



Sample Papers – Set 1

EDEXCEL A Level – Paper 1 (Markets and Business Behaviour)

Question Paper

Time Permitted: 2 hours

Paper Instructions:

- In **Sections A and B**, answer all questions.
- In **Section C**, answer **one** essay question.
- There are 100 marks available in this paper
- The mark allocation for each question are shown in the accompanying brackets.
- You may require the use of a calculator to answer certain questions.

SECTION AAnswer **All Questions**

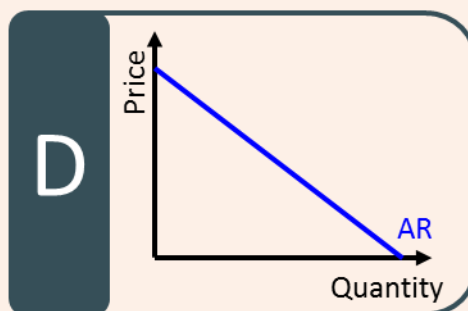
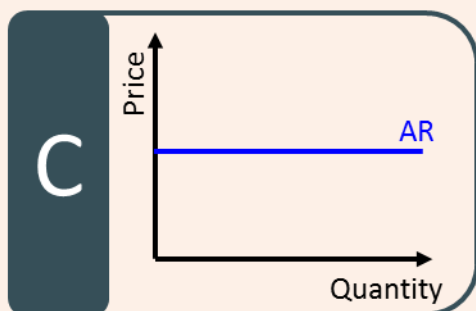
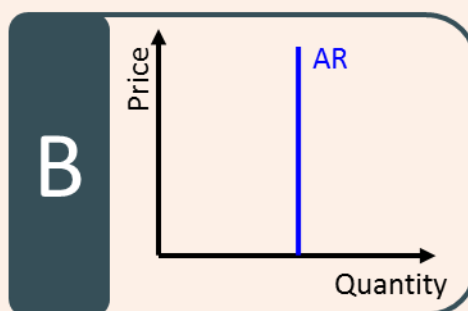
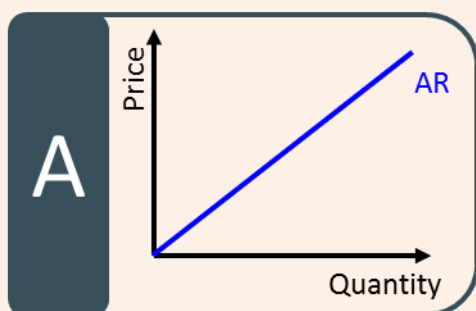
1 In the UK a firm is classed as a monopoly if it has a market share of 25% or more.

a) Which one of the following is an example of a characteristic of a monopoly market structure?

- A high level of interdependency between firms in the market.
- High barriers to entry reducing the contestability of the market.
- A large number of homogeneous goods produced.
- All firms are price takers and have no influence over the market price.

(1 mark)

b) Identify the diagram that correctly represents the average revenue curve for a monopolist.

**(1 mark)**

c) Which of the following describes the expected pricing strategy of a profit maximising monopoly?

- Firm uses its monopoly power to set a price up to the demand curve
- Firm uses its monopoly power to sell as much as it wants at the prevailing price
- Firm charges a different price for each unit sold
- Firm charges a price to ensure that it achieves productive efficiency

(1 mark)

d) One benefit of a monopoly is that it is a market structure which can lead to dynamic efficiency benefits. Explain one reason why monopolies can be dynamically efficient.

- Monopolists can reinvest supernormal profits earned into research and development projects.
- Monopolists can earn supernormal profits which provide the government with higher tax revenues.
- Monopolists can use supernormal profits to reduce the contestability of the market.
- Monopolists can use supernormal profit earned to charge a price above the marginal cost of production.

(2 marks)

- 2** The table shows the breakdown of UK grocery sales (£millions) in quarter 2, 2015 and quarter 2, 2016.

Company	Grocery Sales (£millions)	
	Q2 2015	Q2 2016
Tesco	7,204	7,157
Morrison's	2,758	2,709
Lidl	1,002	1,127
Asda	4,150	3,919
Aldi	1,408	1,562
Sainsbury's	4,162	4,116
Other	4,590	4,717
	25,273	25,307

Source: Kantar World Panel

- a)** The 4-firm concentration ratio of the UK supermarket industry in the second quarter of 2015 was 72.3%.

To 1 decimal place, calculate the 4-firm concentration ratio of the UK supermarket industry. You are advised to show your working.

(2 marks)

- b)** What information can be inferred from the data in the table?

- The industry is perfectly competitive
- There are no barriers to entry present
- There are significant internal economies of scale present
- Some firms in the industry have significant market power

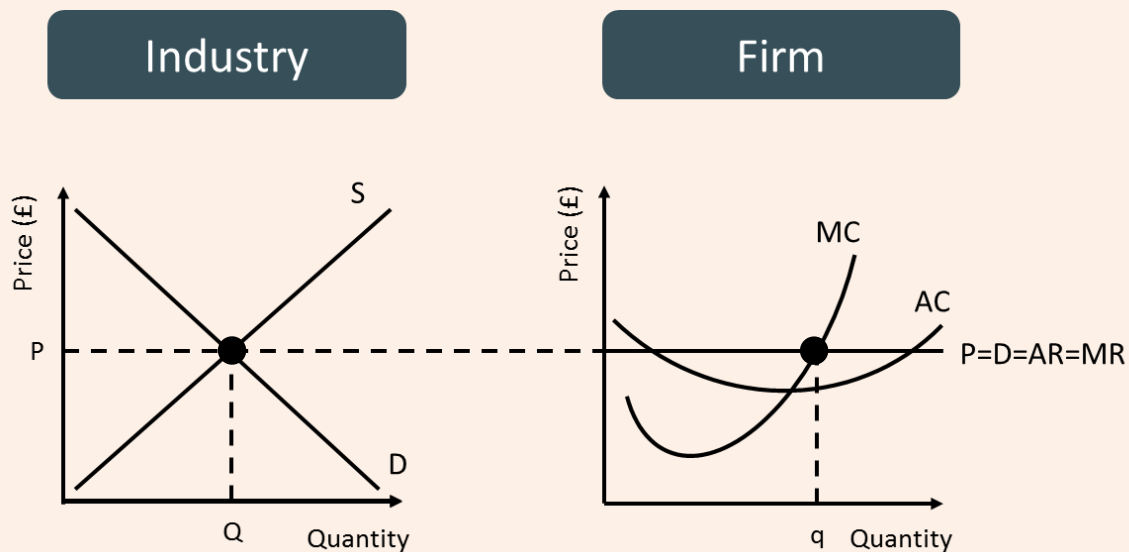
(1 mark)

c) Which one of the following best explains why the market share of the leading supermarket chains in the UK has shrunk?

- Discount firms have undercut incumbent firms to steal market share and sales.
- New entrants have invested heavily on running advertising campaigns to increase the customer turnover rate.
- New entrants have established and secured patents on profitable products.
- Supermarket chains face an inelastic demand curve which prevents incumbent firms from dominating the market.

(2 marks)

- 3 The diagrams represent the market outcome for an industry and one profit maximising firm within the industry.



- a) It can be deduced from the diagrams that this industry is an example of

- An oligopoly
- A monopoly
- Perfectly competitive market
- A monopsony

(1 mark)

- b) At output q the firm makes

- Normal profit in the short-run
- Supernormal profit in the short-run
- Supernormal profit in the long-run
- An economic loss in the short-run
- An economic loss in the long-run

(2 marks)

- c) Explain why the profit-maximising firm will only make normal profit in the long-run.

- Firms enter the market and reduce the market price
- Firms leave the market and increase the market price
- Barriers to entry prevent entry of new firms

(2 marks)

- 4 The payoff matrix shows the pricing strategies of two competing airlines, with the payoffs in profits (£millions)

		Airtropolis	
		High Price	Low Price
EzyAirlines	High Price	100 / 100	30 / 150
	Low Price	150 / 30	50 / 50

- a) Initially Airtropolis and EzyAirlines enter a price agreement which results in both firms earning £100m in profit. Which one of the following reasons best explains how the airlines can achieve this level of profit?
- Firms adopt third-degree price discrimination to maximise joint profits
 - Firms maintain a price cartel to maximise joint profits
 - Firms differentiate their products significantly to maximise joint profits
 - Firms tacitly collude to fix their prices higher to maximise joint profits

(4 marks)

- b) Airtropolis decides to change strategy and break the agreement of setting high prices with EzyAirlines. Therefore, Airtropolis undercuts EzyAirlines' fares.

Identify what the new pricing strategy for EzyAirlines will be in reaction to this?

- Set a low price
- Set a high price

(1 mark)

- 5 A chocolate bar manufacturer is carrying out some research to analyse the impact of increasing the price of one of its chocolate bars from £1. The demand quantities at different prices for the bar are summarised in the table below.

Demand Curve for Chocolate Bars	
Price	Quantity Demanded
£1.75	1,100,000
£1.50	1,200,000
£1.25	1,300,000
£1.00	1,400,000
£0.75	1,500,000

- a) Calculate the PED for the chocolate bar assuming the price rises from £1.00 to £1.25. Give your answer to 2 decimal places.

(2 marks)

- b) This figure suggests that demand for the chocolate bar is

- Price elastic
- Price inelastic
- Unit elastic
- Income elastic
- Income inelastic

(1 mark)

- c) Based on this result, what is the impact on the manufacturer's sales revenue if the price increases from £1.00 to £1.25?

- Sales revenue increases.
- Sales revenue decreases.
- No change in sales revenue.
- Insufficient information given.

(2 marks)**SECTION B**

Read Figure 1 and the following extracts (A to C) before answering **all parts** of question 6.

The UK Rail Industry**Extract A****Price of UK Rail Travel**

In the last decade, the cost of travelling by train in the UK for commuters has increased significantly. The average price of a standard ticket from London to Manchester has increased from £50 in 1995 to £154 in 2013. Since 2010, average rail fares in the UK have risen by 24%, outstripping the average weekly wage growth of 12% across the same period. In the UK, an increasing number of commuters are using the rail network as their preferred mode of transport. Because of this, one million more trains run every year compared to five years ago, and since 2006, passenger journey numbers have increased by 60% to exceed 1.6 billion journeys made annually, the largest increase of any European country.

Source: News Reports, November 2016

Extract B**Structure of the UK Rail Industry**

In 1997 the structure of the UK Rail Industry was radically reshaped. The ownership and control of the UK railway infrastructure was passed down to Network Rail, an arms-length public body of the Department for Transport, which maintains and operates the tracks, signalling and stations in the UK rail industry. Whilst rail infrastructure bears many of the hallmarks of a natural monopoly, the provision of train services themselves arguably does not.

As a result, train services are provided by privately-owned Train Operating Companies (TOCs). Despite TOCs facing a competitive bidding process to secure franchise contracts, once they secure a contract they usually have a monopoly on providing services on their routes.

The Competition and Markets Authority (CMA) has raised concerns about the impact that a lack of 'on rail' competition is having on rail passengers. They outline that rail passengers are suffering from more delays and cancellations on routes despite paying higher fares.

The CMA has made the case to increase ‘on-rail’ competition on selected routes to put downward pressure on rail fares: “A more competitive environment will force companies to be more efficient which may mean lower fares, new routes and destinations, more innovations and flexible ticket pricing.”

Source: News Reports, November 2016

Extract C

Increased Competition on the East Coast Line

The East Coast Line is an example of a route that has benefitted from increased ‘on-rail’ competition. Since 2014, First Hull Trains have competed on the East Coast main line with Virgin East Coast Trains, creating pressure for rail fares to fall and the quality of service delivered to improve. The average price of a ticket from Hull to London has fallen from £96.80 to £79.00. In 2016, First Hull Trains recorded a 97% satisfaction rating with rail passengers in the annual Trains Satisfaction Survey, the highest of any TOC.

The increase in competition has also created encouraged firms to provide a wider range of ticketing options. The difference in price between peak and off-peak train tickets is as stark as ever.

Some industry experts, however, are worried that increasing ‘on rail’ competition may reduce the incentives for firms to compete for TOC contracts. They point out that the typical profit margin for a TOC is around 3%.

Route	Peak	Off-Peak	Advance
Doncaster to London	£84.00	£64.90	£26.50
London to Hull	£106.00	£98.70	£62.50

Figure 1: Average Price of Rail Tickets on Selected Routes

Source: adapted from ‘CMA, Passenger Rail Services: Competition Policy Project’, November 2016

Questions:

Q6a. Using a demand and supply diagram, explain why ‘average rail fares in the UK have risen by 24%’ (**Extract A, lines 3-4**).

[5 marks]

Q6b. Examine two reasons why the UK government subsidises rail travel.

[8 marks]

Q6c. With reference to Figure 1, discuss the likely impact of price discrimination on the profits of Train Operating Companies (TOCs) within the UK rail industry.

[12 marks]

Q6d. Assess one advantage and one disadvantage of Network rail being the sole provider of rail infrastructure in the UK.

[10 marks]

Q6e. Assess the impact of introducing more ‘on rail’ competition in the UK rail industry.

[15 marks]

SECTION C

Answer **ONE** question from this section.

Q7

‘Premier League footballers earn significantly more than nurses and yet contribute far less to society.’

Assess the case for government intervention in labour markets to eliminate pay differentials and achieve a fairer distribution of income.

[25 marks]

Q8

‘In October 2016, despite the environmental concerns from local campaign groups, the UK government approved plans for the development of fracking sites in Lancashire to provide the UK shale gas and oil industry with a boost.’

Assess the view that taxation is the most effective form of government intervention in markets that are affected by negative production externalities.

[25 marks]