Final Exam Study Questions:

(A subset of these questions/concepts will be on the exam. Also, questions on the Midterm #2 study guide that weren’t used could also be on the final.)

Chapter 16 – Monopolistic Competition
- What are the characteristics of Monopolistic Competition?
- What is the difference between monopolistic competition and monopoly?
- What is the difference between monopolistic competition and perfect competition?
- Why is advertising important to monopolistic competitors?
- In the long-run, do monopolistically competitive firms earn positive economic profits? If so why? If not, why not?
- What are the positive and negative externalities associated with monopolistic competition?

Chapter 17 – Oligopoly
- Define oligopoly. How does game theory factor into oligopolistic competition?
- In oligopoly competition, what is the tension between cooperation and self-interest?
- Describe the concept of a Nash Equilibrium. Give an example of a Nash Equilibrium.
- What is the Prisoners’ Dilemma in game theory? Give an example of a situation in economics or political science that is essentially a Prisoners’ Dilemma type game.
- What are a couple of ways the inefficient result of a Prisoners’ Dilemma situation be rectified?
- How does the size of an oligopoly affect the market outcome?
- Define predatory pricing. Why are economists skeptical of its usefulness as a business strategy?

Chapter 10 - Externalities
- Define externality. How do economists view externalities from a market standpoint?
- How does an externality result in a suboptimal market equilibrium? (Use a graph in your answer).
- How does government “internalize an externality”? Give examples for both positive and negative externalities.
- Why do economists like the idea of tradable pollution permits to reduce pollution?
- What are some private solutions to negative externalities?
- What is the Coase Theorem and how does it apply to externalities? Under what conditions does it fail to internalize an externality?
Chapter 11 – Public Goods
- What are the basic characteristic used when describing public goods and common resources?
- What are the characteristics of a public good? Give an example of a public good.
- What are the characteristics of a common resource? Give an example of such a good.
- What is the free rider problem? What are some ways for government to remedy the problem?
- Describe the “tragedy of the commons.”
- Why are property rights important in the study of public goods?

Chapter 9 – Trade Applications
- Suppose the $P_{\text{World}}$ of a good is greater than $P_{\text{Domestic}}$ in a country without trade. What happens to the domestic market for the good after the country opens up to trade?
- If, after opening up to trade, a country imports a good, how does domestic welfare, in terms of the good, change?
- How are the world price of a good, domestic price (before trade) of the same good, and comparative advantage related?
The price of oil, and everything derived from it, has fallen recently. As a result, the price of PVC pipes has dropped significantly and is being used extensively in commercial property landscape watering systems. However, a report just came out from the Union of Concerned Scientists indicating that off-gassing from PVC pipes has had a negative impact on local bee colonies and thus, the local agriculture industry. A) Draw a graph representing the private market for PVC pipes, and any market-failure. Your graph should clearly indicate whether the externality is positive or negative. B) Indicate on your graph, with prices and quantities, what the result of a corrective government policy would be. C) How might the government decide on the pricing of the corrective policy?

Joe’s Brickyard (JB) and Peggy’s Construction Supply (PCS) are a duopoly in the local brick business, know each other well, and know each other’s business strategies, profits, costs, revenue etc. Economists have projected that there will be substantial growth in the building industry in the coming months and Joe and Peggy are planning advertising campaigns to drum up business. Each can engage in an expensive ad campaign (High) or modest ad campaign (Low). The figure below indicates the increase in revenues each will observe given their own ad campaign strategy and their competitor’s. A) Using the dynamics of competition under oligopoly and game theory indicate what is the dominant strategy for both firms. B) What kind of economic concept does this represent and why is it suboptimal from an economic standpoint? C) Can you think of a mechanism, legal or otherwise, where these two competitors could arrive at the optimal solution?

---

**Peggy's Strategy**

<table>
<thead>
<tr>
<th>Joe's Strategy</th>
<th>High Ad campaign</th>
<th>Low Ad campaign</th>
</tr>
</thead>
<tbody>
<tr>
<td>High Ad campaign</td>
<td>16%↑</td>
<td>20%↑</td>
</tr>
<tr>
<td>Low Ad campaign</td>
<td>15%↑</td>
<td>18%↑</td>
</tr>
</tbody>
</table>
The figure below indicates a firm in a monopolistically competitive market. A) What price will the firm charge and how much will it produce in order to maximize profits? B) At this level of output, how much is it charging over marginal cost? What are its maximum profits? C) What is an efficient scale of production for the firm?
The world market for wheat is perfectly competitive. The following graph shows the domestic wheat market in the country of Wheatlandia. $P_{ROW}$ indicates the world price of wheat (where $ROW =$ Rest of World). If Wheatlandia opens up to trade, A) will the domestic price of wheat change and by how much? Will Wheatlandia import or export wheat and much? B) How will domestic welfare change? Who gains and who loses? C) What groups in the country, if any, will want to prevent Wheatlandia opening up the wheat market to the world?

Domestic Wheat Market for the country of Wheatlandia
The following diagram indicates a firm in a competitive market and its corresponding costs curves (Average Total Cost, Average Variable Cost, and Marginal Cost). If \( P_1 \) represents the current market price, what are the firm’s profits? What can we say about this firm’s plans for production in the long-run? If, in the next month, the market price rises to \( P_2 \), what are the firm’s profits and LR production plans? Same question for \( P_3 \) and \( P_4 \). What will most likely happen in the LR in the market if in the SR, price = \( P_4 \)?

Similar to the midterm exams, the final exam will consist of four parts:

- **Part A** will consist of multiple choice questions.
- **Part B** will consist of short answer/definitions/graphs and will be taken from the above listed study questions and from the study guide for Mid #2.
- **Part C** will consist of quantitative/graphical questions.
- **Part D** will consist of an essay question on one the class articles.