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Pearson Edexcel
International
Advanced Level

Centre Number

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Economics
International Advanced Level
Unit 3: Business Behaviour

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| Sample Assessment Material Time: 2 hours | Paper Reference SAM |
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You do not need any other materials.

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| Total Marks |
|-------------|

Instructions

- Use **black** ink or ball-point pen.
- **Fill in the boxes** at the top of this page with your name, centre number and candidate number.
- Answer **two** questions from Section A and **one** question from Section B.
- Answer the questions in the spaces provided
– *there may be more space than you need.*

Information

- The total mark for this paper is 80.
- The marks for **each** question are shown in brackets
– *use this as a guide as to how much time to spend on each question.*
- In your responses, you should take particular care with punctuation and grammar, as well as the clarity of your expression.
- Calculators may be used.

Advice

- Read each question carefully before you start to answer it.
- Check your answers if you have time at the end.

Turn over ►

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Section A: Answer TWO questions from this section.

You should spend 60 minutes on this section.

You should include diagrams in your responses where appropriate.

- 1** Examine the significance of the distinction between fixed costs and variable costs for a firm's decision on whether to continue in business or close down. (20)
- 2** "Monopolies result in a misallocation of resources compared with competition, and should therefore be broken up". Explain and critically examine this reasoning. (20)
- 3** Assess the ways by which a government might promote the international competitiveness of its country's businesses. Include reference to the measurement of international competitiveness in your answer. (20)
- 4** Discuss whether product differentiation under conditions of monopolistic competition can benefit both firms **and** consumers. Refer to examples in your answer. (20)

Do not use pencil. Use black ink or ball point pen.

Put a cross in the box indicating the question from Section A that you have chosen for your FIRST essay. If you change your mind, put a line through the box and then indicate your new question with a cross .

You must answer TWO questions in this section. Please start your second essay on page 8.

Essay Choice 1:

Question 1

Question 2

Question 3

Question 4

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(Total for Question = 20 marks)

Put a cross in the box indicating the question from Section A that you have chosen for your SECOND essay. If you change your mind, put a line through the box and then indicate your new question with a cross .

Essay Choice 2: (This must be different from your first essay response.)

Question 1

Question 2

Question 3

Question 4

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(Total for Question = 20 marks)

TOTAL FOR SECTION A = 40 MARKS

Section B: Answer either Question 5 or Question 6.

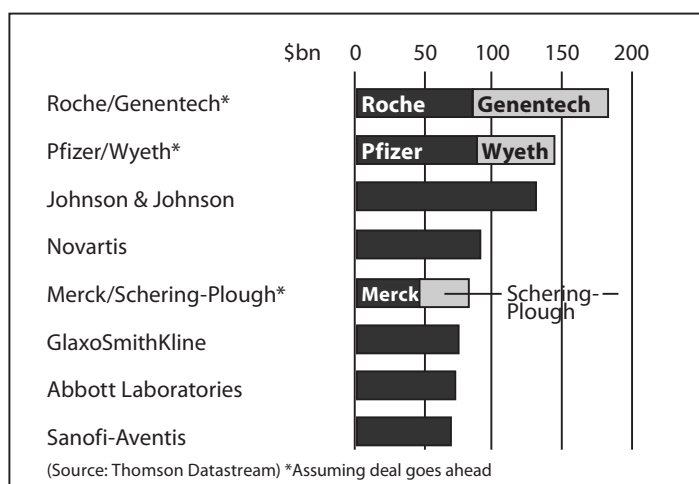
If you answer Question 5 put a cross in this box .

Question 6 starts on page 23.

You should spend 60 minutes on this section.

5 The Pharmaceutical Industry

Figure 1 Global Pharmaceutical Companies by market capitalisation, March 2009, \$bn



Extract 1 Merck's manoeuvres

In recent times there has been a series of mergers between pharmaceutical companies. Merck, a US company, has agreed to take over Schering-Plough; Pfizer is acquiring Wyeth; and Roche, a Swiss pharmaceutical company, is paying \$46.8bn for 44% of Genentech, an American firm.

Big drugs companies hope mergers and takeovers will solve their various problems: the lack of new blockbuster drugs coming through their research pipelines; competition from generic (non-brand name) drugs as patents expire, the global economic crisis, and an over-dependence on sales in America, where health-care reforms are likely to reduce profit margins. However, the evidence suggests that many of the supposed benefits of pharmaceutical mega-mergers fail to materialise: bigger firms are no better at innovation, and are often worse. But bosses are pressing ahead anyway.

The main attraction of buying Schering-Plough is that Merck will double (to 18) the number of drugs it has in late-stage development. Merck will also strengthen its international and over-the-counter sales, both areas where Schering is strong (70% of its revenues come from outside America). In addition, Mr Clark, who will become the boss of the new company, promises that there will be cost savings of \$3.5 billion a year after 2011. But this sounds unlikely, given that both companies are already cutting costs heavily. And if the two firms' research teams are so complementary and do not overlap much, as Merck claims, who is going to get sacked?

The deal does at least answer critics who complained that Merck was not acting as vigorously as competitors in buying rivals and moving into new markets. But it also represents a change in strategy for Merck, which unlike many of its competitors has stayed on the sidelines during the industry's previous waves of mega-mergers. Instead, the company has always preferred to grow by developing new products in its laboratories. The task for Mr Clark will be to make the deal go smoothly, despite his lack of experience with big mergers. 25

(Source: Adapted from 'Merck's manoeuvres' published in *The Economist*, 13 March 2009)

Extract 2 Letter from the Consumers Union to the Federal Trade Commission in the USA

Dear Sir:

On behalf of the Consumers Union, we urge you to review carefully the competitive and innovation consequences of the proposed Pfizer-Wyeth pharmaceutical company merger. Our members consistently tell us that high and ever-rising health care costs are a major household fear, and high brand name prescription drug prices are a particular concern. 25

We urge the Federal Trade Commission to review this proposed merger and its impact on

- long-run competition in the pharmaceutical industry and its likely impact on drug prices; 30
- innovation and the development of new, breakthrough drugs.

The merger will result in thousands of employee redundancies. What percent of those lay-offs are in research and development, and are those lay-offs strictly in areas where the two companies were duplicating research, or are new and unique lines of research being terminated? 35

We are faced with continual abuses of good public policy by many in the industry. For example, some firms use payments to buy delays in the entry of competitive generic drugs into the market.

We hope that you will consider a major study of the entire pharmaceutical industry. Why are prices for consumers so high, why has the breakthrough drug pipeline slowed down, and what policies should we pursue as a nation to encourage the more rapid discovery of affordable medicines? Is this merger between Pfizer and Wyeth good or bad for the goal of affordable, new, life-saving drugs? 40

Thank you for your consideration of these views.

Sincerely, 45
William Vaughan
Health Policy Analyst
Consumers Union

(Source: <http://www.consumersunion.org/pub/campaignprescriptionforchange/009344.html>)

- (a) What does the information provided suggest is the market structure of the pharmaceutical industry? Explain your answer. (4)
- (b) Assess the strengths and weaknesses of Merck being dependent on a growth strategy of 'developing new products in its laboratories' (Extract 1, lines 24–25). (12)
- (c) Evaluate **one** pricing and **one** non-pricing strategy that Merck could adopt to increase sales. (12)
- (d) To what extent would further mergers and takeovers in the pharmaceutical industry be in the best interests of consumers and employees? (12)

(a) What does the information provided suggest is the market structure of the pharmaceutical industry? Explain your answer.

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(b) Assess the strengths and weaknesses of Merck being dependent on a growth strategy of 'developing new products in its laboratories' (Extract 1, lines 24–25).

(12)

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(c) Evaluate **one** pricing and **one** non-pricing strategy that Merck could adopt to increase sales.

(12)

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(d) To what extent would further mergers and takeovers in the pharmaceutical industry be in the best interests of consumers and employees?

(12)

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(Total for Question 5 = 40 marks)

If you answer Question 6 put a cross in this box .

6 Iberia and BA merger

Extract 1 Uniting in the sky – Iberia and BA at last agree to get together to sort out their problems



Like two drowning men, Iberia and British Airways (BA) have long seen each other as potential means of staying afloat. The rate at which the airlines have been sinking at last forced them into each other's arms on November 12th 2009, when a merger was agreed. BA made big pre-tax losses in the year to the end of March as it suffered from the credit crisis and the global economic slump. Iberia actually managed a small profit in 2008. Just as the terms of the merger were agreed Iberia announced a loss in the latest quarter, which includes the usually profitable summer months. BA said that it had lost £292m in the first half of the year, which includes the summer period.

5

These airlines are not alone in their concerns. The total losses for the world's airlines this year are estimated to be £17.6 billion. By agreeing to merge, the two firms will join the trend for big European airlines to get bigger. This has become an attractive means to make substantial cost savings as they compete against low-cost rivals and try to cope with a dramatic fall in numbers of the profit-making business passengers. The two companies estimate that within five years the new group will save some £429m a year by cutting overlapping routes, and by combining maintenance, office functions and business-class lounges. They may also have more buying power when it comes to negotiations to buy new planes from Boeing and Airbus.

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The deal will put the firms back into the big leagues of European aviation. Their combined revenues will put them closer to Air France-KLM, the product of a similar deal in 2004 and Germany's Lufthansa, which has expanded its operations with a series of smaller takeovers of Swiss and Austrian airlines since 2005. Iberia and BA will combine their businesses but maintain separate corporate operations. This will allow them to maintain their roles as the national flag-carriers in Spain and the UK while keeping valuable bilateral international landing rights that go along with that status.

20

One reason for keeping pace with European rivals is that size will become an important factor if consolidation among airlines goes global. The two airlines are already seeking permission from the competition authorities in America and in Europe for an agreement with American Airlines, which would see all three co-ordinating over costs and revenues on transatlantic routes. However, BA may be required to give up landing slots at Heathrow, a price it has been unwilling to pay in the past. 25
30

A protectionist stance in America over the country's troubled airlines has kept a law in place that prevents foreign airlines from owning more than 25% of an American rival. The European Union is pressing for this restriction to be lifted, though there is little sign that it might happen soon. 35

(Source: adapted from Economist.com 'Uniting the Sky' 13 November 2009, http://www.economist.com/businessfinance/PrinterFriendly.cfm?story_id=14887815)

Extract 2 Strike action in response to BA crew reductions and cost cuts

British Airways was preparing for what could be a damaging strike after workers voted to walk out for nearly two weeks. The airline plans to reduce generous staff levels and benefits for Heathrow-based cabin crew.

The union said 80 per cent of its more than 12,000 BA members had voted, recording a 92.5 per cent vote in favour of a strike. The airline has said the move would cause chaos for hundreds of thousands of passengers. 5

"We're hoping that the size of this vote will make the company think again," said a spokesperson for the union, who added that it would not back down unless BA gave way on the crew reductions that prompted the strike.

(Source: <http://www.ft.com/cms/s/0/75a53942-e8aa-11de-9c1f-00144feab49a.html>)

- (a) Using the evidence, explain the type of integration involved in the agreed merger between BA and Iberia. (4)
- (b) Examine the likely reasons why Iberia made a loss during 'the usually profitable summer months', (Extract 1, line 7). Use a diagram to support your answer. (12)
- (c) Assess the likely impact on contestability of the airline industry resulting from the mergers and agreements referred to in the evidence. (12)
- (d) Evaluate the likely benefits of the agreed merger between BA and Iberia. (12)

(a) Using the evidence, explain the type of integration involved in the agreed merger between BA and Iberia.

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(c) Assess the likely impact on contestability of the airline industry resulting from the mergers and agreements referred to in the evidence.

(12)

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(d) Evaluate the likely benefits of the agreed merger between BA and Iberia.

(12)

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(Total for Question 6 = 40 marks)

TOTAL FOR SECTION B = 40 MARKS
TOTAL FOR PAPER = 80 MARKS

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