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CLEARED PRELIMS

NEXT IAS

(To be filled by candidate)

Name of Candidate : NESRIN P FASIM

Roll No. : ..... Contact No. .....

e-mail: ..... Date of Examination : .....

Exam Centre : Old Rajinder Nagar ☐ Online ☑

CSE (MAINS) TEST SERIES-2024

Test-05	ECONOMICS OPTIONAL
Dated : 05-08-2024	*Complete Syllabus: Paper-I*

Time Allowed : Three Hours | Maximum Marks: 250

QUESTION PAPER SPECIFIC INSTRUCTIONS

(Please read each of the following instructions carefully before attempting questions)

There are ***EIGHT*** *questions divided in* ***Two sections*** *and printed in* ***ENGLISH****.*

Candidate has to attempt ***FIVE*** *questions in all.*

Question No. 1 and *5 are compulsory and out of the remaining, any* ***THREE*** *are to be attempted choosing at least* ***ONE*** *question from each section.*

The number of marks carried by a question/part is indicated against it.

Answers must be written in the medium authorized in the Admission. Certificate which must be stated clearly on the cover of this Question-cum- Answer (QCA). Booklet in the space provided.

No marks will be given for answers written in a medium other than the authorized one.

Word limit in questions, wherever specified, should be adhered to.

Attempts of question shall be counted in sequential order. Unless struck off. Attempt of a question shall be counted even if attempted partly. Any page or portion of the page left blank in the Question cum Answer (QCA). Booklet must be clearly struck off.

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(For filling by Examiners only)

Q. No.	Page No.	Max. Marks	Marks	Total	Signature
1. (a)	4	10			
1. (b)	6	10			
1. (c)	8	10			
1. (d)	10	10			
1. (e)	12	10			
2. (a)	14	15			
2. (b)	17	15			
2. (c)	20	20			
3. (a)	24	15			
3. (b)	27	15			
3. (c)	30	20			
4. (a)	34	15			
4. (b)	37	15			
4. (c)	40	20			
5. (a)	44	10			
5. (b)	46	10			
5. (c)	48	10			
5. (d)	50	10			
5. (e)	52	10			
6. (a)	54	15			
6. (b)	57	15			
6. (c)	60	20			
7. (a)	64	20			
7. (b)	68	15			
7. (c)	71	15			
8. (a)	74	15			
8. (b)	77	15			
8. (c)	80	20			
Grand Total					

Remarks

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Observations:

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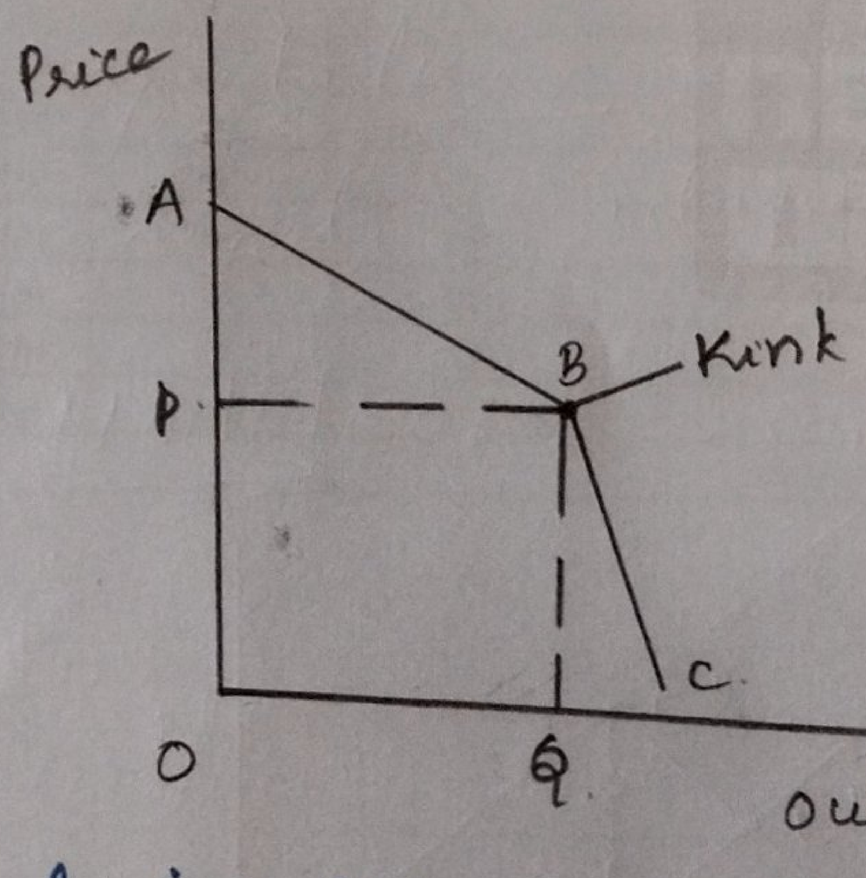
SECTION-A

Write notes on the following in about 150 words each: **(10 × 5 = 50)**

Q.1 (a) Explain price stickiness with a model of oligopoly.

The price stickiness model of oligopoly or Kinked demand curve model was put forward by Paul. M Sweezy to explain price - quantity relationship in oligopoly.

According to Sweezy,



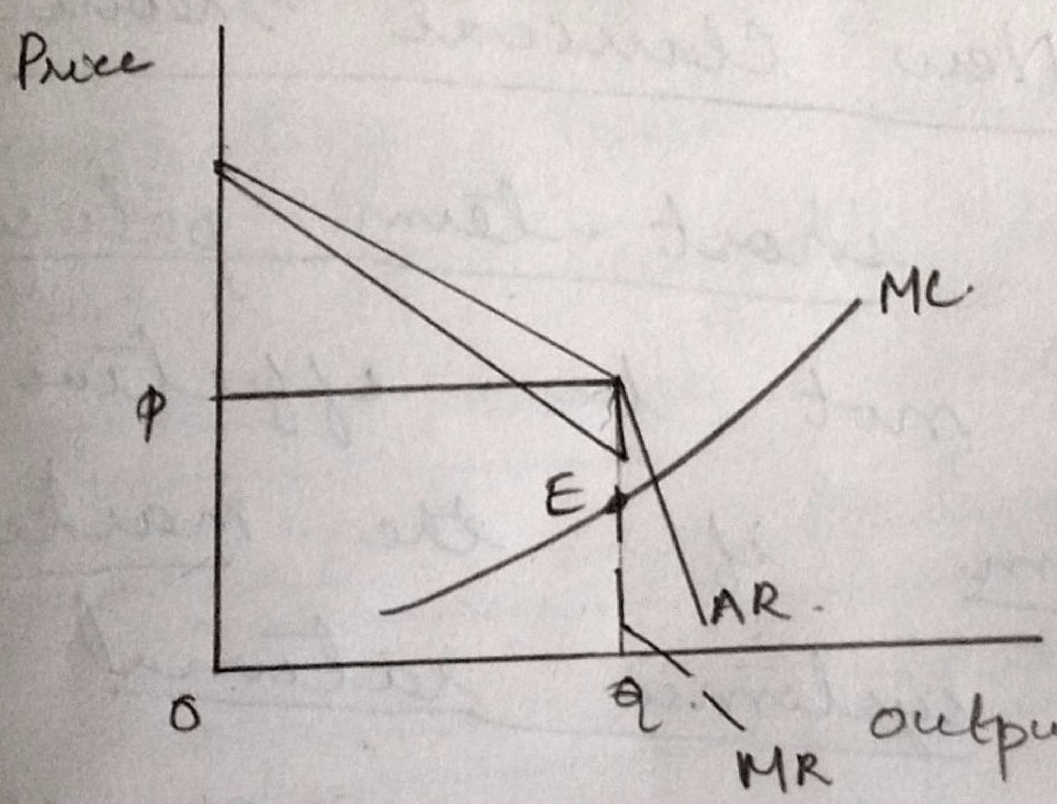
At portion AB → the oligopolist demand curve is elastic because he thinks that if he ~~increases~~ increases the price, other players ~~too~~ would not ~~increase~~ reduce the price and hence he loses the market. At portion BC → the demand curve is steeper because if he ~~reduces~~ increases price above P, ~~th~~ others will not follow and he will lose the market.

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Hence, at the kink, price is determined.

Market output - price determination:



At P → Price is sticky.

The Marginal Revenue ~~Ra~~ curve is discontinuous at the portion of kink due to the oligopoly behaviour → hence Marginal cost passing through discontinuous MR ~~fun~~ portion → equilibrium is determined at [price P] with Q quantity

The model is facing criticisms like how the price is determined earlier and what happens with MC passes at ~~do~~ non-discontinuous portion of MR.

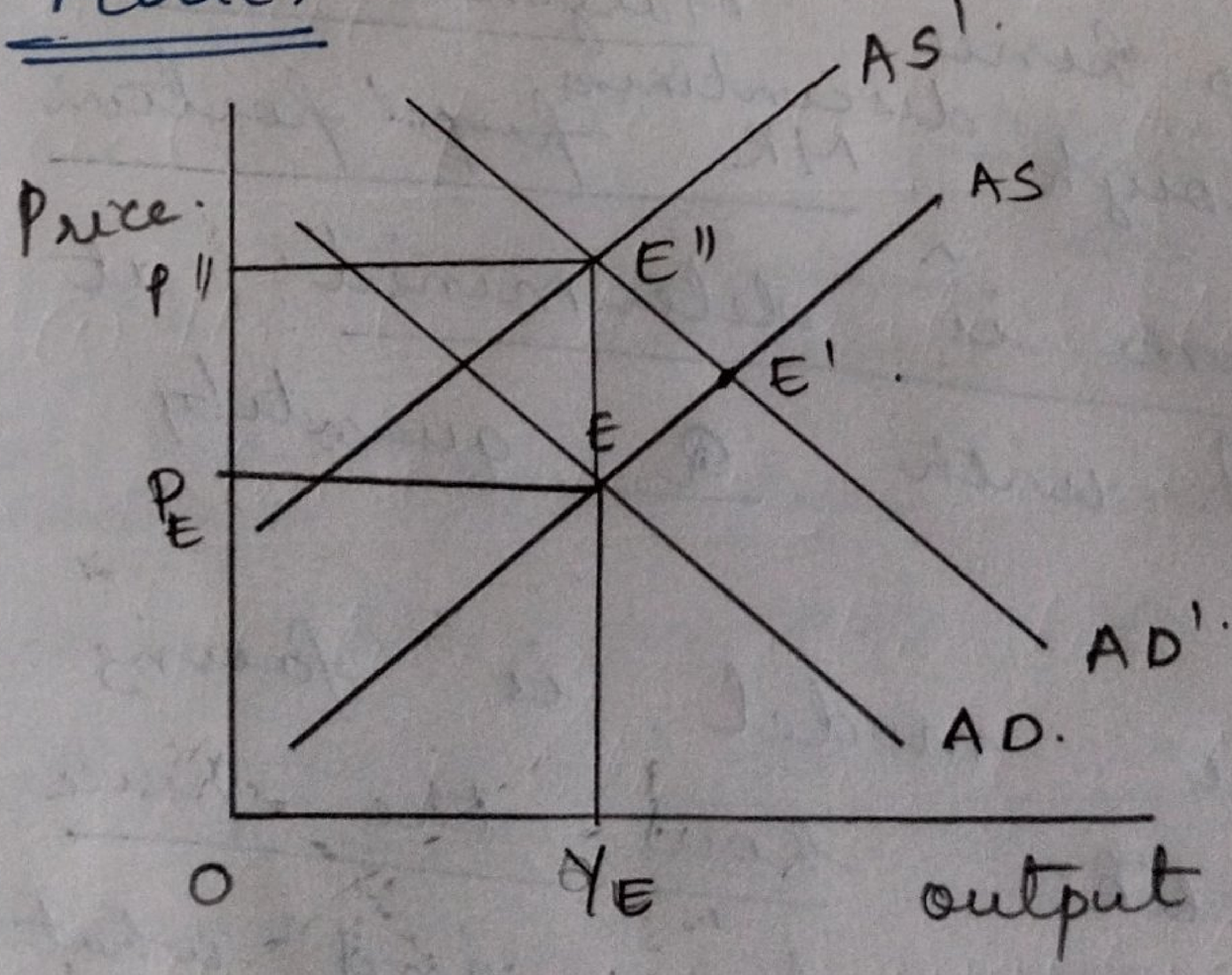
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Q.1 (b) What is policy ineffectiveness proposition?

The policy ineffectiveness proposition was given by Robert Lucas Jr and other New Classical theorists.

It says that short-term policy changes will not be effective in short term if the market players have systemic rational expectations with zero error, as against adaptive expectations

Model



From the figure, initial equilibrium position was E with equilibrium

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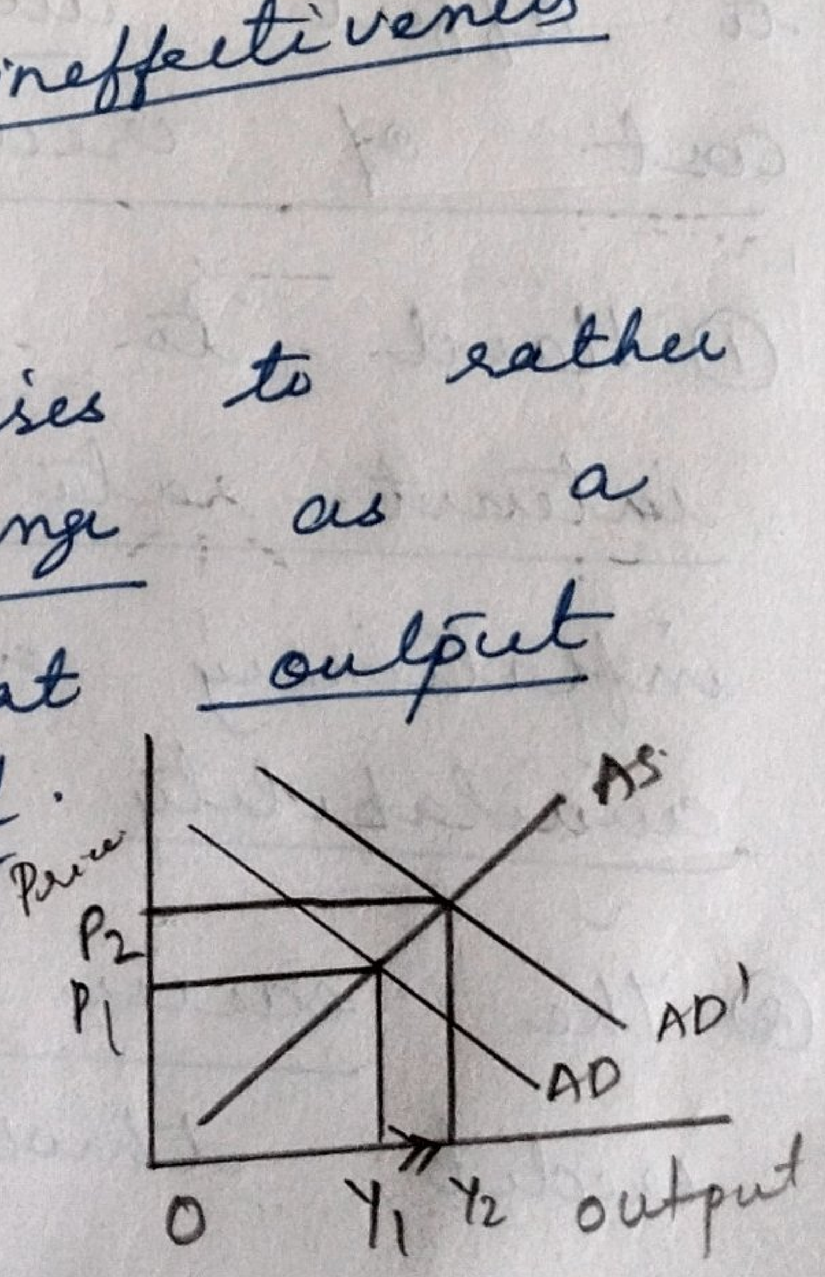
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fuce P_E and quantity ~~Q_E~~ Y_E

Now due to increase in Aggregate demand to AD' due to an expansionary fiscal / monetary ~~no~~ policy, new position will be E', but it won't be attained with higher income ^ output, because due to rational expectation, the workers anticipate the changes and reduces As curve, As curve shifts ~~to~~ upwards to As' and output will be still at Y_E, with only price increases.

This is Policy ineffectiveness proposition.

Lucas advises to rather bring policy change as a surprise, such that output could be increased.



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Q.1 (c) How is it difficult for open market operation to affect both availability and cost of credit at the same time?

Open Market Operation refers to the adjustments in the money supply through interest rates changes to bring stability in market and ensure growth

Egs → Repo rate
→ Reverse Repo rate.
→ sterilisation
→ Buying and selling bonds

It is difficult for OMO to affect availability and cost of credit because:

① Hard to rationalise the interest rate given high inflationary situation → Hence availability will be affected.

② The easier availability of credit through lesser interest

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rate can lead to problem of low revenue for the banks due to less interest rate.

RBI has brought about mechanisms like Priority Sector Lending to agriculture and other sectors to improve the credit availability to the needy by managing cost.

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Q.1 (d) How inflation is affected by both appreciating and depreciating currency?

Depreciation refers to the decrease in exchange rate of domestic currency compared to foreign currency.

Eg ⇒ $1 / ₹80 → $1 / ₹85.

Appreciation refers to increase in exchange rate of domestic currency compared to foreign currency

Eg ⇒ $1 / ₹85 → $1 / ₹80.

In case of real exchange rate

→ Higher real exchange rate → depreciation

Effect on Inflation

Depreciating currency

→ It will lead to increase in ~~exports~~ imports due to more cheaper ~~imports~~ exports and ~~cheap~~ dearer ~~dearer~~ imports

→ hence supply of commodities will be ~~greater~~ lesser than demand

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due to lessee imports → this leads to peaking ~~so~~ demand than supply → Demand pull inflation can take place.

Appreciating currency

→ Appreciation leads to increase in imports and reduction in exports → there will be more ~~demand~~ supply of commodities than demand → deflationary tendencies and low growth

Hence government and RBI tries to keep depreciation and inflation in control through Managed floating exchange rate system via sterilisation operations.

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Q.1 (e) Explain the role of G20 in promoting economic and policy cooperation, giving illustration.

The G20 summit was recently held in India in 2023. It is an organisation with 19 countries and 2 unions - EU and AU, with almost 75% of world GDP.

Role of G20 in promoting economic and policy cooperation

① G20 helped in solving Asian financial crisis of 1999

② Increased trade cooperation through transportation network

eg Recently concluded India - Middle East Economic corridor.

③ Encouraging food security

eg Deccan high level principles
Chennai high level principles.

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(4) Impetus given to Digital Public Infrastructure in recent summit — Delhi declaration on DPI - for efficient service delivery.

(5) Ensuring urde dialogues on renewable energy

(es) triple renewable energy production by end of 2030.

(6) Empowering biofuel - Global Biofuel alliance.

(7) Encouraging wide ranging discussions through Sherpa track and Financial ~~xxx~~ specialists track -

(8) Parliamentary union — (9) ~~Thais~~ Speakers conference on parliament functioning.

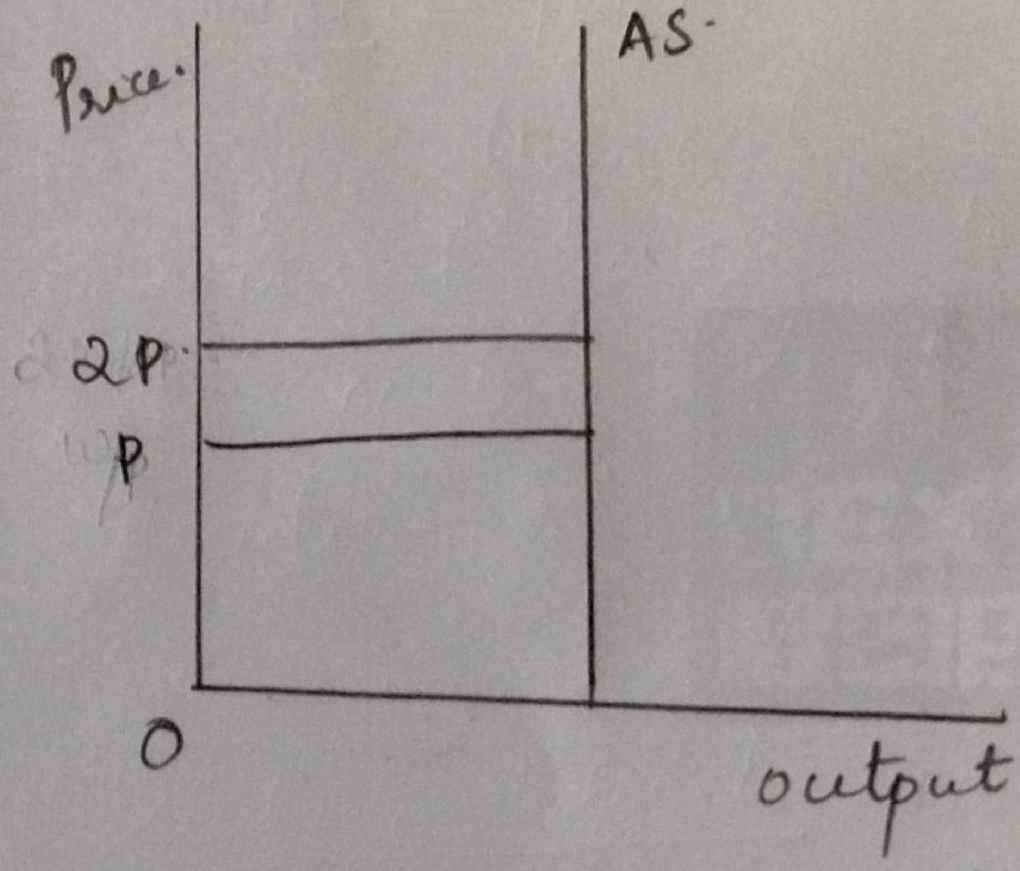
G-20 hence is a growing organisation with wider opportunities.

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Q.3 (a) What are the reasons for differences in Keynesian and Classical AS curve? 15

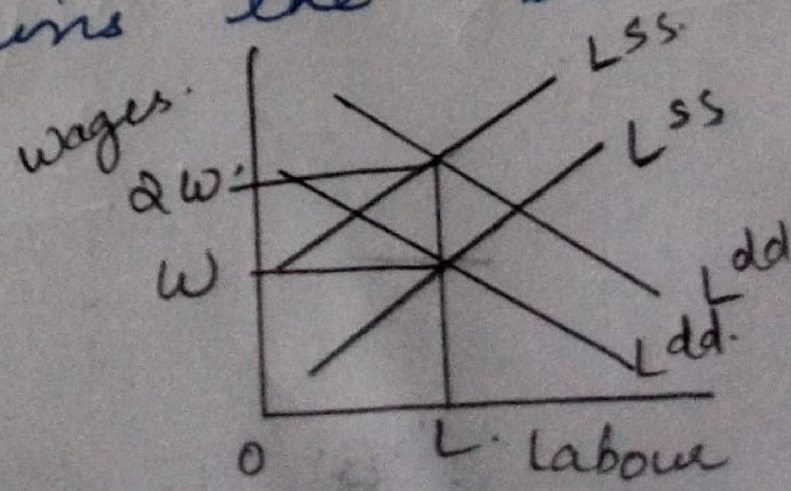
The aggregate supply curve has different shape for Keynesian and Classical model.

Classical Aggregate supply curve



The aggregate supply curve is vertical due to:

① Wage-price flexibility: The labour market will adjust for the change in price by adjusting their nominal wage such that real wage remains the same.



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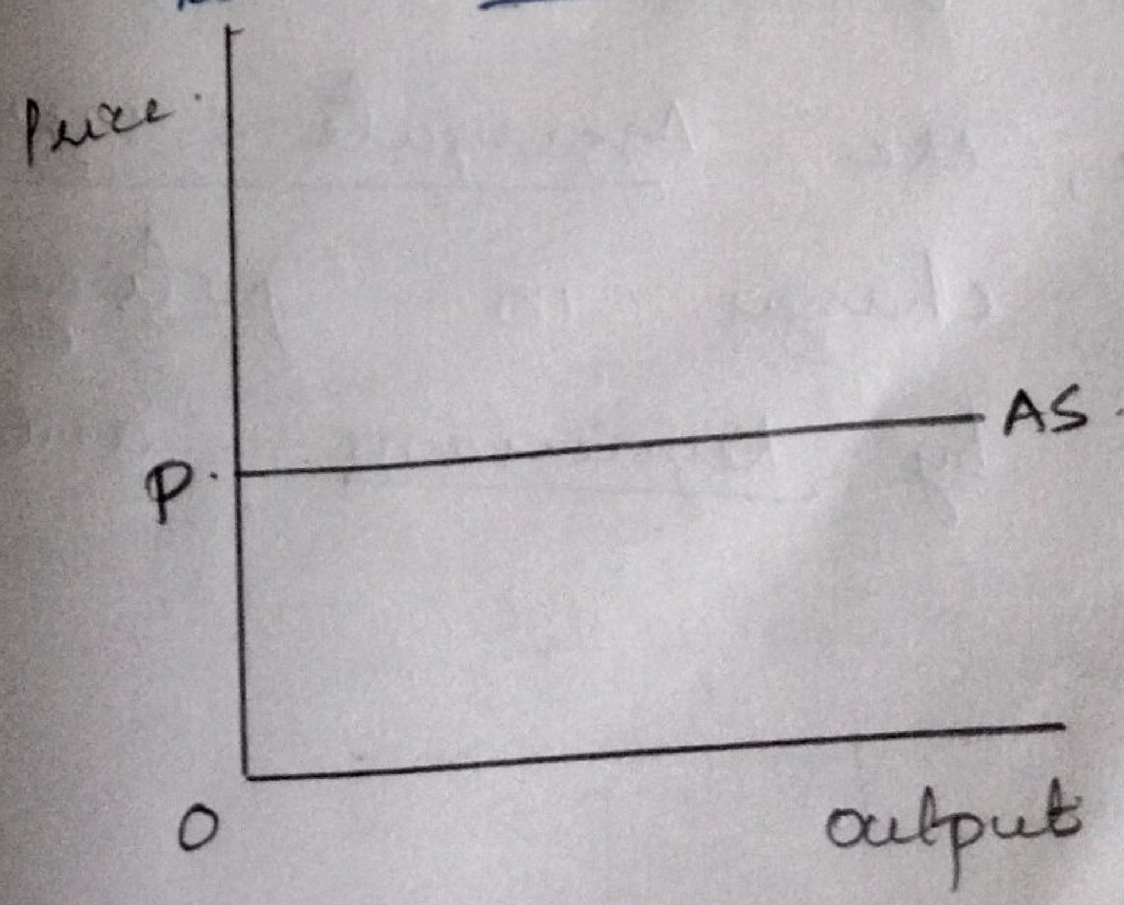
② Assumption of Classical Dichotomy and money neutrality - nominal variables will only impact nominal variables and not real variables.

③ Assumption Say's law → Supply creates its own demand → whatever supplied will be demanded (supply side model).

④ Workers adjusting their forces based on the real wages - they not only consider nominal wage.

Keynesian aggregate supply curve:

It is horizontal in nature



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Due to:

① Wage - price rigidity - the workers do not identify real wages change and take decisions based on purely nominal wage - MONEY ILLUSION - hence they do not allow the nominal wage to fall below a certain level → instead they decide to remain unemployed if wage rate goes below a certain level. Hence there is price-rigidity and AS curve is horizontal.

② Demand side model → equilibrium determined by aggregate demand.

Hence, the Aggregate supply curve brings changes in policy prescriptions by Keynesians and Classicals.

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Q.3 (b) Explain the Cournot model of duopoly with product differentiation. 15

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Cournot model of duopoly refers to the simultaneous setting of quantity determination in a duopoly market with 2 firms

Cournot model with product differentiation

Take demand functions of 2 firms,

$$P_1 = a_1 - q_1 - \frac{q_2}{2}.$$

$$P_2 = a_2 - q_2 - \frac{q_1}{2}.$$

where $P_1 \rightarrow$ price of q_1

$P_2 \rightarrow$ price of q_2.

$a_1 \rightarrow$ attribute of product 1.

$a_2 \rightarrow$ attribute of product 2.

$q_1 \rightarrow$ quantity of firm 1

$q_2 \rightarrow$ quantity of firm 2.

Profit functions

For firm 1,

$$\Rightarrow \pi_1 = P_1 \cdot q_1$$

$$= \left(a_1 - q_1 - \frac{q_2}{2}\right) q_1$$

$$= a_1 q_1 - q_1^2 - \frac{q_2 q_1}{2}.$$

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Profit maximisation:

$$\frac{\partial \Pi_1}{\partial q_1} = a_1 - 2q_1 - \frac{q_2}{2} = 0.$$

$$2q_1 = a_1 - \frac{q_2}{2} \Rightarrow \boxed{q_1 = \frac{a_1}{2} - \frac{q_2}{4}} \quad \text{①}$$

~~$q_1 = \frac{a_1}{2} = q_2$~~ $\qquad \boxed{q_1 = \frac{a_1 - q_2}{2}}$

Best response function of firm 1.

Profit of firm 2:

$$\Rightarrow \Pi_2 = P_2 \cdot q_2.$$

$$= \left(a_2 - q_2 - \frac{q_1}{2}\right) q_2.$$

$$= a_2 q_2 - q_2^2 - \frac{q_1 q_2}{2}.$$

$$\frac{\partial \Pi_2}{\partial q_2} = a_2 - 2q_2 - \frac{q_1}{2} = 0.$$

$$2q_2 = a_2 - \frac{q_1}{2}$$

$$\boxed{q_2 = \frac{a_2}{2} - \frac{q_1}{4}} \quad \text{②}$$

Best response function of firm 2.

On putting ② in ①,

ie., $q_2 = \frac{a_2}{2} - \frac{q_1}{4}$.

$$\Rightarrow q_1 = \frac{a_1}{2} - \frac{\left(\frac{a_2}{2} - \frac{q_1}{4}\right)}{4}$$

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$$q_1 = \frac{a_1}{2} - \frac{\left(\frac{2a_2 - q_1}{4}\right)}{4}$$

$$= \frac{a_1}{2} - \left(\frac{2a_2 - q_1}{16}\right)$$

$$= \cancel{-\frac{a_1}{2}} \cancel{+ 2a_2} +$$

$$\Rightarrow \boxed{\frac{8a_1}{16} \cdot -\frac{2a_2}{16} + \frac{q_1}{16}}$$

This means that as attribute of firm 1 (a_1) is higher, q_1 will also increase. But if attribute of firm 2 (a_2) is higher, it will reduce q_1.

That means with increase in our attribute, quantity demanded of that product will increase but quantity demanded will decrease with the increased attribute of the other product.

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Q.3 (c) Show how idea of monopolistic competition becomes intrinsic to the idea of endogenous growth theory? 20

Endogeneous growth theory refus to theories in growth dealing with the effut of technology endogeneous in the growth model.

In exogeneous growth models like Solow with technology as the exogeneous varable, it ~~led to~~ used perfect competition and constant returns to scale as its assumption.

But with new models like Romer's growth model, the assumption of increasing returns to scale is incoporated to undent and the effut of varables like human capital and technology.

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For instance,

in Romer's model,

$$Y = f(K, AL)$$

Here, there are increasing returns to scale due to the assumption of monopolistic competition involving many sellers and the buyers but differentiated products

For instance, each knowledge is different in Romer's model because of the effects like standing on toe's effect and standing on shoulders effect

The earlier knowledge affecting new capital creation and different labour working on same products in Research & Development (ϕ, λ) cas

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lead to Romer's growth model. Hence Monopolistic competition becomes an important component in Romer's model with,

$$g_A = \frac{\lambda n}{(1-\phi)}$$

where g_A → rate of growth
n → rate of population growth.

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Q.4 (a) Examine the role of fiscal and monetary policy in context of developing nations and show that fiscal policy has larger effect while monetary policy can stabilise. 15

In developing countries like India, fiscal policy is more used for development than monetary policy as empirical evidences show.

Role of fiscal policy and monetary policy in developing nations

Fiscal Policy:

① For regulating the tax structure
② ensuring efficient tax base → for revenue collection.

② For provision of public goods - allocation of goods.

③ For distribution functions — mainly in redistribution — especially subsidies like agricultural subsidies to lift them out of poverty.

④ For regulating taxes — progressive taxation.

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(5) Construction of basic social and economic infrastructure

Eg Roads through PPP projects.

Monetary Policy

(1) To ensure adequate provision of credit to the needy through Open market operations.

(2) Interest rate targeting to control inflation → presently fixed at 4 ± 2 % band for CPI by RBI

(3) Ensuring Priority sector lending to needy sectors. Eg Agriculture

(4) For better regulation of informal credit.

(5) Ensure overall stability. Eg Prescribed Provisioning coverage ratio for of NPA crisis.

However fiscal policy has larger effect in developing countries because:

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(1) Lower transmission mechanism due to ~~was~~ less developed market with less α_g (government multiplier), less b (interest sensitivity of investment demand), more k (income sensitivity of money demand), less h_r (interest sensitivity of money demand).

(2) Many underdeveloped financial markets.

~~(3)~~

While monetary policy could stabilise the market through:

① Efficient interest rate adjustment can trigger investment

② Improve money supply stabilisation

Hence, fiscal policy tends to be more effective than monetary policy in developing countries.

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Q.4 (b) If government promotes purchase from local industry only, then how will it affect the multiplier? How will the economy perform in a flexible exchange rate system? 8+7=15

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The government purchase from local industry will have an impact on Keynesian multiplier on open economy:

We know, Agg. demand for open economy

$$AD = \bar{C} + c(Y - tY) + \bar{I} + \bar{G} + (\bar{X} - (\bar{M} + mY)).$$

At equilibrium, $Y = AD$,

$$Y = \bar{C} + \bar{I} + \bar{G} + c(Y - tY) - mY + (\bar{X} - \bar{M}).$$

Put $\bar{C} + \bar{I} + \bar{G} + (\bar{X} - \bar{M}) = \bar{A}$

$$Y - c(Y - tY) + mY = \bar{A}$$

$$\Rightarrow Y(1 - c(1-t) + m) = \bar{A}.$$

$$\boxed{Y = \frac{1}{1 - c(1-t) + m}\ \bar{A}}$$

$$\text{Multiplier} = \frac{1}{1 - c(1-t) + m}$$

where c = marginal propensity to consume

t = proportional tax rate

m = marginal propensity to import

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Now if Government promotes purchase from local industry only, the value of multiplier will increase because marginal propensity to import decreases,

ie-, multiplier ↑ = $\frac{1}{1-c(1-t)+m\downarrow}$

Hence there will be more multiplier effect with increase in purchase from local industry.

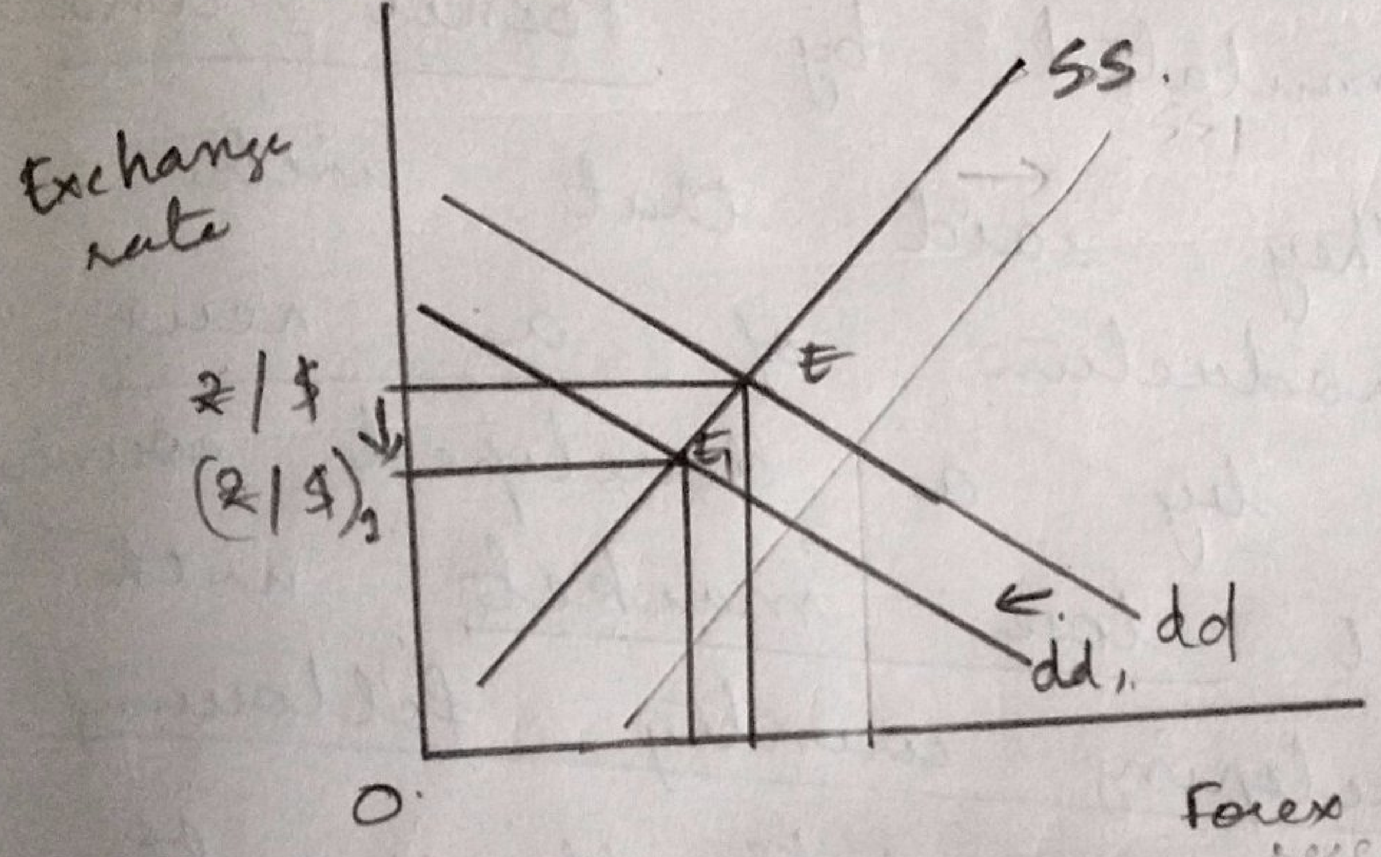
In a flexible exchange rate system, with lesser imports from the world, there will be lesser outflow of forex reserves

→ As a result, its supply increases and supply of domestic currency is comparatively lesser → As a result there

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will be [appreciation] of the Rupee —



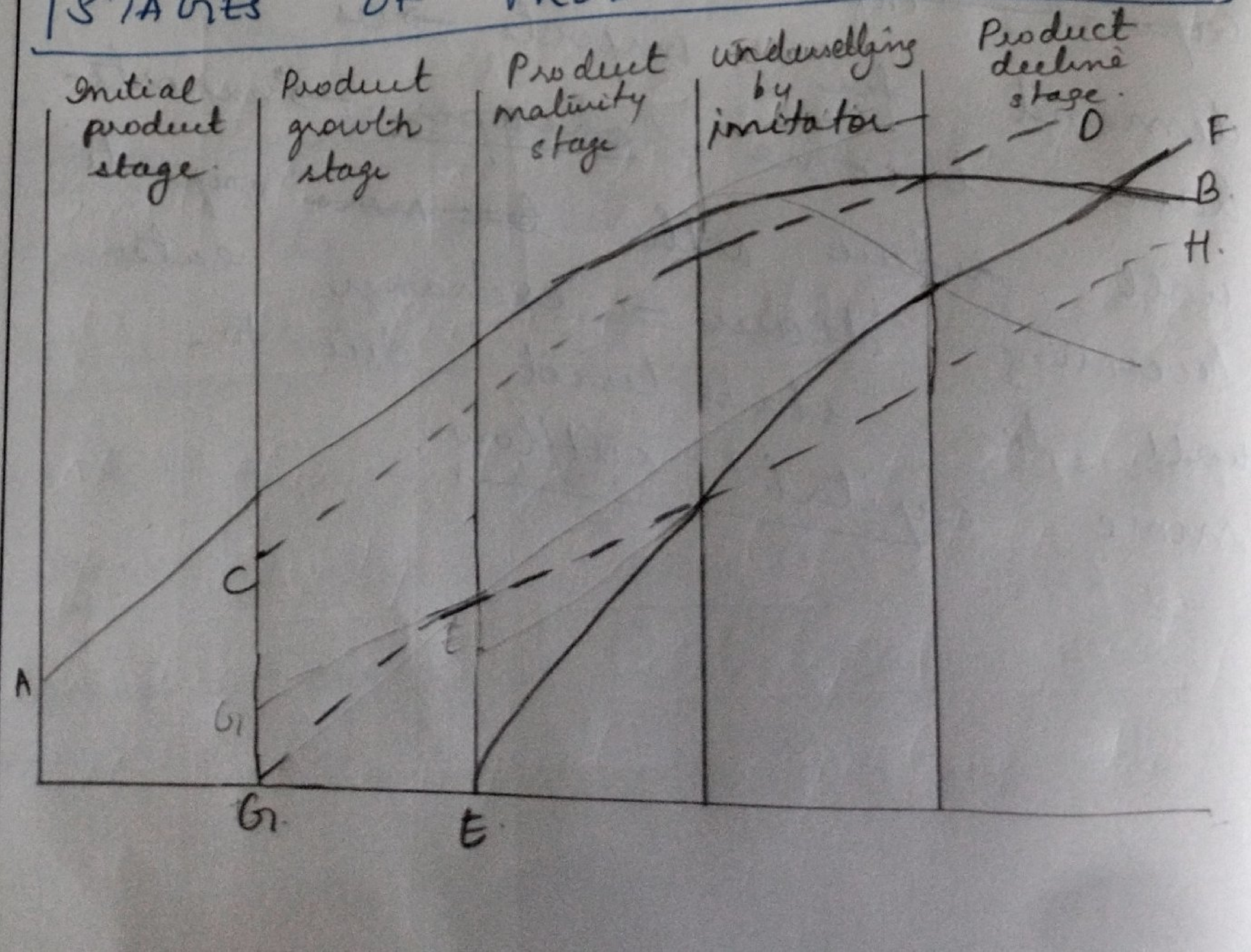
As demand for forex reduces from dd to dd₁, there will be appreciation → there will be more ~~capital inflow due to~~ demand for imports → as imports have become cheaper → exports will reduce with ~~less more~~ becoming dearer → exchange rate will be stabilised due to more capital outflow.

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Q.4 (c) Explain product life cycle theory of trade. 20

The product cycle theory of trade was formulated by Posner and Vernon. They said that with the introduction of a new product by a developed country, it will lose market with the developing country following the production later. Hence the product will become a common one having new significance.

STAGES OF PRODUCT CYCLE THEORY



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AB → production by developed country

CD → consumption by developed country

EF → production by developing country

GH → consumption by developing country

Stage 1 – Initial product stage

In this stage, the initiator country / developed country starts to produce a new commodity through innovation.

Stage 2 – Product growth stage

The initiator starts to develop the product and there will be consumption by the people. They also start trading the commodity to a developing country — consumption picking up from G.

Stage 3 – Product maturity stage

The developing country starts to produce the commodity on their own and still imports

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more from the developed country

Therefore, the developing country is understanding the techniques of production of new commodity

Stage 4 - undercelling by the imitator:

In this stage, the imitator country (developing country) produces the whole amount of commodity ~~by~~ its for its own consumption rather than depending on the developed country who was the initiator of the product.

Stage 5 - Product decline stage:

At this stage, the production of developing country becomes higher than developed country with it ~~importing~~ exporting those

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goods to the initiator developed country.

Hence the consumption becomes more in initiator and the production increased in developing country.

This theory, thereby shows the stages by which a new product expands market and the impact by the imitator.

Criticisms
- → didn't account tariff / quota policies
- → Not all developing countries have enough resources to produce new products.
- → Technology transfer unexplained.

In short at final stage, the initiator/developed country moves to production of a new product.

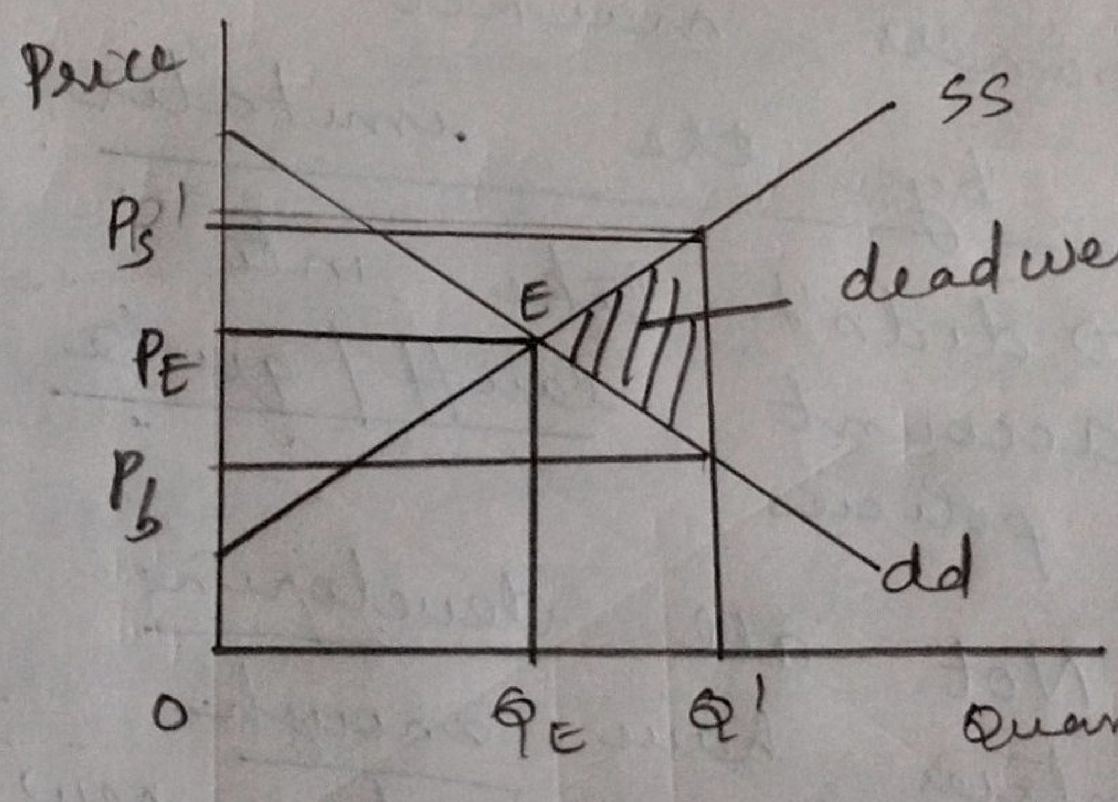
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SECTION-B

Write notes on the following in about 150 words each: **(10 × 5 = 50)**

Q.5 (a) Explain how perverse subsidies are detrimental to growth.

Perverse subsidies refers to those subsidies which can negatively affect the overall output and growth of the economy.



The original equilibrium is at E. With provision of subsidy, the quantity supplied increased to Q'. This affects the overall surplus and leads to a deadweight loss ~~of~~ as shown in the figure.

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Detrimental to growth because:

(1) Reduction in incentive to work

(2) Environmental degradation:

(eg) overuse of urea — present N:P:K ratio is 8:3:1 instead of needed 4:2:1.

(3) Increased consumer spending on unnecessary items → leads to inflation.

(4) Reduces overall growth and output.

They could be resolved through:

→ Rationalise subsidies
→ more DBT and social auditing
→ outcome budgets.

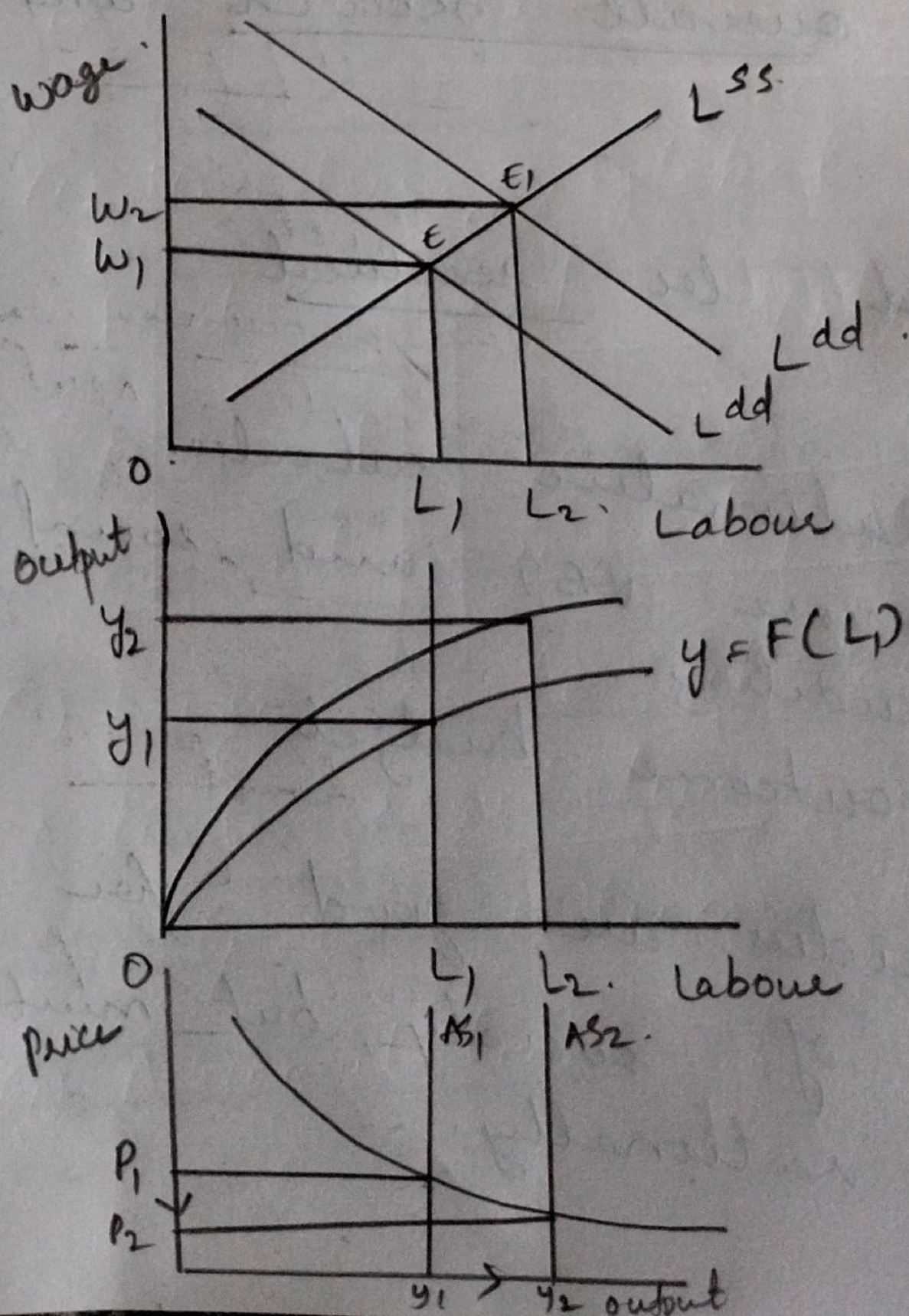
Subsidies are good for upliftment of society, but must be used rationally.

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Q.5 (b) How does equilibrium in classical model change with increase in labour demand if price and wage becomes rigid?

The Classical model rests with the assumptions of Say's law (supply creates its own demand), wage-price flexibility and Clasical dichotomy.

If price and wage becomes rigid with increase in labour demand:



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With rigid wage and price, if labour demand increases, more labour will be demanded and nominal wage increases but no change in labour supply.

The output increases from y_1 to y_2, ~~but~~ with nominal fwer reducing ~~so~~ from P_1 to P_2 and there is no change in real fwer and real wage

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Q.5 (c) What is friendshoring? How is it affecting the flow of trade and investment at global level in recent past?

Friendshoring refers to the phenomenon of directing trade of one country to only some specific country/countries to which it has more political or economic connections.

Effects on global level trade and investment

① Hindering global value chains and global supply chains.

② Reduced economies of scale for intra-industry trade.

③ Large scale absence of trade regulations → price & output determination affected.

④ Accumulation of wealth to

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specific countries

(5) Dollarisation increasing.

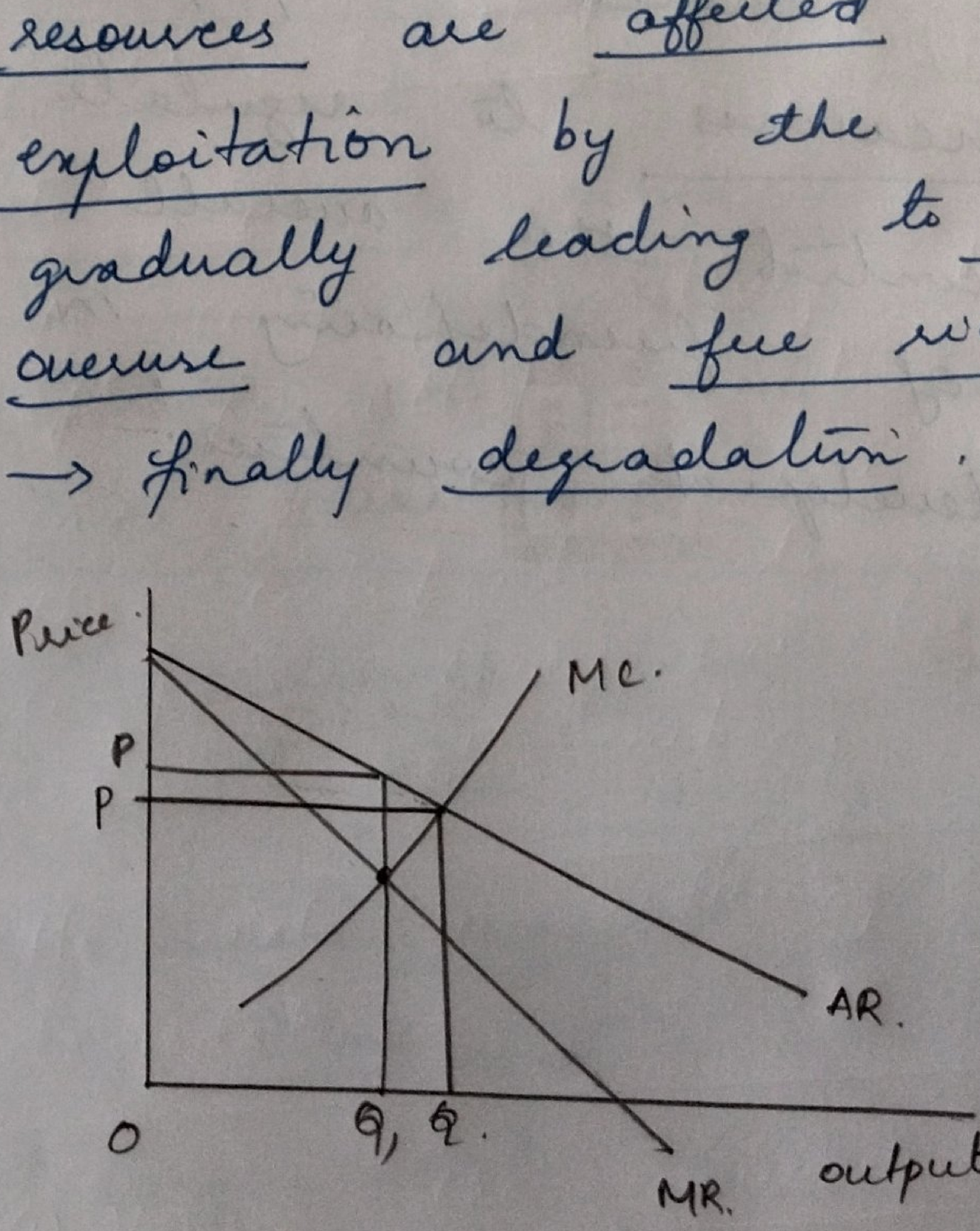
(6) Affecting overall global growth

Write measures to regulate and control the overall effect of frendshoring in less developed countries.

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Q.5 (d) Explain Tragedy of Commons.

Garret Hardin put forward the concept of tragedy of commons which says that the public resources or common pool of resources are affected by over-exploitation by the people gradually leading to their overuse and free wider problem → finally degradation.



According to the theory, in order to address the problem of tragedy of commons, there should be

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price set at ~~AR = Price~~ MC = MR (i.e., ~~Average~~ Marginal Cost) for efficient regulation of the issue. Earlier when fixed at a price of P = MC = AR it had led to the problem of tragedy of commons.

If marginal pricing, while paying a price, the users would be more able to understand the value and hence use the resource efficiently

The tragedy of commons is visible in many areas now — global sea, air — eh. hence, policies there should be and other of UNFCCC to treat them efficiently bodies

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Q.5 (e) What is carbon trading? How does it help in reducing environmental degradation?

Carbon trading refers to the trade of carbon certificates among individuals, companies and countries on the basis of carbon emitted by them.

For eg:

A company emitting less level than permitted levels of carbon can generate revenue by selling the certificates to another company that generates more amount of carbon.

Its role in reducing environmental degradation

① Valuing the environmental losses and attaching price to it - Similar to Pigouvian tax

② Encouragement through 'Pollu' incentivising environmental friendliness

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(3) Closely following 'Polluter pays principle' to realise objective of Common But Differentiated Responsibility.

(4) Encouraging to attach market value to the pollution and emissions.

(5) International cooperation could be involved in reducing environmental degradation.

Challenges
- → global level principle mining
- → Lack of regulation
- → Hindrance to systemic policy reforms.

The new PAT scheme with carbon trading regulations in Budget 2024 offers a fresh hope for India.

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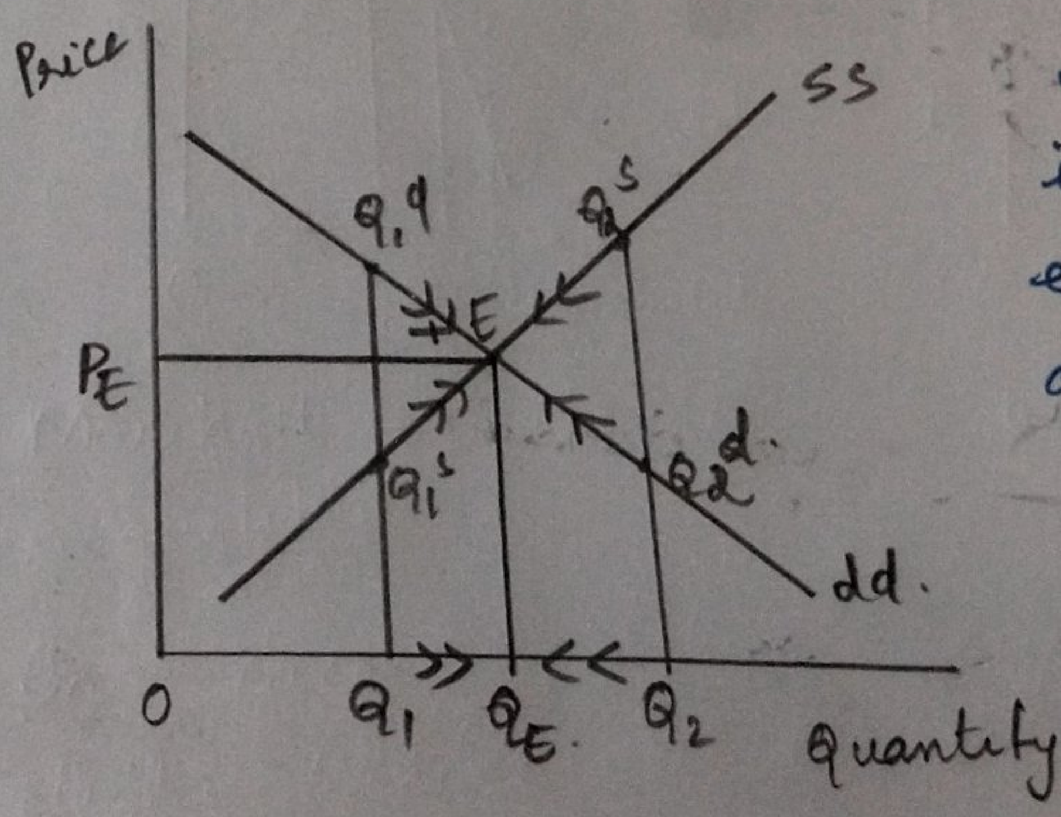
Q.8 (a) How is Marshall's partial equilibrium different from Walras? 15

The Partial equilibrium analysis refers to the determination of price and quantity in market equilibrium, keeping other factors constant.

Two methods were given by Marshall and Walras.

Marshall's partial equilibrium

It is based on quantity adjustment in the determination of equilibrium



Initial equilibrium is at E, with equilibrium price P_E and quantity Q_E.

Adjustment: If quantity is taken as Q_1, then ~~at~~ the willingness to buy is greater than willingness to sell ($Q_1^d > Q_1^s$) → as a result trade increases from Q_1 to Q_E.

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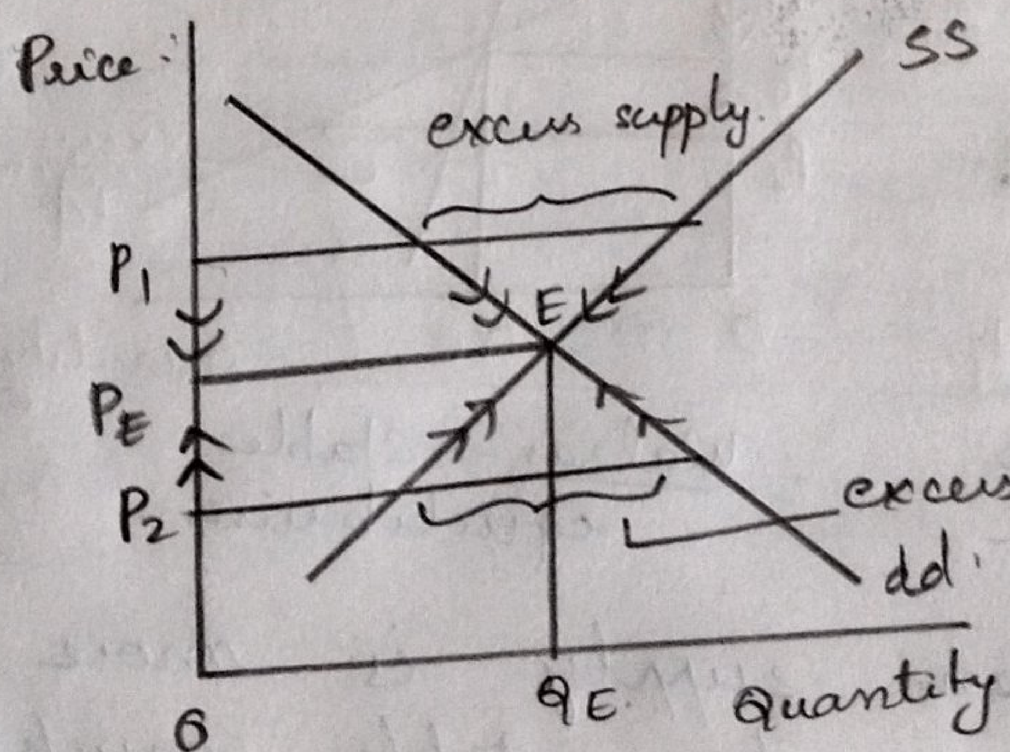
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If the quantity at present is Q_2, willingness to sell is greater than willingness to buy ($Q_2^S > Q_2^d$), therefore quantity traded decreases from Q_2 to Q_E.

Through both these adjustments, equilibrium is attained.

Walras Partial equilibrium

It is based on price adjustment to reach equilibrium.



Initial equilibrium is at E, with equilibrium price P_E & quantity Q_E.

Adjustment: If price is at P_1 → excess supply of goods → price decreases from P_1 to P_E.

If price is at P_2 → presence of excess demand → price increases from P_2 to P_E.

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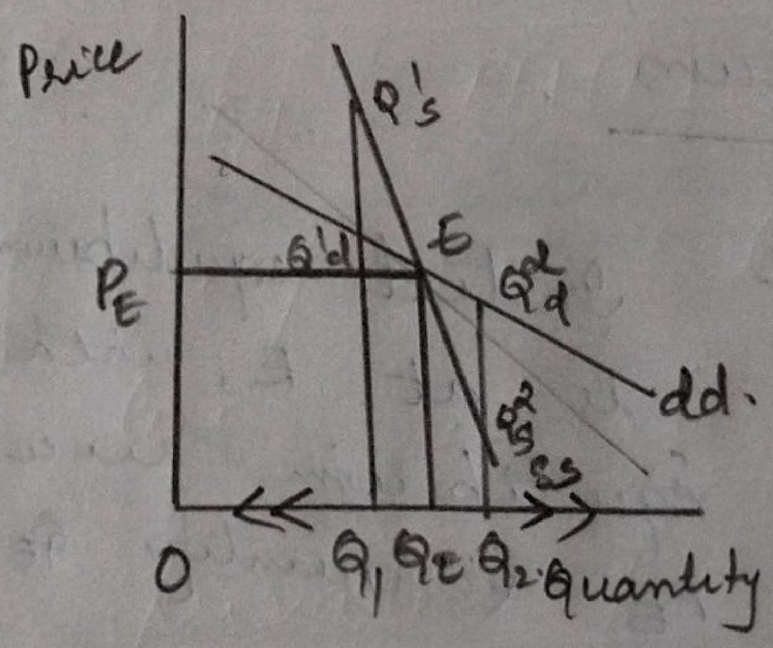
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Hence, the equilibrium is reached.

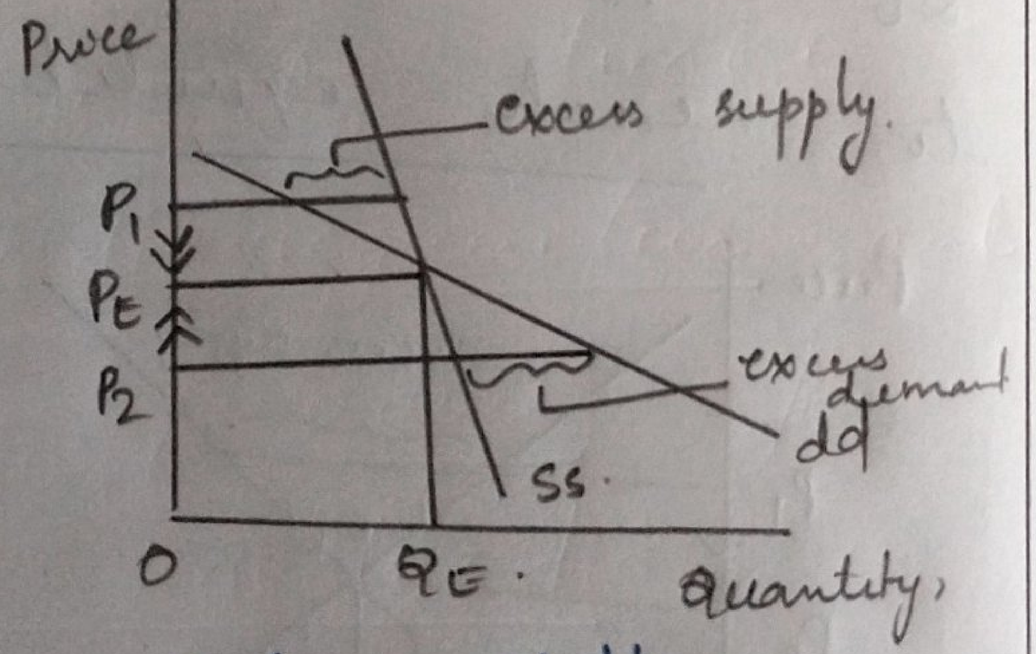
Stability & instability in Marshall's & Walras' equilibrium

- This is based on downward sloping demand and supply curves and their elasticities.

Case 1 - Demand is more elastic than supply.



Marshall → unstable equilibrium



Walras → stable equilibrium.

In case 2, when supply is more elastic there will be stable equilibrium in Marshall and unstable equilibrium in Walras.

Hence Marshallian and Walrasian analysis are important in present context for partial equilibrium analysis.

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Q.8 (b) Critically analyse the role of Public Private Partnership in development. 15

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The Public Private Partnership is the method of funding development projects through public and private funds and mutual relation.

(eg) Private → provide funds
+
Public → provide institutions or regulations.

Some types of PPP models

- Build-operate-Transfer model (building, operating by private people and handing over to government later)
- Hybrid Annuity model (Partial funding by government and operating rowers to private)
- Engineering procurement model (only taking technical help from private companies).

Role of PPP in development

Positive Role

(i) Helps in cumulating funds

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at one go for the projects.

② Easy allocation of resources from market through market mechanism

③ Easy procurement of resources for building infrastructure.

④ Faster completion of projects.
(eg) National Highways built by NHAI in less time.

⑤ Improved land acquisition and less regulatory procedures for private firms involved.

⑥ Easy making of revenue by ~~Negative~~ Government.
(eg) National monetisation pipeline — about ₹3.8 lakh crore mobilised in 2 years.

Negative Role

① Profit motivated rather than

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welfare oriented.

② ~~Improved~~ Less accountability mechanisms for the product.

③ Issues of corruption and loss of government credibility

④ Contracting to close private parties by officials.

④ Issue regarding sub-contracting issues.

⑤ High cost for the consumers to avail public service.

PPP model can be leveraged through efficient regulatory mechanisms with better coordination from ministries and departments.

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Q.8 (c) Compare the impact of quota on import and equivalent tariff in case of monopoly and perfect competition. 20

Quota and Tariff are types of protection measures to regulate trade in an economy.

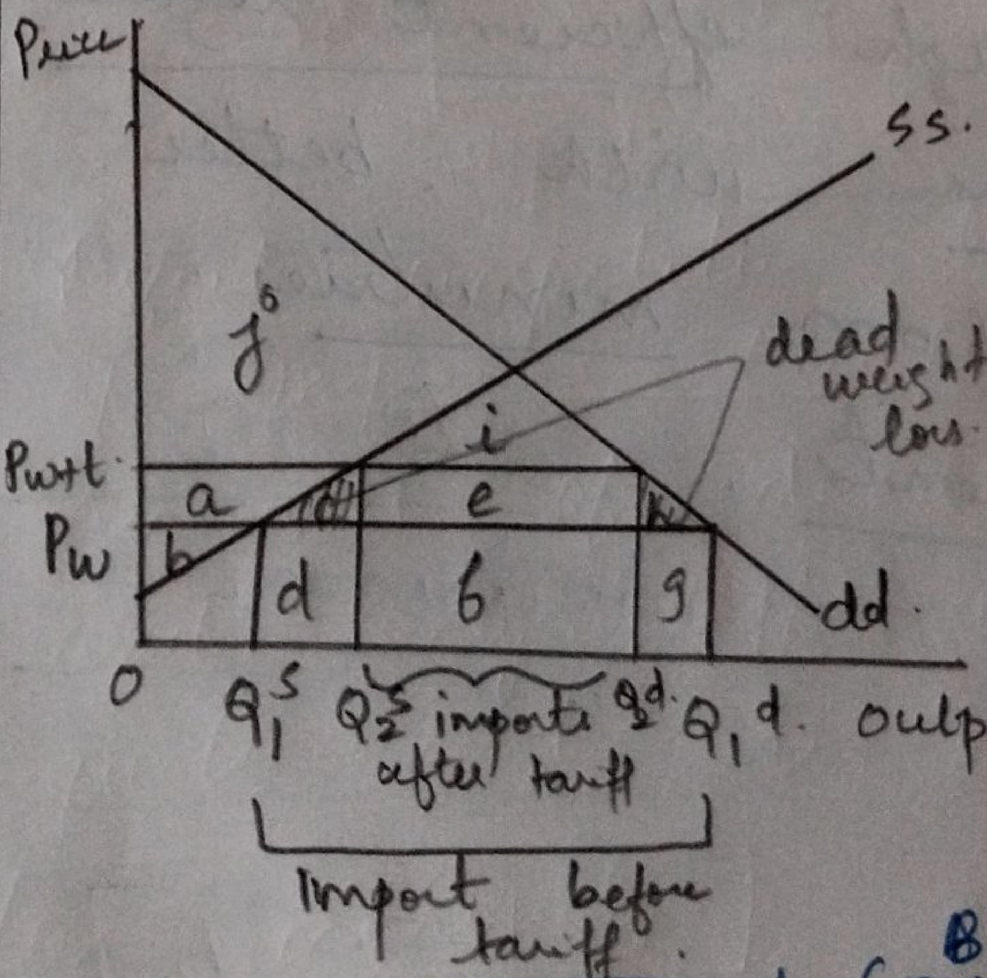
Quota → Quantitative restrictions on import.

Tariff → Price restrictions on import.

It's effects differs in both perfect competition & monopoly

Effect of tariff

Perfect competition:



Pw → world price

Pw+t → new price after tariff.

Q_2^s Q_2^d → new imports after tariff.

Welfare loss:

	Before tariff	After tariff
C.S	a+c+e+h+i+j	j+i.
P.S	b	g+b
Gov. revenue		e

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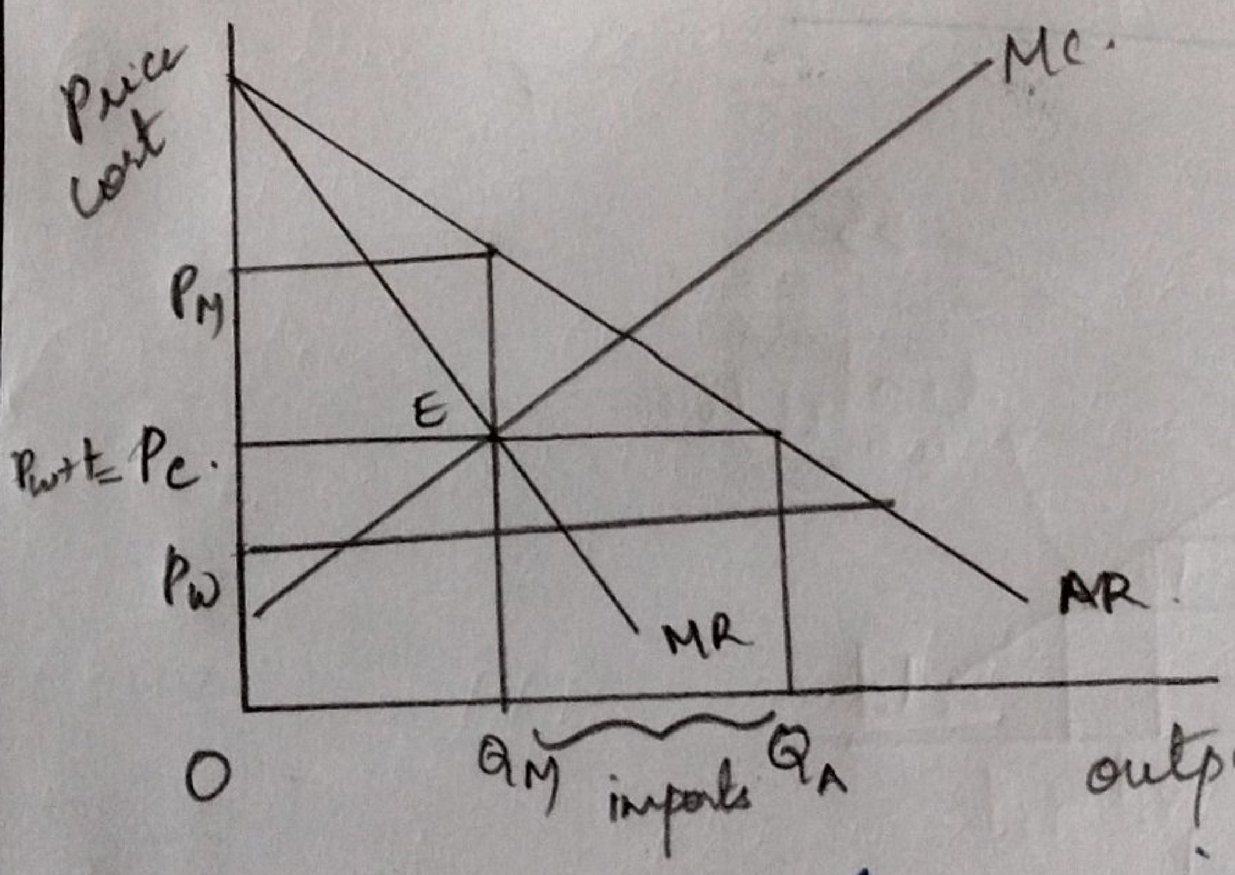
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~~Welfare loss ⇒ $j+i+j+e-(a+c+e+h+i+j+a+j)$~~

Welfare difference = $j+i+a+b+e-(a+c+e+h+x+j+b)$

Deadweight loss = $\boxed{c+h}$ ⇒ consumer distortion + producer distortion loss

Monopoly



If under monopoly, original price would have been P_M at quantity Q_M. (But due to tariff imposition, (MC=MR) the monopolist will lose the market if he/she sets a price P_M, because the price after tariff is set at $P_c(P_w+t)$, allowing for $Q_M Q_A$ imports

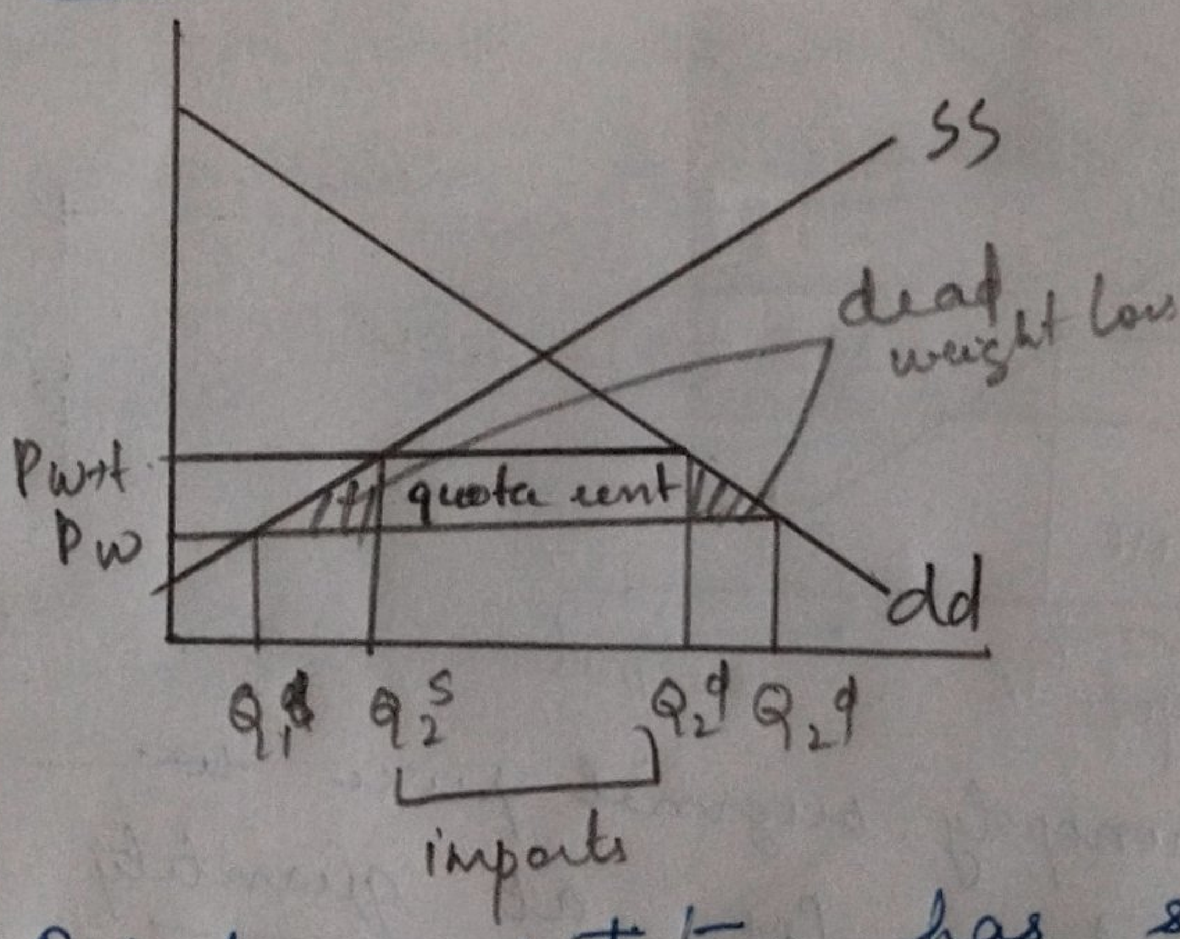
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Hence monopolist would loss if he sets higher price above P_c. So monopolist will set price at $P_c = MC$ and ~~and~~ do not have any gains.

Effect of quota

On Perfect competition



Perfect competition has same results of <u>imposing tariff</u> → ie., same amount of dead weight loss and only difference is ~~price~~ revenue of quota rent as shown above.

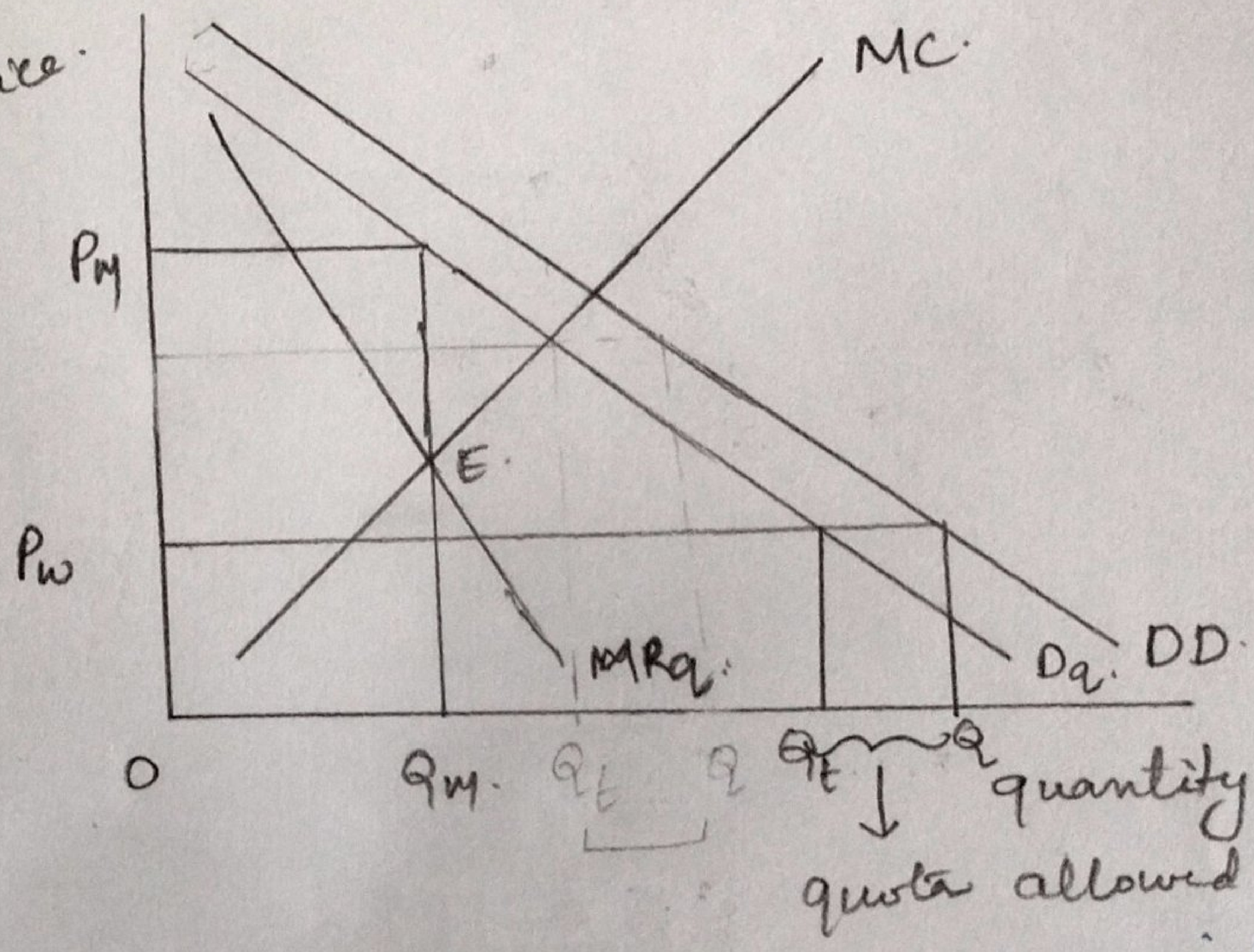
On monopoly

The case is different - The

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monopolist gains from imposing quota than tariff.



In case of quota, the original demand curve is DD, but due to imposition of quota, the domestic demand curve become Dq, as a result, the monopolist can attract profits by supplying Q_M quantity at P_M firms and give rest market $Q_M Q_t$ to other sellers

Therefore, a monopolist can have more market power in case of quota than tariff.