EZY ECONOMICS

Sample Papers – Set 1

AQA A Level – Paper 1 (Markets and Market Failure)

Question Paper

Time Permitted: 2 hours

Paper Instructions:

- In **Section A**, answer **EITHER** Context 1 **OR** Context 2.
- In **Section B**, answer **one** essay question.
- There are 80 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.

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SECTION A

Answer **EITHER Context 1 OR Context 2.**

EITHER

Context 1 **Total for this content: 40 marks.**

The UK Rail Industry

Study **Extracts A, B and C** and then answer **all** parts of Context 1 which follow.

Extract A: Average rail single ticket prices on selected routes in 1995 and 2013

Route	1995	2013
London to Manchester	£50	£154
London to Exeter	£37.50	£114.50
Swindon to London	£20	£58.50
Glasgow to London	£65	£169

Source: Rail Magazine (2015)

Extract B: In favour of privatisation of the UK Rail Industry

Until the mid-1990s the UK rail industry was publicly owned and operated by British Rail. This state-owned enterprise oversaw a period of significant change across the UK rail network, most notably the transformation from steam powered traction to electric traction.

In 1993, the Conservative Government passed the 'British Railways Act' and British Rail was eventually privatised in 1997. The ownership and control of the UK railway infrastructure was passed down to Network Rail, which maintains and operates the tracks, signalling and stations in the UK rail industry.

Network Rail supplies the rail infrastructure to a collection of privately-owned train operating companies (TOCs). These TOCs apply for franchises through the market and if successful provide train services to rail passengers on those selected routes.

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.

Over the next 30 years' passenger demand for rail will more than double putting further pressure on an industry that is already at capacity. Increased levels of rail investment is urgently required to absorb the increasing popularity of rail travel.

Source: News Reports, December 2016

Extract C: Has privatisation of the UK rail industry lessened competition?

Since the privatisation of the rail industry, Network Rail has acted as a natural monopoly in providing and supplying rail infrastructure to 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.

Frances O'Grady, Trade Union Congress general secretary, has stated that rail passengers are paying more and getting less in return: "Fares go up while trains remain overcrowded and rail companies cut guards."

Do UK rail passengers pay too much for rail journeys? Due to a lack of 'on-rail' competition, TOCs have increased their prices quickly on most routes. Average rail fares in the UK have risen by 24% since January 2010, outstripping the average weekly wage growth of 12% across the same period.

Alex Chisholm, Competition and Markets Authority (CMA) Chief Executive claims that increased 'on-rail' competition will create additional consumer benefits, including downward pressure on fares: "A more competitive environment will force companies to be more efficient which can mean lower fares, new routes and destinations, more innovations and flexible ticket pricing."

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.

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%.

Source: News Reports, December 2016

Q1

Using the data in **Extract A**, calculate, to 1 decimal place, the percentage change in the average price of a single ticket from London to Exeter from 1995 to 2013.

[2 marks]

Q2

Explain how the data in **Extract A** show how train operating companies have taken advantage of the lack of 'on-rail' competition in the UK rail industry.

[4 marks]

Q3

Extract B, (lines 15-17) explains that an increase in passenger demand will put further pressure on an industry already at capacity.

With the help of a diagram, explain how increased passenger demand in the UK rail industry could affect the rail fares paid by passengers.

[9 marks]

Q4

In **Extract C**, **(lines 12-16)** the Competition and Markets Authority argues that 'increased rail competition on selected routes will create additional consumer benefits'.

Using the data in the extracts and your own economic knowledge, assess the impact of introducing more competition on rail lines in the UK rail industry.

[25 marks]

Do **not** answer Context 2 if you have answered Context 1.

OR

Context 2 **Total for this content: 40 marks.**

World Oil Market

Study **Extracts D, E and F** and then answer **all** parts of Context 2 which follow.

Extract D: Oil Industry Data

	Year			
Variable	2013	2014	2015	2016
World Oil Demand (mb/d)	92.0	93.2	95.0	96.2
World Oil Supply (mb/d)	90.4	93.8	96.6	97.8
Oil Price ($ per barrel)	105.9	96.3	49.5	38.4

All figures stated represent the annual average for each variable

Source: IEA Oil Market Report (2016)

Extract E: Global Fall in Oil Prices

Since 1960, the global oil market has been under the influence of OPEC, an organisation that effectively acts as a cartel in the world oil market to stabilise: prices for consumers, profits for firms and revenues for governments.

Because OPEC produces over a third of the world's oil supply, it traditionally has used its market share to increase supply when prices are high and decrease supply when prices are low, maintaining price stability in the oil market. From 2010 to mid-2014, world oil prices remained stable at $110 a barrel.

Since then oil prices have dramatically fallen, and at the start of 2016 fell as low as $27 a barrel. The downward pressure on oil prices can be explained by two factors – global demand weakening and increased supply from the US and Russia.

A slowdown in the economy of the world's biggest importer of crude oil – China – has caused world demand for oil to slow by 0.6 mb/d as China's economy moves away from investment and export led growth towards consumption led growth.

The world supply of oil has also increased because of increased supply from non-OPEC countries. High oil prices in 2014 encouraged firms to increase their production of oil by investing to increase their future production capacity. This has resulted in the world supply of oil increasing to 97.8 mb/d in 2016.

The two factors combined has left a supply glut in the oil market and created pressure on oil prices to continue to fall.

Source: News Reports, December 2016

Extract F: OPEC Production Cut

Towards the end of 2016, OPEC announced their first production cut for 8 years in an attempt to revive oil prices. The production cut aims to reduce OPEC oil production by 1.2 million barrels a day, to bring balance and stability back to the oil market.

The OPEC president, Mohammed Bin Saleh Al-Sada, has stated "This agreement comes from a sense of responsibility from OPEC member countries for the general well-being and health of the world economy."

Industry experts anticipate that the production cut will signal an end to the ‘pump at will’ strategy that many OPEC countries have continued to adopt, in the hope that the prevalence of lower oil prices would force higher-cost US shale producers out of the market in the long-run. It is widely understood that OPEC’s strategy to force US shale producers out of business failed due to the long-term nature of the investments made by the US firms.

Spencer Welch, director at IHS energy, raised concerns about how effective OPEC’s production cut would ultimately be without commitment from non-OPEC members and stated that a production cut may encourage the US shale industry to expand their production levels further.

Source: News Reports, December 2016

Q5

Using the data in **Extract D**, calculate, to 1 decimal place, the percentage change in the average annual price of a barrel of oil from 2013 to 2016.

[2 marks]

Q6

Explain how the data in **Extract D** show how the OPEC cartel's market power in the oil market has decreased.

[4 marks]

Q7

Extract E, (lines 18-19) states that world oil supply has increased above oil demand creating a 'supply glut' in the market.

With the help of a diagram, explain how the increase in world oil supply has put pressure on world oil prices to fall.

[9 marks]

Q8

In **Extract F**, **(lines 12-15)** concerns were raised over how effective OPEC's production quota would be in correcting the disequilibrium in the world oil market.

Using the data and your own economic knowledge, evaluate how effective OPEC's production cut is likely to be at raising the worldwide market price of oil.

[25 marks]

SECTION B

Answer **ONE** essay from this section.

Each essay is worth 40 marks.

EITHER

Essay 1

‘Prices for the world’s top-selling medicines are typically higher in developed countries compared to developing countries.'

Q9

Explain why firms in the pharmaceutical industry can charge different prices for the same drug in different countries.

[15 marks]

Q10

Assess the view that price discrimination always leads to undesirable results for society.

[25 marks]

OR

Essay 2

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

Q11

Using economic theory, explain why pay differentials exist between such professions.

[15 marks]

Q12

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

[25 marks]

OR

Essay 3

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 an oil industry with a boost.

Q13

Explain how the development of the UK fracking industry has imposed negative production externalities upon society.

[15 marks]

Q14

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

[25 marks]