Examiners' Report
June 2017

GCE Economics A 9EC0 01

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Introduction

This paper (9EC0 01) was the first examination paper for the new A Level from the specification launched in September 2015. Overall, the performance was impressive across the range of ability with the mean score being 64.3. 9EC0 paper 01 tested candidates on their knowledge and understanding of topics covered in Theme 1 and Theme 3 of the specification content. There was evidence that candidates were well prepared across the specification in new and mainstream areas, Theme 1 and Theme 3 understanding and exam technique, with little evidence of candidates running out of time. The paper comprises three sections. Section A comprises a range of multiple-choice and short-answer questions based on a spread of specification elements in Theme 1 and Theme 3. Section B focused more on Supermarket price wars, food waste and possible mergers, a topical market in the UK economy, with a wide range of data provided from which candidates could draw from to gain application marks. Section B comprises one data response question broken down into a number of parts, the style of the questions are of a consistent format to be expected in years to come. Section C included a choice of extended open-response questions with candidates selecting one from a choice of two; these are not directly related to the data unlike the essay choice in 8EC0 01.

The time available for the paper is two hours and candidates are advised to spend 30 minutes on the 25 marks available in Section A; one hour on the 50 marks available in Section B and 30 minutes on the 25 marks available in Section C. Many candidates showed timing problems on the 15-mark section and the 20-mark essay, having spent a disproportionate amount of time on Section A. Each short question was broken down into a non-supported multiple choice questions, using option boxes which were dealt with well, plus a short question or questions worth 4 or 2+2 or 2+1+1 marks. Four-mark responses were often impressive with good subject knowledge (K), analysis (An) and application (App) where required. There was plenty of evidence of concise responses deploying exam technique effectively to allow candidates more time on Section B and C.

Quantitative questions were usually dealt with well with candidates soundly heeding advice to show their working, although a few candidates would benefit from making clear their final answer(s). Diagrams were not always accurately drawn and fully labelled and some candidates would have benefited from a careful explanation of them, this was truer for Theme 1 diagrams. A significant number of candidates did not indicate which essay they were answering by marking a cross in the box available, although their written responses did make it clear.

Candidates grasped the need to provide logical chains of reasoning with their analysis and applying theory and context to questions. Most candidates grasped the need in the 10, 12, 15 and 25 mark responses that a limited number of points evaluated in depth would be sufficient to access top levels rather than the legacy specification approach where a specific number of points were required. More successful extended answers applied the same approach of carefully explained evaluation applying context or theory to answer the question but there was scope for improvement for many in avoiding Level 1 evaluation (L1e) which does not go beyond the generic or thin opportunity cost or magnitude type response. In some cases evaluation was not evident, restricting a candidate's ability to access top marks. For top level evaluation (L3e) in the essays, 'informed judgement' is required – many candidates attempted this as a conclusion with mixed success – highly effective responses were critical of the assumptions underlying the theory initially put forward and were able to recognise different viewpoints in coming to their own clear judgement. There is a substantial weighting for evaluation marks (25 out of 75 marks) in the level based responses. An 8 mark

question comprises 2 evaluation marks, a 10 mark question comprises 4 evaluation marks, a 12 mark comprises 4 evaluation marks, a 15 mark comprises 6 evaluation marks and a 25 mark question comprises 9 evaluation marks. Consequently, it is vital that candidates make in-depth applied evaluative comments when required by the question, as well as offering judgement using positive economics throughout, in order to avoid disappointment.

Candidates should be reminded of the importance of making sure their answers are clear and concise. A number of candidates used additional paper for Q6(c) where a one sided response would have sufficed, this may have had an impact on their timings elsewhere. In future, candidates should be reminded of the instructions and information on the front of the exam paper – 'Answer the questions in the spaces provided – there may be more space than you need.', 'The marks for each question are shown in brackets – use this as a guide as to how much time to spend on each question.'. In addition, candidates using additional sheets should make it clear on these extra sheets what question each piece of writing refers to.

Finally, candidates should be reminded to not write the answer to a question in the space provided for a different question. If a candidate needs more space to answer a question, they should use additional sheets of paper.

A conclusion should answer the question using positive economics. Candidates would benefit from attempting to weigh up theory and the sufficiency of the data as they write, to offer clear and sustained judgement. The performance on individual questions is considered in the next section of the report and there are two examples of candidate work for each one. These examples act as a guide as to why a question was well answered and also how to improve further.

Section A: multiple-choice and short-answer questions

Most candidates found this method of testing highly accessible, with the mean score at 17.9. A significant number of candidates were very well prepared and demonstrated excellent knowledge and understanding as well as the techniques involved in answering the questions; providing accurate and concise definitions and knowledge, accurate diagrams, calculations and relevant application. The multiple choice questions format provided an accessible format for candidates to select their chosen option and in order to increase candidate accessibility, future options will maintain the placing of options in alphabetical or numerical order.

Section B: data response questions

The new format for data questions met with a positive response on the whole, the mean score was 30.8. Responses to 6(a) on concentration ratio provided confident evidence of candidates' revision and good exam technique in use of four firm calculations and linked development. 6(b) and 6(c) provided an opportunity to test understanding of new specification content in looking at monopsony power on food suppliers and consumers. Nearly all candidates could define monopsony and address the questions in context; only a few became confused with a labour market understanding of monopsony. 6(d) was straightforward, with the overwhelming majority of candidates showing their ability to effectively apply the data to the key concepts in making their points and evaluating. Candidates deployed effectively Theme 3 theory to answer 6(e) although Theme 1 was also valid and awarded highly when carefully applied in depth with coherent chains of reasoning.

Section C: essay

Both essay questions were accessible to candidates though question 7 (sugar tax) proved to be considerably more popular than question 8 (revenue and profit maximisation) by a ratio of 8:1. This appears to be related to the issue of 'sugar tax' being dominant in the news although candidates need to become more comfortable in selecting an 'industry of your choice' as required for Q8. The mean score for Q7 was 15.3 whilst for Q8 the mean was 13.4.

Question 1 (a)

This is a Theme 1 question and a number of responses only stated the equilibrium price and not the quantity as requested. Candidates need to practice completing such tables as part of their exam preparation.

1 The table shows market data for e-cigarette kits. The original equilibrium price is £23.

Price £	Quantity demanded per month (000)	Quantity supplied per month (000)	New quantity demanded per month (000)	New quantity supplied per month (000)
25	5 8	9 10	8	10
24	6 9	8 9	9	9
23	7 10	7 8 —	10	8
22	8 11	6 7	11	7
21	9 12	5 6	12	6

As a result of a successful advertising campaign, demand increased by 3 000 — e-cigarette kits at all prices. At the same time production costs fell leading to an increase in supply of 1 000 e-cigarette kits at all prices.

(a) Calculate the new equilibrium price and quantity following the successful advertising campaign and the fall in production costs. Use the last two columns for your working.

(4)

9000 units
£24

1   The table shows market data for e-cigarette kits. The original equilibrium price is £23.

Price £	Quantity demanded per month (000)	Quantity supplied per month (000)	New quantity demanded per month (000)	New quantity supplied per month (000)
25	5	9	8000	10 000
24	6	8	9000	9000
23	7	7	10 000	8000
22	8	6	11000	7000
21	9	5	12000	6000

As a result of a successful advertising campaign, demand increased by 3 000 e-cigarette kits at all prices. At the same time production costs fell leading to an increase in supply of 1 000 e-cigarette kits at all prices.

(a) Calculate the new equilibrium price and quantity following the successful advertising campaign and the fall in production costs. Use the last two columns for your working.

(4)

~~Old P₁ - Score~~

The new equilibrium price is £24 and the new equilibrium quantity is 9000 per both demand and supply. This is an increase from the old equilibrium of £23 for 7000 e-cigarettes demanded and supplied.

Question 2 (a)

Another Theme 1 question. In this question it was clear who knew their PED formula and who did not. Candidates need to practice such key calculations as part of their exam preparation.

2   Between 2010 and 2015 the average price of tea in the UK increased from £7.20 per kilo to £8.48 per kilo. Over the same period the quantity of tea purchased fell from 97 million kilos to 76 million kilos.

(Source: http://www.theguardian.com/lifeandstyle/shortcuts/2015/aug/05/brew-do-you-think-you-are-why-tea-needs-to-copy-coffee-in-order-to-survive)

(a) Assume that the change in the quantity of tea purchased was only caused by the change in the price of tea. Calculate the price elasticity of demand for tea in response to the rise in its price. You are advised to show your working.

(2)

$$PED = \frac{\% \Delta \text{ in } \text{price } \text{Quantity Demanded}}{\% \Delta \text{ in price}} \qquad \frac{\text{old} - \text{new}}{\text{old}}$$

$$97 = 100\%$$
$$76 = 78.35\%$$
$$= 21.63$$
$$= 21.65$$

$$= \frac{21.65}{£17.7} = 1.217...$$

relatively elastic

ResultsPlus
Examiner Comments

This answer achieves a mark of 2/2.

This candidate has got the correct answer of 1.2, a minus or plus sign is allowed.

ResultsPlus
Examiner Tip

Some margin for rounding up/down is allowed on mark schemes but do try to be as accurate as you can with calculations.

2 Between 2010 and 2015 the average price of tea in the UK increased from £7.20 per kilo to £8.48 per kilo. Over the same period the quantity of tea purchased fell from 97 million kilos to 76 million kilos.

(Source: http://www.theguardian.com/lifeandstyle/shortcuts/2015/aug/05/brew-do-you-think-you-are-why-tea-needs-to-copy-coffee-in-order-to-survive)

(a) Assume that the change in the quantity of tea purchased was only caused by the change in the price of tea. Calculate the price elasticity of demand for tea in response to the rise in its price. You are advised to show your working.

(2)

$$PED = \frac{\% \Delta P}{\% \Delta QD}$$

$\Rightarrow$ Price ↑ of $\frac{8.48 - 7.20}{7.20} \times 100 = 17.78\%$

$\Rightarrow$ QD $\Rightarrow 100 \times \frac{76 - 97}{97} = -21.65\%$

↑ both to 2 dp

$$PED = \frac{17.78}{-21.65} = -0.8211640$$

$$= -0.82 \quad (\text{to 2 decimal places})$$

ResultsPlus
Examiner Comments

This answer achieves a mark of 1/2.

This candidate receives one mark for correct calculations of both percentages. However their formula is the wrong way around. A significant minority of candidates made this mistake.

ResultsPlus
Examiner Tip

Learn your formulas and be careful in applying the formula accurately.

Question 2 (b)

In this question it was clear who knew how to calculate revenue and who did not. A number of candidates lost a mark as 'million' was missing from their answer as the unit of measure.

(b) Calculate the change in total sales revenue for UK tea retailers between 2010 and 2015. You are advised to show your working.

(2)

in 2010 : revenue = £ 7.20 × 97 million = £698.4 mill

in 2015: revenue = £ 8.48 × 76 million = £644.48 mill

Change in revenue = 698.4 − 644.48
= £ 53.92 million
= £ 53920000

ResultsPlus
Examiner Comments

This answer achieves a mark of 2/2.

This candidate achieves full marks for providing the correct answer, being £53.9 million.
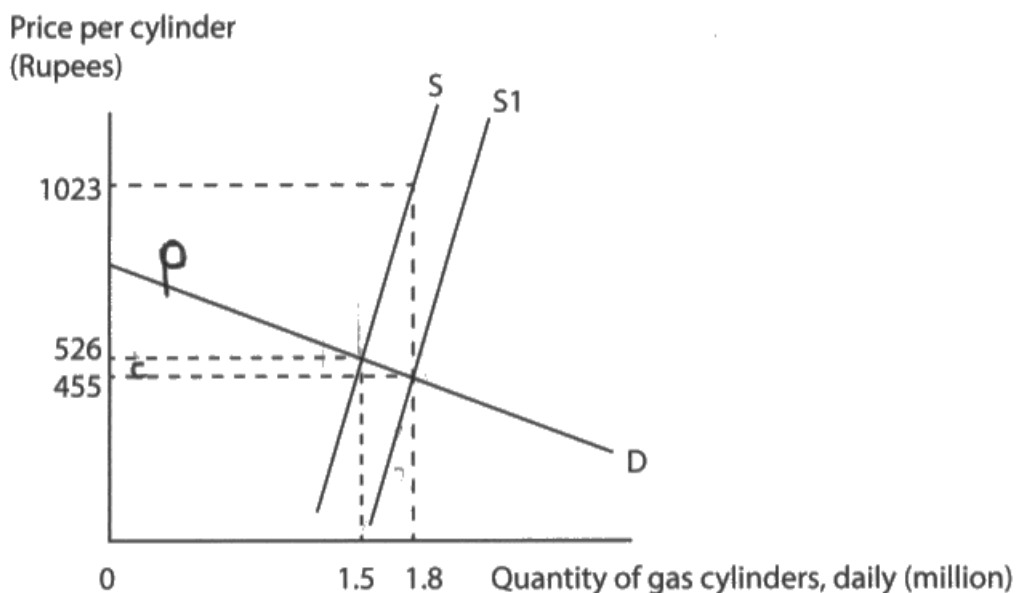
ResultsPlus
Examiner Tip

Always ensure you state the correct unit of measurement.

(b) Calculate the change in total sales revenue for UK tea retailers between 2010 and 2015. You are advised to show your working.

(2)

Total Revenue = Price × Quantity

Old Revenue = 97 × £7.20 = £698.40

New Revenue = 76 × £8.48 = £644.848

△ in revenue is a decrease of £53.92

ResultsPlus
Examiner Comments

This answer achieves a mark of 1/2.

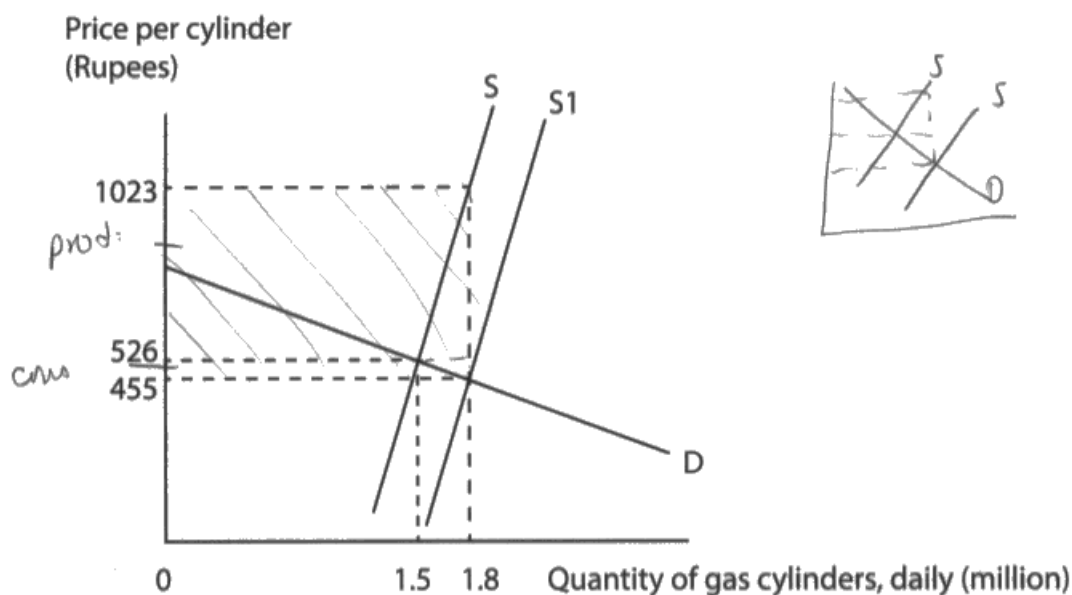This answer can only be awarded 1 mark as million, the unit of measure, is missing.

Question 3 (a)

In this question it was clear who knew how to calculate subsidy and who did not. A number of candidates lost a mark as 'million' was missing from their answer as the unit of measure. Candidates need to practice similar subsidy and tax diagrams from Theme 1.

3   The Indian government has introduced a subsidy on domestic cooking gas cylinders in the city of Mumbai. The diagram below shows the effect following the introduction of the subsidy.

(Source: https://www.iocl.com/products/indanegas.aspx and http://indianexpress.com/article/business/business-others/lpg-subsidy-fixed-at-rs-568-price-to-change-after-march/)
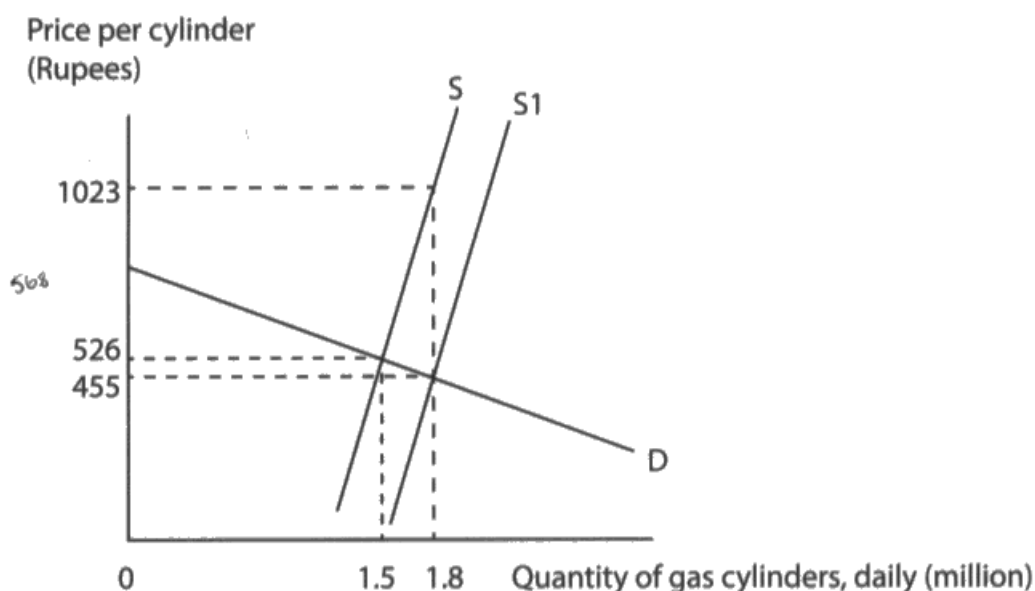
(a) Calculate the total domestic cooking gas subsidy paid daily by the Indian government. You are advised to show your working.

(2)

original = 526 × 1 500 000   = 789 000 000

new   =   455 × 1 800 000   =   814 000 000

814000000 - 789000000 =   1000000000 rupees

1023 - 455   =   568

568 × 1·8million   =   1022400000 rupees.

3 The Indian government has introduced a <u>subsidy</u> on <u>domestic cooking gas cylinders</u> in the city of Mumbai. The diagram below shows the effect following the introduction of the subsidy.

Price per cylinder (Rupees) vs Quantity of gas cylinders, daily (million)

(Source: https://www.iocl.com/products/indanegas.aspx and http://indianexpress.com/article/business/business-others/lpg-subsidy-fixed-at-rs-568-price-to-change-after-march/)

(a) Calculate the total domestic cooking gas subsidy paid daily by the Indian government. You are advised to show your working.

(2)

1023 × 1.8 = 1841.4

455 × 1.8 = 819

1841.4 - 819 = 1022.40

Question 3 (b)

Most candidates achieved full marks but a significant number of candidates lost a mark as the answers were transposed incorrectly i.e. they identified consumers as receiving 87.55 and producers 12.5%. Candidates need to practice similar subsidy and tax diagrams from Theme 1.

3 The Indian government has introduced a subsidy on domestic cooking gas cylinders in the city of Mumbai. The diagram below shows the effect following the introduction of the subsidy.

(Source: https://www.iocl.com/products/indanegas.aspx and http://indianexpress.com/article/business/business-others/lpg-subsidy-fixed-at-rs-568-price-to-change-after-march/)

(a) Calculate the total domestic cooking gas subsidy paid daily by the Indian government. You are advised to show your working.

(2)

Total domestic cooking gas subsidy = 1·8 × (1023 − 455)

= 1022·4 rupees

(b) Calculate the percentage share of the total subsidy received by:

(i) consumers

(1)

consumer receives : $1.8 \times (526 - 455)$

$= 127.8$

percentage share : $\frac{127.8}{1022.4} \times 100$

$= 12.5\%$

(ii) producers

(1)

producer receives : $1.8 \times (1023 - 526)$

$= 894.6$

percentage share : $\frac{894.6}{1022.4} \times 100$

$= 87.5\%$

3 The Indian government has introduced a subsidy on domestic cooking gas cylinders in the city of Mumbai. The diagram below shows the effect following the introduction of the subsidy.

Price per cylinder
(Rupees)

(Source: https://www.iocl.com/products/indanegas.aspx and
http://indianexpress.com/article/business/business-others/lpg-
subsidy-fixed-at-rs-568-price-to-change-after-march/)

(a) Calculate the total domestic cooking gas subsidy paid daily by the Indian government. You are advised to show your working.

(2)

1023 - 455 = 568 × 1.8 = 1022.4
1.022~~t~~

1022.4 million rupees

(b) Calculate the percentage share of the total subsidy received by:

(i) consumers

(1)

1023 - 526 = 497 × 1.8 = 894.6 ÷ 1022.4
~~=~~   = 87.5%

(ii) producers

(1)

526 - 455 = 71 × 1.8 = 127.8 ÷ 1022.4
= 12.5%

Question 4 (a)

This was a straightforward question from Theme 3 that required candidates to fully annotate carefully and correctly. One issue that some candidates faced was incomplete labelling and not carefully identifying the smaller profit/loss box.

4   In 2015 JCB, the construction equipment manufacturer, experienced a 6% fall in revenue. This resulted from a reduction in sales of construction equipment to emerging markets.

(a) Draw a cost and revenue diagram to show the likely impact of a reduction in sales of construction equipment on JCB's profits.

(4)

Area   P₁ A B C – previous profit

Area   P₂ Aˢ Bˢ Cˢ – new profit
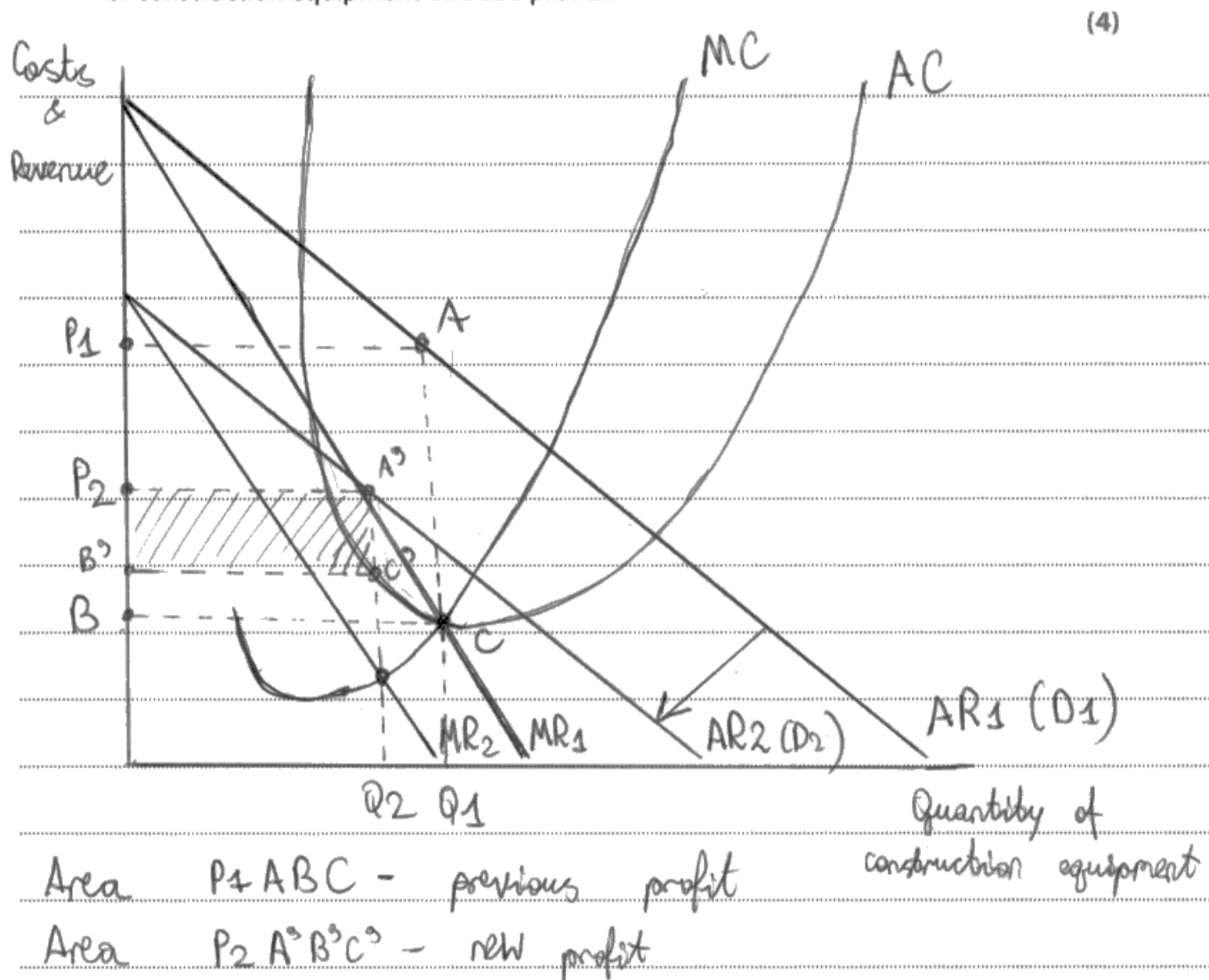
Examiner Comments

This answer achieves a mark of 4/4.

Full marks are awarded for a fully labelled cost and revenue diagram carefully annotating the fall in profits.

4   In 2015 JCB, the construction equipment manufacturer, experienced a 6% fall
    in revenue. This resulted from a reduction in sales of construction equipment to
    emerging markets.

   (a) Draw a cost and revenue diagram to show the likely impact of a reduction in sales
        of construction equipment on JCB's profits.

                                                                                    (4)

Question 5 (b)

Most candidates were able to clearly define these terms. The main problem when not awarded a mark was a failure to link to output.

(b) Explain the difference between fixed costs and variable costs.

(2)

Fixed costs are costs that have to be paid and do not change as output does for example rent or electricity whereas Variable costs are costs that change as output increases/decreases for example in Starbucks case milk, coffee cups etc. these are known as raw materials

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Examiner Comments

This answer achieves a mark of 2/2.

This is a full answer identifying the difference related to output (2/2) but also providing examples.

(b) Explain the difference between fixed costs and variable costs.

(2)

Fixed to variable costs vary (change) depending on the level of output whereas fixed costs remain the same over all levels of output, they do not change.

ResultsPlus
Examiner Comments

This answer achieves a mark of 2/2.

A correct explanation is provided.

Question 5 (c)

Most candidates were able to calculate correctly. The main problem was a failure to indicate the answer as a unit that clearly could be interpreted in pence between 29 and 30.

(c) With reference to Figure 1, calculate the profit (in pence) for a cappuccino drink.
You are advised to show your working.

(2)

13% of £2.27 = 29.51 = 30p
(227p)

ResultsPlus
Examiner Comments

This answer achieves a mark of 2/2.

A clear answer is provided.

(c) With reference to Figure 1, calculate the profit (in pence) for a cappuccino drink.
You are advised to show your working.

(2)

13% of £2·27 = 200·88
227

227 - 200·88 = 26·12p = 26p

ResultsPlus
Examiner Comments

This answer achieves a mark of 1/2.

The wrong answer is provided but one mark is awarded for 13% of £2.27 in their working.

ResultsPlus
Examiner Tip

It is always advisable to show your working in case of a computational error.

Question 6 (a)

In this question it was clear which candidates knew what the four firm concentration ratio meant. Candidates need to practice such key knowledge and why it may change as part of their exam preparation.

(a) With reference to Figure 1 and Extract A, explain **one** likely reason for the change in the four-firm concentration ratio of the supermarket sector between 2010 and 2015.

(5)

One reason for the anocra 3.6% decrease in the four-firm concentration ratio would be the change in consumer habits. Many consumers do a weekly shop at one of the top 4 supermarkets. However, now consumer are opting for more frequent trips to discount stores such as Aldi and Lidl. Because of this both Aldi and Lidls market share have increased. Consumers are habitual and the fact that new habits are being formed shows the change in the concentration ratio.

ResultsPlus
Examiner Comments

This answer achieves a mark of 5/5.

The candidate starts by calculating the four firm concentration ratio for both years and identifies that the ratio has decreased by 3.6 percentage points (benefit of doubt given here as technically it is not 3.6%); thereby picking up 2 marks for analysis and one for implicit knowledge of concentration ratio. They then go on to provide and explain the reason for the change.

ResultsPlus
Examiner Tip

Be careful in future about percentage points change and percentage change.

(a) With reference to Figure 1 and Extract A, explain **one** likely reason for the change in the four-firm concentration ratio of the supermarket sector between 2010 and 2015.

(5)

In 2010 the four firm concentration ratio in the market was 76.1%. Since the it has fallen by 3.6% where in 2015 it is now only 72.5%. One reason for such a fall in the concentration ratio is a change in shopping habbits. Previously shoppers would often plan a weekly shop and go to one of the larger supermarkets in order to purchase their goods. This suited the larger firms as they provided a range of goods and competed on availability. However, emerging brands such as Lidl lacked in variety but competed on price. The consumer habbits have changed from being predominantly a single shop to multiple trips to supermarkets durring the week. This increases the importance of price which suits the smaller shops such as Lidl. As a result more consumers are changing to shop at smaller brands reducing the revenue of larger brands, thus reducing their concentration ratio.

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Examiner Tip

Ensure you carefully apply the data available, as instructed in the question.

Question 6 (b)

This question demonstrates the importance of candidates carefully reading the question and making sure they understand precisely what is being asked of them. Far too many candidates failed to focus on food suppliers and consumers. Also key with this question was understanding the concept of monopsony, bearing in mind this was in the context of supermarket monopsony power. Low scoring responses either did not understand monopsony or confused it with monopoly and did not go beyond quoting the data. Whilst many candidates were able to use the extracts and data effectively, linking the information provided to specific economic theories would have yielded better rewards. (Dis)economies of scale were generally recognised but a failure to develop answers by referring to specific types weakened a number of arguments. However overall, candidates did well with this item achieving a mean mark of 7.73.

(b) With reference to Figure 2 and Extract A, discuss the possible impact of supermarket monopsony power on both food suppliers and consumers.

(12)

Monopsony power is where a buyer in a market has significant buying or bargaining power in their industry. The GCA is investigating this power, the abuse of this power, with a Yougov poll showing 31% of Tescos' food suppliers claiming they are failing to meet the GCC.

High monopsony power of supermarkets leads to them being able to negotiate lower prices from food suppliers, as they need to minimise their costs to engage in the agressive price wars. However this lower price "aggressive price-cutting" means falling revenues for food suppliers, causing AR to fall to
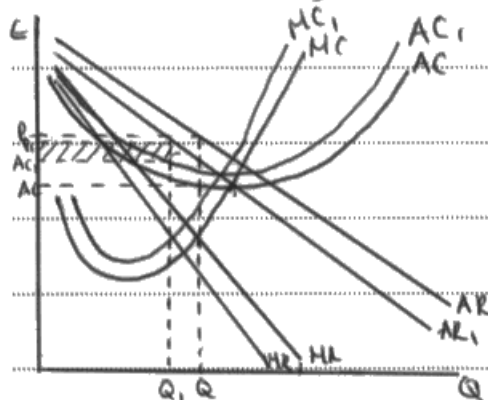
AR₁. This along with being forced to pay for specific packaging and rising marketing costs has led to rising costs for the food suppliers causing AC to increase to AC₁. This has led to shrinking profit margins and therefore falling profits to just the shaded area. Decreased profits will lead to reduced dividends for shareholders, as well as decreased investment. Decreased investment in capital may lead to falling dynamic costs in the long-run

efficiency and rising ~~LRAC~~, which may lead to losses in the future if prices continue to fall and they may be forced to shut-down if prices are less than their variable costs $(P < AVC)$*
However, monopoly food suppliers, e.g Unilever, can act as a counterweight to monopsony power as their control of key brands in supermarket sales can allow them to negotiate more strongly with the supermarkets, so ~~there~~ their revenues

* This is why the number of food suppliers struggling financially has increased 50%.

won't fall as significantly and neither will profits.

By supermarkets having lower costs due to purchasing at lower prices from suppliers, they are able to decrease prices for consumers. This is because the supermarkets are highly interdependent, which has resulted in a price war. This will lead to falling prices for consumers and by 1.7% therefore an increase in consumer surplus. ~~If the supermarkets~~ However as food suppliers are facing falling profits and are investing less the quality of food may fall or there may be less innovation in terms of flavour. The quantity supplied by the food suppliers has also fallen from Q to Q_1, which may lead to shortages. ~~more~~

In order to reduce costs in the long-run, food suppliers could reduce the size of their products, e.g. smaller quantities in jars, in order to reduce costs and improve profit margins, but this will lead to a fall in the quality of good for consumers and falling consumer welfare.

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Examiner Comments

This answer achieves a mark of 12/12.

It achieves Level 3+ (8/8) and Level 2 EV (4e/4e). All reasons are relevant, explained and applied to the context rather than generic.

To get to Level 3 on KAA the candidate has a clear understanding of monopsony, has done both consumers and food suppliers, has applied to the case (and also concentrated on the 'impacts'). Weaker responses focussed on the 'cause' rather than impacts.

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Examiner Tip

Read the question carefully to ensure you meet the full demand of the question and focus on the effects rather than the cause in this case. Ensuring you understand whether the question is asking you to look at the causes or effects/impacts is essential for exam success.

(b) With reference to Figure 2 and Extract A, discuss the possible impact of supermarket monopsony power on both food suppliers and consumers.

(12)

A monopsony is where there is a single buyer for a product, this therefore allows that buyer to squeeze the price as much as they want, as they knew the supplier will almost certainly have to cooperate with them.

From figure 2 we can see that 8 of the largest supermarkets have been reported to have broken the Groceries code of Conduct, this shows that Supermarkets are all trying to purchase their products for the lowest amount possible, potentially damaging these businesses. If a firm such as Tesco decides it is going to cut what it pays for a product, the supplier has little room to negotiate, creating an extremely negative shock to the economy. This could lead to job cuts as the firms no longer have enough money to pay their staff, meaning there is greater pressure on the government to provide welfare payments to these unemployed citizens who are now no longer paying income tax, meaning this decision extremely damaging to the economy as a whole.

For the food suppliers a cut in
prices will simply not be sustainable.
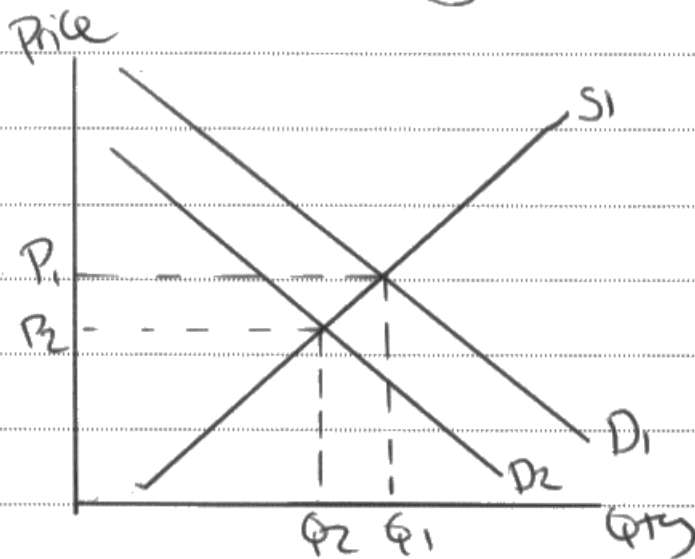
From the diagram we can see how a small
shift in demand (the loss of one customer) has a
large effect on the price and level which can
be charged, starting off a spiral of price
decreases. However on the other hand this
could be seen as a good thing for
consumers as they would simply not
have to spend as much on their weekly
shop, leaving them with more disposible
income which can be used to support other
areas of the economy.
    To Conclude supermarket monopsony
Power has a largely negative impact on
food suppliers, however a wholly positive
impact on consumers.

Question 6 (c)

Two correct measures explained in context with either two evaluative comments per measure, or one evaluation point well developed was required here. Weaker responses tended to either only cover one measure, provide one relevant measure and one non-relevant measure or did not provide evaluation. Minimum price schemes were used effectively as methods to restrict monopsony power with many candidates developing their arguments as to how this would benefit suppliers and evaluating why such schemes effectiveness may be limited. Additionally, regulatory measures usually linked to fines or mergers of suppliers or de-mergers/blocked mergers of supermarkets were well argued. A common error was to provide a subsidy – this was often a confused response lacking in relevance.

(c) Examine measures the government might use to restrict the monopsony power of supermarkets.

(8)

One method the government could use to restrict monopsony power is regulation. The CCA has the power to fine firms 1% of their ~~total~~ annual revenue for abusing their monopsony power. This would act as a deterrent and may result in an increase of the welfare of the food suppliers.

However this ~~is~~ relies upon food suppliers reporting it. Many do not out of fear of losing their contract. Therefore regulation may not be effective.

Another method the government could use is a minimum price scheme. By setting a price of P₁ above the market equilibrium these legally prevent monopsonistic supermarkets for using food suppliers to accept low prices. As a result output increases
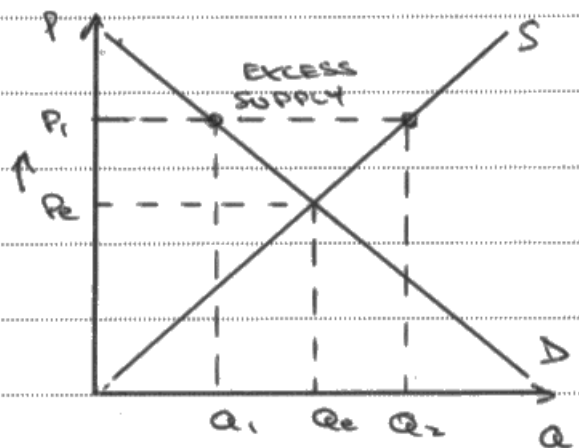
and profits increase for suppliers.

However this may create unemployment. Excess supply at $Q_1 \rightarrow Q_2$ is created which means that for many suppliers their produce wouldn't be bought and their profits would fall

(c) Examine measures the government might use to restrict the monopsony power of supermarkets.

(8)

A monopsony is a single buyer of resources so monopsony power is when these firms are able to lower prices/negotiate lower prices with suppliers due to them being the only buyer. In this case, supermarkets such as Tesco are able to force lower prices when buying from food suppliers.

The government could add regulation to restrict the monopsony power. For example, they may add profit cap to the monopsony so that they have their profit capped at a certain amount. This may inserts

Question 6 (d)

This question proved to be a challenge. Information gaps were not well explained and irrational behaviour beyond habitual shopping habits was badly explained. A lack of understanding of irrational behaviour meant that many candidates failed to secure high marks as did an over-reliance on aspects of the text without explaining or considering whether these were truly examples of information gaps. Many candidates picked up marks by exploring other causes of food waste that they were more able to explain like substandard packaging. They also picked up marks for considering the future with better technology and forecasting.

(d) Assess the extent to which 'information gaps' (Extract B, lines 5 and 6) and 'irrational behaviour' (Extract B, line 11) are the main causes of food waste in the UK.

(10)

supermarkets in the UK are responsible for around 0.2 million tonnes of food waste a year. Info information gaps occur where the two parties have unequal unbalanced information, and in the case of the food industry this 'information gap' between suppliers and retailers is resulting in 4.1 million tonnes of waste. This is because suppliers have more information on the quantity they have supplied than supermarkets and supermarkets have more information on the quantity they demand. This asymetric information has led to suppliers over-producing/over-supplying resulting in waste as supermarket only purchase a fixed quantity. However An information gap on the storage and transportation of the food, due to the complexity of the administrative process, has also have led to food waste as food expires if stored for too long or not transported correctly, e.g. in refridgerated vehicles. However supermarkets and suppliers are co-operating to decrease waste and it still exists. This could be because of the other issues such as the issue of supermarkets only accepting certain specifications of food. This results in high-levels of waste, such as the throwing away of 'misshapen vegetables'.

don't know what to cook with leftovers so don't use them.
Health scares in the media on 'gone-off' food also lead to consumers
throwing away useable food, this has led to packaging development
to keep food fresher for longer reducing waste. consumers also
often irrationally overbuy food, in fearing they will run
out which results in waste when it isn't all used.

However, supermarkets are also responsible for around
0.2 million tonnes of waste, due to strict use-by-dates and
stock mishandling, which could easily be overcome and
the left-over food which is perfectly safe to eat could be
donated to homeless shelters or even used as animal feed.
Food is also wasted as it isn't properly recycled, as fruit,
and vegetables should be used for compost, or animal feed rather than
entering landfill, which if improved would drastically
reduce food waste at all levels of the supply chain.

(d) Assess the extent to which 'information gaps' (Extract B, lines 5 and 6) and 'irrational behaviour' (Extract B, line 11) are the main causes of food waste in the UK.

(10)

Information gaps are when the public do not possess perfect information and are misinformed on a subject due to lack of proper education. Irrational behaviour is when the public do not behave in their own best interests or as they are expected to. These two things could be a main cause for food wastage as consumers are not properly informed on how to store certain foods and as a result end up throwing it away as it has gone off. Additionally, irrational behaviour could mean that a consumer may throw away a perfectly good food items due to superstition or rules of thumb they follow, which are both forms of information gaps. This can lead to poverty.

ResultsPlus
Examiner Comments

This answer achieves a mark of 3/10.

The candidate provides a narrow response with a limited use of context, achieving lower level for KAA and no evaluation.

ResultsPlus
Examiner Tip

Best practice with the full A Level exams is to ensure you have covered the entire specification. Make sure in advance of the exam that you know which questions, such as this one, require evaluation.

Question 6 (e)

This question clearly differentiated between the candidate that understood the theoretical problems of mergers in context, with a coherent chain of reasoning and responses which were theoretically light. Full marks were not always accessed when the answer did not consider carefully the context of the question and data available. Candidates who focused on the question and provided 'problems for Sainsbury's and Morrisons' rather than to other agents achieved much higher scores and were generally able to develop these using the context and wider knowledge of issues of oligopolistic mergers effectively. The mean mark was 8.65.

(e) Discuss the likely problems for Sainsbury's and Morrisons if the suggested merger between them goes ahead. Refer to Figure 1, Extract C and your own knowledge in your answer.

(15)

This is horizontal integration - two firms at the same stage of production in the same industry. One issue could be a lack of synergy leading to diseconomies of scale. Extract C refers to the difficulty of co-ordinating hundreds of thousands of workers, implying that there may be issues in communication. This could cause long run average costs to rise beyond the minimum efficient scale, representing a fall in productive efficiency. According to Forbes, 83% of mergers fail in this manner, where synergies are often imagined but fail to materialise in practice.
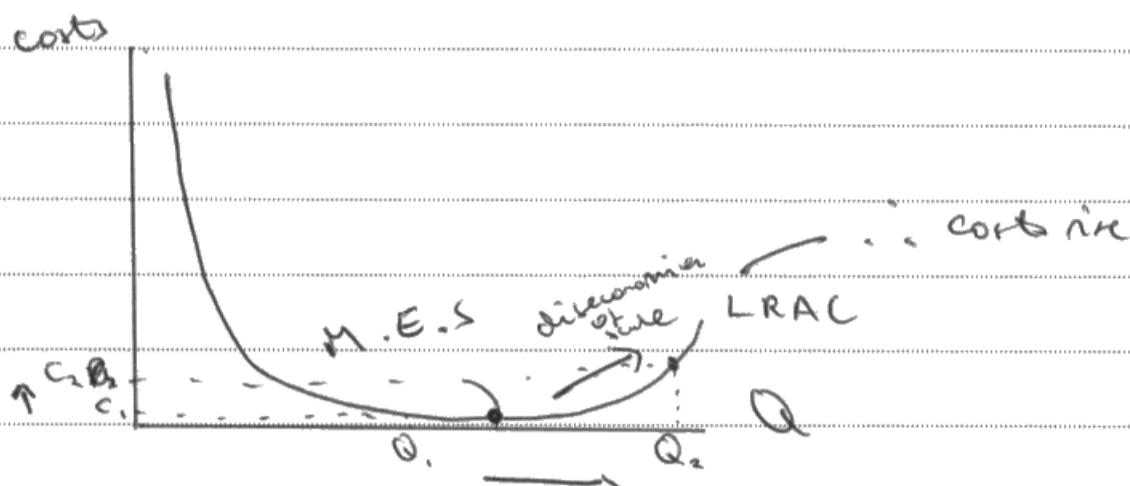
However, to evaluate this, Société Générale does believe some economies of scale could be generated — perhaps financial economies, for example, allowing the merged firm to access credit at lower interest rates. Thus, while there will be some communication difficulties, these may be outweighed by the financial economies of scale, which could lower costs and enable the firm to pass on lower prices to compete in the current price war.

A second problem may be excessive risk arising from over-exposure to the supermarket industry. Food prices have fallen by 1.7% over the last 2 years as Aldi and Lidl continue to gain market share by undercutting others; Tesco has had to issue profit warnings. The resulting merged firm is essentially putting 'all of its eggs in one basket' — in this case the supermarket industry where profits are falling. Thus, this can be viewed as a risky move, since any further deterioration in market trends could mean losses for the firm, with few options to cross-subsidise these losses since it is so heavily focused on this supermarket industry.

However, in evaluation, the merger may

actually enable the survival of Sainsbury's and Morrisons in the industry. The merged firm would control 27.4% of the industry, enabling it to increase monopsony power and be better prepared for a continuation of the price war with larger combined cash reserves. On its own, Morrisons may have struggled in the longer-term. Thus Moreover, the supermarket industry as a whole has fairly constant demand, meaning it is not as risky to be involved in the long term as other markets such as oil.

(e) Discuss the likely problems for Sainsbury's and Morrisons if the suggested merger between them goes ahead. Refer to Figure 1, Extract C and your own knowledge in your answer.

(15)

A merger is where two firms come together to form one much longer firm. In this case, it's a form of horizontal integration, as both Sainsbury's and
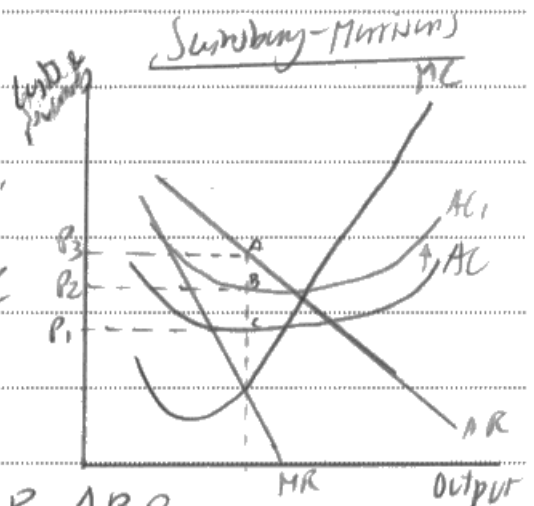
Morrisons operate in the same market.

If Sainsburys and Morrisons merge, their market share would become 27.4%, the second largest share in the market after Tesco at 28.6%. Whilst the CMA have allowed a few other giant mergers recently, such as Lloyds-HBOS, there is still a chance Sainsburys and Morrisons would struggle to be approved. If they were approved, they may later suffer from intense government regulation as the CMA and other authorities would work to ensure the Sainsbury-Morrisons merger wasn't abusing its ~~new position~~ large market power. This may not be the case however, as there could be regulatory capture, where the firm befriends and takes in the regulator so that they regulate less harshly.

As there is considerable overlap between store locations, it is likely that in many places one of the two they would be closed ~~something is unhygienic~~ which would be a long, tedious process and a distraction for the company.

They could suffer from diseconomies of scale including poor communications and unwieldiness. With hundreds of thousands of employees now working for

one company, the firm may struggle to organise their employment and positions as they arrange store closures and attempt to merge successfully. However, the company could also benefit from economies of scale, as their external growth means they could benefit from managerial economies, possessing double the managerial talent as before and attracting even

better managers to organise the chaos and keep control of all the workers.

The merger would require an expensive new IT system to better organise the merging of both companies' stores and the software. This would increase average costs of the new firm, pushing AC up to AC₁, which greatly reduces supernormal profit from P₃ACP₁ to P₃ABP₂. This supernormal profit loss means the company may have to reduce investment and spending on research and development, which in turn reduces their dynamic efficiency in the long run.

Question 7

Responses generally focused on a number of relevant microeconomic issues effectively and broke down the various impacts on different agents to provide effective analysis of a range of microeconomic effects. High scoring responses were well structured and at times provided clear evidence of planning. They made effective use of Theme 1 and Theme 3 theory, going beyond the mostly Theme 1 theory of lower scoring candidates. Diagrammatic analysis is not required but when done well was accurate, well labelled and well explained with a solid chain of reasoning. Candidates at the top end used supply and demand diagrams to consider the tax burden or welfare effects and many candidates used theory of the firm diagrams eloquently to explore the cost and revenue implications. In addition candidates who recognised a negative consumption externality and were able to provide a correct diagram provided well developed responses.

Indicate which question you are answering by marking a cross in the box ☒. If you change your mind, put a line through the box ☒ and then indicate your new question with a cross ☒.

Chosen question number: **Question 7** ☒   **Question 8** ☒

regressive
conflict
foreign
Black

Write your answer here:

An indirect tax is a tax on expenditure. The fact that the proposed tax is 20% on the sale of soft drinks shows that it is an ad valorem tax - a tax levied as a % of the value of the good.
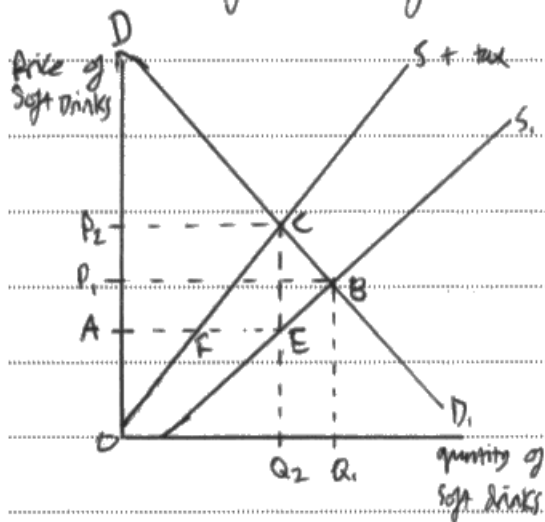
The imposition of an ad valorem tax per unit of soft drink of P₂A will lead to an upward shift of the supply curve from S₁ to S + tax. The price paid by consumers will increase from P₁ to P₂ and the quantity of soft drinks consumed will fall from Q₁ to Q₂. Consumer Surplus, the difference between what consumer are willing to pay and what they actually pay, will fall from the area DP₁B to DP₂C. Producer will now receive a price of A, as opposed to the price P₁ before the tax. This will cause producer surplus to fall from the area OBP₁ to

OAF. As well as this, producers' revenue will fall from the area OQ_1BP_1 to OQ_2EA. The government will earn a tax revenue of the area P_2AEC.

As shown, consumers will ~~pass on~~ have to pay a higher price for soft drinks and their consumer surplus will fall. As well as this, poorer consumers will lose out even more because indirect taxes are regressive. This is because they take up a larger proportion of a poorer person's income than a richer person's income. However, soft drinks are bad for consumer's health since they contain a lot of sugar. ~~The~~ Because of this, the reduction in consumption caused by the tax could be beneficial for consumers as they may have to spend less on healthcare in the future. Also, the extent to which consumer's are affected by a price increase depends on the price elasticity of demand for soft drinks. If demand is price elastic the producer will absorb most of the subsidy, ~~then~~ because if they passed on the price increase then the quantity demanded would fall by a larger proportion, causing their revenue to fall. Therefore if demand is price elastic, consumers won't be badly affected by the tax.

For the government, they will receive tax revenue as shown by the diagram. This tax revenue can be ~~ringfenced~~ and only used for socially beneficial products, which would increase

society's welfare. As "well" as this, the government will benefit from not having to spend as much on healthcare in the future. This is because soft drinks cause many illnesses so a reduction in the quantity consumed of them will reduce the amount of cases of illness like diabetes, which decreases the amount the government will have to spend on healthcare.

However, the imposition of an indirect tax could have unintended consequences. Black markets could be set up where producers and consumers don't pay tax, resulting in a loss of tax revenue for the government. As well as this, consumers may switch to foreign markets to buy their soft drinks, again decreasing tax revenue.

Also, the government uses taxes to raise finance to fund government expenditure. This can cause policy conflicts. For example the government may want to raise as much tax revenue as possible to fund its education spending, but putting too high taxes on soft drinks may cause producers to relocate, decreasing tax revenue.

The imposition of an indirect tax on soft drinks will effectively raise the costs for firms, as shown in the diagram by supply shifting up. This increase in costs will cause a fall in producer profits. If the tax is too high, the increase in costs may cause producers to go out of business, leading to a lack of choice. However, the extent to which

producers' costs are affected depends on the price elasticity of demand for soft drinks. If demand is price inelastic, producer can shift the majority of the tax onto consumer since the quantity demanded won't fall significantly. This will allow producers to maintain their profits.

Indicate which question you are answering by marking a cross in the box ☒. If you change your mind, put a line through the box ☒ and then indicate your new question with a cross ☒.

Chosen question number: **Question 7** ☒   **Question 8** ☒

Write your answer here:

A tax is a sum of money that the government places on certain products to help inhibit its consumption and therefore reduce externalities.

By placing a 20% tax on the sale of soft drinks
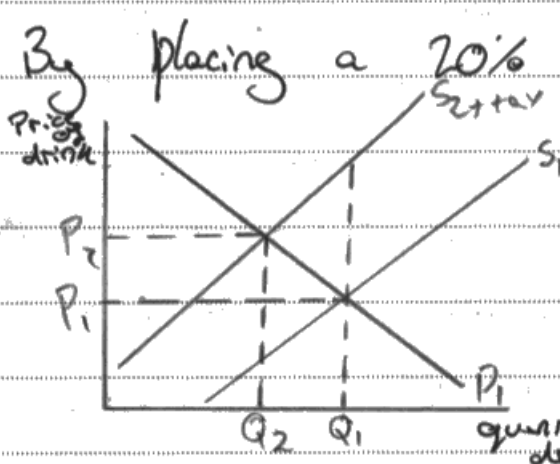
there is an increase in the ~~price~~ There is a shift of supply to the left from S_1 to S_2 and an increase in price from P_1 to P_2

this will also affect quantity sold decreasing from Q_1 to Q_2. This shows a contraction in the demand for soft drinks, but this will depend on the price elasticity of demand in soft drinks as if it is inelastic and so between 0--1 then an increase in price will ~~~~ result in a less then proportionate decrease in the quantity of soft drinks sold. This would fail to achieve a decreased consumption of soft drinks. Therefore it depends on the elastisity of ~~supply~~ demand ~~~~ on soft drinks.
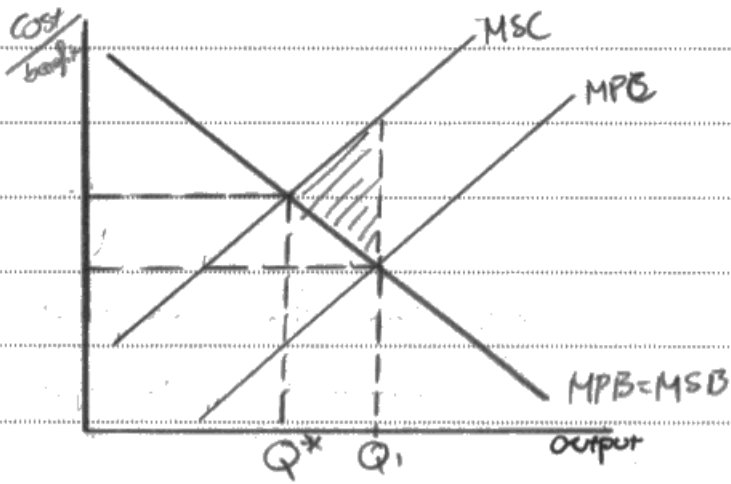
A tax will help to decrease consumption of ~~the~~ ~~g~~ soft drinks which will result in quantity to decrease from Q_1 to ~~Q*~~ a closer value to Q^* with an additional welfare gain of the shaded area. This is due to the fact that soft drinks have a higher social cost than personal cost ~~or~~ producing a negative externality due to ~~trading~~ ~~individuals~~ ~~externality~~ its production of cutting down forests specifically to make sugar cane.

This externality may be reduced by a tax but may cause other unintend consequences to occur which further produce externalities such as additives unhealthy for the body being included.

This tax depend on the elasticity of soft drinks and whether it will be enough to reduce consumption closer to Q^*.

ResultsPlus
Examiner Comments

This answer achieves a mark of 14/25.

In this answer the candidate has used a diagram but it has basic analysis to a Level 2 standard in the written explanation and the evaluation is limited to considering the rice elasticity of demand (Level 2e). The effect of the tax on internalising the external cost, with a benefit of doubt given on deforestation, just secures Level 3 but the evaluation here referring to unintended consequences lacks balance (Level 1e). Overall therefore this answer is a low level 2 for KAA (9 marks) and a mid level 2 for evaluation (5e).

ResultsPlus
Examiner Tip

Remember if you are going to use a diagram try to ensure it is fully labelled and used in context. Evaluation also needs to be well balanced to offer an alternative viewpoint to the one already made.

Question 8

Diagrams for this were clear as was the concept but beyond the argument that shareholders expect MC=MR because they want dividends and managers want MR=0 because performance bonuses are often linked to turnover, the candidates struggled to think of reasons. Stronger candidates examined the idea that MR=MC was quite hard to calculate and the shareholders wouldn't really have a clue given their proximity to the daily operation and inside workings of a business. Effective evaluation often went on to be critical of revenue maximisation along the lines indicated in the mark scheme as well as the principal-agent problem. There was clear differentiation in approach from confused diagrams to fully labelled and annotated diagrams. Candidates struggled to develop chains of reasoning which explained why one objective might be more suitable for firms in a specific industry. The lack of effective application to an industry led to a number of responses failing to develop arguments and to build on a technical understanding of the conditions for the two different objectives.

Indicate which question you are answering by marking a cross in the box ☒. If you change your mind, put a line through the box ☒ and then indicate your new question with a cross ☒.

Chosen question number: **Question 7** ☒ **Question 8** ☒

Write your answer here:
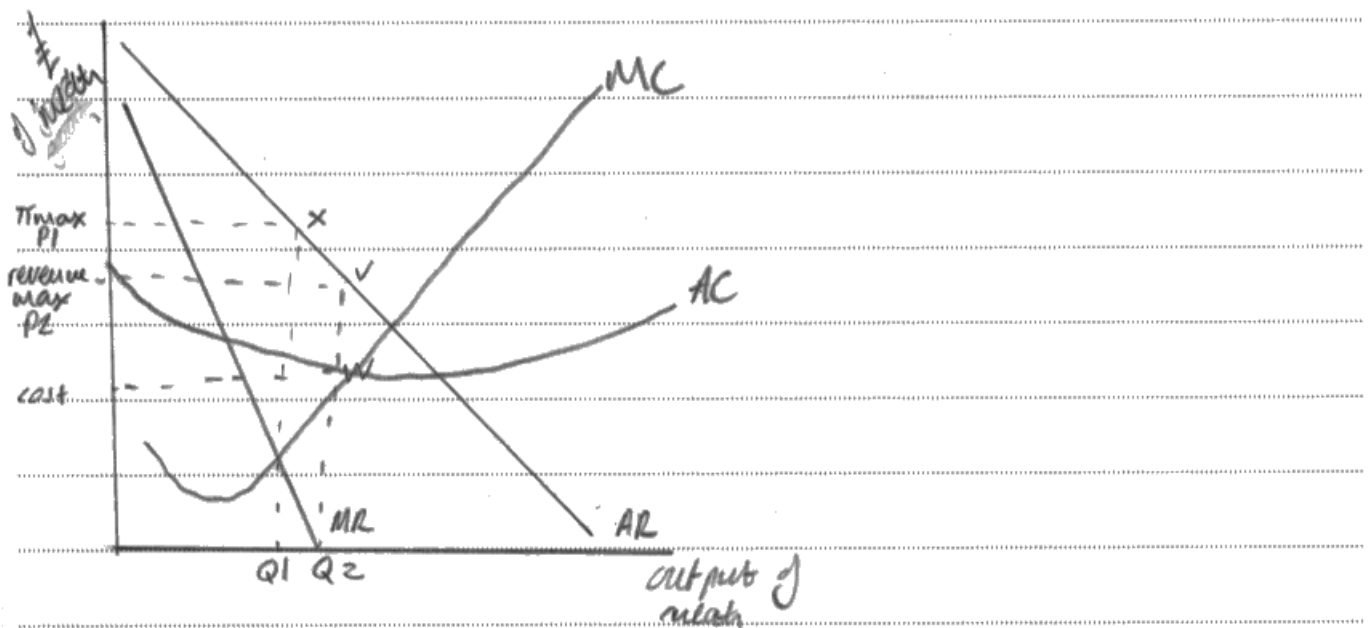
Revenue maximisation is achieved at the output MR=0 and is the output that gives the supermarket the largest total revenue.

One reason revenue maximisation is often a more realistic goal than profit maximisation, is that it can be a useful tool

for increasing market share. Walmart is notorious for producing at $MR=0$, using the additional revenue gained to set up more shops across America. The additional revenue gained from $MR=0$ (instead of $MC=MR$) essentially acts as capital for supermarkets to reinvest and grow. If walmart uses this capital to open 3 new supermarkets, it will also gain economies of scale: assuming it doesn't employ another regional manager, they benefit from managerial economies of scale as the new shops pose no additional regional managerial jobs. ~~However~~ This reduces the cost per unit of food, making the supermarket more competitive by giving them the capacity to reduce prices. However, this might not work as supermarkets operate in an oligopolistic market: gleaning economies of scale from reinvested capital earned by revenue maximizing may result in price wars, with all the supermarkets competitors lowering prices, resulting in a loss of revenue for all the businesses.

In contrast, it is arguable that profit maximisation is a more realistic business aim. As the diagram shows, π maximisation results in the highest amount of supernormal profits for the supermarket, returning: the area $P.Tmax.Cost.W.X$ in supernormal profit. Because of this, it is clear that supermarkets would pursue this strategy: higher profits will keep the shareholders happy and increase the value of the supermarket shares. This lowers the risk of the supermarket being acquired by a competitor due to a cheap share price. However, the π principle

agent problem dictates that profit maximisation is unlikely to be achieved. The managers (agents) at Tesco are are likely to profit satisfice; they understand they need to produce a reasonable level of profit to keep the principle (shareholders) happy, but will then pursue other objectives such as increasing their happiness by playing golf on a wednesday afternoon instead of working on pricing strategies. The tendency of managers to satisfice detracts from the likelihood of profit maximisation occurring, by making it a debatebly, unrealistic business objective.

Another reason that revenue maximisation can be viewed as the most realistic business objective for supermarkets is because it provides the largest incentive for high-level managerial staff. As previously mentioned, the divorce of ownership dictates managers pursue their own objectives. There is a tendency for firms supermarkets to set bonuses based on revenue performance, providing the manager with a large monetary incentive to sell products at P2, where $MR = 0$. If the manager has a larger incentive to revenue maximi then he is likely to become if more productive, lowering the costs per unit of food sold by providing the supermarket with a more efficient service for the same basic wage. If the costs per unit decrease, then the supermarket is more competitive and — given the limited demand facing supermarket — makes more profit due to a fall in costs ($T\pi = TR - TC$). However, revenue maximisation only effective if reducing the price of food goods will result in a noticeable change in demand. The inertia

and 30% off deals means that a decrease in price may not be registered, rendering it useless and resulting in a loss of revenue. Furthermore, supermarkets have a reasonable degree of brand loyalty: a general fall in price at Tesco by 1% is unlikely to attract demand from Waitrose shoppers. Because of this, revenue maximisation has the potential not to work, as consumers may not be aware of the price drop, or may simply remain loyal to their supermarket of choice.

In conclusion, revenue maximisation is not the most effective business strategy for supermarkets. Given the high degree of interdependence of one upon another, a decrease in price to P2 from P1 is not likely to result in an increase of revenue as competitors will engage in a price war as consumers will largely remain loyal to their preferred supermarket. Profit maximisation is a preferred strategy as it returns the largest amount of supernormal profit, keeping the shareholders happy. However, P=MC=MR should be pursued with the knowledge managers are likely to satisfice, so as not to provide false expectation from shareholders.

Chosen question number: **Question 7** ☒   **Question 8**   ☒

Write your answer here:

An ad valorem tax on soft drinks of 20%
would look to decrease the negative externality
in consumption
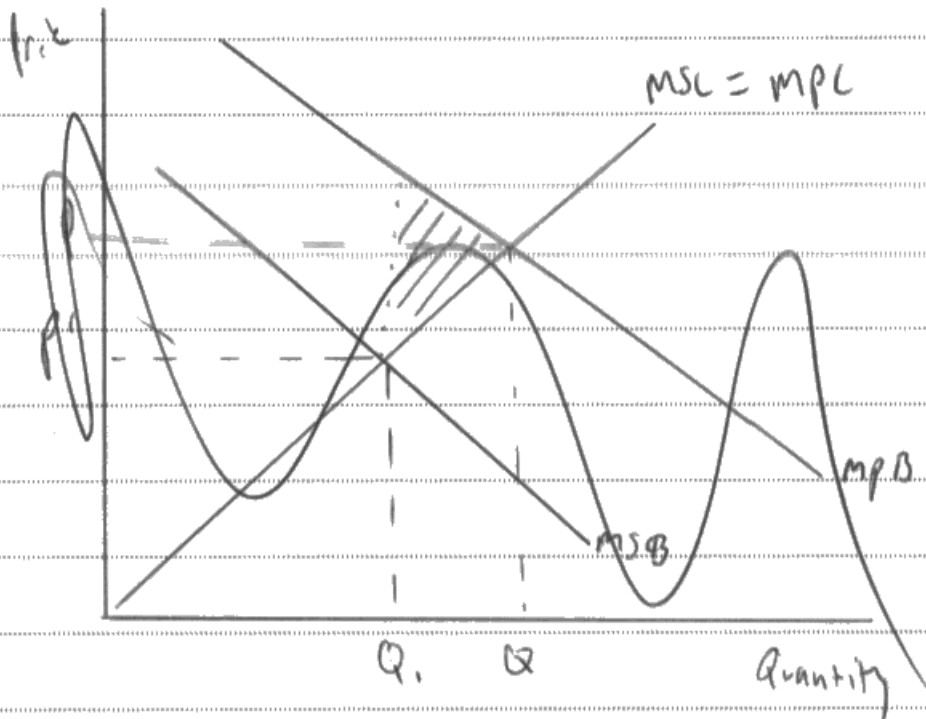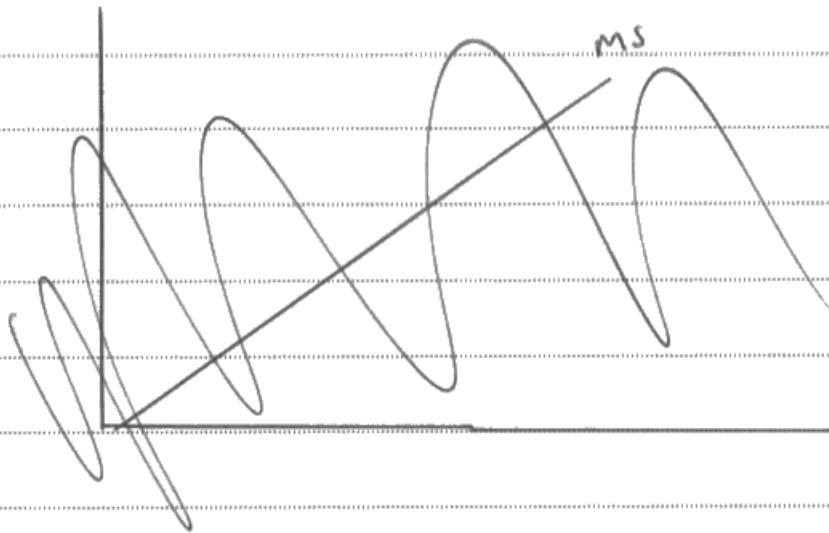
The over consumption of soft drinks at Q₂ rather than Q₁. Show the differene in consumption between the socially optimal level and the dead weigh welfare loss caused by the consumption at Q₂. The tax would lead to an increase in price

Q8
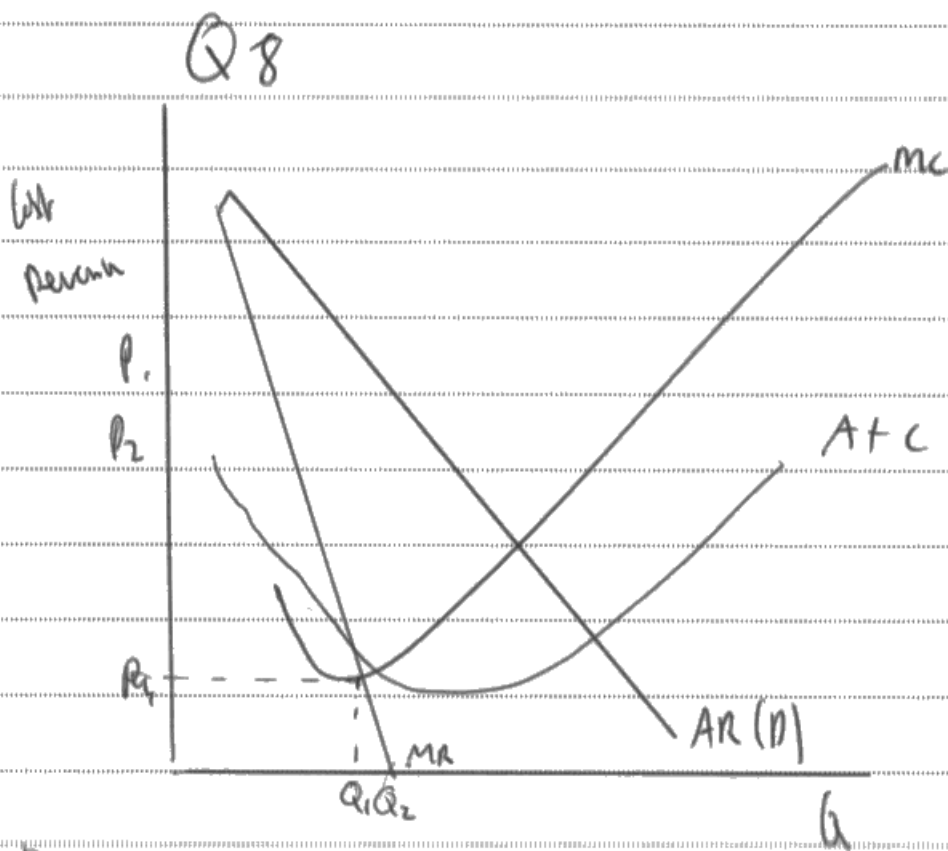
Revenue maximisation is when MR =0 and profit maximisation is when MR = MC Profit maximising is what you assume firms do, However Profit satisficing is likely to occur to prevent the divorce of ownership Problem. This means that the company will change its out put and price level to persue other

objectives so that managers workers are satisfied and don't take part in behaviour that includes using company resource for private benefit. in the diagram profit maximisation is at output Q1 and price P1 this shift to output Q2 and Q1 which allows for.

Paper Summary

Based on their performance in this exam, candidates are offered the following advice:

- Be aware of all formulae and quantitative skills.

- Ensure you carefully study and understand the figures and extracts provided in section B. These form the context for the questions, and answers should be related to this context and not be entirely theoretical. Read the question instructions very carefully to make sure your answer remains relevant.

- It is indicated on the front of the exam paper that 'there may be more space than you need'.

- Ensure diagrams are accurately drawn, full labelled and used to answer the questions set.

- Clearly identify which essay you have chosen by placing a cross in the correct box.

- Focus on logical chains of reasoning that explain your knowledge and evaluation whilst applying theory and data in the level based questions. Quite often candidates move from definitions and a brief explanation of an economic issue straight into thin evaluation. This and a lack of structure were mostly evident in the essays and may be due to time constraints. Practicing full papers under timed conditions is essential in planning schemes of work.

- Practice offering informed judgement, being critical of the underlying assumptions in economic theory and recognising different viewpoints, as you respond to the essay-based optional question.

Grade Boundaries

Grade boundaries for this, and all other papers, can be found on the website on this link:

http://www.edexcel.com/iwantto/Pages/grade-boundaries.aspx