



ADVANCED SUBSIDIARY GCE
ECONOMICS
 The Market System

2881

Candidates answer on the Answer Booklet

OCR Supplied Materials:

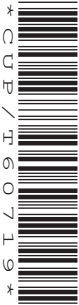
- Designated Answer Booklet [2881/AB]

Other Materials Required:

None

Wednesday 3 June 2009
Afternoon

Duration: 1 hour



INSTRUCTIONS TO CANDIDATES

- Write your name clearly in capital letters, your Centre Number and Candidate Number in the spaces provided on the Answer Booklet.
- Use black ink. Pencil may be used for graphs and diagrams only.
- Read each question carefully and make sure that you know what you have to do before starting your answer.
- Answer **all** the questions.
- Write your answers in the separate Answer Booklet provided.
- Do **not** write in the bar codes.

INFORMATION FOR CANDIDATES

- The number of marks is given in brackets [] at the end of each question or part question.
- The total number of marks for this paper is **45**.
- The quality of your written communication will be taken into account in marking your answer to the question labelled with an asterisk (*).
- This document consists of **4** pages. Any blank pages are indicated.

Answer **all** parts of this question in the accompanying answer booklet.

Mediterranean holidays on offer for £5

Package holidays to Mediterranean resorts are being sold for as little as £5 because there have been so few bookings for early summer. Such is the surplus of package holidays to Greece, Spain and, in particular, Turkey that companies are frantically trying to off load dozens of last minute deals for holidays starting in a few days time. Prices are also being heavily discounted for holidays to be taken later this month – £30 to £80 is the typical cost of a one week self-catering accommodation and flight deal.

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Many tour operators are facing serious threats to their businesses. These threats are on both the demand and supply sides of their markets.

- On the demand side, the huge growth in low-cost flights across Europe, and the fact that now over half of UK households have broadband access, has seen more and more people booking holidays on the Internet. In the current crisis, 'silver surfers', as the over 55 age group is known, have been particularly blamed for the fall in demand. Demand is clearly becoming more price elastic.
- Despite cutting back on supply to maintain prices, package tour operators have a 'fixed cost' problem. This is because certain parts of the package, mainly flights and accommodation, have to be contracted long before the holiday takes place. There is only limited potential, therefore, for minor savings to be made on variable costs such as transport to and from airports. Consequently, fixed costs can account for as much as 80 per cent of the price of a package holiday. This is of particular concern at present given the spiralling costs of aircraft fuel, which is typically as high as two thirds of total fixed costs.

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In theory, package tour operators are seeking to maximise their profits. In reality, as recent business failures have shown, this is not an objective which many firms are achieving in current market conditions.

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- (a) (i) Describe what is meant by a market. [2]
- (ii) How is the price of package holidays determined in the market? [2]
- (b) (i) Using the information provided, state and explain **two** reasons for the fall in demand for package holidays. [4]
- (ii) Using a demand and supply diagram, show how the fall in demand for package holidays has affected the market price. [4]
- (c) Tour operators have reduced supply in order to maintain prices. Using a diagram, explain the effect of a reduction in supply on the market. [5]
- (d) (i) Define the term price elasticity of demand. [2]
- (ii) Explain why the price elasticity of demand for package holidays 'is becoming more price elastic'. (lines 14–15) [4]
- (e) Comment on **one** alternative objective to profit maximisation which package holiday firms might pursue in the current market conditions. (lines 25–27). [6]
- (f) (i) Using examples from the information provided, explain the difference between the fixed costs and variable costs of a package holiday. [4]
- *(ii) Discuss the likely effects of a substantial increase in the cost of aircraft fuel on the market for package holidays. [12]

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