

YISHUN JUNIOR COLLEGE
JC2 PRELIMINARY EXAMINATIONS 2015

ECONOMICS

Higher 2

9732/01

14 AUGUST 2015

1430h – 1645h

Additional materials:

Writing paper

Cover page

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TIME 2 hours 15 minutes

INSTRUCTIONS TO CANDIDATES

Write your name, CTG and index number in the spaces provided on the cover page and on all sheets of writing paper handed in.

Write in dark blue or black pen.

You may use a soft pencil for any diagrams, graphs or rough working.

Do not use highlighters, glue or correction fluid.

Answer **both** questions **1** and **2**.

At the end of the examination, tie a cover page to **two** separate questions:

1. Case Study Question 1, and
2. Case Study Question 2.

INFORMATION FOR CANDIDATES

Including this cover page, there are **7** pages in this question booklet.

The number of marks is given in brackets [] at the end of each question or part question.

You are reminded of the need for good English and clear presentation in your answers.

Answer **all** questions.

Question 1 The grocery retail markets in different countries

Extract 1: Woolworths' 85 cent "cheap, cheap bread" campaign

A South Australian politician has called for the reintroduction of competition laws as concerns grow about a recent price cut on bread by Woolworths, one of the two largest grocery retail firms in Australia. The other major grocery retail firm, Coles, followed suit in cutting prices soon after.

A Woolworths spokesperson said the reduction of prices on its Homebrand white sliced bread from \$1 to 85 cents, was to cater to its customers' needs.

Another grocery retail store owner disagreed. Woolworths' pricing strategy is what he terms as a "loss leader" strategy. A grocery retailer sells a product below cost in order to attract more customers into the store, then hopes the customer goes on to buy other products. While this strategy is employed by most grocery retailers, the difference is that Woolworths and Coles have so much market power it may be damaging to everyone else.

First, Woolworths and Coles use their dominant market share in the grocery retail market to force their suppliers to provide food at a lower price, which in turn enables them to lower the prices of their food products such as bread. Second, the smaller grocery retail firms competing with Woolworths and Coles either have to match the price cut and reduce their profits, or be prepared to lose market share to these two giants should they resist. Third, while consumers may enjoy a short-term gain from cheap bread, such gains may be short-lived. "Woolworths and Coles know that the impact of such a price cut for bread will drive small bakeries out of the bread market. And when the local bakeries are closed, they will not keep selling bread for 85 cents."

Source: Article from www.smartcompany.com.au, September 2014

Extract 2: Tesco charging higher prices for groceries in its chain of One Stop local shops

The grocery retailer with the largest market share in the U.K., Tesco, also owns a brand of convenience stores, One Stop – a fact that not many customers know about. Convenience stores belong to a segment of the grocery retail market. These stores are generally located in convenient locations. It is reported that One Stop charges up to 14 per cent more for the same goods that are also sold in Tesco-branded stores.

In response, Tesco has released a statement claiming that One Stop is an independent chain with a different distribution and supply network and higher operating costs. Other analysts commented that the pricing at One Stop could also be taking reference from a rival convenience store chain, Cost Cutter.

Source: The Daily Mail, March 2010

Extract 3: Deal unites two major grocery retail firms

The planned merger of two grocery retail firms, Royal Ahold and Delhaize, would create one of the biggest U.S. grocery retail chains. Ahold Delhaize, as the merged firm will be called, will have a 4.6% share of the U.S. grocery retail market, making it the fourth-largest firm (see Table 1).

Table 1: Market share of grocery retail firms (or known as supermarkets)

in the U.S.

Firm	Market Share (in %)
Wal-Mart	25.8
Kroger	8.3
Albertson's	5.0
Royal Ahold merged with Delhaize	4.6
Publix	3.0
H-E-B	2.1
Meijer	1.6
Target	1.4
Others	48.2

Source: Euromonitor International, 2014

The firms have relatively little geographic overlap in the U.S. market and could leverage their increase in scale to lower transportation and warehousing costs, as well as garner more negotiating power with food suppliers. Further cost savings can be gained through shared advertising. The current Royal Ahold Chief Executive, who will be the CEO of the merged firm, said that the merger also allows him to invest more in innovation.

The grocery retail business historically is one of razor-thin profit margins. It has been difficult to grow revenue with increasing competition from warehouse stores that sell in bulk, dollar stores that sell inferior versions of most grocery products and even higher-priced "natural" food stores. Therefore, the merger is seen as a defensive move mainly to reduce their costs of production.

While the deal is still subject to regulatory approval, analysts don't expect antitrust issues to crop up. Instead, the two firms need to consider whether they will reap long-term success – will the merger make the firms better grocery retailers that can grow their combined market share, or will the only benefit be from economies of scale?

Source: The Wall Street Journal & The New York Times, both June 2015

Extract 4: Reform competition policy to tackle the market dominance in the grocery retail market

In the Australian grocery retail market, the growing dominance of the top two firms, Woolworths and Coles, is squeezing the profit margins of their suppliers such as farmers and local manufacturers. Small local grocery retail firms are also struggling to compete with the two firms, resulting in a reduced variety of products available to consumers.

The (Australian) Greens, a political opposition party in Australia, wishes to reform the competition policy in Australia to tackle the market dominance existent in the grocery retail market. In their efforts to increase competition, they propose the following measures:

1. Stop dominant firms from buying up any more existing grocery retail firms.
2. Stop dominant firms from buying any agricultural land to prevent control of the supply chain.
3. Strengthen competition laws to ensure dominant firms cannot abuse their market power through pricing strategies.

4. Ensure that business-to-business contracts are fair; especially the contracts between small businesses and large, often dominant, businesses.
5. Increase the resources of competition watchdog (e.g. Australian Competition and Consumer Commission (ACCC)) to monitor and enforce regulations that deter anti-competitive behaviour.

Source: Policy proposals by The Greens, accessed from <http://greens.org.au>, updated as of January 2013

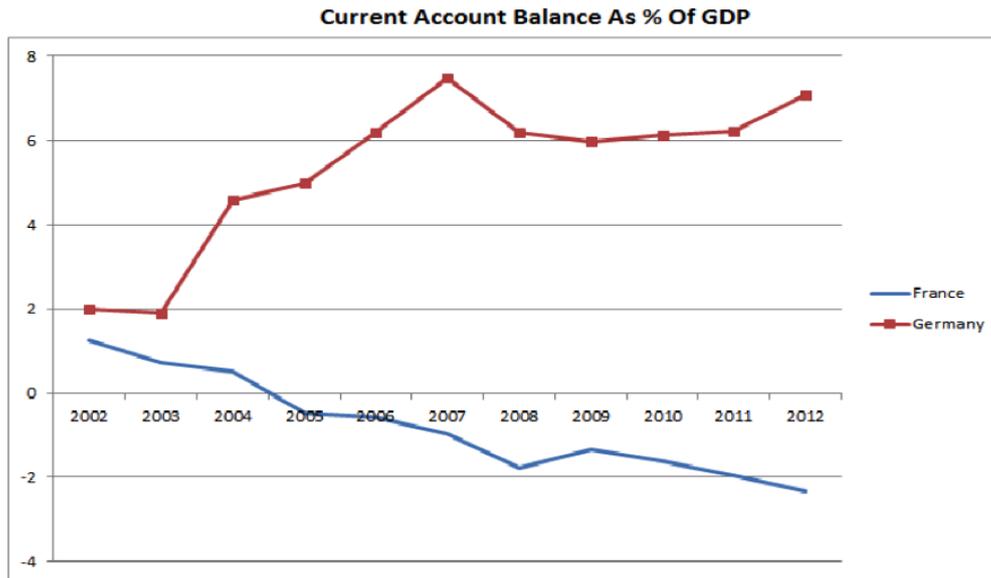
Questions:

- (a) With reference to Extract 1, explain how the cut in prices of the Homebrand white sliced bread may impact:
- (i) the revenue Woolworths earns from the sales of the Homebrand white sliced bread. [3]
 - (ii) the total grocery retail revenue earned by Woolworths. [3]
- (b) Using Table 1, identify and explain the type of market structure that best describes the U.S. grocery retail industry. [2]
- (c) With reference to Extract 2, explain whether Tesco is engaging in price discrimination. [4]
- (d) Discuss whether the market dominance in the grocery retail market brings about more benefits than costs to society. [10]
- (e) In Extract 4, The Greens proposed five measures to reform the competition policy in Australia to tackle the market dominance in the grocery retail market.
- Explain and evaluate the appropriateness of any two measures to “increase competition” in any one grocery retail market, namely the Australian, the U.K. or the U.S. grocery retail market. [8]

[Total: 30 marks]

Question 2 Troubles in France

Figure 1: Trade balances of France and Germany



Source: Trading Economics

Table 2: France's key macroeconomic indicators

Key indicators	2008	2009	2010	2011	2012	2013e ¹
GDP (% real change pa ²)	-0.2	-3.1	1.6	1.7	0.0	-0.2
Private consumption (% real change pa)	0.2	0.2	1.4	0.2	-0.1	-0.2
Consumer prices (average % change pa)	3.2	0.1	1.7	2.3	2.2	0.9
Recorded unemployment (%)	7.4	9.2	9.3	9.2	9.9	10.6
Budget balance (% of GDP)	-3.3	-7.6	-7.1	-5.2	-4.8	-4.0
Public debt (% of GDP)	68	79	82	86	90	93

Source: Economic Intelligence Unit

Extract 5: France's battered economy

On April 16th the IMF issued a grim reminder by forecasting that France will join Spain, Italy, Greece and Portugal in recession in 2013. The worsening outlook leaves the French government not only unable to stick to its promises of budget deficit reduction, but facing an internal political rebellion over how to manage its public finances.

Household consumption fell in both January and February. In March the INSEE business-confidence index dropped to nearly ten points below its level of a year ago. Struggling with the lowest profit margins in the euro area, many firms are putting investment on hold. A persistent deterioration of competitiveness in France has led

¹ e: estimated

² pa: per annum

to a greater loss of world export share over the past ten years than in Germany, Italy or Spain, particularly in manufacturing.

Three-quarters of the structural efforts to reduce the budget deficit this year depends on tax rises. However, France's overall tax burden is already the highest in the Eurozone and is set to rise yet again, to some 46.5% of GDP next year. Thus, the French government has promised that there will be no new taxes in 2014 beyond another Value-Added Tax increase.

This meant that to reduce the budget deficit, the government would have to cut its spending through a pension reform and cutting family benefits for the richest 15% of French households. This would not go well with a minority in the government who fear this will cause the economy to contract.

Source: Adapted from The Economist, 20 Apr 2013

Extract 6: President Hollande converts, proposes “austerity” and to boost growth in France

The policy battle of the last six years has been about how governments should respond to the recession that swept most of the globe, the slow growth that followed, and high unemployment. One camp argued for immediate large increases in government spending financed by borrowing, together with higher taxes on the rich. The other camp recommends decreased government spending paired with tax cut measures. The first camp was more popular initially, with governments around the world first reaching record budget deficits and then passing tax increases on high earners. However, in a major sea change on the policy battlefield this week, President Hollande of France announced a conversion to the second camp, or generally referred to as the “austerity” approach.

The French version of austerity measures is this: the government focuses mainly on cutting government spending, together with announced tax cuts on businesses to complement cuts in government spending. This is particularly significant to economic policy makers around the world as France has the highest ratio of government spending to GDP of any developed economy.

In opposition to those pushing for more government spending as the solution, President Hollande said that only private investments could create jobs and revive growth. In particular, President Hollande is proposing to lower the payroll taxes that businesses pay for hiring each worker. This is not only a big win for businesses, but also recognition that making labour less expensive will encourage business to use more of it.

The results of the few countries in Europe that have tried cutting government spending have been quite positive. As of 2013, Bulgaria, Latvia, Lithuania, Hungary, Poland, and Romania have all cut government spending and seen their economies grow faster than the average for the European Union.

Source: Adapted from Forbes, 18 Jan 2014

Extract 7: France resorting to protectionism

When an international credit agency announced that over 62,000 companies in France would face bankruptcy in 2013, the French government set out to overcome a temporary surge in unemployment in France with a concerted effort of national industrialisation through various policy interventions. The government has pledged billions of euros to fund struggling national firms, a thinly-veiled attempt at protectionism. Yet, are such well-intentioned policies preserving France's future competitiveness within the European market?

The European competition commission Mr Almunia critiqued that "the European economy cannot be invigorated through protectionism...as Europe will not find its place in globalisation by launching a subsidy race with the rest of the world." Many other critics have similarly cited the French policies as the cause of, not the cure for, the French economy heading towards little or no economic growth in the immediate future.

And how is the French government paying for the industrial subsidisation? In one of the bids to increase tax revenue, the French government had increased the tax rate on top earners to 75 per cent. Some top earners have left France as a result; the increase in payroll taxes will also lead to an increase in goods and services, including exports.

Unsurprisingly, France's trade deficit continues to grow, as the result of excessively bureaucratic labour policies and sky-high payroll taxes keeping importers from buying French national products. Protectionism is not only contributing to stagnating economic growth, but also helping to cultivate dangerous conditions that can give rise to regional European and even global economic recession.

Source: Adapted from www.parisglobalist.org, 13 May 2014

Questions:

- (a) (i) Using Figure 1, compare the current account balances as percentage of GDP of France and Germany from 2005 to 2012. [2]
- (ii) Account for France's current account balance from 2005 to 2012. [2]
- (b) Identify and explain the cause of rising unemployment in France. [3]
- (c) Using Figure 1 and Table 2, comment on changes in France's standard of living from 2008 to 2012. [5]
- (d) With reference to the data where appropriate, assess the impact of France's protectionism on consumers and producers. [8]
- (e) Discuss whether the France government should continue with its "version of austerity measures". [10]

[Total: 30 marks]

END OF PAPER

Suggested answers to:
Q1- The grocery retail markets in different countries

**(a) With reference to Extract 1, explain how the cut in prices of the
(i) Homebrand white sliced bread may impact:**

the revenue Woolworths earns from the sales of the Homebrand white sliced bread. [3]

As the question is on how the cut in prices may impact the revenue, we can accept any well-reasoned answer using economic analysis.

Suggested answer 1:

Evidence: [E1P2..... “A Woolworths spokesperson said the reduction of prices on its Homebrand white sliced bread from \$1 to 85 cents, was to cater to its customers’ needs”]

Explain:

Candidates can interpret “cater to...customers’ needs” to mean that the demand for Homebrand white sliced bread (or perhaps cheap white sliced bread as a whole) is price elastic. The argument can be that consumers who choose to consumer cheap white sliced bread are likely to be from the lower income group, so they are more sensitive to price changes for goods and services, i.e. the price of most goods are a larger proportion of their income. An alternative reasoning can be that there are many substitutes to Woolworths’ Homebrand white sliced bread, and therefore demand is price elastic.

Hence, with $PED > 1$ (1m with justification), the cut in price will lead to a more than proportionate increase in quantity demanded, leading to an **increase in total revenue from the sales of the Homebrand white sliced bread (2m).**

Suggested answer 2:

Evidence: [E1P3... “Another grocery retail store owner disagreed. Woolworths’ pricing strategy is what he terms as a “loss leader” strategy...”]

Explain:

This suggests that revenue may fall as a result of a cut in price. This could mean that demand for Homebrand white sliced bread could be price inelastic, because expenditure on the bread makes up a small proportion of income. Any other plausible reasoning is acceptable.

Therefore, with $PED < 1$ (1m with justification), the cut in price will lead to a less than proportionate increase in quantity demanded, leading to an **decrease in total revenue from the sales of the Homebrand white sliced bread (2m).**

(a) the total grocery retail revenue earned by Woolworths.

(ii) [3]

Suggested answer:

Evidence: [E1P3. “Woolworths’ pricing strategy is what he terms as a “loss leader” strategy. A grocery retailer sells a product below cost in order to attract more customers into the store, then hopes the customer goes on to **buy other products**”.

Explain: “buy other products”. [ie besides bread, there are many other ranges of different products, being perishable and non-perishable products that are on the supermarkets shelves.]

Candidates could interpret these to be complements to bread – some may be very weak complements, e.g. fish that isn't eaten with bread, but could be bought at the same supermarket as one may buy bread, or strong complements, e.g. ham, bread spreads such as butter. Nonetheless, the demand for all these complements will increase to varying extent, that means the overall **total grocery retail revenue should increase**.

Mark Scheme:

If a(i) says revenue increases

→ Demand for other products increase → revenue increase (1m)

→ Explain how demand for complement increases (2m)

OR

→ Demand for other products decrease → revenue decrease (1m)

→ Explain how demand for substitutes decrease (2m)

If a(ii) says revenue increases

→ Demand for other products increase → revenue increase (1m)

→ Explain how demand for complement increases (1m)

→ Synthesise a(i) and a(ii) (1m)

OR

→ Demand for other products decrease → revenue decrease (1m)

→ Explain how demand for substitutes decrease (1m)

→ Synthesise a(i) and a(ii) (1m)

(b) Using Table 1, identify and explain the type of market structure that best describes the U.S. grocery retail industry. [2]

Suggested answer

Oligopoly [1m]

(must be supported with case materials):

Use Table 1 as evidence: The industry consists mainly of a few supermarkets. Market is concentrated in the hands of few firms, each with substantial market share. [1m] or small number of firms with significant market share in the industry. [1m] or the 5 firms' concentration ratio of 46.7% of the market share.

(c) With reference to Extract 2, explain whether Tesco is engaging in price discrimination. [4]

Suggested answer:

Yes - [2 m]

Market segmentation – Place (1m) –

Evidence : [E2P1 - “These stores are generally located in convenient locations”]

More price inelastic demand for consumers who value convenience over price, therefore convenience store prices are higher. (1m) –

Evidence : [E2P1 - “It is reported that One Stop charges up to 14 per cent more for the same goods that are also sold in Tesco-branded stores. “]

No - [2 m]

Explaining cost may differ (i.e. not exactly price discrimination) (1m) – Evidence : [E2P2 “In response, Tesco has released a statement claiming that One Stop is an independent chain

with a different distribution and supply network and higher operating costs.”]

Hence, in this case if there is a difference in cost and perceived differences, then the possible reason for the higher price could be the higher cost involved.

(d) Discuss whether the market dominance in the grocery retail market brings about more benefits than costs to society. [10]

Suggested answer:

Thesis: Market dominance bring more benefits than costs to society

- The planned merger of two grocery retail firms, Royal Ahold and Delhaize, would create one of the biggest U.S. grocery retail chains. Can compete more effectively against the other dominant firms –
- **Evidence:** “Could leverage their increase in scale to lower transportation and warehousing costs” [E3P2]
- **Explanation:**
- This explains technical economies of scale, as a result of all these economies of scale; the merged entity which will increase their market dominance allows them to enjoy a lower average cost. This can be passed on to consumers in the form of lower prices.
- Supermarkets benefit from lower cost of production and higher profits. Besides, there is greater ability to achieve productive efficiency and produce on the long run average cost curve (LRAC).

- **Evidence:** “as well as garner more negotiating power with food suppliers”. [E3P2]
- **Explanation:**
- The merged entity which will increase their market dominance allows greater marketing economies of scale where they can enjoy greater discounts when they buy its supplies in bulk.

- **Evidence:** “Further cost savings can be gained through shared advertising.” [E3P2]
- **Explanation:** Cost-savings in production as a result of economies of scale as the merged entity enjoys greater bargaining power in the purchase of its inputs e.g. more effective (joint) advertising → higher advertising cost can be more than offset by higher joint output / consumer base.

- **Evidence:** “merger also allows him to invest more in innovation” [E3P2]
- **Explanation:**
- Increase innovation (increase its dynamic efficiency).
- E.g. create its own online supermarket channel to better compete with the online stores. To provide better customer service to provide greater product differentiation from that provided by the online stores.

- **Evidence:** “merger is seen as a defensive move mainly to reduce their costs of production. [E3P3]
- **Explanation:**
- Streamline their business to ensure greater cost efficiency by reducing wastage and better use of resources.

- Market dominance firms left in the industry will each face a higher demand for their goods and services. Hence, total revenue will rise. With lower cost of production and higher total revenue, profits for the firms will also rise. With supernormal profits earned, they can also engage in research and development to develop better products or provide better services for the consumers. This will also lead to these firms achieving dynamic efficiency. Thus, consumers can also get to enjoy better quality goods and services at a lower price.
- Therefore, with market dominance, it will lead to less allocative inefficiency, lower prices and better products for the consumers (increase in consumer surplus) and higher profits for the firms.

Anti-thesis: Market dominance will bring more costs to society

- **Evidence:** “Woolworths and Coles know that the impact of such a price cut for bread will drive small bakeries out of the bread market. And when the local bakeries are closed, they will not keep selling bread for 85 cents.” [E1P4]
- **Explanation:**
- ⇒ When other supermarket leaves the industry. This also leads to higher market power for the incumbent firms, and thus, these firms can seek to exploit the consumers by charging higher prices. This will then lead to greater allocative inefficiency.

- **Evidence:** “Woolworths and Coles know that the impact of such a price cut for bread will drive small bakeries out of the bread market. And when the local bakeries are closed,” [E1P4]
- **Explanation:**
- Market dominance may not be beneficial as **competition is reduced and consumers may be left with little choice.**
- With **greater market share and market dominance firms may choose not to pass any cost savings** that it reaped from economies of scale to consumers in the form of lower prices.
- Due to the huge supernormal profits by market dominance firms, there could be **greater income inequity**, at the expense of **consumers** paying a higher price.

- **Evidence:** “the difference is that Woolworths and Coles have so much market power it may be damaging to everyone else.” [E1P4].
- **Explanation:**
- It may bring about costs to UK society as well. One such cost will be the loss of jobs for supermarket staffs. If this is a significant industry in the UK, it will cause unemployment level to increase, bringing about several negative consequences to UK economy.

Conclusion

- Overall the market dominance is **likely to bring benefits** to the UK society.

- Strong competition is still available in the UK supermarket. Thus consumers are likely to enjoy price falls and improved services from the market dominance firms. Fewer choices in the supermarket may also not be an issue as the nature of the product is homogeneous and consumers would most likely value price over choices.
- In addition, in the increasingly globalised world, UK supermarkets have to compete against other foreign supermarkets. Therefore, market dominance firms may ensure

efficiency and cost minimizing for supermarkets would have been of society best interest, that if consumer welfare is not compromised.

→ Answers may choose to focus on grocery retail markets in Australia and/or the US.

L3	A balanced and well developed answer on whether market dominance brings more benefits than costs to society. An answer which thoroughly uses data evidence.	7-8
L2	An under-developed answer which explains how market dominance bring more benefits than costs to society. An answer which makes some reference to the data. A good one-sided discussion being market dominance bring more benefit or more cost. (Max 5m) A good discussion being market dominance bring more benefit or more cost without any reference to the text. (Max 5m)	4-6
L1	For an answer that shows a lack of understanding of the benefits and costs of market dominance pertaining to the text. Vague or incorrect explanation with no attempt to use case references.	1-3
E1	Evaluative comments with little or no justification.	1
E2	Evaluative comments with justification.	2

(e) In Extract 4, The Greens proposed five measures to reform the competition policy in Australia to tackle the market dominance in the grocery retail market.

Explain and evaluate the appropriateness of any two measures to “increase competition” in any one grocery retail market, namely the Australian, the U.K. or the U.S. grocery retail market. [8]

Suggested answer:

Any two measures applied to any one grocery retail market

- [1] Stop dominant firms from buying up any more existing grocery retail firms.
- [2] Stop dominant firms from buying any agricultural land to prevent control of the supply chain.
- [3] Strengthen competition laws to ensure dominant firms cannot abuse their market power through pricing strategies.
- [4] Ensure that business-to-business contracts are fair; especially the contracts between small businesses and dominant firms.
- [5] Increase the resources of competition watchdog to monitor and enforce regulations that deter anti-competitive behaviour.

Suggested approach:

[1] Identify one grocery retail market for discussion, i.e. Australia, UK or US

[2] Identify two measures (of the five) that could be used in selected grocery retail market – avoid using a measure that is clearly inappropriate

[3] Explain how these two measures would work, with reference to the selected grocery retail market where relevant

[4] Evaluate the use of these two measures in the selected grocery retail market

[1] Selecting a grocery retail market

1. Candidates are expected to recognise that the grocery retail markets have slightly different characteristics – in the Australian market that are two clear market leaders; in the UK market there is limited information though there are signs of market dominance shown by one firm (Tesco); in the US market while Walmart is the clear market leader by market share, the top 10 firms have less than 50% of the market share which means there are many firms in this ultimately oligopolistic industry.
2. Depending on which market is chosen, there should be appropriate use of two measures that are chosen to specifically target the problems in the selected market.

[2], [3], [4] Using the Australian market as an example:

[2] Identifying appropriate measure: Measure 3 Strengthen competition laws to ensure dominant firms cannot abuse their market power through pricing strategies.

3. Given that Woolworths and Coles presently have very large market share, it is more effective to regulate their behaviour to ensure there is no abuse of market power through pricing strategies.

[3] Explain how the measure works

4. The main type of pricing abuse, is if dominant firms collude and raise prices in a bid to raise their revenue, especially for goods and services where demand is price inelastic. If consumers have few or no viable alternatives due to the sizeable market share of the colluding firms, consumer expenditure on such goods and services will increase – consumer welfare will be harmed while firms' revenues and profits will increase, assuming revenue increases are greater than costs increases. Therefore, preventing such abuse in the form of collusion and the raising of prices will ensure there is still healthy competition between the dominant firms and consumer welfare is not harmed.
5. Another type of pricing abuse, is where firms start a price war with the intent of driving out existing competitors as well as deter potential new entrants. The act of limit pricing / predatory pricing raises the barriers to entry into the grocery retail market, and also puts smaller firms or firms unable to sustain losses over a period of time at risk of shutting down (in the SR) or leaving the industry (in the LR). In the long run, consumers may face higher prices should the dominant firm(s) increase prices once the competitors have been forced out of the industry or new potential entrants have been deterred from entering the market; at the same time, consumers will also face a narrower variety of goods and services. It is also possible that with fewer competitors, the quality of products is no longer as good. By preventing such a pricing strategy from taking place, it will prevent the raising of BTEs, and also not put smaller firms at unfair risks of shutting down / leaving the industry. This will help maintain a healthy level of competition, and ensure that consumer welfare in the long run is taken care of.

[4] Evaluate the measure

6. Point Evaluation: It is an arduous task for the government to have to monitor whether dominant firms in a market are engaging in anti-competitive pricing strategies. It is not easy for the government to get hold of concrete evidence that collusion is taking place, especially if it is tacit in nature, e.g. price leadership. In terms of predatory / limit pricing strategies, it is also not easy to prove that firms are selling at a loss, i.e.

below their costs of production. Also consider that the government agency needs to monitor several markets, and not just the grocery retail market. All of these make it difficult for the government to effectively monitor what is happening in this market. In addition, it is also not easy to enforce in the case of predatory / limit pricing. Even if proven to be the case, it is difficult for the government agency to force the firms to raise prices – the public may not understand the long-term costs when there is predatory / limit pricing, as consumers may focus more on why they are not allowed to enjoy lower prices now.

[2] Identifying appropriate measure: Measure 5 Increase the resources of competition watchdog to monitor and enforce regulations that deter anti-competitive behaviour.

7. Given that there are just two firms with very large market share (Woolworths and Coles), the chances of collusive behaviour may be higher since it is easier to coordinate collusive raising of prices between fewer parties. The government may need to spend more resources monitoring this market more closely.

[3] Explain how the measure works

8. With more resources for the competition watchdog, there can be more investigations carried out to find evidence of collusive intent whenever there are significant increases in prices observed for goods and services in this market. This is for the purpose of monitoring. Once evidence is found of collusive behaviour, the competition watchdog will need to begin legal proceedings to charge the involved firms for violation of competition laws. This is usually a financially costly and time-consuming process, and will require significant resources as well. It is again important to keep in mind that the competition watchdog will have to monitor many consumer markets, and not just the grocery retail market. Therefore, increasing the resources that the competition watchdog has can improve its effectiveness in monitoring and enforcing anti-competitive behaviour, which can in turn serve as a stronger deterrence against anti-competitive behaviour and help to increase competition in markets, including the grocery retail market.

[4] Evaluate the measure

9. Point Evaluation: A common limitation for any form of government intervention is that the government has imperfect information. This measure is designed to improve the availability and accuracy of information that the government has, in order to act appropriately. Possibly, this measure should come first before any other specific measure can be implemented effectively. However, increasing resources for the competition watchdog will incur an opportunity cost; the government will have to forgo expenditure in some other area of government e.g. healthcare, education, housing expenditure – no right / wrong answer but we must recognise that there is a trade-off.

[4] Evaluate the measures as a whole

1. It could be argued whether increasing competition was even desirable to begin with. Answers could cite that excessive competition would bring about wastage of resources when firms engage in fundamentally unconstructive strategies such as persuasive advertising, i.e. does not improve any form of efficiency within the market, but could lead to over-allocation of resources into advertising.

Broad descriptions for Measure 1 (will be further edited)

Stop Woolworths and Coles from buying up any more existing grocery retail firms.

Explanation & Evaluate:

- If Woolworths & Coles starts buying up more existing grocery retail firms → both may have a significant market share → may lead to an even larger entity formed → may have significant market dominance → drive smaller and inefficient players out of the market → in LT, may set higher price.
- However, by stopping Woolworths & Coles from acquiring more existing grocery retail firms → industry may not grow into a market dominated by a few large grocery retail companies with high degree of market concentration (i.e. a large % of the market is taken up by the leading firms) → may mean more competition → competitive price and better quality in their product.
- As such, this measure may be seen as a boost to “increase competition”.
- Evaluation: it depends on the market. For Australia, Woolworths and Coles are already the two largest firms in the industry, so preventing their expansion can help to enhance competition. However, in the US market, allowing two smaller firms to merge may help increase the competition to the larger firms such as Walmart.

Broad descriptions for Measure 2 (will be further edited)

Stop Woolworths and Coles from buying any agricultural land to prevent control of the supply chain.

Explanation & Evaluate:

- This refers to vertical integration, which is the merging together of two businesses that are at different stages of production—for example, a farm rearing poultry and supermarkets like Woolworths or Coles. Merging with something further back in the process is known as backward integration.
- Benefits of vertical integration come from the greater capacity it gives supermarkets like Woolworths & Coles to control access to inputs (and to control the cost, quality and delivery times of those inputs).
- Merging in this way with something further on in the production process (and thus closer to the final consumer) is known as forward integration.
- E.g. If Coles’ poultry/beef is sourced directly from producers. This bypassing of wholesalers to deal directly with producers/growers → may achieve lower costs.
- However the smaller competing retailers using produce wholesalers may be unable to achieve similar low costs could be due to various reasons.
- As such, this measure may prevent Woolworths and Coles control of the supply chain.
- This could be seen as a boost to “increase competition”.
- Evaluation: it depends on the market, and at which stage of production (manufacturing or retailing stage) the government is trying to introduce competition.

Broad descriptions for Measure 4 (will be further edited)

Ensure that business-to-business contracts are fair; especially the contracts between small businesses and large businesses such as Woolworths and Coles.

Explanation & Evaluate:

- This measure will ensure small businesses such as local butcher, baker, green grocer, etc. are protected from unfair contract terms from larger businesses [e.g. Woolworths &

Coles] → will help small businesses who struggle in ensuring appropriate retail tenancy arrangements with their landlords.

- The measure will ensure small businesses run alongside a competitive supermarket industry with a number of participants.
- This measure puts a check on the dominant firms and helps small businesses compete in the marketplace; → will level the playing field for farmers as suppliers to the major supermarkets.
- As the supermarket dominant firms are in a position to abuse their power in the marketplace to demand lower prices from farmers and other suppliers, which are threatening the viability of many farms.
- Due to the dominance, there are few other options for farmers to sell their produce.
- As a result, this measure will ensure farmers are protected from unfair contract arrangements.
- As such, this measure may be seen as a boost to “increase competition”.
- Evaluation: similar to measure 4. This measure is meant to protect small businesses more.

L3	<p>1. Well-developed answer that explained and evaluated any two measures, linked to how these would increase competition.</p> <p>2. Top answers would have made explicit references to the chosen grocery retail market in Australia, UK or the US.</p> <p>Maximum 6m if measures are well-explained but with no reference to specific grocery retail market.</p>	6-8
L2	<p>3. Well-developed explanation and evaluation for only one measure, linked to how this would increase competition.</p> <p>OR</p> <p>4. Under-developed explanation and evaluation for any two measures, linked to how these would increase competition.</p> <p>OR</p> <p>5. Well-developed explanation without evaluation for any two measures, linked to how these would increase competition.</p> <p>Maximum 4m if measures are not linked to how they would increase competition.</p>	3-5
L1	<p>6. Undeveloped explanations, mainly lifting from extracts.</p> <p>7. Erroneous interpretations of what the measures mean, or how they could increase competition.</p>	1-2

Suggested answers to:
Q2- Troubles in France

(a) Using Figure 2, compare the current account balance as percentage of (i) GDP of France with that of Germany, from 2005 to 2012. [2]

Throughout the time period, France was experiencing a current account deficit while Germany was enjoying a current account surplus; both were increasing.

(Note: deficit/surplus – 1m ; increased– 1m; note that Cambridge used increased as well in N2009)

(a) Account for France’s current account balance from 2005 to 2012. (ii) [2]

France’s current account worsened due to falling exports because of the weakening of competitiveness (E7P2). This weakening happened because of expensive labour and high taxes (E9P2) which lead to French product being less competitive.

(Note: 1m for reason ; 1m for explanation of reason)

(b) Identify and explain the cause of rising unemployment in France. [3]

Cyclical unemployment is the type of unemployment caused for falling AD. Causes for the rising cyclical unemployment include falling business confidence together with firms putting investment on hold, falling consumer expenditure and cut in government spending (E7P2). Since C, I and G are falling, AD is expected to fall. As AD falls, unplanned inventories of firms will accumulate, firms will slow down production and hence lesser labour and resources are required leading to cyclical unemployment.

(Note: 1m for identifying the cause; 2m for correct explanation of the cause)

(c) Using Figure 1 and Table 2, comment on changes in France’s standard of living from 2008 to 2012. [5]

It is difficult to fully understand the changes in France’s SOL due to the lack of information using Figure 1 and Table 2 but in general, SOL has stayed fairly constant.

Material SOL (MSOL):

France’s MSOL in general stayed fairly consistent throughout the years. The MSOL measures the basket of goods and services available for consumption. Changes in real GDP can be used as a proxy measurement for changes in MSOL. As seen from Table 2, GDP growth was both slightly positive and negative with consumption growth also remaining fairly stable. Thus, MSOL did not really change.

NMSOL:

France’s NMSOL may in fact have fallen as unemployment rates had been rising. This adds stress to family. However, depending on current working stress and hours, some people may find joy in staying unemployed for a short period as they take breaks to spend time with their loved ones.

Insufficient Information:

There is a lack of information is general to determine the changes in SOL. Data about income inequality would help to understand whether MSOL have improved for individuals as a whole. Further, NMSOL can also be better understood with data on education, healthcare and environmental indicators.

Level	Descriptor	Marks
L1	Explains using data about changes in MSOL or NMSOL. Lesser credit is awarded if mere statements are present.	1-2
L2	Explain using data about changes to both MSOL and NMSOL.	3-4
E1	Justified the lack of information as inability to fully understand SOL changes Note: evaluation mark can still be awarded for one-sided answer as long as evaluative comment is on insufficiency of data.	1

(d) With reference to the data where appropriate, assess the impact of France's protectionism on consumers and producers. [8]

Impact on domestic consumers/households*Positive impact*

- Increase in domestic employment – only if the question refers to “households” and not “consumers”
- Cheaper prices for domestically produced goods and services

Negative impact

- Top income earners need to pay higher taxes to fund the subsidisation.

Impact on domestic producers*Positive impact*

- Reduced COP due to subsidisation → producers earn more profits if they keep prices constant or can reduce prices leading to increase in quantity demanded, and if $PED > 1$ can increase revenue and profits (assuming inc in revenue > inc in costs)
- (theoretical) Increases ability of producers to engage in product differentiation, e.g. R&D and/or advertising → can lead to increase in demand / reduction in PED value / reduction in cost of production

Negative impact

- Subsidisation may reduce incentive to be productive efficient and dynamic efficient (through R&D) if the subsidisation ends up reducing the level of competition in the industry, i.e. raises BTEs for incumbent firms
- To pay for the subsidisation, the govt needs to raise govt revenue through increase in taxes, which could still raise wage costs → net effect may not necessarily be a fall in COP

Level	Descriptor	Marks
L1	States without explaining or explains poorly with mistakes about various impacts of French protectionism on domestic consumers and/or producers	1-2
L2	Explains various impacts of French protectionism on domestic consumers or producers. More credit is awarded if both positive and negative impacts are explained. More credit is also awarded if	3-5

	attempt was made to use evidence from extract.	
L3	Explains various positive and negative impacts of French protectionism on domestic consumers and producers. More credit awarded if evidence from extract is applied.	6-7
E1	Provides an overall assessment of the impact that is well substantiated.	1

(e) Discuss whether the France government should continue with its “version of austerity measures”. [10]

Austerity measures are methods taken to reduce government budget deficit and would in this case mean to cut government spending while also, lowering tax rates to spur growth in order to raise more tax revenue in the long run.

France **should continue** with austerity measures:

Why cut in G is good ...

#1: Austerity will bring about a cut in spending which will allow the government to reduce a *ballooning government debt in Table 2*. This makes debt sustainable reducing political rebellion, due to indecision over FP (E5P1), which can help stabilise the French economy. This may also raise confidence in the government and thus attract foreign and domestic investment that drives economic growth. This is why *Bulgaria, Latvia, Lithuania, Hungary, Poland and Romania have all cut government spending and seen their economies grow faster than the average for the European Union (E6P4)*.

#2: Austerity may be helpful as it would mean *structural reforms in terms of pension and cutting family benefits for the richest 15% of French households (E5P4)*. This can lead to a more equitable distribution of income.

Why cut in T is good ...

#3: Austerity in this case may come in terms of a cut in spending but also together with a *tax cut on businesses (E6P1)*. As mentioned in E6P3, the president is proposing *lower payroll tax that businesses pay for hiring each worker*. This incentivises firms to invest as post-tax profits increases. Investment increases, AD increases leading to unplanned running down of stocks and firms hire more factors of production including labour, reducing cyclical unemployment and leading to a multiple increase in real national income via the multiplier.

France **should NOT continue** with austerity measures:

Why cut in G is not good ...

#4: Austerity should not be continued as domestic demand is already in decline. Low confidence, weak exports together with investments put on hold (E5P2) have worsened SREG and further cut in government spending will lead to a fall in AD and via the reverse multiplier effect lead to fall in real NY.

OR

#5: The cut in G is likely to outweigh the increase in I brought about by the cut in tax. This is because *“France has the highest ratio of government spending to GDP of any developed economy”*. Thus AD is likely to fall, leading to multiple fall in real national income (contractionary effect on the economy).

Evaluative Conclusion:

Whether France should continue on austerity measures heavily depends on the aim of the government and also, the effectiveness of the policy. To begin, public debts as a % of GDP is already rising and this could erode confidence in the country in the long run. This makes the case for austerity. However, it is worth noting that growth is flat or negative and reduction in G may worsen the economy in the short run. This may add to even lower taxes in the future as growth slows.

Level	Descriptor	Marks
L1	Identifies some relevant reasons with poor or no elaboration about being for OR against austerity.	1-3
L2	Explain the reasons for both (i.e. fall in G and T) for OR against austerity well. Explain either cut in G OR cut in T for AND against austerity well. Poorly developed two sided argument. Limited use of case evidence. Explained the effects of cut in G and T without linking to question as to whether should or should not continue with austerity. Max 4m	4-6
L3	Able to explain the reasons for both (i.e fall in G and T) for and against austerity well and thus, whether the government should continue them. Good use of relevant case evidence.	7-8
E1	Makes stand with limited or with an unjustified stand.	1
E2	Makes stand with strong justification.	2