7.1 The Basic Objective of Firms: Profit Maximisation

1. In a perfectly competitive market, a competitive firm

☐ can sell its products at any price it wants.

☑ cannot control the market price.

☑ can adjust its output level to maximise profit.

2. The table below shows the production information of a competitive firm. The firm has a fixed cost of $5 and the market price of the good is $30.

Output (units)	Total cost ($)	Total revenue ($)	Profit ($)	Marginal cost ($)	Marginal revenue ($)
1	20	30	10	15	30
2	30	60	30	10	30
3	50	90	40	20	30
4	80	120	40	30	30
5	120	150	30	40	30

(a) Complete the table.

(b) Under total analysis, the profit-maximising output of the firm is 3 or 4 units.

(c) Under marginal analysis, the profit-maximising output of the firm is 4 units.

3. Given a market price, if the fixed cost of a price taker increases, its profit-maximising output will *(increase / decrease / remain unchanged)*.

4. Given a market price, if the marginal cost for each unit of output of a price taker increases by the same amount, its profit-maximising output will *(increase / decrease / remain unchanged)*.

5. Given a market price, if the average cost for each unit of output of a price taker increases by the same amount, its profit-maximising output will *(increase / decrease / remain unchanged)*.

7.2 The Supply Schedule of a Competitive Firm

6. The supply schedule of a competitive firm is determined by its *(average cost / marginal cost) schedule*.

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7.3 Other Objectives of Firms

7. When a new market opens up, the firms may pursue a higher sales volume for a short period of time and they are likely pursuing the objective of market share maximisation.

8. If a firm participates regularly in charitable activities that are not aimed at making profit, it may be trying to pursue the objective of fulfilling corporate social responsibility.

7.4 Expansion and Integration of Firms

9. A firm engages in *(internal / external)* expansion when it opens more branches.

10. A firm engages in *(internal / external)* expansion when it acquires another firm.

11. A shoe manufacturer acquires a leather factory.

(a) It is an example of vertical backward integration.

(b) List **THREE** possible motives for this type of integration.

to ensure a reliable supply of input / to enjoy economies of scale / to use resources more efficiently / to take advantage of brand names / to diversify sources of income and spread risk (OR any reasonable answers) (Any two)

12. Below shows some cases of business expansion. Identify the type of expansion and determine whether the expansion matches the firm's motive.

Case	**Type of expansion**	**Does the expansion match the firm's motive?**
(a) A car manufacturer opens a car retailing shop to increase its market share.	vertical forward expansion	*(Yes / No)*
(b) A bookshop acquires a salon to spread risk through diversification.	conglomerate integration	*(Yes / No)*
(c) A bus company acquires another bus company to enjoy economies of scale.	horizontal integration	*(Yes / No)*
(d) A retailer of ladies wear starts a new brand of kids wear to use resources more efficiently.	lateral expansion	*(Yes / No)*

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