IB Economics – Theory of the Firm

1.19 Monopolies HL

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1.19 MONOPLIES HL: STUDENT LEARNING ACTIVITY

Answer the questions that follow.

1. DEFINITIONS

Define the following terms: **[10 marks]**

- Allocative efficiency
- Average revenue
- Average total cost
- Average variable cost
- Barriers to entry
- Consumer surplus
- Copyright
- Deadweight loss
- Economies of scale
- Fixed cost
- Homogeneous goods
- Industry
- Long run
- Long-run average cost (LRAC)
- Marginal cost
- Marginal revenue
- Market power
- Market share
- Market structure
- Market supply
- Monopolist
- Monopoly power
- Natural monopoly
- Normal profit
- Output
- P = mc
- Patent
- Positive economic profit
- Price elastic
- Price elasticity of demand (PED)
- Producer surplus
- Productive efficiency
- Resources
- Short run
- Short run shut-down price
- Start-up costs
- Supernormal profit
- Total revenue
- Welfare loss
- X-inefficient

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2. SHORT-ANSWER QUESTIONS

1. Outline the assumptions of the monopoly market model. **[3 marks]**

2. Use a diagram and explain how economies of scale can act as a barrier to entry in a monopoly market. **[5 marks]**

3. Explain, using examples, how branding **and** legal factors can act as a barrier to entry and cause monopoly market to form and be maintained. **[5 marks]**

4. Compare and contrast the demand curve of the monopoly firm with that of a firm operating in perfect competition. **[5 marks]**

5. Explain the relationship between market power and the differences between the demand curves of a firm in perfect competition and a monopoly firm **[5 marks]**

6. Explain why a monopoly firm is a price maker and a firm operating in perfect competition is a price taker. **[5 marks]**

7. Explain the relationship between a monopoly firm's average and marginal revenue curves. **[3 marks]**

8. Explain why the average revenue curve of the monopoly firm is also its demand curve. **[3 marks]**

9. Explain why the demand curve of the monopoly firm is downward sloping. **[3 marks]**

10. Use diagrams and explain why the monopoly firm will only produce in the elastic portion of its demand curve. **[5 marks]**

11. For a monopoly firm, compare and contrast the profit maximising level of output with the revenue maximising level of output. **[5 marks]**

12. Compare the profit maximising rule for a monopoly form with that of a firm operating in perfect competition. **[5 marks]**

13. For a monopoly firm that is maximising profits outline how the firm determines the price that output will be sold for and the level of economic profit the firm will earn. **[5 marks]**

14. Use diagrams and outline the situation where the monopoly firm is: **[9 marks]**
    a. Earning economic profit
    b. Normal profit

c. Subnormal profit

15. Compare the short-run and long-run equilibrium position for a monopoly firm. **[3 marks]**

16. Explain why a monopoly firm making supernormal profits in the short-run can continue making supernormal profits in the long run. **[5 marks]**

Output (units)	Price ($)	ATC ($)	MC ($)	TR ($)	AR ($)
1	10	15.0	5.0		
2	9	9.5			
3	8	7.3			
4	7	6.0			
5	6	5.4			
6	5	5.2			
7	4	5.1			
8	3	5.3			

17. The data in the table above is for a monopoly firm. Use this information to answer the following questions: **[10 marks]**
    a. Calculate marginal cost across the units of output
    b. Calculate total and marginal revenue across the units of output
    c. Determine the revenue maximising level of output
    d. Determine the profit maximising level of output
    e. Determine the price the good is sold for at the profit maximising level of output
    f. Determine the profit per unit and total profit at the profit maximising level of output
    g. Plot the demand, ATC and MC curves, and state whether these curves confirm the results you obtained in the above questions (c to e)

18. Distinguish between a normal and a natural monopoly. **[5 marks]**

19. Explain how economies of scale are relevant to a natural monopoly. **[5 marks]**

20. Explain why governments will not necessarily break up a natural monopoly to increase the level of competition and efficiency in a market. **[5 marks]**

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21. Compare and contrast the price and output levels of monopoly firms and firms operating in perfect competition. **[5 marks]**

22. Use diagrams and the concept of MB > MC, compare and contrast the level of social welfare achieved by a monopoly firm and a firm operating in perfect competition. **[5 marks]**

23. Explain whether a monopoly firm achieves allocative **and** productive efficiency. **[5 marks]**

24. In terms of allocative **and** productive efficiency, compare a monopoly market with a perfect competitive market. **[5 marks]**

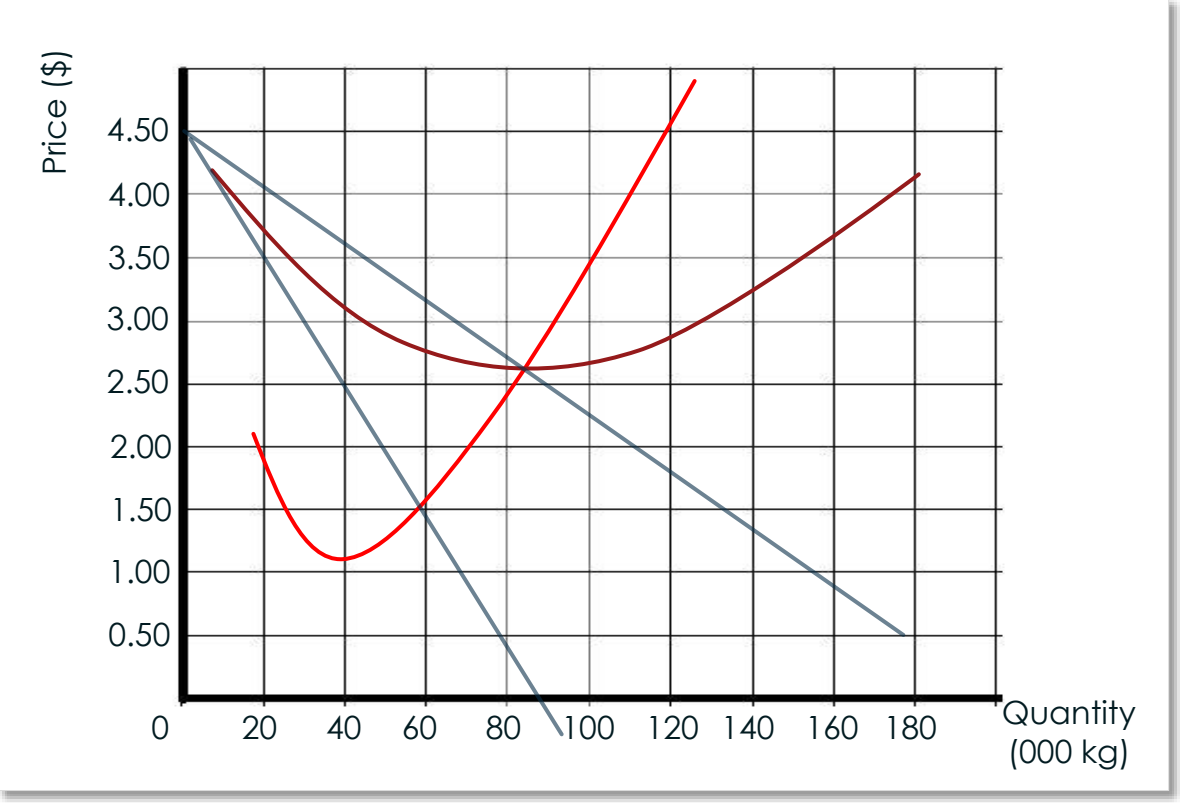
25. Explain why monopoly markets and monopoly power are widely held to be against the best interests of society. **[5 marks]**

26. Explain why some aspects of monopoly power may be desirable for society. **[5 marks]**

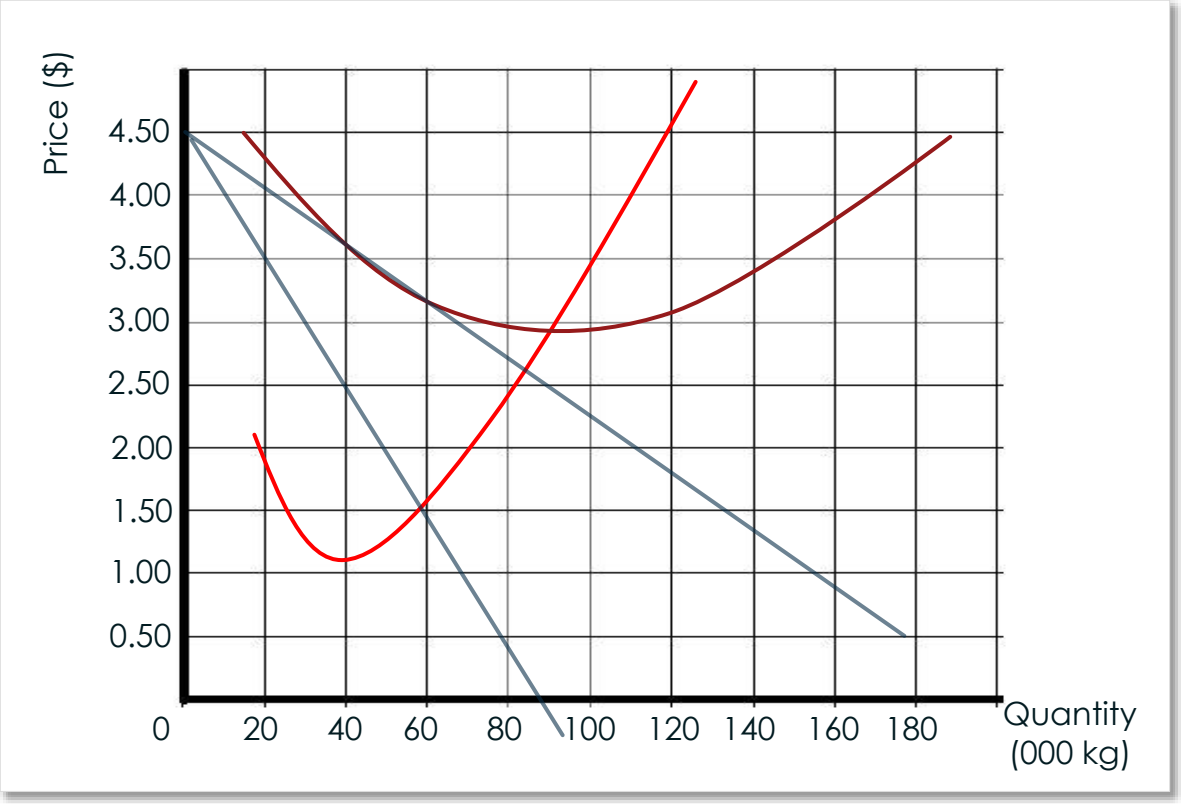
27. Explain the objectives behind government legislation targeting mergers and acquisitions to reduce monopoly powers. **[5 marks]**

28. As methods used to regulate monopolies, compare and contrast marginal cost pricing **and** average cost pricing. **[5 marks]**

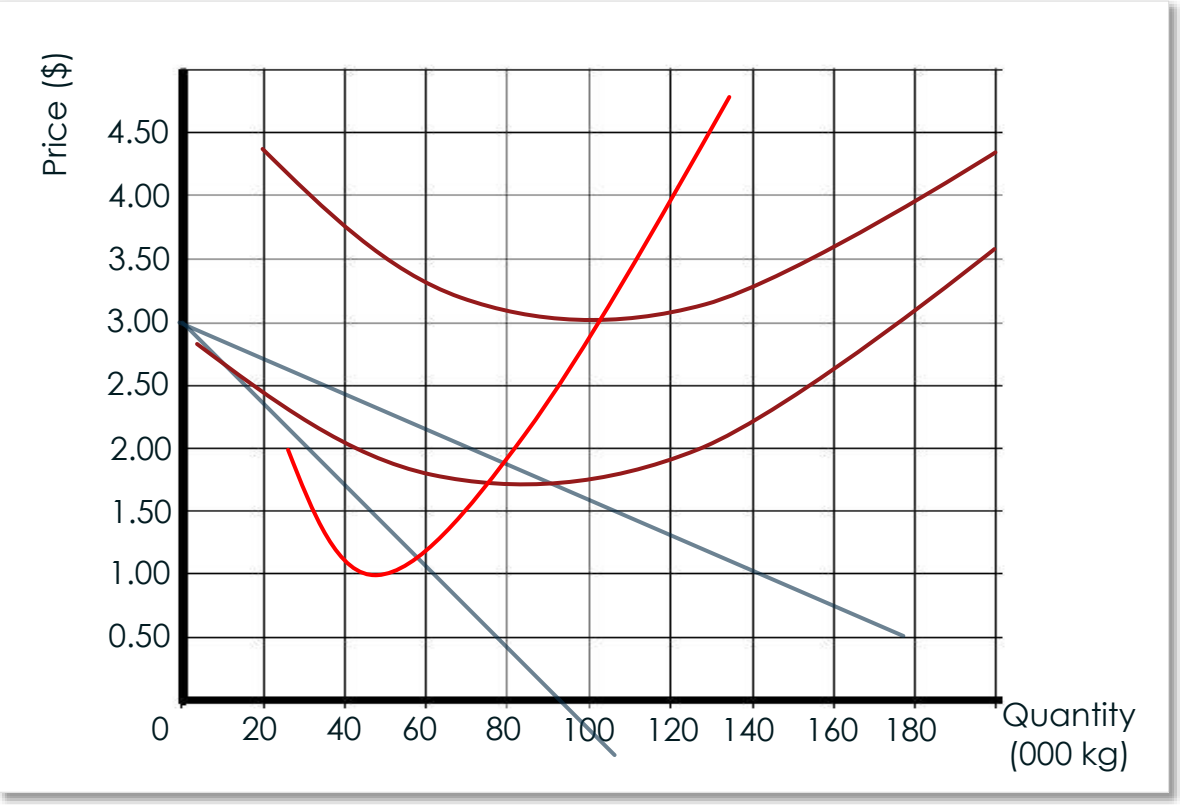
29. Evaluate perfect competition and monopoly markets. **[5 marks]**



30. Use the diagram above to answer the following questions
    a. Label each curve on the diagram above.
    b. Determine the profit maximising or loss making unit of output.
    c. Identify the amount of profit (or loss) the firm is making.
    d. State which type of economic profit the firm is making.
    e. Calculate the amount of profit (or loss) the firm is making.



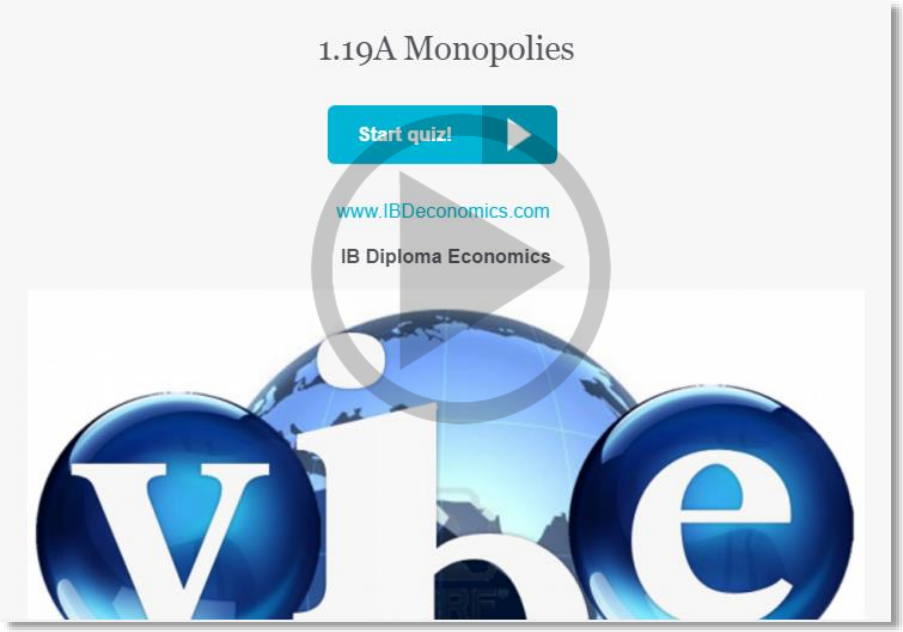
31. Use the diagram above to answer the following questions:
    a. Label each curve on the diagram above.
    b. Determine the profit maximising or loss making unit of output.
    c. Explain why this is the profit maximising (or loss minimising) level of output.
    d. Identify the amount of profit (or loss) the firm is making.
    e. State which type of economic profit the firm is making.
    f. Calculate the amount of profit (or loss) the firm is making.

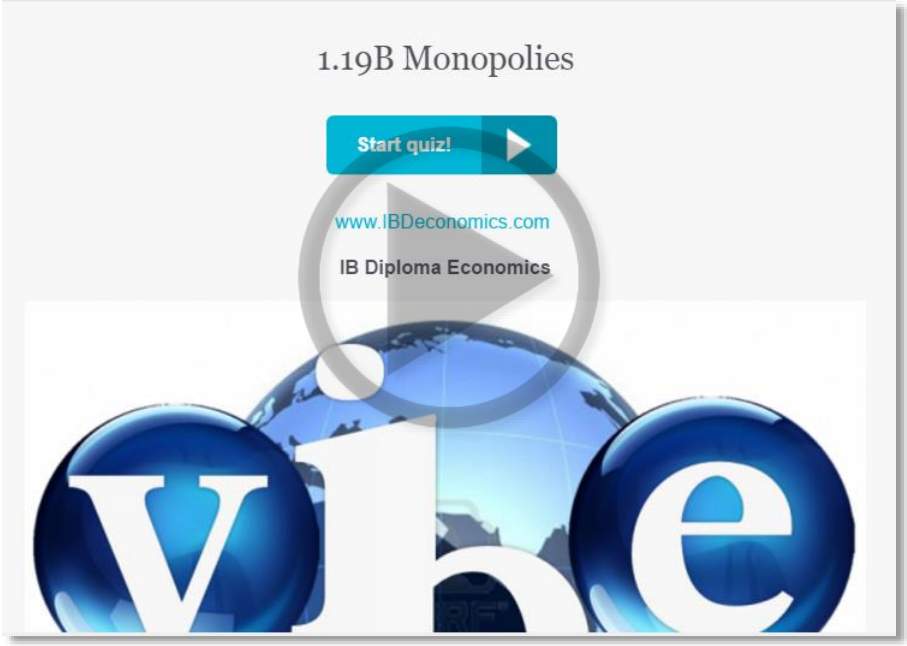


32. Use the diagram above to answer the following questions:
    a. Label each curve on the diagram above.
    b. Determine the profit maximising or loss making unit of output.
    c. Identify the amount of profit (or loss) the firm is making.
    d. State which type of economic profit the firm is making.
    e. Calculate the amount of profit (or loss) the firm is making.
    f. Explain how a firm can be making zero economic profit but still continue operating.

3. INTERACTIVE QUIZZES

Choose the best answer to each question. **[50 marks]**





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