

CA14 ECONOMICS

SECTION 6: MARKET STRUCTURES AND FIRM EQUILIBRIUM

Syllabus references: MKT-01 to MKT-04

Purpose. Original DatalytlQs Academy teaching notes aligned to the KASNEB Revised Syllabus (June 2024).
Suggested study time: 10-12 hours. **Assessment threshold:** 70%. No KASNEB endorsement is implied.

Learning outcomes

After this section, the learner should be able to compare perfect competition, monopoly, monopolistic competition and oligopoly; determine profit-maximising output; distinguish short-run and long-run outcomes; evaluate efficiency, price discrimination and strategic interdependence.

Contents

1. Analytical framework
2. Perfect competition
3. Monopoly
4. Price discrimination
5. Monopolistic competition
6. Oligopoly

1. Analytical framework

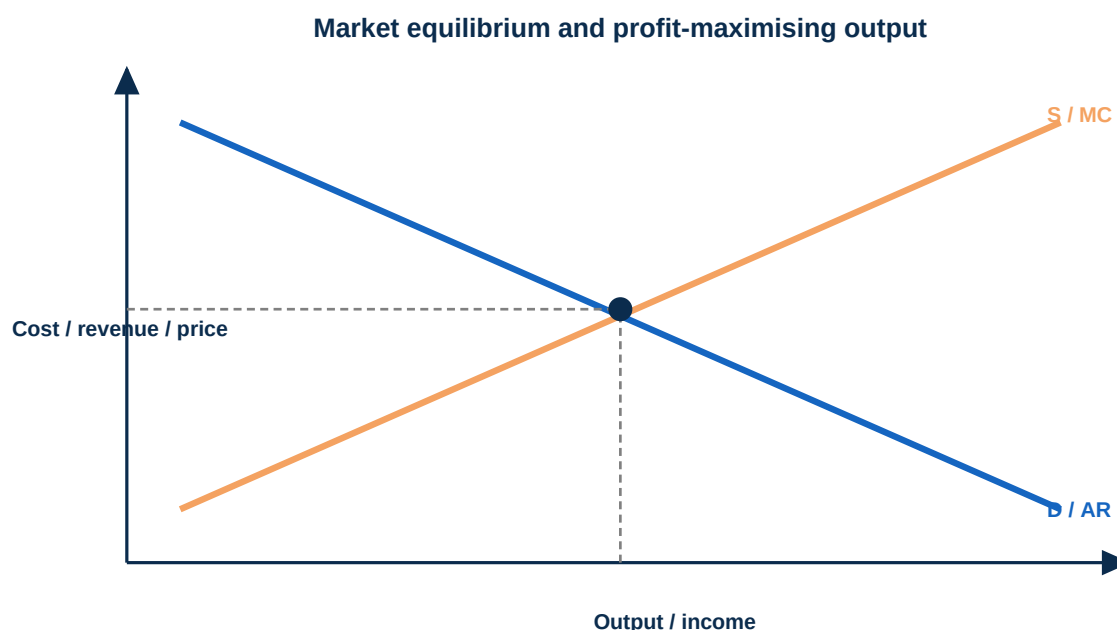
Market structure is compared through number and size of firms, product differentiation, entry barriers, information, control over price and strategic interdependence. The profit-maximisation rule is $MR=MC$ with MC rising, but price and long-run adjustment differ by structure.

Feature	Perfect competition	Monopoly	Monopolistic competition	Oligopoly
Firms	Many small	One dominant supplier	Many	Few large
Product	Homogeneous	No close substitute	Differentiated	Homogeneous or differentiated
Entry	Free	Blocked	Relatively free	Significant barriers
Strategic interdependence	None	Limited direct rivalry	Limited	Central

Examination technique: State the proposition, explain the mechanism, apply it to the question and qualify the conclusion where assumptions or context matter.

2. Perfect competition

A competitive firm is a price taker: $P=AR=MR$. It chooses output where $P=MC$, provided price covers the relevant avoidable cost. In the short run it may earn abnormal profit, normal profit or loss. It continues temporarily when P covers AVC ; it shuts down when $P < \text{minimum } AVC$. Free entry and exit drive long-run economic profit toward zero and output toward minimum ATC under standard assumptions.



Examination technique: State the proposition, explain the mechanism, apply it to the question and qualify the conclusion where assumptions or context matter.

3. Monopoly

A monopolist faces the market demand curve, so MR lies below price for a downward-sloping linear demand. It chooses Q where $MR=MC$ and then charges the price consumers will pay on demand. Monopoly can sustain abnormal profit when barriers persist. Compared with competition, output is usually lower and price higher, creating deadweight loss, although innovation, scale and regulation may qualify the conclusion.

Examination technique: State the proposition, explain the mechanism, apply it to the question and qualify the conclusion where assumptions or context matter.

4. Price discrimination

Price discrimination charges different prices not justified by cost differences. It requires market power, separable customer groups and limited resale. First degree extracts each buyer willingness to pay; second degree varies price by block/version; third degree charges groups different prices. The higher price is charged in the market with less elastic demand, other factors constant.

Examination technique: State the proposition, explain the mechanism, apply it to the question and qualify the conclusion where assumptions or context matter.

5. Monopolistic competition

Firms sell differentiated products and face downward-sloping demand. Short-run abnormal profit attracts entry of substitutes, shifting each incumbent demand left until it is tangent to ATC in long-run equilibrium. Firms earn normal profit but operate with excess capacity: output is below the quantity minimising ATC.

Examination technique: State the proposition, explain the mechanism, apply it to the question and qualify the conclusion where assumptions or context matter.

6. Oligopoly

A few firms recognise mutual interdependence. Outcomes depend on expectations, repeated interaction, capacity and regulation. The kinked-demand model explains possible price rigidity but not the initial price. Game theory represents strategies and payoffs; a dominant-strategy or Nash outcome may be collectively inferior, creating incentives for collusion that competition law constrains.

Firm A \ Firm B	Low price	High price
Low price	40,40	70,20
High price	20,70	60,60

Examination technique: State the proposition, explain the mechanism, apply it to the question and qualify the conclusion where assumptions or context matter.

Worked examples

Worked example 1

Demand $P=100-Q$, so $MR=100-2Q$. If $MC=20$, $MR=MC$ gives $Q=40$; price=60. Profit requires comparing $TR=2,400$ with total cost.

Reasonableness check: Confirm the direction, units and economic interpretation before finalising the answer.

Worked example 2

Two markets have elasticities 2 and 0.5. Under third-degree discrimination, the less elastic market normally receives the higher mark-up.

Reasonableness check: Confirm the direction, units and economic interpretation before finalising the answer.

Common errors and corrections

Error	Correction
Giving a definition without mechanism	Explain the causal link and apply it to the facts.
Using accounting language for an economic concept	Identify opportunity cost, implicit cost or real/nominal basis explicitly.
Drawing an unlabeled diagram	Label axes, curves, initial position, change and result.
Treating a historical pattern as a guarantee	Use it only to guide emphasis; cover the full syllabus.

Original DatalytlQs examination-style practice

Question 1 - Distinguish

Normal profit and abnormal profit.

DatalytlQs model answer: Normal profit is the opportunity cost of enterprise and is included in cost; abnormal profit is revenue above all economic costs.

Question 2 - Calculate

For $P=80-Q$ and $MC=20$, find monopoly Q and P .

DatalytlQs model answer: $MR=80-2Q$; $Q=30$ and $P=50$.

Question 3 - Evaluate

Assess whether monopoly is always harmful.

DatalytlQs model answer: Analyse price/output, efficiency and rent-seeking against scale, innovation, natural monopoly and regulation; conclude by conditions.

Revision summary

Core rule: Reconstruct the model from definitions, assumptions, relationships and diagrams. Memorised labels without mechanism do not earn strong analytical marks.

Evidence requirements

Evidence ID	Learning Objectives	Assessment criteria
E6.1	Four-structure comparison matrix.	Correct method, complete interpretation, labelled working and original learner submission.
E6.2	Competitive firm shutdown and long-run diagram.	Correct method, complete interpretation, labelled working and original learner submission.
E6.3	Monopoly price/output/welfare calculation.	Correct method, complete interpretation, labelled working and original learner submission.
E6.4	Oligopoly payoff matrix and strategic recommendation.	Correct method, complete interpretation, labelled working and original learner submission.

Mastery checklist

Check	Teacher
I can four-structure comparison matrix..	
I can competitive firm shutdown and long-run diagram..	
I can monopoly price/output/welfare calculation..	
I can oligopoly payoff matrix and strategic recommendation..	
Progression rule: Complete E6.1-E6.4 before the section quiz. A score below 70% triggers targeted remediation.	

References and version

KASNEB. *Certified Public Accountants (CPA) Revised Syllabus, June 2024*, Paper No. 4: Economics. Version 1.0, revised 18 October 2026. This is original DatalytlQs Academy instructional content.

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