Write your name here

Surname	Other names

Centre Number | Candidate Number

Edexcel GCE

Economics

Advanced

Unit 3: Business Economics and Economic Efficiency

Monday 23 January 2012 – Afternoon
Time: 1 hour 30 minutes

Paper Reference
6EC03/01

You do not need any other materials.

Total Marks

Instructions

- Use **black** ink or ball-point pen.
- **Fill in the boxes** at the top of this page with your name, centre number and candidate number.
- Answer **all** the questions in Section A and **one** question from Section B.
- Answer the questions in the spaces provided – *there may be more space than you need.*

Information

- The total mark for this paper is 72.
- The marks for **each** question are shown in brackets – *use this as a guide as to how much time to spend on each question.*
- Questions labelled with an **asterisk** (*) are ones where the quality of your written communication will be assessed – *you should take particular care on these questions with your spelling, punctuation and grammar, as well as the clarity of expression.*
- Calculators may be used.

Advice

- Read each question carefully before you start to answer it.
- Keep an eye on the time.
- Check your answers if you have time at the end.

Turn over ▶

P40093A

1/1/1/1/1

P 4 0 0 9 3 A 0 1 3 2

PEARSON

SECTION A: Answer all the questions in this section.

You should spend 35 minutes on this section. Use the data to support your answers where relevant. You may annotate and include diagrams in your answers.

1 In August 2009 the Competition Commission published a Groceries Supply Code of Practice. Large supermarket chains were paying very low prices to some suppliers. Which type of market power does this suggest the large supermarket chains have?

(1)

A Monopsony

B Monopolistic competitive

C Perfectly competitive

D Natural monopoly

E Competitive monopoly

Answer ☐

Explanation

(3)

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(Total for Question 1 = 4 marks)

2 General Motors made a loss of $4.3billion in 2009. Under which one of the following conditions are firms such as this likely to keep operating?

(1)

A The market is highly contestable

B They are covering average variable costs in the short run

C Total revenue is less than total cost in the long run

D They are covering marginal costs in the short run

E There are low sunk costs in the industry

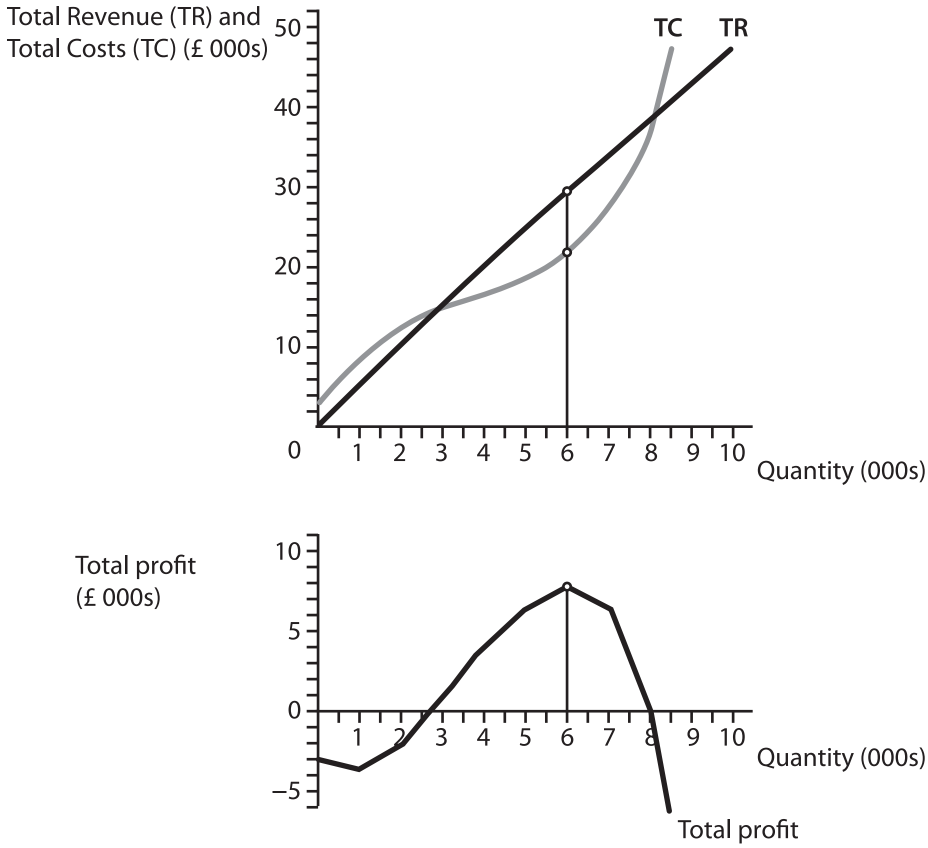
Answer

Explanation

(3)

(Total for Question 2 = 4 marks)

3



The diagrams show the costs, revenue and profit for a profit maximising firm.
What can be inferred from these diagrams?

(1)

A The firm operates in a perfectly competitive market in the short run

B The firm will produce at a quantity of 6,000 units in the long run

C There are barriers to entry and exit

D The firm will produce at **any** output between 2,650 and 8,000 units

E The firm is making a loss

Answer ☐

P 4 0 0 9 3 A 0 4 3 2

Explanation

(3)

(Total for Question 3 = 4 marks)

4 The following matrix shows the possible revenue outcomes of two firms tendering building services to the government. Assuming Hanna Ltd and Jax Ltd have agreed a pricing strategy that will give each a revenue of £1000, what change in pricing strategy would increase the revenue for Hanna Ltd?

(1)

		Hanna Ltd	
		High price	Low price
Jax Ltd	High price	£1000 £1000	£1200 £600
	Low price	£600 £1200	£800 £800

A Both firms set a high price

B Hanna Ltd sets a high price and Jax Ltd sets a low price

C Jax Ltd sets a high price and Hanna Ltd sets a low price

D Both firms set a low price

E The firms engage in tacit collusion

Answer ☐

Explanation

(3)

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(Total for Question 4 = 4 marks)

5 In November 2010, the Indian poultry and pharmaceutical company Venky's bought Blackburn Rovers Football Club in the UK for £23 million. One likely motive for this takeover was to benefit from

(1)

A technical economies of scale

B diversification

C price discrimination

D forward vertical integration

E increased market share

Answer ☐

Explanation

(3)

(Total for Question 5 = 4 marks)

6 A firm selling snack food at a music festival is operating in market conditions of monopolistic competition. It is likely to be

(1)

A allocatively efficient in the short run and productively efficient in the long run

B allocatively efficient in the long run and productively efficient in the long run

C both allocatively and productively efficient in the long run

D neither allocatively nor productively efficient in the long run

E both allocatively and productively efficient in the short run

Answer

Explanation

(3)

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(Total for Question 6 = 4 marks)

7 The price of cotton, a major cost component in the clothing sold by retailers Next, Primark and Debenhams, is predicted to rise significantly. What will be the effect on these firms, if other factors remain constant?

(1)

	Output	Profits
A	Rise	Rise
B	Constant	Constant
C	Fall	Fall
D	Constant	Fall
E	Fall	Constant

Answer

Explanation

(3)

(Total for Question 7 = 4 marks)

8 A large number of small bakeries in a competitive industry are taken over and combined to form a single monopoly supplier. Assuming **constant average costs**, what effect will this have on price and output?

(1)

	Price	Output
A	fall	fall
B	no change	no change
C	rise	rise
D	no change	fall
E	rise	fall

Answer ☐

Explanation

(3)

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(Total for Question 8 = 4 marks)

TOTAL FOR SECTION A = 32 MARKS

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Section B: Answer either Question 9 or Question 10.

If you answer Question 9 put a cross in this box ☒ .

Question 10 starts on page 22.

You should spend 55 minutes on this section.

9 The UK Banking Sector

Extract 1 RBS fined £28 million for sharing price data

Royal Bank of Scotland (RBS) was fined £28.6 million in March 2010 for breaking competition law in the first big case brought against a financial services company, and one of the largest against a company for anti-competitive behaviour. RBS admitted that staff involved in making loans to big law and accounting firms had illegally given pricing data to corresponding staff at Barclays. Barclays had used the information provided by RBS to determine the pricing on its own loans before it reported the lawbreaking to the authorities in 2008. RBS had provided Barclays with broad information about the loan market, as well as specific details of the proposed pricing structure for two new loan facilities. These disclosures took place at a number of social, client and industry events and through telephone conversations between October 2007 and March 2008.

The breach in competition laws occurred before RBS was bailed out by the government, and it is now 70% owned by taxpayers. RBS said yesterday that it was a "deeply regrettable and isolated case".

No action is to be taken against Barclays, as a reward for having acted as an informant within the industry, voluntarily disclosing its part in the affair to the competition authorities.

(Source: © The Financial Times Limited 2010, adapted from 'RBS fined £28 million for price sharing data', by Michael Peel and Sharlene Goff)

Extract 2 Fresh bonus fears as bank profits rise

The UK's five biggest banks – HSBC, Barclays, Lloyds Banking Group, Royal Bank of Scotland and Standard Chartered – have revealed that they made combined profits of £8.4bn in the first half of 2010. This performance is likely to be taken as proof that UK banks have recovered from the credit crisis and benefited from staffing reductions. However, there are concerns that these higher profits will lead to executives claiming greatly increased pay packages. The banks' share prices have jumped this year – RBS is up more than 70%, Lloyds is up nearly 37% – which could trigger the end-of-year bonuses to senior banking staff. Barclays is expected to disclose a bonus-to-salary ratio in line with the 38% paid last year – the highest of the UK banks.

Under pressure from the Bank of England and the Financial Services Authority, banks last year cut dividends and reduced bonuses as a proportion of revenue. The Chancellor said "we will not tolerate banks piling the pressure on the small to medium-sized business sector. The banks have an economic obligation to assist that sector. Every small and medium-sized company that I have visited in recent weeks has had some problem with their bank – either they have found it difficult to renew their overdraft or the bank demanded additional collateral, often someone's house. The danger is, particularly next year when there is a huge amount of refinancing required, that small and medium-sized businesses will suffer from a lack of access to short term loans."

(Source: © copyright Telegraph Media Group Limited, 31st July 2010)

Extract 3 Other views on bank bonuses

The Deputy Prime Minister, Nick Clegg, said last week that the Government will "not stand idly by" if bonuses are too high. This needs to be more than just words. Ministers need to prevent the payouts being made, or at the very least ensure that awards are made entirely in shares (which will have the effect of increasing the capital reserves of banks), rather than cash. And those banks that still insist on resisting ministerial pressure must face a further tax as punishment.

(Source: © *Independent*, www.independent.co.uk/opinion/leading-articles/leading-article-time-for-ministers-to-call-the-banks-bluff-2165552.html, 21st December 2010)

(a) With reference to Extract 1, what is meant by *anti-competitive behaviour* (Extract 1 line 3)?

(4)

(b) Using an appropriate cost and revenue diagram, assess **one** likely reason why banks' profits rose in the UK in 2010 (Extract 2 paragraph 1).

(8)

*(c) Assess the likely impact on economic efficiency in the UK banking industry of increased regulation of UK banks.

(12)

*(d) With reference to Extract 1, assess reasons for Barclays' changing behaviour. Refer to game theory in your answer.

(16)

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(16)

(Total for Question 9 = 40 marks)

If you answer Question 10 put a cross in this box ☒ .

10 The global yogurt market

Extract 1 Yoplait, a French yogurt firm, has plenty of potential buyers

Five years ago the French Government was concerned over rumours that Danone, the world's biggest maker of yogurts, would be bought out by the US giant, PepsiCo. The French prime minister put Danone on a list of companies to be kept under French ownership. Now, however, Yoplait – the world's second-biggest yogurt firm – is on the market. PAI Partners, a French private-equity company, is selling 50% of the firm. The rest is held by Sodiaal, France's biggest dairy co-operative. Once again, bidders are interested.

Demand for yogurt is booming across the world. According to a recent study, it is the fastest-growing sector in the dairy industry. The Chinese have been converted to yogurt in part by the addition of small plastic spoons to pots. Even the United States of America is considered an emerging market when it comes to yogurt. The average French person eats 30kg of yogurt per year compared with only 10kg for Americans.

Although Yoplait is lagging behind Danone in almost all countries, the two are equally placed in America where Yoplait has had a business arrangement with General Mills for 30 years to sell their yogurts. This has been a great success, but General Mills and Yoplait are currently in disagreement over terms for the renewal of their agreement. Ken Powell, the chief executive of General Mills, does not appear keen to take control of Yoplait, but this could change if Yoplait were to move to dissolve the relationship.

The most likely buyer is Lactalis, a French firm that could take over Yoplait in partnership with Nestlé. It put in a $1.76 billion bid for the whole company in November 2010. Other possible buyers include Unilever, a big Anglo-Dutch firm, and America's Kraft. A bid by PepsiCo cannot be ruled out. The maker of fizzy drinks and crisps wants to expand the healthier end of its range. Yoplait would be a perfect fit—as Danone would have been a few years ago.

(Source: adapted from *The Economist Newspaper* 20 November 2010)

Extract 2 Product launch of *Yoplait Greek* yogurt

How do you launch a new product in the $3.7 billion yogurt industry? That's a question that Yoplait recently tackled with the launch of *Yoplait Greek* in March 2010. Greek yogurt is yogurt that has been strained to remove the whey to make it thicker. The market for Greek-style yogurt already has several competitors including *Fage* and *Chobani*. However, *Yoplait Greek* managed to attract 90,000 customers to its website in its first month. This is more than three times the number of visitors to the next largest Greek-style yogurt website. See Figure 1.

Yoplait Greek used a combination of online display and search engine marketing to raise awareness of the product and attract consumers to its website. Display advertisements were placed on social networking sites such as *Yahoo* and *Facebook* to generate awareness. *Yoplait Greek* also had top sponsored search ranking on keywords "yogurt" and "Greek yogurt". The offer to download a coupon was featured prominently on every page on the site. Of the consumers who visited YoplaitGreek.com in March, 45% downloaded a coupon.

Figure 1
Number of visits to Greek-style Yogurt websites, January to March 2010

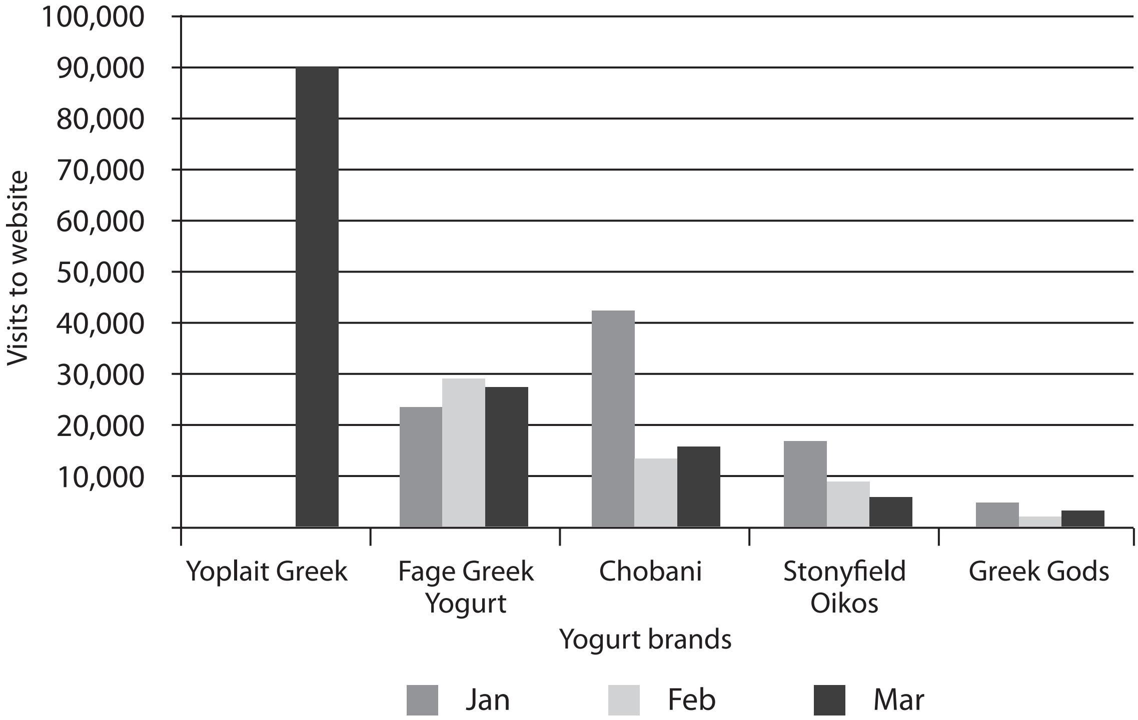
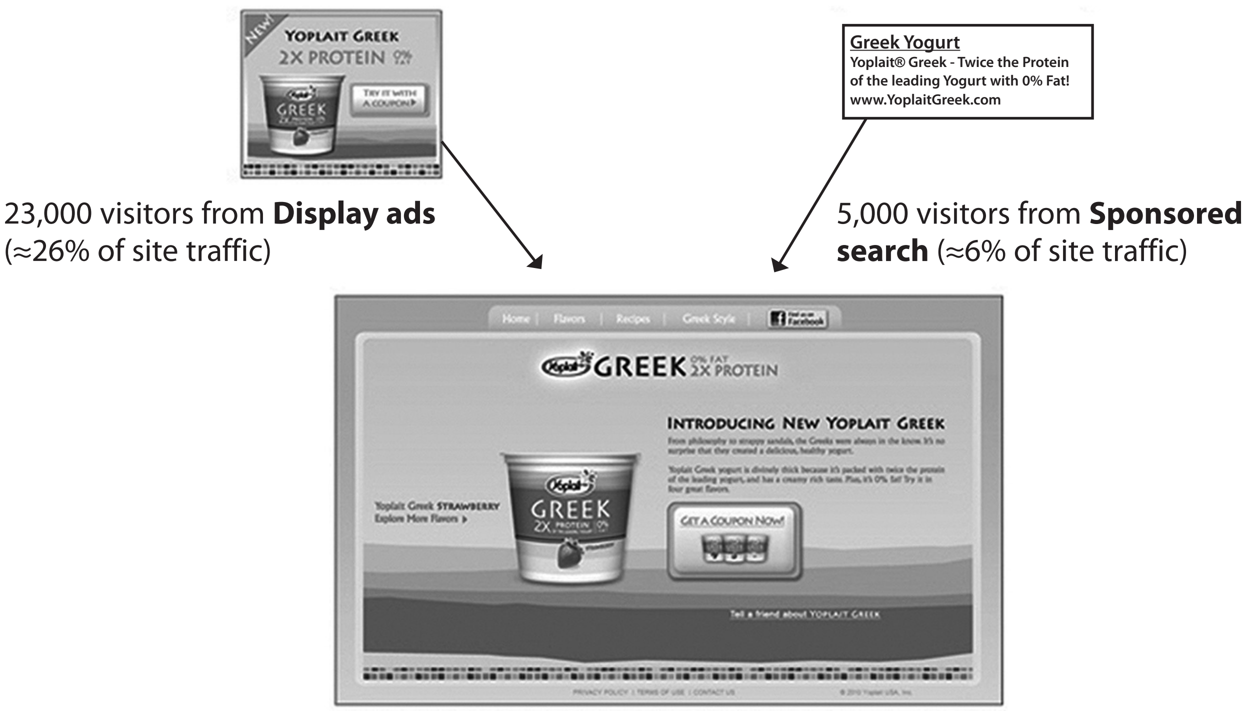


Figure 2
Website visitors to YoplaitGreek.com, March 2010



YoplaitGreek.com
90,000 visitors in March

(Source for Extract 2 & Figures 1 & 2: http://blog.compete.com/2010/05/03/using-the-online-channel-for-cpg-product-launch-yoplait-greek/)

(a) Using the information provided, explain the market structure in the supply of yogurt.

(4)

(b) Discuss **two** reasons why the French government may intervene to prevent the acquisition of Yoplait by an overseas firm.

(8)

*(c) Assume Yoplait is taken over by PepsiCo. Assess the possible benefits to PepsiCo **and** consumers of this acquisition.

(12)

*(d) With reference to Extract 2, discuss how the launch of the new product *Yoplait Greek* yogurt may influence the behaviour of rival firms.

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(16)

(Total for Question 10 = 40 marks)

TOTAL FOR SECTION B = 40 MARKS
TOTAL FOR PAPER = 72 MARKS