IGCSE ECONOMICS · 1.2 BUSINESS ECONOMICS · CHAPTER 17 · PAPER 1

Economies and Diseconomies of Scale

Topic question sheet L17 | **Total: 32 marks** | **Time: 35 minutes** | **Student Book pp. 124–131**

Instructions: answer **all** questions. Write your answers on lined paper. The marks for each question are shown in brackets: use them as a guide to how much to write.

Calculators may be used. Show your working. Draw diagrams in pencil and label them fully. The mark scheme starts on a new page: do not look at it until you have finished.

Section A: Multiple choice

One mark each. Choose **one** answer: A, B, C or D.

1 Employing a specialist cost accountant in a growing business is an example of a: **(1)**

A technical economy
B risk-bearing economy
C managerial economy
D marketing economy

2 Internal economies of scale cause: **(1)**

A falling total costs
B rising average costs
C rising variable costs
D falling average costs

3 Which of the following is an external economy of scale? **(1)**

A Bulk buying
B A local pool of skilled labour
C Cheaper loans for a big firm
D Specialist managers

4 Which of the following is a diseconomy of scale? **(1)**

A Bulk-buying discounts
B Lower interest rates
C Communication problems
D Wider product range

Section B: Short answers

Define, state, calculate, draw and explain. Show your working for calculations.

5 What is meant by **economies of scale**? **(2)**

6 Calculate the percentage fall in Golden Grain's average cost in the first year. You are advised to show your working. **(2)**

7 Draw a long-run average cost curve, labelling economies and diseconomies of scale. **(3)**

8 Explain how risk-bearing economies of scale can lower a firm's costs. **(3)**

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Section C: Data response

Read the extract, then answer the questions. Use evidence from the extract in every answer.

Extract: Golden Grain Rice Mills

Golden Grain owns 3 rice mills in Thailand. Last year it bought 12 smaller mills from rival firms. Because it now buys rice from thousands of farmers, it pays 8% less per tonne than before. It has also hired specialist finance and marketing managers.

However, decisions now have to pass through four layers of management, and mill managers say head office does not understand local problems. Average cost per tonne fell from THB 9000 to THB 7800 in the first year, but has risen to THB 8200 this year.

Fictional case, written for this sheet.

9 With reference to the extract, analyse **two** internal economies of scale that Golden Grain gained from its expansion. **(6)**

10 With reference to the extract, evaluate whether Golden Grain has grown too big. **(12)**

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Mark scheme: Economies and Diseconomies of Scale

How to mark: Multiple choice, Define, State: 1 mark. **What is meant by** (2): two separate parts to the definition. **Calculate**: working and answer (with units). **Draw** (3): one mark per correct labelled feature. **Explain** (3): 1 for a point, 2 for developing it in context. **Analyse** (6): knowledge 2, application 2, analysis 2. **Assess** (9) and **Evaluate** (12) are marked by levels: choose the level that best fits the whole answer. Indicative content is a guide: credit other valid points.

Section A

1 *Employing a specialist cost accountant in a growing business is an example of a: (1 mark)*

Answer: C (managerial economy). Specialist managers are a managerial economy.

2 *Internal economies of scale cause: (1 mark)*

Answer: D (falling average costs). Economies of scale lower average costs.

3 *Which of the following is an external economy of scale? (1 mark)*

Answer: B (A local pool of skilled labour). It benefits all firms in the area.

4 *Which of the following is a diseconomy of scale? (1 mark)*

Answer: C (Communication problems). Communication problems raise costs.

Section B

5 *What is meant by economies of scale? (2 marks)*

Falling average costs (1) as a firm expands/increases its scale (1).

6 *Calculate the percentage fall in Golden Grain's average cost in the first year. You are advised to show your working. (2 marks)*

Working: (7800 − 9000) ÷ 9000 × 100 (1).

Answer: −13.3% (1).

7 *Draw a long-run average cost curve, labelling economies and diseconomies of scale. (3 marks)*

Diagram: axes labelled average cost and output (1); U-shaped curve (1); economies labelled on the falling part and diseconomies on the rising part (1).

8 *Explain how risk-bearing economies of scale can lower a firm's costs. (3 marks)*

Point: large firms sell a wider range of products or in more markets (1).

Development: a fall in sales in one market is offset by others (1), so the firm is more stable and can borrow and plan more cheaply (1).

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Section C

9 *With reference to the extract, analyse two internal economies of scale that Golden Grain gained from its expansion. (6 marks · K2 · Ap2 · An2)*

Knowledge (2): purchasing and managerial economies.

Application (2): pays 8% less per tonne for rice; hired specialist finance and marketing managers.

Analysis (2): bulk buying lowers cost per tonne; specialists make better decisions and raise efficiency; so AC fell from THB 9000 to 7800.

Knowledge 2 · Application 2 · Analysis 2.

10 *With reference to the extract, evaluate whether Golden Grain has grown too big. (12 marks · levels)*

Yes: AC has risen from 7800 to 8200; four layers of management (bureaucracy); head office far from mill managers (distance, communication).

No: AC is still below the original 9000; purchasing and managerial economies remain; problems may be fixed by delegating decisions to mill managers.

Judgement: signs of diseconomies, but not yet too big; it should reduce layers of management; depends on whether costs keep rising.

Levels: L1 1–3 · L2 4–6 · L3 7–9 · L4 10–12 (balanced, well-developed arguments using the data throughout, and a justified conclusion that answers the question).

Original practice questions written in the style of the Pearson Edexcel International GCSE Economics (4EC1) papers. This is not an official paper. Unless a source is given, the firms, countries and figures are fictional and made up for practice.

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