Monopolies Cheat Sheet

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Monopoly definition

The only seller of a good or service which does not have a close substitute.	
Narrow definition	A firm is a monopoly if it can ignore the actions of all other firms.
Broad definition	Other firms in the market are not close enough substitutes

Monopolistic competition

A market structure in which barriers to entry are low, and many firms compete by selling similar, but not identical, products. Difference may be real or artificial.	
Has downward-sloping demand and marginal revenue curves. Small amount of control over price.	
Oligopoly: A market structure in which a small number of interdependent firms compete.	
Every firm that **has the ability** to affect the price of the good or service it sells will have a **marginal revenue curve** that is **below** its demand curve.	
Easy entry and exit to the market	
Highly but not perfectly elastic.	
How monopoloisticaly comp firm maximises profit in the **short run**	1. Calculate Profit = (P - ATC) x Q
	2. Profit is maximised or loss is minimised when MR = MC
May make money, lose money, or break even.	
Long run	
Entry of new firms	Demand will go down (left)

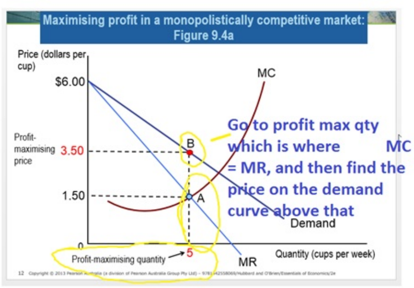
Monopolistic competition (cont)

Will sell fewer products at every price
Demand curve will become more elastic

Four main reasons monopolies arise

Four reasons for high barriers to entry	
Government blocks the entry of more than one firm into a market.	By granting a patent or copyright or By granting a firm a public franchise, which makes it the exclusive legal provider of a good or service.
Control of a key raw material	
Network externalities	Product usefulness increases with number users
Natural monopoly	Economies of scale are so large one firm has a natural monopoly

Maximise profit in monopolistic competition



Price and output decision

Max profit is where marginal revenue = marginal cost	MR = MC
Like every other firm	
Demand curve = product demand curve	
Price Maker	
With a natural monopoly, the average total cost curve is still falling when it crosses the demand curve	

Monopoly affect on economic efficiency?

Will produce less and charge a higher price than a perfectly competitive industry
Causes a reduction in consumer surplus
Causes an increase in producer surplus
Dauses a deadweight loss (allocative inefficiency)
Increases market power (ability to charge higher than marginal cost)
Firms with market power are more likely to earn economic profits, so because R & D requires $$$ they are also more likely to introduce new products

Equilibrium in a perfectly competitive market results in the greatest amount of economic surplus, or total benefit to society