

BASIC THEORY QUESTIONS:

- 1) The problems that we address in this class presume a reasonable understanding of basic price theory.
 - a) Describe the stylized model of perfect competition.
 - b) Why is competition good and monopoly bad?
- 2) I drive a big, fat truck that uses a lot of gasoline and, no doubt, to some extent increases the price of gasoline that you must pay. Am I making you worse off?
- 3) Why is the concept of U-shaped average cost a good characterization of the nature of production within a firm?
- 4) In the very short run practically all costs are fixed. Does that mean that marginal cost is zero? Why or why not?
- 5) Very few industries (maybe none) exhibit the theoretical conditions of perfect competition. Even so, competition from the fringe seems to be common in most markets. Sometimes this is called contestability. Discuss the competitiveness of the fast-food industry in this light.
- 6) Under what circumstances does a company go into bankruptcy? Under what circumstances does a firm dissolve and cease doing business? Is it normal for a bankrupt firm to shut down?
- 7) If all fixed costs for a particular firm are entirely avoidable, i.e. are not sunk and vary with production, will the firm choose to shutdown at the minimum of average variable cost? If not, why not?
- 8) Are positive economic profits inconsistent with a long-run competitive equilibrium? Why or why not?
- 9) What is the hold-up problem? How is it associated with asset specificity? Why do we say that the firm faces a tradeoff between the hold-up problem and the problem of separation of ownership and control?
- 10) What is the contracting-cost nature of the firm? What constrains the growth of the firm? What promotes the growth of the firm? How does the concept of shirking fit into the organization of the firm?
- 11) Are large firms more likely to have monitoring problems? If so, why do large firms exist?
- 12) What did Coase mean when he described the firm as the suspension of the price mechanism? Discuss.

APPLICATIONS:

- 13) How do the profits of a dominant firm and a monopoly compare? How do they both compare to the profits of a cartel? Make an attempt to graphically illustrate your points.
- 14) Describe the entry of Wal-Mart into the Clemson business area in terms of the dominant firm model and explain the costs and benefits to the consumers and producers who were here before Wal-Mart.

- 15) Look up the most recent concentration ratios and Herfindahl (HHI) indices for the following industries: beer; aluminum; breakfast cereal; petroleum refineries. Discuss the competitive nature of these industries.
- 16) Discuss the various theories of oligopoly.
- 17) Recount the evidence that the U.S. Steel merger of 1901 was a merger for monopoly. What evidence is there to the contrary?
- 18) What are some of the key assumptions underlying the Cournot model of a non-cooperative oligopoly? How do rival firms react to one another and what is the structure of their production levels and respective profits?
- 19) According to the game theory strategy posed by the prisoners' dilemma, how should firms choose their strategies? Feel free to present a sample scenario. Consider the case of a single game and the case of repeated interactions.
- 20) *Car Wars*: How do you explain that in a single year (1955 to be exact) American passenger automobile production rose by 45 percent, but then fell by nearly the same amount in 1956? In addition, how do you think the average prices of these cars evolved over these three years, and why?
- 21) What evidence would constitute proof of predatory pricing as opposed to straightforward competition? Use the example of Standard Oil (c. 1900) as an example. Why are price differentials based on cost differences not predatory pricing?
- 22) Discuss the theory of limit pricing. What are the predictions of this model? What evidence exists to support the relevance of this model?
- 23) a) Describe the process of two-tier or multipart pricing. b) Describe how block booking can be a form of price discrimination.
- 24) How does competition expunge price discrimination? How can price discrimination exist in otherwise competitive markets? Give some examples of competition in competitive settings; comment on the nature of competition in these cases.
- 25) The Walker Golf Course at Clemson charges several different sets of prices to students. Students can pay a flat fee of \$250 per semester and play as much as they like for free (if they walk; to ride a cart costs extra). Alternatively, they can pay \$15 per round on weekdays and \$25 per round on the weekend. Explain how the Walker Course makes money by using this pricing scheme.
- 26) *Electric Conspiracy*: What motives led several electrical equipment manufacturers to produce the same exact bids for Tennessee Valley Authority contracts in the 1950s? What characteristics of the electric industry in particular facilitated this behavior? Why was the electric conspiracy a likely candidate for price collusion. Is it likely that automobile companies collude on price?
- 27) Officials of the ADM corporation were found guilty of conspiring to fix prices on a food additive. Give an account of this and speculate on what you think might have been the total loss to society if the government had not found out about this conspiracy.

- 28) I claim that the grocery industry (Ingles, Bi-Lo, Publix, etc.) is competitive because the national brands in the food processing industry wouldn't have it any other way. What do you think of this argument? (Discuss.)
- 29) Many monopolies are created and supported by government. What are the causes and consequences of this?
- 30) The Structure/Conduct/Performance paradigm argues that concentration leads to collusion that leads to excess profits. This argument is supported by a strong correlation between profits and concentration. Brozen-Peltzman-Demsetz object to this by claiming that the causality goes in the opposite direction. What is the compelling evidence of their research? How does the Wal-Mart example fit into this discussion?
- 31) What are the efficiency arguments for vertical integration of production? In what way might vertical integration be anticompetitive?
- 32) How can the phenomenon of not-for-profit institutions be explained within the rubric of the evolution of the firm? Specifically, compare not-for-profit institutions with stock corporations. What characteristics on the demand and supply sides of the market make not-for-profit institutions dominate production in some settings and stock corporations in others?
- 33) Why do people paint their houses before they sell them? Is it correct to say that because the practice survives that it is efficient? (Compared to what alternative?) Is painting a house before selling it the same as women wearing makeup?
- 34) If people can't tell the difference between products like Coke and Pepsi in blind taste tests, what is the point of brand names for these products?
- 35) Religious schism teaches us an important lesson about brand names. What is it?
- 36) The claim is that Holstein steers are the only breed sold at auction for veal. (Veal is cow meat that is light in color and especially tender.) Presumably this is because their stomachs bloat immediately when they first eat grass, and grass turns cow meat from veal to beef. Assume that this is true. How can we know that the Holstein steers bought at auction are slaughtered for veal?
- 37) In the grocery store, oranges are often sold loose or already packaged. Which oranges cost more by the pound or, in other words, if I were to give you one pound of either loose or packaged oranges, which would you choose? Discuss this issue in detail.
- 38) Discuss the application of the Coase Theorem in the following settings: coastal development, restaurant smoking, and the depletion of timber in south Georgia (U.S.), upstate South Carolina, and the Amazon rain forests.
- 39) Should eBay be held responsible when people sell counterfeit goods? Does it matter if the buyers know that the goods are counterfeit? Does it matter if the trademark is expired?
- 40) Why do cable TV companies bundle channels? What will be the likely effect of forcing a la carte pricing on the industry?
- 41) Intellectual property is protected by patents, copyrights, trade-secret and trademark law. What is the fundamental tradeoff faced by society in determining the degree to which these property rights are enforced? What tips the balance?

- 42) Define "public good." Why do we say that intellectual property is a public good? How does this affect the nature of property right protection for intellectual property?
- 43) Define the "the tragedy of the commons"; give some examples.
- 44) Explain the nature of the population problem. How is the population problem related to "the tragedy of the commons"? Also provide solutions, if any exist, to this problem.
- 45) Payola, which is inducements paid by record companies to DJs to get playing time for songs, was made illegal in 1960. Was this a good law? Explain. Is payola from text-book publishers to college professors the same thing as payola to DJs?
- 46) Explain the median-voter, public interest theory of government, in the context of the optimal supply of public goods.
- 47) Explain the special interest theory of government.
- 48) If I break my tennis racket intentionally, I am happy. If I lend you my tennis racket and you break it intentionally, I am sad. Why? And it is not the money. Assume that I would give you the equivalent amount of money if you asked for it.
- 49) Why is the California gold rush of 1848-49 interesting to us?