Past-paper walk-through

Growth and survival of firms ▪ 7.7

eXercise

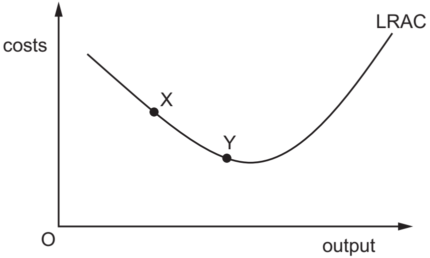
Questions in this set

- 9708/31 N25 Q2 ▪ 1 mark
- 9708/34 N25 Q3 ▪ 1 mark

Question 2

9708/31 N25 ▪ Q2 ▪ 1 mark

2 A small European airline currently produces at point X on its long-run average cost curve (LRAC). It wants a bigger share of the European airline market and proposes to merge with another small European airline. The newly merged firm would produce at point Y on the long-run average cost curve, as shown.



Question 2

Why might the newly merged firm be able to produce at point Y?

A The new airline can negotiate discounts when buying fuel.

B The new airline has many layers of management.

C The new airline is unable to hire enough pilots.

D The workforce of the new airline lacks morale and is demotivated.

Solution 2

Answer: **A**

Why

- Point X is on the downward-sloping part of the LRAC curve, so there are economies of scale still to exploit.
- Merging raises output, which moves the firm further down the curve.
- So average cost falls – the merger is justified by economies of scale.

Question 3

9708/34 N25 ▪ Q3 ▪ 1 mark

3 What is an example of forward vertical integration?

A A firm manufacturing computers merges with a firm that manufactures furniture.

B A firm manufacturing computers merges with a firm that manufactures silicon chips for computers.

C A firm manufacturing computers merges with a retail outlet that sells computers.

D A firm manufacturing computers merges with another firm that also manufactures computers.

Solution 3

Answer: **C**

Why

- Vertical integration joins firms at different stages of the same production chain.
- *Forward* means moving towards the customer – towards retail or distribution.
- So a computer maker merging with a computer retailer is forward vertical integration.