



AS
June 2017

ECONOMICS

Paper 1 The operation of markets and market failure

7135/1

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**DO NOT WRITE ANY ANSWERS IN THIS INSERT.
YOU MUST ANSWER THE QUESTIONS IN THE
ANSWER BOOKLET PROVIDED.**

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CONTEXT 1: SUPERMARKETS

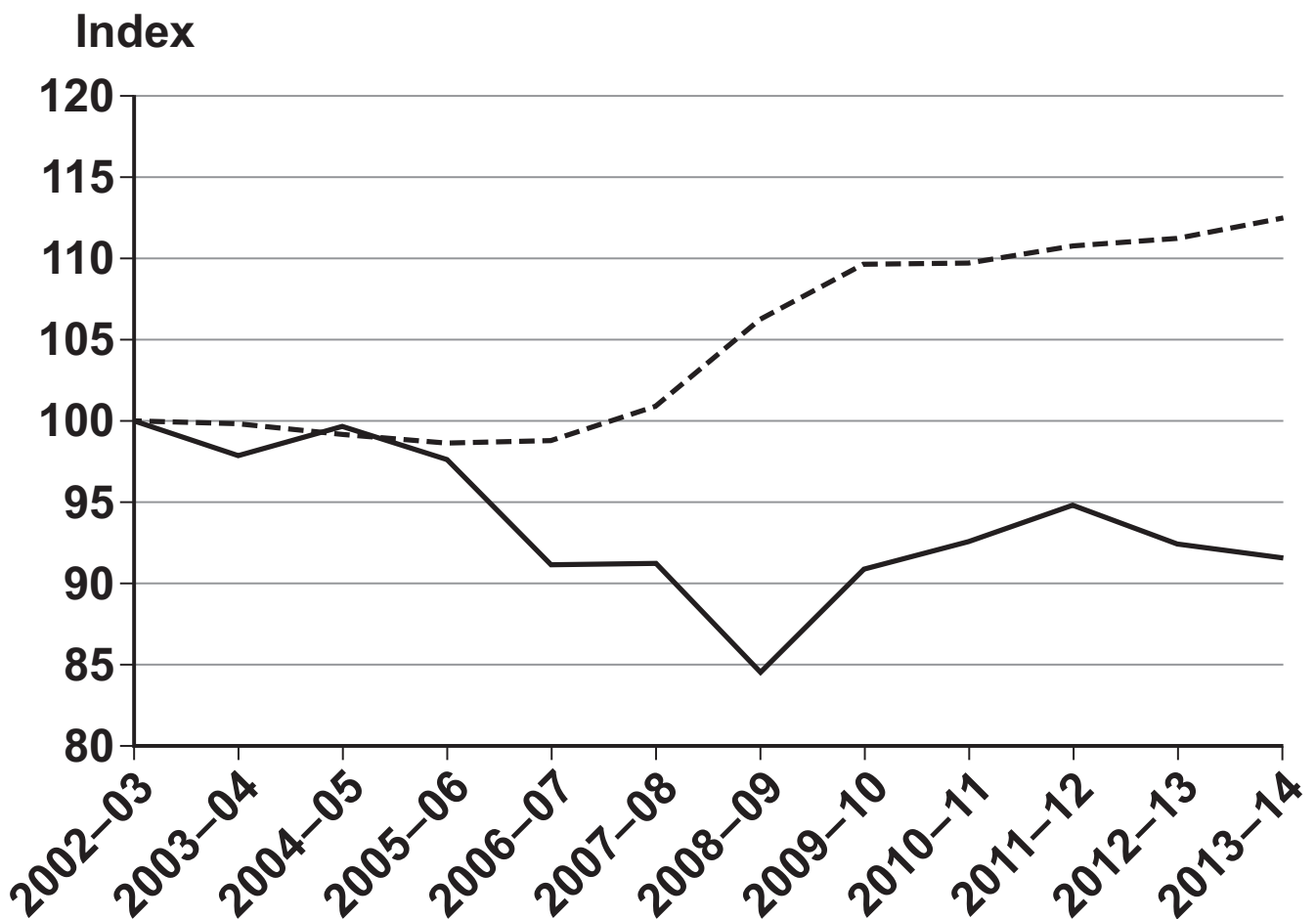
QUESTIONS 21 to 26

- **Extract A: Changes in real income and real food prices for low-income households (UK), 2002–03 to 2013–14 (2002–03 = 100)**
- **Extract B: The rise of the discount supermarkets**
- **Extract C: Effects on consumers and firms**

CONTEXT 2: GAMBLING

QUESTIONS 27 to 32

- **Extract D: Income in the gambling industry in Great Britain, selected types, 2008–09 to 2014–15 (£million)**
- **Extract E: Gambling – problems and recent changes**
- **Extract F: Should the government do more to limit gambling?**

Context 1**Total for this Context: 50 marks****SUPERMARKETS****EXTRACT A: Changes in real income and real food prices for low-income households (UK), 2002–03 to 2013–14* (2002–03 = 100)****KEY**

———— Index of income after housing costs at 2013–14 prices

----- Index of food prices in real terms

*** The data relate to households that had less than 60% of the median income. Both sets of figures have been adjusted for inflation using a variation of the Consumer Prices Index.**

Source: Department for Environment, Food and Rural Affairs, 2015

[Turn over]

EXTRACT B: The rise of the discount supermarkets

The last few years have seen considerable changes to the supermarket industry in the UK. Increased competition from Aldi and Lidl has weakened the monopoly power of well-established firms such as Tesco and Sainsbury's. There has also been more online ordering along with a shift away from shopping in big out-of-town stores to more frequent use of smaller local shops.

In 2014, Aldi's sales grew by 35.3%, increasing its market share to 4.6%, and by December 2015 this had increased further to 5.6%. With Lidl's 4.4%, the two firms combined now have 10% of the market, compared to 5% in 2012. This is in comparison to the 'big four' of Asda (16%), Morrisons (11%), Sainsbury's (17%) and Tesco (28%). Some have fared better than others, with Sainsbury's overtaking Asda in 2015 and Waitrose, who pride themselves on quality and service, also increasing their sales.

So what is driving these changes? Real incomes have fallen, causing many consumers to look for cheaper, and possibly less healthy, products in the 'budget supermarkets' and 'pound shops'. In these difficult times, Aldi and Lidl have been able to exploit considerable internal economies of scale, and by offering low-priced goods they have been able to attract customers from a variety of social backgrounds.

As with other products, people are increasingly ordering online. Aldi has recently announced plans for a limited online service starting in February 2016, and Lidl are also trying to gain access to this market. This will further increase competition, forcing the more established firms to look at ways to improve their service.

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Source: News reports, January 2016

[Turn over]

EXTRACT C: Effects on consumers and firms

Consumers now have much more choice of supermarket retailers and types of shop. Value for money has become increasingly important and supermarkets have been forced to cut prices and offer other incentives to keep and attract customers. 1
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To keep food prices low, there have been claims that supermarkets are using their power to drive down what they are paying farmers, although in August 2015, four of the supermarkets agreed to set a higher minimum price for milk they buy. Earlier in the year, an investigation was launched after firms supplying apples were accused of paying migrant workers low wages and housing them in poor conditions. There was also evidence of supermarkets misleading customers with their price deals. 10
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For some time, the big supermarket chains have been buying land to potentially build more large out-of-town stores but partly to reduce the availability of key sites to their rivals. As people have changed their shopping habits, and with the 'big four' making less profit, less of this land seems likely to be used for future supermarkets, although this situation could change. According to a leading property agent, the empty land could be enough to build 13 500 family homes, which, given the rising number of households, are urgently needed. 20
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So, on balance, have the changes in the supermarket industry been for the better, and if so, for whom?

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Source: News reports, January 2016

[Turn over for Context 1 questions]

CONTEXT 1 – Questions 21 to 26

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 Define 'internal economies of scale' EXTRACT B (lines 25–26). [3 marks]
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 Use EXTRACT B to calculate the three firm concentration ratio for sales in the supermarket industry in December 2015. [4 marks]
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 Use EXTRACT A to identify TWO significant points of comparison between the changes in real income and real food prices for low-income households in the UK over the period shown. [4 marks]
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 Use the data in EXTRACT B to complete the pie chart to show the market shares in the supermarket industry of each of the following in December 2015: Asda, Morrisons, Sainsbury's, Tesco and 'the rest'. [4 marks]
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 EXTRACT B (lines 4–5) refers to 'the monopoly power of well-established firms' in the supermarket industry.
- Explain TWO factors that could influence the monopoly power of firms in the supermarket industry. [10 marks]

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EXTRACT C (lines 30–32) states ‘have the changes in the supermarket industry been for the better, and if so, for whom?’

Use the extracts and your knowledge of economics to assess whether the changes in the supermarket industry are likely to be better or worse for consumers AND firms. [25 marks]

[Turn over for Context 2]

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CONTEXT 2

Total for this Context: 50 marks

GAMBLING

EXTRACT D: Income in the gambling industry in Great Britain, selected types, 2008–09 to 2014–15* (£million)

	2008–09	2009–10	2010–11	2011–12	2012–13	2013–14	2014–15
Bingo	703	627	626	681	701	672	662
Casinos	796	751	797	873	961	1111	1161
National Lottery	2522	2679	2840	3124	3280	3100	3232

*The data relate to ‘gross gambling yield’. This consists of bets and other income from gambling minus payment of winnings but not deducting other costs for the year April to March.

Source: Gambling Commission, 2015

[Turn over]

EXTRACT E: Gambling – problems and recent changes

According to the Gambling Commission, in 2007, before the recession, 68% of adults gambled, but by 2010, this had risen to 73%. As real incomes have fallen, some people have gambled more, but although gambling distracts people from their problems, it can become an addiction, affecting both gamblers and their families. Gamblers are more likely to suffer certain health problems and they are more likely to go to prison, often for theft. Many gambling addicts are also addicted to alcohol.

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The most common form of gambling is the National Lottery. People may be attracted by the ‘chance of winning big money’ or because ‘it’s fun’. However, now that the numbers in the main lottery draw have increased to 59, the chance of winning the top prize has fallen to 1 in 45 million. The betting firm, William Hill, said that there were similar odds of the Duke and Duchess of Cambridge having 11 children all of whom would win Olympic medals. Despite this, in January 2016, sales surged when the top prize reached £66m. With imperfect information, many people either do not know or do not understand that the chance of winning is so low.

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Technological changes, together with advertising, have also had quite an impact in changing tastes. Online gambling has increased considerably, up by 12.5% in 2010 alone. This is due to more online casinos and bingo sites, faster internet

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speeds and more people using their phones to gamble. Meanwhile, although the number of workers in the gambling sector has fallen from 115 564 in 2011 to 104 869 in 2015, it remains a significant employer.

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Source: News reports, February 2016

[Turn over]

EXTRACT F: Should the government do more to limit gambling?

- The minimum age for most gambling activities is 18 but at 16 you can buy a lottery ticket. 1
- How well are age restrictions enforced? In 2013, it was reported that six times as many children tried to enter betting shops than in 2009. 5
- There has been more crime in betting shops in recent years, as some addicted gamblers have become violent. The police were called over 9000 times in 2014, up from 1600 the previous year. For example, after losing £5000 in an afternoon, one gambler in the Midlands used his last £5 to buy a hammer to vandalise the gambling machines. The issue of whether more should be done has divided Members of Parliament: some wanted to reduce the maximum bet on gambling machines from £100 to £2, but there was also pressure from the gambling industry, resulting in no change. 10
- Some years ago, David Cameron, the Prime Minister, said: “Open markets and free enterprise are the best way to increase wealth, health and happiness ... But we must also stand up to business when the things that people value are at risk ... it’s time to place the market within a moral framework”. 15
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So what about gambling? Are people's views about alternative options influenced enough by moral judgements? Is there a place for this market 'within a moral framework'? If so, should there be more regulations or taxes to try to reduce the effects of gambling, in terms of both its private and external costs? Is the gambling industry taking advantage of the poor? Or is it just harmless fun that increases our 'happiness', and should be left to the free market?

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Source: News reports, February 2016

[Turn over for Context 2 questions]

CONTEXT 2 – Questions 27 to 32

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 Define 'external costs' EXTRACT F (line 32).
[3 marks]
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 Use EXTRACT E to calculate, to ONE decimal place, the percentage change in the number of workers in the gambling sector between 2011 and 2015. [4 marks]
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 Use EXTRACT D to identify TWO significant points of comparison between the changes in income for bingo and the National Lottery in Great Britain over the period shown. [4 marks]
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 Use the data in EXTRACT D to draw a bar chart to show income from casinos for the years 2008–09, 2011–12 and 2014–15. [4 marks]
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 EXTRACT E (lines 1–3) states 'in 2007, before the recession, 68% of adults gambled, but by 2010, this had risen to 73%.'
- Explain TWO factors that could have increased the percentage of adults who gamble.
[10 marks]

3	2
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EXTRACT F (lines 29–32) states ‘should there be more regulations or taxes to try to reduce the effects of gambling, in terms of both its private and external costs?’

Use the extracts and your knowledge of economics to assess whether the UK government should intervene more in the gambling industry. [25 marks]

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