Chapter 7
Monopoly and Oligopoly

Multiple Choice Questions

Choose the one alternative that best completes the statement or answers the question.

1. Assume that in order to sell 10 more units of output a firm must reduce its price from $12 to $10. If, previously, the firm had sold 10 units at $12,
   (a) the firm’s marginal revenue is $8.
   (b) the firm’s marginal revenue is $10.
   (c) the firm’s marginal revenue is $12.
   (d) the firm’s marginal revenue is more than $12.
   (e) the firm’s marginal revenue is $2.
   Answer: A

Table 7.1 shows a hypothetical firm's demand and total cost curves.

Table 7.1

<table>
<thead>
<tr>
<th>Output</th>
<th>Price</th>
<th>Total Cost</th>
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<tbody>
<tr>
<td>0</td>
<td>$8</td>
<td>$0</td>
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<td>4</td>
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<td>15</td>
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</table>

2. According to the data in Table 7.1, this firm’s
   (a) ATC is constant for output levels of 1 through 4 units.
   (b) MC equals ATC.
   (c) AVC equals ATC.
   (d) P equals MR.
   (e) All of the above.
   Answer: C

3. According to the data in Table 7.1, this firm’s maximum profit is
   (a) $5.
   (b) $4.
   (c) $3.
   (d) $6.
   (e) $8.
   Answer: D
4. According to the data in Table 7.1, this firm
   (a) is operating in the short run.
   (b) is operating in the long run.
   (c) is a price taker.
   (d) has positive fixed costs.
   (e) has a downward-sloping marginal cost curve.
   Answer: B

5. According to the data in Table 7.1, this firm’s fixed costs are
   (a) impossible to determine from the given data.
   (b) zero.
   (c) $3, whatever is the quantity produced in this example.
   (d) $6 when 3 units are produced.
   (e) $9 when 3 units are produced.
   Answer: B

6. According to the data in Table 7.1, this firm’s profits are maximized when
   (a) output is 0 units.
   (b) output is 1 unit.
   (c) output is 2 units.
   (d) output is 3 units.
   (e) output is 4 units.
   Answer: D

7. According to the data in Table 7.1, MR of the 3rd unit of output is
   (a) $15.
   (b) $7.
   (c) $4.
   (d) $3.
   (e) $1.
   Answer: D

8. Which of the following correctly completes this statement? A monopolistic industry
   (a) contains a single producer.
   (b) produces a product for which there are few close substitutes.
   (c) is characterized by significant barriers to entry.
   (d) faces a downward-sloping demand curve.
   (e) All of the above.
   Answer: E

9. If the demand curve is linear for a price-searching firm,
   (a) marginal revenue is one-half the price.
   (b) the marginal-revenue curve is twice as steep as the demand curve.
   (c) \( P = MR \).
   (d) the demand curve is twice as steep as the marginal-revenue curve.
   (e) marginal revenue is increasing.
   Answer: B
10. Since a monopolist’s demand curve is downward-sloping,
   (a) profit is maximized when the highest possible price is charged.
   (b) price is less than marginal revenue.
   (c) average revenue is less than price.
   (d) marginal revenue is greater than price.
   (e) None of the above.
   Answer: E

11. Which of the following is correct? A monopolist
   (a) will sell less at a higher price than a perfect competitor.
   (b) has a marginal revenue less than price.
   (c) will produce where $MR = MC$.
   (d) is a price-maker.
   (e) All of the above.
   Answer: E

12. If a profit-maximizing firm selects a price at which demand is inelastic,
   (a) it can lower revenues by raising the price.
   (b) it is maximizing profits.
   (c) it is not maximizing profits.
   (d) it should lower its price.
   (e) its marginal revenue is positive.
   Answer: C

13. In the long run, for a monopolistically competitive firm,
   (a) price will equal average total cost.
   (b) price will be greater than marginal costs.
   (c) marginal revenue will equal marginal costs.
   (d) the entry of firms will drive economic profits to zero.
   (e) All of the above.
   Answer: E

14. A monopolistically competitive industry is one in which
   (a) the number of producers is large.
   (b) a heterogeneous product is being produced.
   (c) there is some (limited) price-searching ability.
   (d) there are no barriers to entry.
   (e) All of the above.
   Answer: E

15. In the case of price-searching firms, price
   (a) exceeds marginal revenue.
   (b) equals marginal cost.
   (c) equals average variable cost.
   (d) is less than marginal cost.
   (e) equals average fixed cost.
   Answer: A
16. Which of the following is correct? Pure monopolies
   (a) can earn economic profits that persist over time.
   (b) produce where MC equals P.
   (c) produce where MR equals P.
   (d) charge a price where demand is inelastic.
   (e) charge the highest possible price.
   Answer: A

17. A monopolistically competitive firm
   (a) produces that quantity of output at which P = MC.
   (b) produces that quantity of output at which MR = MC.
   (c) produces that quantity of output where P = ATC in the short run.
   (d) produces that quantity of output at which P = AVC in the short run.
   (e) All of the above.
   Answer: B

18. In the long run, a monopolistically competitive firm
   (a) earns zero economic profits.
   (b) earns a normal profit.
   (c) does not produce at minimum average cost.
   (d) charges a price that equals average cost.
   (e) All of the above.
   Answer: E

19. In the long run, a monopolistically competitive firm
   (a) produces where marginal revenue is greater than marginal cost.
   (b) earns an economic profit.
   (c) does not produce at minimum average cost.
   (d) charges a price that is greater than average cost.
   (e) None of the above.
   Answer: C

20. The main difference between monopolistic competition and perfect competition in the long run is
    that the competitive firm
   (a) makes zero economic profit.
   (b) produces where marginal revenue equals marginal cost.
   (c) produces at the minimum point on the average-cost curve.
   (d) charges a price equal to average cost.
   (e) must leave the industry if it experiences an economic loss.
   Answer: C
21. If a firm’s demand curve is downward-sloping, its marginal-revenue curve
   (a) coincides with the demand curve.
   (b) is half as steep as the demand curve.
   (c) lies below the demand curve.
   (d) shows that the elasticity of demand is constant.
   (e) is positively-sloped.
   Answer: C

22. The marginal-revenue-equals-marginal-cost rule for maximizing profit
   (a) applies only to monopoly.
   (b) applies only to monopolistic competition.
   (c) does not apply to perfect competition.
   (d) is the general rule that all profit-maximizing firms seek to follow.
   (e) applies only to price takers.
   Answer: D

23. Which of the following correctly completes this statement? The monopolist’s marginal revenue will
   (a) be greater than price.
   (b) be less than price.
   (c) be equal to price.
   (d) not change as the level of output increases.
   (e) be equal to average revenue.
   Answer: B

24. Assume that in order to sell 10 more units of output a firm must reduce its price from $8 to $6. If,
   previously, the firm had sold 20 units at $8,
   (a) the producer is a price taker.
   (b) the firm’s marginal revenue is $6.
   (c) the firm’s marginal revenue is $8.
   (d) the firm’s marginal revenue is more than $6.
   (e) the firm’s marginal revenue is $2.
   Answer: E
Table 7.2 shows a hypothetical firm’s demand and total cost curves.

Table 7.2

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<td>4</td>
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<td>20</td>
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25. According to the data in Table 7.2, this firm’s
(a) ATC is constant for output levels of 1 through 4 units.
(b) MC equals ATC.
(c) AVC equals ATC.
(d) All of the above.
Answer: C

26. According to the data in Table 7.2, this firm’s maximum profit is
(a) $5.
(b) $4.
(c) $8.
(d) $3.
(e) $6.
Answer: E

27. According to the data in Table 7.2, this firm
(a) is operating in the short run.
(b) is operating in the long run.
(c) is a price taker.
(d) has positive fixed costs.
(e) has a downward-sloping marginal cost curve.
Answer: B

28. According to the data in Table 7.2, this firm’s fixed costs are
(a) impossible to determine from the given data.
(b) $15 when 3 units are produced.
(c) $5 whatever is the quantity produced in this example.
(d) $10 when 3 units are produced.
(e) zero.
Answer: E
29. According to the data in Table 7.2, this firm’s profits are maximized when
   (a) output is 4 units.
   (b) $P = $10 because $P - MC = $5 (a maximum).
   (c) output is 3 units.
   (d) output is 1 unit.
   (e) output is 5 units.
   Answer: C

30. If a monopoly is earning an economic profit of $10 million, which of the following predictions is
    likely to (eventually) occur?
    (a) Even with significant barriers to entry, these profits will be depleted.
    (b) In the very long run, these profits will be reduced or even depleted by the development of new
        competitive products.
    (c) In the long run, the price of the product must settle at the marginal cost of production.
    (d) In the short run, these profits will be reduced to zero.
    (e) All of the above.
    Answer: B

31. Which of the following correctly completes this statement? A monopolist
    (a) must lower its price to increase the quantity sold.
    (b) must raise its price to increase the quantity sold.
    (c) does not have to worry about sales because it has a monopoly.
    (d) will always make a profit.
    (e) All of the above.
    Answer: A

32. If a monopolist’s demand is inelastic at the current price,
    (a) the monopolist is not maximizing profit.
    (b) the monopolist should raise price.
    (c) the monopolist’s marginal revenue is negative.
    (d) more profit can be obtained by lowering the quantity produced.
    (e) All of the above.
    Answer: E

33. In long-run equilibrium, the product price of a monopolistically competitive firm
    (a) equals average total cost, and marginal revenue equals marginal cost.
    (b) equals marginal revenue, and marginal cost equals average total cost.
    (c) exceeds average total cost and equals marginal cost.
    (d) equals average total cost and equals marginal cost.
    (e) equals average variable cost and equals marginal cost.
    Answer: A
34. If the McDonald’s restaurant on the corner raised prices while other fast-food stores kept their prices constant,
   (a) its sales would not be affected.
   (b) its sales would drop to zero because fast food is a homogeneous product.
   (c) its sales would rise because people like McDonald’s hamburgers.
   (d) the elasticity of demand would be inelastic.
   (e) McDonald’s might lose considerable sales but would keep its loyal customers.
   Answer: E

35. The reason monopolists limit product durability is that
   (a) it is costly to extend the life of the product.
   (b) a more durable product eliminates repeat sales.
   (c) more durable products lower profits.
   (d) less durable products raise profits.
   (e) None of the above.
   Answer: A

36. A Texas firm sells steel pipe in Saudi Arabia and in Britain. The price elasticity of demand is higher in Britain than in Saudi Arabia. Thus,
   (a) the price is likely to be higher in Britain.
   (b) the price is likely to be lower in Britain.
   (c) the price is likely to be equal in Britain.
   (d) more steel pipe will be sold in Britain.
   (e) less steel pipe will be sold in Britain.
   Answer: A

37. Which of the following is correct? A patent granting an inventor the sole right to produce a product
   (a) promotes competition.
   (b) creates barriers to entry.
   (c) provides disincentives to invent.
   (d) lowers prices.
   (e) is economically worthless.
   Answer: B

38. The entry of new firms into a monopolistically competitive industry
   (a) lowers the price elasticity of demand for established firms.
   (b) decreases the number of substitutes.
   (c) reduces the demand for the products of established firms.
   (d) decreases the variety of this product in the industry.
   (e) All of the above.
   Answer: C
39. Marginal revenue is less than price for a monopoly firm because
   (a) the demand curve is downward-sloping.
   (b) additional sales spoil the market.
   (c) price must be reduced on all units sold to sell more units.
   (d) average revenue is falling so marginal revenue must be below it.
   (e) All of the above.
   Answer: E

40. Marginal revenue for a price searcher is
   (a) the average revenue from selling a given number of additional units.
   (b) the average revenue from selling one more unit of output.
   (c) the total revenue from selling a given number of additional units.
   (d) the additional revenue from selling one more unit of output.
   (e) always less than price.
   Answer: D

41. If a monopolist is producing an output level at which marginal revenue is greater than marginal costs, the monopolist
   (a) is maximizing profits.
   (b) should raise price.
   (c) is producing too much output.
   (d) should lower price.
   (e) None of the above.
   Answer: D

42. In comparing monopoly and perfect competition, which of the following statements is true?
   (a) Monopolies automatically earn profits; perfectly competitive firms do not.
   (b) Competitive profits will disappear in the long run as new firms enter the industry; monopoly
       profits can be protected in the long run by barriers to entry.
   (c) In the long run, both monopoly and perfect competition produce at minimum average cost.
   (d) In the short run, both monopoly and perfect competition attempt to minimize average fixed
       costs.
   (e) None of the above.
   Answer: B

43. In order to maximize short-run profits (or minimize losses), any firm (whether competitive or monopolistic) must follow which of the following rules?
   (a) If average revenue is less than ATC, the firm should shut down.
   (b) If average revenue is greater than AVC, the firm should shut down.
   (c) As long as price is greater than AVC, it should produce that quantity of output at which MR = MC.
   (d) If the firm should not shut down, the firm should produce that quantity at which AVC is at a
       minimum.
   (e) If P > AVC, the firm should shutdown.
   Answer: C
44. Which of the following correctly completes this statement? When a firm is making economic profits,
   (a) the firm must be a monopolist.
   (b) the firm’s accounting profits are negative.
   (c) the firm is in a competitive long-run equilibrium.
   (d) \( P > ATC \), where \( ATC \) is measured according to opportunity costs.
   (e) All of the above.
   Answer: D

45. Which of the following correctly completes this statement? Pure monopolies
   (a) may make economic profits that disappear in the short run.
   (b) produce where \( MC = P \).
   (c) produce where \( MR = P \).
   (d) will not produce where demand is elastic.
   (e) None of the above.
   Answer: E

46. Monopolistically competitive firms, in the long run,
   (a) produce an output level greater than the point of minimum average cost.
   (b) tend to go bankrupt.
   (c) produce an output level less than the point of minimum average cost.
   (d) experience increasing product differentiation.
   (e) tend to have relatively inelastic demand curves.
   Answer: C

47. A monopolistic firm that discovered (costlessly) a way to double the durability of its product would
   (a) keep the improved version off the market.
   (b) introduce the improved version only if there is competition.
   (c) introduce the improved version in order to maximize profit.
   (d) introduce the improved version only if the demand is elastic.
   (e) keep the improved version off the market if its current marginal costs are low.
   Answer: C

48. The long-run difference between the pure monopolist and the monopolistically competitive firm is that
   (a) the monopolist is a price-maker, and the monopolistic competitor is a price taker.
   (b) price equals marginal cost for the monopolistic competitor, and marginal revenue equals marginal cost for the monopolist.
   (c) there are more barriers to entry for the monopolist than for the monopolistic competitor.
   (d) product differentiation becomes stronger for the monopolistic competitor in the long run.
   (e) None of the above.
   Answer: C
49. Which of the following correctly completes this statement? Like a perfectly competitive firm,
   (a) a monopolist will produce at that quantity where MR = MC.
   (b) a monopolistically competitive firm can freely enter and exit the industry.
   (c) a monopolistically competitive firm will make zero economic profits in the long run.
   (d) monopolists are profit maximizers.
   (e) All of the above.
   Answer: E

50. The reason that monopoly profits can persist in the long run is that
   (a) monopolists will continue to raise prices if profits begin to fall.
   (b) monopolists do not have to worry about demand.
   (c) barriers to entry prevent new firms from entering the industry and sharing in the profits.
   (d) marginal revenues exceed marginal costs for monopolists.
   (e) monopolists control demand better than competitive firms.
   Answer: C

51. No monopolist would produce where the demand for the product is inelastic because
   (a) potential new entrants could come and spoil the market.
   (b) by raising the price it could raise revenues and lower costs.
   (c) in the long run, demand is perfectly elastic.
   (d) marginal cost would exceed marginal revenue.
   (e) it could increase output, raise revenues, and lower costs.
   Answer: B

52. Marginal revenue is less than the monopoly price because
   (a) the elasticity of demand for a monopolist’s output is infinite.
   (b) the elasticity of demand for a monopolist’s output is equal to one.
   (c) the elasticity of demand for a monopolist’s output is less than one.
   (d) to sell more output the price must be lowered on all units sold.
   (e) to sell more output the price does not need to be changed.
   Answer: D

53. Examples of pure monopoly are difficult to find because
   (a) entry barriers are relatively easy to overcome.
   (b) many monopolies, such as the local electric company, are regulated.
   (c) most products have some substitute.
   (d) economies of scale are important in only a small number of markets.
   (e) the monopolist may not behave like a pure monopolist if it believes it has few potential rivals.
   Answer: C

54. For any profit-maximizing firm, which of the following is true at the profit-maximizing output?
   (a) Total revenue equals total cost.
   (b) Marginal revenue equals marginal cost.
   (c) Average revenue equals price.
   (d) Price equals average cost.
   (e) Average revenue equals marginal revenue.
   Answer: B
55. Typically, we expect monopolists to have positive long-run profits. Which of the following is the source of these long-run profits?
   (a) Price-discrimination by monopolists.
   (b) Low production costs.
   (c) Effective antitrust action.
   (d) Strong demand by consumers.
   (e) Barriers to entry.
   Answer: E

56. Which of the following is correct? If a monopolist is producing a profit-maximizing output
   (a) price equals average cost.
   (b) average cost equals marginal cost.
   (c) price equals marginal cost.
   (d) average cost is increasing.
   (e) price exceeds marginal cost.
   Answer: E

57. Which of the following is true? A profit-maximizing monopolist
   (a) should be regulated to prevent price discrimination.
   (b) has positive short-run profits.
   (c) with long-run economic losses will leave the market.
   (d) has no potential competitors.
   (e) can always prevent entry.
   Answer: C

58. A monopolist’s profit-maximizing output _____ by an increase in fixed cost while an increase in marginal cost _____ the same firm’s output level.
   (a) will be reduced; will not affect
   (b) will not be affected; will not affect
   (c) will not be affected; will reduce
   (d) will be reduced; will reduce
   (e) None of the above.
   Answer: C

59. Economists believe that entry barriers are required for monopolists to maintain long-run economic profits. A monopolist may prevent entry by which of the following?
   (a) A minimal advertising budget.
   (b) Selling its raw material sources to other firms.
   (c) Having substantial economies of scale.
   (d) Having substantial diseconomies of scale.
   (e) Allowing patents on its product to expire instead of filing more patents.
   Answer: C
60. For Pizza Bellisma, a local pizzeria, marginal revenue is
   (a) positive because quantity demanded increases due to a price reduction.
   (b) the additional revenue from total pizzas sold.
   (c) revenue from all pizzas sold.
   (d) the additional revenue from selling one more pizza.
   (e) the additional revenue from selling 50 more pizzas.
   Answer: D

61. Which of the following will be true for both a monopoly and monopolistically competitive firm in the long run?
   (a) Price is greater than long-run average cost.
   (b) Economic profits equal zero.
   (c) Entry is blocked.
   (d) Price exceeds marginal cost.
   (e) Price equals long run average cost.
   Answer: D

62. Monopolistic competition combines elements of competition and monopoly in one market model. At the profit-maximizing long-run equilibrium, which of the following will be correct for a competitive and monopolistic competitive firm?
   (a) Price is greater than the average cost.
   (b) The price-elasticity of demand is infinite.
   (c) Price equals marginal revenue.
   (d) Price is greater than marginal cost.
   (e) Economic profits are zero.
   Answer: E

63. Which of the following will be true for both monopoly and monopolistic competition in the short run?
   (a) Short-run profits are positive.
   (b) Price is greater than marginal revenue.
   (c) Price equals marginal cost.
   (d) Price equals marginal revenue.
   (e) Price equals average variable cost.
   Answer: B
64. The two figures above illustrate different demand curves for an individual producer. With respect to the two figures, which of the following is correct?
(a) The firm in Figure A is a price-taker and the firm in Figure B is a price-searcher.
(b) Both firms are price-searchers.
(c) The firm in Figure A is a price-searcher and the firm in Figure B is a price-taker.
(d) Both firms are price-takers.
(e) None of the above.
Answer: C

65. A price-searching firm’s demand, marginal revenue and marginal cost data are depicted in the figure above. With respect to 100 units of output, which of the following is correct?
(a) 100 units of output is the firm’s profit-maximizing output.
(b) 100 units of output is too low an output level since MR > MC.
(c) 100 units of output is too low an output level since MR = MC.
(d) 100 units of output is too low an output level since MR < MC.
(e) 100 units of output is too low an output level since price is not equal to marginal cost as at 700 units.
Answer: B
66. In the long run, a monopolist can maintain the monopoly position if some barrier to entry exists. A monopolist could prevent entry with which of the following strategies?
(a) Obtaining a patent on the firm’s product.
(b) Developing new (and easily duplicated) technology that reduces the capital requirements of producing the good.
(c) Allowing a state-granted franchise to produce the good to expire.
(d) Lobbying against a requirement for licensing of other producers of similar goods.
(e) Restricting the amount of the firm’s product the monopolist produces.
Answer: A

67. For a monopolist or monopolistically competitive firm, if \( MR < MC \), the firm should (if it is attempting to maximize profits)
(a) lower price.
(b) leave price the same.
(c) raise price.
(d) produce more.
(e) None of the above.
Answer: C

68. Mutual interdependence occurs when
(a) all firms in an industry are affected by the same general economic conditions, like interest rates, consumer expectations, and the unemployment rate.
(b) the actions of all firms together determine the profitability of the industry.
(c) the actions of one firm in an industry affect other firms in the industry and these interrelationships are recognized.
(d) monopolists recognize that they must face eventual competition in the very long run.
(e) All of the above.
Answer: C

69. Cartels are subject to cheating by its members because
(a) one firm can slightly undercut the cartel price and earn substantial profits.
(b) cartels have difficulty preventing entry by non-members.
(c) the threat of antitrust action by the Justice Department is always present.
(d) the cartel’s profit-maximizing output occurs where price equals marginal cost.
(e) member firms typically produce differentiated products.
Answer: A

70. The barriers to entry that might characterize oligopolistic industries include
(a) a learning curve that lowers production costs.
(b) access to distribution channels.
(c) financing advantages of incumbents.
(d) brand loyalty caused by product differentiation.
(e) All of the above.
Answer: E
71. The learning curve creates a barrier to entry for established firms in oligopolistic industries because 
(a) oligopolists learn from the reactions of their competitors.  
(b) inexperienced firms cannot learn to produce the complex products typical of oligopolistic industries.  
(c) the production experience of existing firms provides a cost advantage.  
(d) predatory pricing, to be successful, must be learned from experience.  
(e) collusion is a learned behavior.  
Answer: C

72. The demand curve of an oligopolistic firm 
(a) is the same as the demand curve of a monopolist.  
(b) is known with certainty.  
(c) depends upon the actions of rival firms.  
(d) is the same as its marginal revenue curve.  
(e) lies above the demand curve of a perfectly competitive firm.  
Answer: C

73. Which of the following is correct? A cartel 
(a) prices its products as predicted by Nash equilibrium theory.  
(b) works as predicted by the Cournot model.  
(c) operates best with a large number of member firms.  
(d) is an arrangement that allows participating firms to operate the industry as a perfectly competitive industry.  
(e) is an arrangement that allows the participating firms to earn monopoly profits.  
Answer: E

74. The contradictory theme of cartels is best summarized by which of the following statements? 
(a) If everyone cheats, everyone gains.  
(b) If only a few cheat, everyone gains.  
(c) If one cheats and everyone else cheats, they are all better off.  
(d) One member gains by cheating only if everyone cheats.  
(e) If one cheats and everyone else cheats, they are all likely to be worse off.  
Answer: E

75. If advertising by an individual firm does not add to total industry sales but merely attracts sales from other firms,  
(a) firms would be better off agreeing not to advertise.  
(b) it pays one firm to advertise if the others do not.  
(c) advertising is like a prisoners’ dilemma.  
(d) the worst situation is for every firm to advertise.  
(e) All of the above.  
Answer: E
76. Collusion is easier to achieve when
(a) there are many sellers.
(b) barriers to entry are high.
(c) products are differentiated.
(d) there are infrequent orders.
(e) innovation in the industry’s products is frequent.
Answer: B

77. Which of the following correctly completes this statement? In the case of low entry barriers
(a) effective collusion is harder to arrange.
(b) established firms wish to have high profits to bring in new firms.
(c) collusion would raise long-run profits for established firms.
(d) effective collusion is more likely than in the case of high barriers to entry.
(e) collusion among firms is not possible.
Answer: A

78. If the products produced by oligopolists within an industry are relatively homogeneous, collusive agreements will be
(a) more likely.
(b) based on the prisoner’s dilemma game.
(c) less likely.
(d) easier to detect and more profitable per unit.
(e) possible but infrequent.
Answer: A

79. One major criticism of oligopoly is that
(a) oligopolists can easily become involved in price wars.
(b) focal points cause a redistribution of income.
(c) cartel agreements are unstable.
(d) there are important obstacles to collusion.
(e) if oligopolists collude successfully the result is similar to monopoly.
Answer: E

80. The most critical feature of oligopoly is
(a) mutual interdependence.
(b) homogeneous products.
(c) that oligopolies frequently tend towards collusion.
(d) moderate barriers to entry.
(e) collusive behavior.
Answer: A
81. A credible threat is best described as
   (a) a significant commitment of resources that prevents entry by new competitors.
   (b) a non-cooperative game between oligopolists.
   (c) a rival firm’s best response to its competitors strategy.
   (d) price leadership among oligopolists.
   (e) the prisoner’s dilemma game.
   Answer: A

82. Government regulations require all airlines to ban smoking on domestic flights. One consequence of
   this requirement is to
   (a) create the conditions for a prisoner’s dilemma game among the airlines.
   (b) increase the output level (number of flights) of competing oligopolists.
   (c) reduce competition among airlines.
   (d) increase the cost of providing air travel.
   (e) increase competition among airlines.
   Answer: C

83. When the number of firms is too large for formal or tacit collusion,
   (a) monopoly profits are likely to be earned.
   (b) the market is perfectly competitive.
   (c) the oligopoly will tend toward competitive behavior.
   (d) price and marginal cost will be equal.
   (e) price and average total cost will be equal.
   Answer: C

84. Oligopolies are more likely to earn some monopoly profits through formal or informal arrangements
   when
   (a) barriers to entry are low and the product is heterogeneous.
   (b) the number of producers is small.
   (c) the number of producers is large.
   (d) barriers to entry are low.
   (e) there are legal restrictions to price agreements.
   Answer: B

85. A cartel carries the seeds of its own destruction because
   (a) high prices encourage substitution in the very short run.
   (b) marginal cost exceeds marginal revenue for each member of the cartel who would cheat on the
       output quotas.
   (c) of the prisoners’ dilemma.
   (d) the market demand curve tends to be price-elastic.
   (e) there are substantial gains to cheating if others do not cheat.
   Answer: E
86. Which of the following correctly completes this statement? The main purpose of a cartel
(a) is to operate the industry as if it were a monopoly.
(b) is to serve as an alliance in a price war.
(c) is to regulate the behavior of its members to guarantee economic efficiency and quality standards.
(d) is to share the cost of erecting barriers to entry.
(e) is to guarantee economic profits for all members of the cartel.
Answer: A

87. The moral of the prisoners’ dilemma with regard to oligopoly is that
(a) it generally pays to follow a noncooperative strategy no matter what strategy other oligopolists use.
(b) only irrational people will not cooperate.
(c) do unto others, first.
(d) price wars hurt all sellers.
(e) your firm should pick the strategy that is best, given your rival’s action.
Answer: E

88. Firms in an oligopolistic industry are differentiated from firms in a monopolistically competitive industry by which of the following characteristics?
(a) Significant economies of scale in all oligopolistic industries.
(b) Product differentiation only by monopolistically competitive firms.
(c) A rapid rate of technological innovation by oligopolistic firms.
(d) Relatively inelastic demand curves faced by monopolistically competitive firms.
(e) Mutual interdependence among oligopolistic firms.
Answer: E

89. One empirical question that economists would be very interested in analyzing would be how large the difference between price and marginal cost is in various market structures. If our theory is correct, a study of non-collusive (or rival) oligopoly should show that the difference between price and marginal cost is
(a) greater than that exhibited by monopoly but less than that exhibited by competition.
(b) less than that exhibited by monopolistic competition.
(c) about the same as that of a successful cartel.
(d) less than that exhibited by a pure monopoly.
(e) greater than that exhibited by collusive oligopoly.
Answer: D

90. Study groups are one form of cartels. Ceteris paribus, we would tend to think that study groups will be less stable
(a) for small study groups relative to large study groups.
(b) for easy classes relative to difficult classes.
(c) if the students in the study group have similar academic abilities.
(d) if student output used for grading purposes can be significantly differentiated by individual students.
(e) None of the above.
Answer: D
91. Study groups are one form of cartels. Ceterus paribus, we would tend to think that study groups will be more stable
   (a) for easy courses compared to hard courses.
   (b) if study groups are prohibited by the student code of conduct.
   (c) the easier it is to cheat on tests.
   (d) if the study group meets at a regular time.
   (e) the smaller the number of participants.
   Answer: E

92. Economists argue that when price exceeds marginal cost, this outcome is undesirable from society’s viewpoint since too little output will be produced. For which market structure will the difference between price and marginal cost be greatest (ceteris paribus)?
   (a) non-collusive oligopoly.
   (b) monopolistic competition.
   (c) monopoly.
   (d) collusive oligopoly.
   (e) perfect competition.
   Answer: C

93. Economists believe that collusive behavior among oligopolists tends to be unstable. Which of the following would tend to INCREASE the likelihood of short-lived collusive behavior?
   (a) An oligopolistic industry with relatively high entry barriers.
   (b) An oligopolistic industry with a rapid rate of innovation.
   (c) An oligopolistic industry in which fixed production costs are a small proportion of total costs.
   (d) An oligopolistic industry in which the selling prices of individual firms are widely known to other firms.
   (e) An oligopolistic industry in which products are largely similar (such as various steel products).
   Answer: B

94. Economists believe that collusive behavior among oligopolistic firms is unlikely to last very long. Which of the following would tend to increase the stability of collusive behavior?
   (a) An oligopolistic industry in which entry barriers are relatively high.
   (b) An oligopolistic industry in which fixed costs are a relatively high proportion of total production costs.
   (c) An oligopolistic industry in which products are highly differentiated.
   (d) An oligopolistic industry with a large number of firms.
   (e) An oligopolistic industry operating in an environment where collusive behavior is illegal.
   Answer: A