

## M C - R & U - Reason-Based Questions

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**Q.1. A seller under monopolistically competitive market has full control over price.**

**Ans.** False. Under monopolistically competitive market, a seller has a partial control over price through product differentiation. However, full control over price is not possible owing to the fact that there is a large number of close substitutes in the market.

**Q.2. Demand curve facing a monopolistically competitive firm is likely to be very elastic.**

**Ans.** True. Because, the products produced by the monopolistically competitive firms are close substitutes to each other. If products are close substitutes to each other, the elasticity of demand is high.

**Q.3. Under monopolistic competition, elasticity of demand for the product is greater than under monopoly.**

**Ans.** True. Under monopolistic competition, elasticity of demand for the product is greater than under monopoly. Because under monopoly, there are no close substitutes of the monopoly product while under monopolistic competition, there is a large number of close substitutes.

**Q.4. In the long run with free entry and exit, firms under monopolistic competition earn zero abnormal profits.**

**Ans.** True. In the long run, all firms under monopolistic competition earn only normal profits (or zero abnormal profits). The reason is as under:

**(i)** If firms earn abnormal profits, new firms will be attracted to the industry. As a result, total supply will increase, market price will reduce and abnormal profits will vanish.

**(ii)** New firms will lower the price to create more demand for their product. Consequently, old firms too have to lower the price of their products. Thus, there will be fall in price of both old and new firms and ultimately, they will get only normal profits.

**(iii)** When new firms join the industry, demand for factors of production increases. This should push up factor cost and consequently, the average cost of production. Accordingly, abnormal profits would disappear.

**Q.5. A firm under monopolistic competition enjoys complete monopoly power in the market.**

**Ans.** False. A firm under monopolistic competition does not enjoy complete monopoly power in the market. It only enjoys partial monopoly power. Complete monopoly power arises when a firm has full control over price of the product. It does not happen under monopolistic competition. A firm under monopolistic competition exercises only partial control over price through product differentiation. Accordingly, it does not enjoy complete monopoly power, but only some degree of it.