30 Perfectly & Imperfectly Competitive Markets

Q:1 What are the Conditions of Perfect competition?
OR How a Firm in Perfect Competition is a Price-taker?

(A) Introduction :- Perfect Competition is an ideal concept of a market. Under this market Uniform Price is Fixed by market Forces of Demand and Supply.

(B) Meaning :- "Perfect Competition is a market Situation where Large Number of buyers and Sellers deals with Homogeneous Commodity at Uniform Price determined by demand force and supply force."

(C) Features | Conditions of Perfect Competition :-

1. There are Large number of buyers and Sellers in the market. Each Seller is Price-taker but not the Price-maker.
2. All the Commodities sold in this market must be Homogeneous or identical. It means same in shape, Size, Colour, design etc.
3. There must be Free Entry to and Exit From the market.

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4) All buyers and sellers must have Perfect Knowledge about market condition.

5) There must be Perfect mobility among all the factors of Production i.e Land, Labour, Capital and Entrepreneur.

6) There is No Transport Cost charged by seller so that Uniform Price can be fixed in market.

7) There is No Government Intervention in working of market. It means Government must follows- Laissez Faire Policy.

8) All buyers and sellers must be Rational i.e Each buyer wants maximum satisfaction with Minimum Expenditure.
Each seller wants Maximum Profit with Minimum Investment.

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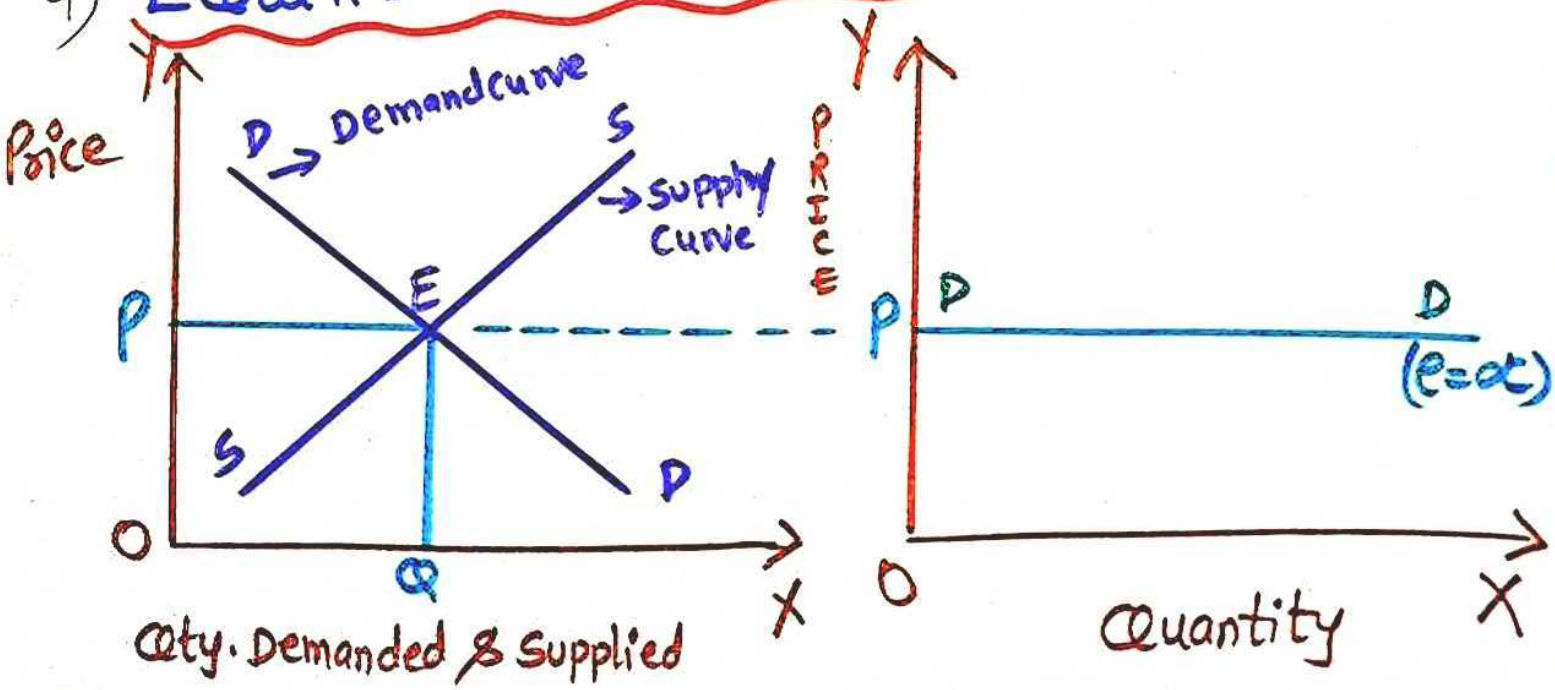
9) **Equilibrium Price Under Perfect Competition:-**



In the above diagram –

i) Price is determined where Demand Curve intersect Supply Curve. It is called Equilibrium Price.
Equilibrium Price = OP

ii) OP Price is fixed in market, where sellers has to sell their Commodity at Uniform Price. Thus every seller is Price-taker in Perfect Competition.

iii) Demand Curve is Perfectly elastic in nature due to Uniform Price. It has Horizontal slope.

Q:2 Explain the Short-Run Equilibrium of a Firm With Excess Profit, Normal Profit and Loss Covering Only TVC ?

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(A) Short-Run Equilibrium of Firm Under Perfect Competition :-

We study the Equilibrium of a Firm with the help of Following Assumptions :–

1) There is Perfect Competition in Product Market.
2) The Firm is Rational. It means seller wants to enjoy maximum profit.
3) There is Perfect competition in Factor Market. It means All firms are Producing goods Under-identical Cost Conditions.
4) The Firm is working under 'U' Shape Cost Curves.
5) Price of the Product is determined by Aggregate Demand and Aggregate Supply.

6. The Firm is a Price-taker.

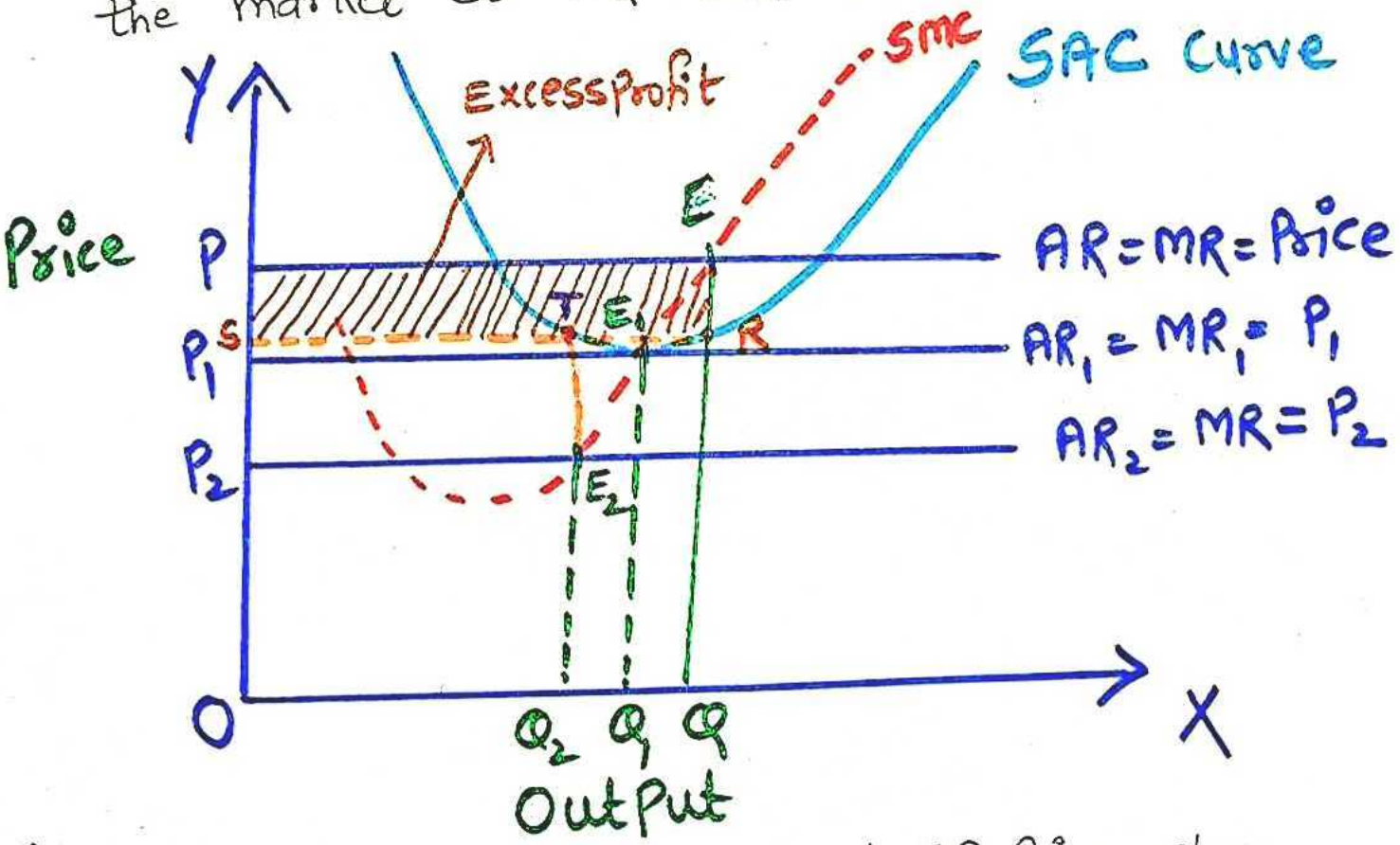
(B) Short-Run Equilibrium of Firm :-

In Short Period, Some inputs are Fixed like- Machinery, Capital, Equipments etc. But Some inputs are Variable in nature Like- Raw-material, Labour etc.

(C) Conditions of Equilibrium :-

1) MR = MC
2) Mc Curve intersect MR Curve from below.
3) Price = AVC.

Under Perfect Competition Each Seller is Price-taker but not Price-maker. As Uniform Price Prevail in the market so AR = MR = Price



1) A firm Produce OQ out put at OP Price where AR = MR = MC at Point E. Here firm enjoys Excess

Profit because $TR > TC$.

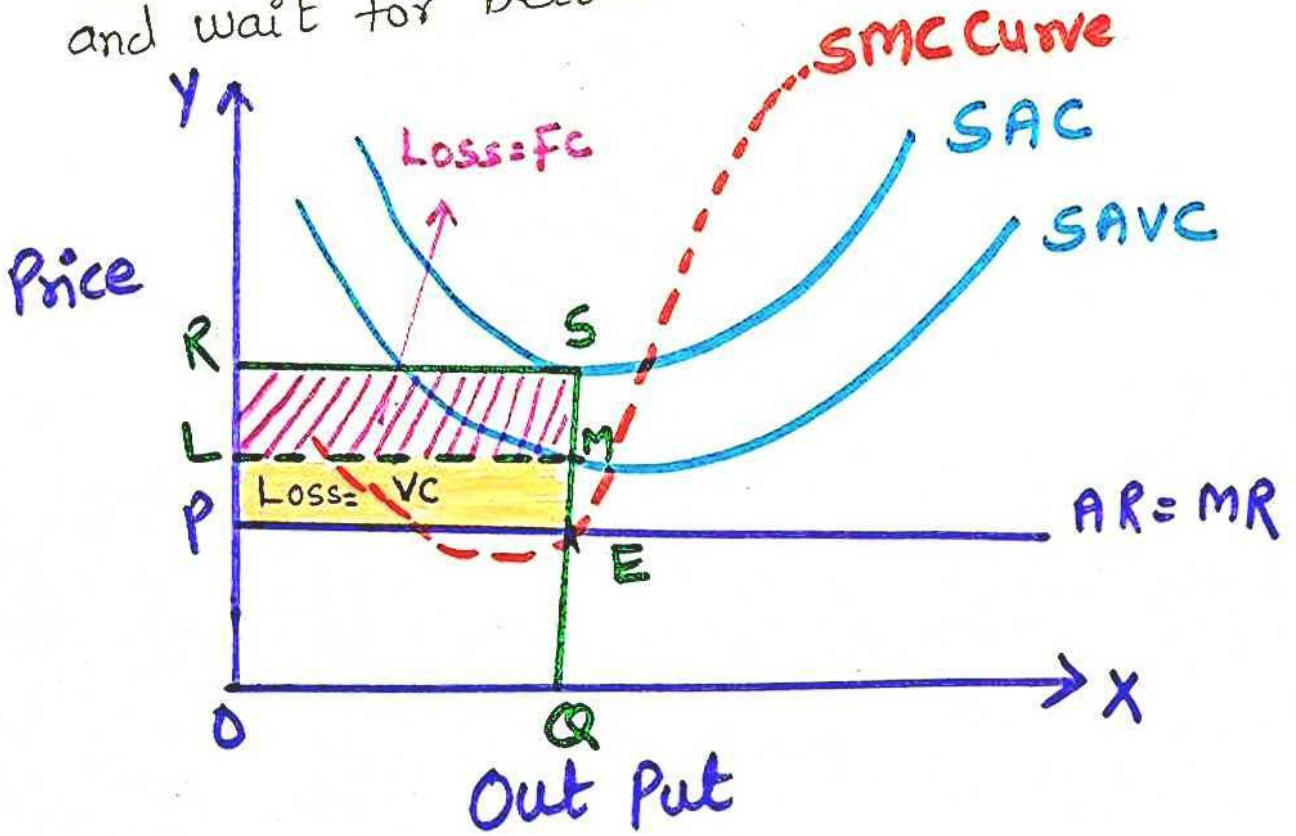
(2) A Firm Produce OQ_1 out Put at OP_1 Price where $AR_1 = MR_1 = MC$ at Point E_1. Here firm enjoys Normal Profit because $TR = TC$.

(3) A Firm Produce OQ_2 out Put at OP_2 Price where $AR_2 = MR_2 = MC$ at Point E_2. Here firm incur Losses because $TC > TR$.

$TC = SOQ_2T$.

$TR = P_2OQ_2E_2$.

(D) **Shut-Down Point :-** In Short-run every firm wants to cover Variable Cost. Fixed Cost can be Cover in Long Period. When firm is Unable to Cover Variable Cost then it is better to Shut-down and wait for better time to come.



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In above diagram we Observe -

1) A Firm Produce OQ output at OP price where- AR = MR = MC at Point E. Here firm suffer huge Losses because they are Unable to cover even Variable Cost.

2) TR = POQE and TC = ROQS

Huge Losses = TC - TR

= ROQS - POQE

Huge Losses = RPES

Loss of Fixed cost = RLMS

Loss of Variable cost = LPEM

Thus here Producer take decision to Shut down because TC > TR and firm is Unable to cover Avg. Variable Cost.

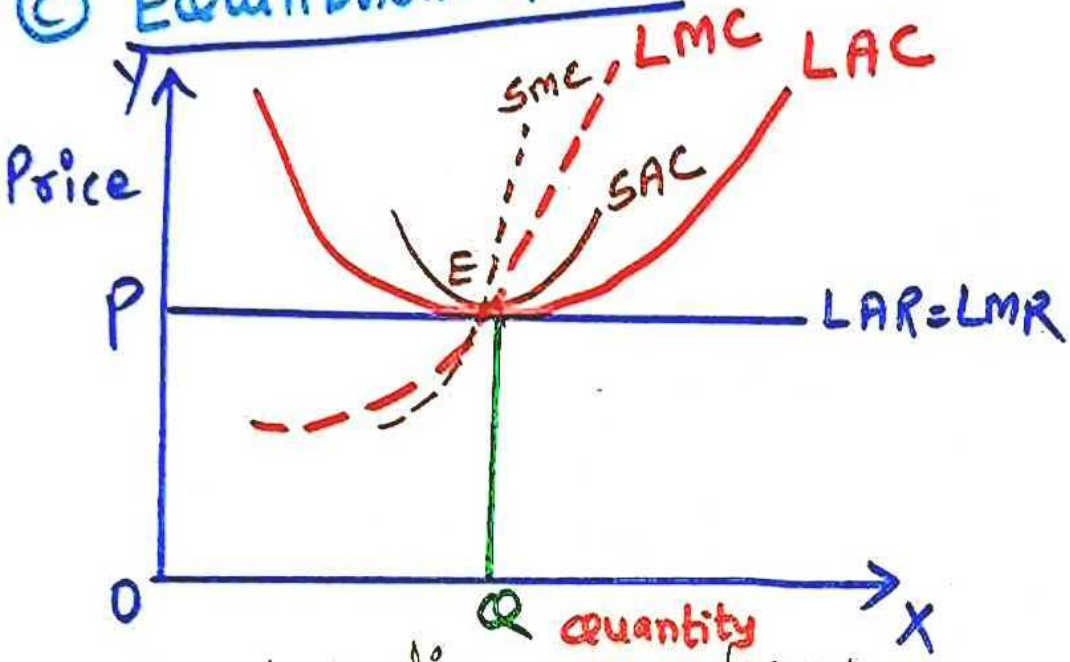
Q:3 Explain the Long-Run Equilibrium of a firm?

(A) **Long-Run Equilibrium :-** In Long Run Producer get Plenty time to adjust different factors as per requirement of market. In Long Run all factors are Variable in nature so Producer can easily increase or Decrease Production Capacity. In Long-Run there is Entry to and Exit from the market. Generally the firms will earn Normal Profit in the market in Long-Run.

(B) Conditions for Long-Run Equilibrium :-

1. LMC = LMR
2) LMC curve intersect LMR Curve from below.

(C) Equilibrium of firm



In the above diagram we observe-

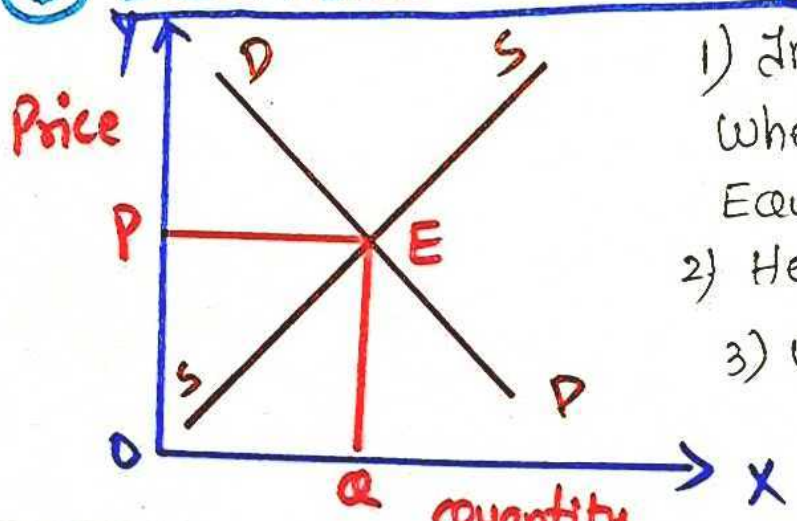
1) Price OP is fixed in Long-Run and Producer enjoys Equilibrium at Point E. Here SMC Coincides with LMC

and Price = LAR = LMR

Thus Price = LMC = SMC = LMR = LAR

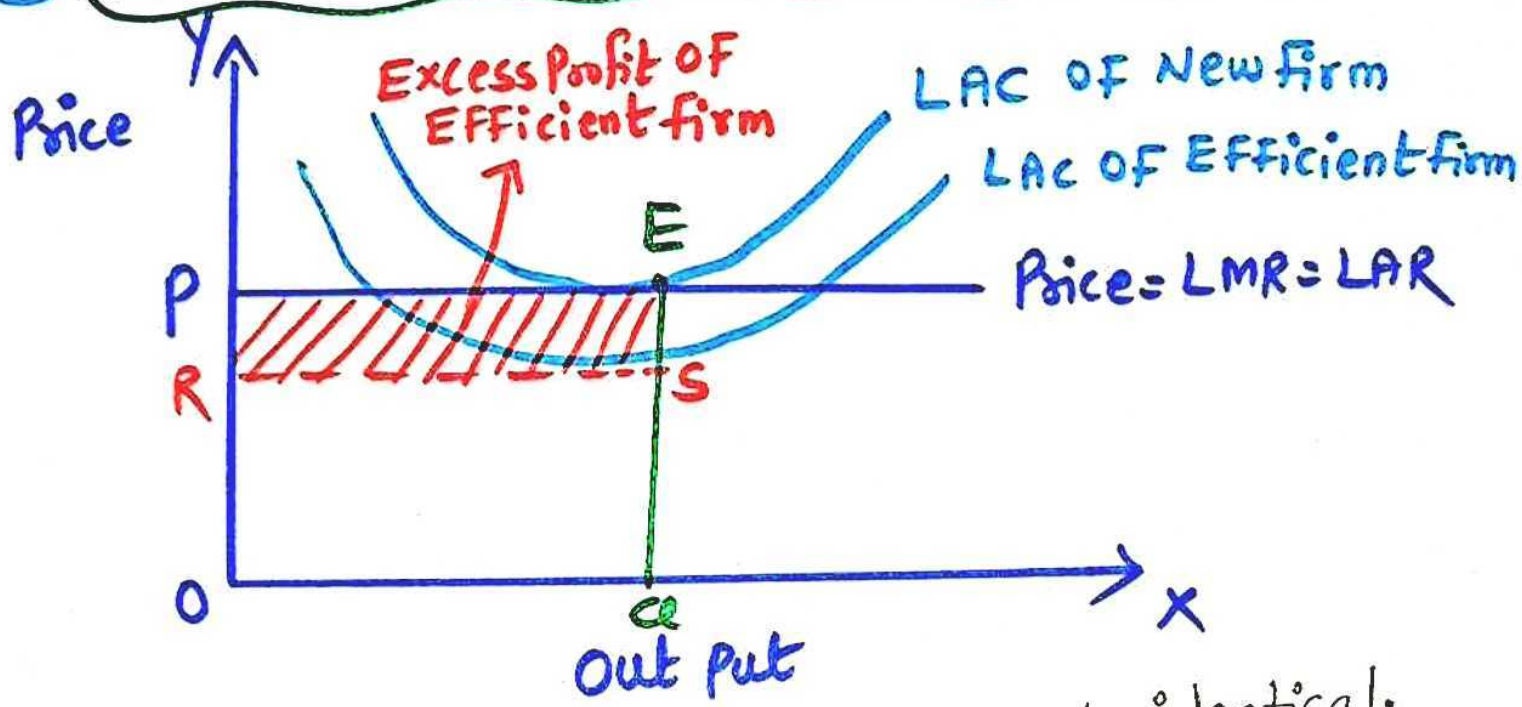
2) Here Producer enjoys Normal Profit because TR = TC.

(D) Equilibrium of Industry :-



1) Industry is in Equilibrium when all the firms are in Equilibrium with Normal Profit.
2) Here Price = MR = AR = LMC = LAC
3) Under these Conditions there is No Entry and Exit

(E) Equilibrium of EFFICIENT and New firm :-



1) In the the Long-Run, Costs are not identical.
2) More established and Efficient firms will have lower Cost than New firms in the Industry.
3) So New firms Can earn Normal Profit in Long Run as TC = TR.
4) But More Efficient firms Can enjoy Excess Profit because TR > TC.

TC = ROQS

TR = POQE

Thus Excess Profit = TR - TC

= POQE - ROQS

Excess Profit = PRSE

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Q:4 Choose the Correct Option :-

① In Perfect Competition at any given time, Price for a Commodity is **Same**

a) Same b) different c) discounted.

② Demand Curve of a firm in Perfect Competition is **Horizontal**

a) Horizontal b) Vertical c) downward sloping

③ In the Long-run all cost are **Variable**

a) Fixed b) Variable c) avoidable

④ A firm's Equilibrium Out Put is Produced at a Point **MC = MR**

a) MC = MR b) MC > MR c) MC < MR

⑤ In Perfect Competition, the actions of an individual buyer or Seller will **Have no impact on the market Price.**

a) Have no impact on the market Price.
b) Have some impact on Production.
c) Have a Significant impact on market supply.
d) Have a Significant impact on market Demand.

⑥ For a firm in a Perfectly Competitive market, the Price of the good is always **Equal to Marginal Revenue.**

a) Equal to Marginal Revenue.
b) Equal to Total Revenue.
c) Greater than Average Revenue
d) Equal to Firm's Efficient Scale of Out Put.

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(7) If a firm in a Perfectly Competitive market doubles the number of units of output sold, then Total Revenue will Exactly Double.

a) more than triple b) Halve
c) Exactly Double d) Remain Constant.

(8) Seller will have Little Reason to Charge Less than the going market Price because Goods Sold are Homogeneous.

a) There will be few buyers in the market.
b) There will be few sellers in the market.
c) Buyers will have greater advantage.
d) Goods sold are Homogeneous.

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(9) Which of the following is not a Characteristics of a Perfectly Competitive market? Pricing Policy of one Seller will affect Pricing Policy of rivals.

a) There are Large Number of buyers
b) Every seller is Price-taker.
c) Pricing Policy of one Seller will affect Pricing Policy of rivals.
d) Products are Homogeneous.

(10) The Demand Curve faced by an individual seller in Perfect Competition is Perfectly elastic

a) Perfectly elastic b) Perfectly inelastic
c) Relatively elastic d) Unitary elastic

(11) A firm in Perfect Competition, might decide to set its Price below the market Price because None of the

above is correct.

a) This would result in higher TR.
b) This would result in higher Profits.
c) This would result in Lower MC.
d) None of the above is Correct.

(12) Suppose a firm in a Competitive market Produces and Sells 100 Units of Output and has a Marginal Revenue of ₹8. what would be the firms Total Revenue?

₹ 800 (TR = Price × Qty = ₹8 × 100 units = ₹800)

a) ₹ 1600 b) ₹ 1000 c) ₹ 800 d) ₹ 2000

(13) If a firm in a Perfect Competition earns ₹ 1000 in TR and has MR of ₹ 10. what is the AR and How many Units were Sold? ₹10 and 100 units.

AR = MR = 10

Units = $\frac{TR}{Price/AR} = \frac{1000}{10} = 100$ Units

a) ₹ 5 and 50 b) ₹ 5 and 100
c) ₹ 10 and 50 d) ₹ 10 and 100.

(14) Suppose a Firm in a Perfectly Competitive market Sells 2000 units and earns TR of ₹ 50,000. what is MR of the firm? ₹ 25

$MR = \frac{TR}{Q} = \frac{50,000}{2000} = ₹25$

a) ₹ 50 b) ₹ 25 c) Less than ₹ 25 d) None of the data.

(15) Changes in the Output of a Perfectly Competitive Firm, Without any Change in the Price of the Product, will Change the Firm's Total Revenue.

a) Total Revenue b) Marginal Revenue
c) Average Revenue d) All the above are correct

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16) A firm in Perfect Competition selling Commodity X., Continue Production. If the market Price for X falls below firm's Avg. Total Cost, but still lies above Avg. Variable Cost, the firm will incur Losses but will Continue to Produce.

a) will Shut Down b) Should raise the Price

c) will incur Losses. but will Continue to Produce.

d) All the above.

(17) Which of the Following Statements is True about the decision of Profit Maximizing firm in a Competitive Market when Price Falls below the Minimum of Average Variable Cost? The Firm will immediately Stop Production to minimize Losses

a) The Firm will Continue to Produce to meet its fixed Costs

b) The Firm will immediately Stop Production to minimize its losses.

c) The Firm will Stop Production as soon as it is able to Pay its Sunk Costs

d) The Firm will Continue to Produce in the Short run but will Likely exit the market in the Long-run.

18) A Profit Maximizing firm will shut-down in the Short-run when. Price is Less than Avg. Variable Cost

a) Price is Less than AVC b) Price is Less than ATC

c) AR > MC d) AR > AFC

19) which of the following statements is correct regarding a firms decision-making?

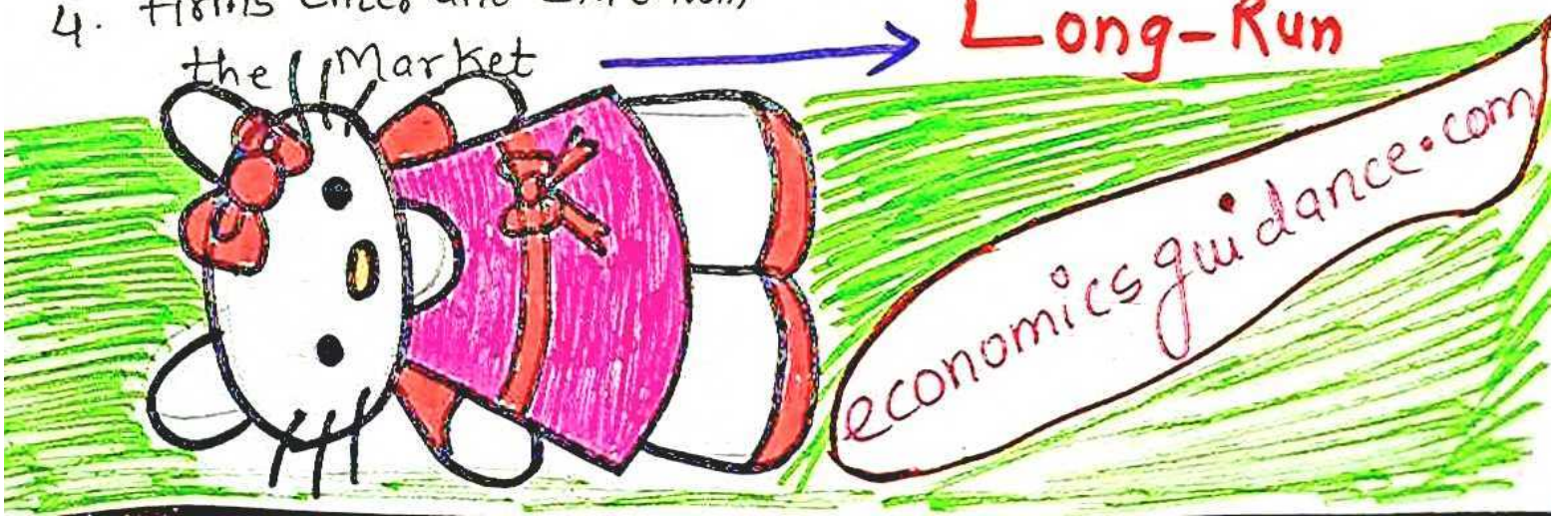
The decision to shut-down is a short-run decision whereas the decision to exit is a Long-Run decision.

a) The decision to shut-down and decision to exit both Short-Run decision

b) The decision to shut-down and the decision to exit are both Long-run decisions.

c) The decision to shut down is a short-run decision, whereas the decision to exit is a Long-Run decision.

d) The decision to exit is a short-run decision whereas the decision to shut down is a Long-Run decision.

Q-5 Match the Following :-

1. AR is Horizontal Line → Perfect Competition
2. TVC > TR → Shut-down Point
3. P = AR = MR = AC = MC → Long-Run Equilibrium
4. Firms Enter and Exit from the Market → Long-Run