

IB Economics – Theory of the Firm I

Exam Practice Questions: 1.21 Oligopolies



1.21 OLIGOPOLIES: EXAM PRACTICE QUESTIONS

Answer the questions that follow.

1. IB ECONOMICS PAPER 1 EXAMINATION QUESTIONS

- Analyse the function of non-price competition for oligopolies **and** firms in monopolistic competition. **[10 marks]**
- Explain price stability in oligopolies. **[10 marks]**
- Analyse the objectives, incentives and difficulties of cartels. **[10 marks]**
- The two oligopoly firms A and B face a 'prisoner's dilemma' as shown below. Explain how this payoff matrix illustrates interdependence and conflicting incentives to collude or compete. **[15 marks]**

Firms A and B pay-off matrix

	Firm B high price	Firm B low price
Firm A high price	Profit = \$20m Profit = \$20m	Profit = \$35m Profit = \$5m
Firm A low price	Profit = \$5m Profit = \$35m	Profit = \$10m Profit = \$10m

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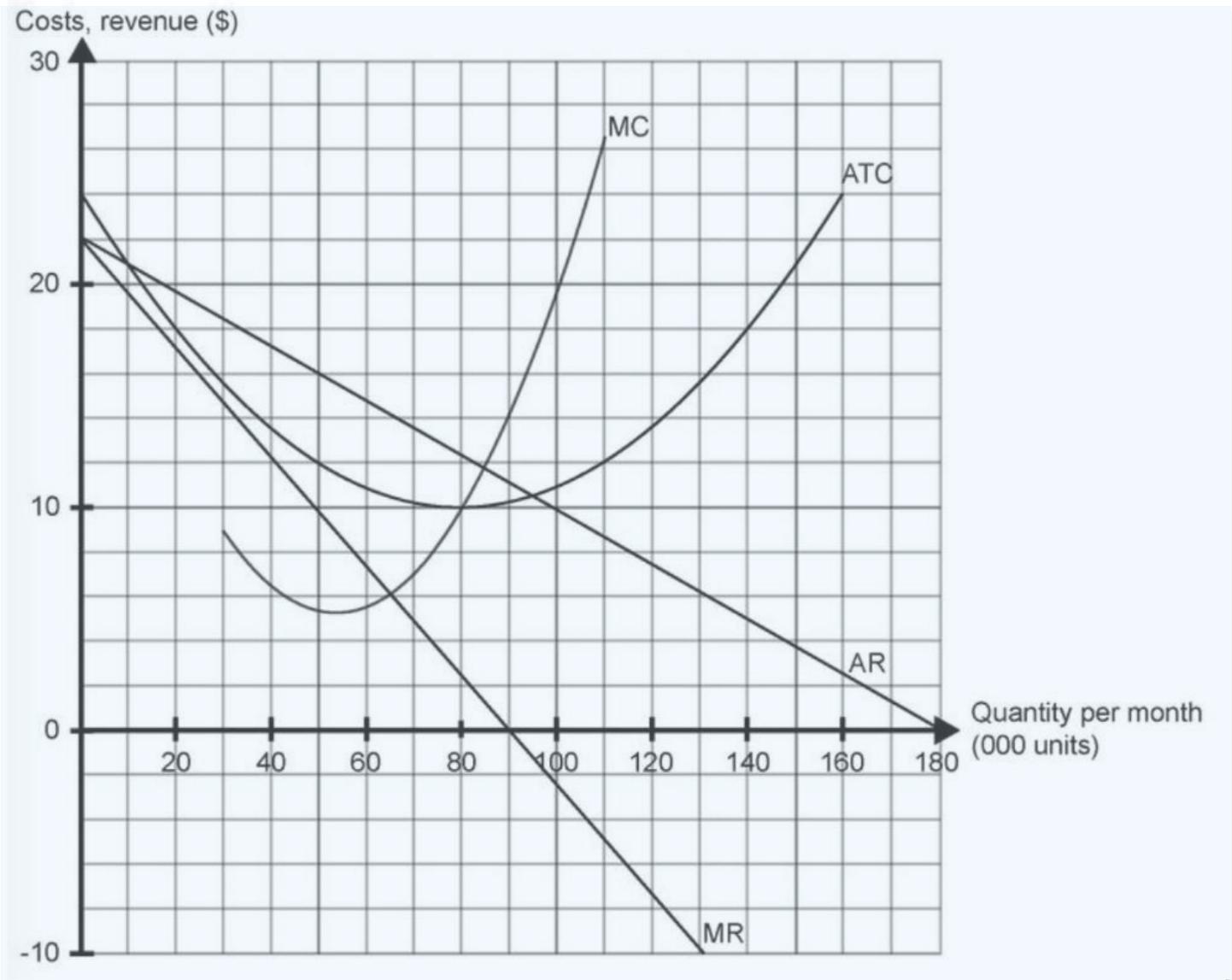
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2. 2. IB ECONOMICS PAPER 3 EXAMINATION QUESTIONS

QUESTION ONE

[25 MARKS]

The following diagram illustrates the average total cost (ATC), marginal cost (MC), average revenue (AR) and marginal revenue (MR) curves for a cartel which acts as a monopoly to maximise joint profits



- a. If fixed costs are \$800,000 per month, calculate the total variable costs at a monthly output of 140,000 units. **[2 marks]**

- b. Outline the difference between explicit and implicit costs of production. **[4 marks]**

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- c. Define the term normal profit. **[2 marks]**
- d. Show and identify the type of economic profit made in the diagram above. **[3 marks]**
- e. Calculate the economic profit made by the cartel if members jointly supply 50,000 units per month. **[2 marks]**
- f. Identify the level of output which would maximise revenue for the cartel and state why this is. **[2 marks]**
- g. Calculate the total revenue per month for members of the cartel if they produce at the revenue maximising level of output. **[2 marks]**
- h. Outline the reason why, even if a cartel achieves its objective of jointly maximising profit, there will be an incentive for members of the cartel to cheat. **[4 marks]**
- i. Outline two conditions, apart from the incentive to cheat, which make cartel structures difficult to maintain. **[4 marks]**

Source: www.IBDeconomics.com