

Firms & Decisions – Summary

Important: This set of summary notes does NOT replace the importance of the main set of notes in providing a clear understanding of the topic that is required in the A Levels.

Check list – Key requirements.

Part (1)

- ☐ Understand the concept of profit as the difference between total revenue and total cost
- ☐ Understand that firms make price and output decisions based on the marginalist principle
- ☐ Sketch the various short run and long run curves and illustrate how changes on costs and revenue affect the various curves
- ☐ Understand that firms have other possible objectives
- ☐ Explain factors that affect the size of firms
- ☐ Explain the different types of economies of scale

[An understanding of the concepts of Average Revenue (AR), Marginal Revenue (MR), Average Total Cost (ATC) and Marginal Cost (MC) will be sufficient. Concepts on product curves and derivation of the cost curves are not required.]

[An understanding that total cost incorporates a necessary minimum economic reward for firms to remain in the market is required.]

[An understanding of the significance of variable costs and irrelevance of fixed costs in the pricing and output decisions of firms is required.]

- ☐ Explain the key features of each of the market structures (PC, MPC, Oligopoly, Monopoly), and their respective demand curves
- ☐ Explain how firms compete in the respective market structures based on their features
- ☐ Understand the relevance of barriers to entry in explaining differences between market structures
- ☐ Use the concept of profits to illustrate real world competitive behaviour of firms (in protecting their profits)
- ☐ Apply these market structure models in analysing and comparing markets; and evaluate their usefulness as explanations of real world competitive behaviour

Key information

Part (1)

Objectives of firms

Profit-maximising objective

Marginalist principle in determining profit maximising output and price

Alternative objectives of firms

Entry deterrence, revenue maximization, profit satisficing, and market share dominance

Costs and revenue

Costs and revenue concepts*

Distinction between short run and long run

Average and marginal costs and revenue

Internal and external economies and diseconomies of scale

*Derivation of costs and revenue curves is not required.

Firms' decisions and strategies

Characteristics of market structures*

Considerations involved in firms' decisions and strategies to achieve objectives including cost and revenue, competitors' actions, business risks, uncertainty considerations*

Decisions and strategies including price and output, price discrimination, shut-down decision, growth of firms, diversification, innovation, product differentiation, competition vs collusion*

Impacts of decisions and strategies on consumers, firms and governments, including efficiency and equity, and consumer welfare.

*Diagrammatic analysis of the comparison of types of market structure is not required.

*Technical analysis of competitors' actions, business risks and uncertainty is not required.

*Diagrammatic analysis of the shut-down decision is not required.

Typical types of essay questions in Firms and Decisions

Part a – pricing and output decision

Part b – strategies

- [2022]: Economists usually begin their analysis of decision-making by firms by assuming that the objective of a firm is to maximise its profit. In reality, however, there are many different objectives that a firm might adopt.
 - (a) Explain the likely effects on a firm's price and output when its objective changes from profit maximisation to profit satisficing. [10]
 - (b) Discuss the most appropriate strategy that a firm could adopt if its objective was to reduce the competition that it faces. [15]
- [2021]: Singapore's telecommunications (telco) market is dominated by four firms — SingTel (32%), StarHub (25%), M1 (22%) and new entrant MyRepublic (15%). Commentators argue that Singapore's telco market might be considered to be an oligopoly.
 - (a) Explain why Singapore's telco market might be considered to be an oligopoly and how economic theory suggests this market structure would affect the firms' pricing and output decisions. [10]
 - (b) Discuss how government intervention in Singapore's telco market could protect consumers, and consider the extent to which such intervention will be successful. [15]
- [2020]: Expectations of quick service restaurants (QSRs) or fast food chains are changing. Innovation is required to keep abreast of changing consumer taste and to maintain a competitive advantage in Singapore, a market known for its discernment of food.
 - (a) Explain how the market structure in which fast food chains operate is likely to influence how prices are determined. [10]
 - (b) Discuss whether innovation is the best strategy for fast food chains seeking to increase their profits. [15]
- [2019]: 2019 questions differ from 2020-2022.

According to the Competition and Consumer Commission of Singapore (CCCS), the takeover of Uber by Grab has led to 'a substantial lessening of competition'. This has made it harder for new competitors to enter the ride-hailing market.

(a) Explain one reason why consumers may be better off and one reason why consumers may be worse off from Grab's takeover of Uber. [10]

(b) Discuss the potential benefits and problems that are likely to be experienced by new competitors considering entering the ride-hailing market dominated by Grab. [15]