

Best Uses:

- ⊙ Try the “blue box” below to improve the accuracy of your diagrams in this section
- ⊙ Make sure you understand the checklist in Table 1.

2.11 Market Power (HL)

SYLLABUS REFERENCE 2.11¹: Theory of the firm: Must know information and how to draw accurate diagrams.

Table 1 Checklist

Need to know checklist: note these webnotes are found in the old economics.isdedu.de website

1. Draw profit max output level for all 4 models
2. SRAC- U shaped **Why? AFC + Diminishing returns.** (webnote 216)
3. LRAC- U shaped **Why? Economies of scale.** (webnote 216)
4. Productive efficiency? **Where? lowest point of AC curve**
5. Allocative efficiency? **Where? MC=AR** see webnote 218
6. Profit maximising o/p? **Where? MC=MR**
7. Abnormal profit? **Where? AR>AC.**
8. Break even point of a firm in PC see (webnote 221)
9. Shut down point of a firm in PC? **Where? mr = mc = avc**
10. DMR: diminishing returns (see webnote 211)

Main 2.3 Focus – Must know for each of the 4 Models
Exam Q’s will focus on:

1. Profit maximising output where **MR=MC** (see item 1,2 and 3 in table 1 below) or alternatives see web 242
2. Normal or supernormal profits
3. efficiency in terms average unit cost
4. high or low level of output
5. importance of economies of scale

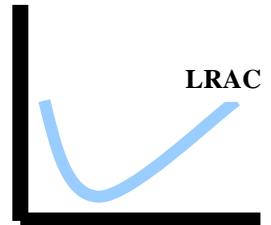
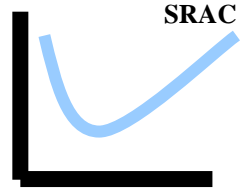


Table1: Summary of the 4 competitive models in the Long Run

Main concepts	<u>PC</u>	<u>M-istic</u>	<u>O</u>	<u>M</u>
1. Max Profit MR=MC	MR=MC	MR=MC	MR=MC	MR=MC
2. Allocatively efficient MC=AR	Yes	No	No	No
3. Productively efficient MC=AC	Yes	No	No	No
S/N Profit	SR only	SR only	SR+LR	SR+LR
Efficiency/price taker or maker	Lowest point of AC. Price taker. Efficient. Competitive Industry.	Not at Lowest point of AC. Price taker or maker. Low price power. Non Price	Not at Lowest point of AC. Often a Price maker. Can have high price	Not at Lowest point of AC. Often a Price maker. Can have high price

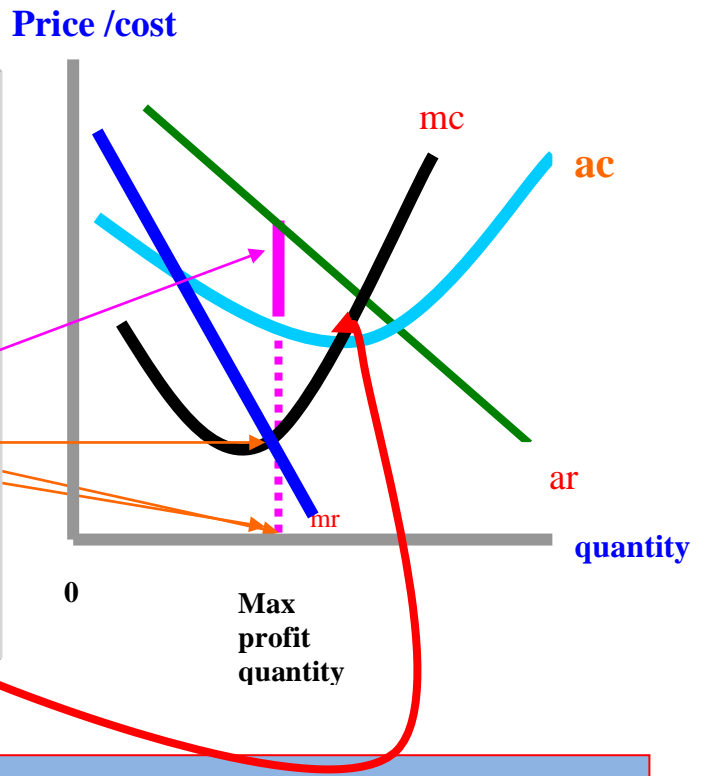
¹ 1 of 1

		competition.	power. Non Price competition.	power. Non Price competition.
Output level/market share	Low	Low	High	High
Econ. Of scale	No	Unlikely	Likely	Likely

The Diagrams: How to draw them accurately?

Note to diagrams:
 Look for the following points in order to analyse/evaluate each of the 4 types of competition:

- 1. S/N exists where $AR > AC$
- 2. Max profit at $MC = MR$
- 3. Efficiency at lowest point of AC



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Tips...to make sure you get your diagrams correct!

1. Draw AR and AC
2. Select a max profit quantity on the x-axis ($mr=mc$)
3. from this point highlight S/N profit where $AR > AC$ (or normal profit or losses)
4. Add in MC cutting AC (at lowest point or not?)
5. Add in MR. It must be where you have marked the profit maximising level of output in item 2 above

Note: remember for PC: $AC=AR$ (ar is drawn horizontal)