GRADO EN TURISMO

Introducción a la Economía

Questions and exercises

Unit 5

Answers

1. **Why in Perfect Competition does marginal revenue coincide with price and in Monopoly it does not?**
   In a market of perfect competition there are so many companies that any one of them is insignificant, therefore, it cannot affect the market price, and it takes it as given (accepting price). This implies that for each unit that sells its total revenue increases by an amount equal to the price at which that unit sells. That is why it is said that Marginal revenue equals price.
   In a monopoly market there is only one company, therefore, the price at which it sells its product depends on the quantity it sells, and is determined by the market demand curve. If you increase your sales by one unit, the price decreases, that is, if before you sold 100 units at a price of € 1,000, you now sell 101 units at a price of € 999, therefore, the total income goes from 100,000 to 100,899, so the marginal revenue is 899, which is less than the price. The price drop affects the last unit sold and all those sold.

2. **In a city there are several ice cream shops in which the price of ice cream is € 2, the marginal cost is € 2 and the average cost is € 1.5. Do you think these companies are making short-term profits? What will happen in the long term?**
   Firms decide their output by equating marginal revenue to marginal cost. In this case, we assume that they are perfectly competitive, so they equal price to marginal cost. Once its production has been determined, to know if they have profits or not, the price must be compared with the average cost (which is the unit cost). These ice cream shops are making short-term profits because the price is higher than the average cost. Consequently, more ice cream shops will open in the city (business entry) in the long term, and that will increase the supply. Then the price of ice cream will go down. Thus until the price is equal to the average cost (price = marginal cost = minimum of the average cost) so there will be no profits or losses in the long term.

3. **Which of the following is an example of price discrimination?**
   a. The price difference between the train ticket and the bus ticket for the route Cartagena - Madrid
   b. The price difference between bunk wagon and comfortable bed wagon on a night train
   c. The most expensive express fee to access the museum without queuing
   d. All are correct

   The answer is c). In the other cases, it is not the same good or service offered at different prices.

4. indicate similarities and differences in terms of:
   a. Number of firms
   b. Company’s power to set the price
   c. Product differentiation
   d. Barriers to entry
   For each of the following types of market: perfect competition, monopoly, oligopoly, monopolistic competition.

5. Why is advertising important in monopolistic competition markets? Give examples of this type of market.