Lecture 12: In-class Problems

AFTERNOON

11/17/2020

Q1)

your reasoning.

2. Identify and explain the sources of market power for each case listed below:

   a. In the early 1990s, the DeBeers diamond cartel controlled almost all of the world's rough diamond production.

   b. Microsoft's Word has a virtual monopoly in word processing, even though many claim that better word-processing programs exist.

   c. Union Pacific dominates the rail shipping market in the north central United States.

   d. In Louisiana, people must pass a licensing test before they can arrange flowers for a living.

(a) absolute cost advantage

(b) switching costs.
network good.

(c) natural monopoly

(d) gov't barrier to entry

Q2)

are maximized.

14. Suppose that a monopolistic seller of designer handbags faces the following inverse demand curve: $P = 50 - 0.4Q$. The seller can produce handbags for a constant marginal and average total cost of $10.

    a. Calculate the profit-maximizing price for this seller.

    b. Suppose the government levies a $4 tax per unit on sellers of handbags. Calculate how this tax will affect the price the monopolist charges its customers.

    c. Who bears the burden of this tax?

(a) Calculate profit-maximizing price

First, maximize profits where MR = MC

↑ given $10

Find MR.

$P = 50 - 0.4Q$ inverse demand

$MR = 50 - 0.8Q$ from formula in book

$MR = MC$

$50 - 0.8Q = 10$

$40 = 0.8Q$

$\Rightarrow Q = 50$

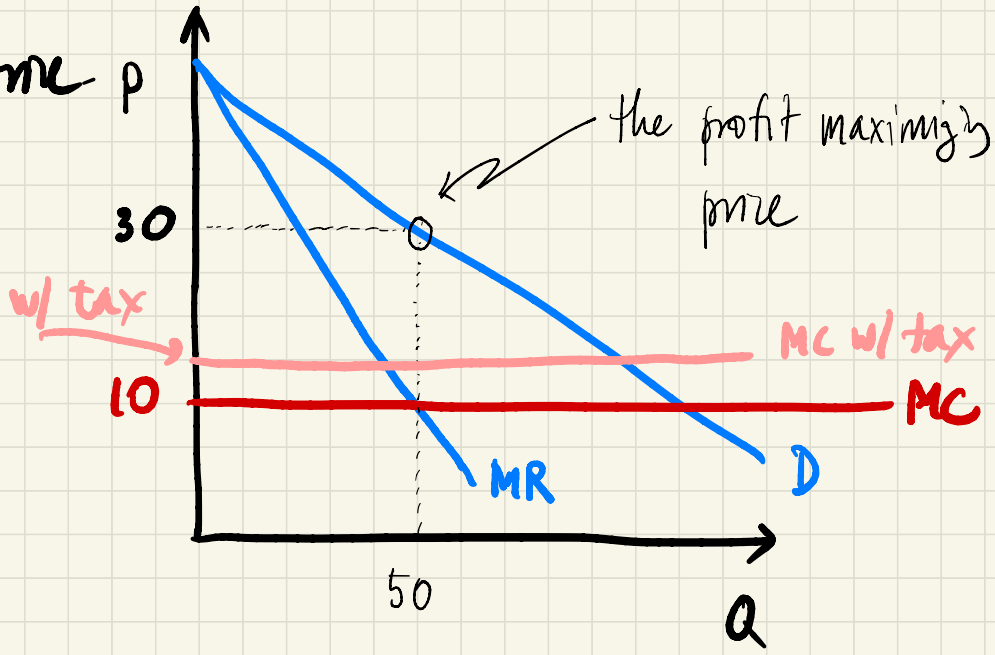
Find profit-maximizing price

Plug $Q = 50$ into demand curve

$$P = 50 - 0.4Q$$

$$P = 50 - 0.4(50)$$

$$P = 50 - 20 = 30$$



MC w/ tax = MC + tax

(b)