

Oligopoly 4

Midterm 2

- Answer key will be posted today
- Graded exams not yet ready; I hope for Thursday
 - Question 3(c) seemed problematic
 - Two equations:
 - profit maximization
 - zero profits

What the data say

- More competitors, lower concentration mostly seems to lower markups
- But lots of “noise”
- Much of the correlation comes at highest levels of concentration
 - Three major rivals often “almost enough”? Four?
- Much due to high profitability of leading firm
 - Intra-industry correlation between share and profitability

Look at Price not Profit?

- Look for markets where can compare price, concentration
 - Local markets: retailing, banking, hospitals...
 - Changes over time
 - Airlines
- Again, higher concentration raises prices, but often less so than Cournot model would suggest

“Modern Methods” in SCP

- Read CP chapter 8 on this
- Why I’m skeptical
 - Relies heavily on strong assumptions about consumer and firm optimization
 - Recall our calculations about profit function
 - Ignores dynamics
 - So does a lot of oligopoly theory, but might hope the econometrics wouldn’t
- Remember CP using “performance” to mean low profits

Bresnahan-Reiss

- CP page 78
- Entry against a monopoly or duopoly lowers price very noticeably
- Entry into oligopoly with 3+ firms doesn’t do nearly so much
 - “Workable competition” with 3+ firms?
 - Statistical significance
 - “Very big” markets
- Is subsequent entry wasteful?

Endogenous Sunk Costs

- What if F rises with market size?
- Especially likely if fierce competition
 - Fierce competition can encourage high concentration—contrast reverse causation
- Innovation, product quality, network effects
- Big markets more competitive or higher quality or both?
 - Contrast traditional economics of “trade”

Welfare Economics of Entry

- Externality (usually good) on consumers
- Externality (usually bad) on incumbents
- Balance?
 - Price effect; other consumer benefits
 - “Business-stealing” effect
 - Monopolistic competition
 - Is muted price effect due to real variety?
- Policy on entry

What's Next

- Enough (for now) on simple imperfect competition
- CP part 3
 - Business practices: Strategies and Conduct
 - Read Chapter 9: price discrimination
 - CP stress monopoly case: why?