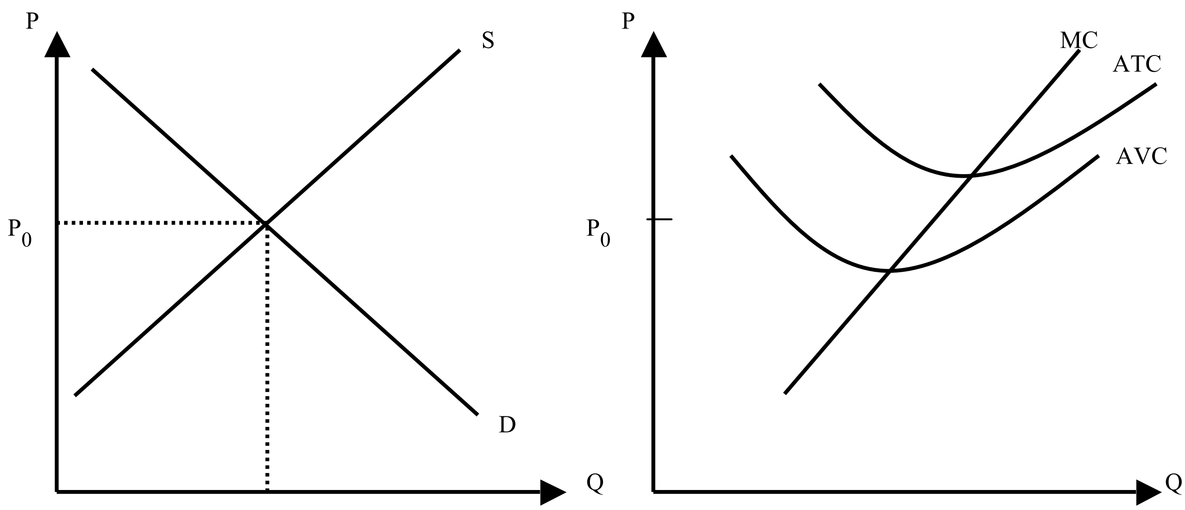
Perfectly Competitive Market

1. The picture on the left panel shows the market equilibrium of a product. The picture on the right panel shows the cost curves of a competitive firm in this market



   (a) Determine the profit maximizing or loss minimizing quantity and price for the firm. Explain why such quantity should be chosen. What is the size of the profit or loss? Should the firm produce at all? Why?

   (b) Analyze the impact of an economic recession on the market price, quantity sold by the firm, the size of profit or loss. Should the firm produce at all? Why? [Specify your assumption clearly]

2. A fruit vender operated in a perfectly competitive market is selling its outputs at the point where profit is maximized. One day the Mafia who controls the area forces the vender to pay a protection fee = 100 baht per day. The vender is still making some profit. Should the vender increase the price or increase the output to cover the extra cost? Draw a graph and explain why?

3. Continue from question 2, if the Mafia charges the protection fee = 1 percent of the selling price instead. The vender is still making some profit. Should the vender increase the price or increase the output to cover the extra cost? Draw a graph and explain why?

4. Suppose the owner of a firm in a perfectly competitive market has special management ability better than the rest of the firm. The special ability helps this firm to have a lower production costs than others. Does it mean that this firm will have excess profit even in the long run? It so, why? If not, why not? [Hint: think about the opportunity cost]