

SU 3

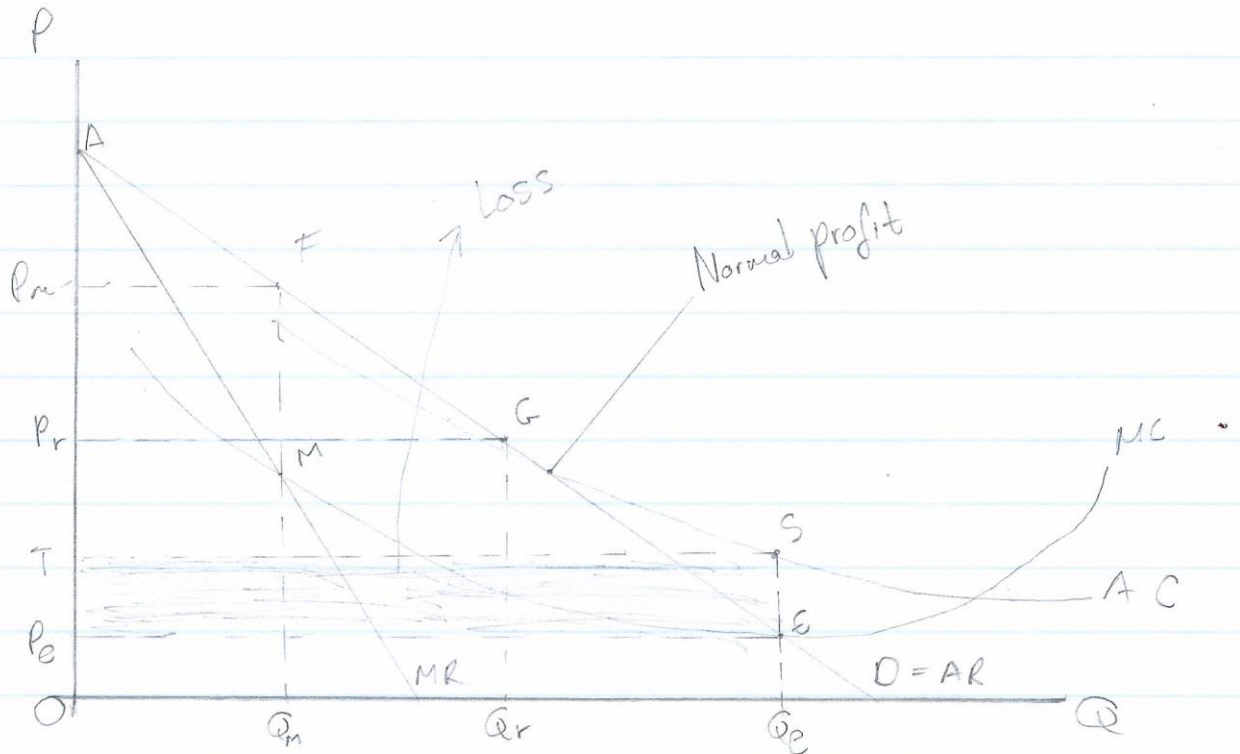
Oct/Nov 2012 SA: Q1: (d) (2 marks)

Any two of:

- deregulation (remove barriers to entry)
- do nothing (in LT... D curve becomes more elastic)
... markets are contestable
- tax policy
 - income tax (no allocation effect) (profits are reduced) (markets are contestable)
 - unit tax - shift AC & MC up... $Q \downarrow$ & $p \uparrow$... (not really getting closer to optimum)
 - lump-sum tax - AC shifts up no allocation effect (profits are reduced)
- price control (set $P = MC$) ... but can MC be measured?

Oct/Nov 2012 SB: Q8: (a) (15 marks)

Nov Oct/Nov 2012 SA: Q3: (15 marks)



Natural monopoly - decreasing cost

• What is a natural monopoly?

→ large capital outlays, economies of scale.
demand satisfied by one firm... e.g.
bulk water supply

→ MC lies below AC over output range for which there is a demand

→ Equilibrium where $MC = MR$ at P_m and Q_m

• Consumer surplus = $A F P_m$

• P.C equilibrium where $MC = P$

• P_e & Q_e

• Consumer surplus = $A E P_e > J B P_m$

• At P_e a loss is made = $T S E P_e$

Role of govt? (using partial framework)

• Nationalise + unit subsidy (ϵ loss = ES)

• privatisation of public corporations? still requires regulation

• regulate (price capping = point G) profit = GH per unit

May/June 2012 SB: Q4: (b) (10 marks)

Artificial (or statutory) monopoly:

- deregulation (remove barriers to entry)
- do nothing (in LT... D curve becomes flatter)... markets are contestable
- tax policy
 - income tax - no allocation effect... (profits are reduced)
 - unit tax - shift AC & MC up $Q \downarrow$ & $P \uparrow$
(not really getting closer to social optimum)
 - lump-sum tax - AC shift up no allocation effect (profits are reduced)
- price control (set $P = MC$)... but can MC be measured?

Natural Monopoly

- regulating
- nationalise
- marginal cost pricing
- average cost pricing
- price or profit capping option.