

A LEVEL

Exemplar Candidate Work

ECONOMICS

H460

For first teaching in 2015

H460/03 Summer 2018 examination series

Version 1

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Introduction

These exemplar answers have been chosen from the summer 2018 examination series.

OCR is open to a wide variety of approaches and all answers are considered on their merits. These exemplars, therefore, should not be seen as the only way to answer questions but do illustrate how the mark scheme has been applied.

Please always refer to the specification <https://www.ocr.org.uk/Images/170839-specification-accredited-a-level-gce-economics-h460.pdf> for full details of the assessment for this qualification. These exemplar answers should also be read in conjunction with the sample assessment materials and the June 2018 Examiners' report or Report to Centres available from Interchange <https://interchange.ocr.org.uk/Home.mvc/Index>

The question paper, mark scheme and any resource booklet(s) will be available on the OCR website from summer 2019. Until then, they are available on OCR Interchange (school exams officers will have a login for this and are able to set up teachers with specific logins – see the following link for further information <http://www.ocr.org.uk/administration/support-and-tools/interchange/managing-user-accounts/>).

It is important to note that approaches to question setting and marking will remain consistent. At the same time OCR reviews all its qualifications annually and may make small adjustments to improve the performance of its assessments. We will let you know of any substantive changes.

Question 31

31 Using Fig. 1.1, compare the profitability of hosting the Vancouver and London Olympic Games. [4]

Exemplar 1

4 marks

~~Van~~ Vancouver's total cost is \$7558 million and ~~the~~ total revenue is \$1578 million. This means ~~the~~ the loss of \$5978 million is made by hosting ~~Vancouver~~ Vancouver Olympic games.

~~London's~~ London's total cost is \$11401 million and total revenue is \$3270 million. ~~The~~ Loss of \$8131 million is made by hosting London Olympic games.

Both Vancouver and London Olympic games were not ^{very} profitable as losses are made. However, London Olympic ^{huge} game made bigger loss, which means it's even less profitable. [4]

Examiner commentary

This answer immediately identifies the total revenues and costs for both Games and correctly calculates the loss made in each instance. This provides the data for the subsequent explanation, with recognition that neither made a profit but that London was the least profitable.

Exemplar 2

0 marks

London had higher costs than Vancouver in general and sporting infrastructure. However they also had significantly higher revenues in things such as sponsorship and ticketing. This meant that the Olympic games in London had a higher profitability than Vancouver as they made a profit.

of US\$ 813.1m compared to US\$ 5978m
in Vancouver

[4]

Examiner commentary

This exemplar begins with a vague description of the level of costs and revenues in Vancouver and London, without using the data. Whilst the final values given, for profit suggests the candidate has correctly calculated Total Revenue – Total Cost, they incorrectly conclude that a profit was made in both Games – the lack of a minus sign illustrates a lack of understanding that a loss was made.

Question 32

32 Evaluate, using the information in Extract 1, whether expenditure on the Olympic Games represents sustainable investment. [8]

Exemplar 1

5 marks

Sustainable investment is investment in ~~capital such~~ that meets the needs of the current generation without causing harm to ~~the~~ investment in future generations. Expenditure on the Olympic games ~~has~~ means that many countries will make a loss, it says 'critics point to the loss made by the majority of previous host cities'. This means that the country will ^{likely} pay for this through borrowing, increasing the national debt. This will have to be paid back and can lead to the government sacrificing future investment to pay it back. Especially, because it can 'lead to severe overcapacity when the event is over' meaning the investment wasn't beneficial for future generations and sacrifices ^{some} future investment.

However, the investment can be beneficial to future generations because it can lead to 'improvements in transport infrastructure'. This means that future generations benefit from the investment and therefore it is sustainable investment even if it involves sacrificing some investment in the future. In addition, ~~the~~ some of it may be funded through contractionary fiscal policy rather than borrowing so national debt may not actually increase ~~by~~ that much, therefore it isn't sacrificing as much future investment.

Expenditure on the Olympic games represents sustainable investment due to the benefits of future generations as well as current generations ~~a~~ such as better transport links. [8]

Examiner commentary

The opening sentence shows clear knowledge and understanding of the concept of sustainable investment. This is followed by relevant application to the case study, recognising that hosting the Games causes a loss and increases national debt. The subsequent analysis is credited as reasonable because it clearly explains the link between rising national debt and sustainable investment, arguing that future generations will lose out as a result of the government having less money to spend on investment going forward because it will be burdened with debt repayments. More technical development on this point – such as including the crowding out effect – would have enabled the answer to earn further analysis marks. Reasonable evaluation is offered as the candidate argues sustainable investment would not be harmed if the Olympics expenditure does not add to national debt and, even if it does, the benefits derived from an improved transport infrastructure would be long term. Further credit would have been given had the candidate explained exactly how future generations would benefit from an improvement in the transport infrastructure – e.g. increased geographical mobility of labour increasing the productive capacity of the economy.

Exemplar 2

3 marks

In the extract we see a strong case that spending expenditure is sustainable investment. Many in favour of the olympics say in the short run the ~~eco~~economy will be harmed by huge losses but they can be recouped in the long run as future generations can benefit. Clearly in 2012 ^{East} London was a massive regeneration giving "tangible benefits to local residents" with improvements in the transport infrastructure, furthermore countries may actually benefit in the medium term such as Japan who predict they could boost their economy by \$249bn if they were to host ^{due} leading to a multiplier occurring from increased tourism and future employment.

However in many cases the olympics is far from sustainable as seen in the Beijing olympics where the cycling race tracks are now weed infested, so there is ^{no benefit} ~~little~~ ^{from} ~~are~~ in the billions spent on it. Similar [8]

3.2 cases are seen in Brazil where the Olympic swimming pools are no longer even in use with billions spent on stadiums which ~~no~~ ^{future} generations and current cannot benefit from.

In conclusion expenditure on transport is very much sustainable but if a ^{hosting} national team does not have ^{success in an event} local people lose interest and sporting arena expenditure goes to waste meaning it does not represent sustainable investment.

Examiner commentary

Knowledge and understanding is shown throughout the first paragraph by identifying relevant evidence from the case study that expenditure on the Olympics represents sustainable investment – e.g. improved transport infrastructure and boost to Japanese economy. However, this material is not taken any further to be credited as analysis. Limited analysis is credited for recognising that the expenditure does not benefit future generations as billions will be spent on facilities that go out of use. This could have been further developed by explaining that the opportunity cost of such expenditure is sacrificing expenditure on alternative projects that may have represented more sustainable investment. Limited evaluation is given for the judgement that correctly states that some of the expenditure on the Olympics (e.g. transport) may be more sustainable than other expenditure (e.g. sports facilities).

Exemplar 3

0 marks

~~Sustainable~~ may
Olympic games represent sustainable investment because foreign ~~AAA~~ MNCs ~~have~~ better reputation on the countries. ^{will have} so FDI will increase through long-run, as the extract 2 says.

However, if the country has heavy regulations, such as ~~on~~ on environment, which may lead to MNCs thinking that ~~the~~ ~~can~~ operating in the country is not profitable, then no FDI will occur.

In addition, expenditure on the Olympic games does not represent sustainable investment.

Examiner commentary

The answer begins with a suggestion that hosting the Olympic Games improves the reputation of the country amongst MNCs. However, there is no explanation as to how this leads to increased FDI nor how this represents sustainable investment. The answer then goes further off course by suggesting environmental regulations may limit FDI, without any link to the Olympics or sustainable investment.

Question 33

33 Using the data in Extract 2, explain what is meant by the multiplier effect of Olympics expenditure. [2]

Exemplar 1

2 marks

33 This is when for every investment in the Olympics occurs (Olympic expenditure), the increase in investment leads to an increase in GDP by '1.7' times the original ~~am~~ value invested. For example, if ~~US\$~~ 100 ^{million} ~~billions~~ was invested, ~~the~~ GDP would increase by US\$ 170 million.

Examiner commentary

This answer clearly states that the injection will lead to a greater final change in GDP and offers application from the extract in the form of a numerical example to support this explanation.

Exemplar 2

0 marks

Multiplier effect is where increase in ^{or} component of AD, ~~can~~ such as investment, causes further increase in other component of AD, such as net export. Olympic expenditure is a government spending, which is a component of AD, which ~~can~~ generated jobs and increase tourist expenditure. The workers with the generated jobs will increase [2] consumption and tourist expenditure is a part of export.

Examiner commentary

The explanation of the multiplier is too vague. Whilst the candidate recognises an injection may cause further increases in aggregate demand, there is no explanation on the final impact on the economy – a greater final change in GDP/output/expenditure/income. There is also no use of the data in Extract 2 as required by the question.

Question 34

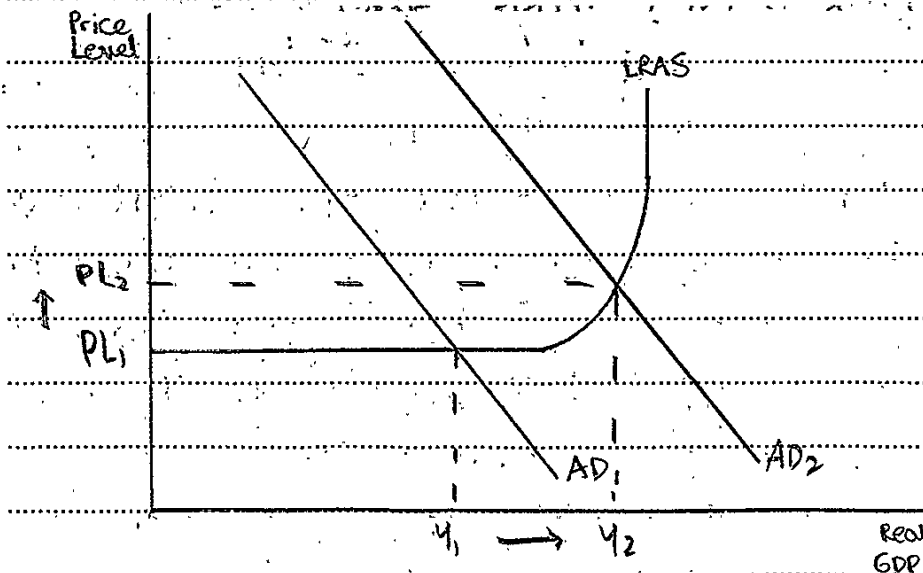
- 34 Evaluate, using the information in Extract 2, the extent to which hosting an Olympic Games has a positive impact on the government's macroeconomic policy objectives. [15]

Exemplar 1

15 marks

A government will aim to have low and positive inflation, limited fluctuations around zero on the balance of payments, low unemployment and a positive, stable and sustainable rate of economic growth.

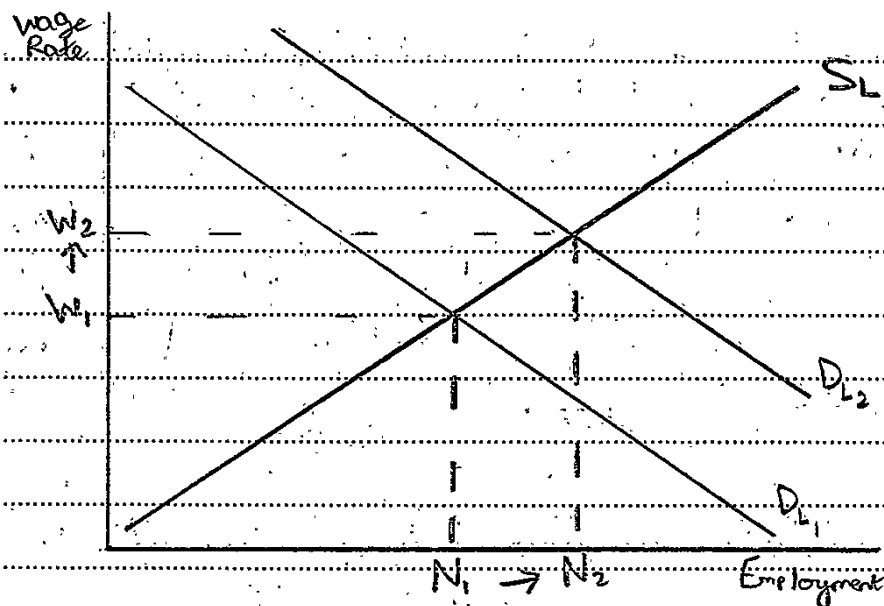
Hosting an Olympic Games will lead to an increase in economic growth.



Hosting an Olympic Games will lead to an increase in investment. As investment is a component of aggregate demand, this will lead to an increase in AD from AD_1 to AD_2 .

This will lead to an increase in real GDP from Y_1 to Y_2 , therefore leading to an increase in economic growth.

Hosting an Olympic Games will also lead to a decrease in unemployment.



Demand for labour in an economy is a derived demand. This means that it is dependent on the country's aggregate demand. The initial increase in investment - an injection - will ^{therefore} lead to an increase in AD. This will lead to an increase in the demand for labour from D_{L1} to D_{L2} . This will lead to an increase in employment from N_1 to N_2 . There will also be an increase in the wage rate from W_1 to W_2 , which may stimulate an increase in consumption and further increase AD through the multiplier effect.

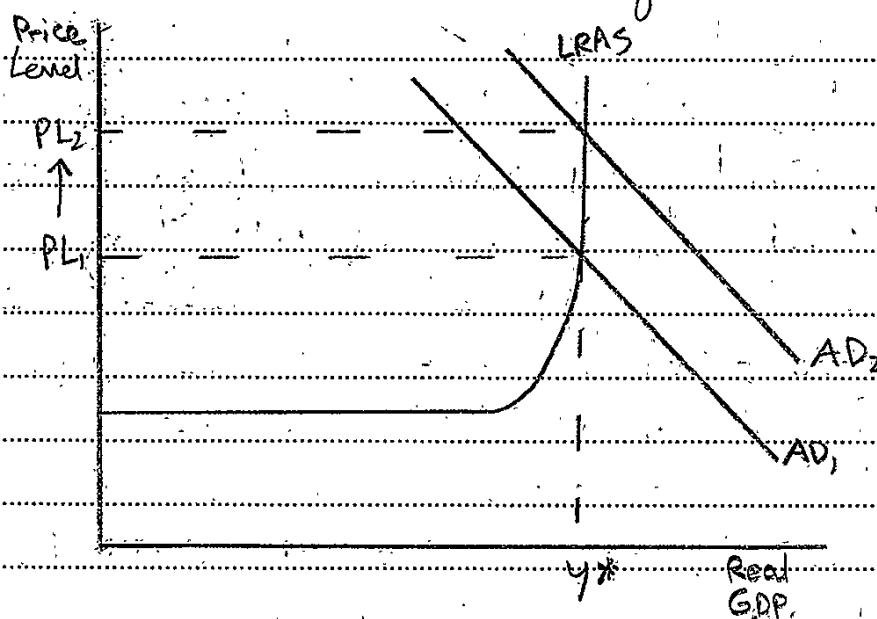
However, hosting the Olympic Games will lead to an increase in inflation. The increase in investment and government spending - both components of AD - will lead to an increase in AD from AD_1 to AD_2 (first diagram). This will lead to an increase in the

price level from PL_1 to PL_2 , resulting in an increase in inflation. This will also lead to goods being exported

becoming less price competitive. This will lead to a decrease in exports. Meanwhile, imports will increase as these goods become relatively cheaper. This will lead to a decrease in net exports, leading to a fall in AD. This will therefore reduce the increase in economic growth caused by the initial

increase in investment.

Overall, hosting an Olympic Games is likely to be beneficial in terms of a country's macroeconomic objectives. This potential benefit will depend on the country's position on the business cycle.



If the country is in a boom, the country is less likely to benefit

from hosting an Olympic Games. This is because the country is already at its ~~an~~ potential real GDP, Y^* . This means that the increase in AD from AD_1 to AD_2 will not lead to increased economic growth. Furthermore, as mentioned in Extract 2, unemployment will not decrease further as it is already at the natural rate of unemployment. Inflation will still occur through an increase in the price level from PL_1 to PL_2 , negatively affecting the economy. The extent to which economic growth will increase will also depend on the multiplier-accelerator model. At higher levels of spare capacity, the multiplier effect will be greater. ~~This~~ ^{the initial injection} increase in ~~economic growth~~ will therefore lead to a greater than proportional increase in economic growth. This will lead to improved expectations, leading to an increase in investment through the accelerator model, further increasing economic growth.

Examiner commentary

Knowledge and understanding of the government's macroeconomic objectives is shown in the first paragraph. Technical economic theory is used throughout the answer to explain the impact of hosting the Olympic Games on these objectives. A clear transmission mechanism between investment and economic growth is offered using aggregate demand, which is then linked to falling unemployment through the concept of derived demand. This is all tied together with the multiplier, making the analysis strong. Reasonable evaluation is credited for a straightforward exposition of how rising aggregate demand is likely to cause inflation. The evaluation becomes good when the rising price level is linked to falling international price competitiveness, worsening the balance of payments. The candidate offers a well-supported judgement that makes the evaluation strong as they consider the circumstances under which the Olympics are most likely to benefit the economy.

Exemplar 2

6 marks

The olympics will have will have a massive impact on the income distribution with the economy. Olympic games will provide jobs in the tourism industry which is known for seasonal ^{its} unemployment, this will mean that in the short run the olympics may boost employment but in the long run many will face hard times with less ^{disposable income} ~~money~~ than their counterparts due to them not being able to work, as there is no derived demand for their labour during certain periods of the year. Sustainable growth is also a problem as the ~~gov~~ economy may see a spike in the rate of inflation in certain periods of the year due to increased tourism from the games, ^{overmore} but once the games are over critics often fear that indeed the multiplier effect occur from this tourism will not be sustainable and ~~is~~ very much short term, even looking at Fig 3.1 we see that an olympics games hardly causes a major change in the rate of growth as many rates are similar. China being a perfect exam of this with Δ in Real GDP rising by ^{the same rate of} 10%.

for 2002 and 2007, little impact on growth is actually seen from ~~the~~ ^{the} olympics.

However it is thought that due to the olympic games there is ^a positive impact on the balance of payment in the form of short run increases in tourist expenditure and long run increases in FDI due to companies becoming more familiar the country, this will obviously have a positive impact on economic growth as components of AD are rising causing economic growth, further could be seen in 2012 in London where

80% of people felt proud to be British with improved consumer confidence in the economy helping to improve economic growth ^{through increase purchases of bikes}. From this we can conclude that if a games is successful and well run it can have a positive impact on all economic agents, causing macro objectives such as greater income equality and economic growth to be met due to the levels of investment ^{and government spending} the economy will receive, this is dependant how well it is targeted, if done correctly can create a scenario in which macro objectives are met because of the games.

Examiner commentary

The answer begins with relevant application from the case study that some employment will be generated in the tourist industry. Limited analysis is credited for linking this to the concept of derived demand, although the explanation of the impact on the distribution of income is too vague to be credited. The candidate would have been better served by explaining that once the Olympics is over individuals would return to being unemployed, meaning there is no long run decrease in unemployment as a result of hosting the Olympics. This is followed by a vague explanation of the inflationary consequences of hosting the Olympics, which cannot be credited as it is not grounded in economic theory – linking to rising aggregate demand would have been a route to achieve this. Limited evaluation is credited for using the data from the case study to argue that hosting the Olympics does not boost economic growth, as there is no evidence that growth rates significantly improve as a consequence of hosting. The consideration of the impact on the balance of payments cannot be credited beyond knowledge and understanding because the explanation does not go any further than what is given in the case study. This is another example of when the candidate would have benefited from grounding their answer in more technical economic theory – analytical credit would have been given had they realised that exports (a component of AD) were rising or explaining the changes in the different components of the balance of payments.

Exemplar 3

5 marks

A government will set or have macroeconomic objectives which they wish to ~~achieve~~ achieve. These objectives look at the nation as a whole and the economic performance.

A few objectives are full employment, stable inflation, greater parity on its balance of payments, reduced income inequality and economic growth.

The Olympic Games is an investment made as a country aims to host the games.

In some cases hosting the Olympic games fits with some objectives.

Lower unemployment is said to be achieved. This is as more employment occurs during the hosting of the Olympic games. This is as stadiums need to be built, roads improved and general infrastructure improved. All this increase in construction means that more people are going to be employed.

This would mean that the unemployment level is decreasing and the employment level is increasing. Conforming with one of the governments macroeconomic objectives.

Another macroeconomic objective is to achieve

economic growth. This is where the countries real GDP has increased. This is achieved as AD increases as well as government revenue. As more people are employed, they now earn a salary. This means that they can now buy goods as they have an income. This increased consumption boosts AD. As well as this, as more people earn an income the government now earns greater tax revenue as more people are employed which comes in line with improving the budget.

The extent to which hosting the olympic games has a positive impact on the government's macroeconomic objectives varied. This is as government will prioritise different objectives.

With that, the olympic games may also go against objectives. One being low/stable inflation. If a government has increased consumer spending this leads to higher AD as demand has increased which can lead to inflation.

Examiner commentary

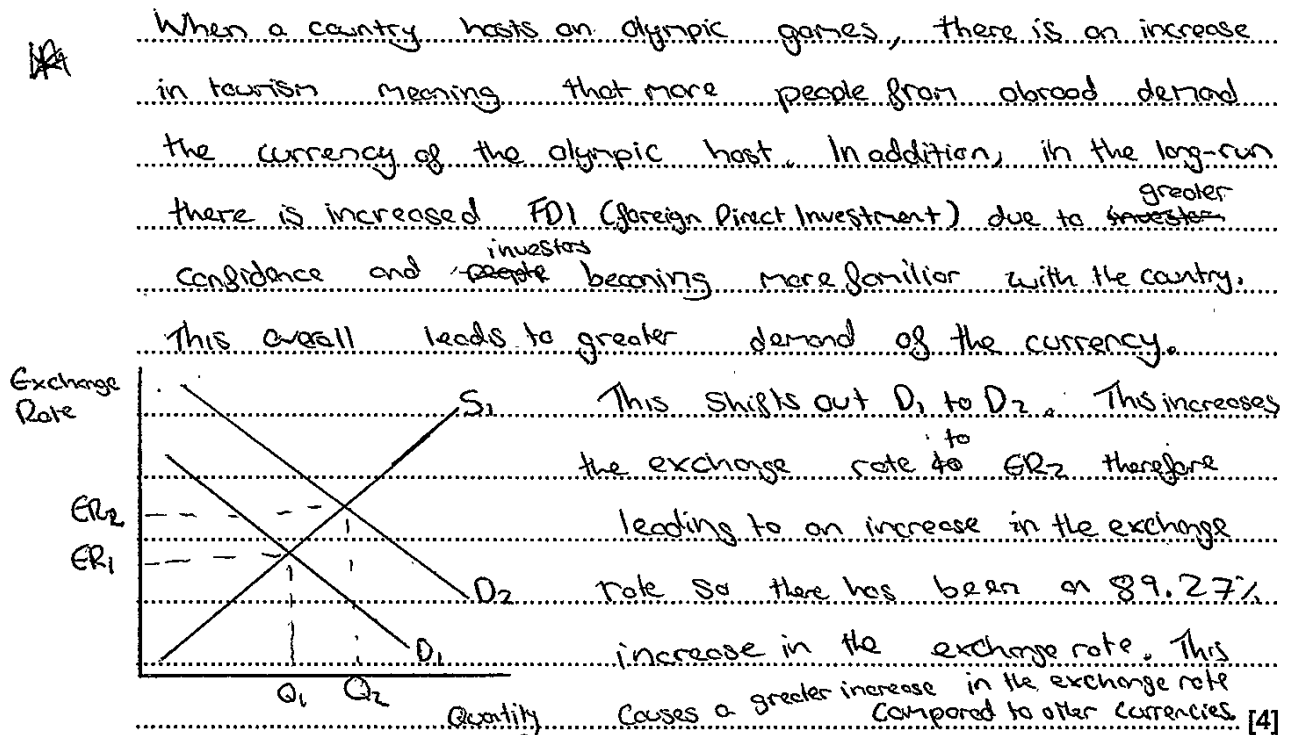
The candidate shows knowledge and understanding of the government's macroeconomic objectives in the second paragraph and goes on to identify that hosting the Olympics will reduce unemployment because construction workers will be required to build the infrastructure. In order for this to be credited as analysis it would need to go further than what is given in the case study, such as by considering the concept of derived demand. Limited analysis is credited for linking the falling unemployment to economic growth through a basic explanation of rising aggregate demand. Limited evaluation is also credited for the basic statement that rising aggregate demand may harm inflation. For the answer to be credited at a higher level deeper analysis would be required, such as by considering whether the growth would be demand or supply side. Consideration of other macroeconomic objectives, such as the balance of payments, would also improve the answer.

Question 35

- 35 Explain, using an appropriate diagram, why the changes in the Olympics index, illustrated in Fig. 2.2, may occur as a result of a country hosting the Olympic Games. [4]

Exemplar 1

4 marks

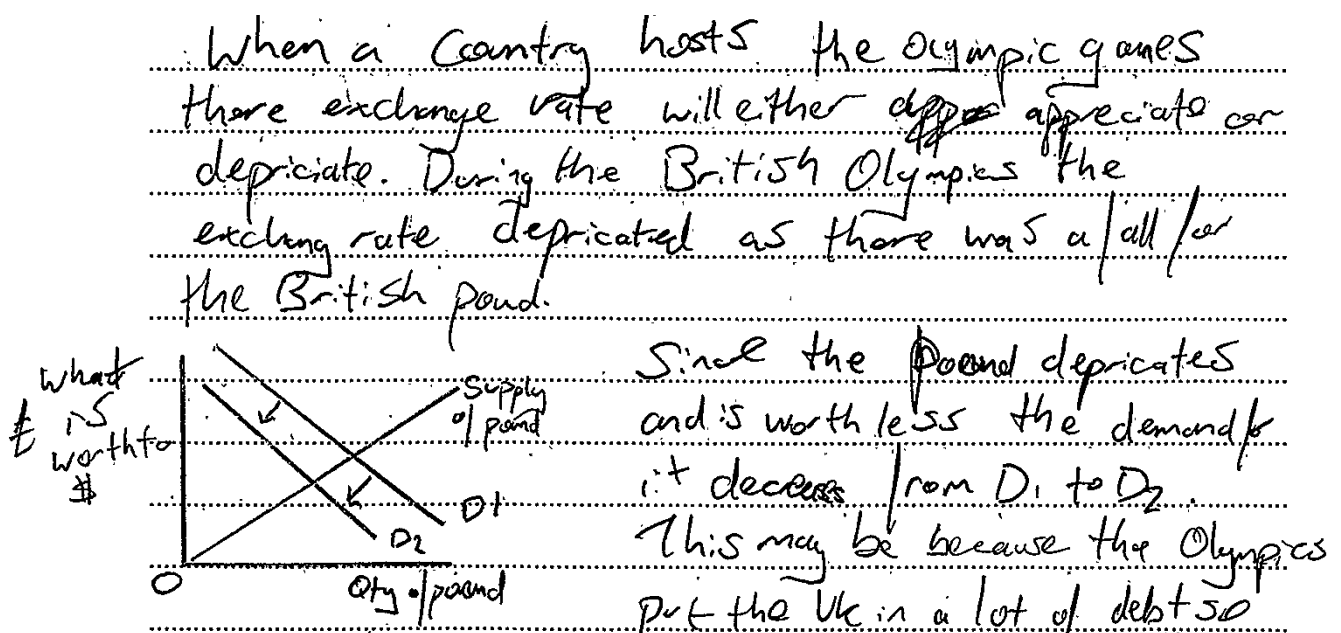


Examiner commentary

The candidate explains the reason for an increase in the demand for the currency (increased tourism) and illustrates the impact on the exchange rate on a diagram, which is accurate and correctly labelled.

Exemplar 2

1 mark



people are less likely to buy the currency of a country in severe debts if it's unstable. [4]

Examiner commentary

One mark is given in Exemplar 1 for correctly labelling an exchange rate diagram (axes and curves), but the candidate misinterprets the data in Figure 2.2 to conclude that there has been a depreciation in the exchange rate.

Question 36

36 Using Fig. 3.1, describe what happened to bicycle prices in the period 2007–2015. [2]

Exemplar 1

2 marks

There was an increase in the price of bicycle overall in the period. The price of bicycle exceeded CPI inflation rate increase in 2009, which means the real value of bicycle increase. However, other years, it's below CPI, which means the real value of bicycle fell from 2007 to 2015 except in 2009. [2]

Examiner commentary

This candidate does consider the date given on the inflation rate in Figure 3.1 and explains what has happened to real prices. The second mark is earned by recognising that the real price was generally falling because nominal bicycle prices were rising by less than the rate of inflation in most years.

Exemplar 2

1 mark

Over the period, the price of bicycles has continued to rise with positive % changes in bikes for every year, except 2012 where the % change in price of bikes was negative, showing there was a fall in price of bikes in that year. [2]

Examiner commentary

In this exemplar the candidate demonstrates that they understand what has happened to nominal bicycle prices over the period, recognising that they have increased in all years other than 2012. However, there is no consideration of the data given on the inflation rate in Figure 3.1, meaning they have not explained what has happened to real prices.

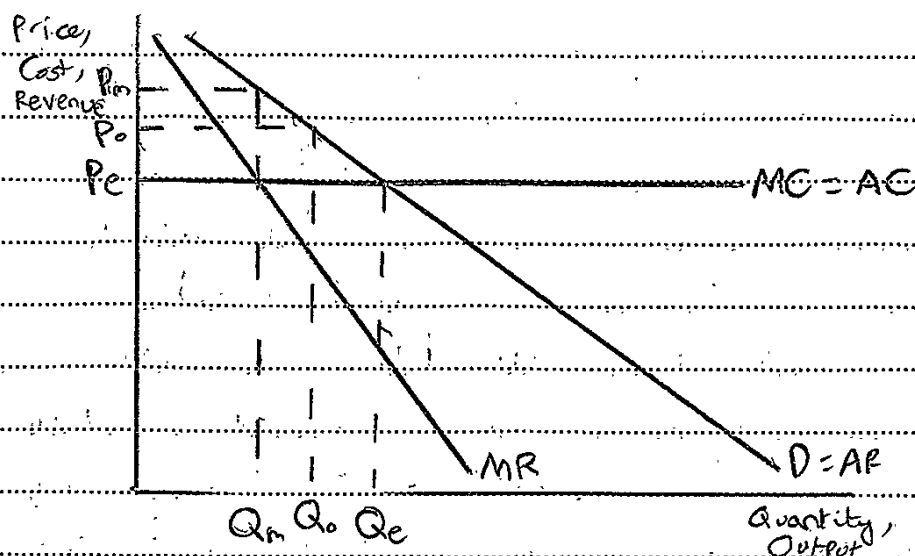
37 Evaluate, using an appropriate diagram, the extent to which consumer welfare is harmed as a result of the bicycle industry being an oligopoly. **[15]**

15 marks

Under a kinked demand curve model, demand is relatively price elastic up to a quantity Q , after which demand is relatively inelastic. Output is determined where $MC = MR$, with MC passing through the discontinuity of the marginal revenue curve. Firms produce at $MC = MR$ because they will

forgo additional profit at lower levels of output, but will make a loss on any units produced beyond Q . Demand is relatively elastic at outputs below Q . This is because an increase in price by one firm is unlikely to be followed by other firms. Equally, firms will not produce at an output above Q - this is because one firm choosing to lower their price will lead to all other firms also lowering their price, resulting in relatively inelastic demand. Consumer surplus will therefore only consist of the area P_eab , leading to lower consumer welfare compared to other market structures with increased competition.

An oligopoly will also harm consumer welfare through a decrease in allocative efficiency. Firms under oligopolistic competition are characterised by their interdependence and



Strategic behaviour. This will lead to some level of both price- and con-

Price Competition. This means that an oligopoly is likely to produce at an output of Q_0 and a price of P_0 CONTD ON PAPER

P_0 between that under perfect competition and monopoly. As price is not equal to marginal cost, the industry will be not allocatively efficient. This will lead to a dead-weight loss of area bcd (first diagram), some of which will be burdened by the consumer, leading to a decrease in consumer welfare.

However, under a game theory model, oligopoly leads to a high level of consumer welfare.

		Firm A		B	figure on left is A's Profit, right is B's Profit
		High Price	Low Price		
Firm B	High Price	25, 25	30, 5		
	Low Price	5, 30	10, 10		

Initially, both firms (in this duopoly model) will charge a high price. However, it is the dominant strategy of both firms to lower their price, which will increase profit from £25 to £30. As both firms choose to lower their price, a Nash equilibrium where firms minimise total profits is reached. This will lead to consumer welfare being maximised.

Furthermore, these oligopoly models do not take into account changes in the quality of bikes.

Under oligopoly, firms have funds for product innovation as a result

of gaining abnormal profits. This will lead to greater utility for consumers riding the newer bikes. And this increase in price reflects this increase in demand for higher quality bikes. This means that consumer welfare is not harmed.

The bicycle industry has a 3-firm concentration ratio of over 50%. This means that the industry is not very competitive. Overall, it's therefore likely that consumer welfare will be harmed as a result of it being an oligopoly. The extent to which consumer welfare is harmed will depend on whether or not the market is contestable. If the level of barriers to entry or effectiveness of these is low, then firms in the industry may be employing a limit pricing strategy, deterring new firms from entering the industry. This means that firms are not profit-maximising, leading to increased consumer surplus and hence consumer welfare.

Whether or not consumer welfare is harmed will also depend on whether firms choose to collude. If there is a credible punishment strategy, then firms are more likely to collude. This will lead to firms acting collectively as a monopoly. This will lead to a lower output of Q_m (2nd diagram) and a higher price of P_m .

minimising consumer surplus and welfare. ~~If~~ In contrast, if firms compete, the price is likely to be closer to that under perfect competition. In this industry however, there are a small number of firms, making it easier to regulate and control the collusion between firms, so firms are likely to collude, leading to consumer welfare being harmed.

Examiner commentary

Diagrams are used to excellent effect throughout this answer. The candidate offers strong analysis of the implications of an oligopoly by explaining the loss in consumer surplus that occurs as a result of collusion, explained through the kinked demand curve. The candidate later explains that the loss in consumer surplus will be even greater if by colluding the oligopolists are effectively able to operate as a monopolist. A range of arguments are offered in evaluation, firstly through the use of game theory to explain that oligopolists are likely to engage in price wars, which will benefit consumers. The point is also made that even if firms do make supernormal profits this could benefit consumers in the form of better quality bicycles. Finally, the candidate reaches a well developed judgement that argues contestability is an important consideration when evaluating the impact of oligopolies on consumers, as in a contestable market oligopolists will not be able to profit maximise and therefore do the harm that was suggested in the analysis.

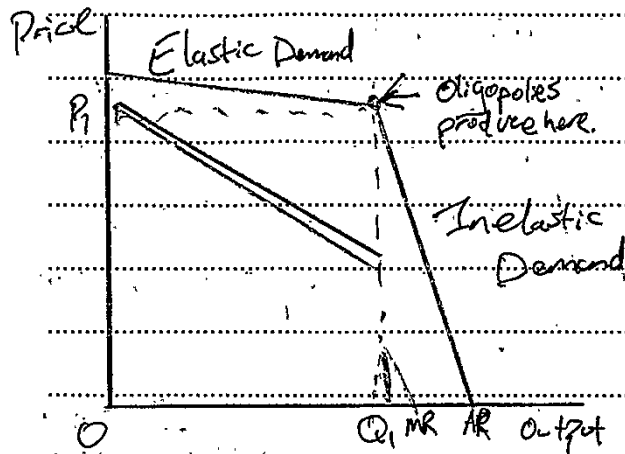
Exemplar 2

9 marks

- 37 Evaluate, using an appropriate diagram, the extent to which consumer welfare is harmed as a result of the bicycle industry being an oligopoly. Collusion
[15]

An oligopoly occurs when there are only a few firms in that market. For the example the bicycle industry is an oligopoly as there are only a few big suppliers of bikes who hold a high market share. ~~then~~ There are only a few firms in an oligopoly as there are high barriers to entry and exit making it very hard for new firms to join the market and drive down prices, thus since there are so few suppliers prices can be quite high. This harms consumer welfare as prices are higher than they need to be allowing

Oligopolies ~~to make~~ have the potential to make supernormal profit. Oligopolies are however likely to suffer from price rigidity preventing prices from being put too high. This can be explained by the kinked demand curve:



Oligopolies will produce here as due to the kinked demand curve we know that if they raise their prices then demand will be elastic as consumers will shop elsewhere at

another firm as the other firms won't raise their prices. If the oligopoly chooses to reduce their prices demand becomes inelastic as this will cause the other firms in the market to price "undercut" them and this may cause a price war as all the firms try and set their prices lower. Since an oligopoly thus cannot change their prices without significantly decreasing demand, price rigidity occurs which is beneficial for consumer welfare as prices do not rise too high as oligopolies cannot afford to without seeing a large fall in demand.

Consumer welfare may be harmed by oligopolies if they choose to collude. Collusion is when ~~the~~ the oligopolies in that market come together and all raise prices at the same time so demand is less affected as the consumers cannot

go to a substitute firm as all prices have been risen rather than just one of the firms. This colluded price rise will increase the oligopolies profit margins, as they will be receiving more for the goods they sell. This will decrease consumer welfare as they are being charged more for a good and are thus having to spend more of their income.

Overall an oligopoly should harm a consumer's welfare as they have the ability to set high prices, however due to price rigidity this may not always be the case.

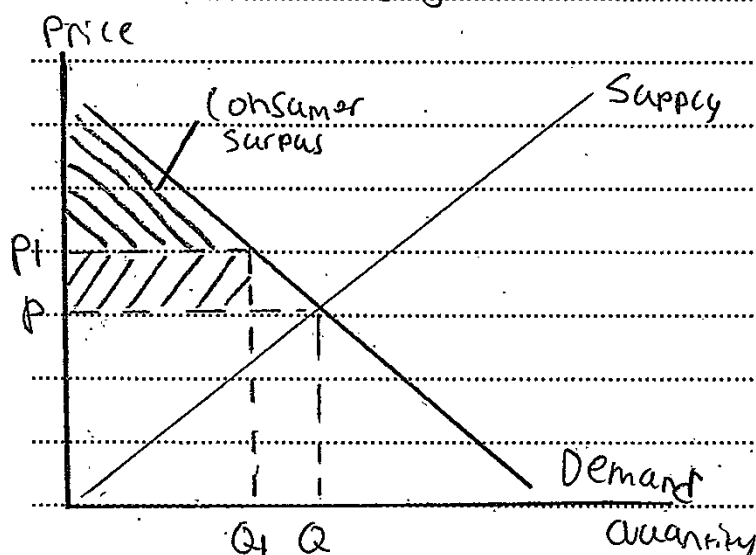
Examiner commentary

The candidate shows good knowledge and understanding of the model of oligopoly applied to the bicycle industry at the start of the answer. The statement that consumer welfare is harmed as a result of oligopolies making a supernormal profit is credited as limited analysis, but the opportunity to be credited as analysis at a higher level is lost by missing the key insight of kinked demand curve theory. Whilst the candidate uses the kinked demand curve to conclude that consumers will benefit from stable prices (for which they are credited with limited evaluation), they could have used it to illustrate the incentive for collusion and therefore high prices. In the following paragraph the reference to collusion causing high prices is enough to take the analysis to reasonable, but this could have been higher had this explanation been integrated with the discussion of the kinked demand curve. The judgement does not take the answer any further as it is simply a restatement of the points made earlier.

Exemplar 3

5 marks

The bicycle market has seen rapid growth since the gold medal winning performance in the 2012 Olympics.



The diagram above shows the increase in price from P to P_1 as a result of the bicycle industry being an oligopoly.

The increase in price also shows the reduction in consumer surplus from P to P_1 , this shows that consumer welfare is harmed as a result of lack of

competition. Evans Cycles, Hectors and Wiggle dominate the market accounting for 50% of the ~~market~~ market share

between them, this may mean there is collusion to increase prices as there is now increased demand, this is proven as customers are willing to purchase £12,000 bikes. Wiggles recent takeover of a rival chain further increases the oligopoly's power as well as increasing the barriers to entry as set up costs will increase.

~~However~~ However the rising price may be due to bicycle equipment improving dramatically over the years. The increase in innovation such as electronic gears and carbon fibre means modern day bicycles are incomparable with those on sale 20 years ago. The amount of independently owned bike shops increasing by over 10% over the past decade it is clear firms see a opportunity in the expanding market.

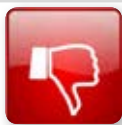
The increase demand for bikes is due to

a desire to ease traffic congestion, reduce pollution and improve the health of the population. The inflation rate shows that the price of petrol and cars are rising, but bikes are sustainable.

Overall, I believe consumer welfare is harmed as a increase in oligopoly power, this is due to the rising prices and lack of competition and ~~collusion~~ collusion. ~~to the~~

Examiner commentary

Limited analysis is offered as there is recognition that collusion can result in high prices. This is applied to the bicycle industry with reference to the firms mentioned in the case study. However, no oligopoly diagram is presented. The answer would have benefited from use of kinked demand curve theory. The answer moves on to offer limited evaluation by suggesting that rising prices may not have been caused by oligopolists exploiting their market power but instead as a result of improvements in the quality of bicycles.



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