

HW#11, Due May 6, 2021 Analyze the case the firm receives subsidy for the following two different cases to find out how the firm's quantity and profit change.

a) The government gives a lump sum subsidy of 20,000 bahts to each firm.

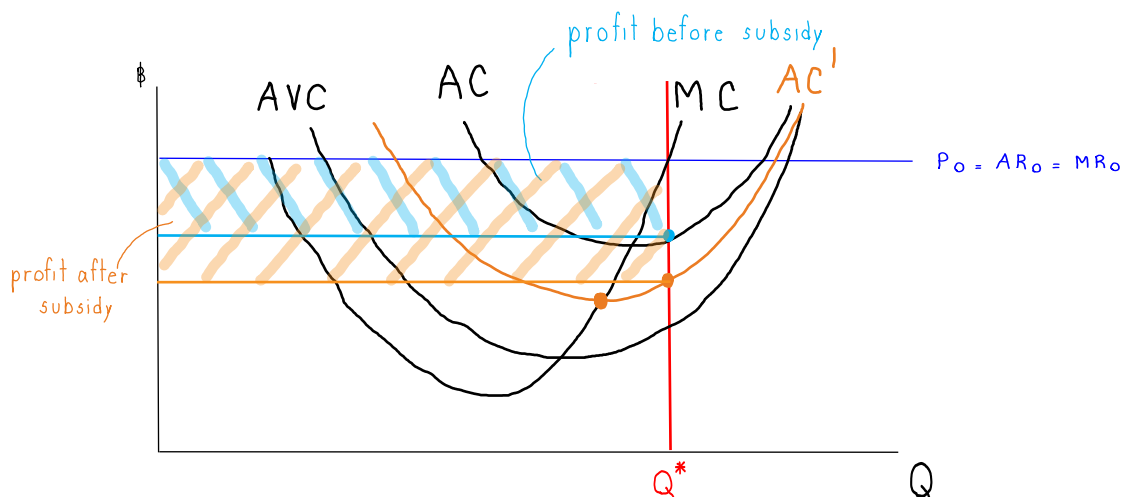
b) Suppose that the firm was producing 1,000 units and the government gives a subsidy of 20 bahts/unit so the total subsidy is also 20,000 bahts if the firm does not change its production of 1,000 units. Do you think, to maximize its profit with the subsidy of 20 bahts/unit, the firm will increase/decrease its production from 1,000 units? Does the firm receive higher profit? Does the firm receive more/less subsidy than 20,000 bahts?

a) The firm receive subsidy for 20,000 baht. \Rightarrow TFC decreases

$$\begin{aligned} TC(Q) &= TFC(Q) + TVC(Q) \\ TC'(Q) &= TFC'(Q) + TVC'(Q) \end{aligned} \quad \left. \begin{array}{l} \text{TVC unchanged} \\ \Rightarrow \text{since } MC = \frac{d}{dQ} TVC(Q) \\ \text{so MC unchanged} \end{array} \right\}$$

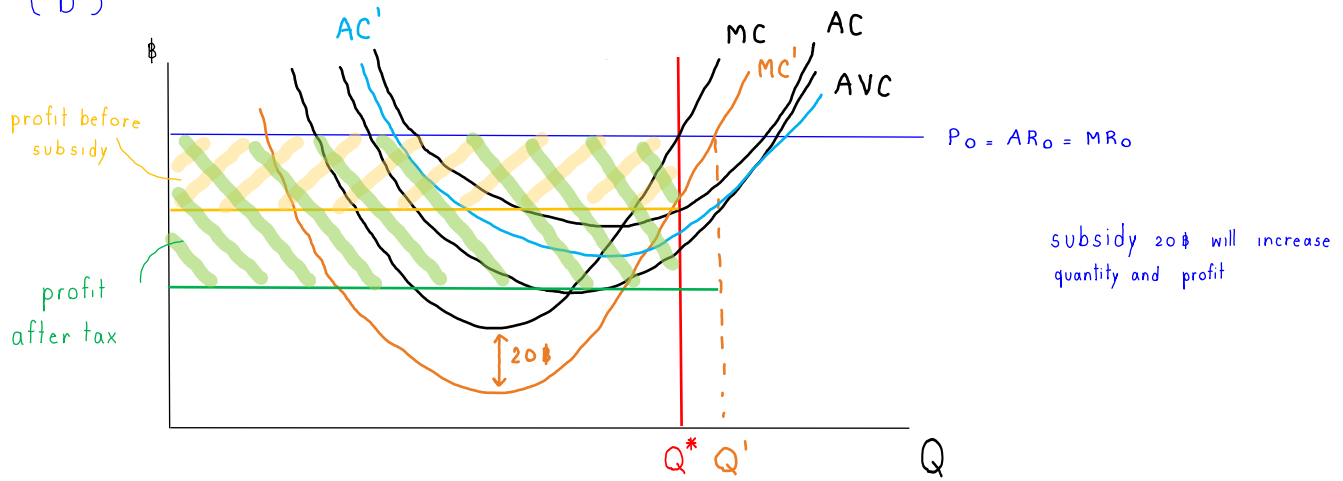
$$\frac{TFC'(Q)}{Q} = \frac{TFC(Q)}{Q} - \frac{20,000}{Q}$$

$$AFC'(Q) = AFC(Q) - \frac{20,000}{Q}$$



Q^* doesn't change because MC and MR stay the same
Profit increases 20,000 baht.

(b)



$$TC(Q) = TFC(Q) + TVC(Q)$$

$$TC'(Q) = TFC(Q) + TVC'(Q)$$

$$= TFC(Q) + TVC(Q) - 20Q$$

$$AVC'(Q) = AVC(Q) - 20$$

$$AC'(Q) = AFC(Q) + AVC(Q) - 20 = ACC(Q) - 20$$

$$MC'(Q) = MC(Q) - 20$$

Before subsidy Equilibrium is at Q^*

- because
1. $MR(Q^*) = MC(Q^*)$
 2. slope of $MR(Q^*) <$ slope of $MC(Q^*)$

After subsidy: Equilibrium is at Q'

- because
1. $MR(Q') = MC'(Q')$
 2. slope of $MR(Q') <$ slope of $MC'(Q')$

The firm will increase its production to Q' to gain more profit and maximize the profit.
 The firm will receive subsidy more than 20,000 baht.