

Revision Worksheet Answers

A2 Economics

Answer: What is Profit?

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WORKSHEET ..Answer..

Revision Topic : What is meant by profit?

Answers to Multiple Choice Questions

Question 1

Correct Answer B (1 mark)

Answer Guide :

The monopoly position of the sports centre allows it to set $MR=MC$ (1 mark). Explanation of condition, e.g. by looking at the margin either side of output level B (2 marks). [Possibility of explaining why the other output levels are not profit maximizing].

Question 2

Correct Answer A (1 mark)

Answer Guide :

Revenue maximization needs to be defined (marginal revenue=zero) (1 mark). This involves a higher level of output than where $MC=MR$ (1 mark) (given that MC is always positive). Therefore the firm needs to reduce price and increase output. This mark can also be earned if the candidate provides a correct diagram (1 mark). Examiners should consider carefully any scripts where the duplicated key (D) has not been crossed out. If there is any suspicion in their minds that this might have disadvantaged candidates they should contact the Principal Examiner, who may ask for the script to be forwarded to him for further consideration.

Question 3

Correct Answer D (1 mark)

Answer Guide :

Explanation (or illustration on the diagram) of the rising price of profit area or falling quantity (1 mark). Identification of $MR=MC$ condition for profit maximization (1 mark). Explanation of $MR=MC$ condition (1 mark)

Question 4

Correct Answer B (1 mark)

Answer Guide :

Explanation of revenue maximization ($MR=0$) (1 mark) Explanation of super-normal profits as $OKLZ - ONMZ$ or as profit per unit LM multiplied by total output MN (2 marks) Also award for shading in of super-normal profits on diagram (1 mark) Diagram showing TR in line with $MR=0$ (2 marks).

Question 5

Correct Answer D (1 mark)

Answer Guide :

Definition of sales maximization (The highest output position attainable for the firm without making a loss (1 mark) Sales maximization is the highest output position where $TC=TR$ (1 mark). Only normal profits achieved (1 mark) Also award: output position where $AC=AR$ (1 mark) Also award reference to output position after sales maximization. (1 mark)

Question 6

Correct Answer B (1 mark)

Answer Guide :

Identification of Profit Maximizing condition $MC = MR$ (1 mark) Calculation of Marginal Revenue (1 mark). Calculation of Marginal Cost (1 mark) If the candidate correctly identifies Profit Maximization from the total cost and total revenue including calculations of difference between TC and TR reward full marks.

Question 7

Correct Answer D (1 mark)

Answer Guide :

Revenue maximization is where average revenue multiplied by output is at a maximum (1 mark) Application - the diagram shows the total revenue curve is at the highest point / the gradient is zero / diagram showing a falling MR curve and being equal to zero when

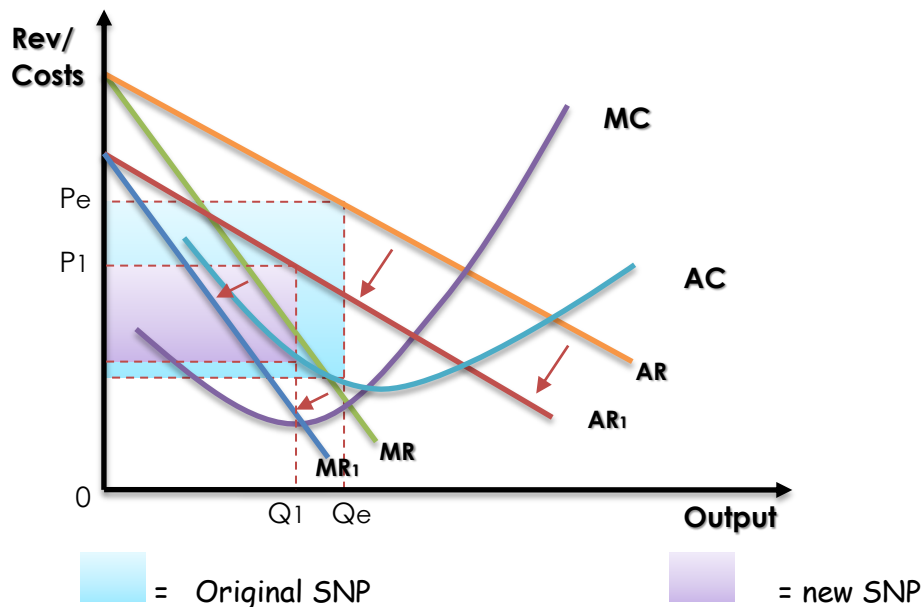
TR is maximized (1 mark) Revenue maximization is the output where marginal revenue is zero ($MR=0$) (1 mark) Marginal analysis: for example, to the left of output Q_e MR is positive / TR is rising, to the right MR is negative / TR is falling (1 mark).

Also award candidates who knock out up to two incorrect options for two marks e.g. Key 'A' is incorrect as this is where total revenue equals total cost / breakeven point (1 mark) Key 'B' is incorrect since profit maximization is at output Q_3 (1 mark) Key 'C' is incorrect since sales maximization is at output Q_5 (1 mark) Key 'E' is incorrect since allocative efficiency is output where $MC=Price$ (1 mark)

Question 8

Correct Answer A (1 mark)

Answer Guide :



Application to diagram showing:

A decrease in average revenue marginal revenue curves e.g. from AR and MR to AR1 and MR1 (1 mark) A lower price and output e.g. from P_e to P_1 and Q_e to Q_1 (1 mark) A decrease in profits (1 mark) e.g. shown graphically the new profit area.

If no application to diagram, award a maximum of (1 + 1) explanation marks.

Question 9

Correct Answer B (1 mark)

Answer Guide :

Allocative efficient pricing is where marginal cost equals average revenue ($MC = AR$ or $MC = Price$). (1 mark) Definition of supernormal profits (where total revenue exceed total costs / profits in excess of that required to keep resources in their current use / profits greater than normal profits). (1 mark). At output level Q4, price (average revenue) exceeds average cost and so supernormal profit is made. (1 mark)

Also award:

Annotation of diagram, for example, shading in areas of supernormal profits. (1 mark)
Be prepared to award knock-out marks, for example option A is incorrect since revenue maximization output of Q2 is greater than profit maximization output of Q1. (1 mark)

Question 10

Correct Answer A (1 mark)

Answer Guide :

Annotation of the diagram up to (3 marks).

The increase in marginal cost curve (1 mark), depicting higher equilibrium price and lower equilibrium output (1 mark), the increase in average cost curve leads to lower profits (1mark)