Exercise walk-through

Growth and survival of firms ▪ 7.7

eXercise

You must be able to

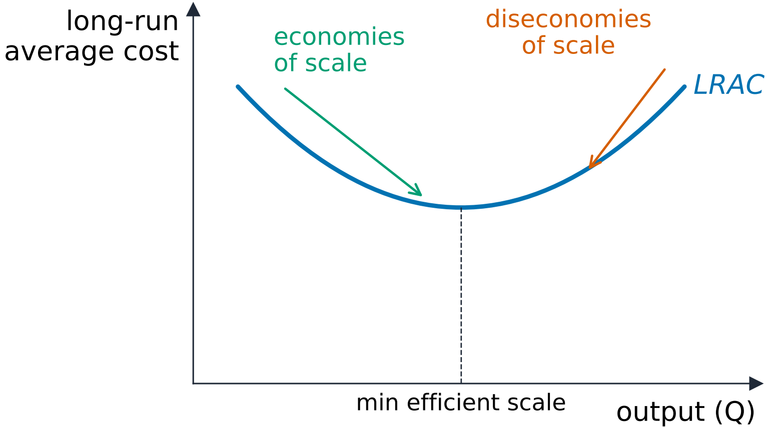
- distinguish internal from external growth and the types of integration
- explain why some firms stay small
- analyse barriers to entry and exit

Method — How firms grow

- **Internal growth 内部增长** (organic): sell more. **External growth 外部增长**: a **merger 合并** / takeover.
- **Horizontal 横向** (same stage), **vertical 纵向** (different stage), **conglomerate 混合** (different industry $\rightarrow$ spread risk).
- **Stay small:** small/local market, owner wants control, few economies of scale, **niche 利基**.
- **Barriers to exit 退出壁垒** (e.g. costly machines) can trap a firm in a loss-making market.

Answer shapes: AO1 + AO2 + AO3 (analysis) + AO4 (a supported judgement *in context*).

Method — How firms grow



Long-run average cost falls with economies of scale, then rises

Method — How firms grow

Many firms (perfect competition) at one end; one firm (monopoly) at the other

Practice 2.1 ▪ 2 marks

State the difference between internal and external growth.

Solution 2.1

Method: How firms grow

Worked steps

internal growth is a firm growing bigger by selling more itself; external growth is joining with another firm through a merger or takeover (2 for a clear difference; 1 for a partial idea).

Practice 2.2 ▪ 2 marks

Define the term *vertical integration*.

Solution 2.2

Worked steps

joining with a firm at a different stage of the same production process (e.g. a maker buying a supplier) (2 for a clear definition; 1 for a partial idea).

Practice 2.3 ▪ 1 mark

State one reason why a firm might stay small.

Solution 2.3

Method: How firms grow

Worked steps

any one of: the market is small/local; the owner wants to keep control; there are few economies of scale; it serves a niche (1).

Exam-style 3.1 ▪ 1 mark

A car manufacturer buying a tyre producer is an example of:

- **A** horizontal integration
- **B** vertical integration
- **C** conglomerate integration
- **D** internal growth

Solution 3.1

A horizontal integration

B vertical integration ✓

C conglomerate integration

D internal growth

Worked steps

B. Joining a firm at a different stage is vertical integration.

Exam-style 3.2 ▪ 6 marks

Explain two reasons why many small firms are able to survive in a market dominated by large firms.

Solution 3.2

Method: How firms grow

Worked steps

[6] For **each** of two reasons: AO1 1 + AO3 up to 2 — e.g. *niche/personal service*: small firms serve a specialised market the giants ignore → loyal customers → they survive. *Few economies of scale*: in some industries large size brings little cost advantage → small firms compete on equal terms. Maximum 3 each.

Exam-style 3.3 ▪ 12 marks

Discuss whether all firms should aim to grow as large as possible.

Solution 3.3

Method: How firms grow

Worked steps

[12] AO1/AO2/AO3 up to 8 + AO4 up to 4. **For growth:** economies of scale lower costs, more market power and profit, and survival. **Against:** diseconomies of scale raise costs beyond the optimum, growth needs finance and is risky, and many owners value control or serve a niche better when small. Judgement: growth suits firms that gain real economies of scale, but staying small is rational for niche or owner-controlled firms — it depends on the industry and the owner's aims.