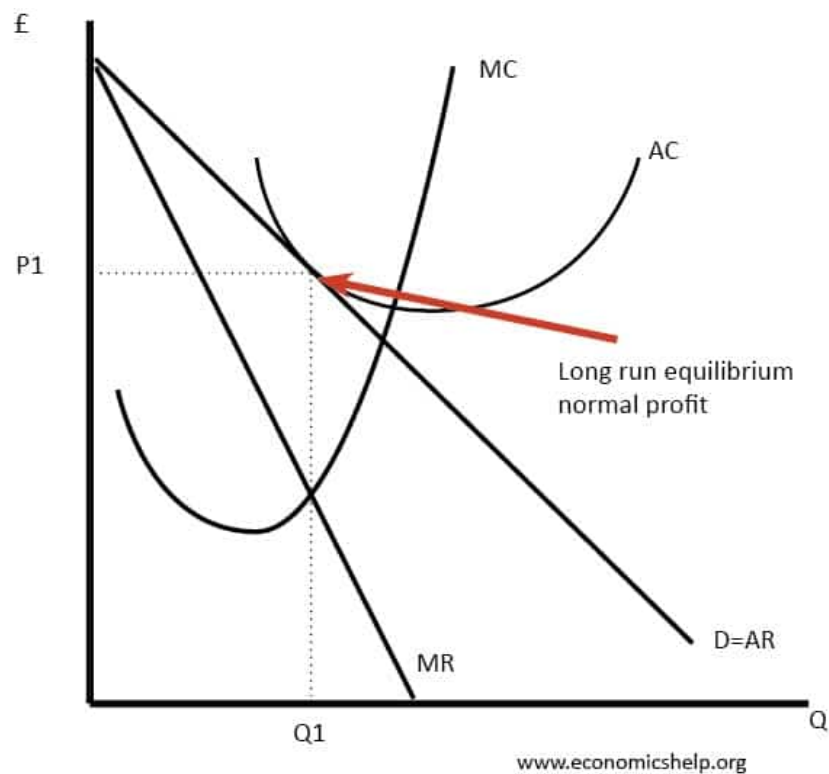


monopoly diagram



- 1) Draw the D=AR curve
- 2) Draw the MR curve (which is twice as steep)
- 3) Draw the MC curve
- 4) Mark the profit max level of output (MR=MC)
- 5) Determine profit max price
- 6) Then draw AC curve to determine:
 - super normal profit (AR > AC)
 - normal profit (AR = AC)
 - subnormal profit (AR < AC)

3 objectives of the firm

- 1) Profit maximising (MR=MC) at Q1
- 2) Revenue maximise (MR = 0) at Q2
- 3) Sales maximising (AR=AC) at Q3

sales maximising is the most a firm can sell whilst not making a loss

Competition

Monopolistic competition is when there are lots of firms all producing slightly different goods or services

notes for 25 marker on markets:

- monopolies good for producers > control prices
- monopolies bad for producers > no competition, so they become complacent
- monopolies bad for consumers > extortion

show consumer surplus on a graph - monopolies good for consumers
money means research, thus innovation

means more choice

as average costs fall, they can pass it on to the consumer, or expand their markets and benefit more consumers by giving them more choice, eg we can import fruit all year round now

benefit from economies of scale

Efficiency

Productive efficiency is when an economy cannot produce any more of one thing without making less of another, when all resources are being employed efficiently

Allocative efficiency is when the production in an economy reflects the producers wants

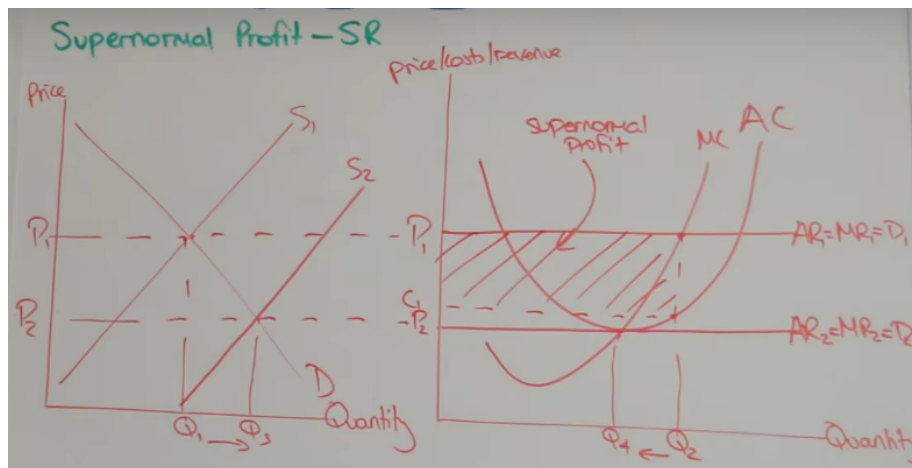
Dynamic efficiency is productive efficiency in the long run

Static efficiency is when an economy is being both productively and allocatively efficient

x-inefficiency is when, due to market conditions, the producer chooses to endure higher average costs, (anything within the AC curve). eg public firms maximising the public's utility

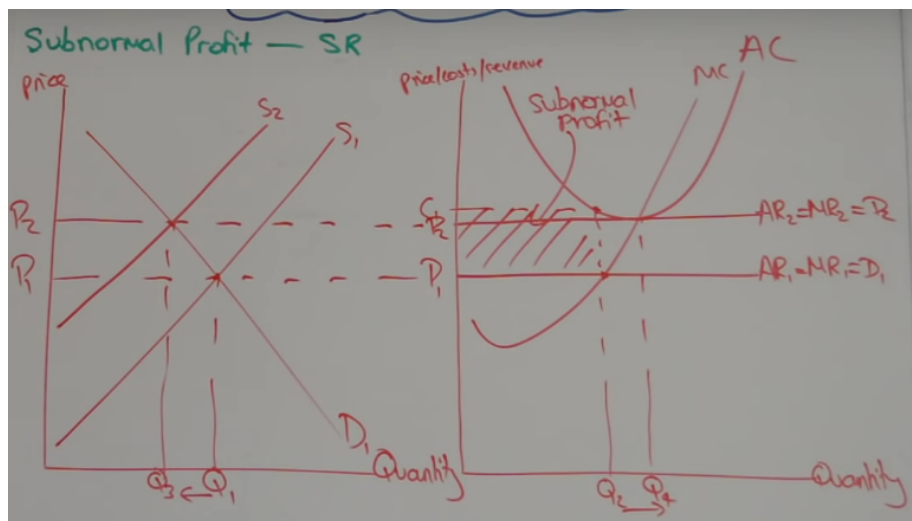
Diagrams

Super normal profit in the Short Run



- Super normal profit can be made in the short run as the market has not equalibrated.
- As more firms join the market, supply shifts left
- This means $AC = AR$, therefore normal profit is made in the **LR**

Sub normal profit in the **Short run**



- As more firms leave the market, due to subNP, allowed by no barriers to exit, supply shifts left
- this pushes prices up and in the **LR** means $AC = AR$ and normal profit can be made

Perfect competition

Best example of real perfect competition is a street market, eg fruit stalls

Perfect competition is based on 4 examples: 1) **Many buyers and many sellers**, each firm is too small to affect the price, they are price takers. 2) **Perfect Knowledge**, all information is available to producers and consumers 3) **No barriers of entry/exit**, firms can enter and leave markets without restriction 4) **Homogeneous output**, all firms produce identical output, there are no brands, consumers are happy to buy the output of any firm

Hit and run competition is when a firm joins a market and leaves immediately as the super normal profits are exhausted.

In a Perfect market it is possible to make Super normal in the **short run** because capital is fixed.

In a perfect market it is *impossible* to make super normal in the **long run**

“Perfectly competitive markets are likely to generate efficiency gains” Explain this statement [12 marks]

- K - productive efficiency gains due to assumptions
- A - eg fruit sellers market take a price of £1 each
- A - super normal profits signal no barrier to entry
- Analysis - no resources wasted
- Eval - impossible to make SNP
- Eval - no dynamic efficiency
- K - PC markets = allocative efficiency
- A - homogeneous product
- A - perfect knowledge
- Analysis - consumer price falls, surplus increases
- Eval - however transport costs
- Eval - charge higher profits for convenience

Explain the role of profit in the economy [15 marks]

- K - Signal \rightarrow SNP ($AR > AC$)
- A Example - SNP earned by Samsung, encourage Apple to allocate more capital + labour to enter the IoT market.

- A - Do an S/D graph of **contextual** fall of supply as apple enters market
- A2 - Explain what the result the graph shows **and** how this shows role of profit in econ
- Eval - However signal function depends on Barriers to Entry.
- Eval- eg brand loyalty reduces the impact of profit as a signal

always take KAA and Eval back to the question

- K -
- A -
- A -

PC markets are good for consumer because low prices **HOWEVER** there is no reason for firms to innovate or decrease LR costs because of the perfect knowledge assumption, meaning consumers will not experience long run benefits

Monopoly

Monopoly is a single firm operating in the market, eg microsoft

Legal monopoly a single supplier by law, eg royal mail

Universal Postal Service Obligation if a letter/parcel is below a certain size, the service *must* deliver it anywhere in the last 50 yards.

Natural monopoly only a single firm can efficiently provide the good or service (eg network rail, national grid, theams water), this is because sunk costs are too high

Monopoly power any firm controlling 25% or more of the market. or “a protected differentiated output. The ability to set the price”

Monopolists do not produce at minimum AC, they fail to achieve productive efficiency

Monopolies charge a price greater than marginal cost of production, they fail to achieve allocative efficiency

Monopolists earn supernormal profit which they can use to invest in R&D, they are likely to achieve dynamic efficiency

Monopolies exist because of barriers to entry

Barriers to Entry/Exit

Legal

- 1) Patents, new firms cannot use tech or methods
- 2) Licences or permits, new firms cannot afford

- 3) Standards and regulations, high costs to meet these
- 4) Insurances, high costs

Technical

- 1) Start up costs
- 2) sunk costs (costs that cannot be recovered when a company leaves a market, eg advertising or specialist equipment)
- 3) Economies of scale, makes it hard for new firms to enter
- 4) Natural monopolies, makes sense for only one firm

Strategic

- 1) Predatory pricing
- 2) Limit pricing
- 3) Heavy advertising

Brand loyalty

- 1) it exists

Barriers to exit:

- redundancy costs
- penalties for leaving contracts early
- sunk costs

Essay tips:

On a monopoly diagram - show profit maximisation, show SNP - show what profit would be in LR ($AR=AC$) (normal profit) - say why its bad for consumer

Monopolies: - bad: restrict output, worst produce

inelastic demand / elastic supply means **consumer** will be hurt by taxes, but benefit from subsidies

elastic demand / inelastic supply means **producer** will be hurt by taxes, but benefits from subsidies

Explain why monopolists are able to earn supernormal profit in the long-run, while perfectly competitive firms can only earn normal profit [15marks]

K - Barriers to entry, prevent new firms entering monopolistic market

A - Facebook, brand loyalty

A - analyse graph below

Graph - Monopoly diagram showing making SNP due to no supply

Eval - However may not want to make SNP in long run due to reducing regulatory body inspections

Eval - regulations can increase costs LR

K - Monopolies are price makers and competitive firms are price takers

A - in a fruit market, they cannot charge more than the person next to them without losing customers

A - talk about the curve

Graph - Making normal profit on a curve

Eval - Transport costs

Eval - realistically no, no perfect knowledge

Why Profit max \neq Revenue max \neq cost minimisation

- 1) average cost minimisation means you need to increase output.
- 2) To turn output into profit you need to sell it.
- 3) To sell the output, you must decrease your price (law of demand).
- 4) profit margins fall.

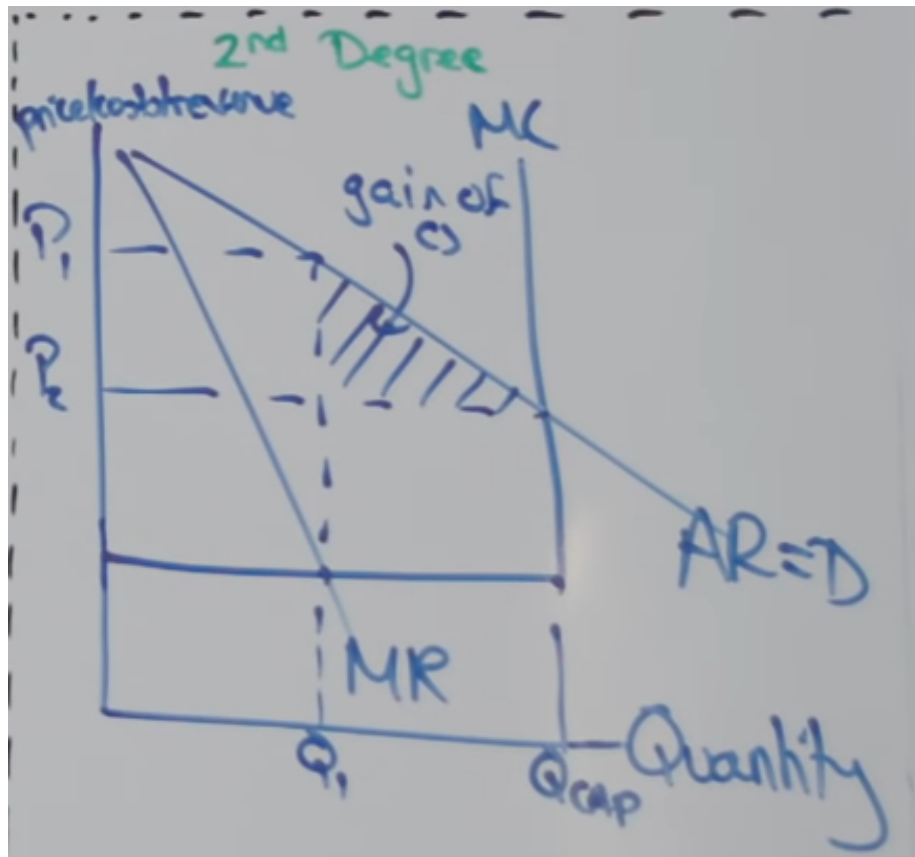
A **deadweight welfare loss** is the consumer and producer surplus lost that cannot be recovered

Price discrimination is when a firm charges different prices, for different consumers, with identical good/services, and no difference in cost of production.

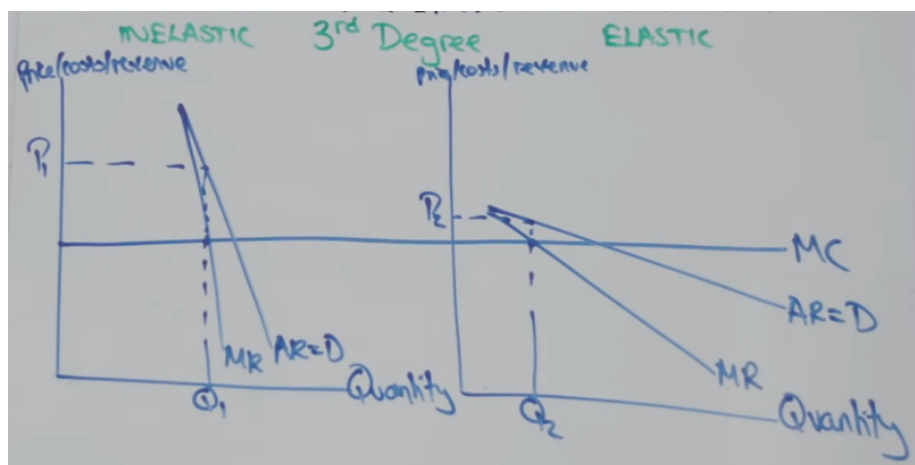
Conditions necessary for price discrimination: - Price making ability - Information to separate the market (knowing who will pay what) - Prevent re-sale (**Market seepage**)

1st Degree price discrimination is when a business charges the maximum possible price for each unit consumed, turning all consumer surplus into monopoly profit.

2nd Degree price discrimination is when a firm which has fixed capacity, eg airplane, hotel etc, and they change prices if needed to fill out the capacity, eg lowering prices at the end of a day to sell tickets.



3rd Degree price discrimination is when a firm changes prices depending on the elasticity of demand



Cons of price discrimination: - Allocative inefficiency - Inequality - Anti-competitive Pricing

Pros of price discrimination: - Dynamic efficiency - Economies of scale - Some consumers benefit - Cross subsidisation
