Market Structures Pack

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Economics
Pack 3

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Short Questions

1.

Name the market structure (Perfect Competition, Imperfect Competition or Monopoly) to which each statement below is most likely to apply:

	STATEMENT	MARKET STRUCTURE
(i)	The firm has a perfectly elastic demand curve.	
(ii)	The product of the firm is unique.	
(iii)	Restaurants could be an example of this market structure.	
(iv)	Average costs of the firm are at a minimum.	

(16 marks)

2.

Define the term ‘non-price competition’. State **two** examples.

Definition: ____________________

____

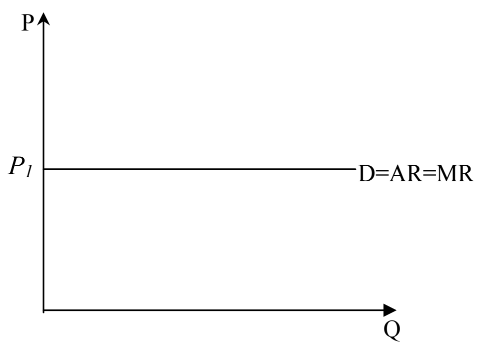
Example 1: ____________________

Example 2: ____________________

(16 marks)

3.

The diagram below represents the demand curve facing a firm in Perfect Competition.



This demand curve is; **(✓ correct answer)**

- Unitary Elastic ☐
- Perfectly Inelastic ☐
- Perfectly Elastic ☐

State the reason for your choice:

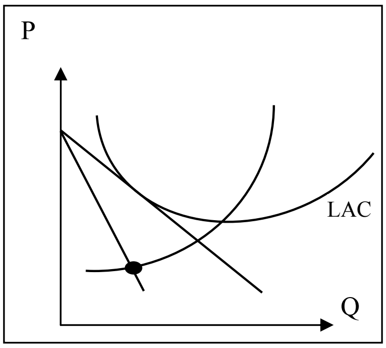
____

____

(16 marks)

4.

The diagram below represents the long run equilibrium of a firm in imperfect competition, which seeks to maximise profits. Label the diagram and use it to describe the long run equilibrium position for a firm in Imperfect Competition.



Description:

(i) ______________________________

(ii) ______________________________

(iii) ______________________________

(iv) ______________________________

(17 marks)

5.

Firms attempting to enter a **monopoly** market must overcome barriers to entry.
Outline **THREE** such barriers to entry.

(i) ______________________________

(ii) ______________________________

(iii) ______________________________

(16 marks)

6.

State three reasons why **profits** are important in a **market economy**.

(i) ______________________________

(ii) ______________________________

(iii) ______________________________

(16 marks)

7.

Define **price discrimination.** State **TWO** conditions under which it would be possible for a firm to price discriminate.

Definition: ______________________________

____

Condition (i): ______________________________

Condition (ii): ______________________________

(17 marks)

8.

"When a firm produces at a level of output at which marginal cost is greater than marginal revenue the firm is maximising profit (or minimising losses)". **True/False**
(Place a circle around your choice and write a one-sentence explanation of your answer).

____

____

(17 marks)

9.

Identify **FOUR** features of an oligopolistic market**.**

(i) ____

(ii) ____

(iii) ____

(iv) ____

(16 marks)

10.

Outline **TWO** benefits to consumers of **<u>non-price competition</u>**.

(i) ____

(ii**)** ____

(16 marks)

11.

Identify **TWO** means by which semi-state companies which are monopolies could be made operate more cost effectively.

(i) ....

(ii) ....

(16 marks)

12.

State **THREE** roles of profits in a market economy.

(i) ....

(ii) ....

(iii) ....

(17 marks)

Long Questions

2011

(a) *Some Telecoms' analysts believe the main mobile operators in Ireland – Vodafone, O2, Meteor and 3 – control an oligopoly and have little reason to make the market really competitive.* *(The Irish Times, November, 2010)*

(i) Outline **three** key features of an oligopolistic market.

Firms in an oligopolistic market may have objectives other than profit maximisation.

(ii) Outline **two** objectives firms in oligopoly may have, other than achieving the maximum level of profits. *(25)*

(b) Using **one** clearly labelled diagram:

(i) Explain the shape of the 'kinked' demand curve facing a firm in oligopoly.
(ii) Explain the long run equilibrium position of this firm. *(25)*

(c) It is suggested that consumers prefer price competition in the market place, yet there are benefits for consumers arising from non-price competition.

(i) Explain **two** reasons why consumers may prefer price competition.
(ii) Describe **two** benefits to consumers of non-price competition.

(25)

[75 marks]

2010

(a) (i) State and explain **three** assumptions underlying the theory of monopoly.
(ii) Outline **two** possible advantages of monopoly as a market structure.

(25 marks)

(b) Iarnród Eireann (Irish Rail) is the state monopoly in the provision of rail transport in Ireland. It operates a system of <u>price discrimination</u> in setting some of its prices.
(i) Explain the underlined term, giving **one** example as practiced by Iarnród Eireann.
(ii) State and explain **three** conditions necessary for price discrimination to take place.

(20 marks)

(c) Using suitably labelled diagram(s), **compare** the long run equilibrium position of the monopoly firm with that of a perfectly competitive firm (assuming both operate under the same cost conditions) under the following headings:

- Price and Output;
- Profits;
- Efficiency. *(30 marks)*

[75 marks]

2009

(a) (i) State and explain the assumptions underlying the theory of **imperfect competition**.
(ii) Outline the advantages imperfect competition may offer consumers.

(30 marks)

(b) Explain with the aid of a diagram in **each** case the conditions for a profit maximising firm to be in equilibrium under imperfect competition:
(i) in the short run;
(ii) in the long run.

(30 marks)

(c) 'Major food retailers in the Irish market, such as Aldi, Dunnes, SuperValu and Tesco operate under conditions of Imperfect Competition'.

Do you agree with this statement? Give reasons for your answer, referring to major food retailers in the Irish market mentioned above.

(15 marks)
[75 marks]

2008

(a) Explain, with the aid of a diagram, the long run equilibrium position for a monopoly firm which seeks to maximise profits.

(25 marks)

(b) **(i)** Define price discrimination.
(ii) Explain **three types** of price discrimination, using suitable examples in each case.

(20 marks)

(c) **(i)** State and explain **three** barriers to entry facing entrants to a monopoly market.
(ii) **Deregulation** of markets (i.e. allowing more suppliers of a good or service into the market) is a continuing development in the Irish economy e.g. energy, mobile phones, transport etc.

Explain how deregulation could affect:
(i) Consumers of the good/service;
(ii) Employees in the industry;
(iii) Profits of existing firms.

(30 marks)
[75 marks]

2007

(a) **(i)** A firm operating under conditions of perfect competition is a '**price taker**'. Explain the concept of being a 'price taker'.

(ii) Explain, with the aid of a labelled diagram, the equilibrium position of a firm in **short run perfect competition.**

(25 marks)

(b) With the aid of a labelled diagram(s), explain the impact which the entry of new firms would have on the market **and** on the equilibrium position of this firm.

(25 marks)

(c) **(i)** Many firms today engage in **product differentiation**. Explain this underlined term showing, with suitable examples, how it can be achieved.

(ii) Explain the effect of product differentiation on the AR and MR curves of a firm, which previously operated under conditions of perfect competition.

(25 marks)
[75 marks]

2006

(a) State and explain **THREE** key features of an **oligopolistic market**.

(15 marks)

(b) With the aid of **ONE** clearly labelled diagram:

(i) Explain the shape of the 'kinked demand curve' under oligopoly.
(ii) Explain the long run equilibrium position of a firm facing a 'kinked demand curve'.
(iii) Explain what is meant by the term 'rigidity of prices' under a 'kinked demand curve'.

(35 marks)

(c) **(i)** Explain **THREE** types of collusion which may occur in an oligopolistic market.
(ii) Do you believe that the Irish retail market for banking services (e.g. personal current accounts.) operates under oligopolistic conditions? Explain your answer.

(25 marks)
[75 marks]

2005

(a) State and explain the assumptions underlying the theory of **imperfect competition**.

(20 marks)

(b) **(i)** Explain, with the aid of a clearly labelled diagram the long run equilibrium position of a firm in **imperfect competition**.

(ii) State and explain **ONE** feature of this firm in long run equilibrium which would be common to a firm in long run equilibrium under **perfect competition**.
(iii) State and explain **ONE** feature of this firm in long run equilibrium which would be common to a firm in long run equilibrium under **monopoly**.

(40 marks)

(c) Consider the retail market for petrol.
Do you believe that this market operates under conditions of imperfect competition? State reasons for your answer.

(15 marks)
[75marks]

2004

(a) Explain, with the aid of a diagram, the long run equilibrium position of a monopoly firm. *(25 marks)*

(b) If firms wish to enter a monopoly market they will face barriers to entry.
Explain **THREE** of these barriers. *(15 marks)*

(c) If a monopoly firm wishes to engage in price discrimination, certain conditions must apply.
State and explain **THREE** of these conditions. *(15 marks)*

(d) Irish semi-state transport companies are facing increasing competition.
Discuss **ONE** possible advantage and **ONE** possible disadvantage of this development for:
- Consumers;

AND
- Employees of semi-state transport companies. *(20 marks)*

[75 marks]

2003

(a) Outline **THREE** key features of an oligopolistic market. (20 marks)

(b) With the aid of ONE clearly labelled diagram:
(i) Explain the shape of the demand curve facing a firm in oligopoly.
(ii) Explain the relationship between this demand curve and the firm's marginal revenue curve.
(iii) Explain the long run equilibrium position of this firm. (40 marks)

(c) Explain THREE methods by which firms in oligopolistic markets may collude. (15 marks)

2002

(a) Outline the assumptions underlying the theory of Perfect Competition. (20 marks)

(b) (i) Explain, with the aid of a labelled diagram, how a firm in Perfect Competition achieves equilibrium in the **short run**.

(ii) Derive and explain the short run supply curve of this firm. (20 marks)

(c) Discuss, with the aid of labelled diagrams, the impact which the entry of new firms would have on the short run equilibrium of existing firms, in perfectly competitive markets, earning supernormal profits. (20 marks)

(d) Firms in Perfect Competition tend not to engage in advertising.
State and explain **TWO** reasons why. (15 marks)

[75marks]

2001

(a) State and explain the assumptions underlying the theory of **Imperfect Competition**. (25 marks)

(b) Draw the demand curve which faces a firm in imperfect competition and justify its shape. (10 marks)

(c) Discuss, with the aid of a clearly labelled diagram, the implications of the assumptions in (*a*) above, on the equilibrium of the firm in the long run under conditions of imperfect competition. (30 marks)

(d) State **ONE FEATURE** of this firm in long run equilibrium which would be common to a firm in long run equilibrium under **EITHER** perfect competition **OR** monopoly. (10 marks)

[75 marks]

Short Questions (Answers)

1.

Name the market structure (Perfect Competition, Imperfect Competition or Monopoly) to which each statement below is most likely to apply:

	STATEMENT	MARKET STRUCTURE
(i)	The firm has a perfectly elastic demand curve.	**Perfect Competition**
(ii)	The product of the firm is unique.	**Monopoly**
(iii)	Restaurants could be an example of this market structure.	**Imperfect Competition**
(iv)	Average costs of the firm are at a minimum.	**Perfect Competition**

4 correct responses x 4 marks each = 16 marks

2.

Define the term 'non-price competition'. State **two** examples.

Definition: **12 marks**

Competition between firms where each firm tries to increase its sales / market share by methods other than changing prices.

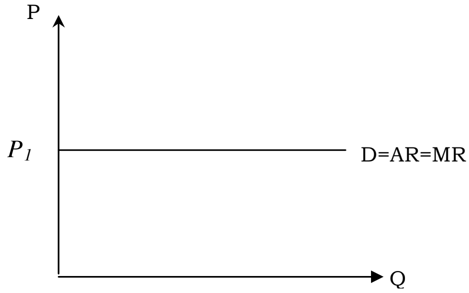
Two examples:

Branding: establishing different brand names for the products
Packaging: use of distinctive packaging to clearly distinguish one product from another
Competitive Advertising: helps create differences between products in the minds of consumers
Opening hours: offer extended opening hours for consumers
Quality of service: improve staff service; improve layout of premises
Sponsorship: local / national events
Special offers: free gifts/ money-coupons/ loyalty cards etc.

2 at 2 marks each.

3.

. The diagram below represents the demand curve facing a firm in Perfect Competition.



This demand curve is; **(✓ correct answer)**

- Unitary Elastic ☐
- Perfectly Inelastic ☐
- **Perfectly Elastic** ☑

State the reason for your choice:

- Any deviation in price from P_1 will result in quantity demand falling to zero.

Perfectly elastic: **4 marks** and bulleted point above: **12 marks**

(16 marks)

4.

The diagram below represents the long run equilibrium of a firm in imperfect competition, which seeks to maximise profits. Label the diagram and use it to describe the long run equilibrium position for a firm in imperfect competition

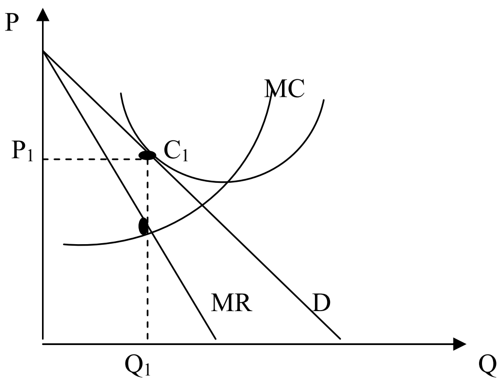


Diagram 5 marks graded.

Conditions:

1. MR = MC, profit maximisation, equilibrium
2. Equilibrium price = P_1
3. Equilibrium quantity = Q_1
4. Normal profit AR = AC/Cost of production C_1
5. Not producing at lowest point of AC curve (inefficient).

4 conditions: 12 marks graded.

5.

Firms attempting to enter a **monopoly** market must overcome barriers to entry.
Outline **THREE** such barriers to entry.

1. **Legal / Statutory / Government Monopoly:**
   Government confers the sole right to supply a good or service/ CIE.
2. **Ownership of a patent / copyright**: A firm has the sole right to a manufacturing process.
3. **Sole rights to raw materials**: Firm may have complete control over the source of raw materials
4. **Large capital investment**:
   - minimum size of a firm required to operate efficiently is so large there is no room for competitors.
   - competitors are discouraged from entering because of the high initial start-up costs.
5. **Entering Trade agreements [collusion / cartels]**:
   ensures that no competition exists within members' segments of the market.
6. **Mergers / takeovers:**
   A firm may ensure their survival by merging / taking over other (rival) firms in the same line of business, such that it becomes a monopolist and no competition exists within the industry.
7. **Brand proliferation:**
   Through advertising a firm's consumers are convinced that there is no suitable alternative to their particular brands

16 marks graded.

6.

State three reasons why **profits** are important in a **market economy.**

1. <u>Encourages risk taking</u>: Profits are a pre-requisite for undertaking risks.
2. <u>Indicates the best use of resources / consumer demand</u>:
   Profits indicate what goods and services consumers demand.
3. <u>Encourages investment</u>: profits may encourage entrepreneurs to invest further in ventures.
4. <u>Provides funds for expansion</u>: Existing business expansion or diversification.
5. <u>Continuity of production</u>: If normal profit is not earned production ceases.
6. <u>SNPs reward entrepreneurs' innovations</u>:
   Those firms which are most efficient / or which minimise costs may earn SNPs.
7. <u>Source of revenue for the government</u>:
   Government earns tax revenues for the benefit of citizens.
8. <u>SNP's may promote Mergers / Takeovers:</u>
   Existing profitable firms may be taken over by multinationals.

16 marks graded

7.

7. Define **price discrimination**.
State **TWO** conditions under which it would be possible for a firm to price discriminate.

When goods or services are sold to different consumers in different markets at varying ratios between marginal cost and price/ the price difference is not due to difference in the cost of production.

1. Monopoly Power.
If freedom of entry existed into the industry, competitors would enter where the firm was charging the higher price and earning SNP and this would continue until only normal profit was earned.

2. Separation of markets.
This ensures that the good bought in the low priced market cannot be offered for resale in the higher priced market. If it was not possible to separate the markets then the above would occur until no price difference existed.

3. Different consumer elasticities of demand.
Consumers with the greater price elasticity of demand are charged the lower prices for their goods e.g. students are assumed to have lower incomes and so are not in the position to pay the full price for certain goods and services.

4. Consumer Indifference.
The difference in price may be so small that consumers are indifferent and so don't mind paying the slightly higher price.

5. Lack of awareness by consumers.
Consumers may be unaware that the good is available elsewhere at a lower price.

6. Consumer attitudes to the goods.
A consumer may be willing to pay a higher price for a good which they consider to be in fashion / provide status e.g. young people and their desire for 'branded' products.

17 marks graded.

8.

7. "When a firm produces at a level of output at which marginal cost is greater than marginal revenue the firm is maximising profit (or minimising losses)". True / $\boxed{\textbf{False}}$
(Place a circle around your choice and write a one-sentence explanation of your answer)

False. The extra cost of producing further units of output is greater than the extra revenue generated therefore the firm could increase its profits by producing less output. The increased output adds more to cost than to revenues earned. Profits are maximised where MC=MR.

9.

4. Identify FOUR features of an oligopolistic market:

1. Few Sellers in the industry*
2. Interdependence between firms*
3. Product Differentiation occurs / firm sells close substitutes*
4. Barriers to entry exist – such as Limit Pricing**.**
5. Collusion may occur.
6. Non-price competition is more common than price competition.
7. Pursuing objectives other than profit maximisation.
8. Existence of Price Rigidity / 'Sticky Prices'.

10.

TWO benefits of non-price competition to consumers.

(a) **Stability in prices**: non-price competition means unchanging prices for the consumer
(b) **Better quality**: commodity; service; after sales service.
(c) **Benefits of advertising / Sponsorship**: improved range/quality of service i.e. media.
(d) **Consumer more informed**: advertising provides consumers with information.
(e) **Consumer loyalty rewarded:** allows consumers get 'free' gifts.

2 benefits x 8 marks each

11.

Identify TWO means by which semi-state companies which are monopolies could be made operate more cost effectively. 16 marks

1. Allow more competition in the sector / deregulation / e.g. electricity provision.
2. Allow the companies form strategic alliances e.g. Aer Lingus
3. Rationalise the company: reduce labour costs / discontinue unprofitable services.
4. Appoint only those members to the boards who have proven expertise in the relevant areas.
5. Reduce the extent of government interference in the day to day running of the companies e.g. Aer Lingus / RTE
6. Privatise the company – this will enforce efforts towards costs reduction.

12.

7. State THREE roles of profits in a market economy. (17 marks)

1. Encourages risk taking.
2. Indicates the best use of resources / consumer demand (what goods and services consumers want)
3. Encourages investment.
4. Provides funds for expansion.
5. Normal profit ensures that production continues.
6. SNP is the reward for cost reduction and the development of new ideas / reward for efficiency.
7. Source of revenue for the government.
8. SNP's act as a signal to other firms to join the industry.

Long Questions (Answers)

2011

(a) *Some Telecoms' analysts believe the main mobile operators in Ireland – Vodafone, O2, Meteor and 3 – control an oligopoly and have little reason to make the market really competitive.*
(The Irish Times, November, 2010)

(i) Outline **three** key features of an oligopolistic market.

Firms in an oligopolistic market may have objectives other than profit maximisation.

(ii) Outline **two** objectives firms in oligopoly may have, other than achieving the maximum level of profits.
(25)

(i) Outline **three** key features of an oligopolistic market.

1. Few Sellers in the industry.
Because of this each seller can influence the price of the commodity and /or the output sold.

2. Interdependence between firms.
Firms in oligopoly do not act independently of each other. They will each take into the account the likely reactions of their competitors, hence prices tend to be rigid.

3. Product Differentiation occurs.
The commodities which firms sell are close substitutes. Firms will engage in advertising to persuade consumers to buy their product rather than a competitor's product.

4. Barriers to entry.
These are common in an oligopolistic market as existing firms will wish to maintain their share of the market. Examples of barriers include: high costs of setting up in the industry, brand proliferation etc.

5. Collusion may occur.
Firms within the industry may meet to control the output in the industry and/or control prices e.g. OPEC.

6. Non-price competition is more common than price competition.
Due to the fear of how competitors will react, firms tend not to engage in price competition but rather they engage in non-price competition to gain consumers.

3 features x 5 marks each

(ii) Outline **two** objectives firms in oligopoly may have, other than achieving the maximum level of profits.

1. Prevent government market intervention/interference
Firms may fear that the existence of supernormal profits would attract government intervention into the market and thereby restrict the firm's activities.

2. Discourage the entry of new firms into the industry
Firms may set prices at a low level which is intended to discourage the entry of new firms into the industry (limit pricing). By pursuing this policy they are forsaking higher present profits for potentially higher future profits.

3. Maximisation of sales / increased share of market
Once a minimum level of profit is earned to reward shareholders, provide funds for reinvestment etc. the firm may concentrate on maximising sales; increasing its share of the market. It may wish to achieve economies of scale; decrease the level of sales of rival firms; become the most dominant firm in the market.

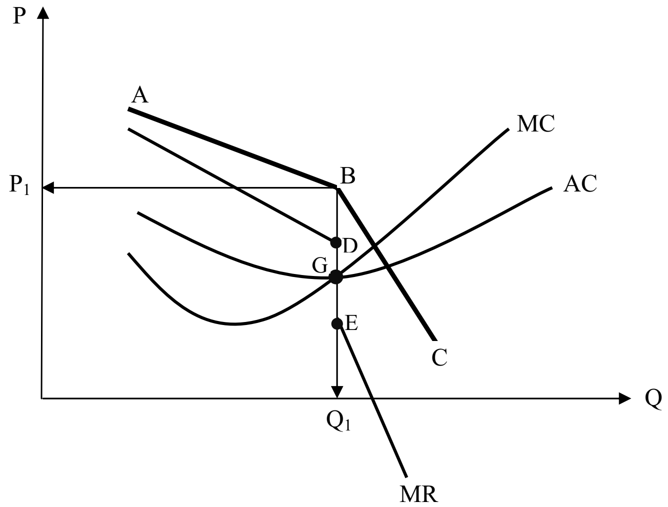
4. Maintain adequate profits.
- The owners of the business may prefer to earn stable/moderate levels of profits rather than constantly striving for large supernormal profits as this is what they are satisfied with.
- Where the managers are not owners they may tend towards a more conservative approach rather than a dynamic drive to profit maximisation.

2 x 5 marks each

(b) Using **one** clearly labelled diagram:
(i) Explain the shape of the 'kinked' demand curve facing a firm in oligopoly.
(ii) Explain the long run equilibrium position of this firm. *(25)*

Diagram: 9 marks

Price axis
Quantity axis
Kinked D/C
Distinct MR curve
MC
AC
P_1
Q_1
Point G



(i) Shape of the demand curve: **8 marks**

Demand curve - AB
If this firm increases its price others will leave their prices unchanged so this firm will lose many customers – this portion of the D/C is elastic.

Demand curve – BC
If this firm lowers its price others will match this price decrease so this firm will gain few additional customers – this portion of the D/C is inelastic.

(ii)
The long run equilibrium position of this firm: **8 marks**

1. Equilibrium occurs at point G where (a) MC = MR & (b) MC is rising.
2. The firm will produce Q_1 and sell this output at price P_1
3. The firm's cost of production is shown at point G.
4. Should costs rise between points D and E then market price tends to remain constant at P_1.
5. This firm is earning SNPs because AR exceeds AC o*r* barriers to entry exist.

(c) It is suggested that consumers prefer price competition in the market place, yet there are benefits for consumers arising from non-price competition.

(i) Explain **two** reasons why consumers may prefer price competition.

(ii) Describe **two** benefits to consumers of non-price competition. (*25*)

(i) Reasons why consumers may prefer price competition

1. Lower prices / value for money
Consumers will benefit from availability of commodities at lower prices. Consumers will be able to get better value for their limited income.

2. Higher disposable income
With lower prices consumers will now have a higher disposable income, resulting in a better standard of living.

3. More choice
As consumers have a greater disposable income they can now choose how to spend this additional income.

4. Preferable to non-price competitive measure because:
- Consumers pay for non-price competitive measures e.g. advertising;
- Offers may be unwanted / of little value; tokens may go unused etc.

(ii) Benefits of non-price competition.

1. Consumer loyalty rewarded
Consumers can, by shopping in selected stores, receive loyalty points which can be used as they wish.

2. Stability in prices
Non-price competition means prices will not be constantly changing and so consumers do not have to worry that they are losing out on bargains / may be better able to budget.

3. Better quality commodities / services
Firms may improve the quality of their commodities; offer better service and/ or after sales service to consumers.

4. Allows consumers to save and / or avail of 'free' gifts
With regular shopping consumers can 'save' their loyalty points for those time periods when they incur additional expenses e.g. Christmas; Easter etc. Consumers may benefit from 'free' gifts from retailers e.g. free turkeys at Christmas.

5. More informed consumers
Through advertising consumers may acquire more information about products and services and so can make more informed choices.

25 marks (7+6+6+6)

2010

(a) (i) State and explain **three** assumptions underlying the theory of monopoly.
(ii) Outline **two** possible advantages of monopoly as a market structure. (25 marks)

(i) Assumptions of Monopoly

One firm in the industry
- One firm exists within the industry so there is no distinction between the firm and industry.
- One firm supplies the output in the entire industry.

Controls price *or* output
- A firm can control price or output but not both.
- If it sets the price the output produced will be determined by consumers.
- If it sets the output the price will be determined by the market.

Profit maximisation
- It is possible for the firm to earn SNP's in both the short run and long run.
- A firm aims to make maximum profits and it achieves this when MC = MR

Barriers to entry
- If a monopoly market structure is to continue into existence into the long run there cannot be freedom of entry into the industry.
- These barriers prevent the entry of new firms into the industry to threaten the position of the monopolist.

3 points at 5 marks each. State: 2 marks. Explain: 3 marks.

(ii) Possible advantages of monopoly as a market structure

Economies of scale
Production on a large scale may help the firm benefit from economies of scale and these cost savings may be passed on to the consumer in the form of lower prices.

Guarantee supply of product / service
The supply of the product / service may be guaranteed and provided where profit is minimal (e.g. a state monopoly) so consumers benefit e.g. provision of bus services in areas of low population.

Employment
As there is no competition employees have greater security of employment/may benefit from preferential conditions of employment /better rates of pay and pensions.

Reduced use of scarce resources
There may be less duplication in the provision of products / services. There may be less need for competitive advertising so society's resources are not wasted. Certain services may be best provided by one provider e.g. train tracks /electricity grid so as to avoid duplication.

Potential for innovation/ R & D
The (supernormal) profits that monopolies may make could be used for investment in R&D and secure their dominance in the market. Inventors/creators need patent protection otherwise they may not invent.

2 points at 5 marks each. State: 2 marks. Explain: 3 marks.

(b) (Irish Rail) is the state monopoly in the provision of rail transport in Ireland. It operates a system of price discrimination in setting some of its prices.
(i) Explain the underlined term, giving **one** example as practiced by Iarnród Eireann.
(ii) State and explain **three** conditions necessary for price discrimination to take place. (20 marks)

Price Discrimination: **6 marks**

When a good or service is sold to different consumers / different markets at varying ratios between marginal cost and price *or* the price difference is not due to difference in the cost of production.

Example: **2 marks**

- A student being charged a lower rate for travel from Cork to Dublin than another passenger
- Consumers being charged different rates for peak and off-peak travel.

(ii) State and explain **three** conditions necessary for price discrimination to take place.

1. Monopoly Power.
If freedom of entry existed into the industry, competitors would enter where the firm was charging the higher price and earning SNP and this would continue until only normal profit was being earned.

2. Separation of markets.
The good bought in the low priced market cannot be offered for resale in the higher priced market. If it was not possible to separate the markets then the above would occur until no price difference existed.

3. Different consumer price elasticities of demand.
Consumers with the high price elasticity of demand are charged the lower prices for their goods e.g. students are assumed to have lower incomes and so are not in the position to pay the full price for certain goods and services.

4. Consumer Indifference.
The difference in price may be so small that consumers are indifferent and so don't mind paying the slightly higher price.

5. Lack of awareness by consumers.
Consumers may be unaware that the good is available elsewhere at a lower price.

6. Consumer attitudes to the goods.
A consumer may be willing to pay a higher price for a good which s/he considers to be in fashion / provide status e.g. people and their desire for 'branded' products.

3 points at 4 marks each. State: 2 marks. Explain: 2 marks.

(c) Using suitably labeled diagram(s), compare the long run equilibrium position of the monopoly firm with that of a perfectly competitive firm (assuming both operates under the same cost conditions) using the following headings:
- Price and Output;
- Profits;
- Efficiency. (30 marks)

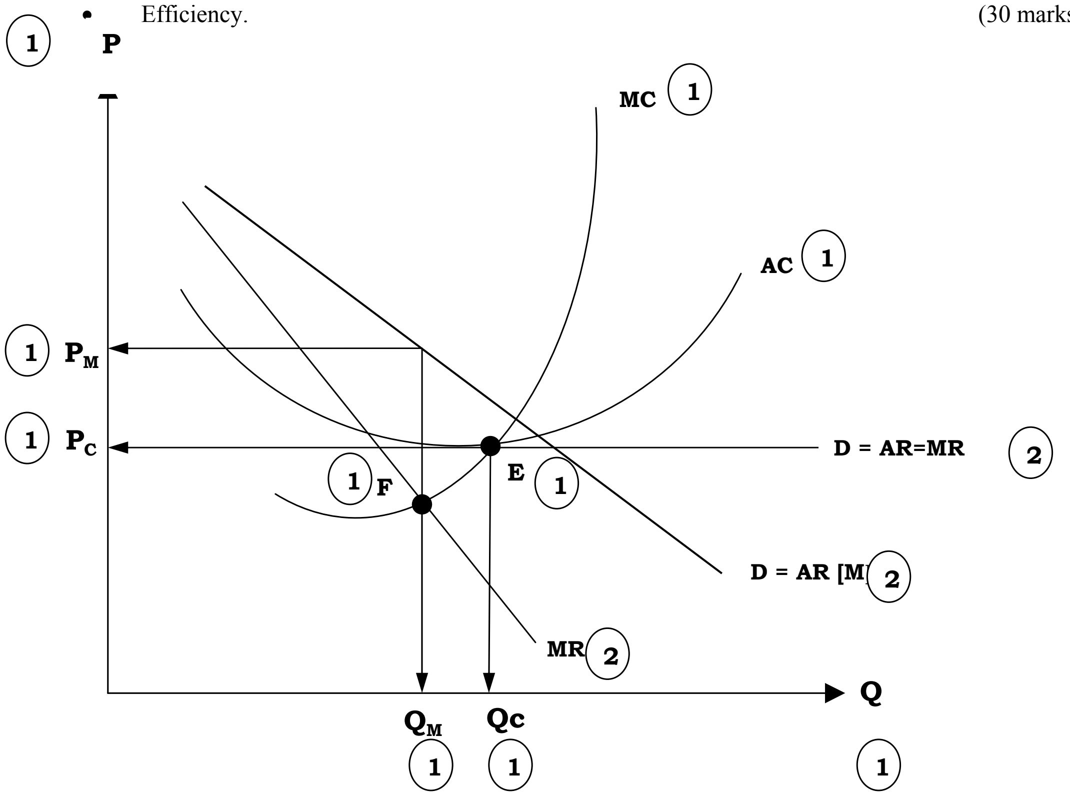


Diagram
10 items at 1 mark each + 3 items at 2 marks each = 16 marks.

	Comment	Marks
Price	A firm in a monopoly position sells its output at a <u>higher price</u>– P_m rather than P_c.	**3 marks**
Output	A firm in a monopoly position produces a <u>smaller output</u> than in perfect competition – Q_m rather than Q_c.	**3 marks**
Profits	Because AR = AC **(1)** a firm in PC earns normal profit **(1).** **(2)** Because AR > AC **(1)** a firm in monopoly can earn SNPs. **(1).** **(2)**	**4 marks**
Efficiency	A firm in PC produces at the lowest point of AC **(1)** and so is efficient **(1)**. **(2)** A monopoly may not produce at the lowest point of AC **(1)** and so maybe inefficient **(1).** **(2)**	**4 marks**
		14 marks

2009

(a) (i) State and explain the assumptions underlying the theory of **imperfect competition**.

1. **There are many buyers in the industry.**
   - An individual buyer, by his/her own actions, can't influence the market price of the goods.
2. **There are many sellers in the industry.**
   - An individual seller can influence the quantity sold by the price it charges for its output.
3. **Product differentiation exists.**
   - The goods, supplied by the producer, are not homogenous but are close substitutes.
   - Firms use branding to distinguish their products from one another.
4. **Freedom of entry and exit.**
   - No barriers to entry exist within the industry.
   - It is possible for firms to enter/leave the industry as they wish.
5. **Reasonable knowledge.**
   - Within the industry each firm has reasonable knowledge of profits made by other firms.
   - Consumers have a reasonable knowledge of the prices being charged for different products.
6. **Each firm attempts to maximise profits.**
   - Firms produce where MC = MR
   - Each firm will attempt to minimise costs of production.

5 points @ 4 marks each graded

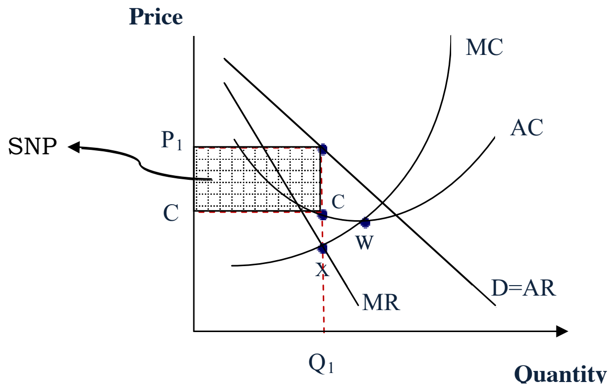
(ii) Outline the advantages imperfect competition may offer to consumers.

- **Greater choice**
  Goods are not homogenous, but are close substitutes, therefore consumers have a greater choice of goods/services.
- **Normal Profit**
  In the long-run consumers are not being exploited as the firm is earning normal profits.
- **Lower prices**
  Competition between firms in the industry will help lower prices and make them more competitive for consumers.
  Some items such as newspapers, magazines, sporting and music events may be cheaper due to the revenues earned by the supplier from competitive advertising.
- **Innovative goods/services**
  Innovation is encouraged as firms will constantly strive to gain a competitive edge over their rivals, hence, consumers get the benefit of modern up-to-date goods/services.
- **Access to information**
  Consumers may have more information available to them because of the extensive competitive advertising used within the industry.

2 points @ 5 marks each graded

(b) Explain with the aid of a diagram in each case the conditions for a profit maximising firm to be in equilibrium under imperfect competition:

(i) **In the short run**



Marking of Diagrams

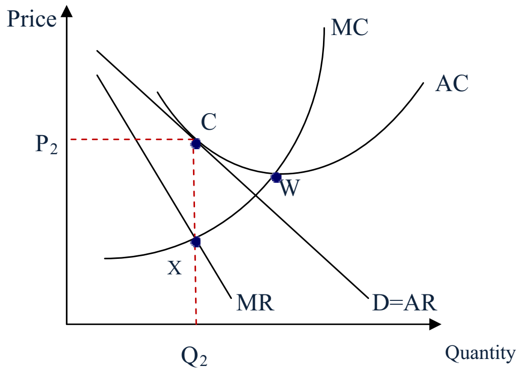
Short Run	Long Run
P & Q	
MR	
D=AR	AC = AR:
AC	Correct equilibrium:
MC	Lowest point of AC
Correct equilibrium	
7 marks	**5 marks**

Explanation of short run equilibrium:

- Equilibrium/ Profit maximisation occurs at point X where MC = MR (*MC is rising and cuts MR from below*).
- The level of output produced is Q_1 and the price the firm sells this output at is P_1
- The average cost of production is shown at point C / not producing at lowest point of AC.
- This firm is earning super normal profits because AR > AC.

4 points @ 2 marks each = 8 marks

(ii) **In the long run**.



Explanation of long run equilibrium:

- Equilibrium / profit maximisation occurs at point X where MC = MR (*MC is rising and cuts MR from below*).
- The level of output produced is Q_2 and the price the firm sells this output at is P_2.
- The average cost of production is shown at point C.
- This firm is earning normal profits because AR = AC**.**
- The firm is not producing at the lowest point of AC / this indicates that the firm is wasting scarce resources.

5 points @ 2 marks each = 10 marks

(c) 'Major food retailers in the Irish market, such as Aldi, Dunnes, SuperValu and Tesco, operate under conditions of Imperfect Competition'.

Do you agree with this statement?
Give reasons for your answer, referring to major food retailers in the Irish market mentioned above.

No, I do not agree with this statement. It is an **oligopolistic market** because:

1. The industry is dominated by a few large retailers/multiples, who hold a major share of the market such as Tesco, Dunnes Stores, Superquinn etc.
2. New firms may find it difficult to enter due to barriers to entry such as economies of scale, brand proliferation and control by existing firms of the channels of distribution.
3. Mutual interdependence between the firms: Firms interact by taking account of each others marketing / pricing strategies. They are concerned with maintaining or increasing their share of the total market e.g. the current Tesco and Dunnes Stores advertising / pricing campaigns.
4. The products sold are close substitutes: Competitive advertising is important as is heavy 'product loyalty' promotion. Various gimmicks are used to attract customers. Sellers also use 'brand names' extensively to maintain consumer loyalty.

2 reasons @15 marks graded

(Development must refer to the food retailers in the Irish market)

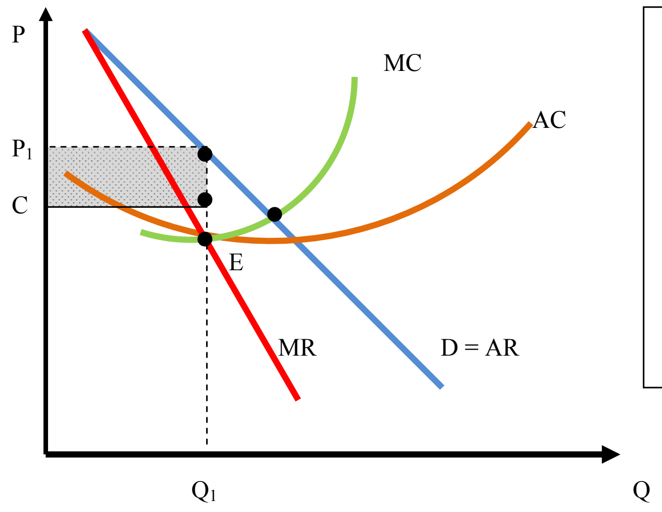
Note:
Arguments for imperfect competition from a local market point of view were also accepted

2008

(a) Explain with the aid of a diagram, the long run equilibrium position for a monopoly firm which seeks to maximise profits. (25 marks)

Diagram: 10 marks graded

(a)



- Price axis
- Quantity axis
- P_1
- Q_1
- C
- MC
- AC
- D = AR
- MR
- E

1. **<u>Equilibrium</u>**
- Occurs at point E where
- MC = MR and MC is rising and cuts MR from below.

2. **<u>Price charge & /Output produced</u>**
- The firm produces output Q_1 and sells it at price P_1 on the market

3. **<u>Cost of production</u>**
- The cost of producing this output shown at point C.
- Because AR=AC this represents normal profit.

4. **<u>Super Normal Profits.</u>**
- This firm is earning SNP's – represented by the shaded area above.
- They are earning SNP's because AR > AC and
- they can continue to earn SNP's because barriers to entry exist..

5. **<u>Waste of Scarce Resources</u>**
- Because the firm is not producing at the lowest point of the AC curve it is wasting scarce resources.

5 points of explanation at 15 marks graded.

(b) (i) Define price discrimination.
(ii) Explain **three types** of price discrimination, using suitable examples in each case (20 marks)

When the same goods or services are sold to different consumers (in different markets) at varying ratios between marginal cost and price/the price difference is not due to a difference in the cost of production.

Definition: 8 marks graded.

(ii) Explain **three types** of price discrimination, using suitable examples in each case

Type	**Explanation**	**Example**
1st Degree	• A monopolist attempts to remove consumer surplus. • A monopolist identifies those consumers who are prepared to pay a higher price and consequently charges them that higher price. • This type of price discrimination can occur in one-to-one confidential services.	Visiting a medical consultant / solicitor
2nd Degree	• A monopolist gives discounts for bulk buying	Night Saver Electricity Magazine subscriptions 3 for 2 offers
3rd Degree	• Consumers have different price elasticities of demand. • Consumers with inelastic demand pay a higher price than consumers with elastic demand	Business air travel vs. leisure air travel Special rates / prices for students and old age pensioners.

3 explanations at 4 marks each graded (must include example).

(c) (i) State and explain **three** barriers to entry facing entrants to a monopoly market.

(ii) Explain how deregulation could affect:
(i) Consumers of the good/service;
(ii) Employees in the industry;
(iii) Profits of existing firms. (30 marks)

(i) State and explain **three** barriers to entry facing entrants to a monopoly market.

1. **Legal / Statutory Monopoly**
   Other firms may not be allowed into the industry because the government confers on a firm the sole right to supply a particular good or service e.g. Iarnród Éireann.

2. **Ownership of a patent / copyright**
   If a firm has the sole right to a manufacturing process then no other firm can compete with it. Other firms are not allowed to use this patent until the time period for it has expired.

3. **Ownership of raw materials**
   A firm may have complete control over the source of essential raw materials i.e. an oil drilling company.

4. **Large capital investment**
   - In some industries the minimum size of a firm required to operate efficiently is so large that there is no room for competitors once one firm has established itself.
   - Competitors are discouraged from entering because of the high initial start-up costs.

5. **Trade agreements /collusion/cartels**
   By entering trade agreements with other firms, a firm can share out the market so that no competition exists within its segment of the market.

6. **Mergers / takeovers**
   A firm may ensure its survival by merging / taking over other rival firms in the same line of business, such that it becomes a monopolist and no competition exists within the industry.

7. **Monopolies based on fear, force or threats**
   An individual / firm may stop other individuals/firms providing similar goods/services by means of threats/force /instilling fear into potential entrants i.e. the supply of illegal drugs.

8. **Brand proliferation**
   A firm may gain monopoly power if, through its advertising, consumers are convinced that there is no suitable alternative to its particular brands.

3 barriers at 5 marks each graded.

(ii) **Explain** how deregulation could affect:
(i) Consumers of the good/service;
(ii) Employees in the industry;
(iii) Profits of existing firms.

	Statement	Explanation
Consumers of the good/service	**Lower Prices.**	Increased competition / an increase in supply may cause prices to fall.
	Increased availability of service.	With an increase in the number of suppliers, availability of the good/service may expand e.g. taxis in Dublin.
	Increased efficiency.	With increased choice in suppliers the consumer may benefit from increased efficiency by firms.
	Loss of essential non-profit making services	Non-profit making services may be discontinued by companies in an effort to reduce costs
	Loss of quality in service	Quality of services may disimprove to cut costs
	Higher prices in future	There may be higher prices in the future in order to survive the competition
Employees in the industry	**Loss of employment in existing businesses.**	With increased competition existing suppliers may suffer from a loss of business resulting in a loss of jobs.
	Job opportunities with new suppliers.	New suppliers may offer increased employment opportunities.
	Changed working conditions.	The drive towards increased profits may mean that businesses may reduce the benefits to existing / new employees.
Profits of existing firms	**Decreased profits**	If existing businesses experience a loss of business, their market share falls resulting in a loss of profits.
	Increased profits	If the existing businesses are able to meet the new competition and expand their business activities the opposite of the above may occur. Business may experience economies of scale.

3 at 5 marks each graded – 1 effect in each case.

2007

(a) (i) A firm operating under conditions of perfect competition is a **'price taker'.**
Explain the concept of being a 'price taker'**.**

- This means that the individual firm must accept the price as it is set on the market.
- Each firm supplies such a tiny fraction of the market it cannot influence the market price.

6 marks graded.

(ii) Explain, with the aid of labelled diagram, the equilibrium position of a firm in **short run perfect competition.** (25 marks)

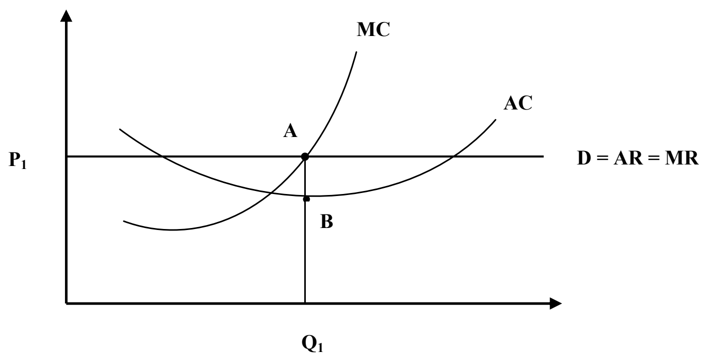
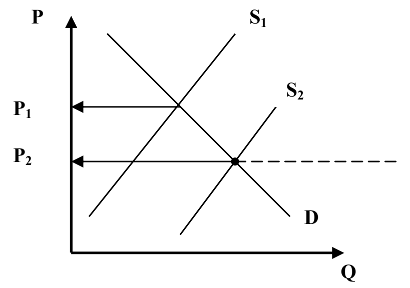
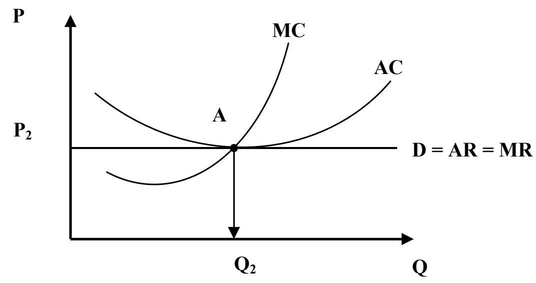


Diagram	*Explanation*
• MC curve	• At point A: MC = MR
• AC curve	• The firm produces Q1
• D = AR = MR	• Firm will sell this output at P1
• Point A	• Firm will earn SNP's because AR > AC.
• P1	
• Q1	
• Cost is at point B.	

19 marks graded.

(b) With the aid of a labelled diagram (s), explain the impact which the entry of new firms would have on the market **and** on the equilibrium position of this firm. (25 marks)





Market and Individual Firm.

Mkt. Diagram	Firm Diagram	Explanation Key Points
	• P axis	• Market supply curve shifts out to the right.
	• Q axis	• Market price falls / the firm's D/C falls
• D	• AC	• Firm will now produce a smaller quantity.
• S1	• MC	• Amount of SNP's earned will fall / be eliminated.
• S2	• D = AR = MR	
• P1	• P2	
• P2	• Q2	
	• Equilibrium point	

25 marks graded.

(c) (i) Many firms today engage in **product differentiation**. Explain this underlined term showing, with suitable examples, how it can be achieved.

(ii) Explain the effect of product differentiation on the AR and MR curves of a firm, which previously operated under conditions of perfect competition. (25 marks)

(i) 17 marks graded.

Product Differentiation

The goods which are produced are **close substitutes** / **similar goods** / **not identical goods**.

Product differentiation can be achieved by:

Explanation	**Example**
Branding Establishing different and distinctive brand names for the products	Nike, Addidas, Reebok
Competitive Advertising Creating differences in the products in the minds of consumers e.g. through packaging which clearly distinguishes one product from another	Daz v. Surf Kellogs Cornflakes
Product innovation Firms develop their product further (add value) so that it is better or more advanced than that of competitors.	Lyons pyramid tea bags; Avonmore – super milk. Fairy detergent – anti bacterial agents.

(ii) 8 marks graded.

Effect of product differentiation on the AR and MR curves of a firm

As a result of product differentiation:

- A firm's AR will be downward sloping from left to right.
  As products are close substitutes:
  If a firm lowers price it can expect to attract some but not all customers from other firms; if the firm increases prices it may expect to lose some but not all customers – so the firm will sell less at higher prices and more at lower prices. Consequently the demand curve (AR curve) facing the firr is downward sloping.
- If AR is falling then MR is also falling and lies below AR. To encourage more customers the firm must drop the price. The AR Curve is falling. The revenue from the increased sales will be reduce by the falling revenue on each unit previously sold at a higher price but now at a reduced price.

2006

(a) State and explain **THREE** key features of an oligopolistic market. *(15 marks)*

1. Few Sellers in the industry.
Because of this each seller can influence the price of the commodity/or the output sold.

2. Interdependence between firms.
Firms in oligopoly do not act independently of each other. They will each take into the account the likely reactions of their competitors. Hence **prices tend to be rigid**.

3. Product Differentiation occurs.
The commodities which firms sell are close substitutes. Firms will engage in advertising to persuade consumers to buy their product rather than a competitor's product.

4. Barriers to entry.
These are common in an oligopolistic market as existing firms will wish to maintain their share of the market. Examples of barriers include: high costs of setting up in the industry, brand proliferation etc.

5. Collusion may occur.
Firms within the industry may meet to control the output in the industry and/or control prices e.g. OPEC.

6. Non-price competition is more common than price competition.
Due to the fear of how their competitors will react firms tend not to engage in price competition but rather they engage in non-price competitive measures to gain consumers.

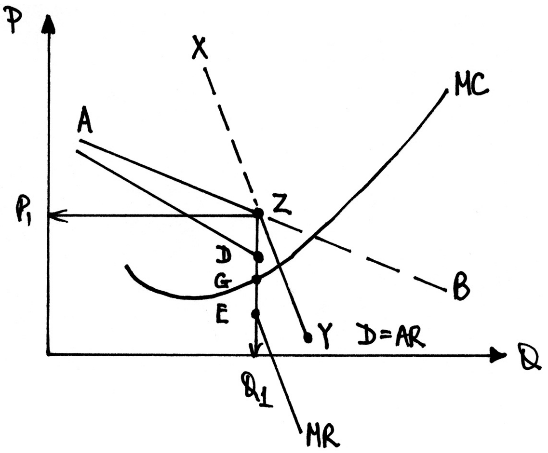
7. Pursuing objectives other than profit maximisation.
Firms may have objectives other than maximizing their profits i.e. increasing their share of the total market, limiting profits to discourage government investigation, satisfaction with the existing level of profits (e.g. in a small family business)

3 features x 5 marks each = 15 marks graded
Must state TWO of the first THREE listed features.

(b) With the aid of **ONE** clearly labelled diagram:

(i) Explain the shape of the 'kinked demand curve' under oligopoly.
(ii) Explain the long run equilibrium position of a firm facing a 'kinked demand curve'.
(iii) Explain what is meant by the term 'rigidity of prices' under a 'kinked demand curve'. *(35 marks)*

Marking scheme: Diagram – 9 marks graded



(i) Shape of the demand curve: ***8 marks graded***

- ***This firm faces an ELASTIC D/C - demand curve AB*** If a firm increases its price other firms leave their prices unchanged - so this firm will lose many customers.
- ***The firm faces an INELASTIC D/C - demand curve XY*** ***If*** a firm lowers its price other firms will match this price decrease - the firm will gain few additional customers.

(ii) the long run equilibrium position of this firm: ***10 marks graded***

- Equilibrium is achieved where (a) MC = MR & (b) MC is rising.
- This occurs at point G in the diagram.
- The firm will produce Q_1 and sell this output at price P_1
- Reference to unchanging prices: should costs rise between points D and E then market price tends to remain constant at P_1.
  Reference to profits: as barriers to entry may exist, this firm can earn SNPs if AR exceeds AC.

(iii) Explain what is meant by the term 'rigidity of prices' under a 'kinked demand curve'

8 marks graded

- This occurs when prices tend not to change when costs change in an oligopolist Industry.
- This is because firms are fearful of the likely reaction of their competitors should they change prices.
- Between points D & E as MR is constant, if MC changes prices tend not to change.

(c) (i) Explain **THREE** types of collusion which may occur in an oligopolistic market.
(ii) Do you believe that the Irish retail market for banking services (e.g. personal current accounts) operates under oligopolistic conditions? Explain your answer. *(25 marks)*

(i)

1. Pricing Policy / Limit Pricing

One firm, with the tacit agreement of others, could reduce prices forcing unwanted entrants out of the industry.

2. Production/output policy

Firms could join together to limit output to certain agreed amounts.

3. Sales Territories.

Firms could divide up the markets between them and agree not to compete in each other's market segments.

4. Refusal to supply firms.

Firms may not supply those firms who buy from firms not in the cartel.

5. Implicit Collusion

Each firm recognises that behaving as if they were branches of a single firm their joint profits would be higher. So firms do not provoke their rivals by cutting prices. Instead they try to increase market share by engaging in non-price competitive measures.

3 forms of collusion at 5 marks each graded.

(ii) Do you believe that the Irish retail market for market for banking services (e.g. personal current accounts) operates under oligopolistic conditions? Explain your answer. *(25 marks)*

The retail market for personal banking services in Ireland operates under oligopolistic conditions because:

1. **Few Sellers**.
   There are relatively few banks providing personal services within the market e.g. AIB, Bank of Ireland etc. Even with the entry of new banks these two dominate the market.

2. **Interdependence between firms.**
   The banks do not act independently of each other. They closely take into the account the likely reactions of their competitors to any changes they may make.

3. **Close substitutes.**
   The services provided are very close substitutes. There is competitive advertising and heavy 'product loyalty' promotion. Various gimmicks are used to attract customers.

2 reasons at 5 marks each graded.

2005

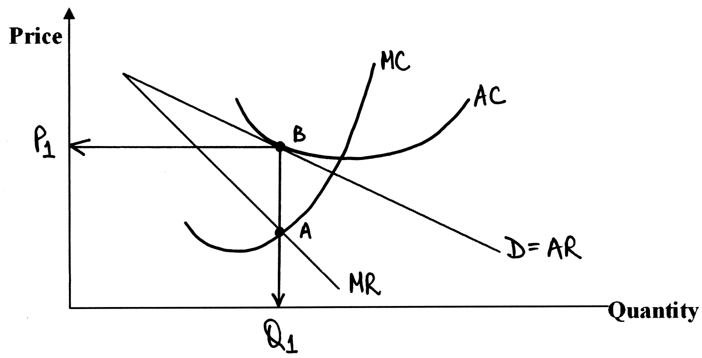
(a) State and explain the assumptions underlying the theory of imperfect competition. *(20 marks)*

1. There are many buyers in the industry.
   - Each buyer acts independently.
   - No individual buyer, by his/her own actions, can influence the market price of the goods.
2. There are a large number of sellers within the industry.
   - Each seller acts independently.
   - An individual seller *can* influence the quantity sold by the price it charges for its output.
3. Product Differentiation exists.
   - The goods, which are supplied by the producers, are not identical goods but are close substitutes.
   - Firms try to establish in the minds of the public that the goods are not perfect substitutes by selling their goods under brand name.
4. There is freedom of entry into and exit from the industry.
   - Firms already in the industry cannot prevent new firms from entering the industry.
   - No barriers to entry exist within the industry.
   - It's possible for firms to enter/leave the industry as they wish.
5. Reasonable knowledge as to profits made by other firms.
   - In the industry everyone concerned has reasonable knowledge as to profits made by other firms.
   - Consumers may not be fully aware of the prices being charged for different products.
6. Each firm tries to maximise profits.
   - The sole aim of each firm is produce that quantity which will maximise its profits in the short run.
   - Hence the aim of a firm is to minimise costs.
   - It will produce where MC = MR.

5 points at 4 marks graded.

(b) (i) Explain with the aid of a clearly labelled diagram the long run equilibrium position of a firm in imperfect competition.
(ii) State and explain **ONE** feature of this firm in long run equilibrium which would be common to a firm in long run equilibrium under **perfect competition**.
(iii) State and explain **ONE** feature of this firm in long run equilibrium which would be common to a firm in long run equilibrium under **monopoly**. *(40 marks)*

(b) (i) The long run equilibrium position of a firm in imperfect competition. **Diagram: 16 marks**



8

Explanation of long run equilibrium:

1. Equilibrium occurs at point A where MC = MR (*and MC is rising and cuts MR from below*).
2. The level of output produced is Q_1 and the price the firm sells this output at is P_1.
3. The average cost of production is shown at point B.
4. This firm is earning normal profits because AR = AC.
5. The firm is not producing at the lowest point of AC (point C).
   This indicates that the firm is wasting scarce resources.

(b) (ii) and (iii)

Perfect Competition	Monopoly
1. Both earn Normal Profit Because AR = AC.	1. Both wasteful of resources Neither produces at the lowest point of average cost:
	2. Downward sloping D/C Both must lower P to increase Q_D
	3. Price is greater than MC Indicates than more of the good could be produced.

Explanation of long run equilibrium and Part (b) (ii) and (iii): 24 marks graded.

(c) Consider the retail market for petrol.
Do you believe that this market operates under conditions of imperfect competition?
State reasons for your answers. *(15 marks)*

The retail market for petrol operates under conditions of imperfect competition because:

1. There are many sellers of petrol within the market e.g. Shell, Statoil, Maxol.
2. The products sold are close substitutes. There is competitive advertising and heavy 'product loyalty' promotion. Various gimmicks are used to attract customers. Sellers also use 'brand names' extensively to maintain consumer loyalty.
3. Each seller can influence the demand for petrol by altering the price as consumers are becoming far more sensitive to the price differences for petrol.

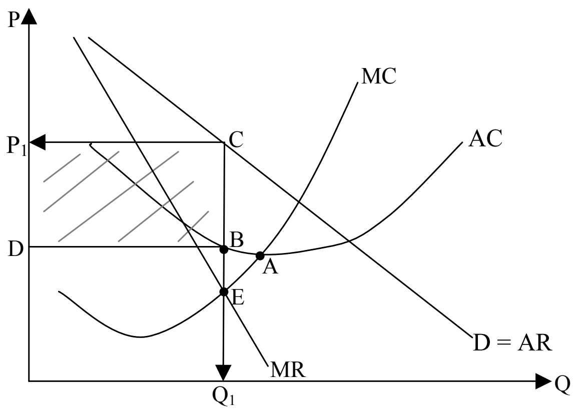
15 marks graded.

Note: Arguments for oligopoly market from a national point of view were also accepted.

2004

(a) Explain, with the aid of a diagram, the long run equilibrium position of a monopoly firm (25 marks)

Diagram



Marking Scheme
9 marks: 9 x 1 mark each

- **Price axis**
- **Quantity axis**
- **D = AR**:
- **MR**
- **AC**
- **MC**

- **Point E / Equilibrium point**
- **Output : Q_1**
- **Price: P_1**

Explanation: 16 marks graded

1. Equilibrium
- **Occurs at point E where**
- **MC = MR [and MC is rising]**

2. Price / Output
- **The firm produces Q1**
- **and sells it at P1**

3. Cost / Normal profit
- **The cost of producing this output / normal profit is shown at point** *B*

4. SNP's
- **The firm is earning SNP's of** *P_1CBD*
- **because AR > AC)**
- **or they can continue to exist due to barrier to entry.)**

5. Use of Scarce Resources
- **The firm is not producing at the lowest point of AC (point A)**
- **hence this firm is wasting scarce resources / inefficiency**

(b) If firms wish to enter a monopoly market they will face barriers to entry. Explain THREE **of these barriers.** ***(15 marks)***

3 points x 5 marks graded.

1. <u>Legal / Statutory Monopoly.</u>
Other firms may not be allowed into the industry because the government confers on a firm the sole right to supply a particular good or service i.e. Aer Rianta.

2. <u>Ownership of a patent / copyright.</u>
If a firm has the sole right to a manufacturing process then no other firm can compete with it. Other firms are not allowed to use this patent until the time period for it has expired.

3. <u>Sole rights to raw materials.</u>
A firm may have complete control over the source of essential raw materials i.e. an oil drilling company.

4. <u>Large capital investment.</u>
- In some industries the minimum size of a firm required to operate efficiently is so large that there is no room for competitors once one firm has established itself.
- Competitors are discouraged from entering because of the high initial start-up costs.

5. <u>Trade agreements /collusion – cartels.</u>
By entering trade agreements with other firms, a firm can share out the market so that no competition exists within its segment of the market.

6. <u>Mergers / takeovers</u>
A firm may ensure their survival by merging / taking over other (rival) firms in the same line of business - such that it becomes a monopolist and no competition exists within the industry.

7. <u>Monopolies based on fear, force or threats</u>
An individual / firm may stop other individuals/firms providing similar goods/services by threats/force – instilling fear into potential entrants i.e. the supply of illegal drugs.

8. <u>Brand proliferation</u>
A firm may gain monopoly power if through its advertising consumers are convinced that there is no suitable alternative to their particular brands

(c) If a monopoly firm wishes to engage in price discrimination, certain conditions must apply. State and explain THREE **of these conditions.** ***(15 marks)***

1. Monopoly Power.
If freedom of entry existed into the industry, competitors would enter where the firm was charging the higher price and earning SNP and this would continue until only normal profit was being earned.

2. Separation of markets.
This is, so that the good bought in the low priced market cannot be offered for resale in the higher priced market. If it was not possible to separate the markets then the above would occur until no price difference existed.

3. Different consumer elasticities of demand.
So that consumers with the high price elasticity of demand are charged the lower prices for their goods e.g. students are assumed to have lower incomes and so are not in the position to pay the full price for certain goods and services.

4. Consumer Indifference.
The difference in price may be so small that consumers are indifferent and so don't mind paying the slightly higher price.

5. Lack of awareness by consumers.
Consumers may be simply unaware that the good is available elsewhere at a lower price.

6. Consumer attitudes to the goods.
A consumer may be willing to pay a higher price for a good which they consider to be in fashion / provide status e.g. young people and their desire for 'branded' products.

3 points x 5 marks graded.

(d) Irish semi-state transport companies are facing increasing competition.
Discuss ONE possible **advantage and** ONE possible **disadvantage of this development for:**
- **Consumers** AND
- **Employees of semi-state transport firms.** ***(20 marks)***

CONSUMERS

Advantages	Disadvantages
1 x 5 marks graded.	**1 x 5 marks graded.**
1. Quality of services. **The competition may force the semi-state companies to improve the quality/efficiency of the service provided.**	**1. Loss of non-profit making services.** **Non-profit making services may be discontinued by the semi-state company in an effort to reduce costs.**
2. More competitive prices. **Increased competition may force the firm to offer consumers more competitive prices.**	**2. Possible reduction in safety standards.** **In the drive towards increased efficiency shortcuts may be taken resulting in a possible decline in safety.**
3. Increased choice / availability of services. **Consumers may now be able to avail themselves of a wider choice of services.**	**3. Decline in standards of service.** **The service provided by the semi-state company may deteriorate in quality in an effort to save costs.**
	4. Disruption to supply of service. **The fear of workers about the effects of competition may cause them engage in industrial disputes disrupting the service for consumers.**

EMPLOYEES OF SEMI-STATE TRANSPORT COMPANIES

ADVANTAGES	DISADVANTAGES
1 x 5 marks graded.	**1 x 5 marks graded.**
1. More motivated workforce. **Competition may pressurise the workforce to become more innovative in their jobs**	**1. Loss of job / reduced job security.** **The biggest risk is the loss of their job through rationalisation of services.**
2. Reward/Incentive for innovation. **If the semi-state firm can meet the challenges of competition, employees may reap more rewards for their innovation i.e. higher bonuses.**	**2. Changes in conditions of employment / Loss of benefits** **The firm may change the conditions of employment for its employees resulting in a worsening of these.**
3. Provision of extra services. **It may now be possible for the company to aggressively pursue its share of the market, without state restrictions, ensuring a growth in employment / additional job security.**	**3. Curtailment in Pay / Pensions ↑'s** **The firm may limit the pay / pension increases due to its employees.**
4. Opportunities from settlement packages **Workers might take the opportunity to change career / use their settlement packages to invest / start a business.**	

2003

(a) Outline **THREE** key features of an oligopolistic market. (20 marks)

1. Few Sellers dominate the industry.
Because of this sellers can influence the selling price of the commodity/or the output sold.

2. Interdependence of firms.
Firms in oligopoly do not act independently of each other. They will each take into the account the likely reactions of their competitors; hence prices tend to be rigid.

3. Product Differentiation occurs.
The commodities, which the firms sell, are close substitutes. Firms will engage in advertising to persuade consumers to buy their product rather than competitors' products.

4. Barriers to entry.
These are common in an oligopolistic market, as existing firms will wish to maintain their share of the market. Examples of such barriers include: high costs of setting up in the industry, brand proliferation etc.

5. Collusion may occur.
Firms within the industry may meet to control the output in the industry and/or control prices e.g. OPEC.

6. Non-price competition is more common than price competition.
Due to fear of how their competitors will react firms tend not to engage in price competition but rather engage in non-price competitive measures to gain consumers from rival firms.

7. Pursuing objectives other than profit maximisation.
Firms may have objectives other than maximizing of profits i.e. increasing their share of the total market, limiting profits to discourage government investigation, satisfaction with the existing level of profits (e.g. in a small family business)

3 features x 6 marks each graded
Must state TWO of the first THREE listed points.

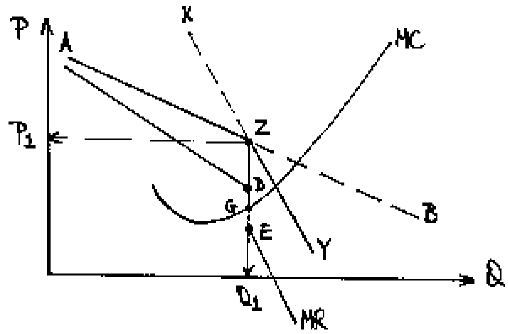
Examples:
Petrol/Oil companies - Shell, Statoil, Esso etc.
Motor Car Manufacturers - Ford, General Motors, Nissan etc.
Retail Banks - AIB, Bank of Ireland etc.
Supermarkets - Tesco, Dunnes Stores, Superquinn etc.
Detergent Manufacturers - Proctor & Gamble, Smith & Nephew.

1 example x 2 marks = 2 marks

(b) With the aid of ONE clearly labelled diagram:
   (i) Explain the shape of the demand curve facing a firm in oligopoly.
   (ii) Explain the relationship between this demand curve and the firm's marginal revenue curve.
   (iii) Explain the long run equilibrium position of this firm. (40 marks)

Diagram

Axes	**2 marks**
Kinked D/C:AZY	**2 marks**
MR	**2 marks**
MC	**2 marks**
Equilibrium: P1 & Q1	**2 marks**



(i) Shape of the demand curve: ***12 marks graded***

- If a firm increases its price other firms leave their prices unchanged - so this firm will lose many customers. This firm faces an <u>ELASTIC</u> D/C - demand curve AB.
- If a firm lowers its price other firms will match this price decrease - the firm will gain few additional customers. Hence the firm faces an <u>INELASTIC</u> D/C - demand curve XY.
- If the price leader sets price at point Z then the firm faces a distinct demand curve: <u>AZY</u>, kinked at point Z.

(ii) Relationship between this D/C and the firm's marginal revenue curve: ***8 marks graded***

- Because the D/C is kinked the firms MR curve consists of 2 distinct parts
- and is constant between point D and point E**,** so irrespective of what happens to costs the firms revenue does not change.

(iii) The long run equilibrium position of this firm: ***10 marks graded***

- Equilibrium is achieved where (a) MC = MR and (b) MC is rising.
  This occurs at point G in the diagram.
- The firm will produce Q_1 and sell this output at price P_1.

Reference to profits position
As barriers to entry may exist this firm can earn SNP's – if AR exceeds AC.
or
Reference to Price Rigidity
Should costs rise between points D and E the market price tends to remain constant at P_1.

(c) Explain THREE methods by which firms in oligopolistic markets may collude.
(15 marks)

1. Pricing policy / Limit Pricing
   One firm, with the tacit agreement of others, could reduce prices forcing unwanted entrants out of the industry.

2. Production/output policy
   Firms could join together to limit output to certain agreed amounts.

3. Sales Territories.
   Firms could divide up the market between them and agree not to compete in each other's market segment.

4. Refusal to supply firms.
   Firms may not supply those firms who buy from firms not in the cartel.

3 x 5 marks each graded

2002

(a) The assumptions underlying the theory of Perfect Competition.

1. There are many buyers in the industry.
- No individual buyer can influence, by his/her own actions, the market price of the goods.
- Each individual firm is a price taker.
- Each individual buyer acts independently.

2. There are many sellers in the industry.
- No individual seller can influence, by his/her own actions the market price of the goods.
- Each individual firm is a price taker.
- Each individual seller acts independently.

3. The goods are homogeneous.
- The goods, which are supplied by the producers, are exactly the same/ identical.
- Thus it is pointless for firms to advertise.

4. There is freedom of entry to and exit from the industry.
- Firms already in the industry cannot prevent new firms from entering the industry.
- No barriers to entry/exist within the industry.

5. Perfect knowledge as to profits and prices.
- In the market everyone concerned has perfect knowledge as to profits made by other firms in the industry.
- Consumers are fully aware of the prices being charged for the products.

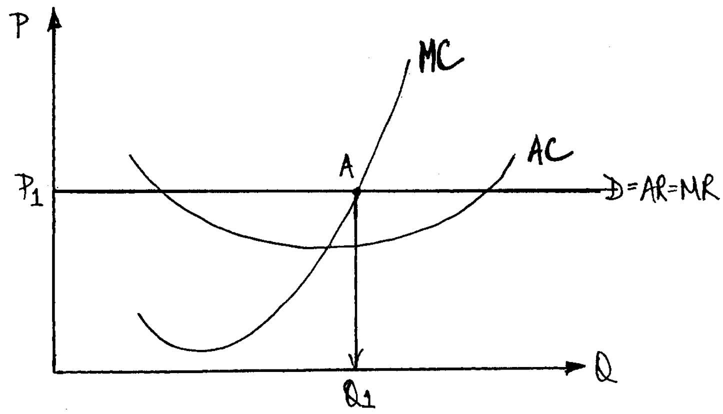
6. Each firm tries to maximise profits.
- The aim of each firm is to produce that quantity where MC = MR.

7. Firms face a perfectly elastic supply of factors of production.
- If a firm wants to increase output it can do so and acquire the necessary factors of production at the existing price i.e. a scarcity of factors of production will not arise, thereby pushing up price.

8. No collusion exists on the market.
- No collusion exists between buyers or sellers of the good. Buyers do not group together with other buyers or sellers do not group together with other sellers in order to influence the price at which the good is sold.

5 x 4 marks graded

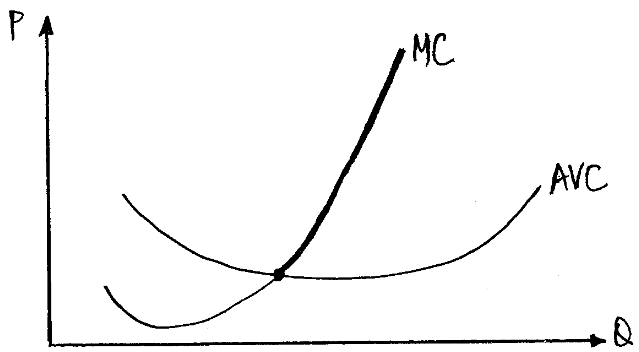
(b) (i) How a firm in Perfect Competition achieves short run equilibrium **10 marks**



In the diagram above:

- the firm will produce where MC=MR, at point A, and produce Q1
- the firm will sell this output at price P1

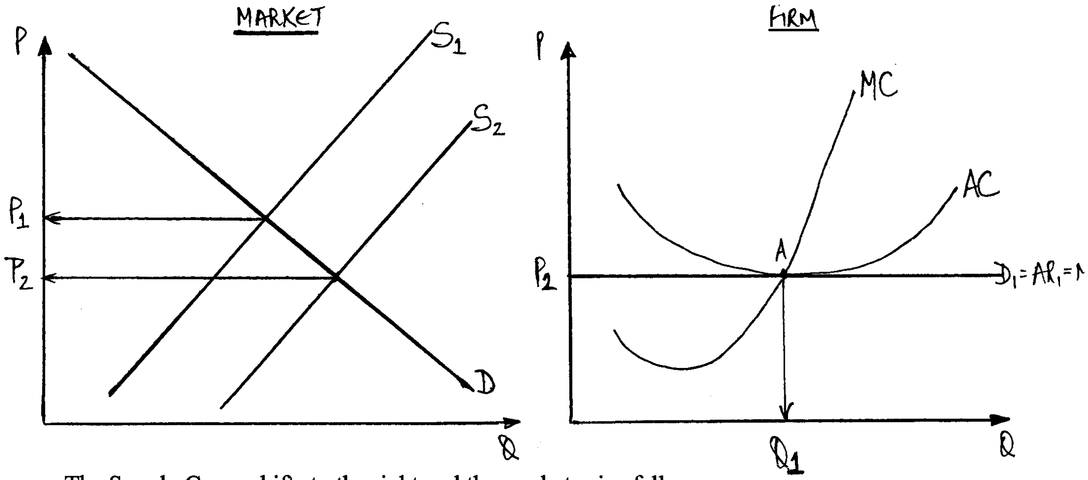
(ii) Derive and explain the short run supply curve of this firm. **10 marks**



- The short run supply curve is that part of the Marginal Cost Curve above the lowest point of the Average Variable Cost.

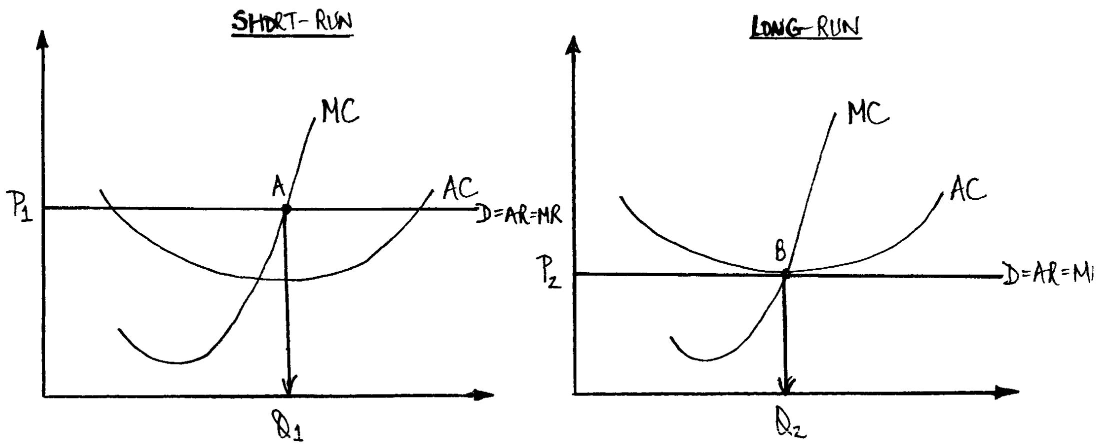
(c) Effect of entry of new firms into a industry earning SNP's	20 marks

Option A –
Diagrams 10 marks/Explanation 10 marks



- The Supply Curve shifts to the right and the market price falls.
- This results in reduced SNP's or SNP's being eroded.

OPTION B
Diagrams 10 marks/Explanation 10 marks



- The S/C shifts to the right and the market price falls.
- This results in reduced SNP's or SNP's being eroded.

(d) Firms in Perfect Competition tend not to engage in advertising.

<u>1. Homogeneous goods</u>
Because the goods are identical, and no differences exist, there is no point in advertising.

<u>2. Increased costs / no additional revenue</u>
If a firm advertises it would increase its own costs and decrease its profits / gain no additional revenues for itself.

<u>3. Benefits the entire industry</u>
Advertising by a single firm would not just benefit this firm, but the entire industry.

<u>2 reasons 8m + 7m graded</u>

2001

(a) State and explain the assumptions underlying the theory of imperfect competition. (25 marks)

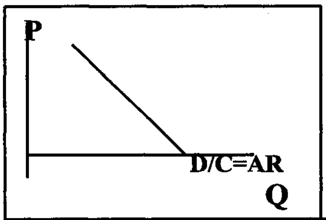
1. There are many buyers / sellers in the industry.
    - No individual buyer can influence, by his/her own actions the market price of the goods.
    - An individual seller can influence the quantity sold by the price it charges for its output.
2. Product Differentiation exists.
    - The goods, which are supplied by the producers, are not identical goods but are close substitutes.
    - Firms try to establish in the minds of the public that the goods are not perfect substitutes by selling their goods under brand names.
3. There is freedom of entry to and exit from the industry.
    - Firms already in the industry cannot prevent new firms from entering the industry.
    - No barriers to entry exist within the industry.
4. Perfect/Reasonable knowledge as to profits made by other firms.
    - In the market everyone concerned has perfect / reasonable knowledge as to profits made by other firms in the industry.
    - Consumers may not be aware of the prices being charged for different products.
5. Each firm tries to maximise profits.
    - The aim of each firm is produce that quantity where MC = MR.

Marking scheme

State: 5 points at 3 marks each = 15 marks
Explain: 5 points at 2 marks each = 10 marks.

(b) Draw the demand curve which faces a firm in imperfect competition and justify its shape. (10 marks)

Diagram



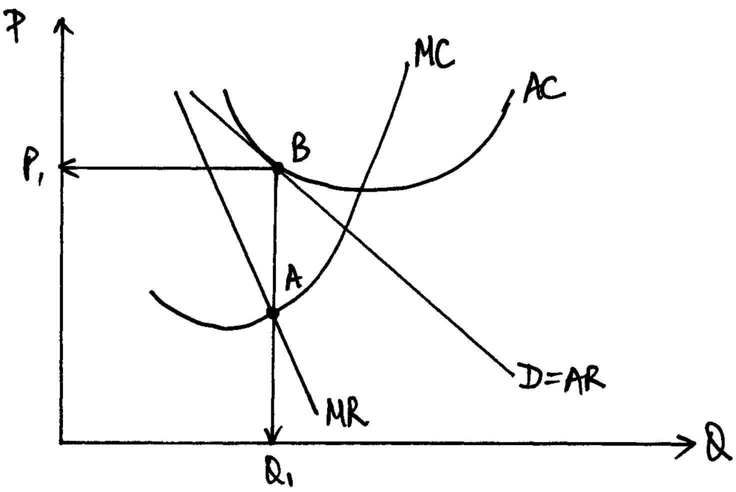
Marking Scheme
Diagram: 4 marks
Effect of a) in Price) 6 marks on demand)

Explanation

- **Because there are many goods, which are close substitutes, if a firm increases its price, there will be a reduction in demand, as some consumers will switch to the competitive goods, which have become relatively cheaper.**
- **If a firm lowers its price it will increase its sales, as some consumers of other substitute goods will switch to this firm's good because it is relatively cheaper.**

Either of the above points

(c) Discuss, with the aid of a clearly labelled diagram, the implications of the assumptions in (a) above on the equilibrium of the firm in the long run under conditions of imperfect competition. (30 marks)



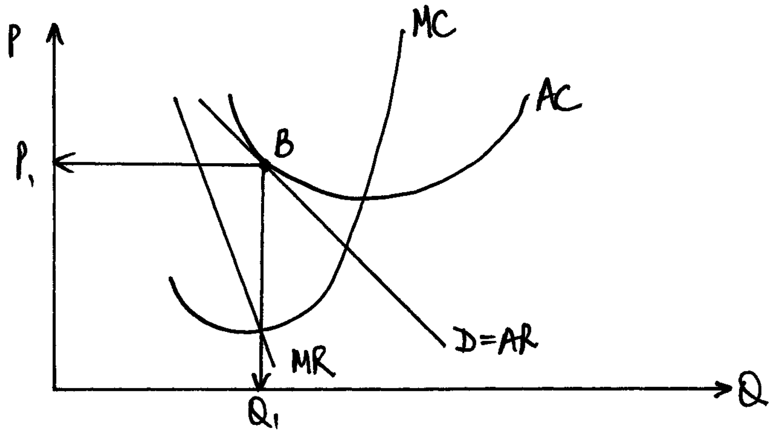
Marking Scheme for Correct Diagram – 18 marks:

Labelling
Price axis, Quantity axis, AR (D), MR, AC and MC: 6 at 1 mark each

Equilibrium output:
Point A (where MC = MR and Output produced Q): 6 marks

Equilibrium price:
Point B (where AR = AC and Price charged P): 6 marks

Diagram – Repeated



Marking Scheme for Correct Diagram – 18 marks:

Labelling
Price axis, Quantity axis, AR (D), MR, AC and MC: 6 at 1 mark each
Equilibrium output:
Point A (where MC = MR and Output produced Q): 6 marks
Equilibrium price:
Point B (where AR = AC and Price charged P): 6 marks

Option A: Candidate assumes short run as starting point

1. In the short run super normal profits may exist within the industry, because there is:
   (a) Perfect knowledge of profits and
   (b) Freedom of entry into the industry
   New firms are attracted into the industry.

2. As these firms enter the existing firms within the industry will lose some of their share of the market – the demand curve facing each individual firm will shift into the left.

3. This adjustment will continue until the super normal profits are eroded and there is no further incentive for new firms to join the industry.

4. So each individual firm achieves long run equilibrium when:
   a) MC = MR and MC is rising (Point A on the above diagram);
   b) AR = AC (point B on the above diagram), the firm is covering its long run costs.

Marking scheme: 12 marks graded

(d) State ONE FEATURE of this firm in long run equilibrium, which would be common to a firm in long run equilibrium under EITHER perfect competition OR monopoly. (10 marks)

Perfect Competition	Monopoly
1. Both earn Normal Profit. AR = AC.	1. Both wasteful of resources. (Neither produces at the lowest point of average cost).
	2. Downward sloping D/C. Both must lower P to increase QD
	3. Price exceeds marginal cost.

<u>One feature clearly stated: 10 marks</u>