

A-Level Edexcel Economics: Oligopoly Past Paper Questions

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The following table shows global sales of PCs by company in 2015.

Company	Sales of PCs (million)
Lenovo	57 182
НР	53 534
Dell	39 049
Apple	20 794
Acer Group	19 680
Others	86 461
Total	276 700

(Source: IDC, reported in *The Times*, 14th January 2016)

(c) Calculate the five-firm concentration ratio. You are advised to show your working.

(2)



Firms tendering for a private finance scheme from the government verbally agree with each other to fix a higher price than if there were independent bids. This is an example of:	
	(1)
A tacit collusion	
B overt collusion	
C symmetric information	
D monopolistic competition	
E regulatory capture.	
Answer	
Explanation	(3)



The grid below shows the possible pricing strategies of two ice-cream companies Juju and APJ. Assuming that demand is price inelastic, which of the following strategies shown in the grid would maximise the revenue of the two firms?

(1)

		Juju's price	
		High	Low
APJ's price	High	Α	В
	Low	С	D

- A Both firms set a high price
- **B** APJ sets a high price and Juju a low price
- **C** Juju sets a high price and APJ a low price
- **D** Both firms set a low price
- **E** Both firms set a price to increase consumer surplus.

Answer		
Explanation		

(3)

5

10

15

20

25

30



Question 4

Extract 2 Kraft takes over Cadbury to become world's biggest confectioner

Kraft's offer to buy Cadbury was accepted by Cadbury's board on 19 January 2010. Kraft, the US food giant, will pay £11.7 billion for Cadbury in cash and shares, some 50% more than the firm's value before the bidding started in September.

Kraft's acquisition may be a good deal for both companies. Kraft has little presence in Britain's confectionery market, where Cadbury is strong, but it has thriving businesses in mainland Europe and Russia where Cadbury has made minimal progress. Cadbury is strong in India and various Commonwealth countries, and has a booming chewing-gum business, particularly in Europe and Latin America, an area where Kraft has little expertise. Between them they can make up lost ground in China, where Mars holds the upper hand. The deal is also set to yield cost savings of £414m a year for the combined firm, operating at a larger scale in emerging markets. This is a good deal for most Cadbury's workers. However, the fact that so much of the deal is financed by debt is a negative: borrowing that looks cheap today could double in price tomorrow. That would eat up the cost savings on marketing and administration already factored into the purchase price, and perhaps force undesirable cuts to operations. Cadbury is already efficient: under its current management it has reduced costs significantly, for example, by off-shoring more of its operations.

Three-quarters of mergers result in a fall in short run profits. In such a sensitive consumer sector, the risks of a culture clash and brand destruction are high. That is what happened to Terry's, a smaller York-based chocolate company bought by Kraft in 1993. Terry's has lost visibility in Britain since production was relocated to central Europe in 2005. The same problem could await Cadbury.

There are understandable fears that foreign owners will be more likely than domestic ones to axe British jobs or use British profits to pay off their global debts. But all successful big firms, British and foreign alike, respond to the demands and opportunities of the global marketplace these days, and, as Cadbury's current managers have shown, their behaviour is rarely determined by their nationality.

The management practices of multinational companies tend to be better than the average in any country they operate in. In theory, then, Kraft's takeover of a British firm should bring better management to Britain. One problem: Cadbury is itself a multinational, and in no need of lessons from Kraft.

Source: adapted from http://bit.ly/89Azni 'Cadbury goes American. Is this healthy for British manufacturing?' *The Economist* Jan 19th 2010 and http://bit.ly/aaFiRe Jan 21st 2010 'Manufacturing blues: Another one bites the dust' Jan 21st 2010

) Assess how the newly combined Kraft and Cadbury food company could increase its share of the chocolate market in competition with Mars. Refer to game theory in your answer.

(12)



Early in the morning on 19 September 2013, Microsoft revealed that the price of its new games console Xbox One would be £429 in the UK. Later that day, Sony announced that its new PlayStation 4 games console would be sold for £349 in the UK.

One possible reason why Sony chose to price its product significantly lower than Microsoft was because

		(1)
Α	it had first mover advantage	
В	it wanted to undercut Microsoft and take a large market share	
c	it wanted to benefit from relatively price-inelastic demand	
D	it was colluding with Microsoft	
E	it had higher sunk costs in developing the new games console	
An	swer	
Ex	planation	(3)



Supermarkets selling freshly baked bread are operating in an oligopoly. They tend to keep prices stable for a popular, frequently compared product, an 800 gram white loaf. One reason for this might be			
Α	supermarkets know that the pricing decisions of one supermarket will impact on those of other supermarkets		
В	supermarkets are independent and base their prices on costs alone		
c	there is heavy regulation in the industry to prevent tacit collusion		
D	supermarkets are unable to engage in non-price competition		
E	if prices were cut by one supermarket then the others would leave prices unchanged		
An	swer		
Exp	Explanation		

(3)

5

5

5



Question 7

Egg farming, egg distribution, food manufacturing and supermarkets

Extract 1 A letter from a chicken farmer

Our problems started four years ago when the big egg packaging and distribution firms merged, purchasing nearly 70% of the eggs produced. I lost £40 000 last year and I could see the profits of Noble Foods [the UK's biggest egg distributor] increasing. There was no competition anymore and prices paid to egg farmers stayed low, while everything else, like the cost of chicken feed, was going up. New EU regulations preventing the housing of hens in conventional 'battery' cages have meant installing new cages, costing over £14 per hen. Many egg farmers like me are unable to absorb the costs of buying the new cages and some egg farmers have left the industry. 750 000 hens have been slaughtered across the UK.

Extract 2 The egg distribution business - profile of Noble Foods Limited

Noble Foods, the UK's largest egg packaging and distribution business, operates 160 vehicles from seven sites, 365 days a year, employing over 150 full-time drivers in temperature controlled vehicles. Eggs are collected from over 325 individual farm producers located throughout the UK and transferred to a packing centre, where they are sorted and boxed for delivery to customers. Pre-tax profits at Noble Foods increased by £1.4 million in 2011.

(Source: © 2011 Noble Foods Ltd)

Extract 3 Increased costs of eggs for food manufacture

Eggs – both in liquid and powdered form – are used in a variety of food products from biscuits and cakes to pasta and mayonnaise. The reduced supply of eggs, caused by the new EU regulations, is damaging the profits of some food manufacturers. Several of them are closing down their production lines because they cannot afford the soaring cost of eggs from distribution firms. However, they cannot raise their prices because supermarkets refuse to pass on any increase to consumers.



Extract 4 British farmers forced to pay the cost of supermarket price wars

Farmers say they are being forced out of business by the unfair buying practices of supermarkets. Discounts such as "buy one get one free" are not a generous gift from the supermarket. There is public ignorance of how supermarkets buy produce and the system that allows them to offer lower prices while increasing their profits. Tesco's profits were above £3.5bn for the first time last year and Sainsbury's rose by nearly 13%. These results are achieved largely by getting suppliers to reduce their prices or not pass farmers' cost increases through to the supermarkets. Most sectors of British farming, from eggs to fruit, vegetables and pork, have had reduced prices paid for their produce in the past year, despite record increases in costs.

(Sources 1, 3 and 4: adapted from © The Guardian 2 July 2011, © The Observer and © Parliamentary copyright 2011)

Figure 1 Egg types in the EU

Types of eggs produced in EU	Minimum cage requirements per hen	Market share in UK, 2012 forecast
Hens in conventional cages, 'battery'	550cm ²	Banned January 2012 under new EU regulations
'Caged' hens in EU-compliant cages	750cm² and a minimum height of 45cm with nest area, perching space and a scratching area	49%
Barn eggs	1110cm² free to move in large indoor area	4%
Free range eggs	As barn, with daytime access to open air pen, 4m ²	44%
Organic free range eggs	As free range, plus organic food (no artificial growth enhancers)	3%

Figure 2 UK egg market information 2011

Egg production	9 691 million eggs	
Egg consumption	11 512 million eggs (32 million per day)	
Consumers of eggs in the UK		
Retail (supermarkets etc.)		47%
Food Manufacturers		25%
Foodservice (hotels, restaurant	s)	28%



(d) Assess reasons why supermarkets are not increasing the retail price of eggs to cover the increased production costs of egg farmers. Use game theory to support your answer.

(16)



In July 2016 Apple's share of the UK market for smartphones was 38%.

Evaluate whether such a high market share for one company is in the consumer interest. Use appropriate diagrammatic analysis in your answer.

(Total for Question 8 = 25 marks)

