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June 2024

GCE Economics A 9EC0 01

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Introduction

This was the eighth 9EC0_01 examination in the 2015 Specification series and proved to be both accessible and challenging in equal measure. There were many excellent responses seen throughout the marking process, though many candidates missed straightforward marks for a range of reasons that we will explore. The questions covered a wide range of microeconomic issues from Themes 1 and 3, and gave candidates the opportunity to respond to topical data questions as well as the chance to showcase their own knowledge in the longer questions, particularly in Section C.

Section A continues to highlight the requirement to practise quantitative skills. Calculation-type question in Q1(b) and Q5(c), together with interpreting the numerical value of elasticities in Q1(a) and Q2(a) were straightforward but in many cases poorly answered. Q3(a) asked candidates to draw a cost and revenue diagram to illustrate different business objectives. There were 4 marks available here, and candidates were expected to illustrate the differing equilibria on both the x and y axes, to obtain the available marks. However, many neglected to mark the points on both axes, thereby dropping easy marks. For future series, the simple act of practising these kind of questions in conjunction with the mark scheme will embed good practice. Candidates are also reminded to refer to the stem to gain application marks. The question paper does not inform candidates of what the breakdown of marks is, so it is good practice to use the numbers in the stem. Furthermore, though there are no explicit marks for definitions, there are marks for understanding, so a definition or formula is one way of demonstrating this. Q5(a) asked candidates to explain the market structure of mortgage lending in the UK. A calculation of any concentration ratio from the data provided provided a way for candidates to manipulate the data and gain marks in the process. Where diagrams are specifically asked for, the requirement is obvious, but candidates can often obtain marks for drawing a relevant diagram even when it is not specifically asked for. It is essential, however, that these diagrams are fully explained. Overall, the responses to Section A were consistent with previous years, but could certainly have been better.

Section B contained the usual mix of points-based and levels-based questions. Q6(a) required the drawing of a supply and demand diagram, and the vast majority of candidates indicated a shift in both supply and demand. However, many candidates missed one of the curves either on the diagram itself or by not referring to a supply or demand factor at all. Q6(b) contained both marks for knowledge, application, analysis and evaluation. A clearly structured response here requires a clear statement of the reason, and then reference to the extract to gain the relevant application marks. This is best achieved by the use of quotation marks to differentiate the knowledge form the application. Without this clear distinction, examiners may not be able to award the separate knowledge or application marks. Candidates were asked to examine two factors which might influence the supply of labour in the electronics industry. However, many candidates then went on the discuss factors affecting demand, which could not be rewarded.

The levels-based questions in Section B are best viewed as a balance of breadth and depth. All require the development of knowledge, application and analysis on one side, together with evaluation of the significance, value or extent of the argument or factors considered. Q6(c) asked whether firms in the electronics industry benefit from economies of scale. This required a good understanding of what economies of scale actually are, together with an argument to say that firms do benefit and another one to say they don't. Q6(d) asked candidates to discuss the likely concerns of the competition authorities regarding the proposed merger. Here, a clear understanding of two concerns was expected. One concern is insufficient to access full marks.

Q6(e) asked candidates to discuss possible methods of government intervention to reduce electronic waste. Most candidates produced clear responses here and the best were those that used clearly labelled and well explained diagrams to access the top level of knowledge, application and analysis. Substantial evaluation is vital on 15 mark questions because there are 6 marks available for the skill, compared to only 4 marks on Q6(c) and Q6(d). Candidates are reminded to consider this in their approach to this question.

Section C, as usual, gives candidates a choice of questions. The vast majority attempted Q7, which was the question on rising energy bills. Candidates could use an industry of their choice, but the majority referred to the hotel industry mentioned in the introductory stem. The quality of responses was very wide-ranging but on the whole strong. Candidates are again reminded to clearly explain the diagrams they use and to consider the appropriateness of the evaluative comments made. For example, government intervention in terms of a maximum price for energy could be used, but it must be explained in the context of the industry chosen.

Q8 was altogether less popular and the quality of responses more varied than Q7. The 2022 paper had included a 15 mark question on the contestability of the coffee shop industry, and the examiners' report highlighted that many candidates 'confused contestability with competitiveness'. Competitiveness is about the extent of actual competition in an industry, whereas contestability is about the threat of potential competition becoming actual. Many candidates wrote responses about the extent of actual competition in the industry and confused this with potential competition. Again, candidates were able to choose their own industry, and the clear use of theory should be supported by relevant application to maximise the available marks. There are 9 marks available for evaluation, and candidates are reminded to use the conclusion of their answers to develop a justified judgement in order to access full marks.

Overall, the standard of responses was consistent with last summer's paper.

Question 1 (a)

In this question, candidates were asked to explain one likely reason for the difference in the price elasticity of demand for the 18+ student bus ticket and the adult bus ticket. Marks were awarded for an understanding of PED, the recognition that the demand for the adult bus ticket was more price inelastic, and the reason for this. Responses to this question tended to be strong, though there was some confusion regarding precisely what the numbers meant. A typical mistake was to say that the PED for the 18+ student bus ticket is more elastic, which it isn't, because it is less inelastic than the PED for the adult bus ticket. Some candidates also thought the value of –0.7 is more inelastic than –0.4, which it isn't.

1 The table below shows price elasticity of demand for bus tickets in London 2021

Age	Price elasticity of demand
18+ Student	−0.7
Adult	−0.4

(Source adapted from: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/669090/youth-travel-concessions-price-elasticity.pdf and https://tfl.gov.uk/fares/find-fares/bus-and-tram-fares#on-this-page-4)

(a) Explain **one** likely reason for the difference in the price elasticity of demand for the 18+ student bus ticket and the adult bus ticket.

(4)

• Difference in incomes is likely to affect Price Elasticity of Demand. Student demand is more elastic, at -0.7, compared to Adult PED of -0.4. This is because Students are likely to have lower incomes. Bus tickets are therefore a higher % of their income, making Student's Demand more sensitive to changes in price.

~~An increase in price will lead to a more than proportionate fall~~ However, both PED figures are relatively inelastic as bus tickets are a necessity.

Students' demand ✓ more responsive to a change in price than adult demand.

ResultsPlus Examiner Comments

This is a strong response, which achieved all 4 marks. The candidate has clearly identified that differences in incomes are significant, because the cost of a bus ticket comprises a higher proportion of the students' incomes when compared to adults. The candidate clearly uses the values of –0.4 for adults and –0.7 for students. They tell us that both values are price inelastic. Although the candidate previously said that the PED for students is more 'elastic', which is untrue, we ignored this inaccuracy because of the final sentence. There is a clear recognition throughout the response that the student demand for bus tickets is more price sensitive than that for adults.

ResultsPlus Examiner Tip

Precision is essential to maximising the available marks. Student demand for bus tickets is not more elastic than that for adults. It is less inelastic.

1 The table below shows price elasticity of demand for bus tickets in London 2021

Age	Price elasticity of demand
18+ Student	−0.7
Adult	−0.4

(Source adapted from: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/669090/youth-travel-concessions-price-elasticity.pdf and https://tfl.gov.uk/fares/find-fares/bus-and-tram-fares#on-this-page-4)

(a) Explain **one** likely reason for the difference in the price elasticity of demand for the 18+ student bus ticket and the adult bus ticket.

(4)

One likely reason for the difference in PED is that students have ~~lower savings and~~ incomes than adults. Therefore, 18+ students likely have lower savings than adults, and pay greater attention to what their paying for. As a result they are more responsive to changes in price than adults, with a PED of -0.7. The degree of necessity of bus travel is therefore higher to students.

ResultsPlus
Examiner Comments

This second response achieved 3/4 marks. The candidate gains marks for the recognition of the significance of incomes and the explanation of the importance of them where the price elasticity of demand is concerned. The value of – 0.7 for the PED for student bus tickets is also creditable. However, the last sentence is incorrect because it implies that the PED for student bus tickets is more price inelastic than that for adult bus tickets, which according to the data, it isn't.

Question 2 (a)

This question asked candidates to explain one likely reason for the difference in the price elasticity of supply between New York and Texas. Candidates had to recognise that Texas was price elastic and New York was price inelastic. An understanding that PES is about the supply side is crucial and there were a significant minority of candidates who talked about demand side factors such as the size of the population in New York compared to that in Texas. Here, we were looking for an understanding of planning regulations or shortages in the factors of production, particularly land, in the state of New York compared to Texas.

2 The table below shows price elasticity of supply for housing in the US in 2020.

US State	Price elasticity of supply
New York	+0.5
Texas	+1.8

(Source adapted from: https://bankunderground.co.uk/2020/02/25/the-declining-elasticity-of-us-housing-supply/)

(a) With reference to the data above, explain **one** likely reason for the difference in the price elasticity of supply.

(4)

One likely reason for PES for housing being more elastic in texas with +1.8 is ~~that~~ that there is likely more space in texas for developers to buy ~~an~~ land and build homes on. This means it will be easier to increase the quantity of homes available, therfore making supply more elastic.
This contrasts with New York, where buildings will be more densely packed together so there is less open space so it is harder for people to build more housing, making it more inelastic at +0.5.
NYC may also have more technical difficulties + delays in transporting materials such as steels due to more crowded infrastructure

ResultsPlus
Examiner Comments

This first response achieves all 4 available marks. There is an implicit recognition that in Texas it is easier to increase the supply of houses, which makes supply more price elastic, demonstrating that the candidate understands what price elasticity of supply is. The candidate uses the value of PES effectively and gives a clear explanation of why supply is more responsive because there is more space available on which to build houses. This is then contrasted with New York, which has price inelastic supply because there is less available space.

2 The table below shows price elasticity of supply for housing in the US in 2020.

US State	Price elasticity of supply
New York	+0.5
Texas	+1.8

(Source adapted from: https://bankunderground.co.uk/2020/02/25/the-declining-elasticity-of-us-housing-supply/)

(a) With reference to the data above, explain **one** likely reason for the difference in the price elasticity of supply.

(4)

One likely reason is that Texas has more land area and therefore more housing than New York. Therefore Texas will have a higher PES due to a higher amount of substitute housing, while new York is inelastic as there are fewer substitute houses.

ResultsPlus
Examiner Comments

This response scored 3 marks. There is a recognition that the available land makes Texas more price inelastic in the supply of housing whereas New York is price inelastic. Although the reason given, the quantity of substitute housing, confused price elasticity of supply with price elasticity of demand, there is still creditworthy material here.

ResultsPlus
Examiner Tip

Again, precision is key. Be sure to understand the determinants of the price elasticity of supply in relation to those of price elasticity of demand.

Question 3 (a)

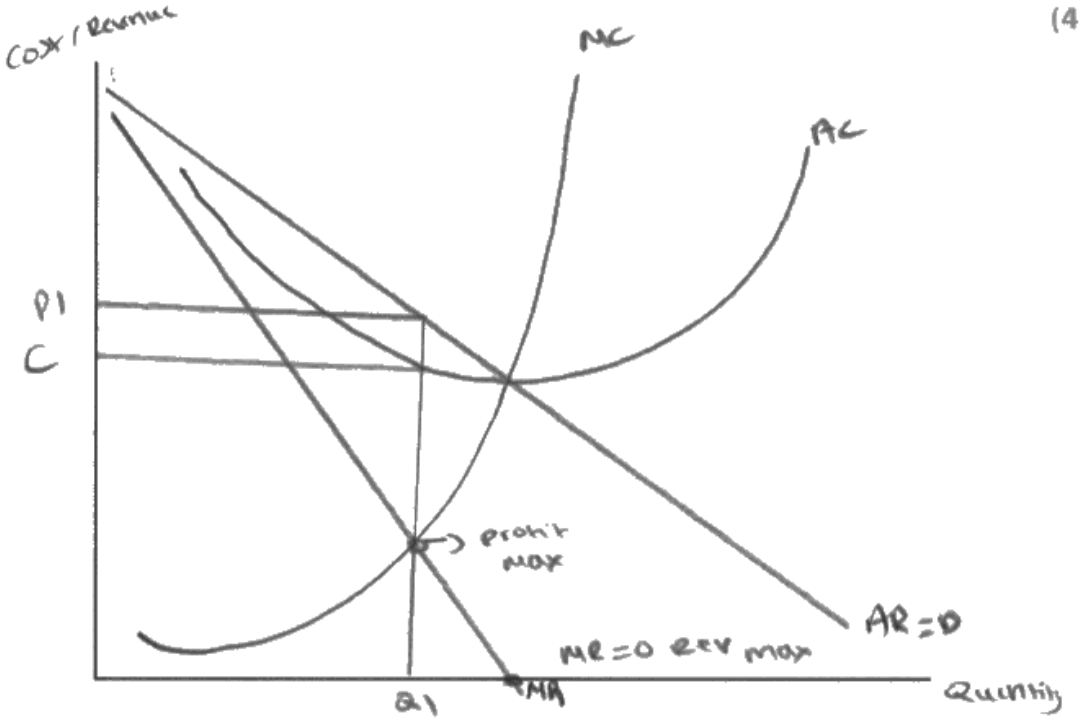
This question is looking for an accurate diagram showing the difference between profit maximisation and revenue maximisation. Candidates had to mark both the output and the price to achieve all four marks. The typical mistake on this question was a failure to mark the price accurately. Many candidates indicated profit maximisation as MR=MC, or revenue maximisation as MR=0. This would gain two marks only.

3 Peloton is a firm which makes exercise bikes. Peloton's objective is to prioritise selling fitness services rather than to achieve short-term profit maximisation.

(Source adapted from: https://www.forbes.com/sites/shelleykohan/2022/01/26/peloton-prioritizes-access-and-acquisition-over-profits/?sh=13d8ee474f40)

(a) Draw a cost and revenue diagram to illustrate the different business objectives: profit maximisation and revenue maximisation.

(4)



(b) If Peloton changes its objective to sales maximisation, then without making a loss, it operates at an output where:

(1)

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Examiner Comments

On this response we can see the candidate has clearly marked the profit maximising point at MR=MC, and this point has been extended down to the x axis and labelled Q1. This point has also been extended up to the AR curve and then across to the y axis, and marked at P1. The candidate has also marked the revenue maximising point where MR=0. However, they have not extended this point up to the AR curve and the y axis. Overall, this response scored 3 marks.

ResultsPlus
Examiner Tip

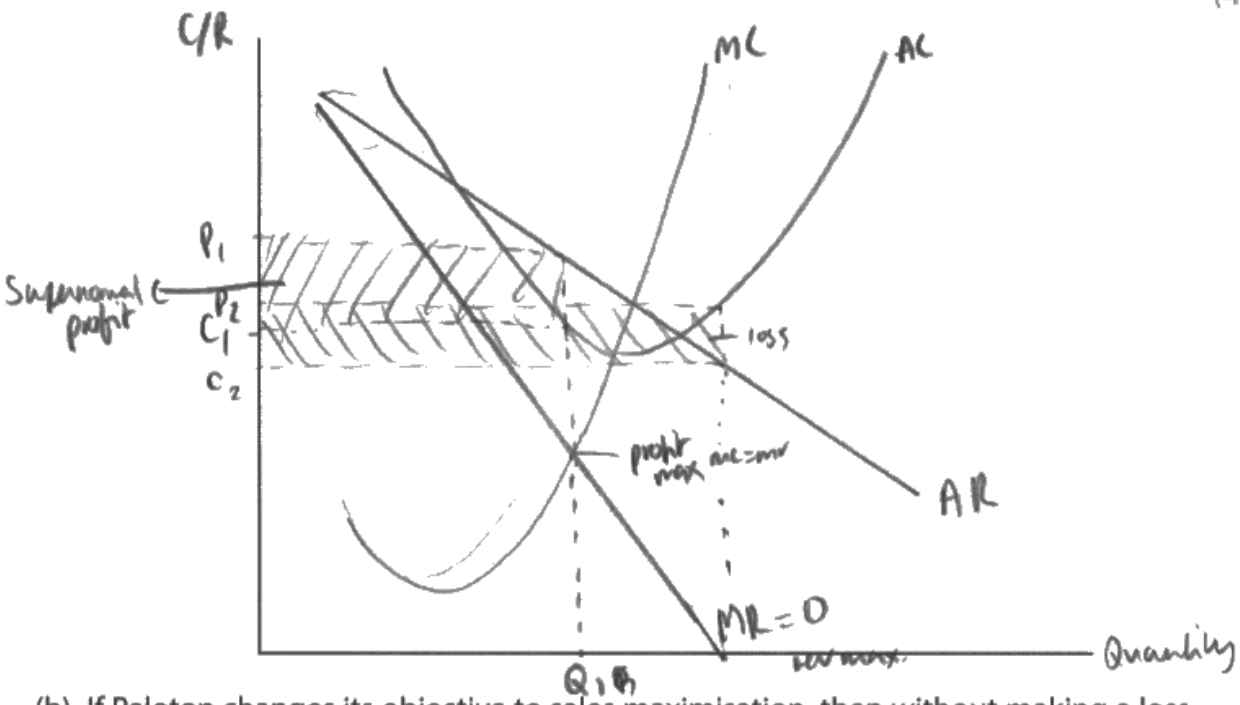
Always ensure that you label diagrams accurately. Practise the drawing of these systematically as you prepare for the examination.

3 Peloton is a firm which makes exercise bikes. Peloton's objective is to prioritise selling fitness services rather than to achieve short-term profit maximisation.

(Source adapted from: https://www.forbes.com/sites/shelleykohan/2022/01/26/peloton-prioritizes-access-and-acquisition-over-profits/?sh=13d8ee474f40)

(a) Draw a cost and revenue diagram to illustrate the different business objectives: profit maximisation and revenue maximisation.

(4)



(b) If Peloton changes its objective to sales maximisation, then without making a loss, it operates at an output where:

(1)

ResultsPlus
Examiner Comments

On this response the candidate has correctly indicated the point of profit maximisation and extended this point to the x and y axes. They have also indicated the point of revenue maximisation and extended it to both axes. Although the extension of the revenue maximising point indicates P2 as higher than C2, the candidate correctly recognises that this is a loss, and has marked the shaded area as a loss. As a result this response scored full marks.

Question 4 (a)

On this question, candidates had to explain one likely reason for the maximum price for an undergraduate university programme. The stem mentions the figure of £9250 per year for the next two years. Candidates referring to either the sum or the time period could access the application mark, with the rest of the marks being awarded for a legitimate reason and the explanation of it. Though there were no marks for a definition of a maximum price, a diagram or a definition of a maximum price was awarded as understanding. Concepts such as positive externalities in consumption could also be awarded. Note that the term 'merit good' is not on the specification. Candidates had to explain the difference between private and social benefits or give some indication that they knew what external benefits in consumption actually are.

4 In 2022 the government announced that the maximum undergraduate tuition fee for universities in England will remain at £9 250 per year for the next two years.

(Source adapted from: https://questions-statements.parliament.uk/written-statements/detail/2021-10-21/HCWS339)

(a) Explain **one** likely reason for the maximum price for an undergraduate university programme.

(4)

One likely reason for a maximum price for an undergraduate University program is to ~~correct for that market~~ increase the provision of a merit good.

Tertiary education has benefits to society that exceed its private benefits. This means it is undersupplied without ~~good~~ government intervention.

By maintaining a maximum price of £9250 per year, for 2 extra years, the government increases provision of the good, ~~not~~ causing excess demand.

This excess demand should increase consumption (or at least willingness to consume) ~~the~~ University education which is a merit good.

ResultsPlus
Examiner Comments

This response achieves all four marks. Although the term 'merit good' isn't on the specification, it is clear from the candidate's explanation that they know tertiary education has benefits to society which are greater than the private benefits alone. For this reason government intervenes to correct this underconsumption. The reference to a maximum price leading to increased consumption shows an implicit understanding of what a maximum price is, and there is specific reference to the cost of tuition being fixed at £9250 for the next two years.

ResultsPlus
Examiner Tip

Be careful to explain any concept using the terminology of the specification.

4 In 2022 the government announced that the maximum undergraduate tuition fee for universities in England will remain at £9 250 per year for the next two years.

(Source adapted from: https://questions-statements.parliament.uk/written-statements/detail/2021-10-21/HCWS339)

(a) Explain **one** likely reason for the maximum price for an undergraduate university programme.

(4)

To ensure that students are able to afford the tuition. As education has a greater societal benefit than private benefit. It is important the the gap is closed between the two curves (MPB-MPC)

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Examiner Comments

This second response scored 2 marks only. The first mark is awarded for the notion of education being made more affordable, and the second for a sense of education having external benefits in consumption, though the concept isn't developed. There is no application mark.

Question 5 (a)

On this question, candidates had to use the information in the market share chart to explain the market structure of mortgage lending in the UK. The most effective method here was to calculate the n-firm concentration ratio, which was worth two marks. This calculation indicated that the market structure was oligopolistic. Marks were then available for some explanation of the characteristics of oligopoly, such as high barriers to entry or a few large firms. Some candidates mistakenly identified monopolistic competition or monopoly from this data.

(a) With reference to the information on the preceding page, explain the market structure of mortgage lending in the UK.

(4)

The market structure is oligopolistic. This is because there are multiple large firms who have a significant market share and although Lloyds does have a slightly larger share, it is not a monopoly. Additionally, the market share of 'other' suggests the main firms in the oligopoly are not completely dominant.

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Examiner Comments

This response clearly recognises that the market structure of the UK mortgage industry is oligopolistic. The candidate then tells us that there are multiple large firms with significant market share. There is then a final mark for the reference to Lloyds being the largest firm. Overall, this response scored 3 marks.

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Examiner Tip

To maximise your marks, always refer to the stem for numerical data. Quoting the table provided or, better still, manipulating the numbers provides access to higher marks.

(a) With reference to the information on the preceding page, explain the market structure of mortgage lending in the UK.

(4)

The market structure of mortgage ~~lending~~ lending in the UK is an oligopoly. The 5 firm concentration ratio is 64%, meaning the market is dominated by the top 5 firms, and they have the highest market share. An oligopoly has a very ~~highly~~ high concentration ratio between few firms, this is a key feature of the oligopoly market structure.

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Examiner Comments

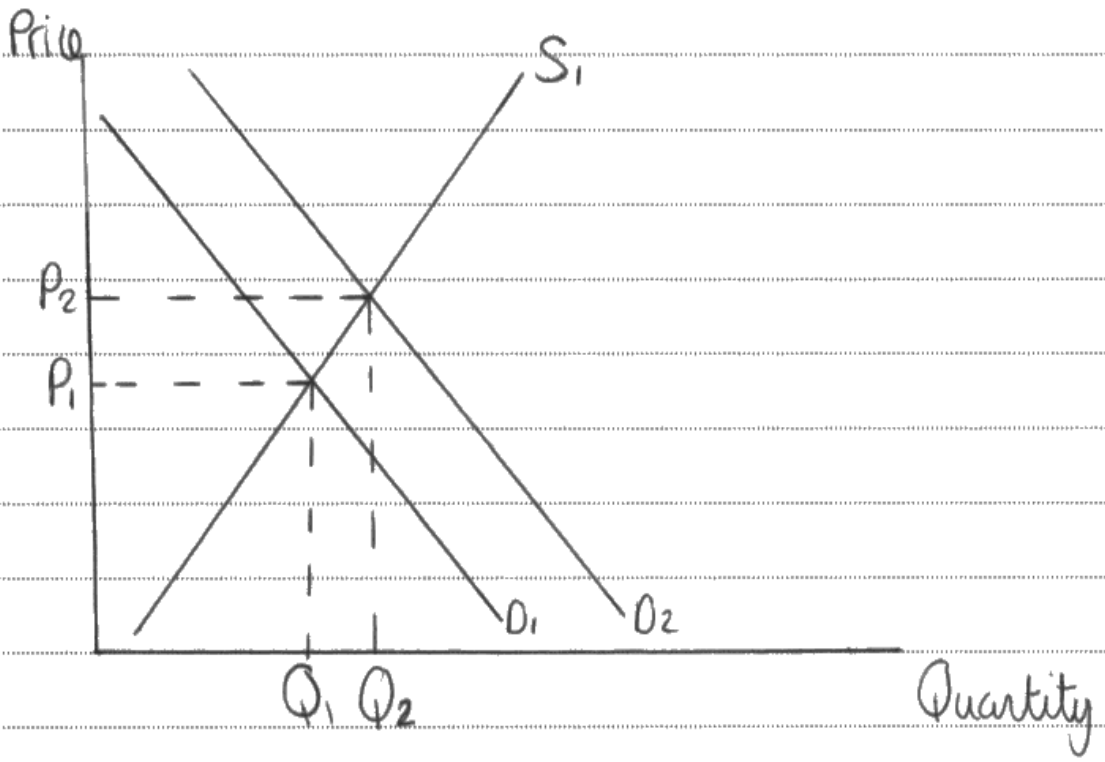
This second response achieved full marks. The candidate informs us that this industry is an oligopoly. They have then used the numerical data to calculate the five-firm concentration ratio of 64%. They go on to tell us this is typical of oligopolistic industries. A very efficient response.

Question 6 (a)

In this question, the first of our Section B examples, candidates had to use Extract A to explain the likely reasons for the change in price of electronic devices. A supply and demand diagram was specifically asked for. The most efficient approach was to draw the diagram indicating the correct shifts, then explaining why the shift occurred the way it did. The application mark was reserved for a specific data reference, such as the increase in the price of computer chips from $0.20 to over 1. Typical issues on this question were the failure to either indicate both shifts or to not explain them in the written narrative.

6 (a) With reference to Extract A, explain the likely reasons for the change in price of electronic devices. Include a supply and demand diagram in your answer.

(5)



There has been a rise in price for electronic devices due to a rise in demand (shown by D_1 shifting outward to D_2) and then the price rising from P_1 to P_2. This is due to a factor such as the growing popularity of home entertainment - which has caused the outward shift in demand, thus causing an expansion along the supply curve.

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Examiner Comments

This response has correctly illustrated a right shift in demand, and explained why this has happened. The reference to the growing popularity of home entertainment gains the application mark. However, there is no reference to the shift of the supply curve referred to in the extract. Overall, this response scores 3 marks.

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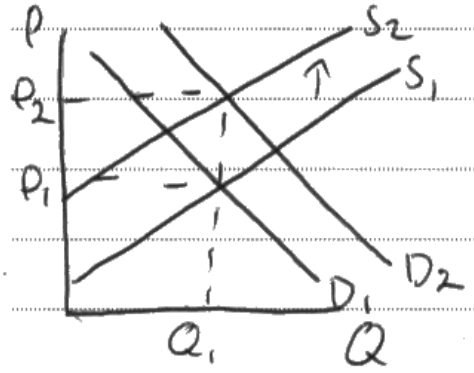
Examiner Tip

Carefully reading the extract is essential to maximising the marks on data response questions. The data contains relevant information that candidates can use.

6 (a) With reference to Extract A, explain the likely reasons for the change in price of electronic devices. Include a supply and demand diagram in your answer.

(5)

Extract A states, "The prices of electronic devices have risen for a range of reasons, including higher material costs and the growing popularity of home entertainment". Therefore there has been a rise in demand for electronic devices as well as a fall in supply as costs of production have increased. Supply ~~[illegible]~~ falls as it shifts upwards from S_1 to S_2. Demand increases from D_1 to D_2. As there is a fall in supply despite the increase in demand, quantity demand remains at Q_1 due to a lack of supply. As costs of production have increased prices move from P_1 to P_2.



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Examiner Comments

This second response is significantly better than the first. The candidate uses the extract and quotes it directly. They pick up on the fact that higher material costs have also caused the supply curve to move inwards. The drawing of the new supply curve and the explanation of the reason gains access to all the marks available for this question.

Question 6 (b)

This question asked candidates to examine two factors which might influence the supply of labour in the electronics industry. The response had to be specific to the electronics industry to access the application marks, the best way to do this is the use of quotation marks. It is best practice to state one reason and then clearly reference it from the extract. Not clearly differentiating the two means examiners may not award the knowledge mark and the application mark separately. This is where good examination technique is important. The analysis of how or why the factor affects the supply of labour then gets the analysis mark. Remember that two factors are asked for. Many candidates erroneously discussed demand side factors. Factors such as changing wage rates had to be carefully explained to show how the supply of labour is affected.

elasticity (inelastic) -> info gap

P, A

(b) Examine **two** factors which might influence the supply of labour in the electronics industry.

(8)

one factor that may influence the supply of labour in the electronics industry is elasticity. Since working in the electronics industry is highly skilled, it is likely that the elasticity of the supply of labour is ~~this~~ low (inelastic). This is likely due to a lack of wanting to train to be qualified to work in the electronics industry. This may reduce the supply of labour since ~~less~~ more highly skilled & experienced employees in the electronics industry retire".

However, this depends on the substitute of machinery/capital. It is stated that production is becoming more automated, meaning that capital has a benefit over labour, whether that is a higher PPP or lower costs than labour. This depends on the short & long run. In the short run, capital may not be as productive as labour (↓PPP) and will lead to government intervention, such as subsidising teaching/training in the electronics industry. This will end up stimulating supply of labour in the long run as training will be complete in the long run and capital would no longer be a fixed variable. Ultimately, the LR would actually increase the supply of labour.

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This first response scored six marks. The first knowledge mark is achieved by reference to the inelastic nature of labour supply and this is explained to achieve the first analysis mark. The first application mark is gained by the reference to the electronics industry in the final sentence of the first paragraph. However, because there is no second factor discussed, the second available knowledge and analysis mark cannot be accessed. However, there are two application marks available, and these can be achieved for separate pieces of data. The reference to production becoming more automated at the start of the second paragraph is sufficient to gain the mark. Furthermore, the quality of the evaluation is very strong, so both evaluation marks can be awarded.

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Examiner Tip

If two factors are asked for then two must be supplied to gain full marks. However, application and evaluation marks are not linked to just one reason.

(b) Examine **two** factors which might influence the supply of labour in the electronics industry.

(8)

One factor may be the shortage of staff. This is because every year highly skilled employees in the electronic industry retire. This means that there will be less workers available in the market, causing a shift inward for supply. This all depends on the magnitude of the retiring, and if the new skilled employees can replace them at the same supply.

Another factor may be due to the shortage in skills. This is because the nature of the industry is becoming increasingly technical. This means higher skilled workers are required and thus leads to a fall in the available supply of workers who are able to successfully fill the role with the correct qualifications. This all depends on whether the electronic business needs a labour intensive - which requires more staff or capital intensive - which requires less staff.

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This second response is a very efficient piece of writing, demonstrating excellent examination technique. The candidate uses two separate paragraphs and achieves one knowledge, application, analysis and evaluation mark in the first paragraph. The process is replicated perfectly in the second paragraph where the other 4 marks are achieved.

Question 6 (c)

This question is the first of the levels-based responses, and was looking for an assessment of whether firms in the electronics industry benefit from economies of scale. The approach here was to write one paragraph on why the firms benefit and another on why they didn't. Whilst many candidates considered several factors it was possible to obtain full marks by discussing one factor on either side, in depth. Many candidates confused economies of scale with dynamic efficiency, which is about the change in productive efficiency over time. This would cause the long run average cost curve to move downwards. Economies of scale happen when the firm moves further along the original long run average cost curve, towards the minimum efficient scale. Overall, most candidates could discuss the different types of scale economies, such as financial or managerial, and then evaluate by discussing likely diseconomies of scale or whether dynamic efficiency was more significant than economies of scale, given the nature of the industry. The key point here was to assess the extent of these economies in the electronics industry.

(c) Assess whether firms in the electronics industry benefit from economies of scale.

(10)

Firms in the electronics industry do benefit from economies of scale, as they can purchase materials (i.e. components) in bulk which creates lower marginal costs due to bulk buying discounts. This creates significant benefits for these companies as lower costs allow them to make greater profits (ceteris paribus), which can be retained and used for greater innovation or development of new products, for example.

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Examiner Comments

This first response is a weak response that gained only three of the marks available. The candidate only tells us that firms in the electronics industry benefit from economies of scale. The point about bulk buying discounts accessing lower costs is valid, but the candidate then goes on to discuss gains in dynamic efficiency achieved through new product development. There is no evaluation of the points made. This response achieved bottom level 3, for 3 marks.

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Examiner Tip

This a 10 mark question, with 6 marks available for knowledge, application and analysis, and 4 marks for evaluation. To access the marks you should aim to spend roughly 6 minutes developing the KAA and 4 for the evaluation. To access full marks you just need to develop one argument on either side. Efficient use of time is important!

(c) Assess whether firms in the electronics industry benefit from economies of scale.

(10)

Electronic firms may benefit from internal financial economies of scale. This is because the growing size of firms, with "Nvidia" and "Arm" agreeing a "£29.5 billion deal" will mean firms within this industry can negotiate loans from banks at lower rate of interest, because they are seen as more trustworthy and have more collateral. Therefore, these firms can drive down their long run average costs because they are able to finance "innovation" which will drive productivity increases and whilst having to pay less in interest payments to banks. This helps firms in this industry become more productively efficient. However, firms benefiting from this internal economies of scale may not be realised. Extract C says the "innovation" many of these firms undertake is "high risk" so banks may not actually see the proposed loan as 'safe' and will not charge low interest on them. Furthermore, it is likely to only be the dominant firm within the "electronic industry" who will benefit from low interest 'priority' loans if they are given, so smaller firms within

the industry will be unlikely to benefit from the internal economies of scale.

Firms in the electronic industry may also benefit from marketing economies of scale. This is where costs of marketing to promote the company are spread over a larger number of consumers which reduces the average cost of marketing for these firms. Extract C notices the fact that "Arm" has been taken over by "its US rival Nvidia". This suggests that the integrated company now has a consumer base in [redacted] Britain (with "Arm" being based in "Cambridge", and the US. Therefore, the firm can market its "computer chips" worldwide, which reduces the average cost of advertising. Despite this assumption, however, the cost of integrating with firms in different countries may outweigh the reduced average costs gained from marketing economies of scale. Furthermore, as in trying to achieve the internal economies of scale from integrating with an overseas firm, as "Nvidia" have done, the two firms may suffer from communication diseconomies of scale as communication within the company now have to go through more layers of hierarchy which may slow productivity and increase average cost more than they

one reduced by marketing economies of scale. Ultimately, it depends on how far firms can exploit this internal economies of scale to see if it will be beneficial in the wider context.

ResultsPlus
Examiner Comments

It is clear from this second response that the candidate has achieved considerably more in the time available. The candidate talks about the economies of scale potentially achievable through the proposed merger of Nvidia and ARM. There are two well developed points, the first concerning the financial economies of scale from being bigger, which can then be invested into the firms becoming more productively efficient. This point is then well evaluated. The candidate then discusses marketing economies of scale, again in the context of the merger, and evaluates by discussing potential diseconomies of scale. This response achieved full marks.

Question 6 (d)

For this question, candidates were expected to discuss two concerns of the competition authorities regarding the proposed merger. The typical pattern here was for candidates to focus in on the likelihood of impediments to the operation of competition or a substantial lessening of competition. Evaluation then focussed on the potential gains of various economies of scale which could result in lower prices for consumers, or the dynamic efficiency gains resulting in better quality products. Responses to this question tended to be very good on the whole.

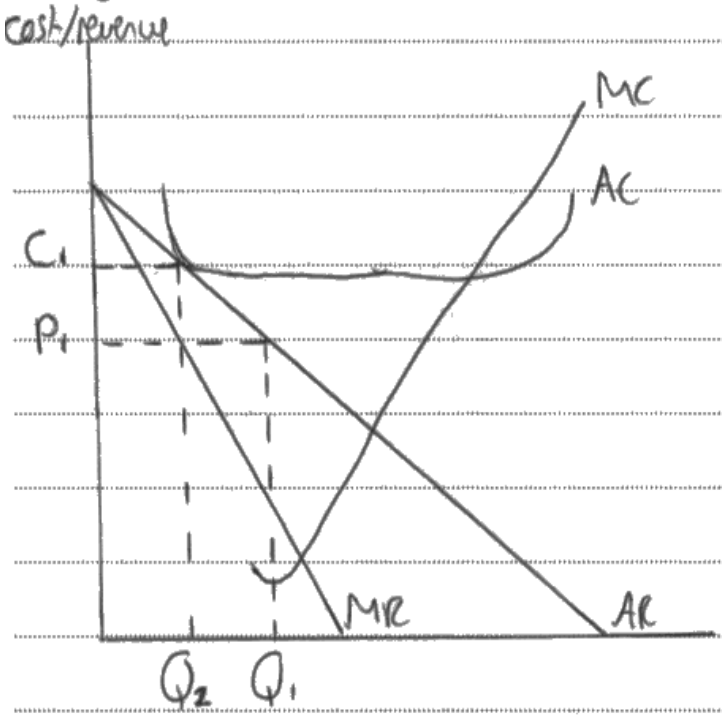
(d) Discuss the likely concerns of the competition authorities regarding the proposed merger of the two companies referred to in Extract C.

(12)

One concern for the competition authorities would be the reduced choice for firms surrounding products such as computer chips, which then drives up prices for consumers. The competition authority is an authority which ensures a market is competitive and if not, takes steps to make it competitive. By allowing the takeover of the Cambridge business for computer chips by Nvidia, this will raise a serious concern surrounding the competitiveness of the market. This is because there is a reduced choice for firms that are reliant within the market for computer chips, creating a possible monopoly state within the market. A monopoly then restricts competition by being the price setter, causing a reduced choice for consumers when it comes to products such as phones due to the fall in available substitutes. This would then cause a fall in the consumer surplus - which is the ability and willingness to pay the price set and the actual price set, with the difference between these falling due to a rise in price and reduction in choice. This would be problematic as the government aims to maximise social welfare, and this merger would lead to a reduction in this due to the falling consumer surplus. This could all depend on the available substitutes for computer chips within the market, with the elasticity coming into play. If the computer chips are elastic, then this means the merger won't be majorly

problematic due to there being alternative solutions and products. This would mean there is elastic supply of chips, causing a fall in potential prices for businesses, leading to longer term stability over supplies and a more competitive market due to more bargaining power.

Another concern would be the ~~rise~~ fall in competition from businesses due to rising costs. This is because costs are what makes up the equation for a businesses profits - revenue - costs. By having a shortage globally of compute chips, accompanied by this potential merger - there will be a restriction in the supply available for compute chips. This scarcity of supply will lead to a rise in cost for the chips, which then disrupts the manufacture of the goods provided and rises costs. These rising costs will makes business profits fall.



The rise in costs will lead to a fall in supernormal profits and actually cause a normal profit - where AC = AR. This means that if the business were to keep losing costs, it could fall to the shut-down price; P < AVC.

This all depends on the policies put in place by the government - with the idea that maximum prices could be introduced in order to stop the dominant supplier from exploiting businesses. This would mean that business costs would stay the same and even fall in the long term, allowing the same levels of competition and thus a healthy market for competition. This would then cause the government to reach its objective of social welfare maximisation as a result.

ResultsPlus
Examiner Comments

This first response is a well written and well developed example, which scored 9/12. The first argument is about reduced choice for firms within the industry, which will potentially reduce consumer surplus. This first argument achieved bottom level 3. The evaluation of the argument achieved bottom level 2. The second argument is in some ways a development of the first, and dives further into the notion of rising costs and lower profits. We felt this was rather confused in places, but still merited top level 2. Again, the evaluation regarding government intervention was in context and we awarded bottom level 2 for this. Overall this response achieved bottom level 3 KAA and bottom level 2 evaluation.

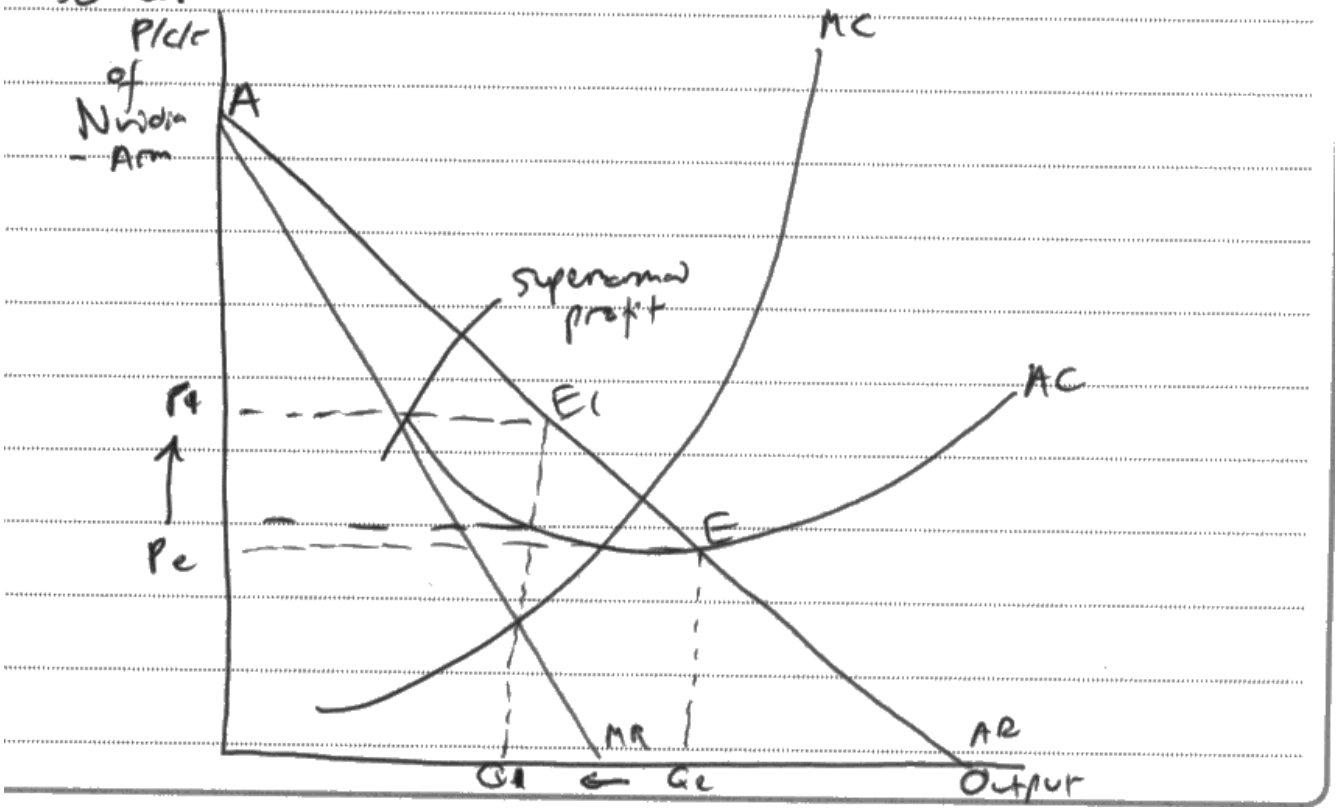
ResultsPlus
Examiner Tip

It is important to clearly distinguish two specific concerns in this question and explain concepts with clarity and in context.

(d) Discuss the likely concerns of the competition authorities regarding the proposed merger of the two companies referred to in Extract C.

(12)

One concern the "Competition and Markets Authority" may have had about the "$29.5 billion deal" of Nvidia's takeover of Arm was a Substantial Lessening of competition (SLC). This is where the merger of two firms results in a significant reinforcement of monopoly ~~power~~ "oligopoly" power, and the benefits to efficiency could have otherwise been achieved. Through this takeover deal, the new firm may have gained significant monopoly power within the electronics market, which may result in far higher costs for firms purchasing their "computer chips", which will in turn harm consumer welfare if these higher prices are passed on. This effect is seen on the diagram below.



Whereas before, in a more competitive market, the firms Nvidia and Arm may have been pricing at AC = AR, where the consumer surplus (for electronics firms buying the computer chips) was AEPe, at the higher price that the new, larger firm can charge where MC = MR (the profit maximising point), the new consumer surplus for firms is reduced to AE1P1. The CMA may recognise that the SLC will result in higher prices for consumers of electronic products, as firms have to pay higher prices for computer chips at the new, consolidated, larger firm. However, the CMA may find this ~~loss of a~~ proposed merger less of a concern if it will result in dynamic efficiency for the new firm. With electronics being a luxury item, not a necessity, consumers may not mind paying higher prices if their electronics are faster and more durable due to more advanced "computer chips" that the new merged firm can provide in the long term if they reinvest their supernormal profits. In which case, instead of blocking the merger, the CMA may find some regulation of the new firm more desirable for consumer welfare, such as some profit regulation to ensure the price does not get excessively high.

The CMA may have also had concerns about the "reduced choice for firms" within this industry as the new merged firm may be able to exploit economies of scale and drive other computer chip producers out of the market. This may be detrimental for the industry because it may exacerbate the "global shortage of computer chips" as more suppliers are forced out of the market. This will result in more price volatility for electronic firms who are producing "electronic goods" not allowing for long term buying planning, as the price of their input costs will become unreliable & dictated by the production capacity of the dominant firms such as the consolidated ARM-Nvidia company. Therefore, the CMA may choose to block the merger to prevent these effects. But, the CMA may instead be able to combat this effect if the merger takes place by placing performance targets on the new firms' output. Therefore, businesses are aware of the projected supply of computer chips & there is less volatility of their input costs. It depends on what the CMA wants to prioritise in the industry, where it be the dynamically efficient possibilities of the new merged firm in which case performance targets may be the best option, or to block the merger & improve choice across the industry.

ResultsPlus
Examiner Comments

In this second example, the candidate discusses how the merger could lead to a substantial lessening of competition. The candidate explains how this could lead to a fall in consumer welfare if these higher prices are passed on. The quality of the analysis, in context, is excellent. It is linked to a clearly drawn and labelled diagram. This first paragraph achieved top level 3. The first evaluative chain focusses on government intervention to mitigate the impact of the merger and considers how some consumers may not mind paying higher prices for higher quality products. This achieved level 2. The second KAA paragraph concerns another potential concern, that of the merger leading to a reduction in the number of firms in the industry as a consequence of the economies of scale achieved by the newly merged firm. This scored top level 3 due to the precision of analysis and the embedding of information from the extract. The evaluation focusses on the potential dynamic efficiency gains available to the new firm and how the competition authorities must weigh these against the potential costs. This scored top level 2. Overall, this response scored full marks.

Question 6 (e)

For this question it was important to discuss a range of possible methods of government intervention to reduce electronic waste. Extract D provided a range of these, so candidates were able to perform well on this question, though good examination technique really made the difference again. The approach was to choose two complementary methods, perhaps indirect taxation and subsidisation, and then illustrate them with clearly drawn and explained diagrams. This is a classic example of how diagrams could be used to support an answer without being specifically asked for. Having said this, full marks could be achieved without the use of a single diagram. The key was clear analysis and evaluation of the proposed methods.

Government intervention is when the government gets involved in a economic problem because the free market wont provide a solution.

One possible meathod is to Subsidise recycling initiatives. For example recycling firms are given money in order to promote and collect recycling electronic waste. When they collect a citain amount they are rewarded with finance.

This however can be a very expensive way of dealing with the problem as the amount of Subsidies that would have to be given out to recycling firms would be not worth it, and it would be the tax payer paying for it all.

The goverment could launch an educational campaign educating people on the significance of why they should recycle electronic

waste.

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Examiner Comments

This response discussed two methods that the government could use to deal with the problem of electronic waste. The subsidisation of recycling initiatives was explained, followed by the launching of an educational campaign. The first argument was rather descriptive and there was only a basic development of how and why the policy might be effective. The evaluation of the policy focussed on the cost of the subsidy to the taxpayer. The second argument contained very little development at all and there was no attempt to evaluate its probable effectiveness. Overall, this response achieved level 1 KAA, 3 marks, and level 1 evaluation, 2 marks. 5 in total.

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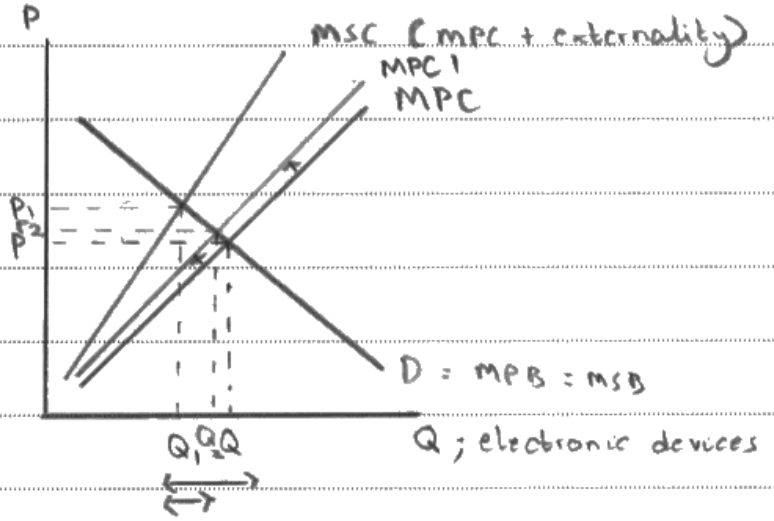
Examiner Tip

In the 15 mark questions it is important to develop arguments in detail. Diagrams are helpful and will focus the analysis. There are also 6 marks for evaluation, so take the time to consider why the methods proposed may not be effective.

(e) With reference to Extract D, discuss possible methods of government intervention to reduce electronic waste.

(15)

The government could reduce electronic waste through the implementation of a tax on electronical devices. By doing so, ~~the~~ it can attempt to internalise the negative externality caused by the use of devices, electronic waste, by raising their costs of production. As a result, the level of production contracts to a level nearer to the socially optimum level. For example, by taxing the 1.2 million tonnes of electrical devices sold in the UK, less will be produced, therefore decreasing the value of 700 000 ~~appp~~ tonnes that did not make it to recycling. Consequently, the externality is internalised, as shown below;



Q - Free market

Q_1 - Social optimum

Q_2 - Free market after tax

Initially, there is allocative efficiency in the market caused by the externality as electronic devices are overproduced (Q to Q_1) The tax reduces the overproduction (Q_2 to Q_1), hence internalising the externality.

However, evaluating this, the extent to which a tax internalises the externality depends on the price elasticity of demand for electronic devices. If price elasticity of demand is inelastic, the tax becomes inefficient as producers can simply pass on the increased costs as a higher price to consumers. As a result, as supply is shifted leftward, it moves along a steeper demand curve, rendering its effect on the reduction in supply relatively useless - the overproduction is ever so slightly decreased.

Furthermore, the government could reduce electronic waste through the implementation of financial initiatives, such as a recycling subsidy. A subsidy would encourage recycling by decreasing ~~the~~ a firm's costs, incentivising it to recycle. For example, given that only 20%. of appliances ~~it~~ are recycled, a subsidy would decrease the ~~#~~ quantity of devices not-recycled, reducing the issue.

In evaluation, a subsidy has a high opportunity cost. Therefore, the money spent on the subsidy could be spent elsewhere, such as in increasing awareness/education of environmental protection, in schools or workplaces. Moreover, a subsidy to solve the issue of recycling may be ineffective due to strong effect of habitual behaviour, affecting rationality of consumers.

ResultsPlus
Examiner Comments

This second response is clearly much better than the previous one, and scored 13/15. The first method is the use of a specific tax on the manufacturers of electronic devices. This is linked to a diagram which shows the negative externalities of production, and demonstrates how the tax would work to reduce them. The narrative uses the extract and clearly answers the question. This achieved top level 3. The evaluation of the method is very good, and achieved bottom level 3. However, the second method focussing on subsidies is not as well developed as the first. It just makes level 3. The evaluation of the method is also in context and gets into level 3. Overall, this response achieved level 3 KAA, 8 marks, and level 3 evaluation, 5 marks.

Question 7

In this question, candidates were asked to evaluate the microeconomic effects of rising energy bills on the hotel industry or an industry of the candidates' choice. Inevitably, most responses focussed on the hotel industry because the stem provided a location, a specific real world example, and a pathway into a discussion about the buying power of larger hotels. The responses to this question tended to follow the impact of cost and quality of provision, as hotels reduced services in a struggle to balance the books. There were many imaginative responses which discussed the differential impact depending on location, time of year, and whether the hotel was small or part of a large chain. Again, the good use of accurately drawn cost and revenue diagrams often significantly enhanced the quality of many responses. Short run shutdown scenarios were particularly effective.

effects of ↑ energy bills — hotel industry

- ↓ profits → however counteracted by ↑ prices? → depending on PeD
- unable to afford to keep hotel running?

Firstly, rising energy bills are likely to cause hotels to experience reduced profits. These are part of their costs, which, if all else stays the same, will cause profits to fall. This means that they may not be able to afford to expand their operations, which can be especially important to smaller hotels who rely on each customer as a source of revenue, as opposed to global chains whose high profits aren't affected by the individual customer. If smaller hotels are able to supply more rooms by expanding, they are able to improve their profits and potentially cover the additional costs incurred through the increased energy bills, pulling them away from a potential shut down situation in the long term.

However, increased costs can be counteracted by greater revenue through increasing prices. Although this is likely to cause reduced demand, the increasing prices will introduce more revenue per customer, which would be a huge benefit to

smaller hotels such as local, independent 'BnBs' who, as previously mentioned, rely on each individual customer as a source of revenue to keep them away from a point of shut down. However, this does depend on their customers' price elasticities of demand; if this is high, even a small price change could make potential customers go elsewhere, whereas a low PeD wouldn't change demand as much. This strategy is very uncertain, however, so hotels may be reluctant to continue especially if they don't have perfect knowledge.

Another effect of rising energy bills, especially on smaller hotels such as the one in Scarborough, which saw a 400% rise in monthly energy bills, is a lack of demand. A rise in energy bills for one hotel is likely to mean that everyone is suffering from the same problem, including households. This means that customers may not be able to afford to go on holiday or buy a hotel room, so demand falls.

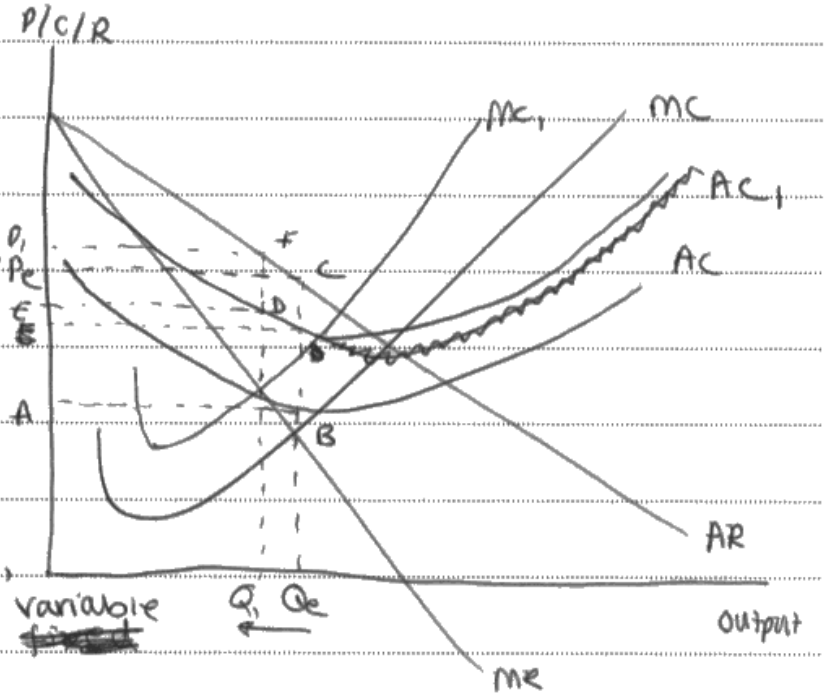
ResultsPlus
Examiner Comments

In a 25 mark essay it is good practice to write two developed KAA paragraphs to approach the top level, and to ensure that there is in depth evaluation of both arguments. In this first example we see two KAA paragraphs, the first one regarding the impact of rising energy bills on costs. The candidate explains how rising costs will reduce profits for hotels, which will in turn reduce their ability to expand their operations. This first paragraph was awarded level 2. The candidate then makes a valid evaluative point by explaining that hotels could increase their prices to counter higher costs, but that this would depend on the price elasticity of demand of their customers. This was awarded level 2 evaluation. The candidate then makes a second KAA point about falling customer demand affecting the entire industry because of the scale of the increase in cost. This is not particularly well developed, and was awarded level 2. There was no further evaluation. Overall, this response scored level 2 KAA, 7 marks, and level 2 evaluation, 4 marks. This is 11/25 in total.

ResultsPlus
Examiner Tip

Writing a 25 mark essay is a crucially important skill. There are 4 across all three papers in the series. There should be at least two KAA paragraphs to develop both the depth and breadth of argument. There should be in depth evaluation of each KAA paragraph. At the end of the essay there should be a conclusion that works towards a justified judgement.

One microeconomic effect of rising energy bills on the hotel industry would be a decrease in abnormal profit. As energy increasing from '£2000 to £8000', there is an increase in variable ~~cost~~ and MC costs, causing AC to shift to AC_1 and MC_1.



Therefore, hotel firms see a significant decrease in profit from ABCP_e to DEFP_1. This causes a loss of the ability for reinvestment to improve the quality of hotels by improving services, such as concierge services. ~~Therefore, [illegible] hotel firms may see a subsequent decline in demand due to the lack of services meeting consumer needs. For example, in the hotel~~ and potential unemployment of labour. Therefore, as staff members may fall, hotels may see a subsequent decline in consumer welfare, due to the service-based nature of hotels. This may result in a decline in demand, further reducing profits for hotel firms. However, this is largely dependent on the

location of hotels, affecting the elasticity of demand. for example, hotels located in tourist areas and near amusement parks, meaning relatively price consumers are less likely to be affected by service as they are purchasing the experience of the area, rather than the hotel, directly, rendering these hotels to be relatively price inelastic. On the other hand, those that are resorts intended for customers to spend the majority of their time at, may suffer more from worsened service as a result of smaller profit margins.

Another effect on rising energy bills on the hotel industry, would be a decline in competition as smaller firms are forced out of the market. Due to the fact that small firms are unable to 'negotiate better deals', they are likely to be unable to cover their average variable costs, reaching shut-down point. Therefore, there is a fall in competition as the number of firms in the market decrease. This can, in turn, negatively impact consumers as prices increase due to higher market concentration. Moreover, this allows oligopolies to form as there are fewer firms in the hotel industry, which opens up the market to collusion, further harming consumer interests. In the UK, the hotel industry can

be said to be an oligopoly due to the dominance of Travelodge, Premier Inn and and Holiday Express, as bed and breakfasts. Therefore, these firms may be able to divide the market, leaving consumers with even less choice, as their demand is forced by the location of their holiday. However, this is dependent on whether the CMA is able to limit this collusion by fines or whistleblower policies, which have increased to up to £250,000. Therefore, the consumer interests, harmed by oligopolies, would be protected. Additionally, the government may subsidise smaller ~~firms~~ firms in order to prevent the lessening of competition, further reducing unemployment and negative impacts of oligopolies for consumers.

Overall, the most significant impact of increased energy bills would be ~~causing~~ a decrease in the number of firms in the market, allowing the formation of an oligopoly. However, with the rise of AirBnB, it can be argued that the hotel industry is beginning to become more contestable. and so oligopoly. Therefore, smaller hotel firms may be able to transition into accomodation for AirBnBs and shift their resources. ~~On the other hand, Furthermore~~. Hence, this allows consumers to maximise welfare due to lower prices in the long run and smaller

firms are able to maintain substantial levels of profit by readjusting to AirBnBs, and renting out the space.

ResultsPlus Examiner Comments

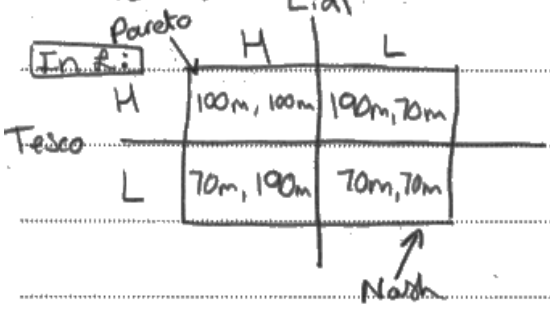
In this second example we see a very strong response. The first KAA paragraph explains how rising costs reduce abnormal profits. The analysis is deepened by a carefully drawn diagram which shows the increase in both average and marginal costs, and the reduction in profits. The candidate moves on to explain how this would reduce hotels' quality of service and lead to potential job losses. This was awarded level 4. The next paragraph then develops some strong evaluation, explaining how the negative impacts would depend on where the hotel is located, because the quality of service is less relevant when the location itself is a more important factor. This was awarded level 3 evaluation. The second KAA paragraph discusses the negative impact on competition, explaining that smaller hotels may not benefit from the scale of operations that would allow bigger hotels to absorb cost increases. There is then a discussion of the possibility of oligopolistic collusion which then leads to higher prices for consumers. This was also awarded level 4. The candidate then moves on to evaluate by saying that the government may take measures to offset the negative effects on competition. This was awarded level 2 for evaluation. Finally, the candidate then attempts a conclusion, and prioritises the negative impact on competition. However, this then brings in new material on Airbnb and contestability. Overall this response achieved 16 marks for KAA and 7 for evaluation, so 23 in total.

Question 8

This question, quite similar to Q6(e) from 2022, expected candidates to evaluate the level of contestability in the fragrance industry. It was asking whether the level of contestability is high or low in that particular industry. Other industries could, of course, be chosen, but the approach was fundamentally the same. This was not a popular question, and the quality of responses was significantly poorer than those seen in Q7. Many candidates did not discuss contestability. A contestable market occurs when there is freedom of entry and exit into the market. It is not the same as the existing level of competition in a market. In a contestable market, it is not the number of firms that is important but the ease with which **potential** competition can become **actual** competition. When candidates talked about the extent of barriers to entry or the extent of sunk costs they were able to access marks. However, many candidates talked about perfect and monopolistic competition and neglected to mention sunk costs or hit and run competition at all. The key takeaway from this example is to only attempt questions when the content is fully understood.

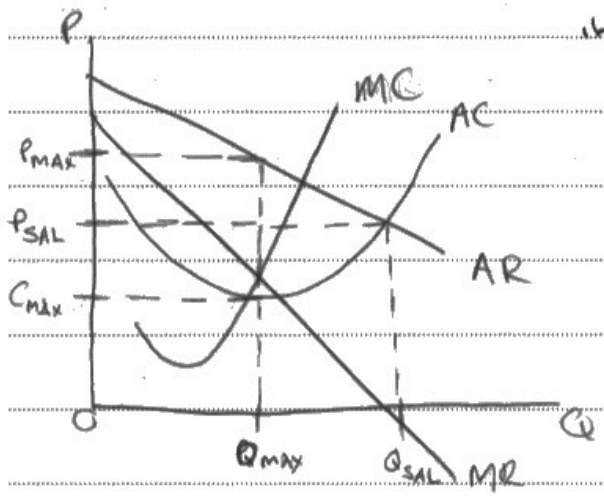
Contestability refers to the ease of entry & exit into a market & the ability to compete within said market. ~~The If a market is contestable, then there is a smaller number of~~

The supermarket industry operates as ~~an~~ an oligopoly, with Tesco, Lidl & ~~Sainsbury's~~ Sainsbury's amongst others operating as the ~~leaders of the market~~ largest firms, & are considered price makers. As such, they are able to collude tacitly or ~~overtly~~ overtly at a point where their prices are set to maximise profits, shown on the left where they both operate at the Pareto equilibrium, making both making £100m respectively. ~~If Tesco~~ & Other oligopolistic firms such as Sainsbury's will also follow in order to maximise their profits. This creates a barrier to entry within the market, as new firms who enter the market will not be able to ~~benefit from this~~ compete with these firms ~~prices~~ & ~~so~~ will not be able to garner as much profit as they are price takers & will be forced to charge at a price that will damage their sales.



However, it is likely that oligopolistic firms will not operate at the pareto equilibrium in the long run, as the personal benefit to either Lidl or ~~Tesco~~ Tesco of deviating from their agreement benefits them personally & as firms are profit motivated, they are likely to use aggressive ~~price~~ pricing strategies ~~such as~~ to undercut ~~either~~ & gain a huge short-run supernormal profit. In this case, the market becomes ~~less contestable~~ even less contestable, as firms entering the ~~market~~ market must take the current high market price.

It can be argued, however, that the supermarket industry is actually a monopoly, as ~~Tesco~~ Tesco currently has a 26% market share, which fits the CMA definition of a monopoly of 25% or more market share. As such, Tesco is able to change their objectives in the short run from profit max to sales max, ~~in order~~ to sacrificing short term supernormal profits for normal profits at a price which is significantly lower than the competition. This acts as a limit pricing & limits the quantity of firms that can enter the market as they are unable, with a lack of economies of scale which Tesco benefit from, to offer such low



prices. Tesco may also move along the AR curve between profit max & sales max to control the level of existing firms within the market, causing existing firms to leave. This therefore supports the argument that the supermarket industry is not a contestable market due to the abuse of monopoly power, as it ~~leads~~ leaves smaller firms vulnerable & unable to compete in the set market conditions.

However, the supermarket industry has a large number of smaller firms which may be argued to ~~shift~~ market share as the market concentration contradicts the argument that Tesco is a monopoly. Futhermore, in particular geographical areas where there is a lack of supermarkets, smaller firms may become local monopolies, ~~but~~ & make huge ~~the~~ amounts of supernormal profits, however this in the Long Run will signal for firms to enter the market ~~to~~ within the area, but it can be argued geographically that the market may be contestable.

ResultsPlus
Examiner Comments

This first response to the question made a reasonable attempt to address the issues surrounding contestability in the fragrance industry. there is some good context and the discussion of relevant theory such as limit pricing. However, the candidate doesn't really get to grips with what contestability actually is. In this response the candidate has discussed the supermarket industry and how its barriers to entry make it oligopolistic. The evaluation is somewhat confused, hinting that the collusive equilibrium previously discussed may not be achieved because of price wars, but that this now constitutes another barrier to entry. The second KAA paragraph on limit pricing is well developed and achieved level 3 KAA. Tesco is a legal monopoly, though there are multiple large competitors, and some local monopolies. Overall, this essay mixed elements of competitiveness and contestability and struggled to fully answer the question. Overall, this response achieved bottom level 3 KAA, 10 marks, and bottom level 2 for evaluation, 4 marks, so 14 in total.

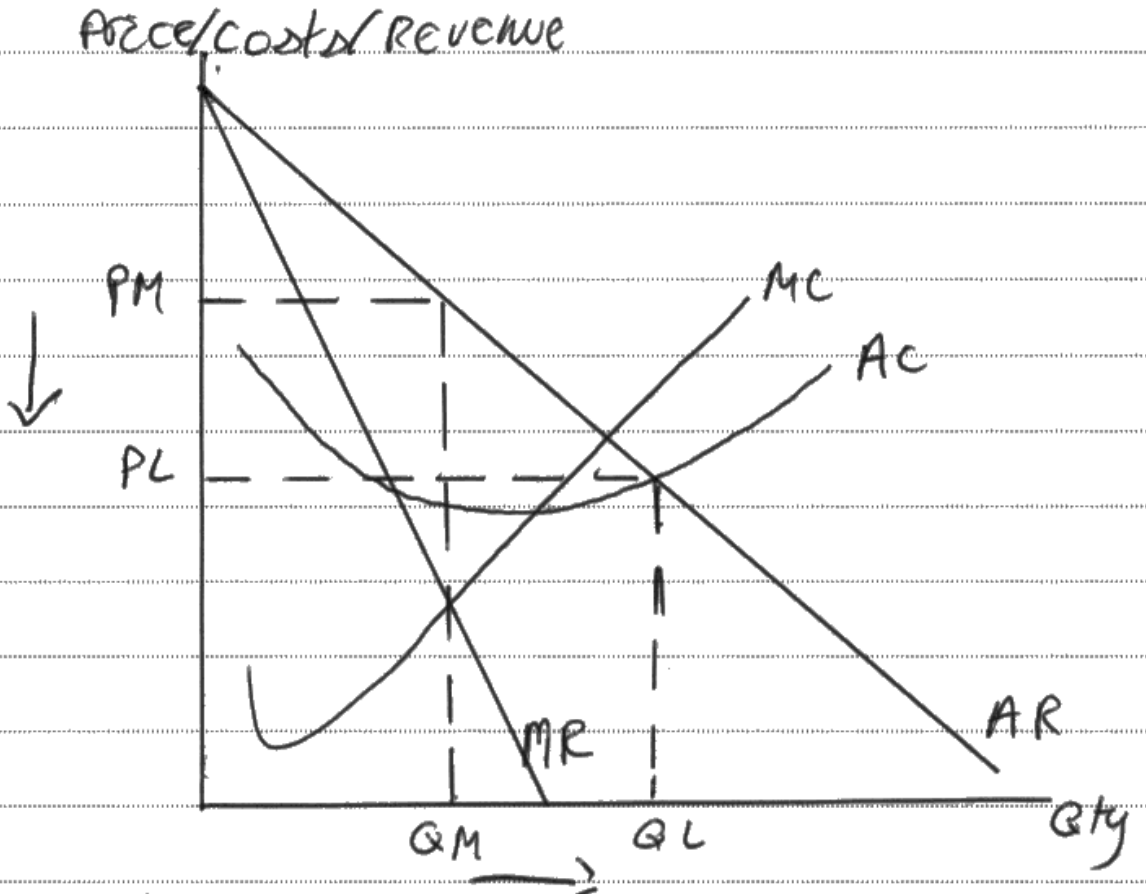
ResultsPlus
Examiner Tip

Accurate understanding of theory is crucial. This question is asking whether the level of contestability in the industry is high or low. It is not asking whether the industry is competitive but whether the industry behaves as if it is competitive. This is because of the threat of **potential** competition becoming **actual** competition. If new firms can easily enter and exit the industry to compete for any supernormal profits, the industry is contestable.

Contestability refers to the threat of new entrants into a market.

The supermarket industry in the UK can be described as not very contestable. This is because there are very high sunk costs. The ~~land on which to build the supermarket~~ advertising for example represents a large expenditure of supermarket firms since product loyalty is high. As product loyalty is high, to attract customers, firms like Lidl or Aldi must advertise. Furthermore, the supermarket industry is dominated by a few large firms, Tesco, Asda, Sainsbury's and Morissons. Therefore, it is very high for new firms to enter. This is because the leading firms benefit from very large economies of scale - a process by which as output increases, unit costs of production rise due to bargaining power for

example. Hence, if firms want to reduce the risk of new entrants, they may engage in limit pricing as shown below.



As shown above, a firm like Tesco may change their business objectives to discontinuise entry; from profit maximisation at MC = MC to limit pricing at AC = AR. At this point, the firm is breaking even and since they already benefit from larger economies of scale, their AC will be much lower than a new entrant's AC hence, new entrants will not enter

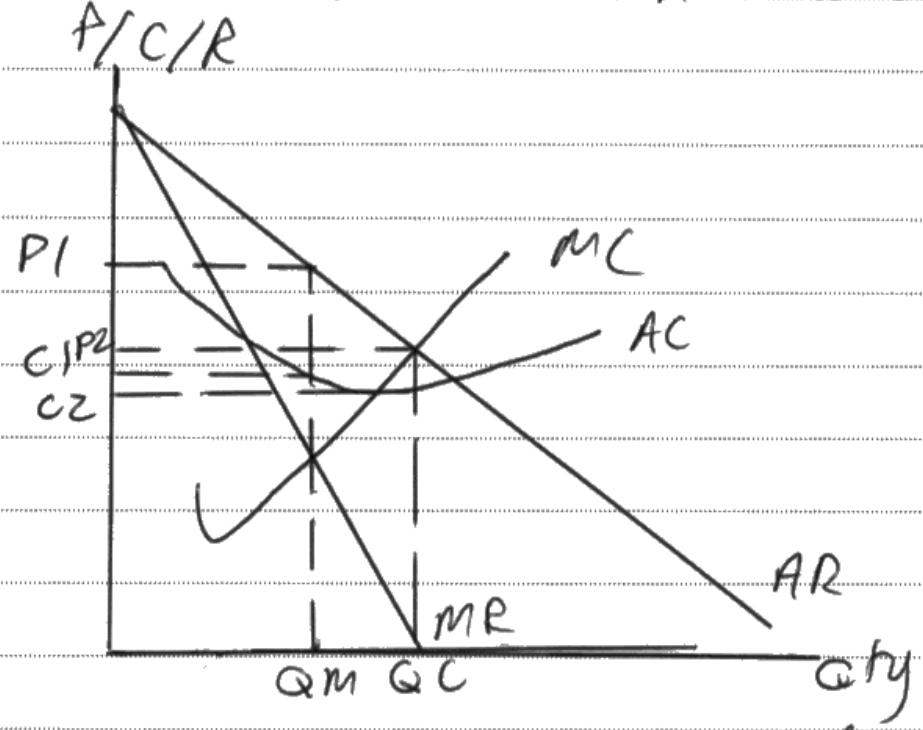
since they would have to also price at PL, a point at which they would be making a loss.
However, to evaluate this point, the CMA in the UK may not allow firms to engage in limit pricing and may impose a financial penalty for doing so. This would increase contestability within the market as the price would be set higher thus, allowing new entrants to make superhormal profits.

It could also be argued that the supermarket industry is not contestable due to product loyalty. Indeed consumers may be used to shopping at the Tesco's and may therefore have developped a habbit of shopping there. Due to benefits such as the Tesco clubcard for example, this habbit will be reinforced as regular shoppers will benefit from discounts in the form of club-card points. Shoppers will therefore not want to change supermarket

and hence contestability will be low as shoppers may be more used to Tesco products and may prefer the layout of Tesco stores. Therefore due to habitual behaviour, contestability will be low as it will take a long time for a new firm to gain market share. An example of this is Lidl. Lidl took a lot of time to gain customers and a large market share in France. This is because French customers were more used to shop at "Carefour" or "Auchan". Hence, Lidl did not gain a large ~~custom~~ customer share right from the start, indeed it took them very long to gain supernormal profits too.

However, regulators could make the supermarket industry more contestable through ~~regulation~~ de-regulation. Indeed, policies such as lower food standards would decrease the barriers to entry within the market. This would lead to increased competition which would greatly benefit customers. This would increase consumer surplus

as firms would price their products at a lower price meaning they may instead produce at the allocatively efficien level (MC = AR) as shown below.



As shown above, price would fall from P1 to P2 increasing consumer surplus and quantity would rise from Qm to Qc. This therefore would greatly benefit consumers. And firms too as they would still be making supernormal profits of P2, C2. They could reinvest this into R and D for example to, in the future reduce costs of production and lower the MC and AC curves as variable costs would fall. This would allow greater dynamic efficiency

as more supernormal profits would be made which could be used to either reduce price or reward shareholders through dividends.

Therefore, the supermarket industry is not contestable due to the high barriers to entry and great economies of scale firms benefit from. I believe the most important reason why it is not contestable is due to consumer loyalty which is high especially within supermarket companies.

ResultsPlus
Examiner Comments

This second response is a much better attempt to answer the question. There is a clear definition of what contestability is. The candidate then discusses sunk coats, limit pricing, and draws a clear diagram to explain how the theory works. There are plenty of good contextual examples which illustrate the theory. There is some discussion of intervention by the competition authorities to increase contestability. A real strength of the response is the way the candidate uses clear signposting to say why their point either increases or reduces contestability. This is certainly evident when the Tesco Clubcard is discussed in the context of brand loyalty and how this constitutes a significant barrier to entry which reduces contestability. Overall, this response achieved level 4 KAA, 15 marks, and level 2 evaluation, 5 marks, giving 20 in total.

Paper Summary

Based on the responses to this paper, candidates are offered the following advice:

- Practise key diagrams such as cost and revenue, externalities and subsidies. Carefully label these and clearly show the direction of any changes on the diagram. Shading should be clear. Clear diagrams enable knowledge, application and analysis marks, and can be referred to in evaluation to really explore the importance an argument.
- For application, try to picture yourself as an economist advising a particular firm or sector on the impact of a change or policy. Context is crucial because what may work in one industry may not apply to another.
- Your responses will score highly if they show clear evidence of development. Examiners are looking for a 'chain of reasoning'. Make one point per paragraph, apply it to the context of the question, and then explain it carefully, step-by-step. Aim for quality over quantity. Your task is to choose a strong argument then carefully explain to the examiner in terms of how and why it is important. When you evaluate the argument you can then question why the argument may not apply in this situation. Evaluation is about the scale or significance of the point you make.
- When the question asks for 'factors' or 'concerns' note that it is asking for more than one factor or concern. If you ignore this you will lose marks.
- Clear 'signposting' throughout your response makes it easy to follow. For example, 'the first concern may be ... this is because....'
- Be sure to answer the specific question set. A good tip is to link your point back to the question at the end of each paragraph you write.
- Make sure you use subject specific terms and concepts. These are all in the specification, and examiners write questions based on the specification. It tells you what you need to know. You won't be asked about concepts or diagrams that aren't on the specification.
- Equally, writing about theories or using diagrams that aren't on the specification doesn't necessarily add to the quality of your answer. The mark scheme that is used by the examiners is based on the specification. Try to stick to what is on the specification. You should be aiming to make the marking of your paper as straightforward as possible.
- Furthermore, make sure your writing is clear. If examiners cannot easily read what you have written, they may lose the thread of your argument. In some cases they cannot read it at all.
- Crucially, practise writing against the clock. This makes it easier to write your responses neatly, and in time.

Grade boundaries

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

https://qualifications.pearson.com/en/support/support-topics/results-certification/grade-boundaries.html

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