Oxford Cambridge and RSA

Monday 4 October 2021 – Morning

A Level Economics

H460/01 Microeconomics

Time allowed: 2 hours

You can use:
- a scientific or graphical calculator

Please write clearly in black ink. **Do not write in the barcodes.**

Centre number | | | | | | Candidate number | | | | |

First name(s) _____

Last name _____

INSTRUCTIONS
- Use black ink. You can use an HB pencil, but only for graphs and diagrams.
- Answer **all** the questions in Section A, **one** question in Section B and **one** question in Section C.
- Write your answer to each question in the space provided. If you need extra space use the lined pages at the end of this booklet. The question numbers must be clearly shown.

INFORMATION
- The total mark for this paper is **80**.
- The marks for each question are shown in brackets **[ ]**.
- Quality of extended response will be assessed in questions marked with an asterisk (*).
- This document has **20** pages.

ADVICE
- Read each question carefully before you start your answer.

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SECTION A

Read the following stimulus material and answer **all** parts of Question 1 which follow in this section.

The UK air travel sector

The UK's biggest airline, easyJet, has reported profits before tax of £445m on revenues of almost £6bn, in the financial year ending September 2018. As the largest of the UK operators (see Table 1), easyJet faces strong competition from other 'budget' airlines (Flybe and Jet2), package holiday firms (TUI and Thomas Cook) and the previous market leader, British Airways. The recent growth of easyJet in the UK has been helped by the closure of Monarch in December 2017 and continued labour disputes at British Airways.

	2015	2016	2017
easyJet	58.6	63.3	68.3
British Airways	41.3	42.1	42.8
TUI	10.6	10.9	11.3
Jet2	5.9	6.7	9.7
Flybe	7.8	8.4	9.2
Thomas Cook	6.4	6.6	7.3
Monarch	5.7	5.4	3.4

Source: CAA

Table 1 – UK Passenger numbers (million)

Across the whole of Europe, easyJet flew a record 88.5 million passengers, up 10% on the previous year, and filled 93% of its seats – meaning only 13 seats are empty on an average flight. Over the year, this 'load factor' (the percentage of seats sold across all flights) has increased by 9.8%. Typically, airlines have been satisfied with a load factor of around 75%.

Revenue per seat for easyJet in 2018 was £62, leading to a profit of £6.53 on each seat. But the airline had an additional £65 m cost from "a change in approach to IT development" and a £40m cost from taking over the landing slots of the failed Air Berlin, at Tegel airport in Germany.

A growing amount of easyJet's revenue comes from what it calls 'ancillary' sources. When a customer buys a ticket online, they are also able to book hotel accommodation, car hire and airport transfers. The business aims to grow its holiday sales, offer an improved customer loyalty programme and target the business-travel market, with "a more personalised product including new business fares".

Although it is now common throughout the airline industry, easyJet was one of the first airlines to introduce a 'dynamic pricing model' which sees the price of a ticket increase as the date of the flight moves nearer. Table 2 shows how the prices quoted on two separate routes were lower if booked on the 18 December 2018 compared to the 18 March 2019. As the weeks go by, the price quoted will increase as the date of travel moves nearer. There are always exceptions to the rule, due to other supply and demand factors, but, in general, the sooner a customer books the better price they get.

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Route	Date when price was quoted	Date of travel		
		6 April 2019	1 June 2019	5 October 2019
London Gatwick to Gran Canaria	**18 December 2018**	£194	£74	£60
	18 March 2019	£259	£80	£76
London Luton to Barcelona	**18 December 2018**	£110	£42	£39
	18 March 2019	£122	£46	£42

Source: www.easyjet.com (accessed 18/12/18 & 18/03/19)

Table 2 – Ticket prices quoted on different dates (seat only)

On most routes, customers have a choice of airline, and in each case the service is largely identical. It is now common practice on these short and medium-haul routes that food, seat reservations and luggage are not included in the basic ticket price (see Table 3).

Airline	Basic price including all taxes	Seat reservation	One piece of check-in luggage
British Airways	£143	Included with luggage	£20
easyJet	£74	£6 to £18.50	£42
Thomas Cook	£73	£10	£48
TUI	£311	£11	£25

Source: Company websites (accessed 18/12/18)

Table 3 – Ticket prices quoted for London Gatwick to Gran Canaria (to travel on 1 June 2019)

Air travel is often said to be a demerit good. Politicians and economists have argued over the degree of control needed in the market and whether it is taxed enough. Most passengers entering or leaving the UK on a commercial flight will pay the Air Passenger Duty (APD) which was introduced by the UK government in 1993 for environmental reasons. However, a report published in 2018, called the 'Roadmap to decarbonising European aviation' considers other policies to reduce carbon emissions from air travel. The report criticises the lack of taxation of jet fuel across the world, saying: "Artificially cheap tickets through tax exemptions and government subsidies have propped up and propelled the industry." There is certainly a strong case for the current tax-free status of jet fuel to end.

Substitution, persuading travellers to switch from planes to trains, is another solution proposed in the report. It calls for, "greater competition in the rail sector in order to improve performance and drive down operating costs and fares". This suggestion would have been unthinkable 20 years ago. Today, speed and comfort have marginally improved for train travel (as there are now more fast routes). While, especially for shorter distances, flying has become increasingly unpleasant and time-consuming.

"It used to be a rule that, in order to compete with a one-hour flight, a train journey could be a maximum of three hours," says Mark Smith, of rail travel website Seat61. "That was allowing for an hour in the air and two for security, boarding and transfers. That simply is not the case anymore, with longer check-in and security times."

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At the same time as taxing air travel with the APD, the UK government subsidises some routes. One example, introduced in March 2019, is on a new route between Newquay (in Cornwall) and London Heathrow. Around 170 000 passengers are predicted to use the service each year. Over the first four years, the Department for Transport and Cornwall County Council will each pay up to £1.7m, representing a subsidy of £10 per passenger for a return flight. The UK Transport Secretary at the time, Chris Grayling, said, "Maintaining and enhancing air routes that help bring together the UK is one of the key benefits. This new route will see the people of the south west profit from a direct connection into [Heathrow], building on the government's ongoing commitment to the Newquay route, protecting choice and strengthening trade and travel opportunities for the whole UK."

1 **(a)** Refer to **line 11**. Calculate, using information from the stimulus material, the average cost of a seat on an easyJet plane in 2018.

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..... **[2]**

(b) Refer to **lines 14–18**. Explain, using evidence from the stimulus material, what is meant by joint demand.

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..... **[2]**

(c) Using **Table 2**, explain the concept of utility.

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..... **[2]**

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(d) "There is certainly a strong case for the current tax-free status of jet fuel to end." (lines 36–37)

Explain, using a diagram, the impact on the level of consumer surplus if jet fuel is taxed by the UK government.

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..... **[4]**

(e) Evaluate **two** factors which may determine the value of the price elasticity of demand for air travel. **[8]**

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(f)* Evaluate, using evidence from the stimulus material, government intervention in the market for air travel. **[12]**

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SECTION B

Answer **EITHER** Question **2 OR** Question **3**.

EITHER

2* The gender pay gap for full-time workers in the UK has fallen from 17% to 9% in the past 20 years. However, the gap is still over 30% in many engineering and manufacturing jobs but is much smaller, or even negative, in many service sector jobs, including in the health sector.

Evaluate, using an appropriate diagram(s), whether wage differentials are mainly caused by the presence of a monopsonistic employer. **[25]**

OR

3* The nature of the market experienced by internet-based firms, such as Amazon Marketplace, eBay and Alibaba, means that they may not have an objective of profit maximisation.

Evaluate, using an appropriate diagram(s), how a firm's objectives, other than profit maximisation, may affect its price and output decisions. **[25]**

Question .....

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SECTION C

Answer **EITHER** Question **4 OR** Question **5**.

EITHER

4* China is the world's second largest economy, has the fastest growing consumer market and is the second largest importer of goods – all from a centrally planned economy. However, more than 50% of China's surface water is not fit for human consumption.

Evaluate whether economic incentives are required to achieve an efficient allocation of resources. **[25]**

OR

5* According to scientists, there are at least half a million pieces of space rubbish in the earth's atmosphere.

Delhi, India's capital city, sees 80 deaths a day due to air pollution.

Evaluate how the problem of scarcity can be used to explain the requirement to make choices between free goods and economic goods. **[25]**

Question .....

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END OF QUESTION PAPER

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ADDITIONAL ANSWER SPACE

If additional space is required, you should use the following lined page(s). The question number(s) must be clearly shown in the margin(s).

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