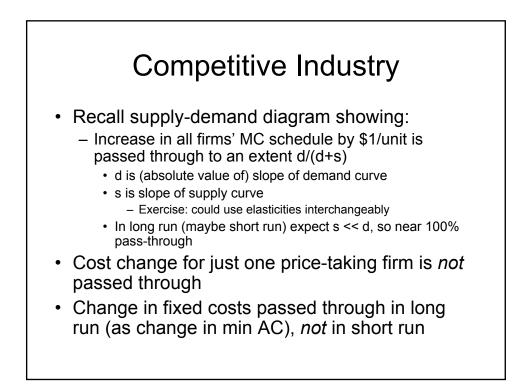
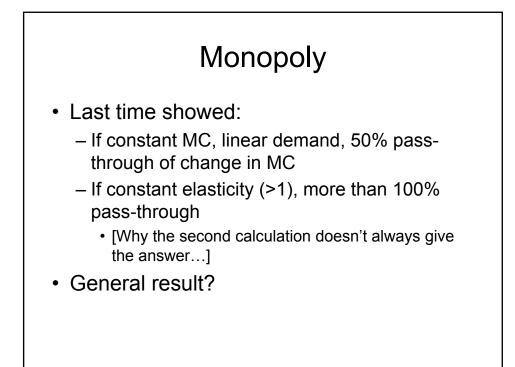
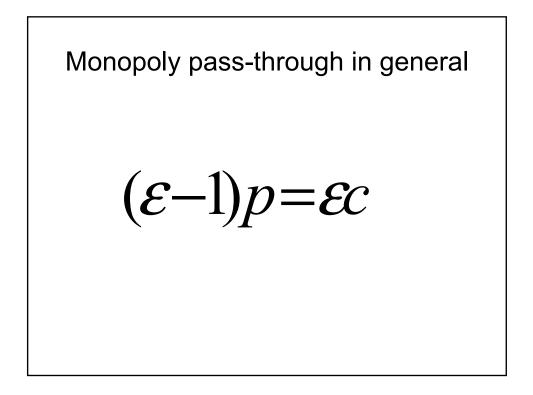
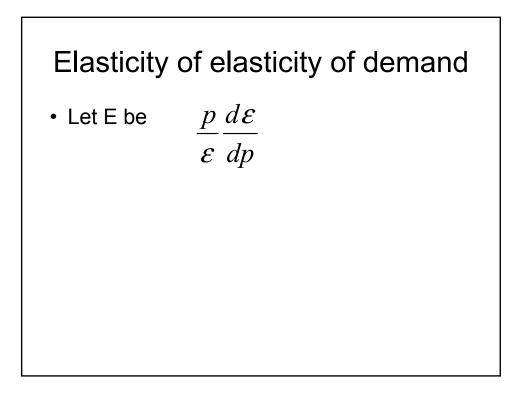
Pass-Through and Market Power

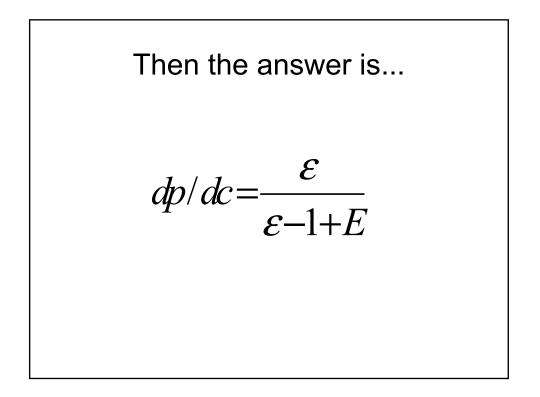
Economics 121 Spring 2006 Joseph Farrell





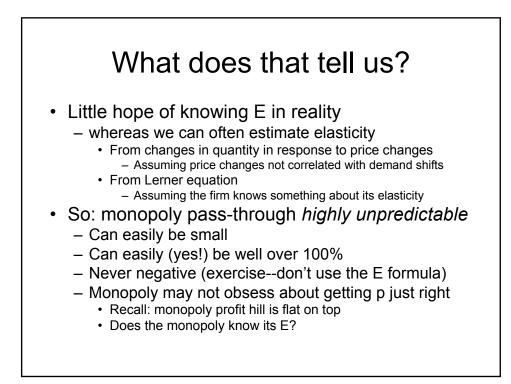






How can we check?

- Constant elasticity certainly implies E=0
- · Formula is correct then
- · Can you think of other checks?
 - Calculate [epsilon] and E for linear demand



Effect on firms

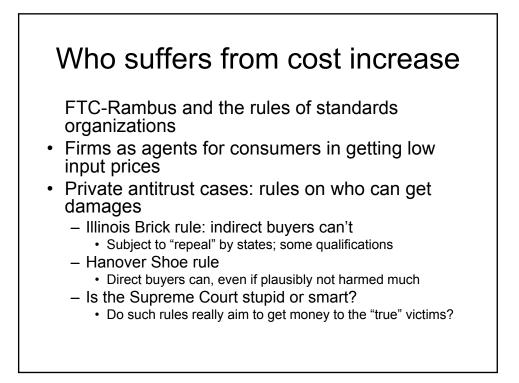
- Asked about effect on downstream buyers
- But how much do firms care about cost increases when there is pass-through?
- "Monopoly can just pass it through"

Effect on competitive firms

- Cost effect: lose Q dc
- Price effect: gain Q dp
- Why can we calculate as if firm keeps Q?
- Consumers lose Q* dp
- So firms plus consumers total lose Q* dc

Effect on Monopoly

- Monopoly loses Q* dc
- Why not a countervailing price effect?
 - Balanced by quantity effect-not chosen optimally
 - Monopoly could have changed price/output before, so that doesn't help much
- · Consumers also lose!
- Total loss more than Q* dc
 - Maybe much more... more than twice...
 - No simple adding-up as in competitive case



Next Topic

- Cartels and collusion
- Read CP chapter 5, 122-150