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General Certificate of Education  
January 2011

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## Economics

Assessment Unit A2 1

Business Economics

[AE211]

FRIDAY 28 JANUARY, AFTERNOON

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### TIME

2 hours.

### INSTRUCTIONS TO CANDIDATES

Write your Centre Number and Candidate Number on the Answer Booklet provided.  
Answer **Question 1** and **one** question from **Questions 2, 3 or 4**.

### INFORMATION FOR CANDIDATES

The total mark for this paper is 80.

Quality of written communication will be assessed in all questions **except 1(a)**.

Figures in brackets printed down the right-hand side of pages indicate the marks awarded to each question or part question.

### ADVICE TO CANDIDATES

You are advised to take account of the marks for each part question in allocating the available examination time.

## Question 1

Study the information below and answer the questions that follow.

### Case study: Trouble brewing for UK pubs

#### Source 1

#### The UK pub market – key data

| Year | Pub company | Independent | Brewery | Total |
|------|-------------|-------------|---------|-------|
| 2003 | 31700       | 19073       | 8900    | 59673 |
| 2004 | 31500       | 18700       | 9200    | 59400 |
| 2005 | 31000       | 17800       | 9450    | 58250 |
| 2006 | 30400       | 17700       | 9400    | 57500 |
| 2007 | 29742       | 17245       | 9345    | 56332 |
| 2008 | 29564       | 16165       | 9107    | 54836 |
| 2009 | 28336       | 16039       | 9089    | 53464 |

*UK Public Houses Market Development Report (October 2009) © Crown Copyright - House of Commons Business & Enterprise Committee report on pub companies (April 2009)*

**Fig. 1: Structure of the UK pub industry – number of UK pubs by ownership 2003–2009**

| Pub company     | Number of outlets |
|-----------------|-------------------|
| Enterprise Inns | 7581              |
| Punch Taverns   | 7287              |
| Admiral Taverns | 2386              |
| Marston's       | 1932              |
| Greene King     | 1428              |

*© Crown Copyright House of Commons Business & Enterprise Committee report on pub companies (April 2009)*

**Fig. 2: UK pub companies and number of outlets 2009**

## Source 2

### UK is losing up to 52 pubs a week

UK pubs closed at a rate of 52 per week in the first half of 2009 – a third more than the same period in 2008 – according to a report published by the British Beer and Pub Association. The rate of closures was the fastest since the number of UK pubs began being tracked in 1990.

The report stated that the UK pub industry was facing the most difficult period in its history, with one in twenty pubs facing closure and almost all of them reporting that they expect to cut jobs over the next year.

The reasons for the difficulties are clear, the report said. The biggest impact is the recession. There are fewer people going out and fewer people spending money in pubs and bars.

However, the economic pressures of the recession have been added to by a number of other factors such as the smoking ban, the fact that excise duty on alcohol has risen by 45% since 2000, regulatory burdens and supermarkets selling alcohol as a loss leader.

Not everyone, though, is convinced that all pub closures are simply a result of external factors. Mark Hillman, owner of the “Bull and Duck” argues that, in most cases, pubs fail because they do not meet the needs of their customers. “Many pubs are closing because they have failed to modernise” he said. “These pubs are from a period of history and what they offer is no longer relevant, society has changed – the pubs need to change too.”

*Adapted from © BBC News at [bbc.co.uk](http://bbc.co.uk)*

### Source 3

#### Pub companies face OFT probe

Until 1989 most UK pubs were owned by breweries, but leased to tenants who were “tied” to selling only those products produced by the brewery. This system was broken up in 1989 because of concerns that brewery dominance of the UK pub industry was anti-competitive. The legislation which brought this about, known as the “Beer Orders”, stipulated that breweries should be limited to owning a maximum of 2000 tied pubs.

There then emerged a new business model, that of the pub company or “pubco”. In this model, a company controls a series of pubs, which it either manages itself, or leases to tenants. However, some analysts argue that the situation has not really changed. This is because most, although not all, pub companies insist that tenants only buy products supplied by the pubco itself.

Pub companies argue that this tied arrangement benefits pub companies, lease holders and customers alike. They argue that the tied arrangement allows them to avail of purchasing and distribution economies of scale with the benefits being shared equally between the three. A representative of one of the largest pub companies stated that “the tied arrangement allows us to buy in bulk and pass the savings on to our tenants and customers. In addition it allows us to have some control over the quality of products sold in our establishments and, since we generally purchase the most popular brands, we can ensure that our customers are able to purchase the brands they prefer”.

However, like the brewery pub ownership model, the pubco model and the pubco tie have generated a great deal of criticism. In particular, there have been concerns that pubcos (which are not limited to a maximum of 2000 pubs) are restricting competition and are profiteering at the expense of landlords and customers.

One industry analyst stated that “Almost 40% of pubs in the UK are owned by the five largest pub companies. While no one company by itself dominates the market, all five have significant market power which allows them to operate on profit margins in excess of 50%. To put this in perspective, the profit margin of a typical pubco is nine times greater than that of Tesco.”

One pub landlord went further and called on the government to outlaw all tied arrangements and place a limit on the number of pubs owned by any one company. “Tied arrangements are anti-competitive and hurt landlords, customers, and local brewers, the ‘beer tie’ should be scrapped immediately and the large pub companies broken up to ensure that, like the breweries, no company can own more than 2000 pubs.”

*Source: adapted from various sources August 2009*

## Source 4

### The social costs and benefits of pubs

Community pubs are one of the UK's oldest and most popular social institutions. A good pub is more than just a private company selling alcohol for a profit. A good pub provides a meeting place where social networks are strengthened and extended. A good pub supports local charities and sports teams while providing a place to drink in a safe, regulated and controlled environment. A good pub can improve the health of its customers by providing a space where friends can relax after a hard day's work.

However, every industry has its Achilles' heel – go into any city centre on a Saturday night and you will see binge drinking on a terrifying scale. Millions of livers in the UK are being mistreated. The NHS bill for alcohol abuse now runs at an estimated £2.7bn per year.

So who is to blame for this binge drinking problem? Unruly teens? The drinks companies? Celebrities? The government?

None of the above, says Kevin O'Boyle, a drinks industry analyst. "The blame for the current malaise can be placed squarely at the door of pub landlords and pub companies. They aim to drain every last penny from their customers, regardless of the impact on their health or well-being. I appreciate that all businesses need to make a profit. However, I feel that it is morally wrong for pub companies to seek to maximise profits at the expense of their social and environmental responsibilities."

*Source: adapted from various sources August 2009*

- 1 (a) Describe the changes in the structure of the UK pub industry between 2003 and 2009 as shown in **Fig. 1**. [5]
- (b) Explain the causes of the decline in the number of UK pubs. [10]
- (c) Assess the extent to which the UK pub market is oligopolistic. [10]
- (d) Evaluate the view expressed in Source 4 that "it is wrong for pub companies to seek to maximise profits at the expense of their social and environmental responsibilities". [15]

## Essays:

Answer **one** question from **Questions 2, 3 or 4.**

### 2 “Competition Commission criticised for being weak and ineffective”

- (a) Explain why some industries are natural monopolies. [15]
- (b) Evaluate the policies that governments could use to deal with market dominance and the abuse of monopoly power. [25]

### 3 “Mergers should be banned”

- (a) Explain the difference between organic growth and growth by acquisition or merger. [15]
- (b) Critically examine the view that mergers are against the public interest and should be outlawed. [25]

### 4 “Firms’ behaviour at odds with economic theory”

- (a) Explain how the short run price and output decisions of a profit maximising firm would differ from those of a revenue maximising firm. [15]
- (b) Critically examine the view that traditional economic models of firms’ behaviour are outdated and unrealistic. [25]

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**THIS IS THE END OF THE QUESTION PAPER**

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