PEARSON EDEXCEL A-LEVEL ECONOMICS B · 9EB0

ECONOMICS



EXAM QUESTION PACK

4.2 MARKET POWER AND MARKET FAILURE

SCORE	PERCENTAGE
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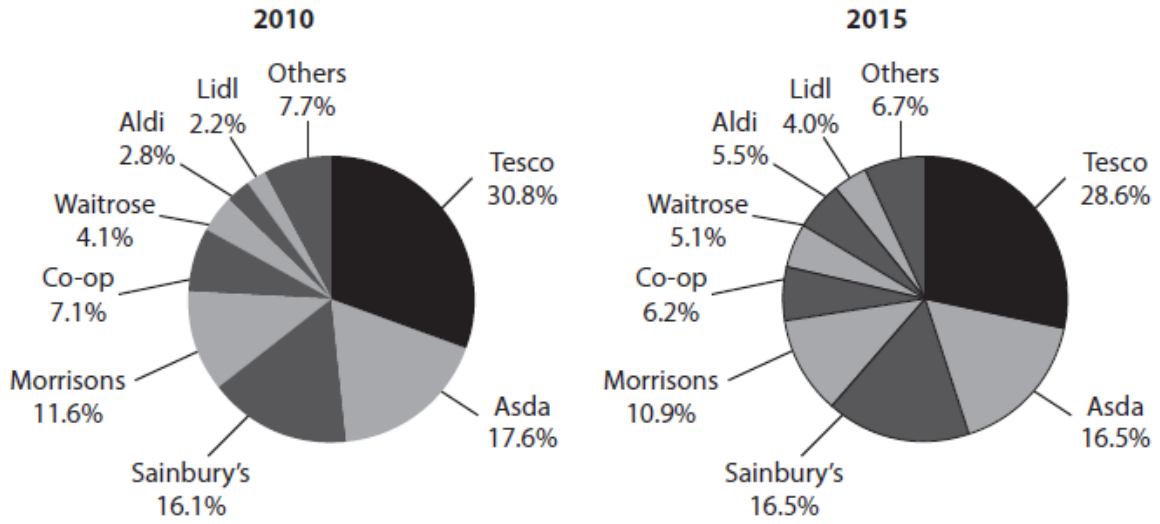
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Questions

Q1.

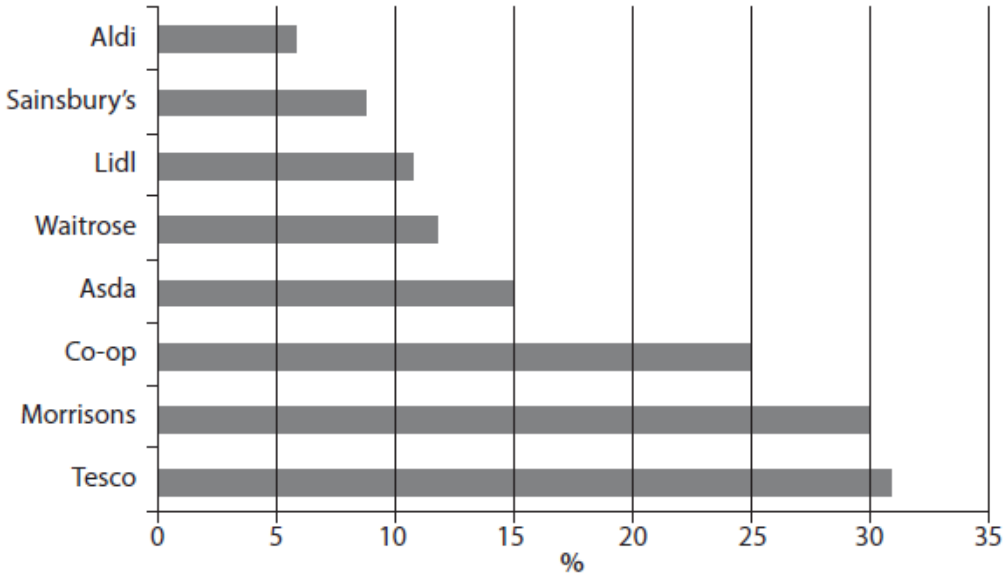
Supermarket price war, food waste and possible mergers

Figure 1: Market shares by total revenue in the UK supermarket sector, 2010 and 2015



(Source: Kantar worldpanel, http://www.kantarworldpanel.com/en/grocery-market-share/great-britain/snapshot/11.10.15/)

Figure 2: Proportion of food suppliers reporting that the following supermarkets fail to meet the Groceries Code of Conduct, 2015.



(Source: YouGov poll of more than 1100 food suppliers to supermarkets. Reported in The Times, 23 June 2015)

Extract A

Supermarket price war puts pressure on their food suppliers

The number of food suppliers (to supermarkets) struggling to remain in business has increased by more than 50% over the past year as supermarkets engage in an intense price war. It has never been tougher for the UK's food suppliers according to a study by accountants Begbies Traynor. It blames aggressive price-cutting by the supermarkets and delays in payments to food suppliers as the main causes of the difficulties. Further problems include food suppliers being forced to pay excessive amounts for packaging specified by supermarkets and funding in-store promotions. Almost 90% of struggling food suppliers are small and medium-sized businesses.

The price war has contributed to food prices paid by consumers falling by 1.7% over the past two years.

The market shares of the big four supermarkets – Tesco, Asda, Sainsbury's and Morrisons – are under pressure as shopping habits change. Many consumers are switching from one main weekly shop to shopping more frequently at local discount stores such as Aldi and Lidl or purchasing goods online from other grocery retailers.

The big four supermarkets have responded by putting more pressure on their suppliers despite an investigation by the Groceries Code Adjudicator (GCA). The GCA has the power to fine supermarkets up to 1% of their annual sales revenue if they break the Groceries Code of Conduct. A YouGov study found considerable differences between the supermarkets in meeting the Code with Aldi performing well but Tesco badly. Despite the Groceries Code, many food suppliers are reluctant to complain for fear of losing contracts with the supermarkets.

(Source: adapted from 'Supermarket price war takes toll on UK food suppliers'. Rupert Jones, The Guardian, 20th July 2015)

Extract B

Food waste in the supply chain

A report from the British Retail Consortium reveals that supermarkets are directly responsible for around 0.2 million tonnes of food waste every year. This is due to the expiry of use-by-dates and poor handling of stock.

However, 4.1 million tonnes of food waste occurs annually in the food supply chain before it even reaches the supermarkets, indicating the existence of information gaps. The supermarkets are cooperating with food suppliers and farmers to try to reduce this waste. This involves improving forecasts for supply and demand of food and increasing the reliability of transportation and storage.

Consumers, the final stage of the supply chain, waste a further 7 million tonnes of food each year. This suggests irrational behaviour. Supermarkets are also working with consumers to reduce the waste by providing advice on how to store and use leftover food. The development of packaging designs to keep food fresher for longer is one of the innovations under way to reduce waste.

(Source: adapted from 'Supermarkets tally up food waste bill'. Will Nicholls, in Businessgreen, 19th January 2015. http://www.businessgreen.com/bg/news/2390792/supermarkets-tally-up-food-waste-bill)

Extract C

Proposed merger activity in the supermarket sector

Analysts at Société Générale, an investment bank, have recommended a merger between Sainsbury's and Morrisons. They claim it would lead to increased economies of scale and market power for the combined business. Such a merger between the third and fourth largest supermarkets in Britain would have been unrealistic a few years ago due to concerns of its impact in reducing competition. However, the chances of getting permission from the Competition and Markets Authority have increased following the growth of Aldi and Lidl. Giant mergers have been approved in other sectors such as Lloyds-HBOS (banking) and British Telecom-EE (telecommunications).

The suggested merger would have its challenges. There is considerable overlap between the locations of the stores and the enlarged company would require the rationalisation and co-ordination of hundreds of thousands of employees. A new expensive IT system is likely to be required and the underlying difficult market trends would remain in the food retailing industry.

(Source: adapted from 'Tesco-bury and AS-Morrisons. Could Britain's supermarkets be about to merge?' Graham Ruddick, in The Telegraph, 16th December, 2015. http://www.telegraph.co.uk/finance/newsbysector/retailandconsumer/11699724/Tesco-burys-and-AS-Morrisons.-Could-Britains-supermarkets-be-about-to-merge.html)

(a) With reference to Figure 1 and Extract A, explain **one** likely reason for the change in the four-firm concentration ratio of the supermarket sector between 2010 and 2015.

(5)

(b) With reference to Figure 2 and Extract A, discuss the possible impact of supermarket monopsony power on both food suppliers and consumers.

(12)

(c) Examine measures the government might use to restrict the monopsony power of supermarkets.

(8)

(d) Assess the extent to which 'information gaps' (Extract B, lines 5 and 6) and 'irrational behaviour' (Extract B, line 11) are the main causes of food waste in the UK.

(10)

(e) Discuss the likely problems for Sainsbury's and Morrisons if the suggested merger between them goes ahead. Refer to Figure 1, Extract C and your own knowledge in your answer.

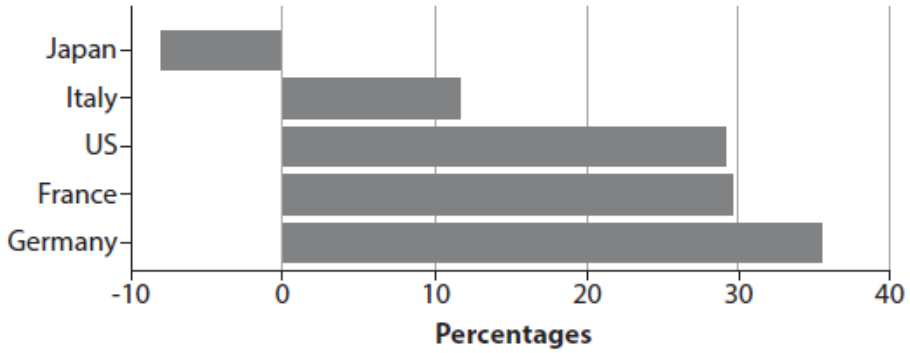
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Q2.

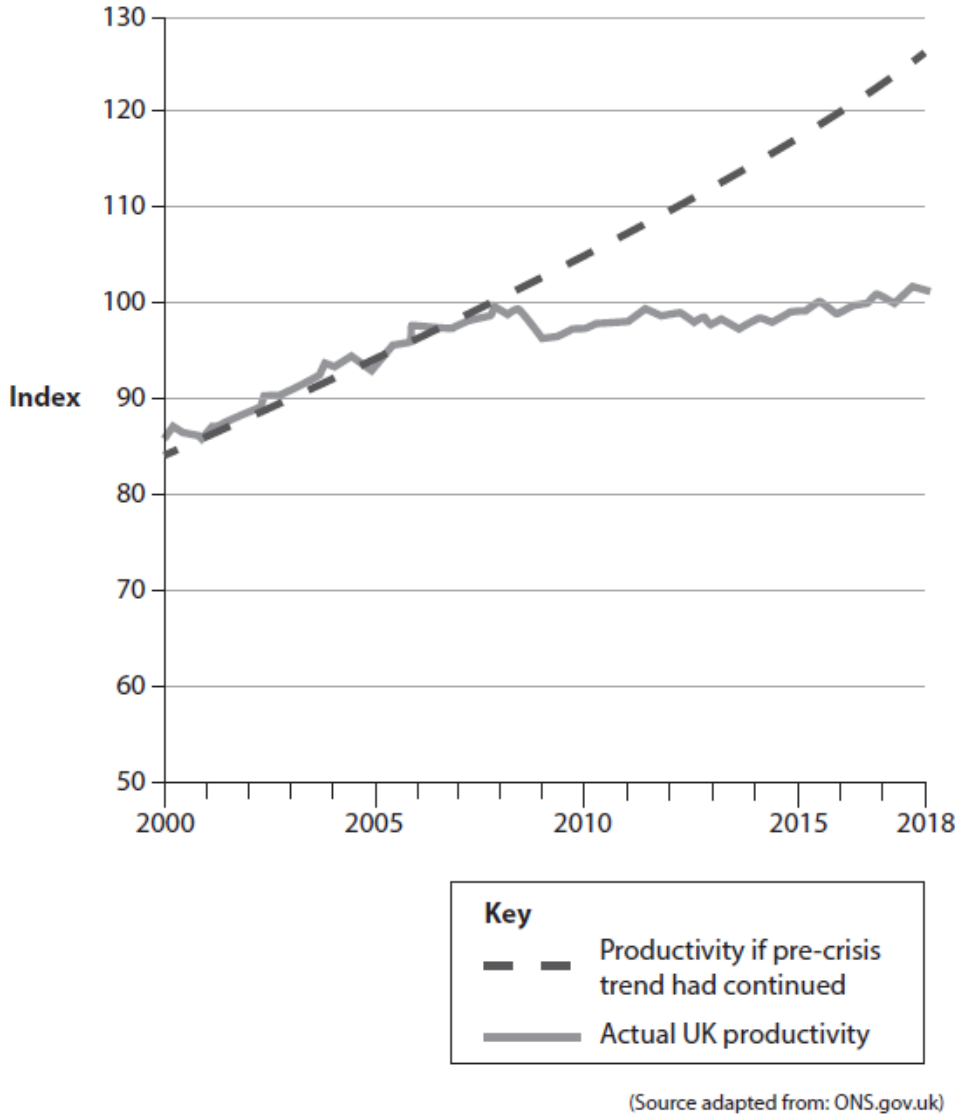
The UK economy

Figure 3: GDP per hour worked, nominal values at PPPs, percentage above or below UK level, 2018



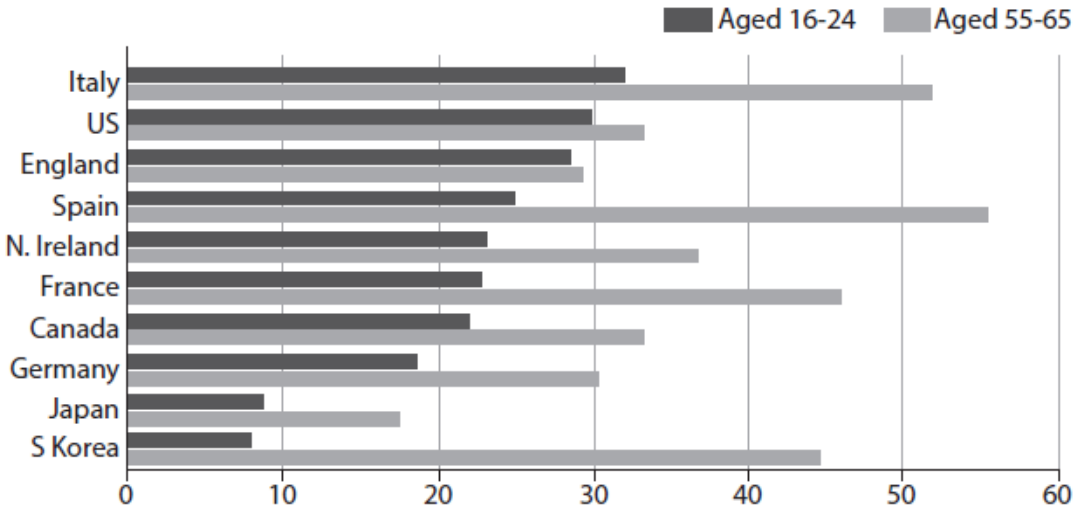
(Source adapted from: ONS.gov.uk)

Figure 4: UK index of output per hour worked, base year 2016 = 100



(Source adapted from: ONS.gov.uk)

Figure 5: Proportion of adults with low literacy and/or numeracy skills, by age, selected countries



(Source adapted from: OECD.org)

(Figures 3, 4 and 5 Source: FT.com 2016 data published https://www.ft.com/content/6ada0002-9a57-11e8-9702-5946bae86e6d 2018)

Extract D

The end of the High Street?

Homebase, the UK's second-largest do-it-yourself (DIY) retailer, made £20–40 million a year profit up to 2016. The Australian conglomerate Wesfarmers bought Homebase for £340 million in 2016, and began to rebrand 24 stores under its own name. It scaled back on curtain, cushion and other homeware sales in favour of power tools and building materials. In 2018 Wesfarmers sold the DIY chain for £1, in the face of "extremely challenging" market conditions and excess store space. The chain was bought by restructuring specialist Hilco, which had also rescued the music chain HMV in 2013, and the stores have gone back to using the Homebase name. Over 70% of Homebase stores are currently losing money and the new owner wants to exit loss-making stores and agree to rent reductions, as sales fell 10% in 2018. Homebase has gone back to popular products and brands dropped by its previous owner Wesfarmers.

The closures will add to the mounting job losses on Britain's high streets. About 25 000 jobs have gone in the first seven months of 2018, according to analysis by an economics thinktank. A further 8 300 jobs are under threat at suppliers, with the multiplier effect meaning that GDP is £1.5 billion less than projected.

Several Marks & Spencer clothing stores closed their doors for the last time as the high-street chain pushes ahead with a transformation plan. It plans to close 100 stores by 2022. Toys R Us, Poundworld and Maplin have shut down completely, while New Look, Mothercare and Carpetright have plans to close hundreds of stores as losses rise sharply. Increasing rents and higher business rates have occurred at the same time as falling consumer confidence. Meanwhile, House of Fraser employees and pensioners are nervously awaiting more details about their future. The £90 million rescue deal by Sports Direct, the sportswear chain controlled by Mike Ashley, will protect 16 000 jobs for the time being.

(Source adapted from: https://www.ft.com/content/00d0bb9e-a6ee-11e8-8ecf-a7ae1beff35b 24 August 2018 and https://www.theguardian.com/business/2018/aug/13/homebase-close-80-stores-high-street-job-losses-mount Patrick Collinson 13 Aug 2018)

(a) With specific reference to Figure 3, explain why productivity is measured by 'GDP per hour worked, nominal values at PPPs'.

(5)

(b) Apart from literacy and numeracy skills in young workers, examine **one** reason for the trend in productivity in the UK, over the period shown in Figure 4.

(8)

(c) Discuss factors that are causing many high street retailers in the UK to close some branches or shut down completely.

Use a cost and revenue diagram to support your answer.

(12)

EITHER

(d) Evaluate possible microeconomic and macroeconomic policies which could be used to improve UK competitiveness.

(25)

OR

(e) Evaluate the microeconomic and macroeconomic effects of a decline in the literacy and numeracy skills of a country's young workers.

(25)

(Total for question = 50 marks)

Q3.

(a) With reference to Figure 5 and Extract C, explain **one** likely reason for the fall in the exchange rate of the Turkish lira.

(5)

(b) Discuss the costs to the Argentine economy of an inflation rate "estimated by some economists to be over 25%". (Extract D, line 9)

(12)

(c) With reference to Extract E, examine the impact of restrictions on beef exports on how Argentine farmers decide to use their land.

(8)

EITHER

(d) With reference to the information provided and your own knowledge, evaluate the likely microeconomic and macroeconomic effects of the imposition of 'price controls' (Extract E, line 8) in Argentina.

(25)

OR

(e) With reference to the information provided and your own knowledge, evaluate the likely microeconomic and macroeconomic effects of the 23% devaluation of the Argentine peso.

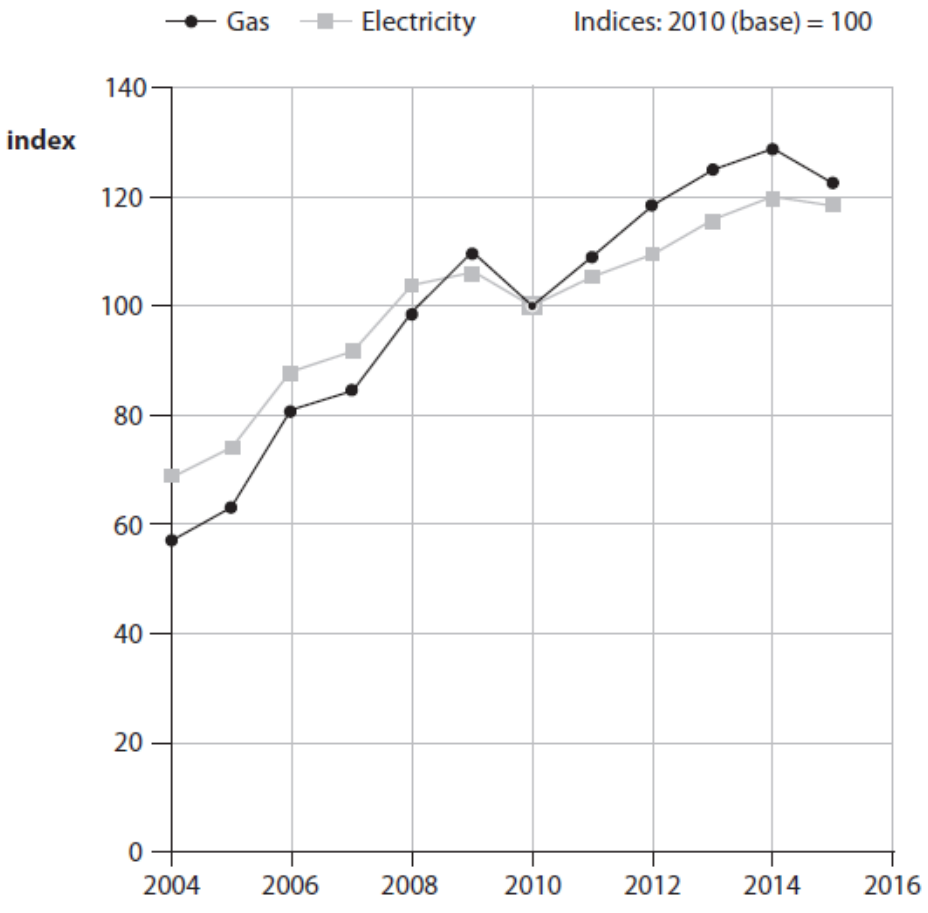
(25)

(Total for question = 50 marks)

Q4.

The UK energy market

Figure 1: UK retail electricity and gas real price indices, 2004–2015



(Source: https://assets.publishing.service.gov.uk/media/5773de34e5274a0da3000113/final-report-energy-market-investigation.pdf)

Figure 2: UK retail electricity and gas supply: market share by company, 2016

Company	Electricity %	Gas %
British Gas	23	36
EON	16	13
SSE	16	13
EDF	12	8
Scottish Power	11	9
RWE (nPower)	10	9
Other companies	12	12
Total	**100**	**100**

(Sources: https://www.ofgem.gov.uk/chart/electricity-supply-market-shares-company-domestic-gb and https://www.ofgem.gov.uk/data-portal/retail-market-indicators)

Extract A

Competition and Markets Authority (CMA) report into the UK energy market

An investigation into the UK energy market by the CMA concluded that customers have been paying £1.4 billion a year more than they would in a fully competitive market. It found that 70% of domestic customers of the six largest energy firms were on an expensive standard rate. These customers could each save over £300 a year by switching to a cheaper deal but appear reluctant to do so.

However, the CMA investigation found no evidence of anti-competitive practices by firms. There has even been an increase in new entrant energy suppliers over recent years and their combined market share has reached 12% in both gas and electricity supply.

To protect consumers, the CMA has introduced various measures to open up and increase competition in the UK energy market. These include:

- the creation of a database designed to help consumers switch energy suppliers – rival suppliers can directly contact these customers
- the conversion of all homes to smart energy meters making it easier for customers to measure energy consumption and switch supplier
- new rules to protect the four million vulnerable customers using prepaid meters – this includes a temporary price cap until smart meters have been installed.

(Source: adapted from 'Competition and Markets Authority Final report into Energy Market Investigation' https://www.gov.uk/government/news/cma-publishes-final-energy-report-in-full)

Extract B

Proposals to regulate profits in the UK energy market

Currently energy retail companies make an average profit of 7% of total revenue. The Chairman of the Competition and Markets Authority (CMA) suggested that these profits are as much as five times higher than they should be, given the companies' limited role in marketing, metering and billing customers. He recommended a profit cap of 1.25% of total revenue.

However, Scottish Power criticised proposals for regulating profits saying that it would reduce investment in the energy industry and undermine long-term energy provision. The firm claimed that such a low rate of return is below the profit margin made by supermarkets.

All six large energy firms are vertically integrated – producing as well as distributing gas and electricity. This can provide efficiency benefits but also harm competition.

(Source: adapted from 'Profit cap doesn't fit with new investment, energy boss warns', by Robin Pagnamenta, *The Times*, 19th September 2016)

Extract C

Skills shortages in the UK energy sector

The energy sector is facing a skills shortage of engineers and technicians. Some 29% of employers in the gas and electricity industries report unfilled job vacancies compared with an average of 18% across all industries.

A lack of information and advice on career prospects for young people is partly to blame - many graduates have a negative image of the work involved. There is also a lack of students taking science, technology, engineering and maths-based subjects at school and university. Less than one-fifth of the energy sector's workforce are women.

The energy sector is characterised by an ageing workforce - data from the UK Labour Force Survey reveal that around two-thirds of workers are aged over 50. These cannot easily be replaced as a long time period is required for training and developing workers' skills in a highly regulated industry.

Urgent action is required by businesses and the government to reduce labour immobility to benefit the energy sector. This action could include policies to increase investment in training programmes, recruit skilled workers from overseas, change the industry image and deal with its ageing workforce.

(Source: adapted from 'Sector insights: skills and performance challenges in the energy sector', by the UK Commission for Employment and Skills, March 2015; https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/416998/15.03.25._Energy_SLMI_-_evidence_report.pdf)

(a) With reference to Figure 1, explain **one** likely reason for the overall trend in the real price of gas and electricity.

(5)

(b) With reference to Extract A, discuss the likely effectiveness of 'measures to open up and increase competition' in the UK energy market.

(12)

(c) With reference to Extract B, assess how the regulation of energy suppliers' profits is likely to affect consumers **and** suppliers in the energy market.

(10)

The price elasticity of demand for electricity in the UK is estimated to be –0.35 in the short run and –0.85 in the long run.

(d) With reference to Extract A and your own knowledge, examine **two** possible reasons for the

change in price elasticity of demand for electricity over time.

(8)

(e) With reference to Extract C and your own knowledge, discuss policies businesses **and** government might implement to reduce labour immobility to benefit the energy sector.

(15)

(Total for question = 50 marks)

Q5.

Read extracts A and B before answering this question.

Hand car wash (HCW) firms in the UK

Extract A

What is the true human cost of your £5 hand car wash (HCW)?

The UK's hand car washes (HCWs) are extremely price competitive, but they have also been linked to modern slavery. Are they ever fair for workers?

There is little agreement about how many HCWs there are in the UK. Estimates range from 10 000 to 20 000. This lack of accurate information about the industry makes government regulation very difficult. Automated car washes, with their fierce rotating bristles, used to be the first option for drivers in a hurry. Now there is more choice. While the economy slows and incomes fail to keep up with inflation, demand for HCWs has grown. Many people see paying £5 for a car washed by someone else, rather than cleaning it at home, as a small expense which yields a high utility. But what is the true cost of a £5 car wash – and what should we be paying?

The growth of HCWs is partly the result of changes in the structure of industry in the UK. Many petrol stations have closed as drivers fill up at supermarkets. Garages and their forecourts have closed as cars become more reliable and locked into service agreements. The available sites for HCWs have therefore increased significantly and rents have fallen.

HCW entrepreneurs have identified available land and have benefitted from changes in the labour market, partly as a result of EU migration. UK drivers are now able to obtain cheap and effective hand car washing. For many migrants, car washes are a first job. "They accept car washing for a short period while they improve their language skills and move into other industries," says Ian Clark, a professor of work and employment at Nottingham Business School. "But there are also car-wash workers without networks who are in a dead end, working there for long periods."

Many drivers are only interested in getting the cheapest wash. If the price is very low, it probably means that workers are receiving less than the minimum wage and working in poor conditions. Crude calculations illustrate the problem. A £5 HCW employing five workers for 10 hours a day would need to wash 79 cars a day to just cover the wage costs. This assumes the workers are paid the minimum wage. This is one car every seven and a half minutes. Even if the profit can be higher on valet services, the price of which can be as little as £12 for a full inside-and-out clean, it's hard to see how a car wash price as low as £5 pays a living wage. This ignores all other costs which HCWs incur such as business rates and rent.

Evidence from car-wash workers is limited but Clark and others have been able to build a picture of some of the tougher conditions on drenched forecourts. "Like nail bars and small garment manufacturers, car washes are what we call 'hard-to-reach places,'" Clark explains. As part of the research, Clark and his team spoke to workers from 45 HCWs in the Midlands.

Clark and his team met and observed workers who lacked waterproof boots or trousers, or hi-vis jackets and gloves. "They're spraying around hydrochloric acid solution for alloy wheels, breathing in the vapour and fumes," Clark says. Some workers were paid a little over half the minimum wage.

(Source adapted from: https://www.theguardian.com/world/2018/jul/16/true-human-cost-5-pound-hand-car-wash-modern-slavery)

Extract B

Government intervention in the HCW industry

There are three main areas of government intervention that might impact on labour intensive firms such as HCWs:

First, there is the planning issue which focuses on the impact on the environment, for example, the disposal and recycling of waste water and chemicals. There could be planning regulations to prevent the use of tarmac rather than concrete on forecourts. Tarmac allows waste water and chemicals to seep into the sub soil. It could also be a requirement to have a sludge trap to stop the waste entering waterways.

Second, there is the health and safety issue for workers. Prolonged exposure to chemicals and lack of protective clothing puts the health of workers at risk. Performance targets could involve minimum levels of protective clothing and rest breaks for the workers.

Third, there is the issue of tax. The informal nature of the business type makes tax evasion easier.

Not all UK HCWs violate regulations. There are legitimate, regulated HCW firms as well as examples of good practice by independent outlets. One national supermarket, Tesco, has banned all independent hand car washes from its car parks. It is now in a partnership agreement with national car wash operator Waves. It uses a WashMark certificate of quality and compliance which was introduced by the industry to improve working conditions. Other major supermarkets are considering similar changes. One adviser believes £9 is a reasonable minimum price for a basic wash. Some pressure groups have developed a mobile phone app where evidence of unreasonable conditions can be reported by drivers.

Involving drivers in the issue, and making them demand fairer car washes, creates an incentive for good businesses to improve practices and come forward to get a WashMark certificate.

(Source adapted from: https://www.parliament.uk/documents/commons-committees/environmental-audit/Hand-Car-Wash-evidence.pdf research into HCWs by Professor Ian Clark, Nottingham Business School May 2018)

(a) Using the information provided, explain the market structure that best describes the hand car wash (HCW) industry in the UK.

(5)

(b) Examine **two** reasons why the demand for HCWs increases during a period when consumer 'incomes fail to keep up with inflation' (Extract A line 8).

(8)

(c) Discuss the likely effects of changes in the level of migration on firms such as HCWs in the UK. Use a labour market diagram and the information provided to support your answer.

(12)

EITHER

(d) Evaluate the microeconomic and macroeconomic factors which determine the number of firms in an industry. Refer to HCWs or another industry of your choice.

(25)

OR

(e) Evaluate the microeconomic and macroeconomic effects of increased government intervention in an industry. Refer to HCWs or another industry of your choice.

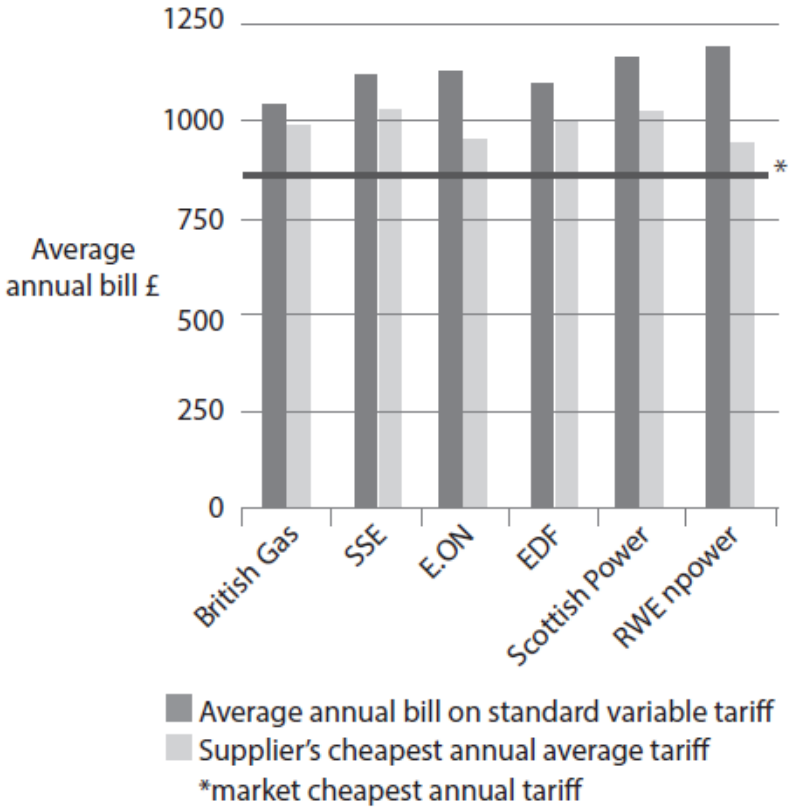
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(Total for question = 50 marks)

Q6.

Energy and telecommunication markets in the UK

Figure 1: Average annual household bill from the Big Six UK energy suppliers, 2017



(Source: https://www.lovemoney.com/news/67298/standard-variable-tariff-compared-cheapest-deal-provider-savings)

Extract A

Energy price cap to fix 'broken' market in UK

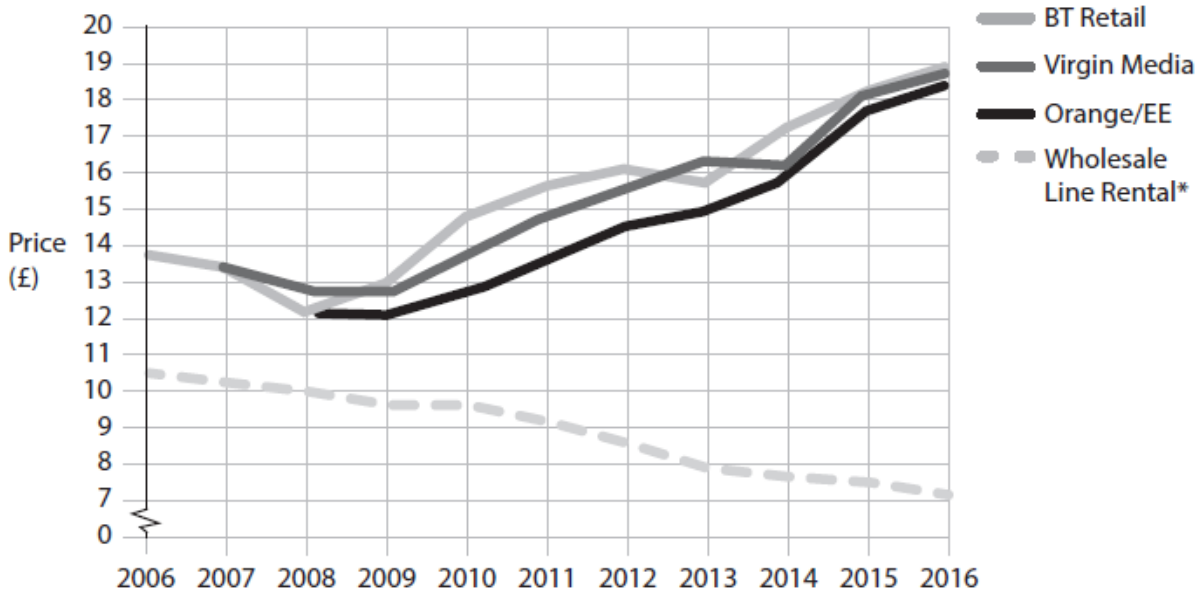
The Prime Minister recently said that the regulator Ofgem (Office of Gas and Electricity Markets) should limit electricity and gas suppliers' most expensive tariffs.

Under the planned new legislation, the energy bills of 11 million households will be capped for as long as five years. The government claimed this cap could save households up to £100 a year. This legislation would force Ofgem to change the licence conditions for energy suppliers so that they are required to cap electricity and gas prices. The measure will apply to anyone on a standard variable tariff, the expensive plans that customers are moved to when cheaper, fixed-price deals end. Ofgem will need to consult energy companies on how the cap is calculated, the government said. The Prime Minister repeated her claim that she had to act because the 'market is broken', a charge the big energy companies reject. "I have been clear that our broken energy market has to change – it has to offer fairer prices for millions of loyal customers who have been paying hundreds of pounds too much," she said.

However, Michael Lewis, chief executive of E.ON said "the government must guard against any unintended consequences that undermine customer service and push up prices as a whole. A price cap will not be good for customers. It will reduce competition and innovation". Smaller suppliers such as First Utility said the Big Six had only themselves to blame for the cap, because they had kept millions of people on standard variable tariffs.

(Source: adapted from 'UK puts energy efficiency at heart of climate change strategy', Adam Vaughan, Copyright Guardian News & Media Ltd 2017 https://www.theguardian.com/money/2017/oct/12/may-energy-price-cap-ofgem-electricity-gas-tariffs)

Figure 2: The monthly rental cost of a telephone landline



*Wholesale line rental – the rental price BT Openreach charges telephone service providers

(Source: https://www.ofcom.org.uk/about-ofcom/latest/features-and-news/landline-prices-review)

Extract B

BT profit rises

BT Group, which includes BT Openreach and BT Retail, reported a rise in profit as revenue increased following the integration of the consumer mobile business, EE. BT finalised the takeover of EE in August 2016, and the integration has resulted in BT controlling 35% of the mobile consumer market. The profit of the UK-based telecommunication group in its second quarter 2017 rose to £566 million.

BT Group chief executive Gavin Patterson said: "We will operate a multi-brand strategy with UK customers being able to choose a mix of BT, EE or Plusnet services, depending on which suits them best. The acquisition enables us to offer great value bundles of services and customers are set to be the winners as we compete for their business".

(Source: adapted from www.marketwatch.com (Oct 27 – 2016) and http://home.bt.com/news/bt-life/bt-to-retain-ee-brand-as-acquisition-confirmed-11364037422234)

Extract C

BT to slash landline charges for 1 million customers

Rental charges for landline-only customers – households with a telephone-only contract but no BT broadband – will fall from £18.99 to £11.99 per month after the regulator attacked existing deals as 'poor value for money'. This rental reduction will save a million landline-only customers £84 a year.

The regulator Ofcom (Office of Communications) said it stepped in because these bills for landline-only customers – nearly two-thirds of whom are over 65 – have "soared" in recent years. This is despite BT and other landline providers benefiting from significant cuts in the wholesale line rental cost of providing the service by BT Openreach. Many landline-only customers are elderly, and have been with BT for decades. Ofcom has focused on BT because it accounts for two-thirds of the UK's 1.5m landline-only customers.

A spokesperson for Ofcom said "This position [of dominance] has allowed BT to increase prices without much risk of losing customers, and other providers have followed BT's pricing lead. We expect BT's price cut to mean other providers will follow suit". Ofcom said that over three-quarters of BT's landline-only customers have never switched provider, which has left them a prime target for price rises. The regulator said that all major landline providers have increased their line rental charges by between 23% and 47% in recent years, while their own costs for providing the service have fallen about 27%. Ofcom said it is also looking at measures to help people shop around for better deals with more confidence.

(Source: adapted from 'BT to slash landline charges for 1m customers', Mark Sweney, Copyright Guardian News & Media Ltd 2017 https://www.theguardian.com/business/2017/oct/26/bt-to-slash-landline-charges-for-1m-customers)

(a) With reference to Extract A, explain the difference between a positive statement and a normative statement.

(5)

(b) With reference to Extract B, examine the likely benefits to consumers of the integration between BT and EE.

(8)

(c) With reference to Extract C, assess possible reasons why many 'landline-only' customers do not switch to a cheaper telephone provider.

(10)

(d) Discuss **one** likely reason for the rise in BT's profit (Figure 2, Extracts B and C). Use a cost and revenue diagram to support your answer.

(12)

(e) Discuss methods of government intervention to protect consumers within the utilities markets, such as energy and telecommunications.

(15)

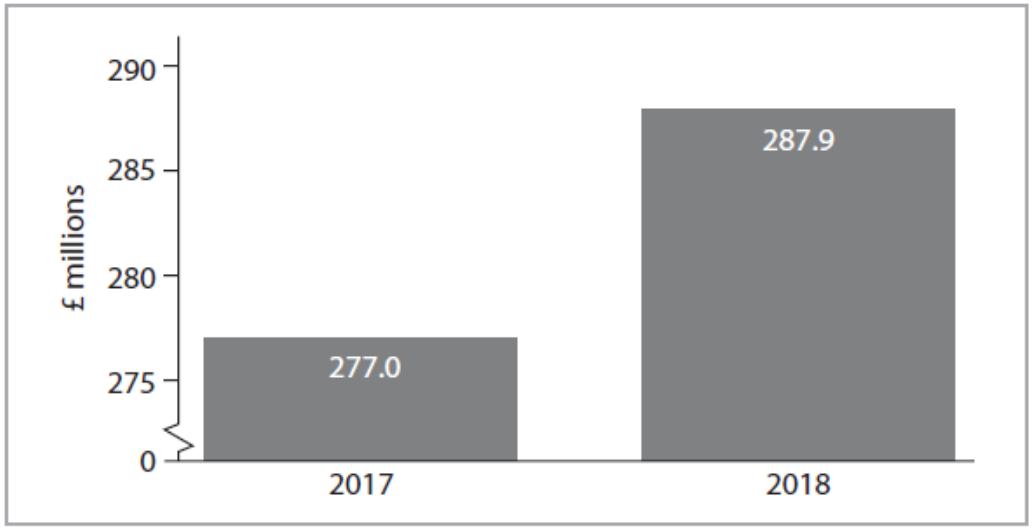
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Q7.

Use the data to support your answers where relevant. You may annotate and include diagrams in your answers.

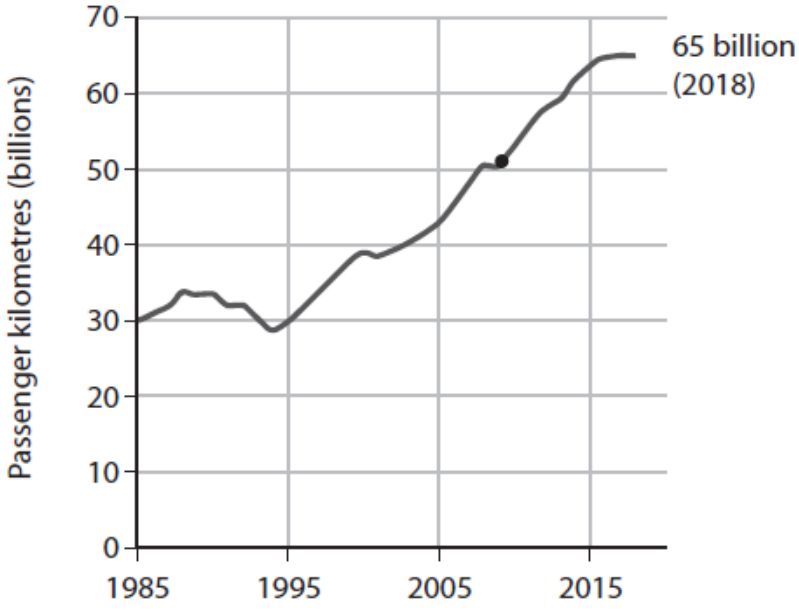
The UK Rail Industry

Figure 1: UK government subsidy to Northern, a train operating company in Northern England



(Source adapted from: https://www.theyworkforyou.com/wrans/?id=2018-10-18.181280.h)

Figure 2: Rail passenger kilometres travelled per year in the UK, billions



(Source adapted from: fullfact.org)

Figure 3: Price of a single off-peak train journey, Edinburgh to Leeds Saturday 22nd December 2018 19:00 hours

Adult	Young Persons (16–25) Railcard
£105.30	£69.50

(Source: https://www.lner.co.uk/buy-tickets/booking-engine)

Extract A

The case for nationalisation

Privatisation has not made the rail industry cheaper to operate, despite the promise from one government source that it would see private companies bringing: "more competition, greater efficiency and a wider choice of services".

One reason, suggest the critics, is fragmentation. Instead of pushing British Rail into the private sector as a single supplier the government chose to break it into three components of track, train operators and rolling stock i.e. the trains and carriages. This has encouraged each part of the rail industry to prioritise its own profits rather than collaborating to improve the system.

Privatisation, meanwhile, never really worked. The rail network of 2 500 stations and 32 000 km of tracks was renationalised in 2001. This has encouraged the government's transport secretary, a supporter of private sector involvement, to argue that the state Network Rail monopoly should be removed so that companies can bid to build new rail lines to upgrade the railway.

The privately-owned train operators are now the subject of fierce criticism, due to overcrowding and cancelled services. Private companies are supposed to compete to win a bid to be the train operator for a region for a short number of years. However in recent years the number of private companies bidding or renewing their contract as rail operators has fallen. In May 2018 the government rescued the East Coast line by renationalising it. The line had been run by the private rail operator Virgin Rail, which was suffering lower passenger numbers and revenue than forecast.

Some argue that there is a simple solution: reunite track and train in the only feasible manner, nationalisation.

(Source adapted from: https://www.ft.com/content/d82848ca-f7ba-11e7-88f7-5465a6ce1a00)

Extract B

Southern Rail boss paid £495 000

The Chief Executive of Southern Rail, the private-sector train operator that has become associated with delays, losses, cancellations and strikes, was paid £495 000 last year. This increased calls for nationalisation and a maximum wage for executives at companies with government contracts. In contrast the average base pay for a train driver in the UK is £47 705, although they can earn up to £63 000.

Nearly a third of Southern Rail trains were late in 2016 as it tried to deal with a labour dispute that involved extensive strike action. The rail trade unions are opposed to planned changes to the role of train guards, which they claim will put passenger safety at risk.

(Source adapted from: Rob Davies, The Guardian 10 April 2017
https://www.theguardian.com/business/2017/apr/10/southern-rail-boss-double-pay-rise)

(a) Refer to Figure 1. Explain the likely effect of the change in subsidy levels between 2017 and 2018 on rail fares.

Include a supply and demand diagram in your answer.

(5)

(b) With reference to Figure 2, examine **two** possible factors which may have influenced demand for rail travel since 2008.

(8)

(c) Assess whether complete nationalisation of the rail industry might protect employees.

(10)

(d) With reference to Extract A, paragraph 3, discuss whether the rail network can be considered to be a natural monopoly.

(12)

(e) Discuss the likely benefits of price discrimination to rail passengers. Use a diagram to support your answer.

(15)

(Total for question = 50 marks)