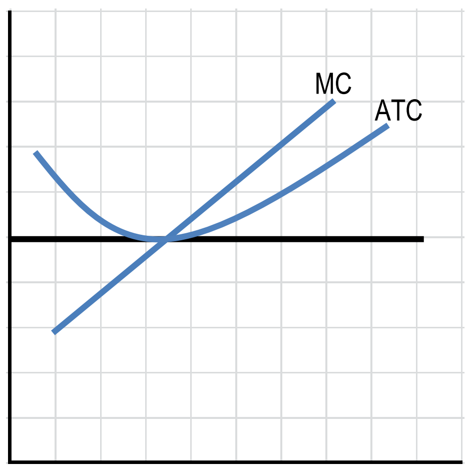
CONCEPT: PERFECT COMPETITION AND EFFICIENCY

● Perfectly competitive markets ____________ both productive efficiency and allocative efficiency.

□ ***Productive Efficiency*** – producing at the ______________________________

- The lowest possible cost is ____________________
- In the long run, perfect competition forces firms to produce at ______________________



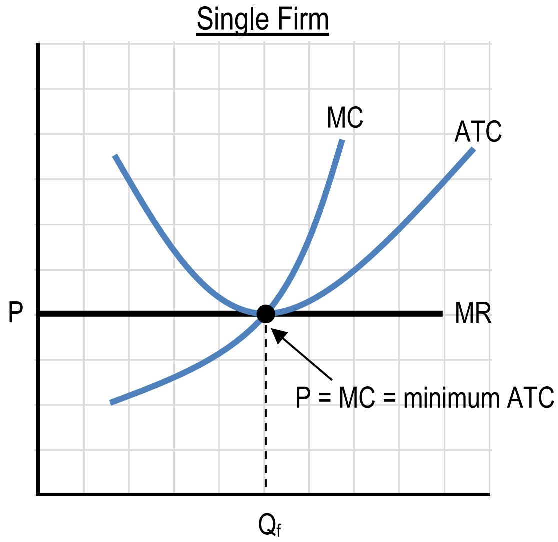
□ ***Allocative Efficiency*** – production represents ______________________________

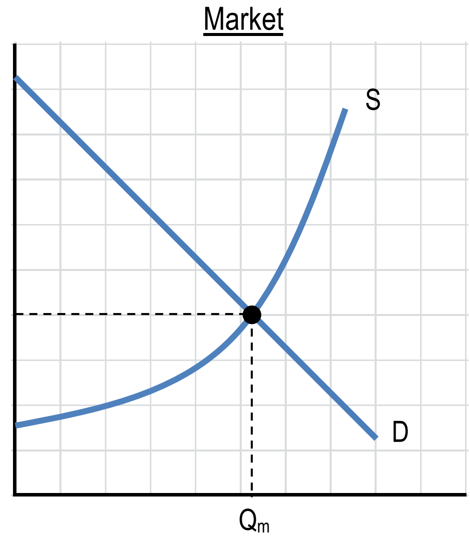
- Producing means producing up to the point that the _______ = _______

Allocative Efficiency in Perfect Competition

1. The price of a good represents the MB to consumers of the last unit sold. (P = MB)
2. In perfect competition, firms produce up to the point where the price (MR) equals marginal cost. (P = MC)
3. Thus, firms produce up to the point where MB to consumers equals MC to producers. (P = MB = MC)

PRACTICE: Use the following graphs to answer the questions below:





The firm is a price taker because:

a) It has a U-shaped ATC curve
b) The profit-maximizing point occurs where MC equals ATC
c) The MC curve has an upward slope
d) The MR curve is horizontal

When this firm is producing the profit-maximizing output:

a) Total revenue is equal to total cost
b) It earns an economic profit
c) Only allocative efficiency is reached (i.e. no productive efficiency)
d) Only productive efficiency is reached (i.e. no allocative efficiency)

When P = MC = minimum ATC for individual firms, in the entire market:

a) Consumer surplus is larger than producer surplus
b) Producer surplus is larger than consumer surplus
c) Supply and demand are the same
d) Total surplus is at a maximum