AQA - A Level Economics

Individuals, Firms, Markets and Market Failure

5.2 Perfect competition, imperfectly competitive markets & monopoly

Worked Examples

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Contents

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5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 1

A firm selling snack food at a music festival is operating in market conditions of monopolistic competition. It is likely to be

[1]

A Allocatively efficient in the short run and productively efficient in the long run

B Allocatively efficient in the long run and productively efficient in the long run

C Both allocatively and productively efficient in the long run

D Neither allocatively nor productively efficient in the long run

E Both allocatively and productively efficient in the short run

Answer ☐

Explanation [3]

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 1

Answer:
✅ **Correct answer: D – neither allocatively nor productively efficient in the long run [1]**

Explanation:

In **monopolistic competition**, there are **many firms** in the market, and each sells a **slightly differentiated product** , like different snack stalls at a music festival offering burgers, tacos, or fries. **[1]**

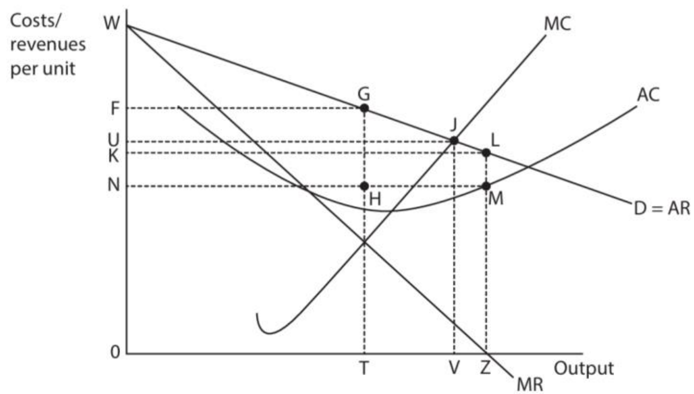
The firm is **not allocatively efficient** because **price is greater than marginal cost (P ≠ MC)**. This means it's not producing at the point where resources give maximum benefit to society , so, not welfare-maximising. **[1]**

It's also **not productively efficient**, as it's **not producing at the lowest point on its average cost (AC) curve → AC ≠ MC**. So, it's not minimising costs either. **[1]**

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 2

The diagram shows the costs and revenues for a firm with monopoly power.



Which of the following statements is true?

A At output T the firm is revenue maximising **[1]**

B At output V the firm is allocatively efficient

C At output Z the firm is productively efficient

D At profit maximising output the supernormal profits are KLMN

E At output Z the price is zero

Answer

Explanation [3]

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 2

Answer:
✅ **Correct answer: D – At profit maximising output the supernormal profits are KLMN [1]**

Explanation:

Allocative efficiency happens when:
Price = Marginal Cost (P = MC or AR = MC)
This means the value consumers place on the good (shown by the price) is equal to the cost of the resources used to make it , so society's welfare is maximised. **[1]**

A **monopoly** is a single firm that has a 25%+ market share. **[1]**

At **output V**, the **AR (demand) curve intersects the MC curve**, which means:
Price = Marginal Cost so **Allocative efficiency.**
Even though this is unusual for a monopoly (they usually set higher prices and restrict output), it might happen if:

- The government forces **marginal cost pricing**
- Or if the monopoly is trying to maximise welfare for some reason. **[1]**

Exam Style Question 3

Assume a firm is operating under conditions of perfect competition. The market price is above the firm's average cost. Which of the following are the most likely long run consequences for this firm?

[1]

A Its price will fall, and it will increase output

B Its price will fall, and it will decrease output

C Its price will rise, and it will increase output

D It will keep its price and output unchanged

E It will shut down and exit the industry

Answer ☐

Explanation [3]

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 3

Answer:

✅ **Correct answer: B – Its price will fall, and it will decrease output [1]**

Explanation:

In perfect competition there are **lots of small firms selling the same product**. No firm can set its own price, they are **price takers**. In the short run, firms can **make supernormal profits. [2]** However, this attracts new firms into the market because they want a piece of the profits. As more firms enter, supply increases, market price falls and **profits shrink until all firms just make normal profit** (price = average cost). **[1]**

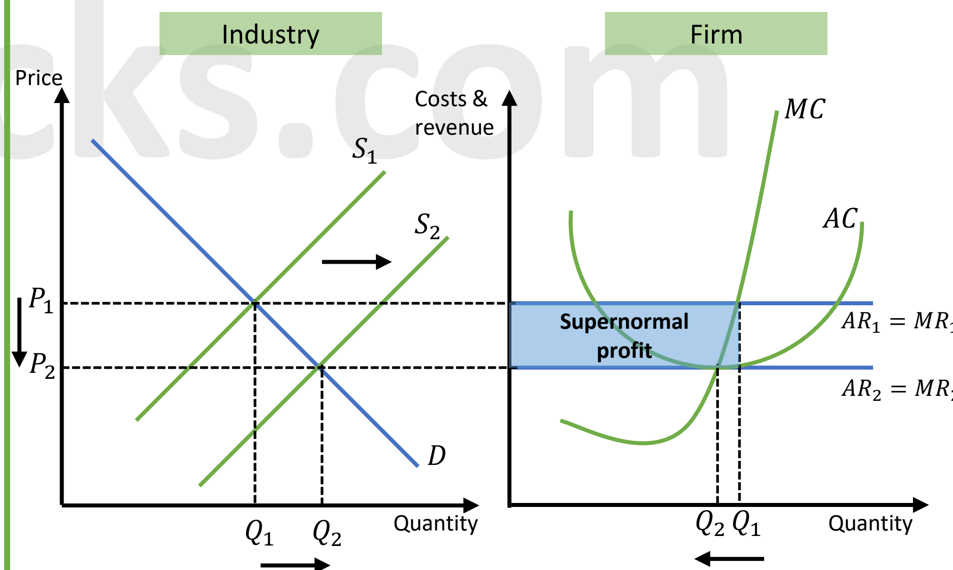


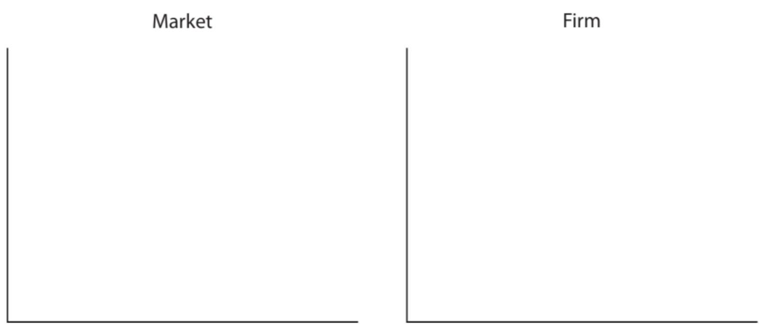
Diagram [3 marks]

Exam Style Question 4

In Sicily, many household's can grow lemons of the same quality as each other. Chiara decides to sell lemons at her local market, expecting to make a normal profit. She notices that all of the many lemon sellers are charging exactly the same price.

(a) Draw diagrams showing the equilibrium positions for both the lemon market and a typical firm in the long run.

[4]



(b) Which **one** of the following will exist in the short run if Chiara makes a loss?

[1]

- ◯ **A** Allocative efficiency and productive efficiency
- ◯ **B** Allocative efficiency and productive inefficiency
- ◯ **C** Allocative inefficiency and productive efficiency
- ◯ **D** Allocative inefficiency and productive inefficiency

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Exam Style Question 4

Answer:

(a) Draw diagrams showing the equilibrium positions for both the lemon market and a typical firm in the long run.

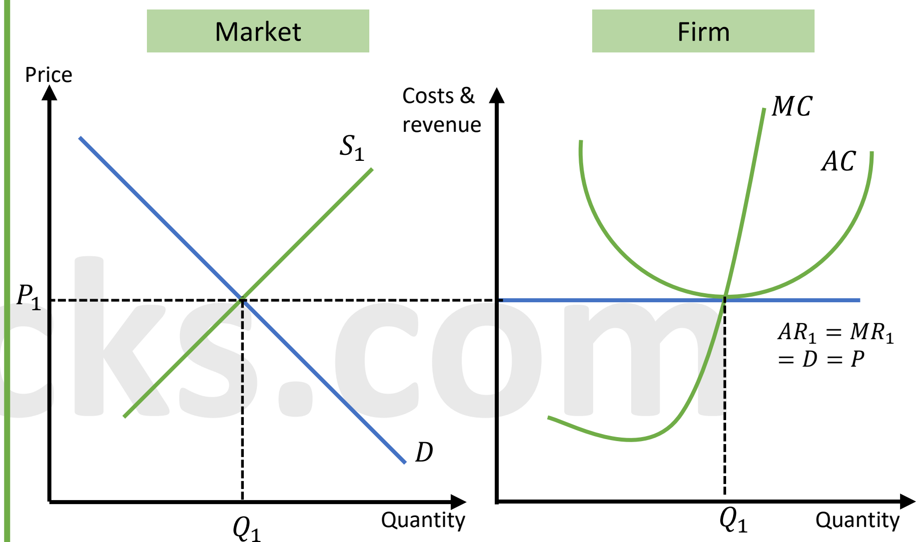

Diagram [4 marks]

(b) Which will exist in the short run if Chiara makes a loss?
Correct answer: **B — Allocative efficiency and productive inefficiency**

Reasons:
- **A incorrect** because the firm is not operating at its minimum point on the AC curve.
- **C incorrect** because P=MC so the firm is allocatively efficient.
- **D incorrect** because of the reasons given in A and C.

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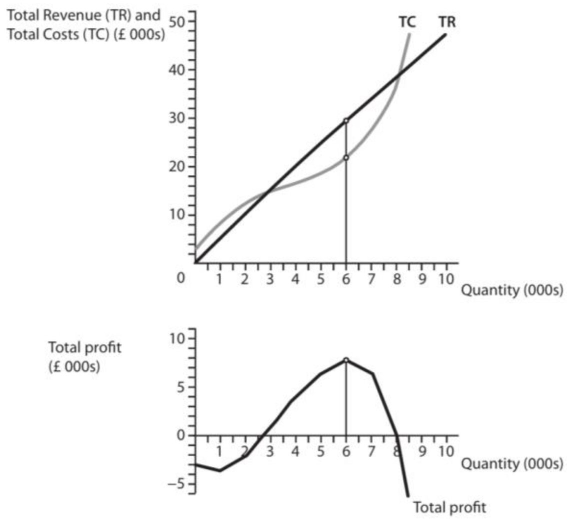
Exam Style Question 5



The diagrams show the costs, revenue and profit for a profit maximising firm. What can be inferred from these diagrams? **[1]**

A The firm operates in a perfectly competitive market in the short run

B The firm will produce at a quantity of 6,000 units in the long run

C There are barriers to entry and exit

D The firm will produce at any output between 2,650 and 8,000 units

E The firm is making a loss

Answer ☐

Explanation [3]

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 5

Answer:

✅ **Correct answer: A - The firm operates in a perfectly competitive market in the short run [1]**

Explanation

The **total revenue (TR)** curve is **a straight line with a constant gradient**, meaning **price is constant [1],** this suggests the firm is a **price taker**. **[1]**

That's a **hallmark of perfect competition** , where the firm accepts the market price and cannot influence it.

The **total cost (TC)** curve shows increasing costs, and the **gap between TR and TC** is biggest at 6,000 units → that's where **profit is maximised**.

The **total profit** graph peaks at **£8,000**, confirming the firm is making **supernormal profit**. **[1]**

In **perfect competition**, firms **can make supernormal profit in the short run** because:

- Not enough firms have entered yet
- There's not yet full adjustment in the market

Exam Style Question 6

According to the Royal Mail, more hair and beauty salons opened on UK high streets last year than any other types of independent business, with a net increase of 10%, representing 626 new salons.

(Source: adapted from https://www.theguardian.com/small-business-network/2016/nov/18/beauty-boom-or-bust-uk-too-many-salons)

(a) The UK hair and beauty industry is an example of monopolistic competition because: [1]

A Firms spend nothing on advertising and research

B The industry is dominated by a few large firms

C The products are homogenous

D There are low barriers to entry and exit

(b) Draw a cost and revenue diagram to show the **long-run** equilibrium of a firm in monopolistic competition. **[4]**

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Exam Style Question 6

Answer:

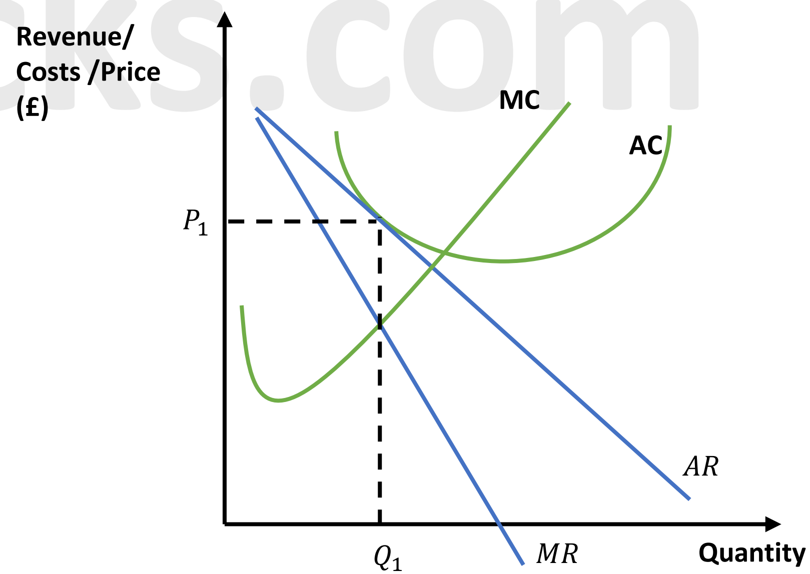
✅ **Correct answer: D – There are low barriers to entry and exit. [1]**

Option A ❌ Firms **do** spend on advertising and branding , salons especially.

Option B ❌ The market isn't dominated by a few large firms, there are **many** small, independent ones.

Option C ❌ The products aren't **homogeneous** each salon tries to be a bit different with its look, service, or niche.

(b) Draw a cost and revenue diagram to show the long-run equilibrium of a firm in monopolistic competition. [4]



5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 7

Which of the following characteristics is shared by a monopolist and a firm operating under conditions of monopolistic competition?

[1]

A Low or no barriers to entry to the industry

B Productive efficiency in the long run

C Some degree of price setting power

D Supernormal profits in the long run

E Allocative efficiency in the long run

Answer ☐

Explanation [3]

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 7

Answer:
✅ **Correct answer: C – Some degree of price setting price [1]**

Explanation
Both **monopolists** and firms in **monopolistic competition** share one key trait: They're not price takers , they're **price setters.**

So, they both face a **downward-sloping demand curve** (or Average Revenue curve), which means:
- They can **raise or lower their price** and **still sell their product**
- They're not forced to charge the market price like in perfect competition **[1]**

A **monopolist** is a firm that dominates the entire market. It's the only seller, so it has **strong price-setting power**. **[1]**

A firm in **monopolistic competition** is one of many sellers, but each offers a slightly different product , like barbers, cafés, or bakeries. This **differentiation gives them a bit of control over price**. **[1]**

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Exam Style Question 8

A firm in long run equilibrium under monopolistic competition will be

[1]

A Allocatively but not productively efficient

B Productively but not allocatively efficient

C Productively and allocatively inefficient

D Making supernormal profits

E Allocatively and productively efficient

Answer ☐

Explanation [3]

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 8

Answer:

✅ **Correct answer: C – Productively and allocatively inefficient [1]**

Explanation

A firm in **monopolistic competition** is one of many sellers, but each offers a slightly different product and therefore the demand is not perfectly elastic. **[1]**

Productive efficiency = producing at the **lowest point** on the average cost curve (AC).

Allocative efficiency = when **price = marginal cost (P = MC)**. This is where society's wants are met perfectly , we're not overproducing or underproducing.

Firms face a **downward-sloping demand curve** because of product differentiation (each business offers something a bit unique).

That means price is **always greater than marginal cost (P > MC)** → not allocatively efficient. **[1]**

Firms also don't produce at the **minimum point on the average cost curve** → not productively efficient. **[1]**

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Exam Style Question 9

The following table shows global sales of PCs by company in 2015.

Company	Sales of PCs (million)
Lenovo	57 182
HP	53 534
Dell	39 049
Apple	20 794
Acer Group	19 680
Others	86 461
Total	**276 700**

(Source: IDC, reported in *The Times*, 14th January 2016)

Calculate the five-firm concentration ratio. You are advised to show your working. **[2]**

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Exam Style Question 9

Answer:
To calculate the **five-firm concentration ratio**, we need to work out how much of the total market is controlled by the **top 5 firms**.

Step 1: Add the sales of the top five firms

57,182 + 53,534 + 39,049 + 20,794 + 19,680 = 190,239 million

Total market sales = 276,700 million

Step 2: Calculate the concentration ratio:

$$Five - firm\ concentration\ ratio = \left(\frac{190{,}239}{276{,}700}\right) \times 100$$

$$Five - firm\ concentration\ ratio = 68.76\% \approx \mathbf{68.8\%}\ \textbf{[2]}$$

Exam Style Question 10

The following table shows the sales (millions) of tablet computers in quarter 3, 2012 and quarter 3, 2013:

(a) The 3-firm concentration ratio in quarter 3, 2012 was 59.2%. Calculate the 3-firm concentration ratio in quarter 3, 2013 in the market. You are advised to show your working. **[2]**

Sales of tablets (millions)		
Manufacturer	**Quarter 3, 2012**	**Quarter 3, 2013**
Apple	14.0	14.1
Samsung	4.3	9.7
Asus	2.3	3.5
Lenovo	0.4	2.3
Acer	0.3	1.2
others	13.5	16.8
Total	**34.8**	**47.6**

(Source: http://appleinsider.com/articles/13/10/30/ipads-marketshare-drops-11-in-q3-on-lack-of-new-models-android-posts-significant-gains)

(b) It can be deduced from this data that the tablet computer market is:

A Monopolistically competitive **[1]**

B Perfectly competitive

C Oligopolistic

D A natural monopoly

(c) Explain **one** barrier to entry that is likely to exist in the tablet computer market. **[2]**

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Exam Style Question 10

Answer:

(a) Calculate the 3-firm concentration ratio in Quarter 3, 2013

📊 **Top 3 firms in Q3 2013:**

- Apple = 14.1 million
- Samsung = 9.7 million
- Asus = 3.5 million

🧮 **Step 1: Add their sales**

$$14.1 + 9.7 + 3.5 = \mathbf{27.3\ million}$$

🧮 **Step 2: Divide by total sales and convert to a %**

$$(27.3 \div 47.6) \times 100 = \sim\mathbf{57.35\%}$$

✅ **Answer:** The 3-firm concentration ratio is **57.4%** (rounded to 1 decimal place). **[2]**

(b) What type of market is this?

✅ The correct answer is: **C – Oligopolistic [1]**

🔍 **Explanation:**

An **oligopoly** is a market dominated by a few large firms exactly what we see here. The top three firms (Apple, Samsung, and Asus) control over 57% of the market. That's a strong indicator that a few big players are holding most of the power, which is classic oligopoly behaviour.

(c) Explain one barrier to entry in the tablet market

Barriers to entry are obstacles that make it difficult for new firms to enter a market. One major **barrier to entry** in the tablet market is **high start-up costs**. **[1]** New firms need to invest **huge amounts of money** into, product development & design, advertising & building brand recognition, etc... **[1]** All of these make it tough for small or new firms to join the market and compete effectively.

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Exam Style Question 11

The following matrix shows the possible revenue outcomes (£ per day) for two firms tendering for contracts to supply in-service training programmes to local authorities. Assuming Hanna Ltd and Jax Ltd have colluded, and agreed a price that will give each a revenue of £1000 per contract, what subsequent actions would lead to a revenue of just £800 per contract?

[1]

		Hanna Ltd	
		High price	Low price
Jax Ltd	High price	1000 / 1000	1200 / 600
	Low price	600 / 1200	800 / 800

A Both firms set a high price

B Hanna Ltd sets a high price and Jax Ltd sets a low price

C Jax Ltd sets a high price and Hanna Ltd sets a low price

D Collusion breaks down

E The firms engage in tacit collusion

Answer

Explanation [3]

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 11

Answer:

Correct answer: D – Collusion breaks down [1]

Explanation

Collusion – When rival firms agree (formally or informally) to avoid competition by fixing prices or limiting output. **[1]**

In the matrix, both **Hanna Ltd** and **Jax Ltd** originally **colluded** and agreed to charge a **high price**, which gave them each **£1000** in revenue per contract. This is shown in the **top left cell** of the matrix. **[1]**

But now they're both earning **£800** and this happens when both **set a low price** (bottom-right cell). So, what went wrong?

Collusion has broken down. This means that although they initially agreed to work together to keep prices high, at least one of them chose to "cheat" and undercut the other, likely to grab more market share and profits for themselves. **[1]**

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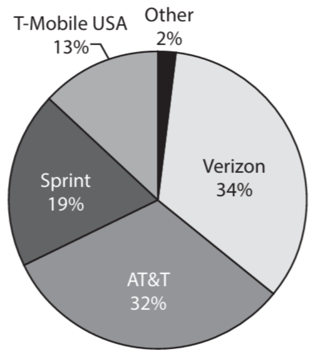
Exam Style Question 12

The diagram shows the market share of the cell [mobile] phone market in the USA.



In August 2014, after a failed attempt at a merger, a price was broke out between T-Mobile USA and Sprint. Under which market conditions are such price wars most likely to occur?

[1]

A Monopolistic competition in the short run

B Monopolistic competition in the long run

C Markets where there is a low concentration ratio

D A low degree of interdependence between firms

E Oligopoly

Answer

Explanation [3]

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 12

Answer:

✅ **Correct answer: E – Oligopoly [1]**

Explanation

A **price war** happens when firms keep undercutting each other by lowering prices to gain more customers but in the process, everyone's profits take a hit. This kind of situation is **classic oligopoly behaviour**. **[1]**

An oligopoly is a market dominated by **a few large firms**. These firms have **interdependent decision-making**, meaning one firm's pricing decision affects the others, so if one drops prices, others feel pressured to follow. **[1]**

You can clearly see that four firms (Verizon, AT&T, Sprint, T-Mobile USA) make up **98%** of the mobile market in the USA, that's a **high concentration ratio**, which is another sign of an oligopoly. **[1]**

In oligopolistic markets, **firms are watching each other closely**. If one lowers prices, others will respond to protect their market share. After the failed merger, T-Mobile and Sprint started cutting prices to stay competitive therefore, a **price war**. **[1]**

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 13

Early in the morning on 19 September 2013, Microsoft revealed that the price of its new games console Xbox One would be £429 in the UK. Later that day, Sony announced that its new PlayStation 4 games console would be sold for £349 in the UK.

One possible reason why Sony chose to price its product significantly lower than Microsoft was because

[1]

A It has first mover advantage

B It wanted to undercut Microsoft and take a large market share

C It wanted to benefit from relatively price-inelastic demand

D It was colluding with Microsoft

E It had higher sunk costs in developing the new games console

Answer ☐

Explanation [3]

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 13

Answer:

✅ **Correct answer: B – It wanted to undercut Microsoft and take a large market share [1]**

Explanation

Market share refers to the proportion of the sales relative to other firms. **[1]**

Undercutting is a classic move in a competitive market with **interdependent firms** (meaning each firm's decisions directly affect the others) as a way to increase sales. **[1]** Microsoft revealed their price **first**, so Sony had the upper hand in responding. Since the products are **close substitutes**, price becomes a key factor and a cheaper option is very attractive to consumers. **[1]**

From a game theory angle if **both firms charge a high price**, they get equal, decent revenue.
But if one undercuts, they **gain market share and revenue**, while the other **loses out**. **[1]**

❌ **Why not the other options?**

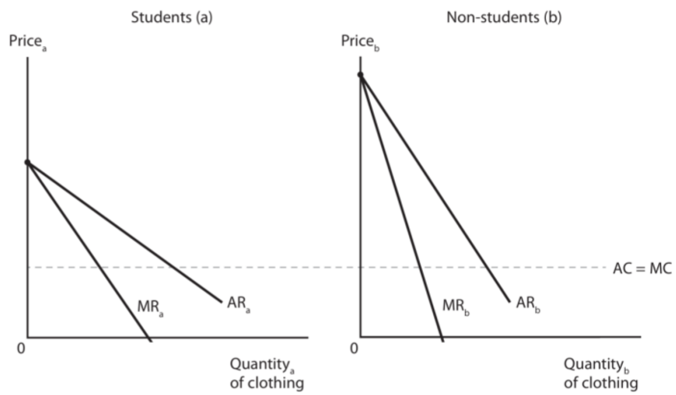
- **A (First mover advantage)** – Microsoft moved first, not Sony, and that put them at a disadvantage.
- **C (Price-inelastic demand)** – In this market, demand is **price-elastic** , consumers are sensitive to price changes.
- **D (Colluding)** – There's zero evidence of that. If they were colluding, they would've agreed on the same price!
- **E (Higher sunk costs)** – That would usually push the price **up**, not down.

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 14

River Island is a clothing retailer. Students are offered a River Island student discount code to benefit from a 10% price reduction as an attempt by the firm to increase profit.

(a) Complete the third-degree price discrimination diagram below. Draw the impact on each sub-market by showing the price and profit. **[4]**



(b) Which **one** of the following is necessary for a firm to be able to practise price discrimination?

[1]

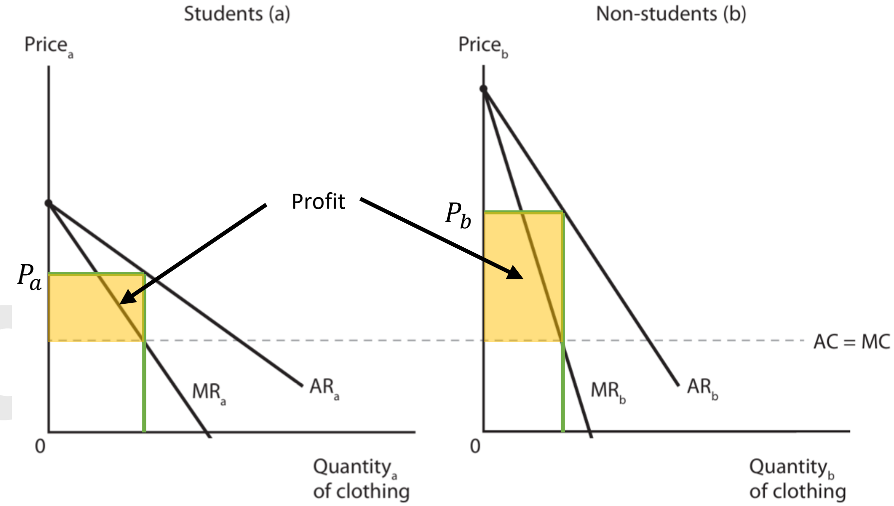
- ○ **A** It has some degree of market power
- ○ **B** It is able to store its product
- ○ **C** Its product has different features in different markets
- ○ **D** The costs of supplying some customers are higher

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 14

Answer:

(a) Complete the third-degree price discrimination diagram below. [4]



(b) Which **one** of the following is necessary for a firm to be able to practise price discrimination?

✅ **Correct answer: A – It has some degree of market power [1]**

❌ **Why not the others?**

- **B –** Nice to have but not needed for price discrimination.
- **C –** That's **product differentiation**, not price discrimination.
- **D –** That's **cost-based pricing**, not price discrimination.

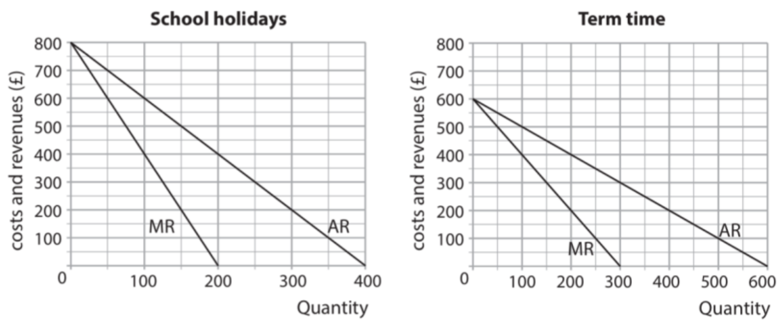
5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 15

A monopolist supplier of holidays to a small island resort splits the market into two sub-markets: one for school holidays and the other for term time. The diagrams show the average revenue (AR) and the marginal revenue (MR) curves for holidays in the two sub-markets.

If the marginal cost of providing one holiday is £200 at any time of the year, what prices should the holiday firm charge in the two sub-markets to maximise profits?

[1]



	Price in school holidays, £	Price in term time, £
A	200	200
B	300	300
C	400	300
D	400	500
E	500	400

Answer ☐

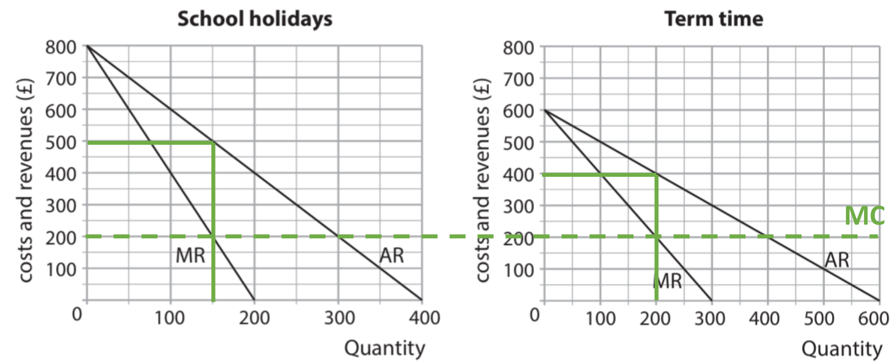
Explanation [3]

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 15

Answer:
✅ **Correct answer: E – £500 in school holiday, £400 in term time [1]**

Explanation
Price discrimination, which is when a firm **charges different prices to different groups of consumers** based on their **elasticity of demand**. **[1]**



- In **School Holidays**, the **MR = MC (£200)** point hits MR at a lower quantity. If you trace up from that point to the **AR curve**, the price is **£500**. **[1]**
- In **Term Time**, MR = MC at a slightly higher quantity, and tracing up to the AR curve gives you a price of **£400**. **[1]**

So:
- **Price in school holidays = £500**
- **Price in term time = £400**

👉 That's option **E**.

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Exam Style Question 16

In December 2013, Virgin Trains quoted the following prices for a single train journey on 27 December at 07.55 hours between London and Manchester:

Passenger/ticket type	Price
Advance	£67.00
Senior citizen advance	£44.20

[1]

The most likely explanation of this pricing strategy is

A To increase revenue

B To take advantage of the lower price elasticity of demand for rail tickets of senior citizens

C That it is easy for tickets to be bought by a senior citizen and used by any passenger

D That the cost of providing seats for advance passengers is higher

E To attract the attention of the competition authorities

Answer ☐

Explanation [3]

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 16

Answer:

✅ **Correct answer: A – To increase revenue [1]**

Explanation

This question is a classic case of **price discrimination**, which is when a firm charges **different prices** to **different groups of consumers** for **essentially the same product** , in this case, a train ticket from London to Manchester. **[1]**

Price discrimination helps a firm **maximise revenue** by charging consumers **what they're willing to pay**.

Revenue refers to the money that is coming into the firm. **[1]**

Virgin Trains is charging **£67** for an advance ticket and **£44.20** for senior citizens.
Senior citizens tend to have **more elastic demand** (they're more price-sensitive; they might travel at off-peak times or not travel at all if it's too expensive). **[1]**
Charging them less means **they're more likely to buy the ticket**, which means **more total revenue** for Virgin Trains than if they priced all tickets the same.

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 17

A bowl of freshly cooked noodles in a Thai market costs 30 baht before 6pm and 60 baht after 6pm every day. What economic reasoning best explains this price change?

[1]

A The demand for noodles is more price inelastic after 6pm

B The cost of making noodles falls after 6pm

C Before 6pm the firms have a high degree of market power

D Firms supplying noodles in this market are aiming for allocative efficiency

E Noodles bought before 6pm can be resold in the same market after 6pm

Answer ☐

Explanation [3]

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 17

Answer:
✅ **Correct answer: A – The demand for noodles in more price inelastic after 6pm [1]**

Explanation
This question is a classic case of **price discrimination**, which is when a firm charges **different prices** to **different groups of consumers** for **essentially the same product. [1]**

Price inelastic demand means that even when the price goes up, people still buy the product because they **need** or **really want** it and don't have many alternatives. **[1]**

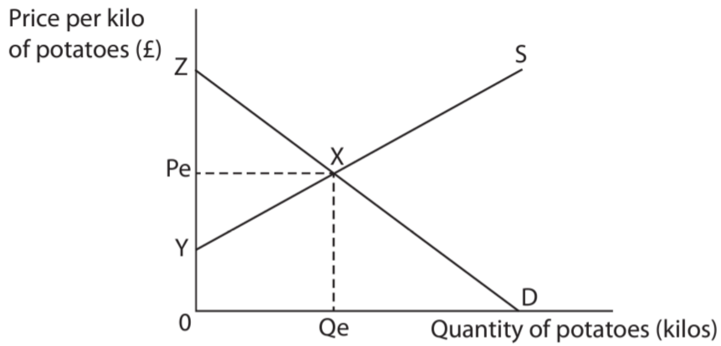
Before 6pm, the price is **30 baht**. After 6pm, it **doubles to 60 baht** yet people still buy the noodles. That suggests they're less sensitive to price at that time, probably because:

- They're hungry after work,
- Fewer food stalls are open, and
- Convenience wins over price.

This all adds up to **inelastic demand** (when demand barely changes despite a higher price). **[1]**

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 18



The diagram shows the market for potatoes where the initial equilibrium price is Pe and quantity Qe. Use the diagram in your explanation?

An increase in demand for potatoes is most likely to

[1]

A: maintain price at Pe and decrease producer surplus

B: raise price and increase producer surplus

C: maintain price at Pe and increase consumer surplus

D: raise price and decrease consumer surplus

Answer ☐

Explanation [3]

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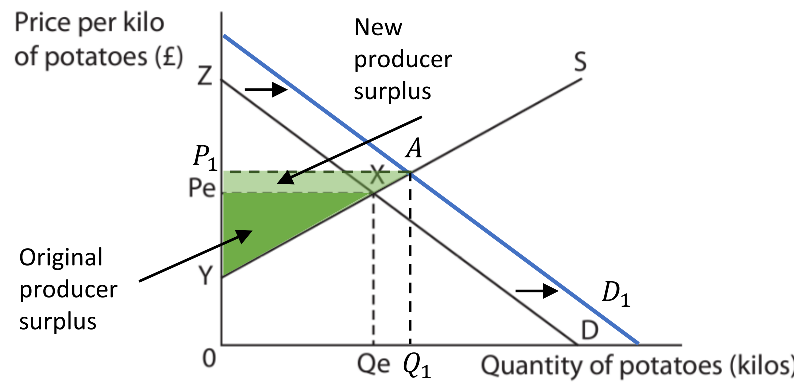
Answer:
B [1]

Explanation:

Definition: Producer surplus is the difference between the price producers are willing to supply to the market and the actual market price **OR** the area between the supply curve and equilibrium price line. **[1]**

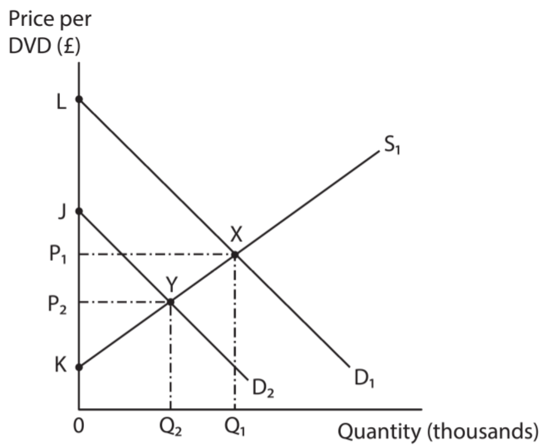


Annotated diagram [2]

Rejection marks

- **A and C: Incorrect** since an increase in demand will cause an increase in price. **[1]**
- **D: Incorrect** as an increase in demand will cause an increase in consumer surplus. **[1]**

Exam Style Question 19



The diagram shows the market for DVDs. A decrease in demand from D_1 to D_2 will cause a fall in

[1]

A: producer surplus to P_2JY

B: consumer surplus to LXP_1

C: producer surplus to P_2YK

D: consumer surplus to $0P_2YQ_2$

Answer ☐

Explanation [3]

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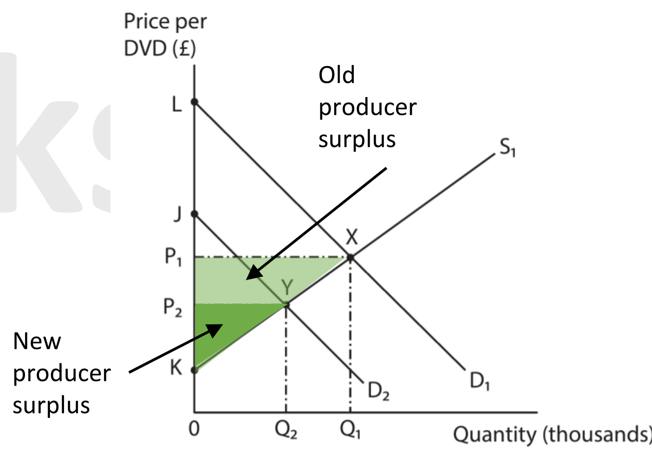
Answer:
C [1]

Explanation:

Definition: Producer surplus is the difference between the price producers are willing to supply to the market and the actual market price **OR** the area between the supply curve and equilibrium price line. **[1]**



Annotated diagram [2]

Rejection marks

- **A: Incorrect** as P_2JY is the new consumer surplus area. **[1]**
- **B: Incorrect** as LXP_1 is the original area of consumer surplus. **[1]**
- **D: incorrect** as $0P_2YQ_2$ is the new area of total revenue or total expenditure. **[1]**

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Exam Style Question 20

Neringa is prepared to pay £2,500 for a luxury cruise to the Caribbean. If the current price is actually £2,000, which of the following might cause her consumer surplus to increase?

[1]

A: An increase in wages paid to cruise holiday workers by £500 per year

B: A decrease in value added tax placed on luxury cruise holidays

C: An increase in the price of the cruise to £3,000

D: A decrease in the number of companies offering luxury Caribbean cruises

Answer

Explanation [3]

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 20

Answer:
B [1]

Explanation:

Definition: Consumer surplus is the difference between the price one is prepared to pay for a good and the actual price **OR** the area above the equilibrium price and below the demand curve. **[1]**

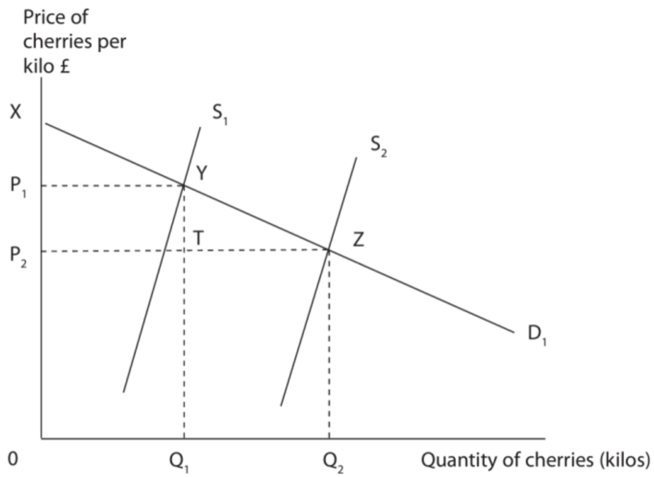
Definition: VAT is a tax placed on the expenditure. **[1]**

Consumer surplus is the difference between what someone is **willing to pay** (£2,500 in this case) and what they actually pay (£2,000 here). To **increase consumer surplus**, the price Neringa pays must go **lower**, making the gap between her willingness to pay and the actual price bigger. A **decrease in VAT** would reduce the price of the cruise, directly increasing Neringa's consumer surplus. **[1]**

Rejection marks

- **A (increase in wages): Incorrect** because this doesn't directly affect the cruise price for Neringa.
- **C (price increases to £3,000): Incorrect** as a higher price would **reduce** her consumer surplus, not increase it.
- **D (fewer cruise companies): Incorrect** as this could reduce competition and possibly **increase prices**, lowering her consumer surplus.

Exam Style Question 21



The diagram shows the market for cherries. In year 1 demand is represented by D_1 and supply by S_1. In year 2, the supply of cherries increases to S_2. This causes consumer surplus to increase to the area:

[1]

A: XYP_1

B: YTZ

C: P_1YTP_2

D: XZP_2

Answer

Explanation [3]

5. Perfect competition, imperfectly competitive markets and monopoly

Exam Style Question 21

Answer:
D [1]

Explanation:

Definition: Consumer surplus is the difference between the price one is prepared to pay for a good and the actual price **OR** the area above the equilibrium price and below the demand curve. **[1]**

Original consumer surplus is XYP_1. **[1]**

Increase in consumer surplus is P_1YZP_2. **[1]**

Please see the '5.1 Perfect competition, imperfectly competitive markets and monopoly Revision Notes' pack for detailed notes.

For more revision notes, tutorials, worked examples and more help visit www.tutorpacks.com