

Edexcel (B) Economics A-level

Theme 4.1: Competition and Market Power

Flashcards

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List the 4 types of market structures



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1. Monopoly
2. Oligopoly
3. Imperfect competition
4. Perfect competition



What is the main goal of a monopoly?



What is the main goal of a monopoly?

Profit maximisation



Do monopolies face high or low barriers to entry?



Do monopolies face high or low barriers to entry?

High barriers to entry



How much of the market share must a firm have in order to gain monopoly power?



How much of the market share must a firm have in order to gain monopoly power?

25%



How do economies of scale help monopolies maintain their market share?



How do economies of scale help monopolies maintain their market share?

It gives incumbents a cost advantage, so they can offer consumers lower prices, thus deterring new entrants



How does limit pricing work?



How does limit pricing work?

Firms will offer their goods at prices below the production costs, so new entrants cannot enter the market and gain a profit



How does an oligopoly differ from a monopoly based on the number of firms?



How does an oligopoly differ from a monopoly based on the number of firms?

A monopoly usually has 1 firm in the market, whereas an oligopoly has more than 1



What does it mean if firms are interdependent?



What does it mean if firms are interdependent?

The actions of one affect the actions of all others



How high are barriers to entry in an imperfectly competitive market?



How high are barriers to entry in an imperfectly competitive market?

Low barriers to entry



Do firms have market power in imperfectly competitive markets?



Do firms have market power in imperfectly competitive markets?

Firms have relatively low market power in these markets



Are firms price makers or takers in perfect competition?



Are firms price makers or takers in perfect competition?

Price takers



Is there a degree of product differentiation in perfect competition?



Is there a degree of product differentiation in perfect competition?

No, products are homogenous



What is the main objective of perfectly competitive firms?



What is the main objective of perfectly competitive firms?

Short-run profit maximisers



What happens to market saturation as firms start to make more profit in perfect competition?



What happens to market saturation as firms start to make more profit in perfect competition?

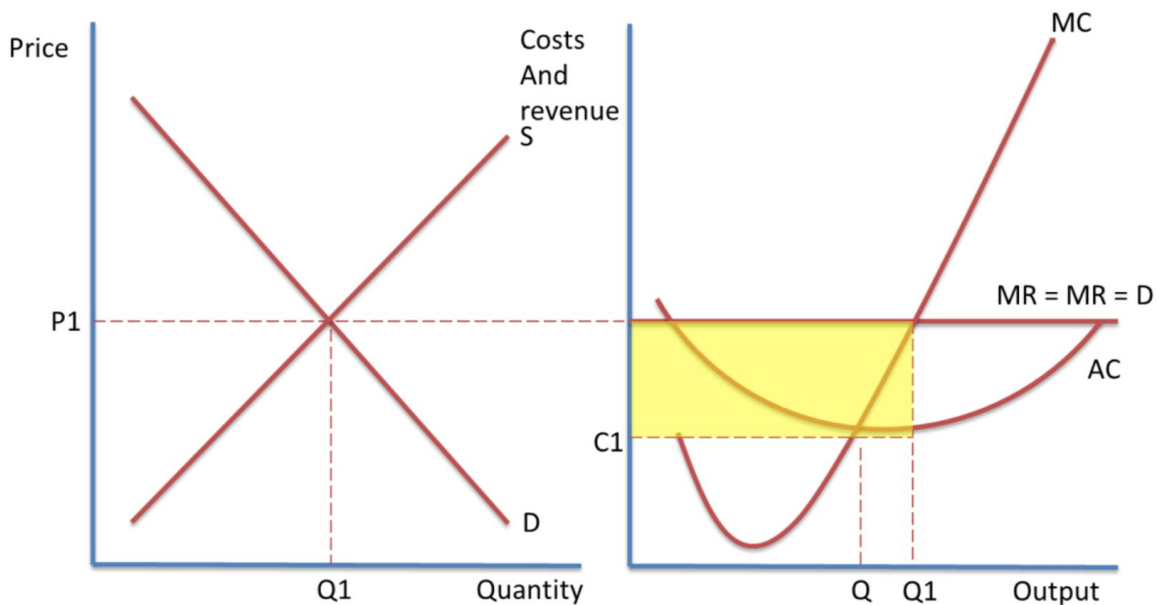
New entrants start joining the market due to the new profit motive, thus making the market more saturated



Draw two graphs representing short run supernormal profits in a perfectly competitive market



Draw two graphs representing short run supernormal profits in a perfectly competitive market



Why is this supernormal profit only in the short run?



Why is this supernormal profit only in the short run?

New entrants will join the market, attracted by the extra profit, thus shifting supply outwards and reducing that supernormal profit



Are there any economies of scale in perfectly competitive markets?



Are there any economies of scale in perfectly competitive markets?

No



Describe price skimming



Describe price skimming

This is when a new, unique product enters the market, so the price of it is set high before new entrants create their own versions of the product



Describe price penetration



Describe price penetration

This is when goods are initially given a low price in order to attract consumers and boost customer loyalty



What price is a good with a high PED most likely to have?



What price is a good with a high PED most likely to have?

A low price, because quantity demanded is more sensitive to price changes



What is a contestable market?



What is a contestable market?

These are markets that face actual and potential competition



What is productive efficiency?



What is productive efficiency?

This is when firms operate on the lowest point of their average cost curve



What is hit-and-run competition?



What is hit-and-run competition?

This occurs when firms enter the market, take up the supernormal profits, and then exit



Why are firms in contestable markets constantly innovating?



Why are firms in contestable markets constantly innovating?

This is so they don't lose market share or profit with the arrival of new firms into the market



How do low barriers to entry affect contestability?



How do low barriers to entry affect contestability?

Low barriers to entry increase contestability



Give an example of legal barriers to entry



Give an example of legal barriers to entry

Patents and Intellectual Property Rights
(IPRs)



How does consumer loyalty affect elasticity of demand?



How does consumer loyalty affect elasticity of demand?

This makes goods more PED inelastic



How do you calculate the concentration ratio of the top firms in a market?



How do you calculate the concentration ratio of the top firms in a market?

Add together the proportion of market share of these top firms



How does collusion affect price and consumer surplus?



How does collusion affect price and consumer surplus?

It usually results in an increase in price and decrease in consumer surplus



Why is there less likely to be collusion when there are many firms?



Why is there less likely to be collusion when there are many firms?

It is easier for firms to get caught by regulatory bodies



How does tacit collusion differ from overt collusion?



How does tacit collusion differ from overt collusion?

Tacit collusion occurs when there is no formula agreement, whereas the latter involves formal agreements



What is the most famous example of a cartel?



What is the most famous example of a cartel?

The Organisation for Petroleum Exporting Countries (OPEC)



How does price leadership increase market stability?



How does price leadership increase market stability

If the dominant firm changes their price, all other firms will most likely follow suit else they risk losing market share



Which UK industry is always in price wars?



Which UK industry are always in price wars?

The UK supermarket industry



What are sunk costs?



What are sunk costs?

Unrecoverable costs



What is game theory used to predict in oligopolies?



What is game theory used to predict in oligopolies?

Used to predict the outcome of a decision of one firm when they have imperfect information about their competitor



What is the Nash equilibrium?



What is the Nash equilibrium?

This is the optimal strategy for all firms in an oligopoly



How could supernormal profits yield positive externalities?



How could supernormal profits yield positive externalities?

By investing these supernormal profits into R&D to increase productivity



How do supernormal profits benefit the government?



How do supernormal profits benefit the government?

It increases tax revenues



Define price discrimination



Define price discrimination

This is when a firm charges different prices to different consumer groups for the same good/service



How does price discrimination benefit monopolies?



How does price discrimination benefit monopolies?

It maximises their profit potential



How does first degree discrimination differ from third degree?



How does first degree discrimination differ from third degree?

First degree involves charging individual consumers different prices, whereas third degree involves charging consumer groups different prices



How could price discrimination be dangerous for firms?



How could price discrimination be dangerous for firms?

They could face regulatory scrutiny by the Competition and Markets Authority (CMA)



What is allocative efficiency?



What is allocative efficiency?

This occurs when resources are allocated to the best interests of society



What is marginal utility?



What is marginal utility?

This is the extra satisfaction derived from consuming one extra unit of output



What is the law used to describe the demand curve?



What is the law used to describe the demand curve?

The law of diminishing marginal utility

