

A2 Economics Unit 4 04 June mark scheme

(1) B 1 mark

Definition of total revenue (1 mark) Revenue per unit, or price, or AR, is EG or BD (1 mark) therefore $DE \times BD = TR$ (1 mark)

Also award: the profit maximising firm will produce where $MR = MC$

(1 mark), shading the relevant area (1 mark)

(2) C 1 marks

Definition of allocative efficiency ($p = MC$) (1 mark). Diagram showing firm in perfect competition and that it is allocatively efficient in short (1 mark) and long run (1 mark).

Also award: at least one assumption of perfect competition (1 mark) verbal argument about efficient resource allocation issue (1 mark) 3 marks

(3) D 1 mark

Definition of horizontal integration (1 mark) A potential benefit such as purchasing economies of scale (1 mark). Tying the benefit to the hotel industry e.g. buying food for the hotel restaurants (1 mark). 3 marks

(4) E 1 mark

Explanation and examples of two public interest issues e.g. potential negative effects of resulting monopoly power such as higher prices, lower quality of service etc. (2 marks). Tying the issues to the water industry (1 mark).

Also award: worries that there would be a reduction in competition (1 mark) 3 marks

(5) C 1 mark

Reference to fact that RPI stands for rate of inflation (1 mark). Explanation that X stands for expected efficiency improvements (1 mark) link to being able to keep profits from further efficiency gains (1 mark) 3 marks

(6) C 1 mark

Definition of concentration ratio (1 mark). Meaning of high

concentration (1 mark) explanation this encourages cartels (1 mark). Also award: definition of cartel (1 mark) 3 marks

(7) E 1 mark

Definition of price discrimination (1 mark). Explanation of link from price discrimination to greater supernormal profits - may be in the form of a diagram, or written argument (2 marks). 3 marks

(8) A 1 mark

Definition of cost-plus pricing (1 mark) Diagram or written explanation that with flat AC a constant mark up is a possible strategy for tacit collusion for a firm worried about possible price wars (2 marks) Also award: diagram showing flat AC (1 mark). 3 marks

(9) D 1 mark

Definition of contestability in terms of low barriers to exit through low sunk costs (1 mark). Explanation of advertising expenditure as sunk cost (1 mark) application to chewing-gum (1 mark). 3 marks

(10) C 1 mark

Candidates may achieve full marks with a diagram only so long as impact of rising AC on profit is indicated, and the unchanging price, output and falling profit are marked (3 marks). Also accept equivalent written explanations: no effect on p, q because $MR = MC$ unaffected.

Fall in profit as costs rise with no change in revenue. (3 marks) 3 marks Also award: definition of AC (1 mark)

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Question 11

(a) Standard diagram showing $MR = MC$ and price - diagram must show price for both marks (2 marks). A brief statement the firm will be profit maximising at $MR=MC$ (1 mark) statement that this is appropriate behaviour when a firm is "safe from competition" 4 marks (1 mark).

(b) Diagram showing fall in demand both AR&MR (1 mark) resulting fall in price (1 mark), fall in output (1 mark) and fall in profit (1 mark). For just a Supply and Demand diagram showing fall in demand and lower price (1 mark)

Written explanation of diagram - reference to fall in ARJMR, description of changes in price, output and profit - or further elaboration of consequences (2 marks).

Candidates may achieve up to 6 marks for a written explanation with no diagram but only if they have covered all the issues described above. 6 marks

(c) Use of 2 items of data up to 2 marks each (4 marks) Fig 1: perhaps Reuters underperforming relative to other firms of equivalent market value. Fig 2: significant levels of profit early on. Also Fig 2: upward trend in revenue versus falling trend in profit towards the end. Extract 1: A great deal of effort to cut costs to raise profits. Perhaps an attempt at long-run profit maximising? Also, as a plc company there is a divorce between ownership and control - although the text refers to the cost cutting demanded by shareholders.

Evaluation (4 marks) to awarded if candidate in discussing the data has referenced: movements in revenue versus costs or profits, long run versus short run issue, some sense of conflicting

evidence, assessment of magnitude of figures involved, conclusion looking at balance of evidence. Any two evaluation arguments to a maximum of (4 marks). 8 marks

(d) Definition of allocative inefficiency, $P > MC$. (1 mark) Explanation that with limited competition price may rise above marginal costs (2 marks)

Definition of productive inefficiency (firm not at min AC) (1 mark) evidence in extract to support this, or diagram showing productive inefficiency at $MR=MC$ on a monopoly diagram (2 marks)

Also award definition (1 mark) and explanation (2 marks) of other kinds of economic inefficiency, e.g. X-inefficiency, dynamic inefficiency. 6 marks

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Question 12

(a) Definition of vertical integration (2 marks), application to railway industry identifying at least two different stages of production e.g. track provision, leasing of trains, train operating companies (4 marks). 6 marks

Diagram showing monopoly showing profit before intervention (1 mark) new intervention price lower than before (1 mark)

resulting fall in profit (1 mark)

Written analysis, explaining these changes (3 marks).

Also award: reference to regulator acting as a surrogate for competition

(1 mark). 6 marks

A reduction in charges to the TOC's will reduce their costs and these may be passed on to consumers, increased consumer surplus, alternatively, the TOC's may take this opportunity to reinvest in better services, Also award: reduced entry costs may encourage competition and therefore lower prices and better services. Any two arguments up to (3 marks) each.

Evaluation 4 marks - up to three marks for each of any two points to a max of 4: firms may keep the extra profit or return it to shareholders, reduced costs may still not compensate for reduced franchise terms, benefits may take a long time to come, the biggest problem may be Network Rail not the TOC's?

Prioritisation of benefits. 10 marks

Analysis: (6 marks) Definition of economies of scale: fall in long-run (1 mark) average costs (1 mark) Identification of two potential economies of scale (2 marks) Application to provision of rail infrastructure (2 marks). Also award: natural monopoly diagram (1 mark)

Evaluation: (4 marks). Any two points up to a maximum of 4:

diseconomies of scale, unpredictable rises in costs during expansion, relative significance of the economies considered, increasing inefficiency as the state takes greater control again. 10 marks

(d) Understanding what a franchise period is - may well be implicit (2 marks)

Analysis of at least two advantages or disadvantages of consequences of shorter franchises (3 marks)

Evaluation: consideration of other side of the argument, or discussion of the particular significance of the issues discussed, or a conclusion discussing the net benefits (3 marks)

Advantages to the economy might include an ability to get rid of complacent, inefficient or incompetent train operating companies, as a discipline for the incumbent firms to achieve efficiency and quality of service.

Earlier entry of dynamic new companies

Disadvantages might include:

a short franchise may deter the taking of risks - leading to poor investment

less incentives for innovation

dissuading new entrants

8 marks