COVENANT UNIVERSITY
NIGERIA

TUTORIAL KIT
OMEGA SEMESTER

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COURSE: CBS 221

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ECN 321
INTERMEDIATE MICROECONOMICS THEORY II
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QUESTIONS

1. Define the concept of Cost on the Short Run (SR).
2. Explain the behavior of the firm's cost function in the Short Run (SR).
3. How is the Output Determination decision taken in the Short Run (SR) cost analysis?
4. Differentiate the firm's Short Run (SR) and Long Run (LR) cost function diagrammatically.
5. Distinguish between the Average Cost (AC) of a firm and it's Marginal Cost (MC).
6. How is the Output Determination decision taken under the Long Run (LR) cost consideration?
7. Among the Total Cost (TC), Average Cost (AC), Marginal Cost (MC), Fixed Cost (FC) and Variable Cost (VC), which one is most crucial to the firm's production behavior and why?
8. What are the conditions for cost minimization for the producer given the theory of cost?
9. What are the conditions for cost maximization on the Long Run (LR)?
10. Given the Short Run equilibrium consideration, how does a firm make the price and output decision in a perfectly competitive market.
11. Define the concept of Price Ceiling as a Governmental Policy measure of the Perfect Competitive Market.
12. Explain with the aid of well labelled diagrams the Short Run pricing and output conditions within the perfectly competitive market using the Total Cost and Total Revenue Approach.
13. Explain each of the characteristic used to classify a market as being perfect.
14. Examine and explain the Long Run pricing and output equilibrium determination in a perfectly competitive market.
15. Explain and differentiate the concept of Returns to Scale.
16. Show diagrammatically the Long Run Cost Curve of a producer explaining the factors responsible for the unique shape.
17. Define the concept of the Long Run Cost Curve (LRATC).
18. With relevant explanations and diagrams, distinguish concisely between the equilibrium position of the consumer and the producer respectively.
19. What are the effects of Tariffs and Quotas in regulating market operations?
20. What is the fundamental difference between the behavior of Monopoly and Duopoly markets

ANSWERS

1. Define the concept of Cost on the Short Run (SR).

The concept of Cost is focused on the utilization of the lowest possible level of input to produce a particular volume of output as targeted by firm. This is also expected to give consideration to the event of the firm's ability to adjust some or all available factors of production.

On the Short Run (SR), the firm is able to adjust a few factors (variable factors) of production within a production period to obtain the lowest possible cost incurred to produce a required level output volume, while every other factors (fixed factors) are held constant.

3. How is the Output Determination decision taken in the Short Run (SR) cost analysis?

The Output Determination decision is taken in the short Run by a firm is to produce output volume at the point where the Marginal Revenue (MR) or the price of the good is equal to the Marginal Cost (MC) of producing an additional unit of the good.

i.e; MC=MR

5. Distinguish between the Average Cost (AC) of a firm and it's Marginal Cost (MC).

Average Cost (AC): This is the value of the cost of production of a good per unit of the output volume. It comprises of the Average Fixed Cost (AFC) and the Average Variable Cost (AVC).

The AFC decreases as output increases; while the AVC increases with increase in output volume. The two components combine to give a U-shaped Average Cost Curve

Marginal Cost (MC): The Marginal Cost is the value of the difference in term of cost that would be incurred by a firm by embarking on the production of an extra unit of the volume.

7. Among the Total Cost (TC), Average Cost (AC), Marginal Cost (MC), Fixed Cost (FC) and Variable Cost (VC), which one is most crucial to the firm's production behavior and why?

    The Marginal Cost

    Why? The Marginal Cost (MC) is required by the firm in the determination of the determination of the production output volume with respect to both the firm's demand curve and the market demand curve.

9. What are the conditions for cost minimization on the Long Run (LR)?

    On the Long Run (LR), all factor of production can be varied. The cost minimization decision is therefore based on both the volume out output as well as the prices of factors of production. This places observable restrictions on the firm as the firm must seek factor inputs at the minimal price level in order to educe cost.

11. Define the concept of Price Ceiling as a Governmental Policy measure of the Perfect Competitive Market.

    This is a deliberated policy made by the Government restricting the price of a good to a particular level in order to fix the amount of both producer and consumer surplus within the market.

    The new price is set such that it is either more than or less then the equilibrium price as determined by the forces of demand and supply.

    Such Governmental regulations are aimed at protecting the income of the consumers in order to increase their purchasing power

13. Explain each of the characteristic used to classify a market as being perfect.

    There is perfect knowledge of all information

    There are no barriers to entry into and exit out of the market

The market has goods that are homogeneous and identical
The factor inputs are equally homogenous in nature
The producer is a price taker
There is freedom from Government intervention
There are no externalities within the market
Profit on both the long run and short run are normal

15. Explain and differentiate the concept of Returns to Scale.

    Return to Scale: This is the quantitative change in the output of the firm in the production of goods within the market as a result of proportionate increase in all factor inputs.

    Constant Return to Scale: This is the corresponding equal level of output volume due to the same quantity of factor inputs.

    Increasing Return to Scale: This is a more than proportionate increase in the volume of output goods as a result of a lower level of factor inputs.

    Decreasing Return to Scale: this is a less than proportionate volume of output of goods produced from the combination of a quantitatively greater level of factor inputs.

17. Define the concept of the Long Run Cost Curve (LRATC).

    TheLong Run Average Cost, (LRATC)curve of a firm shows the minimum or lowest average total cost at which a firm can produce any given level of output in the long run (when all inputs are variable)

19. What are the effects of Tariffs and Quotas in regulating market operations?

    Direct Effects:

    - Reduction in the level of consumption
    - Increase in the localized domestic production of goods and services
    - Reduction in the volume of imports
    - Increase in the revenue obtained from the imported good and services

    Indirect Effects

    - Promotion of inefficient industry promoted by the protection which has little or no comparative advantage internationally.
    - Creation of trade wars between nations.