

LEARNING UNIT 9

- **DATE:** 2014
- **MODULE:** PMIC6111
- **TEXTBOOK REFERENCE:** P241
- **THEME:** Monopoly and imperfect competition

- **OBJECTIVES:** BY END OF LEARNING UNIT 9– YOU SHOULD KNOW THE FOLLOWING:

LEARNING UNIT 9

Monopoly

- **Monopoly** – there is only one seller of a good or service that has no close substitutes

LEARNING UNIT 9

➤ *Barriers to entry:*

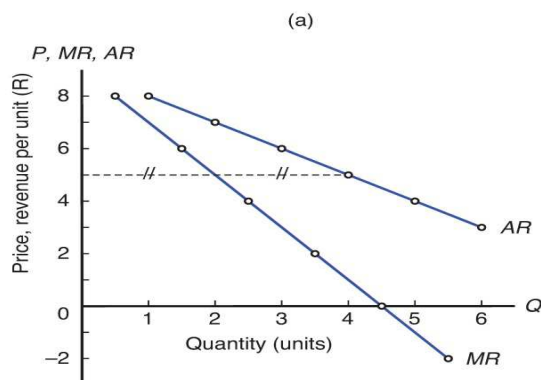
- Natural monopoly, economies of scale
- Limited size of the market
- Exclusive ownership of raw materials
- Patents
- Licensing
- Sole rights
- Import restrictions
- Firms can create their own barriers

(*Examples:* predatory pricing, excess capacity)

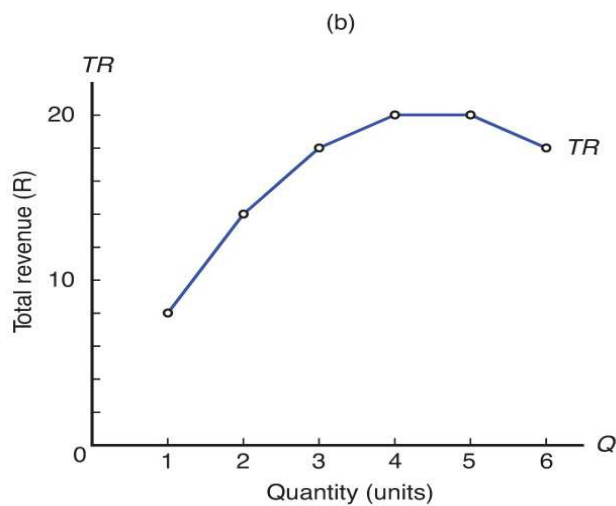
LEARNING UNIT 9

- *Revenue:* TR, AR and MR under monopoly

Marginal, average and total revenue under monopoly (and imperfect competition)



LEARNING UNIT 9

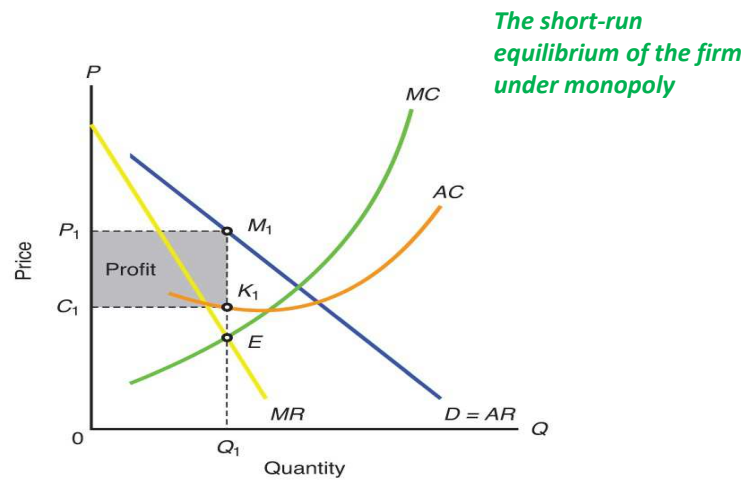


LEARNING UNIT 9

Quantity	Average revenue (R) AR (or price P)	Total revenue (R) TR (= PQ)	Marginal revenue (R) MR
0	0	0	
1	8	8	8
2	7	14	6
3	6	18	4
4	5	20	2
5	4	20	0
6	3	18	-2

Average, total and marginal revenue when the demand curve for the product of the firm slopes downward: a numerical example

LEARNING UNIT 9



LEARNING UNIT 9

➤ *Price discrimination:*

- First-degree price discrimination - product
- Second-degree price discrimination - quantities
- Third-degree price discrimination - buyers

LEARNING UNIT 9

Monopolistic competition

- *Monopolistically competitive market* – a large number of firms produce similar but slightly different products
- *Differentiated (or heterogeneous) product* – different varieties of a product
- Price competition and non-price competition

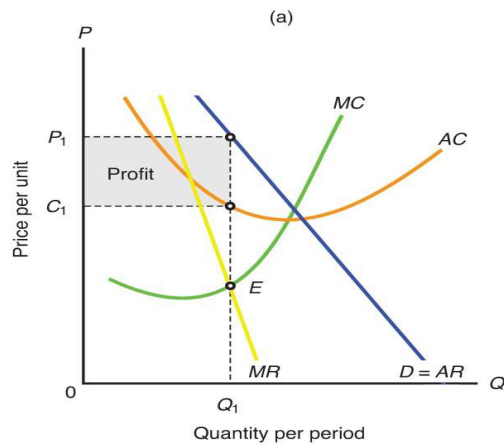
LEARNING UNIT 9

- *Salient features of monopolistic competition:*
 - Each firm produces a distinctive, differentiated product
 - Each firm faces a downward-sloping demand curve for its particular product
 - There are a large number of firms in the industry
 - There are no barriers to entry or exit

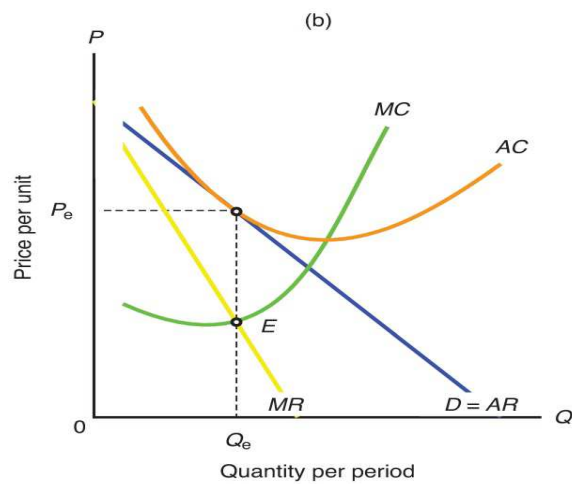
LEARNING UNIT 9

➤ Equilibrium position

The equilibrium of the firm under monopolistic competition



LEARNING UNIT 9



LEARNING UNIT 9

Oligopoly

- *Oligopoly* – a few large firms dominate the market
- *Duopoly* – there are only two firms in the market

LEARNING UNIT 9

The main features

- high degree of interdependence between the firms
- uncertainty
- barriers to entry

Two strategies:

- Collusion – conditions.
- Competition – normally not price competition.

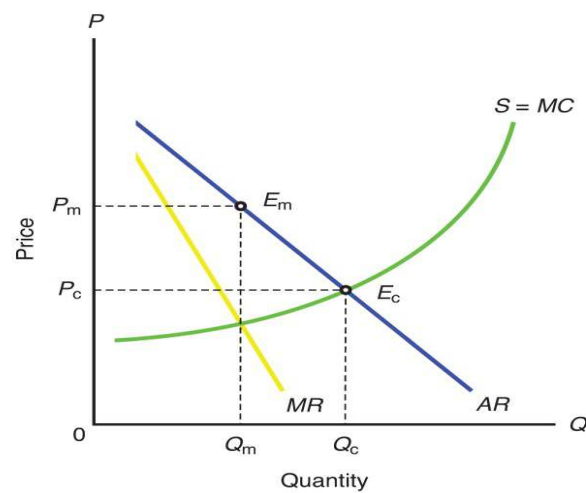
LEARNING UNIT 9

Comparison of monopoly and imperfect competition with perfect competition

Monopoly vs. perfect competition

If the industry is a monopoly, the price will be higher and the output lower than if perfect competition prevails

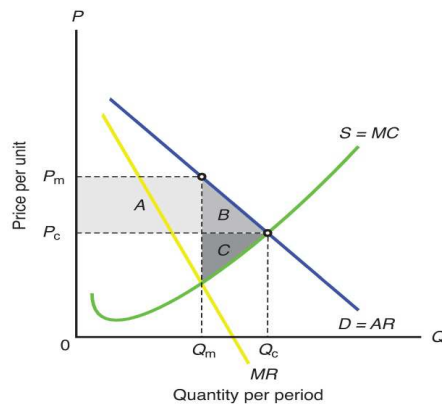
LEARNING UNIT 9



LEARNING UNIT 9

Social costs of a monopoly

Dead-weight loss to society



The social costs of monopoly

LEARNING UNIT 9

Popular misconceptions about a monopoly:

- Can charge virtually any price it wants
- Can charge the highest price it can get
- Guaranteed an economic profit
- Has almost absolute economic power

LEARNING UNIT 9

The case against monopoly (bigness):

- Output is lower and price is higher
- Little or no incentive for innovation
- Managerial inefficiency
- Questionable quality of products or service
- Unfair or socially unacceptable distribution of income and wealth
- Rent-seeking behaviour
- Economic power, politically powerful