Microeconomics, Module 13: “Market Power” (Chapter 11)

Illustrative Test Questions

(The attached PDF file has better formatting.)

{*Note for candidates:* Some illustrative test questions in this module and in the subsequent modules relate to sections of the textbook that are not required reading for this course. Landsburg is a wonderful story-teller, and his analyses are fascinating. The final exam will test only those sections of the textbook that are in the required reading, but you may want to read other portions as well.}

Question 13.1: Vertical Merger

A vertical merger takes place between two monopolists: a computer manufacturer and a memory chip supplier. The merger may increase social welfare because the new firm

A. Gets both consumers’ surplus from buying memory chips and producers’ surplus from selling memory chips.
B. Earns monopoly profits in both the memory chip market and the computer market.
C. Can force the memory chip supplier to sell at below cost to the computer manufacturer.
D. Will behave competitively in the market for computers.
E. Has the resources to spend more on research and development.

Answer 13.1: A

Question: What does statement A mean?

Answer: Before the merger, the memory chip supplier set quantity to maximize producers’ surplus. After the merger, the firm sets quantity to maximize the sum of producers’ surplus and consumers’ surplus.

Question 13.2: Horizontal Merger

Which of the following is the best example of a horizontal merger?

A. A merger of a lumber mill and a furniture manufacturer.
B. A merger of a popcorn company and a book publisher.
C. A merger of two local grocery store chains.
D. A merger of a spark plug producer and an automobile manufacturer.
E. A merger of an insurance company and an actuarial consulting firm.

Answer 13.2: C

A and D are vertical mergers; B is a conglomerate; E is either a vertical merger, if the consulting firm provides services to the insurance company, or a conglomerate, if the consulting firm provides services to non-insurance firms.

Question 13.3: Competitive Strategy

Borrowing, “lying low,” and future re-entry are strategies that a firm can use to counter

A. The effects of regulation
B. A supplier’s imposition of resale price maintenance
C. Predatory pricing
D. A proposed buy-out
E. Arbitrage opportunities

Answer 13.3: C

Question 13.4: Resale Price Maintenance

Firms may practice resale price maintenance to enforce a cartel among retailers. Why else might a firm practice resale price maintenance?

A. To guarantee high monopoly prices.
B. To guarantee that retailers will supply customer service.
C. To prevent retailers from appropriating part of the firm's monopoly profit.
D. To force retailers to absorb the cost of selling the good.
E. To prevent retailers from forming a cartel.

Answer 13.4: B

This is Landsburg's alternative explanation. See the discussion forum postings for the standard explanation.

Question 13.5: Resale Price Maintenance

Who gains from resale price maintenance?

A. The manufacturer, but not the retailers or consumers.
B. The retailers, but not the manufacturer or consumers.
C. The manufacturer and the retailers, but not the consumers.
D. The retailers and the consumers, but not the manufacturer.
E. The retailers gain, and the manufacturer and consumers may also gain.

Answer 13.5: E

Landsburg shows a scenario where all three parties gain in his alternative explanation.