Past-paper walk-through

Differing objectives and policies of firms ▪ 7.8

eXercise

Questions in this set

- 9708/31 N25 Q1 ▪ 1 mark
- 9708/31 N25 Q7 ▪ 1 mark
- 9708/32 N25 Q9 ▪ 1 mark

Question 1

9708/31 N25 ▪ Q1 ▪ 1 mark

1 What is likely to lead to the principal-agent problem?

A a manager of a business makes decisions on behalf of the owner

B music festival tickets are purchased by a person who intends to sell them at a large profit

C the government is the only buyer of a pharmaceutical product

D there is only one firm that manufactures the product

Solution 1

Answer: **A**

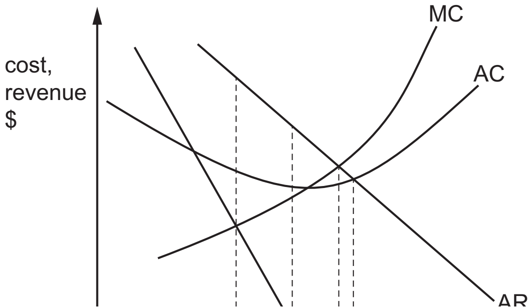
Why

- The principal–agent problem arises when one person acts on behalf of another.
- Their interests differ, and the agent has information the principal does not.
- A manager deciding for the owner is the textbook case – the manager may pursue growth or salary rather than profit.

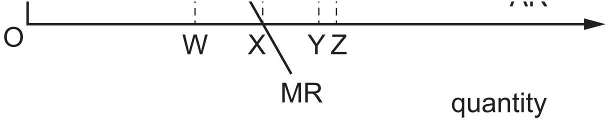
Question 7

9708/31 N25 ▪ Q7 ▪ 1 mark

7 The diagram shows the cost and revenue curves of a firm.



Question 7



The firm changes its objective from revenue maximisation to sales maximisation.

What will be the effect on quantity produced?

A it will decrease from Y to W

B it will decrease from Z to W

C it will increase from X to Y

Question 7

D it will increase from X to Z

Solution 7

Answer: **D**

Why

- Revenue maximisation is where marginal revenue equals zero.
- Sales maximisation is the largest output at which the firm still breaks even – where AR equals AC.
- So the output rises when the objective changes, because breaking even permits more output than MR $= 0$.

Question 9

9708/32 N25 ▪ Q9 ▪ 1 mark

9 What is the essential feature of nudge theory?

A the aim of satisficing

B the establishing of a legal requirement

C the existence of a contestable market

Question 9

D the idea of persuasion

Solution 9

Answer: **D**

Why

- Nudge theory changes the way choices are framed while leaving all the options open.
- So it works by altering the default or the salience of a choice, not by compelling anyone.
- A legal requirement removes the choice, which is the opposite of a nudge.