



Province of the
EASTERN CAPE
DEPARTMENT OF EDUCATION

2020

ECONOMICS GRADE 12

**MICROECONOMICS – TOPIC 6: PERFECT
COMPETITION**

LEARNER NOTES

BOOK 01

FOREWORD

The Learner Support Notes were developed by Mrs. L. Booï, the Economics Subject Advisor from OR.Tambo District in collaboration with Dr. T.B Rantsane, the Subject Planner from the Provincial ECDoE.

The motive behind producing these simplified learner support material is to support Grade 12 learners in the Microeconomics, in general and Perfect Competition, in particular as they prepare for the final 2020 NSC Examination during the Covid-19 period. The disruption to teaching, learning and assessment caused by Covid-19 is immeasurable but we have not lost hope that the “CLASS OF 2020 LEARNERS” can with maximum support from everyone, realise their dreams.

The notes guide candidates on the important aspects to consider under each topic, such as concepts/diagrams / illustrations/cartoons and tips on how to answer questions.

These NOTES should be used in conjunction with:

- Prescribed textbooks and sources
- 2017 Grade 12 Economics Examination Guidelines
- Economics Mind The Gap (CAPS),

where detailed information is provided before answering the questions provided.

The Economics Mind the Gap is an important source to use to study the summary of topics.

Learners should understand the action verbs in order to know how to respond appropriately to the question. For example; name, evaluate, explain and describe. Refer to 2017 Grade 12 Economics Examination Guidelines for the explanation of the action verbs.

Topics that are included in these notes:

- Microeconomics
- Assessment Activities

A summary of important aspects is included in each topic. Learners can obtain other information from prescribed textbooks and other sources

It is important to learn all key concepts and understand them so that you can be able to answer any question asked correctly.

We wish you success in your endeavours to pass your NSC Examination in 2020

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TOPIC 6: PERFECT MARKETS

MAIN TOPIC: MICROECONOMICS	
TOPIC 6: PERFECT MARKETS	CONTENT DETAILS FOR TEACHING, LEARNING AND ASSESSMENT PURPOSES
Examine the dynamics of perfect markets with the aid of cost and revenue curves	<div style="border: 1px solid black; padding: 5px;"> NOTE: 1. Review cost and revenue tables and curves done in Grade 11. 2. Distinguish between short and long term/run. </div>
6.1 Perfect competition	<ul style="list-style-type: none"> Briefly describe the concept Examine the characteristics of a perfect market.
6.2 Individual business and industry	<ul style="list-style-type: none"> Distinguish between individual businesses and the industry. Use graphs to explain the derivation of the demand curve for the individual business. Construct a revenue table to show that $D = P = AR = MR$ Use graphs to explain profit maximisation using: <ul style="list-style-type: none"> Total cost and total revenue curves Marginal cost and marginal revenue curves Derive the supply curve from cost curves <div style="border: 1px solid black; padding: 5px; margin-top: 10px;"> The examination of individual business and industry should be accompanied by an analysis of tables and graphs. </div>

(Taken from 2017 Grade 12 Examination Guidelines)

RECAP: COST AND REVENUE TABLES AND CURVES

(Recap in this context refers to revising work that was done in previous grade. The topic recapped is also examinable in the current grade)

Distinguish between short and long term/run

Production takes place in the short run and the long run

Short run

- Description:** The short run is the period of production where **only the variable factors of production** can change. *(Variable factors of production are those that do change with output, which means more are employed when production increases and less when production decreases. Examples include labour, energy, raw materials directly used in production)*
- In other words, the business is faced with at **least one of its production factors being fixed** (cannot be changed). The input that is most commonly fixed in the short – run is land or capital (machinery and equipment).
- If a business wants to produce more output, it can increase labour by hiring more workers (casual or part time labour can be employed within minutes). However, land

cannot be increased in the short run. Neither can capital. **WHY?** It takes time to find these factors and even longer to find the money to buy them.

- The time period is too short to permit the number of firms in the industry to change. It also differs from one business to the next

Long run

- **Description:** The long run is the period of production where **all factors can change**.
- The time is long enough for variable and fixed factors to change. It allows enough time for new firms to enter the industry and/or existing firms to exit.
- In the long run, the firm can increase labour, capital and land in order to increase output/production. A business has enough time over **the long run** to buy a larger factory, more vehicles, employ more skilled and unskilled workers and more or improved machinery.

TEST YOUR KNOWLEDGE

1.1 Give ONE term for each of the following descriptions. Write only the term next to the number.

1.1.1. The period of production where only the variable factors of production can change. (1)

1.1.2 The duration (period) during which at least one factor of production is fixed (1)

1.2 Various options are provided as possible answers to the following question. Choose the answer and write only the letter.

1.2.1 The term 'long run' refers to a period where ... factors of production can change.

A both variable and fixed

B only variable

C only fixed

D floating (2)

1.3 Briefly explain the term short run. (2)

1.4 Why is it only possible in the long run to vary all factors of production? (2)

NOTE: Make sure you understand the difference between short and long run as these will be used in the discussions on Perfect and imperfect markets.

1.1 COSTS

1.1.1 SHORT – RUN COSTS

a) TOTAL COSTS

Description: Total cost (TC) is the sum of fixed and variable costs.

Formula: Total cost = Fixed Cost + Variable Cost ($TC = FC + VC$)

Total costs will be different for each unit produced, because variable costs change with each unit produced. (*Refer to Mind The Gap Figure 6.2 Page 83*)

Variable Costs/ direct costs/prime costs

Description: Variable Costs (VC) are costs that change with the number of units produced. They increase as quantity increases. **HOW?** – When a bakery produces one cake, it will use two eggs, but when it produces 100 cakes, it will use 200 eggs.

Examples: payments for labour (wages), electricity, raw materials

(NOTE: Salaries are not regarded as an example of variable costs. Do not confuse with the commonly used term ‘wages and salaries’)

Fixed Costs/ indirect costs/Overheads

Description: Fixed costs (FC) are costs that do not change with output. They remain the same even when the number of units produced changes. The quantity produced in the short run will not influence fixed costs. Fixed costs remain constant in the short run. **HOW?** - If a businesswoman rents a factory to produce cool drink bottles, she will pay the same amount of rent whether she produces 100 bottles or 10 000 bottles a month.

Examples: rent, insurance premiums, depreciation

COST SCHEDULES

All the different costs to be discussed can be represented in a cost schedule/table.

Table 1: A cost schedule for producing good x

Quantity (Q)	Fixed Cost (FC)	Variable Cost (VC)	Total Costs (TC) = FC + VC
0	10	0	10
1	10	4	14
2	10	6	16
3	10	10	20
4	10	16	26
5	10	30	40
6	10	45	55

COST CURVES

The costs can also be presented using curves.

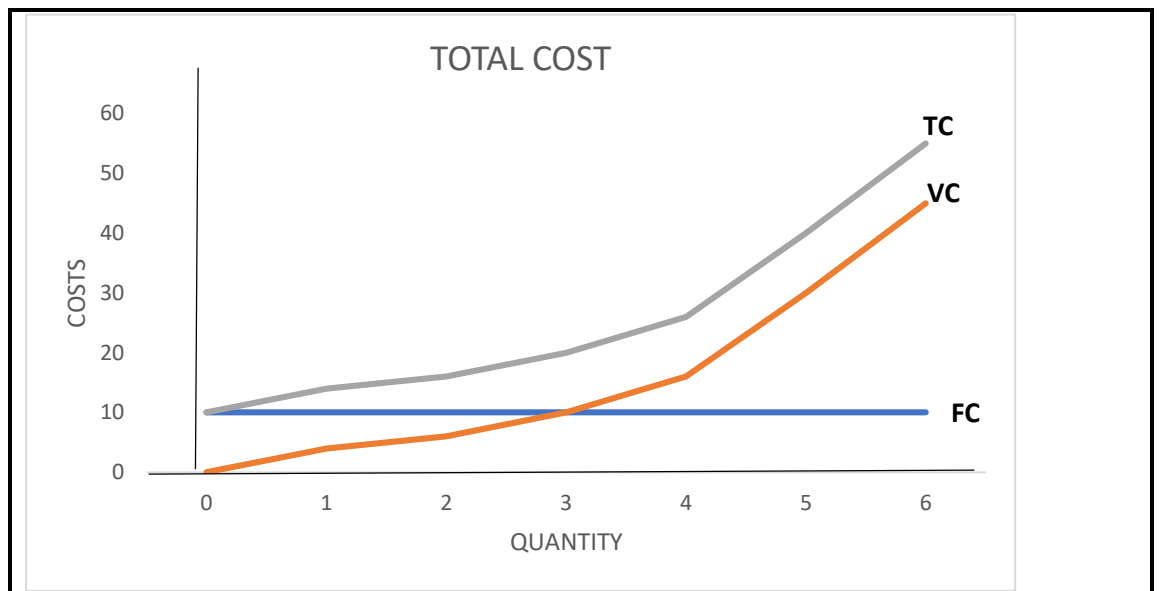


Figure 1

DESCRIPTION OF CURVES

The shape of the cost curves is very important.

Fixed cost curve (FC) – The fixed cost curve is a horizontal line, because fixed costs stay the same for all quantities. From Fig 1, the horizontal line is at 10. (Refer to Table 1)

Variable cost curve (VC) – The variable cost curve begins at 0 (there are no variable costs at zero units produced), slopes upwards from left to right and more sharply at the last quantities produced. This is because the costs increase slowly at low levels of output. However, as cost of, for example, electricity, rises faster, so is the VC curve. This also influences the shape of the TC curve.

Total cost curve (TC) – The total cost curve begins on the horizontal line of the fixed cost curve (FC) because at zero units, the only costs are the fixed costs. It then slopes upwards to the right. It has the same shape as the VC curve.

TEST YOUR KNOWLEDGE

1.1 Give one word/term for the following descriptions.

1.1.1 The costs that remain the same even if the output changes. (1)

1.1.2 Costs that change according to the changes in output (1)

1.2 Various options are given. Choose the correct option

1.2.1 An example of a fixed-cost item

A. electricity

B. rent

C. telephone

D. water

(2)

1.3 Give any TWO examples of variable costs. (2x1)

1.4 Give any TWO examples of fixed cost. (2x1)

b) AVERAGE COSTS (AC/ATC)

Description: Average costs are costs per unit of production.

Formula: Total cost divided by number of units ($AC = TC \div Q$)

This shows what it costs in total to produce each unit.

Average Fixed Cost (AFC) = $FC \div Q$

Average Variable Cost = $VC \div Q$

c) MARGINAL COSTS (MC)

Description: Marginal cost is the additional cost of producing one more unit of a product. Marginal cost is the amount by which total cost increases when one extra product is produced.

Formula: $MC = \Delta TC \div \Delta Q$ (Δ is read as 'change' which is the difference between two items)

The marginal cost is important because it shows whether a business must produce more or fewer units of a product. To do this marginal cost needs to be compared with marginal revenue. When marginal cost is less than the marginal revenue, the business will produce more units of a product. When marginal cost is more than the marginal revenue, the business will produce fewer units of a product. (See discussion on profits and losses)

TABLE 2

Quantity (Q)	Fixed Cost (FC)	Variable Cost (VC)	Total Costs (TC) = FC + VC	AFC = $FC \div Q$	AVC = $VC \div Q$	ATC = $TC \div Q$	MC = $\Delta TC \div \Delta Q$
0	10	0	10				
1	10	4	14	10	4	14	4
2	10	6	16	5	3	8	2
3	10	10	20	3,3	3,3	6,6	4
4	10	16	26	2,5	4	6,5	6
5	10	30	40	2	6	8	14
6	10	45	55	1,7	7,5	9,2	15

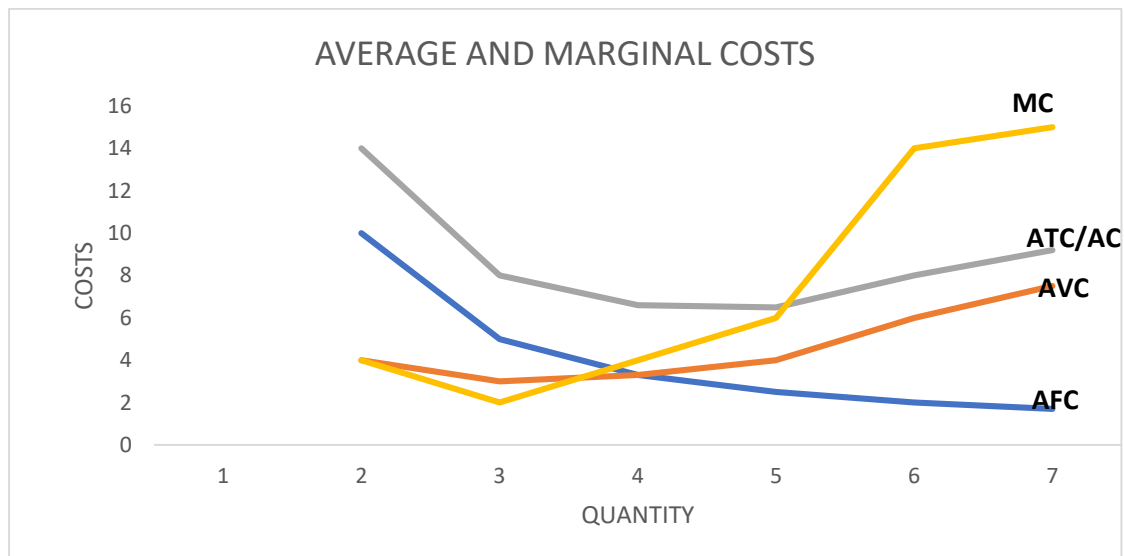


Figure 2

DESCRIPTION OF CURVES

AFC – slopes downwards from left to right. This is because its value decreases for each unit.

AVC – is roughly U – shaped. It first decreases and then increases.

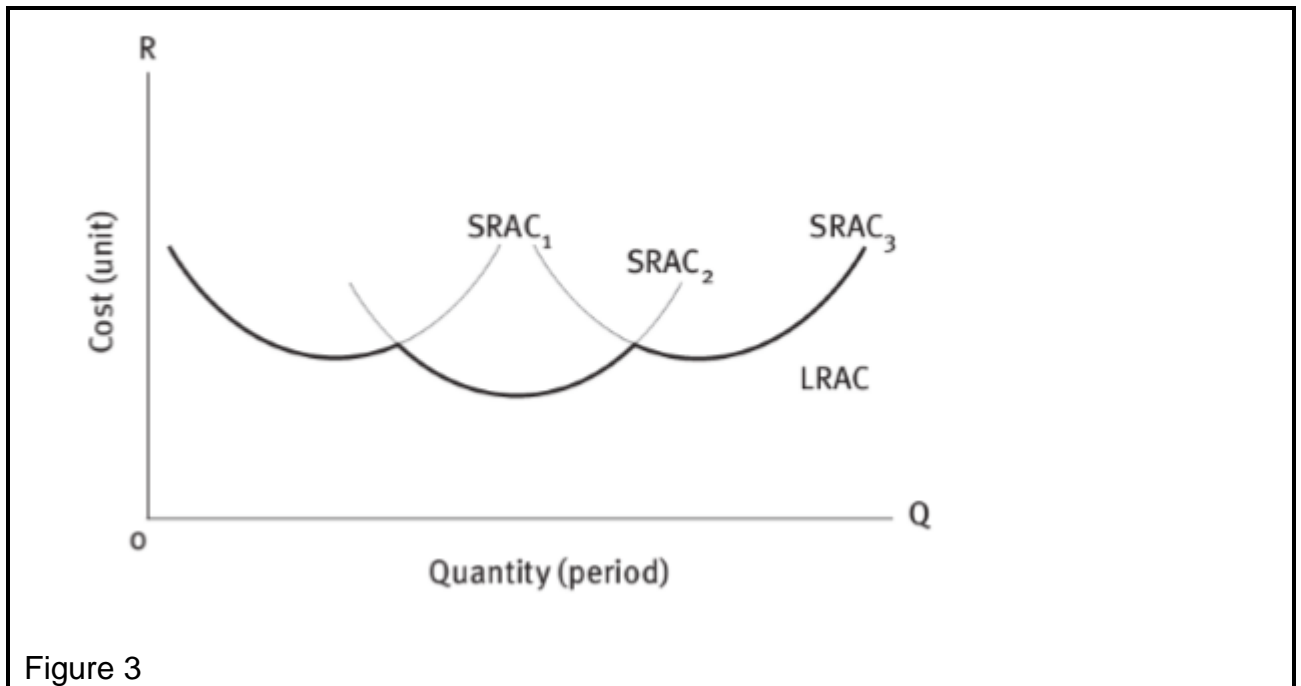
ATC/AC – the ATC has the same U – shape as the AVC curve. The ATC/AC will always be above the AVC curve because the ATC is the sum of the AFC and AVC.

MC – first slopes downwards sharply, then gradually slopes upwards because it is a change in total costs. The MC curve begins at the same place as the AVC curve.

LONG – RUN COSTS

(Briefly describe the term long run.....)

A long run cost curve is created by putting together all short run cost curves over the time period.



How do you differentiate between a short run and long run curves?

- Long run cost curves are **'flatter'** than short run cost curves.
- Example, the shape of the short – run Average Cost curve (SRAC) is U- shaped (or shaped like a smile), as shown in Figure 3, now compare the U – shape (or the smile) of the LRAC and that of the SRAC. Do you notice that LRAC is flatter (a more open smile) than SRAC?(the Long run MC will be a flatter J, long run AR will be 'flatter' or more inelastic)
- Secondly, differentiation is done by **labelling** the curves short or long run. Refer to Figure 3, there is SRAC, which stands for **Short – Run Average Cost** and LRAC, **Long Run Average Cost**

1.2 SUMMARY OF REVENUE CURVES AND CALCULATIONS

FOR PERFECT MARKET

a) TOTAL REVENUE (TR)

Description - Total revenue is the total income received from the sale of goods or services

Formula – Total revenue (TR) = Price (P) x Quantity (Q)

The more units a business sells, the more total revenue it earns.

b) AVERAGE REVENUE (AR)

Description - Average revenue refers to the amount a firm earns for every unit sold.

Formula – Average Revenue (AR) = Total revenue (TR) ÷ Quantity (Q)

For a perfect market, AR is equal to price because every unit is sold at the same price.

(See discussion under Characteristics of a Perfect Market).

c) MARGINAL REVENUE (MR)

Description – Marginal revenue is the additional income received from selling one more unit of a product. It is the difference between two consequent (one following the other) total revenues.

Formula - $MR = \Delta TR \div \Delta Q$ (read as change in total revenue divided by change in quantity)

TABLE 3

Price (P)	Quantity (Q)	Total Revenue (TR) - $P \times Q$	Average Revenue (AR) $TR \div Q$	Marginal Revenue (MR) $\Delta TR \div \Delta Q$
25	1	25	25	25
25	2	50	25	25
25	3	75	25	25
25	4	100	25	25
25	5	125	25	25
25	6	150	25	25

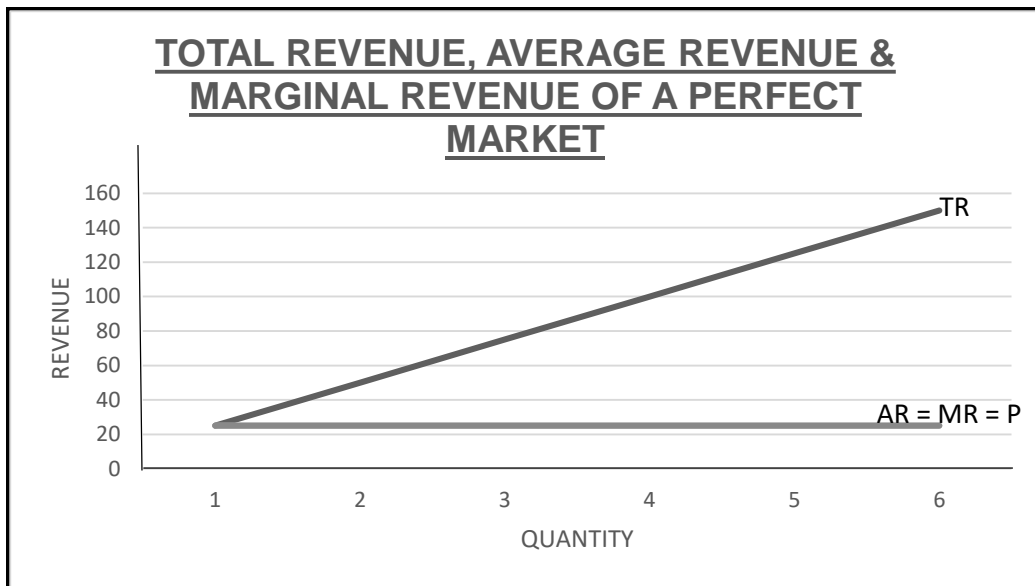


Figure 4

TAKE NOTE

- The TR curve for a perfect market slopes upwards from left to right as more units are sold.
- The AR curve for a perfect market is a horizontal line at the Price ($P = 25$)
- The MR curve for a perfect market equals the AR curve and therefore a horizontal line at the Price ($P = 25$)

FOR IMPERFECT MARKETS

We use the same formulas to calculate TR, AR and MR for perfect and imperfect markets. Changes are in the values used, that is for imperfect markets, there are different prices. This will be discussed further in IMPERFECT MARKETS. Also the revenue curves of the imperfect market are different from those of perfect markets.

REVENUE FOR THE IMPERFECT MARKET

Quantity (Q)	Price (P)	Total Revenue TR	Average Revenue (AR)	Marginal Revenue (MR)
1	12	12	12	12
2	8	16	8	4
3	6	18	6	2
4	4.5	18	4.5	0
5	3	15	3	-3

Table 4

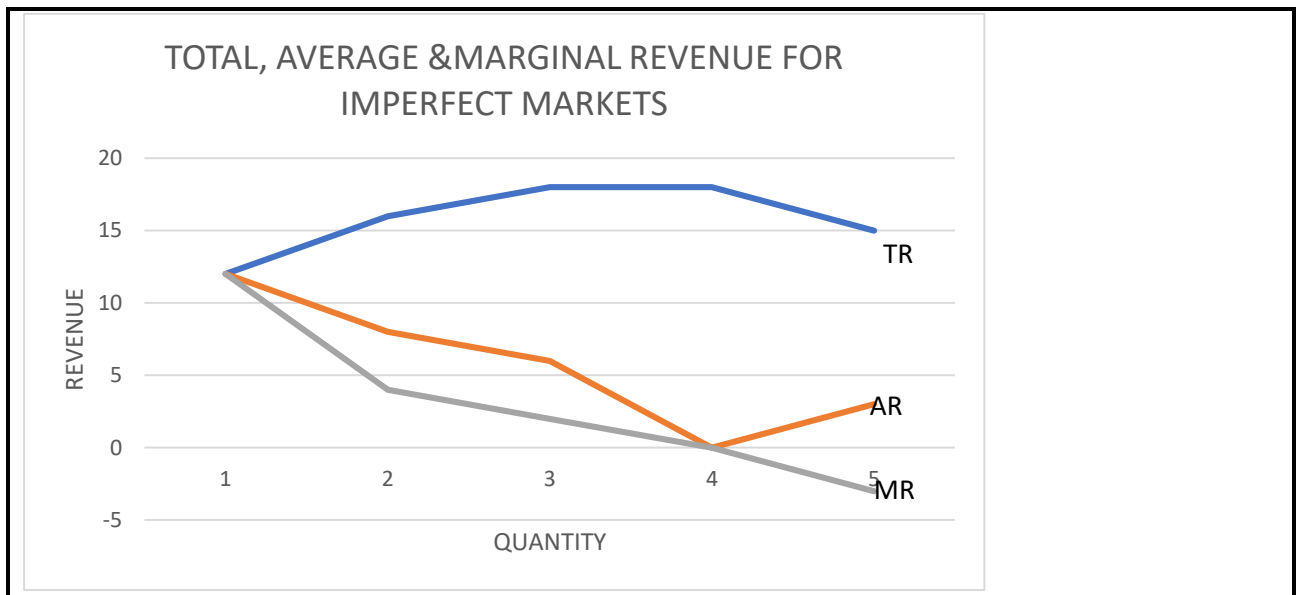


Figure 5

TAKE NOTE:

- The shape of the TR curve for an imperfect market first increases then decrease. It has an arch shape (like an upside- down U) This is due to the law of demand. (*What does the Law of Demand state?*).
- The AR curve of the imperfect market slopes downwards from left to right. This is because of the inverse (when Q increases AR decreases) relationship between quantity and AR
- The MR curve of the imperfect market begins at the same level as the AR. It also slopes downwards from left to right like the AR but it is **ALWAYS BELOW THE AR CURVE**.
- There is always a **relationship** between the MR and TR curve. As long as the **MR increases or positive, TR is also increases**. When **MR = 0** (MR intersects horizontal axis) **TR curve will be on maximum**. When **MR curve is negative, TR curve declines**.

TEST YOUR KNOWLEDGE

1.1 Various options are given as correct answers. Choose the correct answer.

1.1.1 The average revenue of a firm in a perfectly competitive market is equal to its ...

- A selling price.
- B total cost.
- C marginal cost.
- D economic profit. (2)

1.1.2 Unit cost is also known as ... cost.

- A marginal
- B total
- C average
- D variable (2)

1.1.3 In any market the average revenue is the same as the

- A price.
- B marginal revenue.
- C supply.
- D profit (2)

1.1.4 The difference between total cost and variable cost is ... cost.

- A average
- B marginal
- C fixed
- D unit (2)

1.2 Give one word/term for the following descriptions.

1.2.1 The amount by which the total cost increases when an extra unit is produced

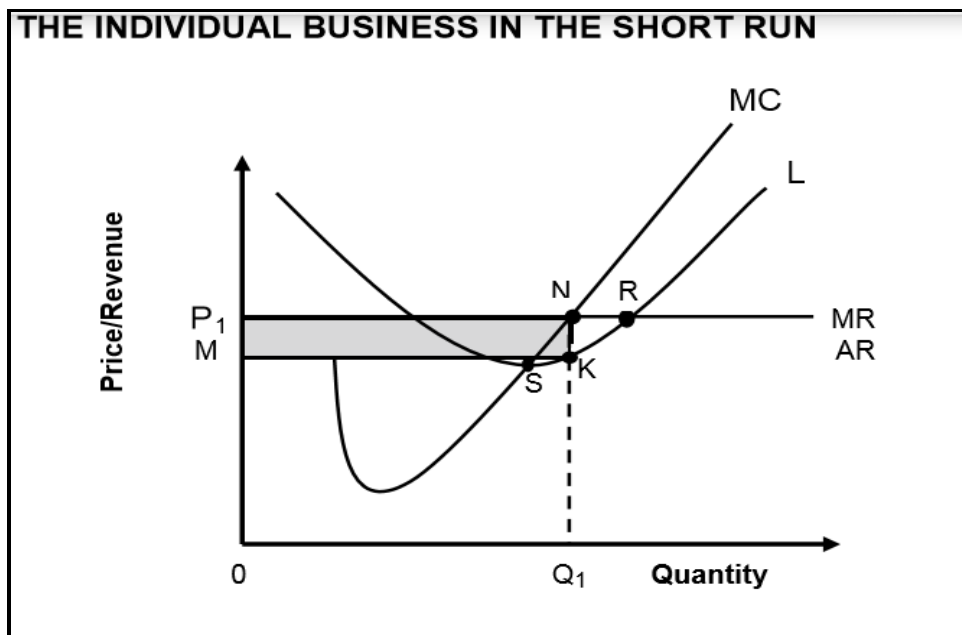
1.2.2 The additional cost incurred when production increases by one more unit

1.2.3 The additional revenue earned when sales increase by one more unit

1.2.4 Total income received from the sale of goods and services (4x1)

2.1 Study the following graphs and answer questions that follow:

Graph 1

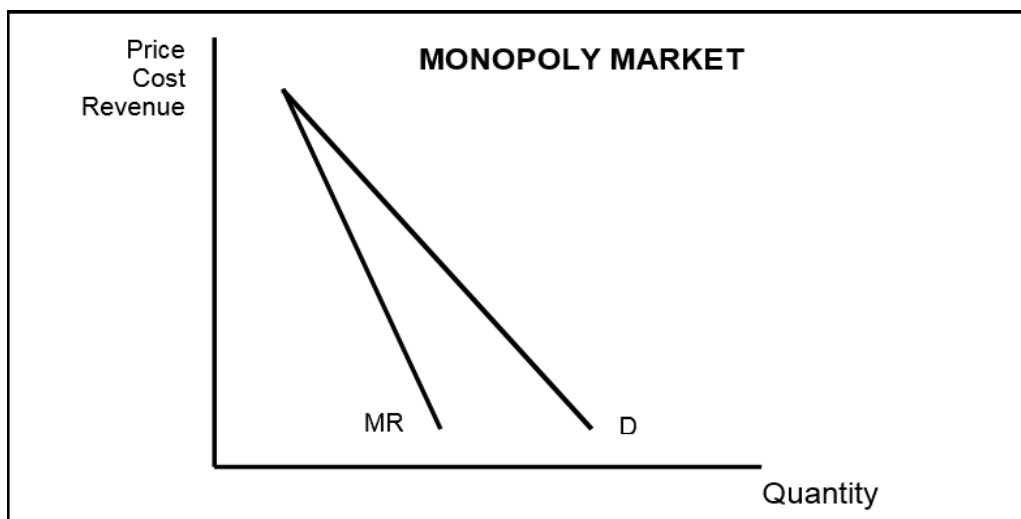


2.1.1 Name the curve labelled L. (1)

2.1.2 Briefly explain the term short run. (2)

2.2 Study the following graphs and answer questions that follow:

Graph 2



2.2.1 Which curve represents the average revenue (AR) curve? (1)

2.2.2 Why does the marginal revenue (MR) curve lie below the demand curve? (2)

2.2.3 Briefly describe the term marginal cost. (2)

2.3 Study the following table and answer questions that follow:

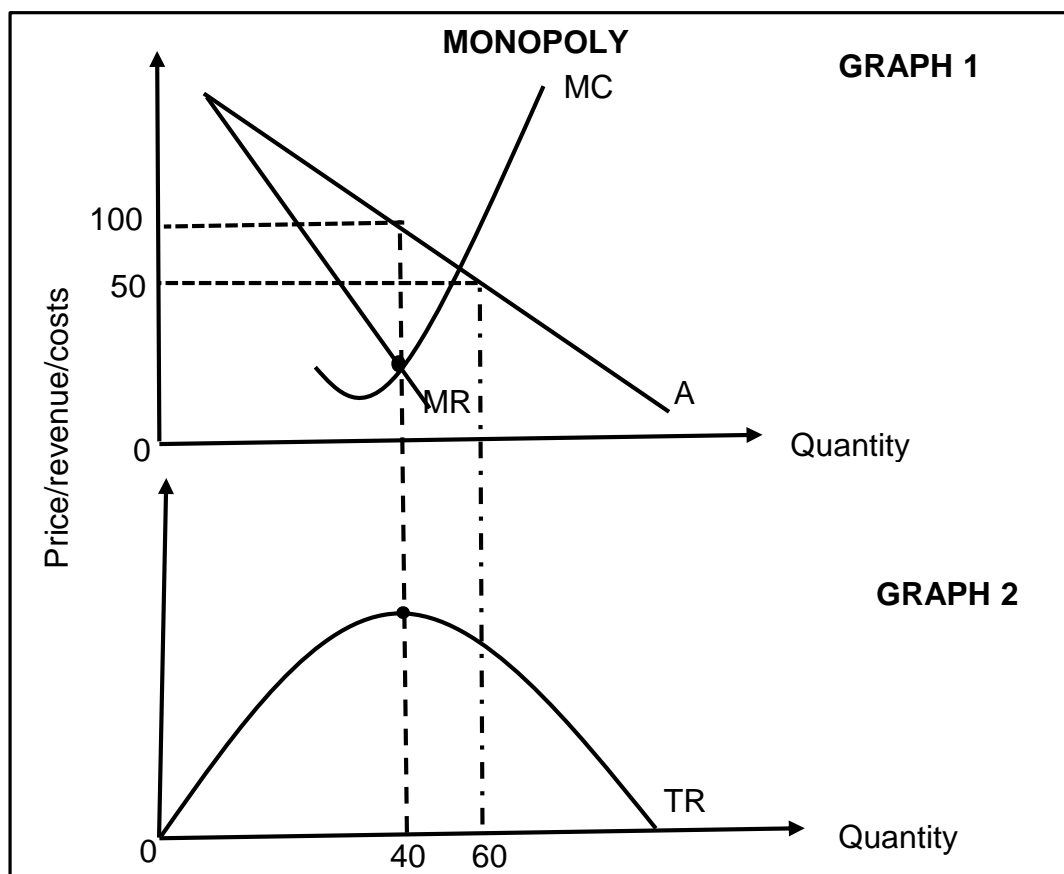
Table 5

COSTS AND REVENUES							
UNITS	PRICE	TR	AR	TC	MC	AC	PROFIT
0	16	0	16	10	-	-	-10
1	14	14	14	12	2	12	2
2	A	24	12	13	1	6,5	11
3	10	30	10	17	4	5,66	13
4	8	B	8	22	5	5,5	10
5	6	30	6	30	8	6	0
6	4	24	4	39	9	D	E
7	2	14	2	49	10	7	-35

2.3.1 For which market structure are these costs and revenues? (1)

2.3.2 Calculate the values of A–E. Show all calculations. (5)

2.4 Study the following graphs and answer questions that follow:



Graph 3

2.4.1 Provide a suitable label for curve A. (1)

2.4.2 Explain a reason for the shape of the total revenue curve. (2)

2.5 Study the following table and answer questions that follow:

Table 6

COST AND REVENUE TABLE							
OUTPUT	PRICE	AR	MR	TR	AC	MC	TC
1	21	21	21	21	23	24	23
2	18	18	15	36	19	15	38
3	15	15	9	45	15	7	45
4	12	12	3	48	14	A	56
5	9	9	-3	45	15	19	75

2.5.1 What is the effect on total revenue when marginal revenue is positive? (2)

2.5.2 Briefly explain the term marginal revenue. (2)

2.5.3 Calculate the value of A. Show all calculations. (4)

2.6.1 Why is the marginal revenue curve (MR) in the perfect market the same as the demand curve? 2019 (2)

2.6.2 What is the effect on a business if the average cost is more than the average revenue?

The business will suffer losses (economic losses) (2)

6.1 Perfect competition	<ul style="list-style-type: none">Briefly describe the conceptExamine the characteristics of a perfect market.
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(Extracted from 2017 Grade 12 Examination Guidelines)

6.1 PERFECT COMPETITION

(This is an essay type question. When answering the question, please note:)

- Structure of the essay, which is always given in the question paper, Section C.
- Introduction: as you will see, describing the market structures (perfect and imperfect) involves the characteristics. When you answer in an essay, WRITE**

ONLY ONE OR TWO CHARACTERISTICS IN YOUR INTRODUCTION, to avoid repetition and losing marks in the main part of the essay.

Description: A perfect market is a market where no single buyer or seller has a noticeable influence on the price of a good

Characteristics

(It is important to list and explain the characteristics)

Products are homogenous (i.e. identical)

- All products are identical in all aspects. There are no differences in style, design and quality. (there are no brand names, for example if one is buying tea, there is no Joko, Five Roses etc. Tea is just tea. Also design is identical, there are no square- shaped, round – shaped tea bags.)
- It makes no difference where and from whom which a product is bought. It is also easy for any firm to replicate the product.
- In this way products compete solely on the basis of price and can be purchased anywhere.

There is a large number of buyers and sellers

- The market is so large (many buyers and sellers) that an individual buyer or seller cannot influence the market price.
- Sellers are **price - takers**, they accept the prevailing market price (market price is price determined by forces of supply and demand – market forces). If they increase prices above the market price, they will lose customers (Law of demand applies). (Also if they lower prices below the market price, they will lose on profits, i.e they will not get the same profit they would be getting if they were selling at the market price)

No preferential treatment/discrimination

- The market is impartial and impersonal - nobody has an advantage over others. (buyers do not have any personal reasons for buying from certain sellers – they do not mind from whom they buy)
- In a perfect market no collusion takes place – buyers and sellers act independently from one another. (Collusion occurs when buyers and sellers make an agreement to limit competition)

- Buyers and sellers base their actions solely on price, homogenous products fetch the same price and therefore no preference is shown for buying from or selling to any particular person.

Complete freedom of entry and exit

- The market is totally accessible – there is complete freedom for businesses to enter into and exit from the market.
- Buyers are free to buy whatever they want from any firm and in any quantity.
- Sellers are free to sell what, how much and where they wish.
- There are no legal, financial or technological barriers to entry and exit.

There is no State interference and no price control.

- Perfect market is an unregulated market. (the government does not intervene in how the market operate)
- Buyers do not form groups to obtain lower prices, nor should sellers combine to enforce higher prices (collusion does not exist)

Efficient transport and communication

- Efficient transport ensures that products are made available everywhere.
- Efficient communication keeps buyers and sellers informed about market conditions.
- This makes the access to the markets possible.

Buyers and sellers have full knowledge

- Both buyers and sellers have full knowledge of all current market conditions.
- Sellers have complete knowledge about production costs and market opportunities
- Buyers have complete knowledge about price, quality and the availability of goods and services

All factors of production are completely mobile

- Labour, capital and other factors of production can move freely from one market to another.

In the real world, an example of a 'pure perfect market' does not exist. Foreign exchange markets and stock exchanges are close examples. The agricultural and mining sectors almost meet the characteristics of perfect markets.

Therefore, the perfect market, is nevertheless, a good starting point for the analysis of how prices and production are determined in practice.

TEST YOUR KNOWLEDGE

Discuss in detail, without the use of graphs, the market structure of a perfect market. (30)

(Taken from Economics P2 SCE May – June 2018 Question Paper)

6.2 Individual business and industry

- Distinguish between individual businesses and the industry.
- Use graphs to explain the **derivation of the demand curve** for the individual business.
- Construct a revenue table to show that $D = P = AR = MR$
- Use graphs to explain **profit maximisation** using:
 - Total cost and total revenue curves
 - Marginal cost and marginal revenue curves
- Derive the supply curve from cost curves

The examination of individual business and industry should be accompanied by an analysis of tables and graphs.

(Extracted from 2017 Grade 12 Examination Guidelines)

6.2 INDIVIDUAL BUSINESS AND INDUSTRY

- **NOTE:** Microeconomics is a branch of economics that studies the behaviour of individuals and firms in making decisions regarding the allocation of scarce resources and the interactions among these individuals and firms. *(Source: Wikipedia)*

DESCRIPTION OF CONCEPTS

- **Individual business** – a single producer or supplier of a specific product such as milk or clothing. Another name used for an individual business is ‘*firm*’
- **Industry** – refers to a group of individual businesses that produce or sell the same product.
- **Examples:** let us look at the **cell phone industry**. Can you name the different producers of cell phones?

(Samsung, Huawei, Motorola etc.)

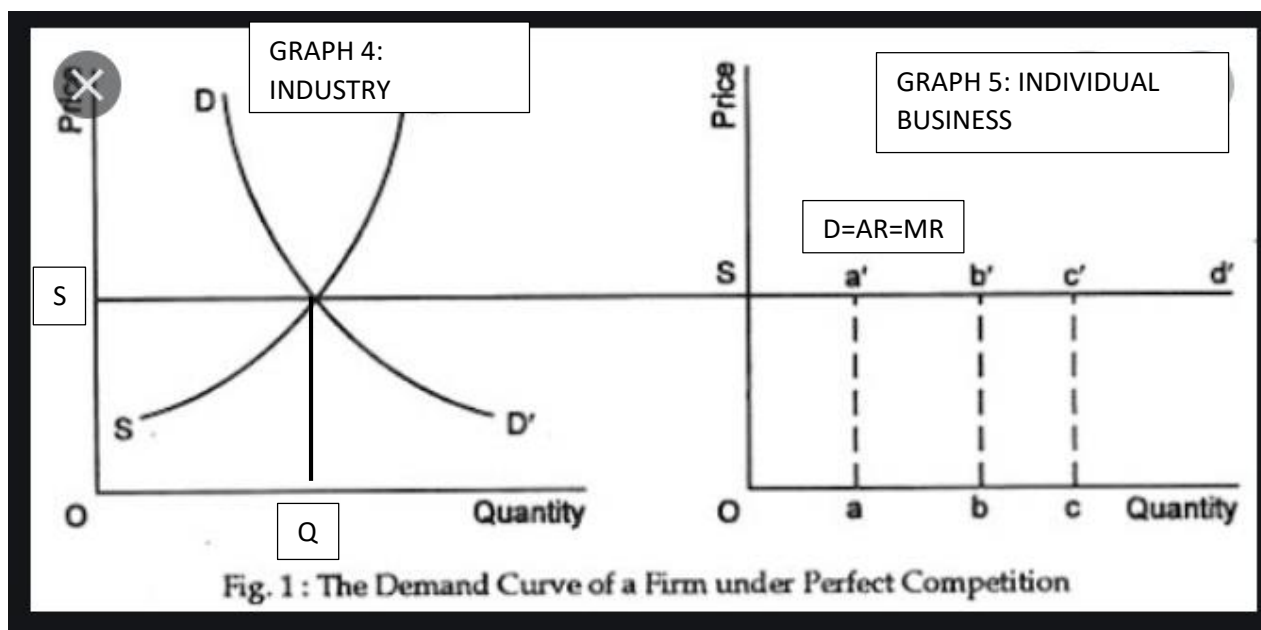
Now each producer or supplier represents an individual business. The cell phone industry is represented by all the manufacturers of the cell phones.

Another example: think of the different car names you saw as you were coming to school. (Toyota, Isuzu, Mercedes Benz, BMW etc.). Those can be regarded as individual firms which together represent the car industry.

- Remember that for a perfect market, products are homogenous (identical in every aspect)
- The individual businesses in the perfect market are price takers. (an individual business cannot influence the price but takes the price that has been set by market forces of supply and demand)
- For a perfect market the shapes of the demand curve of an individual business/firm and that of the industry are different.
- The demand curve of an individual business/ firm is a **horizontal line at the market price**.
- The demand curve of the industry has a **negative slope from top left to bottom right**. (the normal demand curve)

DERIVATION OF THE DEMAND CURVE FOR THE INDIVIDUAL BUSINESS

- In this section, we will look at how we arrive at the horizontal demand curve for the individual business, using graphs.
- As discussed earlier, prices are determined by market forces (demand and supply) in perfect competition and individual businesses are price takers.
- **The above is shown in the graphs below:**



(Source: adapted from economicsdiscussions.net)

EXPLANATION

- The individual business derives its price from the market price that has been determined by the market. (The single producer cannot influence the market price). This implies that a producer can sell any quantity of the good at the current market price.
- If the single producer increases the price it charges (charges more than the market price), the quantity it will sell will decrease to zero as consumers will rather buy the goods from another source who is charging the market price.
- The single producer, also will not decrease the price it charges (charging less than the market price) as it is able to sell any quantity it wishes at the current market price.
- The horizontal line in the **GRAPH 5** (Sd') represents the demand curve of the individual business. Note that it is exactly on the level of the market price S as determined in **GRAPH 4**.
- Recall, the cost and revenue curves discussed earlier.
- The AR and MR will also be equal to the market price. (**REFER TO TABLE 7 BELOW**)
- **Therefore, in perfect competition, the horizontal demand curve also represents the AR and MR curves.**
- **In summary: Demand of an individual business for a perfect market = perfectly elastic demand (horizontal) = market price = AR=MR**

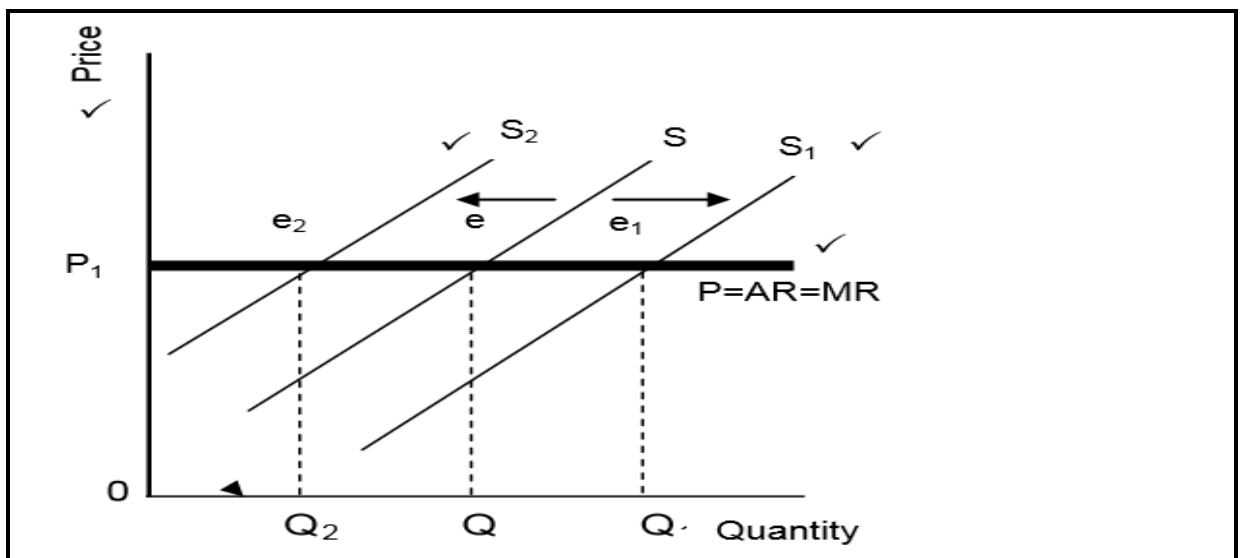
TABLE 7

Price (P)	Quantity (Q)	Total Revenue (TR) - $P \times Q$	Average Revenue (AR) $TR \div Q$	Marginal Revenue (MR) $\Delta TR \div \Delta Q$
25	1	25	25	25
25	2	50	25	25
25	3	75	25	25
25	4	100	25	25
25	5	125	25	25
25	6	150	25	25

Construct a revenue table to show that $D = P = AR = MR$

You can use the above table to draw the AR and MR curve when $P = 25$.

THE DEMAND CURVE FOR THE INDIVIDUAL BUSINESS AND CHANGES TO ITS SUPPLY.

Graph 6

- The above graph 6 is based on the assumption that P_1 is the market price and the market quantity is Q .
- If the individual producer increases its supply, the supply curve will shift to the right from SS to S_1S_1 .
- The new equilibrium is at E_1 , where $DD = S_1S_1$ (Remember $DD = P = AR = MR$)
- At the new equilibrium, the quantity has increased from Q to Q_1 , but equilibrium price has remained at P_1 (constant).

- When the individual producer decreases its supply (SS shifts to the left from SS to S2S2), equilibrium quantity has decreased but equilibrium price has remained constant.
- This explanation proves the fact that an individual producer is not able to influence the equilibrium market price by manipulating its supply.

TEST YOUR KNOWLEDGE

1. With the aid of graphs, explain the following about an individual business under conditions of perfect competition:

The effect on price if the individual producer increases or decreases his output
(supply) (14)

(Source: Economics Paper 2 February/March 2017 Question paper)

2. What will happen if one firm in the perfect market decides to increase its selling price? Nov 2014 (2)
3. Discuss, with the aid of graphs, the individual business in a perfect market under the following headings:
4. Derivation of the demand curve (10 marks) June 2019 EC
5. With the aid of graphs, briefly explain how price is determined for an individual producer in a perfect market. (8) (Economics P2 November 2018 QP)

PROFIT MAXIMISATION

**Use graphs to explain profit maximisation using: - Total cost and total revenue curves
- Marginal cost and marginal revenue curves**

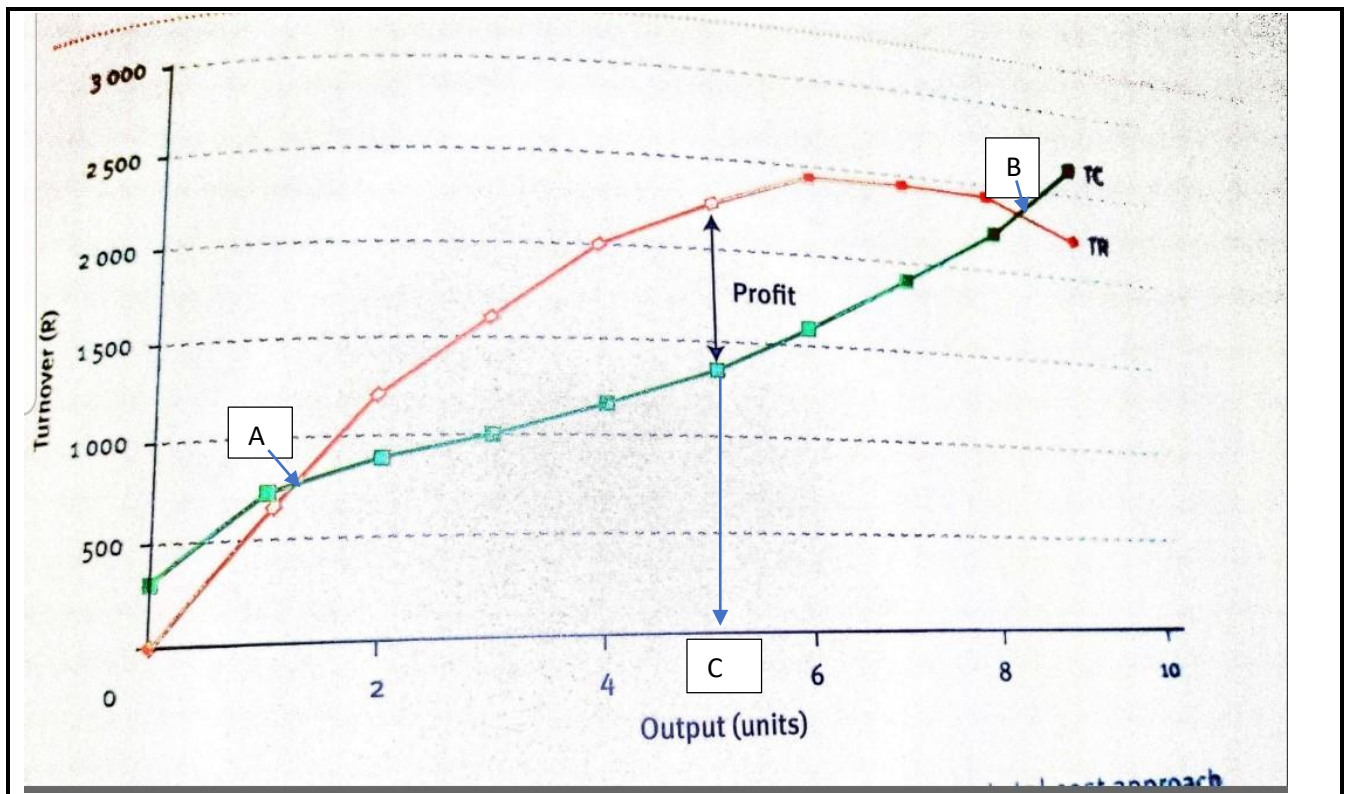
Introduction

- Firms are in business to maximise profits.
- An individual business in the perfect competition market wants to maximise its profit (make the largest profit possible, *ceteris paribus*), but cannot influence price.
- It can, however, sell any quantity of products at the prevailing market price.
- A business can only maximise its profits by choosing the quantity it wants to sell
- We say all businesses want to find their **optimal** output. (Optimal in this context means the best that can ensure the highest profit.)
- **Profit is the positive difference between revenue and cost.**

- We can determine the optimal output of an individual business by its total revenue (TR) and total cost (TC) curve OR by its marginal revenue (MR) and marginal cost (MC) curve.

Profit maximising: Total revenue and total cost

Graph 7



(Photo adapted from Via Afrika Economics Grade 12 Learner's book)

EXPLANATION

- In Graph 7 above, TR starts at the origin. This means that TR is zero when no units of output are produced.
- TR increases with a positive slope as output produced also increases.
- TC starts at R250. This is the level of fixed costs as they have to be paid even if no output is produced. (Remember: Because of this, the TC curve will never start at the origin)
- The two curves intersect at A and B. Both at these points, $TR = TC$. (You should be able to determine the level of output where this happens). Point A and B are known as

break -even points. At both points the business is said to be making **normal profit (to be discussed later)**

- Between points A and B, the TR curve is above TC curve, indicating profit made.
- We have to determine where the largest profits are made, that is where profits are maximised.
- **Conclusion:** A business will maximise its profits when it produces at the output level where Total Revenue exceeds Total Cost by the largest amount possible.
- **This is the profit maximisation rule.**
- The business maximises its profits when it produces output C (The optimum output level is achieved at C where it is the output produced when the distance between TR and TC is at its highest). (You will need to be able to identify these in Data response questions)

Profit maximisation: Marginal revenue and marginal costs

Graph from Fast track, explanation from Clever economics

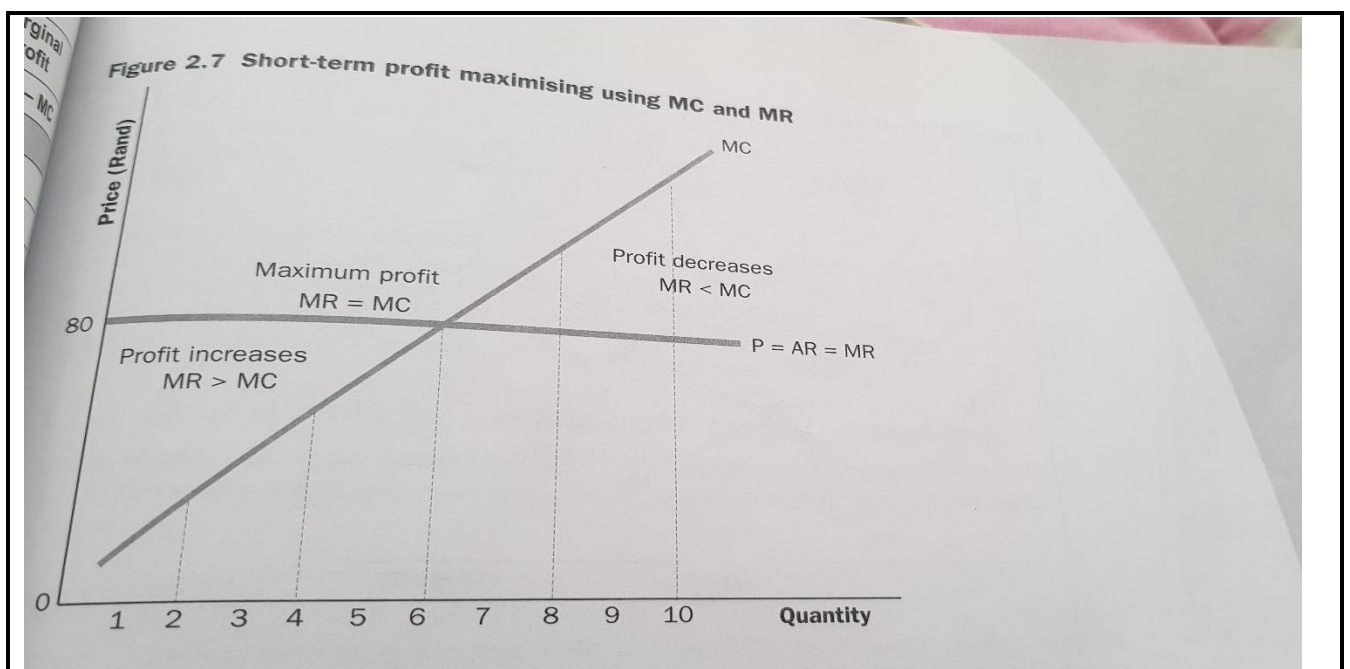


Figure 2.7 (Photo taken from Fast Track Economics Grade 12 Learner's Book)

- The second approach to determine where profits are maximised and identify optimal output level is to compare the marginal revenue and marginal costs for each unit produced.
- Let us remember that, for each unit sold, $\text{marginal profit} = \text{MR} - \text{MC}$.

- If $MR > MC$, marginal profit is positive (increases). The business will expand its output. This is because the added benefit of producing that extra unit is more than the added cost of producing it. (Go back to descriptions of Marginal Revenue and Marginal Cost)
- If $MR < MC$, then marginal profit is negative (decreases). The business will reduce its output. This is because the added benefit of producing that extra unit is less than the cost of producing it.
- If $MR = MC$, marginal profit is zero. Total profits are maximised. The business will continue to produce at this level
- A business will therefore maximise its profits when it produces at the output level where **$MR = MC$ (profit maximising rule)**

TEST YOUR KNOWLEDGE

With the aid of a graph, explain why marginal cost should be equal to marginal revenue to maximise profits. June 2019 EC (8)

Discuss perfect competition under the following headings:

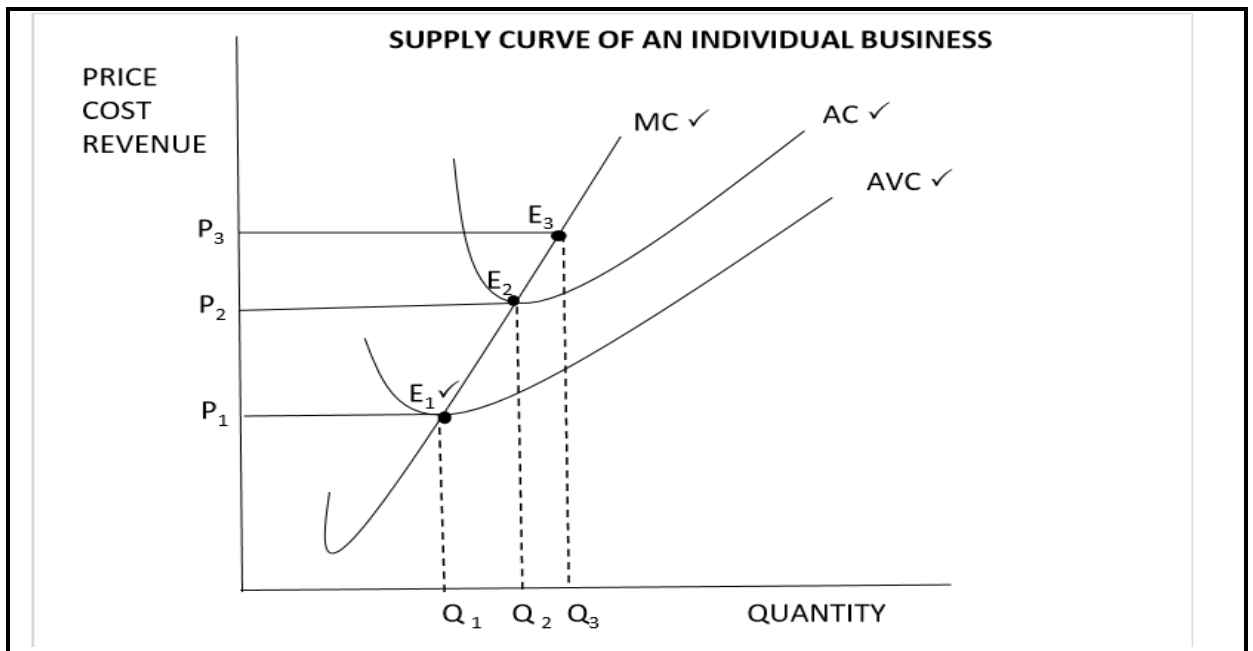
→ A comparison of the demand curve of the individual producer and industry

→ Profit maximisation (30) November 2014

Use graphs to support your discussion

DERIVING THE FIRM'S SUPPLY CURVE FROM COST CURVES

- Refer to previous discussion on Cost curves and their shapes.
- The firm's (individual business's) supply curve is determined by its MC curve and AVC curve.
- Refer to the graph below: **(You must be able to draw and explain the graph. In drawing the curves take note of shape and positioning of each curve)**



Graph 8

- The individual business's supply curve is the upward – sloping portion of its MC curve above the AVC intersection. Remember the MC intersects the AVC at its lowest point.
- This starts from point E1 (shutdown point) and moves upwards (E2; E3.)
- The firm will only produce when the price lies above the minimum point on the AVC. (a business will close its doors if it cannot cover its variable costs)

6.3 MARKET STRUCTURE

Description: Market structure refers to characteristics/features of the market which includes how the market is organised, the number of buyers and sellers and the nature of costs and revenue generated and the way buyers and sellers interact.

Four broad types of market structures (perfect competition, monopolistic competition, oligopoly and monopoly) are prescribed for Grade 12 learners.

Characteristics

It is crucial that learners should understand the characteristics of each market structures since these features make each different from another.

As you cover each type of market structure learners are expected to compare and contrast perfect competition, monopolistic competition, oligopoly and monopoly in detail in terms of the following.

- Number of businesses

- Nature of product
- Entrance
- Control over prices
- Information
- Examples
- Demand curve
- Economic profit/loss
- Decision-making
- Collusion
- Productive/Technical efficiency
- Allocative efficiency

A comparative analysis of the four market structures according to the afore-mentioned aspects should be made at the end the four market structures.

6.4 OUTPUT, PROFITS, LOSSES AND SUPPLY

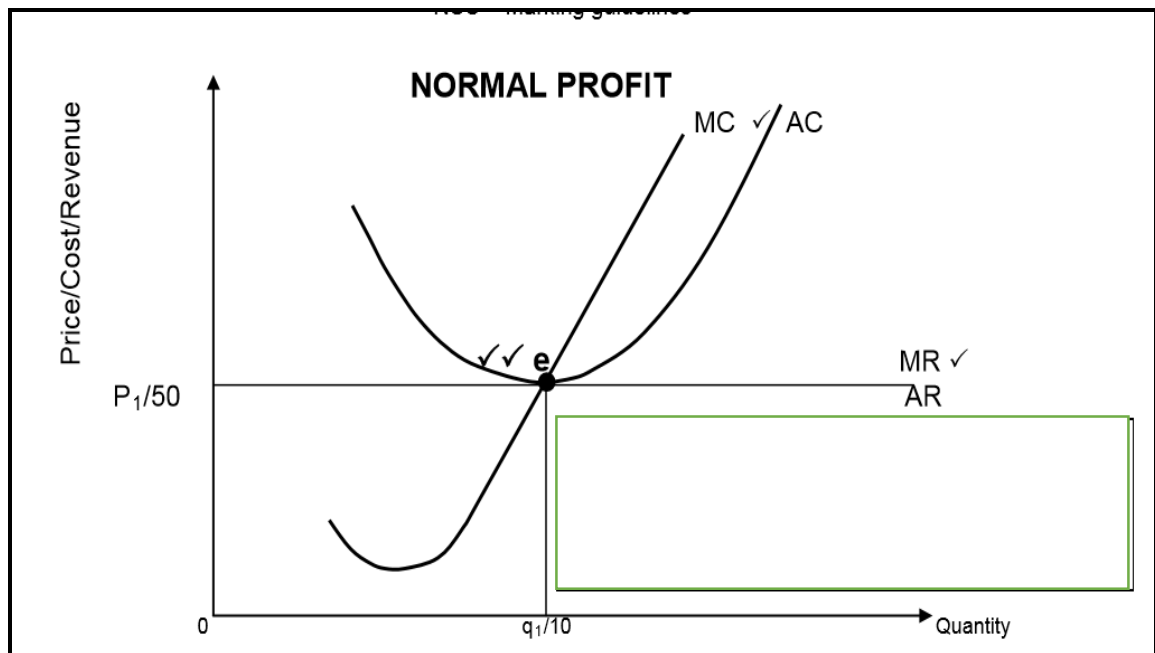
INDIVIDUAL BUSINESS AND INDUSTRY

Examine in detail the various equilibrium positions with the aid of graphs

Explain economic profit, economic loss, normal profit with the aid of graphs (short run)

Normal profit of an individual businesses

Graph 9(a)



(The ticks are a guide into what is important when you are required explain normal profit with the aid of a graph. Maximum mark for a graph is usually 4 marks and maximum of 4 marks for the explanation)

- **Description of concept:** Normal profit is the minimum earnings required to prevent the entrepreneur from leaving and applying his or her factors of production elsewhere.
- A business makes normal profit when its revenue equals its explicit and implicit costs.
- **Explicit costs** refer to the actual expenditure of a business such as purchases of raw materials, wages and interest paid.
- **Implicit costs** refer to value of inputs owned by entrepreneur and used in the production process. These include an acceptable compensation for the entrepreneur and the opportunity cost of the factors of production.
- **Refer to Graph 9(a): Explanation**
 - ✓ The demand curve is the horizontal line $P_1 = AR = MR$
 - ✓ The business will produce at the output level where $MR = MC$ (**Profit maximisation rule**). Point e is where $MR = MC$ and quantity produced is $q_1/10$
 - ✓ Profit or loss in a business is determined by the position of the lowest point of its ATC/AC curve. The lowest point of $AC = P$ (market price) = AR

✓ If $AC = AR$, then $TC = TR$.

✓ **Calculation of normal profit:** Remember that $AC=AR$ and total cost is equal to total revenue (Normal profit is represented by OP_1eq_1 and is equal to 500)

$$TR = P \times Q; TC = P \times Q$$

Now substitute with the figures from the graph

$$\text{Therefore: } TR = (50 \times 10) = 500$$

$$TC = (50 \times 10) = 500$$

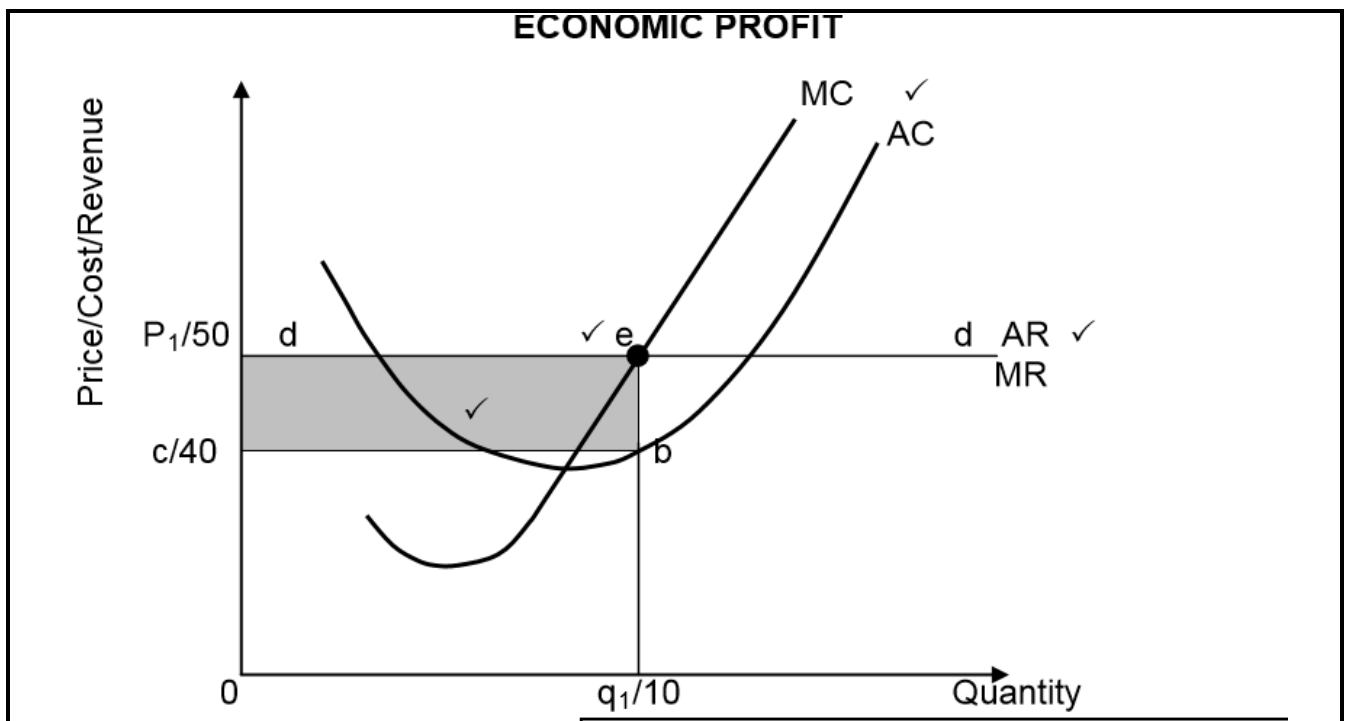
✓ **Conclusion:** A business makes normal profit when the lowest point of its $AC =$ to the market price/ AR .

✓ This is also the business's long run equilibrium (All businesses under perfect competition make normal profit in the long run)

✓ Normal profit is also known as the break – even point, because Revenue = Costs

- **Economic profit of an individual businesses**

Graph 9(b)



- **Description of concept:** Economic profit is profit that a business makes that is more than the normal profit.

- A business makes economic profit when its revenue is more than all of its costs.
- Economic profits are also known as surplus, extra, excess, supernormal profits
- Economic profits do not last long under perfect competition. This is because these high profits will attract more businesses into the same industry/market and output/ supply will increase. (this will be discussed later under long term equilibrium)

Refer to Graph 9(b): Explanation

- ✓ The demand curve is the horizontal line $P_1 = d = AR = MR$.
- ✓ The business is in equilibrium (it is maximising profits) at point e where $MR = MC$ and the business will produce at quantity q_1 and market price P_1
- ✓ The lowest/ minimum point of the AC curve lies below the market price.
- ✓ This means that the AR is more than AC. It also implies that TR will be more than TC.

- ✓ **Calculation:** • Profit = TR – TC

Total revenue = $Q_1 \times P_1 = (50 \times 10)$ (the price corresponds with AR curves)

Total cost = $Q_1 \times C_1 = (40 \times 10)$ (the price corresponds with the AC curve)

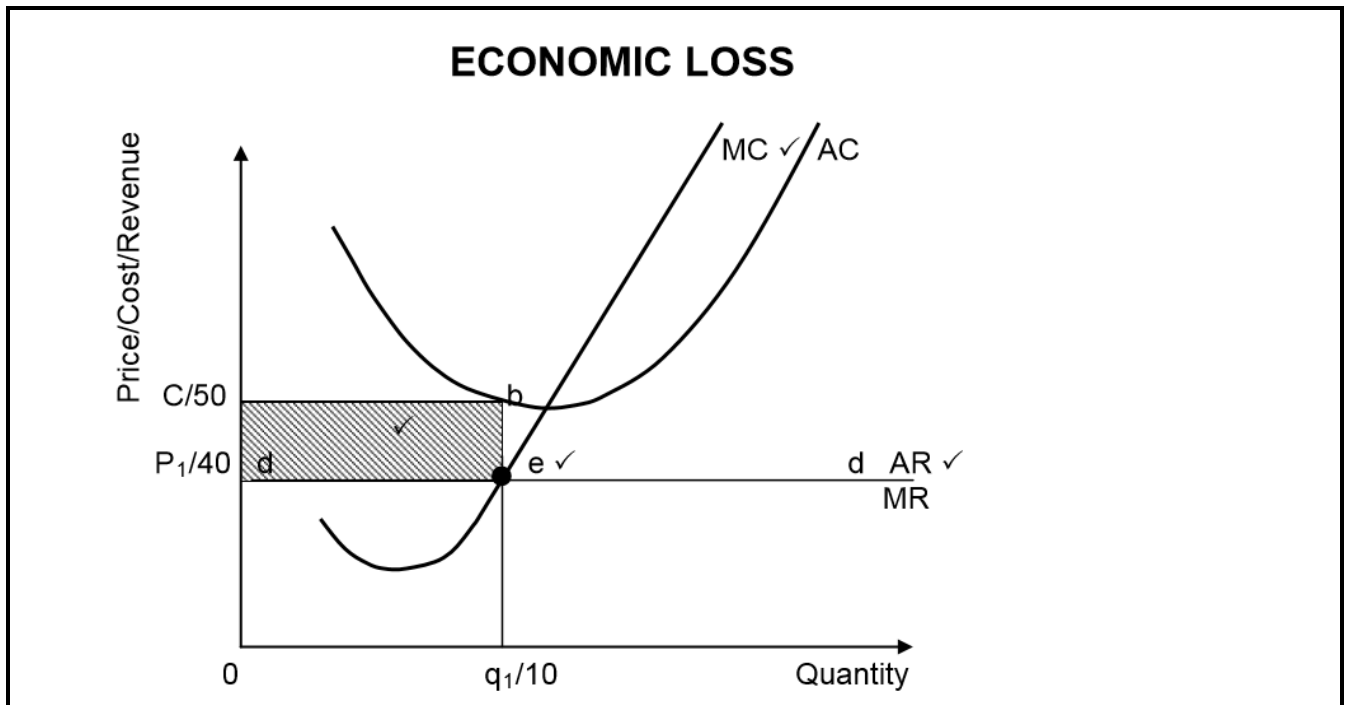
TR – TC

$R500 - R400 = R100$ which is the economic profit.

The economic profit is represented by the area cP_1eb - the shaded area. (You must ALWAYS show this area either by shading or labelling it when required to draw the graph. Also ensure that you first draw the AC curve before the MC curve. The MC must always cut the AC curve at its lowest point)

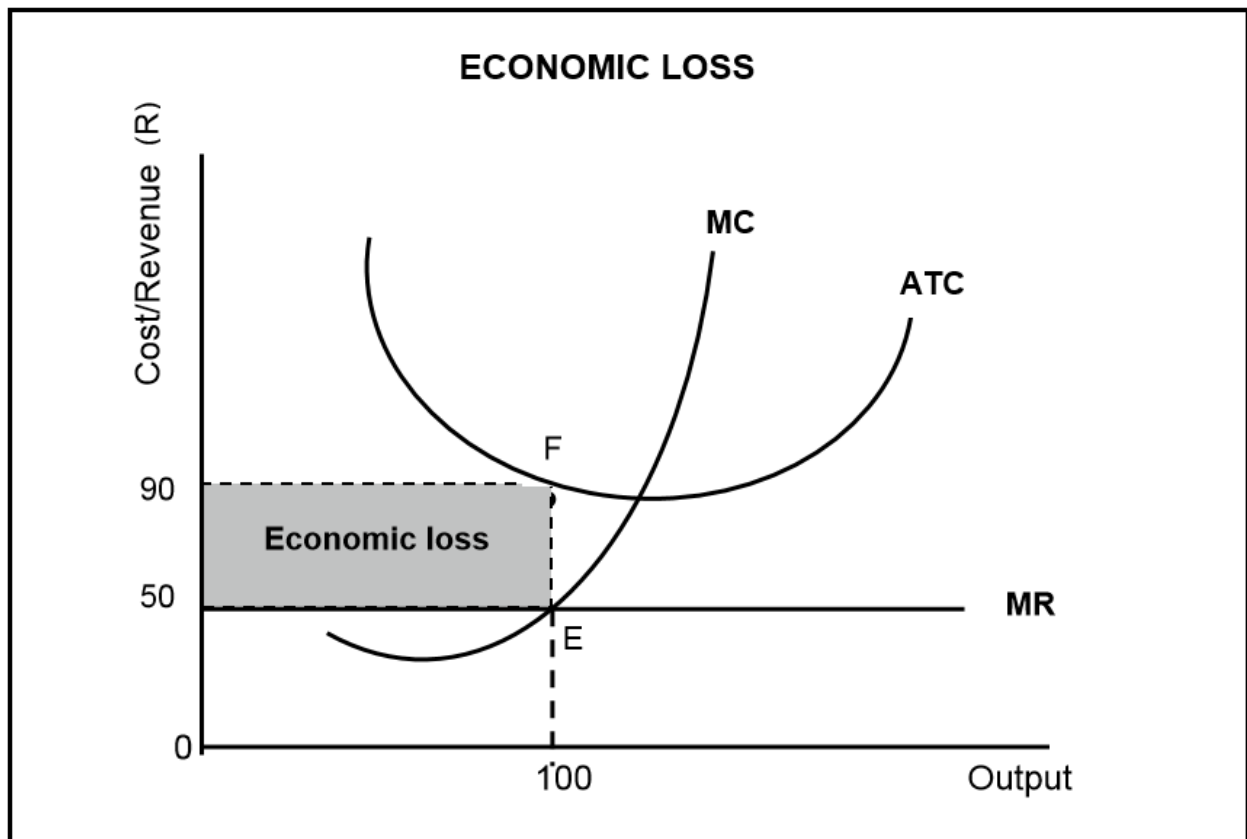
- Economic loss of an individual businesses

Graph 9(c)



- A business makes an economic loss when its revenue is less than its costs.
- It is usually when it is making less than normal profit.
- The minimum point of the short-term average cost curve (AC) is higher than the market price
- The business is in equilibrium (it is maximising profits) at point e where $MR=MC$ and the business will produce at quantity Q_1 and market price P_1
- **Calculation:** Total revenue = $Q_1 \times P_1$ (40×10) = 400
 total cost = $Q_1 \times C$ (50×10) = 500
 The economic loss is represented by the area P_1cbe = 100. (You can also put a minus sign next to the answer to show the economic loss).

TEST YOUR KNOWLEDGE



Graph 10

- 1.1 Identify the market structure in the graph above. (1)
- 1.2 Give the value of the market price depicted above. (1)
- 1.3 How will this equilibrium position change in the long run (long term)? (2)
- 1.4 What conditions must exist for this firm to shut down? (2)
- 1.5 Calculate the economic loss faced by this firm. (4)

Source: Economics P2 November 2016 QP

LONG RUN EQUILIBRIUM IN A PERFECT MARKET

- In this sub section, we will discuss how firms make normal profits in the long run.
- Under perfect competition, individual businesses can only make normal profit in the long run. (Can you describe what is long run?)

- The economic profit and economic loss are short run positions under perfect competition.
- **WHY?** The following changes can occur in the long run:
 - ✓ New businesses can enter the industry and existing firms can exit the industry.
 - ✓ All factors of production can become variable and businesses can expand or reduce their output.
 - ✓ Businesses can move from making short – run economic profit or an economic loss to making only **long - run normal profit**. This is illustrated in the graph below.

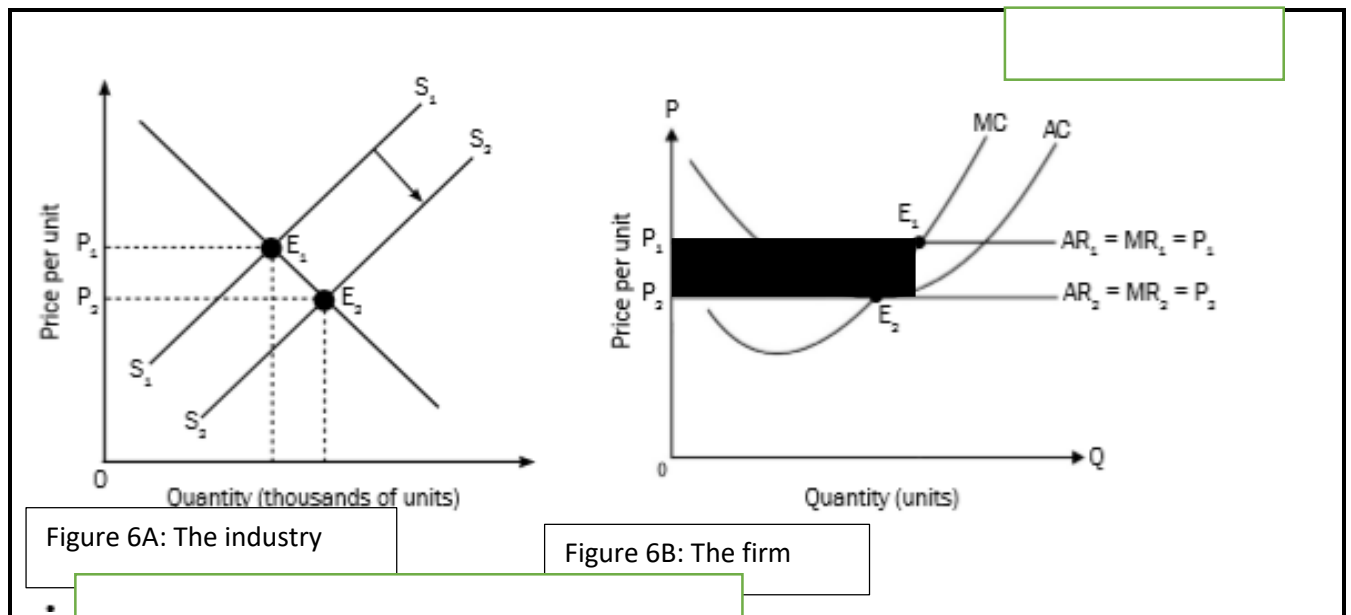


Figure 6 A & Figure 6B – Adapted from 2nd Mind The Gap Economics

EXPLANATION

- In the graph above (Figure 6B), the minimum point of AC curve lies below the market price P_1 . The firm is making an economic profit indicated by the shaded area ($P_1E_1E_2P_2$)
- Refer to Figure 6A (the industry), high profits (economic profit made by the firm), attract more businesses into the industry. This results in an increase in supply.
- The increase in supply is shown by the shifting of the industry supply curve to the right from S_1S_1 to S_2S_2 . This causes the market price to decrease from P_1 to P_2 .

- Since an individual business is a price taker, it has to take this lower market price P2. A new demand curve for the firm will be formed at P2 ($P2 = AR2 = MR2$)
- If the business does an accurate cost estimate, it will recognise that, if it expands, it will be able to produce at a lower cost in the long term. This is illustrated by the downward sloping portion of the AC curve.
- The prospect of increased profit would therefore encourage the business to build a bigger plant. The unit costs in the long run will then decrease as the business begins to enjoy economies of scale.
- Economies of scale occur when the cost per unit decreases when output expands. This implies that when a business produces more units, the cost of additional units will be cheaper than previous units.
- The long run equilibrium will be reached at E2. This is at the price that corresponds to the lowest point of the AC curve after an increase in supply.
- At this point, the business is making normal profit and there will be no incentive to leave or enter the industry. New businesses will stop entering the market as there are no more economic profits
- Therefore, the conclusion is: under perfect competition, the market price will settle over the long run at a level that corresponds with the lowest point of the AC curve – only normal profits will be made.
- The above discussion explains the long run equilibrium position of a firm which makes economic profit. **What would be the situation if the firm initially is making economic loss?**
- The process will be the opposite to when businesses make an economic profit. **HOW?**
- (Draw graphs of both an industry and firm as above, but the industry should indicate a decrease in supply and the firm show an economic loss)

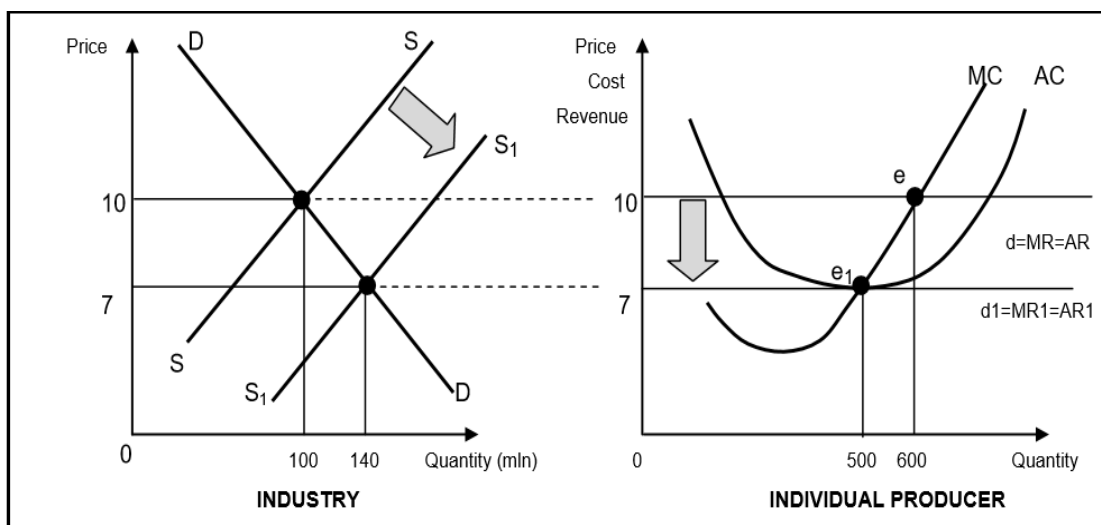
EXPLANATION:

- ✓ A business can also make an economic loss in the short – run.
- ✓ This position will, however, change in the long – run.
- ✓ Some businesses will exit the market (as opposed to more entrants when the business was making economic profit)
- ✓ Others will reduce their output level

- ✓ The supply will decrease and the supply curve will shift to the left of the original industry supply curve. (show this in your graph)
- ✓ The market price will increase. (Show this by referring to your graph)
- ✓ An individual business is a price taker and now has to take the new market price. (Show the new demand curve at the new price)
- ✓ This will result in the business making a normal profit again in the long run.

TEST YOUR KNOWLEDGE

1. Study the graph below and answer the questions that follow:

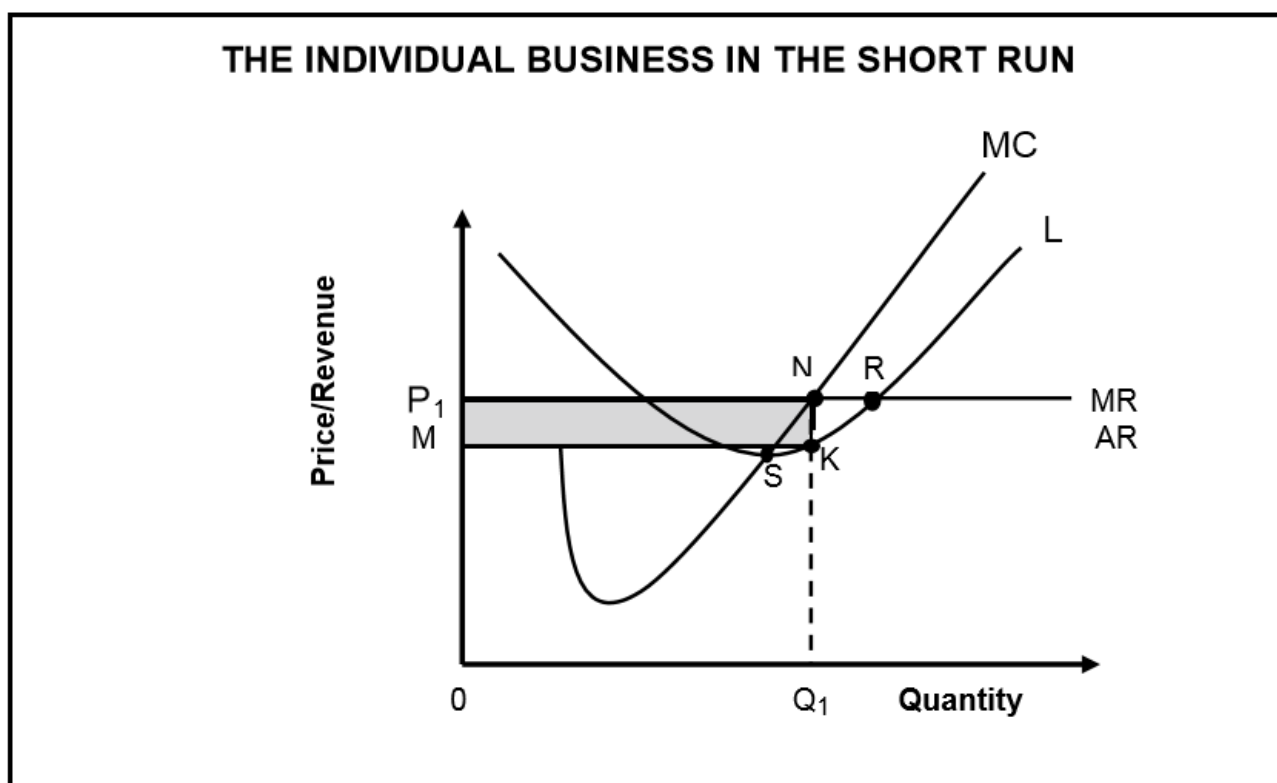


Graph 11

- 1.1 Where does the marginal cost curve (MC) intersect the average cost curve (AC)? (1)
- 1.2 Identify the price where the individual producer will make an economic profit. (1)
- 1.3 Briefly describe the term marginal cost. (2)
- 1.4 Why is the marginal revenue curve (MR) in the perfect market the same as the demand curve? (2)
- 1.5 Explain how long-run equilibrium is achieved in the market. (2 x 2) (4)

Economics P2 November 2019

2. Study the graph below and answer questions that follow



Graph 12

- 2.1 Which point (label) on the graph indicates profit maximisation? (1)
- 2.2 Name the curve labelled L. (1)
- 2.3 What is depicted by the shaded area? (2)
- 2.4 Briefly explain the term short run. (2)
- 2.5 Explain why this equilibrium position will NOT remain fixed. (2 x 2) (4)

Economics P2 November 2015

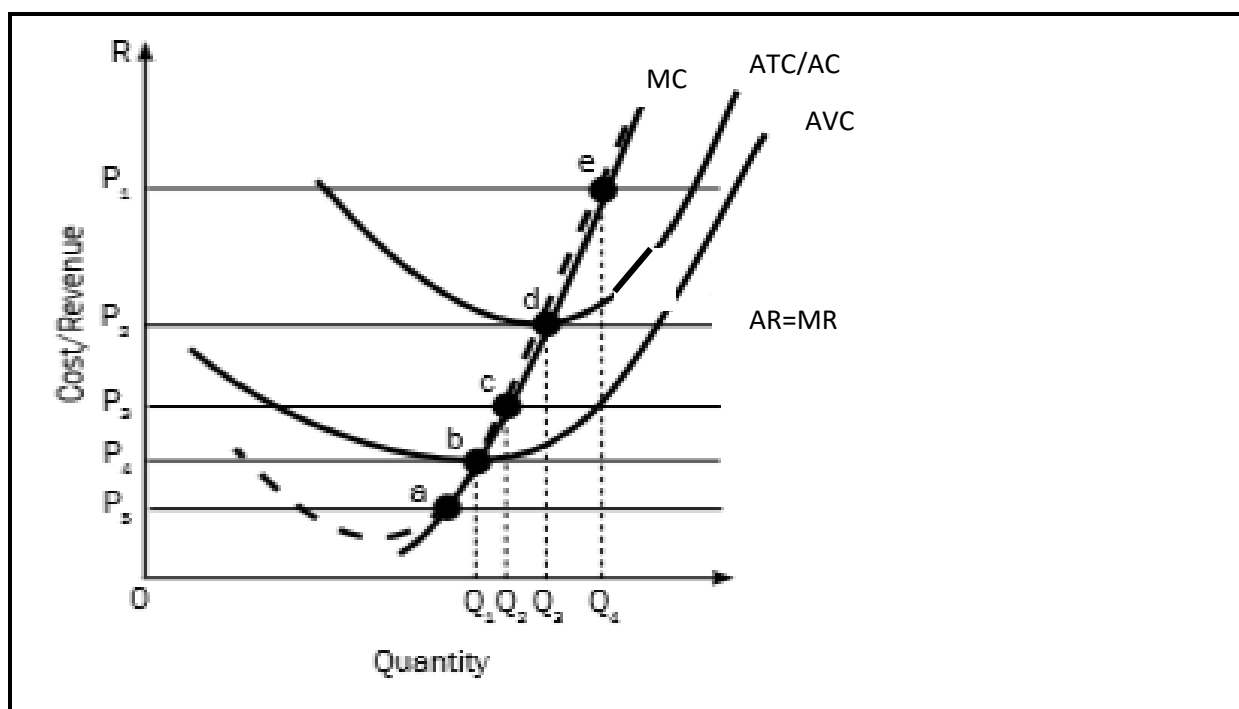
3. Explain the effect on the market in the long run, if the businesses in a perfect market made an economic profit. Economics P2 Feb/March 2018 (2x2) (4)
4. Without using a graph, explain why the price of a product (8)

Economics P2 Feb/March 2017

GRAPHIC EXPLANATION OF SHUTDOWN POINT USING COSTS AND REVENUE (FC, VC, TC, TR, AR AND AVC)

- What happens if the market price decreases? When will the firm consider closing down?
- The firm has to make decisions regarding the level of output every time the market price changes. (Remember the profit maximisation rule $MR = MC$)
- Refer to the graph below

Graph 13



Source: 2nd Mind The Gap Economics

EXPLANATION

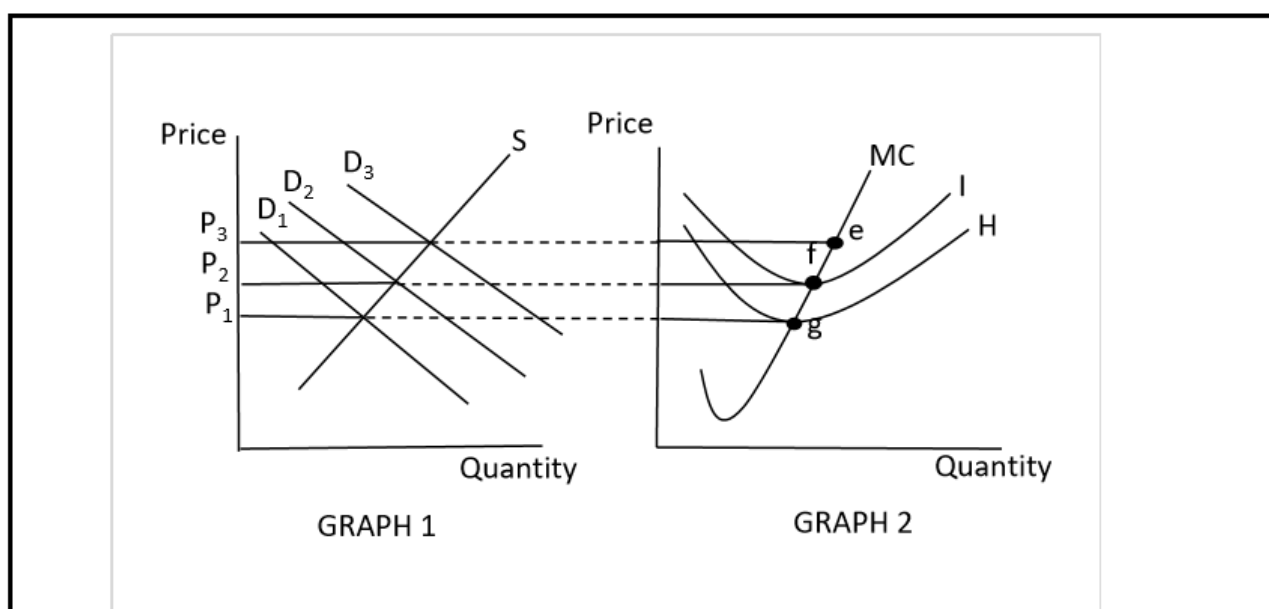
- if the market price is P_2 , AR and MR of the business is also P_2 .
- At P_2 , MC intersects the MR curve at point d. ($MR = MC$ at d)
- The firm is making normal profit at point d by producing output Q_3 since the MC cuts the AC at d (lowest point of the AC)
- Point d is also known as the break -even point.
- If the market price increases to P_1 , MR intersects MC at e. point e is above AC. The output produced is Q_4 (An increase of output from Q_3). Due to the increase in the level of output, the business will make economic profit at a market price of P_1 .
- **What will happen if the price decreases to P_3 ?** $MR = MC$ at point c. Point c is below AC curve. The business is making economic loss, which implies that it is no longer

able to cover all its production costs. However, the business will not close down immediately. They will introduce measures to minimise the loss.

- **The loss minimising rule states that when the business is no longer able to cover all its production costs, they will reduce their level of output to where $MC = MR$.** If this rule is applied, then the business will reduce its output to Q_2 .
- At this market price, the business can still pay its average variable costs and parts of its average fixed costs. Although they are making a loss, the business will be kept operational in the hope that it will break – even once more.
- At P_4 , the output level is Q_1 since $MR = MC$ at point b (the corresponding output). The market price is so low that the business is only able to pay its variable costs. Should the price drop below P_4 , the business will not be able to continue and will be forced to close down. Point b is known as the **close – down or shut – down point**
- **According to the shut – down rule: A business will shut down when the lowest point of the AVC curve is higher than the market price.**

TEST YOUR KNOWLEDGE

1. With the aid of a well-labelled graph (cost and revenue curves), explain the shut-down point for the individual firm in a perfect market. Economics P2 Nov 2018 (8)
2. Study the graph below and answer the questions that follow.



- 2.1 Which market structure do the graphs above represent? (1)
- 2.2 Give a correct label for curve H in Graph 2. (1)
- 2.3 What effect will an increase in demand have on the market price? (2)

- 2.4 Briefly describe the supply curve of an individual firm in this market structure. (2)
- 2.5 Why will a business not produce to the left of point 'g'? Economics P2 June 2019 EC (4)
3. Draw a clearly labelled graph indicating the shut-down point for the perfect competitor. Briefly explain why a business will stop producing goods at this point. (10)

Economics P2 Feb/March 2016

TIPS ON DRAWING GRAPHS

- Start by drawing the Revenue curves.
- Then draw the AC curve followed by the MC – why?
- Drawing of the MC curve in relation to the AC curve. This tends to distort the interpretation of the graph.
- the technical aspects need to be remembered, e.g. the correct shape, positioning and labelling of cost and revenue curves in the perfect and imperfect markets.
- Practise step by step drawing of the cost and revenue curves. Correctly label each step as you draw. Emphasis must be placed on the average cost curve (i.e. 'smile') which must always be drawn before the marginal cost curve (i.e. 'tick'). This will ensure that the MC always intersects the AC at its minimum point.
- **Focus on the equilibrium position/point of the firm, where $MR = MC$ which determines the profit or loss position of a firm.**
- **This point is regarded as the profit maximising point in the case of economic profit, a break-even point in the case of normal profit and loss minimising point in the case of economic loss.**
- **The explanation of the graph should follow the basic steps irrespective of which market structure is involved.**
- Identify profit maximising/loss minimising point first ($MR = MC$). This is most important as it impacts on all other variables in the explanation.
- The price and quantity should be determined. Note that in an imperfect market a line must be extended upwards from profit maximizing point to the demand curve to read off the price.
- The next step is to compare AR (price) to AC to determine whether economic profit, economic loss or normal profit is made.
- Indicate the total economic profit from the graph.
- This could take the form of labels or a calculation.
- Profit and loss calculations. There is confusion in the application of the formula, Profit = $TR - TC$. **Be careful on how you present your final calculations. A figure showing loss must be accompanied by a negative sign. If it appears without the negative sign, then the word 'loss' should accompany the figure.**

- The equilibrium position could then be classified as short term or long term or both.

6.5 COMPETITION POLICIES

6.5 Competition policies	<ul style="list-style-type: none"> • Briefly describe the competition policies • Outline the aims/objectives of the competition policy • Briefly describe SA's anti-monopolistic policy • Briefly describe the Competition Act, 1998 (Act 89 of 1998), as amended • Explain the role of the Competition Commission, Competition Tribunal and Competition Appeal Court • Give your opinion of the successes/failures of the competition policy. (relate to current examples)
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6.5.1 Description

- **Description: Competition policy** is the structures governments have in place for the regulation of markets and monopolies.
- Most countries have **competition policies** that promote healthy competition.
- South Africa's first competition policy was introduced in 1955 and was later reviewed because it became ineffective in preventing formation of oligopolies in the country.
- In 1979, the Maintenance and Promotion of Competition Act was introduced.
- The Act was amended in 1986 to give the Competition Board more powers but was also faced with technical flaws which prevented effective application.
- The **Competition Act of 1998** (Act No 89 of 1998) was passed by parliament in 1998. (This Act is part of South Africa's anti – monopolistic policy)
- This came after much review of the previous competition legislation, especially after 1994.

WHY PROMOTE HEALTHY COMPETITION?

- **Competition** among companies can spur the invention of new or better products, or more efficient processes. (Firms may race to be the first to market a new or different technology).
- Innovation also **benefits** consumers with new and better products, helps drive economic growth and increases standards of living.
- Consumers pay the lowest possible price for the product.
- Customer gets better customer service, optimised product, and at the same time, a management which is listening to the customer.

6.5.2 AIMS/OBJECTIVES OF THE COMPETITION POLICY

- To improve the efficiency of markets through legislation
- To promote healthy competition between businesses
- To prevent unfair methods of achieving and exercising market power
- To prevent the abuse of economic power by monopolies
- To regulate the increase of market power by means of takeovers (buying of one company by another) and mergers (the combination of two companies into one large company)
- To prevent restrictive practices, especially price fixing and collusion by oligopolies
- To protect the consumer against unfair practices and inferior products/ to provide for markets in which consumers have access to, and can freely select, the quality and variety of goods and services they desire.
- To contribute to South Africa's development objectives to ensure all South Africans have equal opportunities to participate fairly in economic activities/ To promote employment and advance the social and economic welfare of South Africans
- To achieve a more effective and efficient economy in South Africa
- To establish independent institutions to monitor economic competition

6.5.3 SOUTH AFRICA'S ANTI- MONOPOLISTIC POLICY

- Strict anti-monopoly policy was enacted after 1994 to boost the competition policy. This policy emphasizes that there should be no restrictions on entry to any industry which will harm the disadvantaged groups.

NB: The Anti - Monopolistic Policy wants to achieve the aims / objectives of the Competition Policy listed above. In other words, learners can write the objectives of Competition Policy when asked to answer a question on South Africa's Anti – Monopolistic Policy.

6.5.4 COMPETITION ACT OF 1998 (ACT 89 OF 1998) as amended

- **Description:** The Act provides for the establishment of a **Competition Commission** responsible for the investigation, control and evaluation of restrictive

practices, abuse of dominant position, and mergers; and for the establishment of a **Competition Tribunal** responsible to adjudicate such matters; and for the establishment of a **Competition Appeal Court**; and for related matters.

- To simplify the above description, the Competition Act of 1998 makes provision for the establishment of **three institutions** to achieve the objectives of the Act.

PLEASE NOTE:

- It is important to be able to discuss the role of each institution
- Ensure that you study the Competition Act in detail (your teacher will give guidance)
- Be able to show knowledge of the Act and of the three institutions which are responsible for carrying out the Competition Act.
- Research recent investigations by the Competition Commission into anti – competitive behaviour by firms (ask guidance from your teacher)
- Visit the following websites for more information and recent stories)
- <http://www.compcom.co.za/>
- <http://www.comtrib.co.za>

6.5.5 ROLE OF THE COMPETITION COMMISSION, COMPETITION TRIBUNAL AND COMPETITION APPEAL COURT

COMPETITION COMMISSION

Description: A **statutory** (*required, permitted*) body constituted in terms of the Competition Act of 1998 by the Government of South Africa empowered to investigate, control and evaluate restrictive business practices, abuse of dominant positions and mergers in order to achieve equity and efficiency in the South African economy.

Role/functions

- Investigates and evaluates anti – competitive conduct (restrictive business practices) in contravention of the Act.
- assessment of the impact of mergers and acquisitions on competition/ allowing or disallowing mergers and acquisitions to go ahead
- monitoring competition levels and market transparency in the economy

- identify **impediments** (*obstructions*) to competition
- making recommendations to the Competition Tribunal for approval (it will make a recommendation about penalties for businesses it finds guilty)

COMPETITION TRIBUNAL

Description: Competition Tribunal is an independent adjudicative body (**adjudicate means make a formal judgement on a disputed matter**) established in terms of the Competition Act of 1998. It has **jurisdiction** (*official power to make legal decisions and judgements*) throughout the Republic of South Africa. It exercises its functions in accordance with the Act, the Constitution and without fear, favour or prejudice.

Role/ functions

- accepts or rejects the investigation and recommendation of the Competition Commission
- granting of exemptions, authorise or prohibit large mergers (with or without conditions)
- adjudicate in relation to any conduct prohibited by the Act
- grant an order for costs on matters presented to it by the Competition Act

COMPETITION APPEAL COURT

Description: It is established in terms of the Competition Act of 1998. It is a special division of the High Court. It has jurisdiction throughout the Republic of South Africa and is a court of record.

Role/functions

- may consider any appeal from, or review of, a decision of the Competition Tribunal
- confirm, amend or set aside a decision or an order that is the subject of appeal or review by the Competition Tribunal.
- Give any judgement or make any order as circumstances require
- Confirm an order by the Competition Tribunal for the **divestiture** (*the action or process of selling off subsidiary business interests or investment*) of assets by parties who have contravened the Act.

The Competition Commission (Commission) is one of three independent statutory bodies established in terms of the Competition Act, No. 89 of 1998 (the Act) to regulate competition between firms in the market. The other bodies are the Competition Tribunal (Tribunal) and the Competition Appeal Court (CAC). The Commission is the investigating and prosecuting agency in the competition regime while the Tribunal is the court. The CAC hears appeals against decisions of the Tribunal. Although each of the bodies functions independently of each other and of the State, the Commission and Tribunal are administratively accountable to the Economic Development Department (EDD), while the CAC is part of the judiciary.

6.5.6 OPINIONS ON SUCCESS/FAILURE OF COMPETITION POLICY IN SA

The competition policy is successful by:

- making provision for institutions like the Competition Commission, Competition Tribunal and Appeal Court to investigate any unfair competition in the country
- functioning as an investigator and evaluator of restrictive business practices
- making recommendations about penalties for businesses found guilty of abuse
- implementing the Competition Tribunal who accepts or rejects the investigation and recommendation of the Competition Commission and confirms penalty imposed
- making it possible for businesses to appeal for a penalty imposed by the Competition Appeal Court
- curbing the economic power of big conglomerates to arrive at a more equitable distribution of income and wealth
- regulating mergers and takeovers to regulate market power of mergers

(Refer to practical examples where Competition policy has succeeded)

The competition policy is not successful because of:

- frequency of investigations into collusive behaviour e.g. cement / steel / bread / bank industries
- fines were too lenient and not acceptable to some parties
- too many competitors still preventing affirmative action/young black industrialists entering into the market (BEE)

TEST YOUR KNOWLEDGE

1. Name any TWO institution created to carry out the Competition Act in South Africa. (2x1)
2. What is the view of the competition policy on the formation of cartels? (2)
3. Study the extract below and answer question that follow:

COMPETITION COMMISSION PROHIBITS MERGER

In February 2018, the Competition Commission prohibited the proposed merger between SA Airlink (Pty) Ltd and FlySafair (Pty) Ltd. SA Airlink has a monopoly or near monopoly on most routes it operates on. FlySafair, on the other hand, has been growing in terms of existing routes as well as venturing into new routes.

[Adjusted from Compcom.co.za]

- 3.1 Name the Act that gives all South Africans an equal opportunity to participate fairly in economic activities. (1)
- 3.2 Which institution accepts or rejects recommendations from the Competition Commission? (1)
- 3.3 Briefly describe the role of the Competition Appeal Court. (2)
- 3.4 How can small, medium and microenterprises contribute to the goals of the competition policy? (2)
- 3.5 If the merger were allowed, how would it benefit the companies involved? (2 x 2)

4. Study the extract below and answer questions that follow:

NEW AMENDMENTS TO COMPETITION ACT

The government introduced the Competition Act, 1998 (Act 89 of 1998) to promote competition and enhance the efficiency of the South African economy. The Competition Commission, Competition Tribunal and Competition Appeal Court play an important role in the administration of the Act.

Companies that are suspected of collusion are investigated and if they are found guilty, they are fined heavily. In the new amendment of section 73A of the Competition Act, provision is made for new criminal sanctions to be imposed on individuals.

[Adapted from Businessstech.co.za, 2016]

- 4.1 Which institution imposes fines on companies that are guilty of collusion? (1)
- 4.2 What is the role of the Competition Appeal Court? (1)

- 4.3 State any ONE aim of the competition policy. (2)
- 4.4 How does competition in the market benefit the consumer? (2)
- 4.5 Briefly discuss the success of the competition policy of South Africa. (2 x 2) (4)
- 5.1 Explain the aims of South Africa's anti-monopoly policy. (8)
- 5.2 Explain the roles played by any TWO key institutions that monitor competition in South Africa. (8)
6. How successful is the competition policy in promoting a more competitive economy? (8)

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