OUTLINE — October 2, 2017

- Market Failure
- Monopoly
- Oligopoly
- Monopolistic Competition

PS 2 distributed today, due Wed/Thurs Oct 11/12
Exam to be discussed in section today/tomorrow

Big Bottom Line of First Third of Course

- In perfect competition,
  in the long run,
  firms produce profit-maximizing quantity
  where p = MC
  and ATC is minimized

"Market Failure"

- If any of these assumptions isn't satisfied…
  - perfect competition
  - profit maximization
  - utility maximization
  - well-defined private property rights
  - full information
- …then markets "fail" . . .
  - . . . to produce q* where p = MC

Market Failure

- Four sources of market failure
  - Imperfect Competition
  - Externalities
  - Public Goods
  - Imperfect (Asymmetric) Information

Market Failure: Imperfect Competition

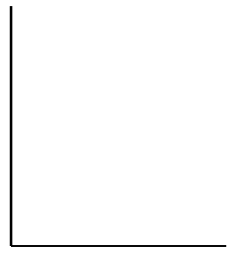
- Monopoly
  - One firm
  - No close substitutes
  - Barriers to entry
    - Patents
    - Government franchises
    - Owning scarce resource
    - Economies of scale
    - Illegal means

Monopoly

- Goal: max profit π = TR – TC
- Max profit when choose q so that MR = MC
- But, MR is not constant for a monopolist

Profit Maximization

P	q_d	TR	MR
10	0		
9	4		
8	8		
7	12		
6	16		
5	20		
4	24		



Marginal Revenue, in general

Choose q so that MR = MC

Profit Earned by (single-price) Monopolist

Monopoly vs. Perfect Competition

Price Discrimination by a Monopolist

Oligopoly

- Few firms in a concentrated industry
  - ➜ top 4 firms sell over 90%
  - ➜ power to influence price
- Product may be homogeneous or heterogeneous
- Key: inter-dependence of firms
- *Suggestion: Take Econ 121*

Monopolistic Competition

- Lots of firms
- No barriers to entry/exit
- *Heterogeneous* product

Profit Maximization

- Max profit when choose q so that MR = MC

Entry erodes profit

Long-Run Equilibrium

Effect of increased variable cost?