility of factors of production:** ✓ All factors of production are completely mobile, ✓✓ in other words labour, capital and all other factors of production can move freely from one market to another. ✓✓

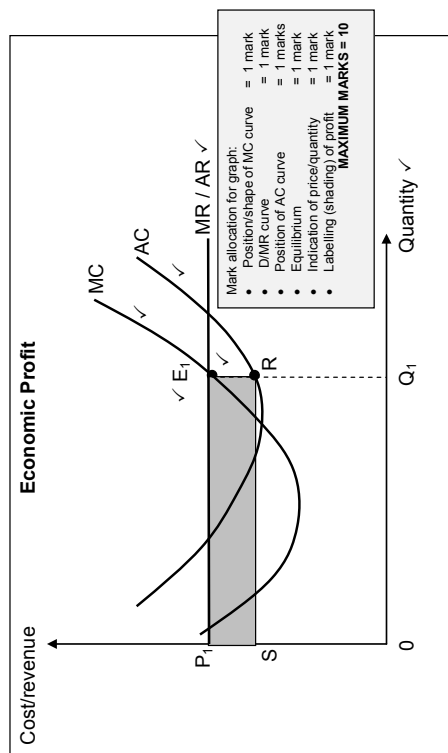
- i) **No collusion:** ✓ Collusion between sellers does not occur. ✓✓ In a perfectly competitive market, each buyer and seller acts independently from one another. Collusive practices are illegal in South Africa, according to the Competition Act 1998. ✓✓

Max. 26

NOTE: A maximum of 8 x 1 marks will be allocated for headings

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BODY: ADDITIONAL PART**Conclusion**

The characteristics above indicate that the market has to meet strict requirements before it can be described as perfectly competitive ✓✓
Although there very few examples, the conditions of a perfect market does serve a frame of reference when studying other markets. ✓✓

(Any other relevant conclusion)

(Max. 2)**(Max. 10)**

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QUESTION 6: CONTEMPORARY ECONOMIC ISSUES 40 MARKS – 25 MINUTES

Tourism is one of the fastest growing industries worldwide.

- Critically discuss the effects of tourism. (28 marks)
- Evaluate how tourism benefits the households in your community by using appropriate examples. (10 marks)

[40]**Introduction**

In general we say that tourism involves people moving from their usual place of residence to a destination where they make use of the facilities and take part in activities ✓✓

Any other relevant definition.

(Max. 2)**BODY: MAIN PART****1.1 GDP ✓**

- Biggest impact on services industry than on agriculture or manufacturing ✓✓
- Indirect contribution: service-based industry – responsible for 65% of GDP in developed economies and 40% of GDP in developing countries ✓✓
- Direct contribution: contribution of 6,8% of GDP compared to 11,6% worldwide. ✓✓

1.2 Employment ✓

- Employs 7% of SA workforce (1,12 million) ✓✓
- largest provider of jobs and earner of foreign exchange, due to:
 - ❖ Tourism is labour intensive ✓✓
 - ❖ Tourism employs many skills ✓✓
 - ❖ Tourism can provide immediate employment ✓✓
 - ❖ Tourism provides entrepreneurial opportunities ✓✓

1.3 Poverty ✓

- Tourism is fast + effective distribution mechanism in development of rural areas ✓✓
- Prime tourism attractions located in rural areas ✓✓
- Promote balanced + sustainable form of development ✓✓
- Provides alternative to urbanisation, permitting people to continue - a rural family existence, enfranchising both women and youth ✓✓
- Offers diversity of income sources to poor people:
 - ❖ Allowing them a stake
 - ❖ Empowering them
 - ❖ Creating partnerships ✓✓

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