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Level 3 Economics, 2019

91400 Demonstrate understanding of the efficiency of different market structures using marginal analysis

2.00 p.m. Monday 18 November 2019
Credits: Four

Achievement	Achievement with Merit	Achievement with Excellence
Demonstrate understanding of the efficiency of different market structures using marginal analysis.	Demonstrate in-depth understanding of the efficiency of different market structures using marginal analysis.	Demonstrate comprehensive understanding of the efficiency of different market structures using marginal analysis.

Check that the National Student Number (NSN) on your admission slip is the same as the number at the top of this page.

You should attempt ALL the questions in this booklet.

If you need more room for any answer, use the extra space provided at the back of this booklet.

Check that this booklet has pages 2–11 in the correct order and that none of these pages is blank.

YOU MUST HAND THIS BOOKLET TO THE SUPERVISOR AT THE END OF THE EXAMINATION.

TOTAL

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QUESTION ONE: Perfect competition – falling dairy prices and interest costs

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Dairy prices slip to lowest level in two years.

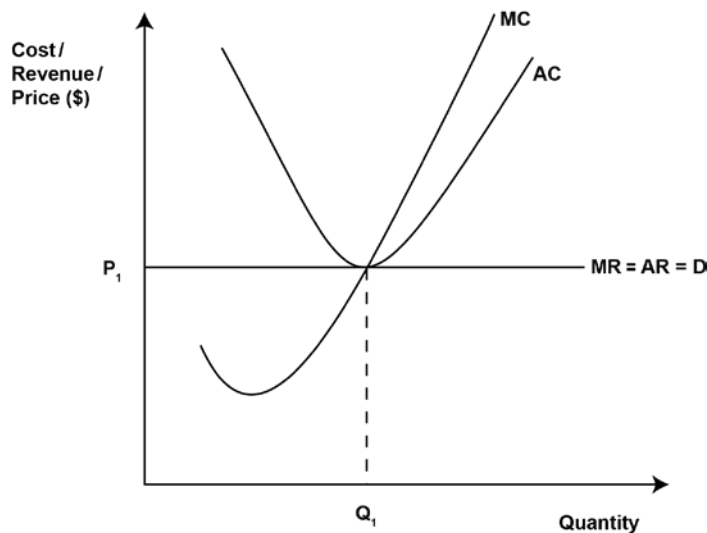
<https://www.rnz.co.nz/news/country/368822/dairy-prices-slip-to-lowest-level-in-two-years>.

Dairy prices forecast to keep falling until next year.

<https://www.radionz.co.nz/news/business/376461/dairy-prices-forecast-to-keep-falling-until-next-year>.

The headlines, above, indicate a lower income received by dairy farmers in New Zealand.

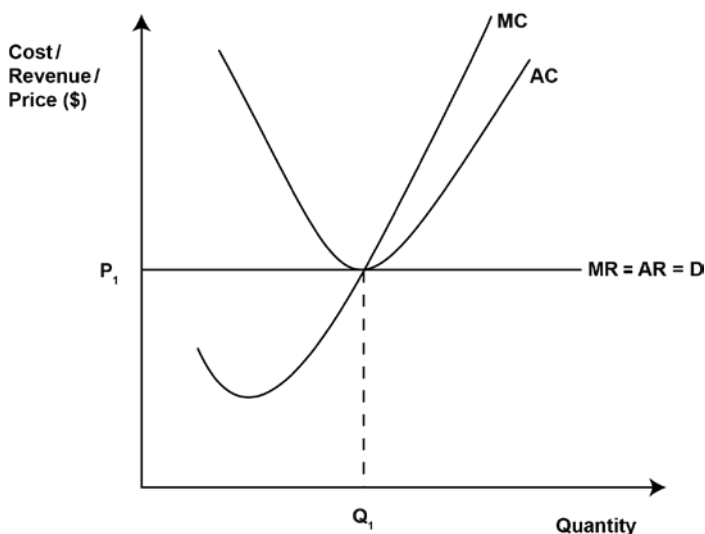
Graph One: A perfect competitor earning normal profit



- (a) Complete Graph One, above, to show how **falling dairy prices** would affect the individual New Zealand dairy farmer in the short run. Clearly label any curve shifts and any changes in the short-run price, quantity and economic profit earned.

Debt servicing is a fixed cost for dairy farmers; a decrease in interest rates would decrease their fixed costs.

Graph Two: A perfect competitor earning normal profit



- (b) Complete Graph Two, above, to show how a **decrease in interest rates** would affect the individual New Zealand dairy farmer in the short run. Clearly label any curve shifts and any changes in the short-run price, quantity and economic profit earned.

- (c) Use marginal analysis to compare and contrast the impact of falling dairy prices with the impact of a decrease in interest rates on an individual New Zealand dairy farmer's short-run price, output and economic profit earned. Refer to both graphs in your answer.

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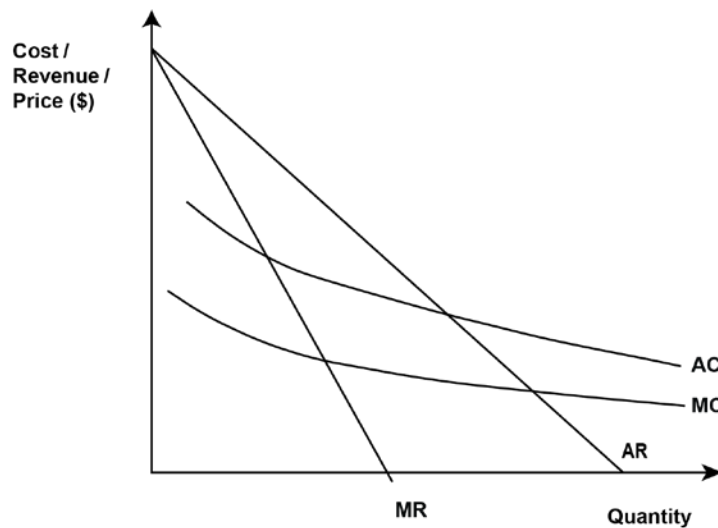
QUESTION TWO: Natural monopoly – average-cost and marginal-cost pricing

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The Commerce Commission regulates markets in New Zealand where there is little or no competition.

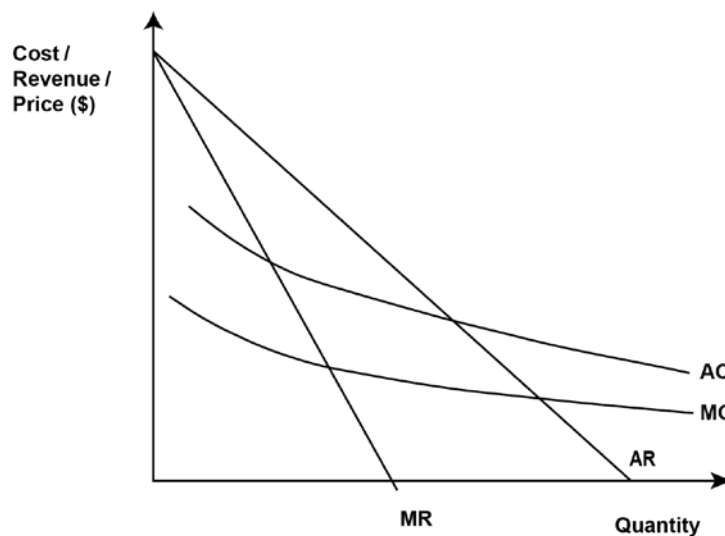
Price regulation is one way of controlling natural monopolies. They can be regulated using average-cost or marginal-cost pricing.

Graph Three: A natural monopoly



- (a) (i) On Graph Three, above, clearly shade and label the price, output, consumer surplus and deadweight loss (if any) resulting from **average-cost pricing**.
- (ii) State the type of economic profit earned by the natural monopoly.

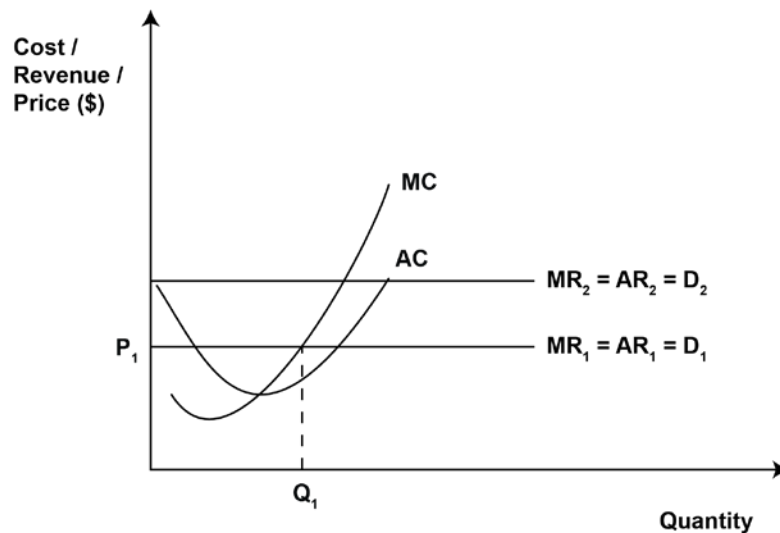
Graph Four: A natural monopoly



- (b) (i) On Graph Four, above, clearly shade and label the price, output, consumer surplus and deadweight loss (if any) resulting from **marginal-cost pricing**.
- (ii) State the type of economic profit earned by the natural monopoly.

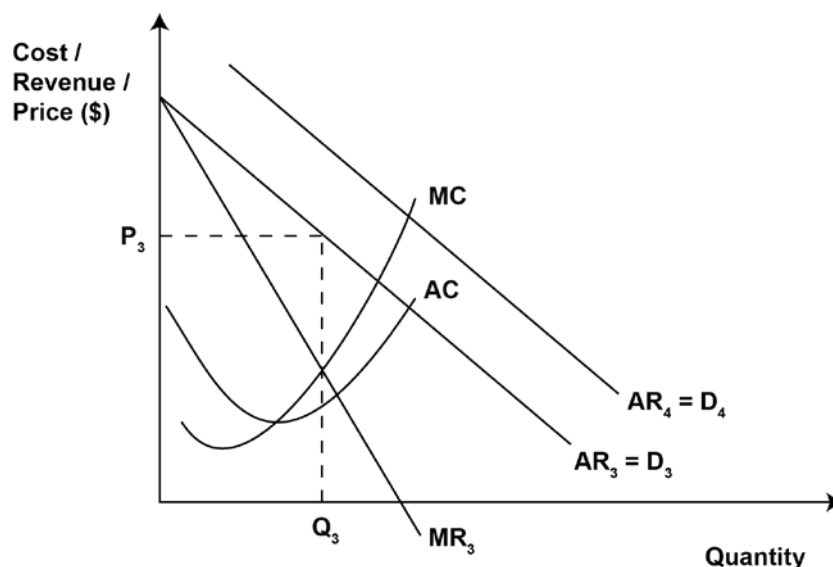
QUESTION THREE: Increase in demand for perfect competition and monopoly

Perfect competition and monopoly are very different market structures with distinct characteristics. An increase in market demand for products from each market structure will therefore produce different outcomes.

Graph Five: Perfect competition with an increase in demand

An increase in demand has been indicated by a shift upwards of the $MR=AR=D$ curve.

- (a) Complete Graph Five, above, to show how an increase in market demand would affect the perfect competitor's short-run pricing and output decisions. Clearly label the new price and quantity, and shade in the new economic profit earned.

Graph Six: Monopoly with an increase in demand

An increase in demand has been indicated by a shift to the right of the $AR=D$ curve.

- (b) (i) Complete Graph Six, above, to show how an increase in market demand would affect the monopoly's marginal revenue. Clearly add and label the new MR curve.
- (ii) Complete Graph Six to show how an increase in market demand would affect the monopoly's short run pricing and output decisions. Clearly label the new price and quantity and shade in the new economic profit earned.

Extra space if required.
Write the question number(s) if applicable.

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