

Chapter 9

Monopoly

These slides supplement the textbook, but should not replace reading the textbook

What are the four types of markets?

- Perfect competition
- Monopoly
- Monopolistic competition
- Oligopoly

What is a monopoly firm?

The only seller of a
good or service with
no close substitutes

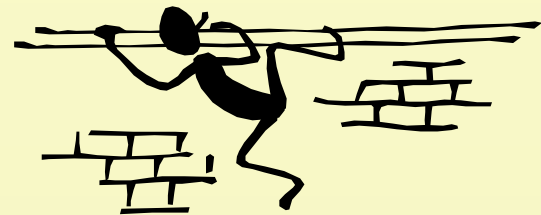
What is a monopoly market?

A market in which the monopoly firm operates



What is a barrier to entry?

Any impediment that prevents new firms from competing on an equal basis with existing firms in an industry



What are some examples of a barrier to entry?

- Legal restrictions
- Economies of scale
- Control of essential resources

**Can a monopoly make
an economic profit in
the long run?**

Yes!



**Because of these
barriers to entry**

What is a patent?

A legal barrier to entry that conveys to its holders the exclusive right to supply a product for 20 years

What is an innovation?

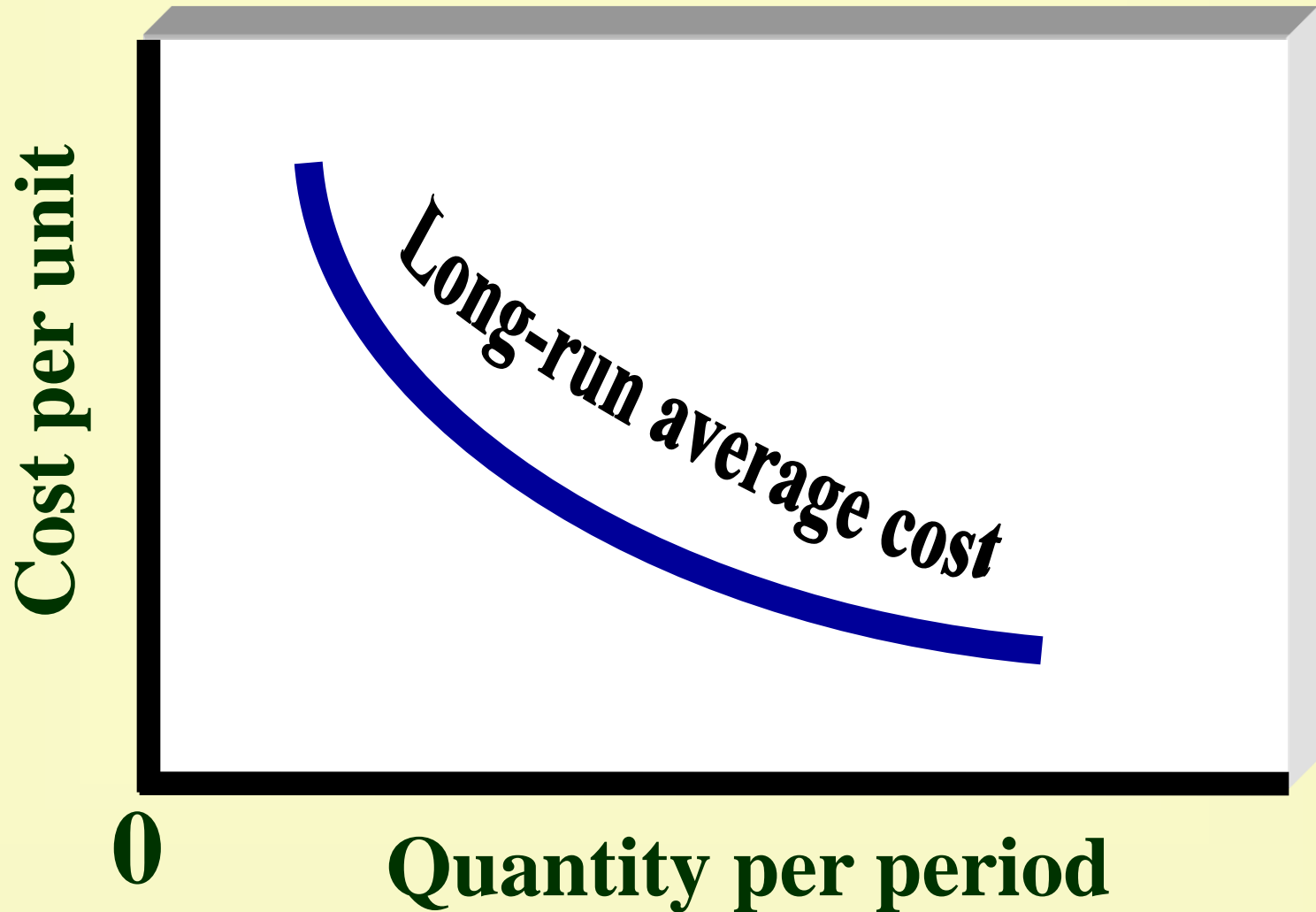
The process of turning an invention into a marketable product



When does a firm experience economies of scale?

When a firm increase
resources in the long
run and efficiency
increases

Economies of Scale as Barriers to Entry



What is a price searcher?

A firm that has some control over the price it charges because its demand curve slopes downward



What is a single price monopoly?

A Monopoly firm that is limited to charging the same price for each unit of output sold

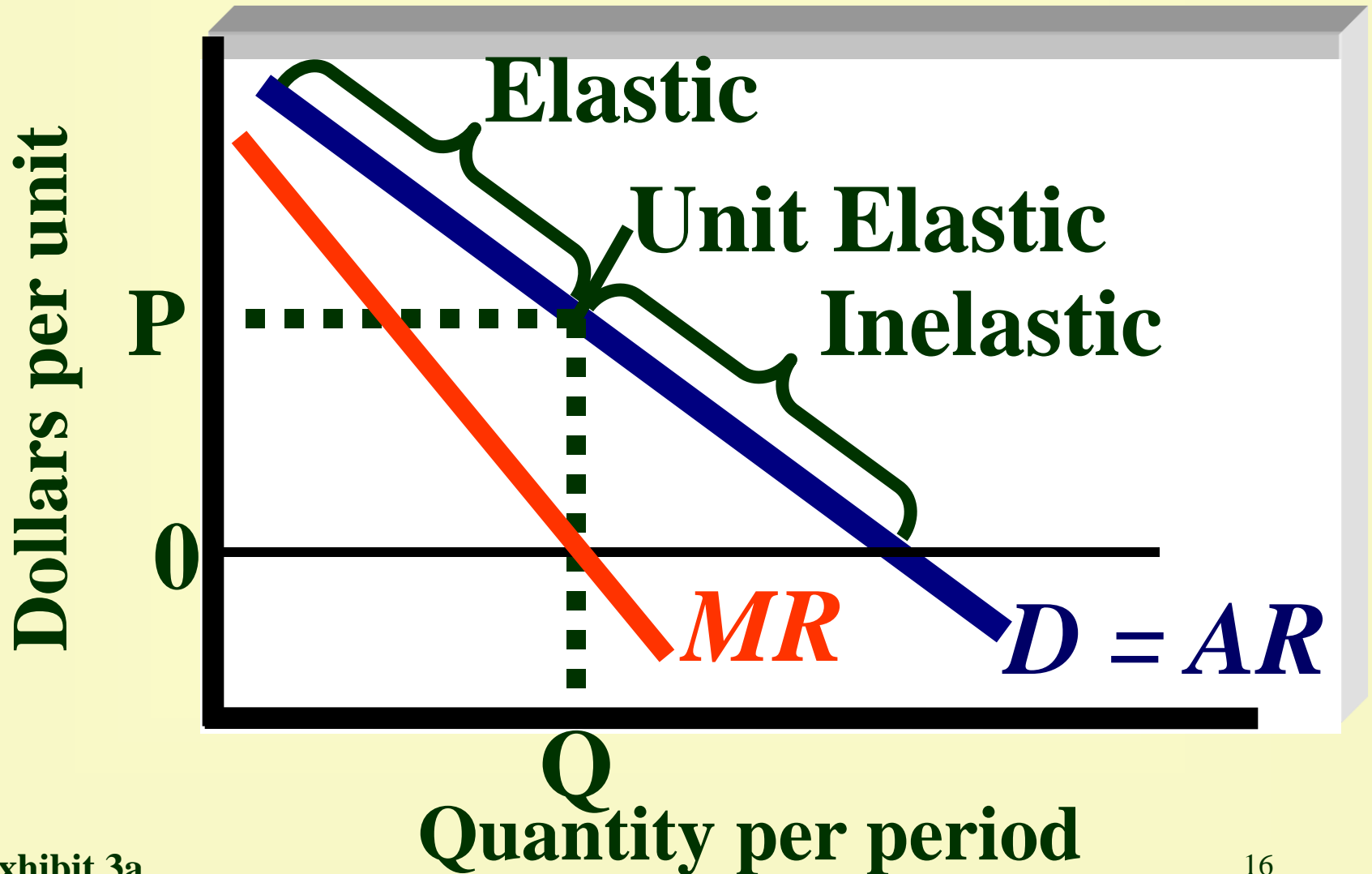
What is the monopolist's demand curve?

The market demand curve

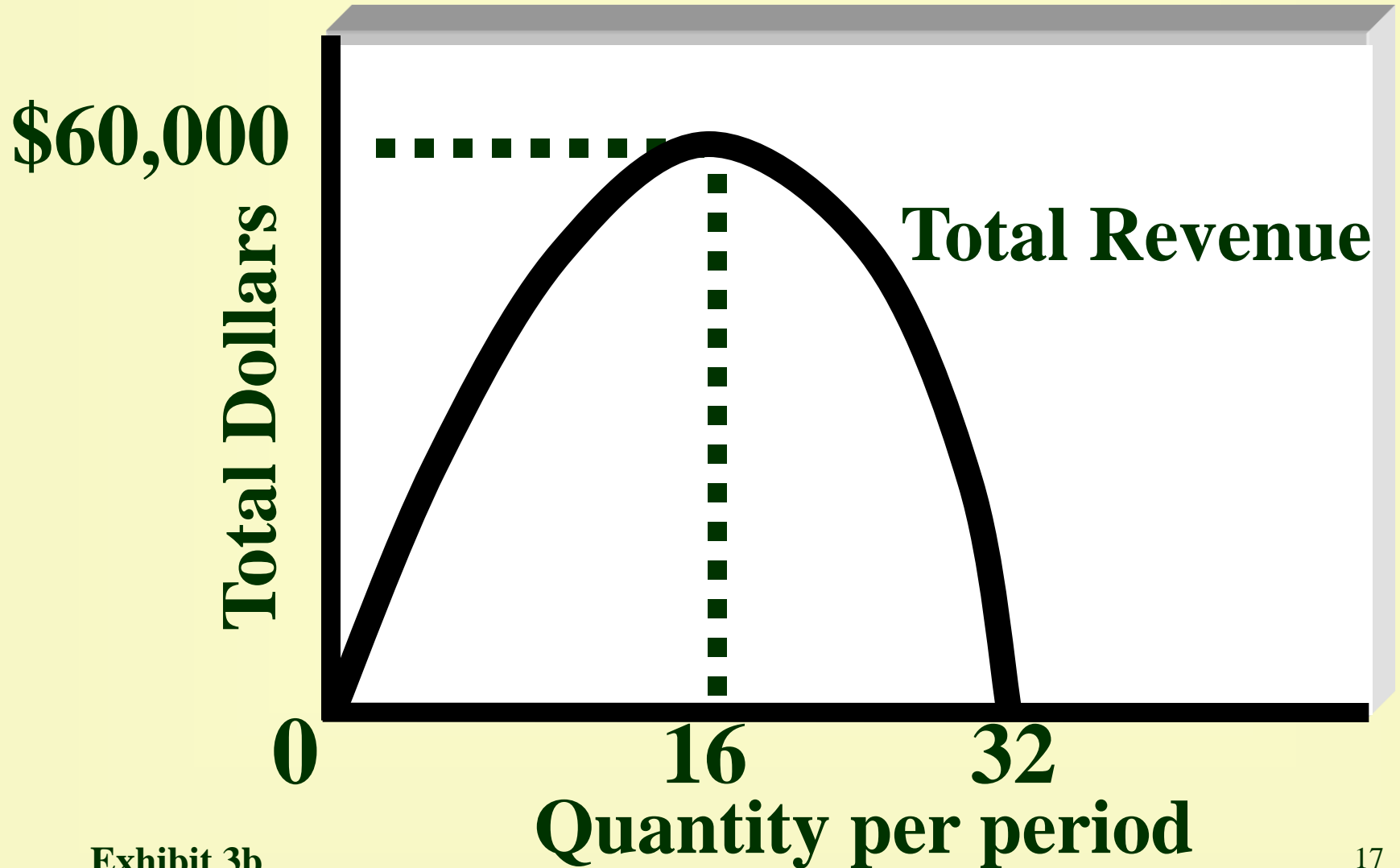
How is the demand curve derived for the single price monopoly?

It's average revenue curve

Monopoly Demand Loss & Gain in Total Revenue from Selling One More Unit



Monopoly Demand Loss & Gain in Total Revenue from Selling One More Unit

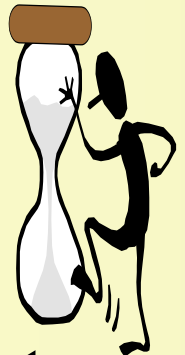


What is a natural monopoly?

Due to economies of scale, one firm can operate at lower average cost than can two or more firms

How does the government foster monopolies?

- Patents, trademarks, copyrights
- Exclusive government franchises

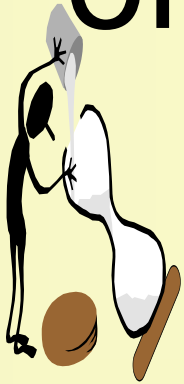


What is the purpose of patents and copyrights?

To give people and firms the incentive to invest their time and money into new products and creative works

What is a government franchise?

A government granted
right to be the sole seller
of a product or service



When does the government grant a franchise?

When it thinks the market in question is a *natural monopoly*

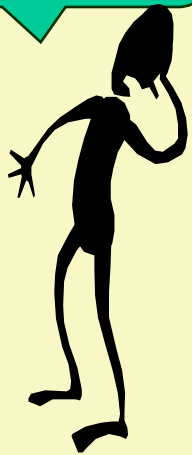


What are examples of a government franchise?

- The U.S. Postal Service
- Local telephone service
- Local electric, gas, water utilities, garbage collection, cable TV

Is a government franchise a win-win deal for the protected company?

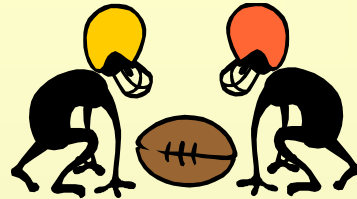
No!



Most often the
government regulates
its prices and profits

What is the government's objective?

For the monopoly to
make a normal profit



Why is $MR < P$ for all but the first unit of output for a single price monopoly?

In order to sell additional units the firm not only has to lower price on the *last* unit, but on all *previous* units

MR is less than price for all but the first unit of output

Q P TR MR

10	5.25	52.50	3.00
11	5.00	55.00	2.50
12	4.75	57.00	2.00
13	4.50	58.50	1.50
14	4.25	59.50	1.00

What is TR at the 3rd unit?

<u>Price</u>	<u>Q</u>	
\$50	2	
\$40	3	\$120
\$30	4	
\$20	5	
\$10	6	

What is MR at the 3rd unit?

<u>Price</u>	<u>Q</u>	
\$50	2	
\$40	3	\$20
\$30	4	
\$20	5	
\$10	6	

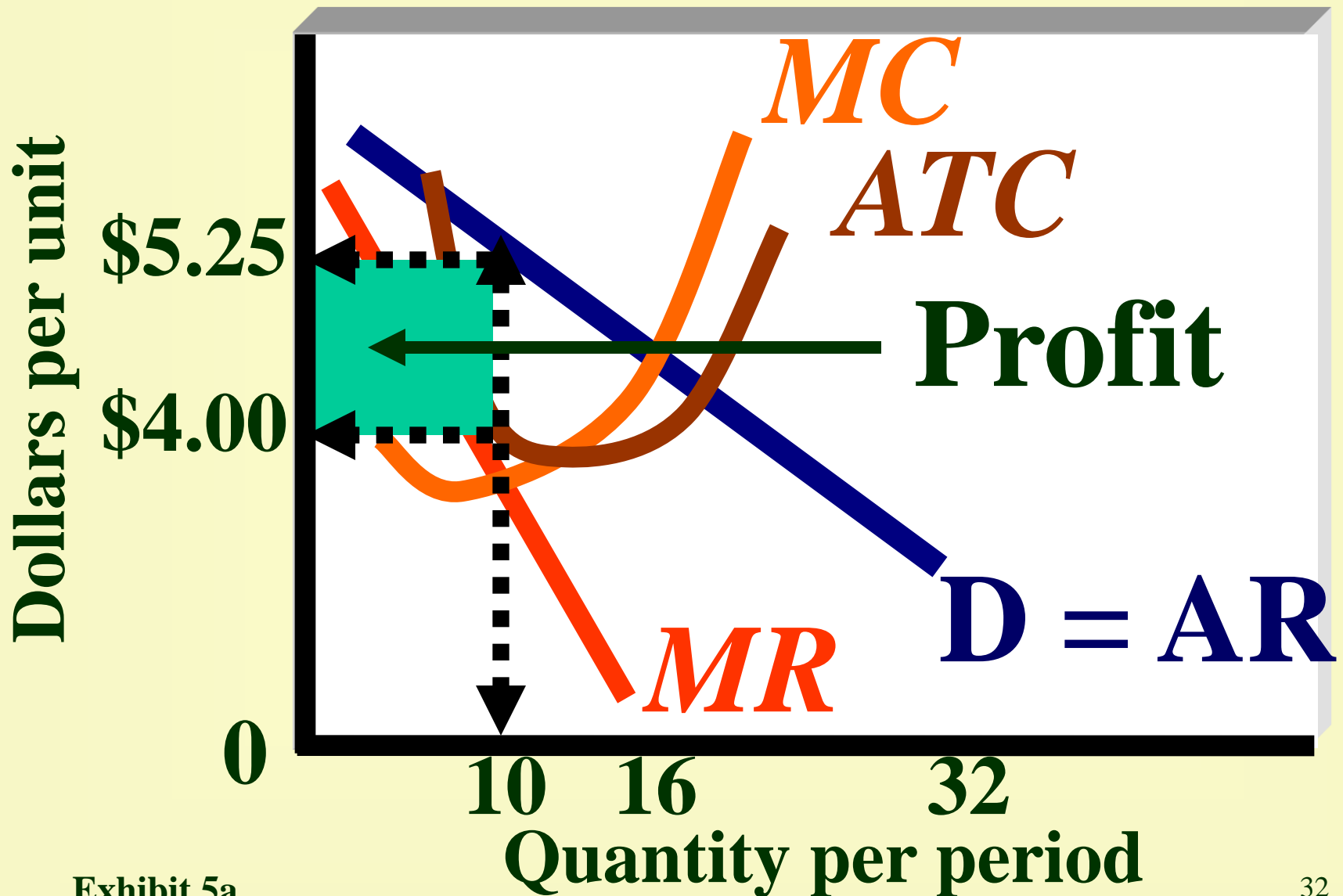
What is MR at the 5th unit?

<u>Price</u>	<u>Q</u>	
\$50	2	
\$40	3	
\$30	4	-\$20
\$20	5	
\$10	6	

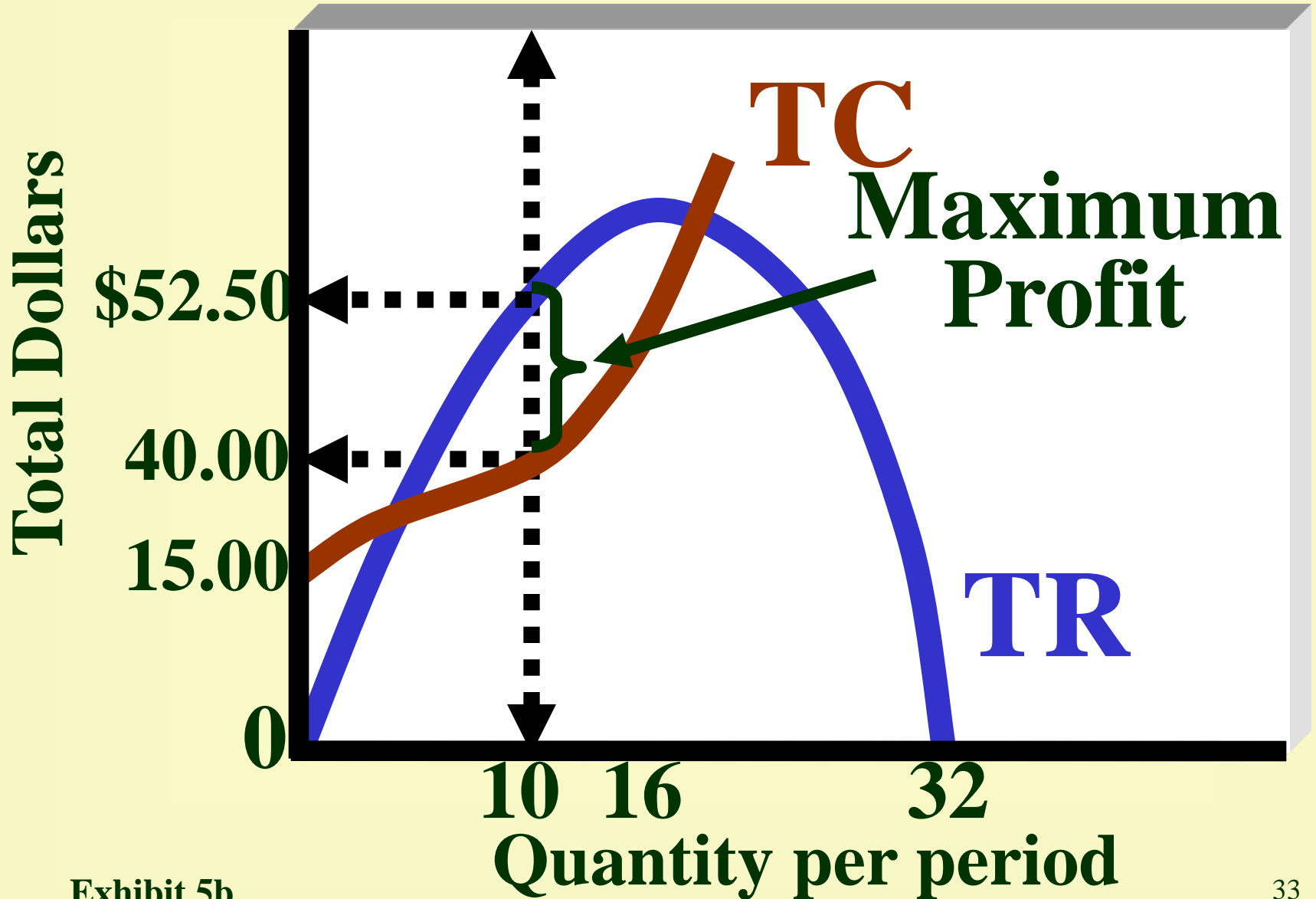
Short-Run Cost & Revenue for a Monopolist

Q	P	TR	MR	TC	MC	+, -
8	5.75	46.00	4.00	35.25	1.50	10.75
9	5.50	49.50	3.50	37.25	2.00	12.25
10	5.25	52.50	3.00	40.00	2.75	12.50
11	5.00	55.00	2.50	43.25	3.25	11.75
12	4.75	57.00	2.00	48.00	4.75	9.00

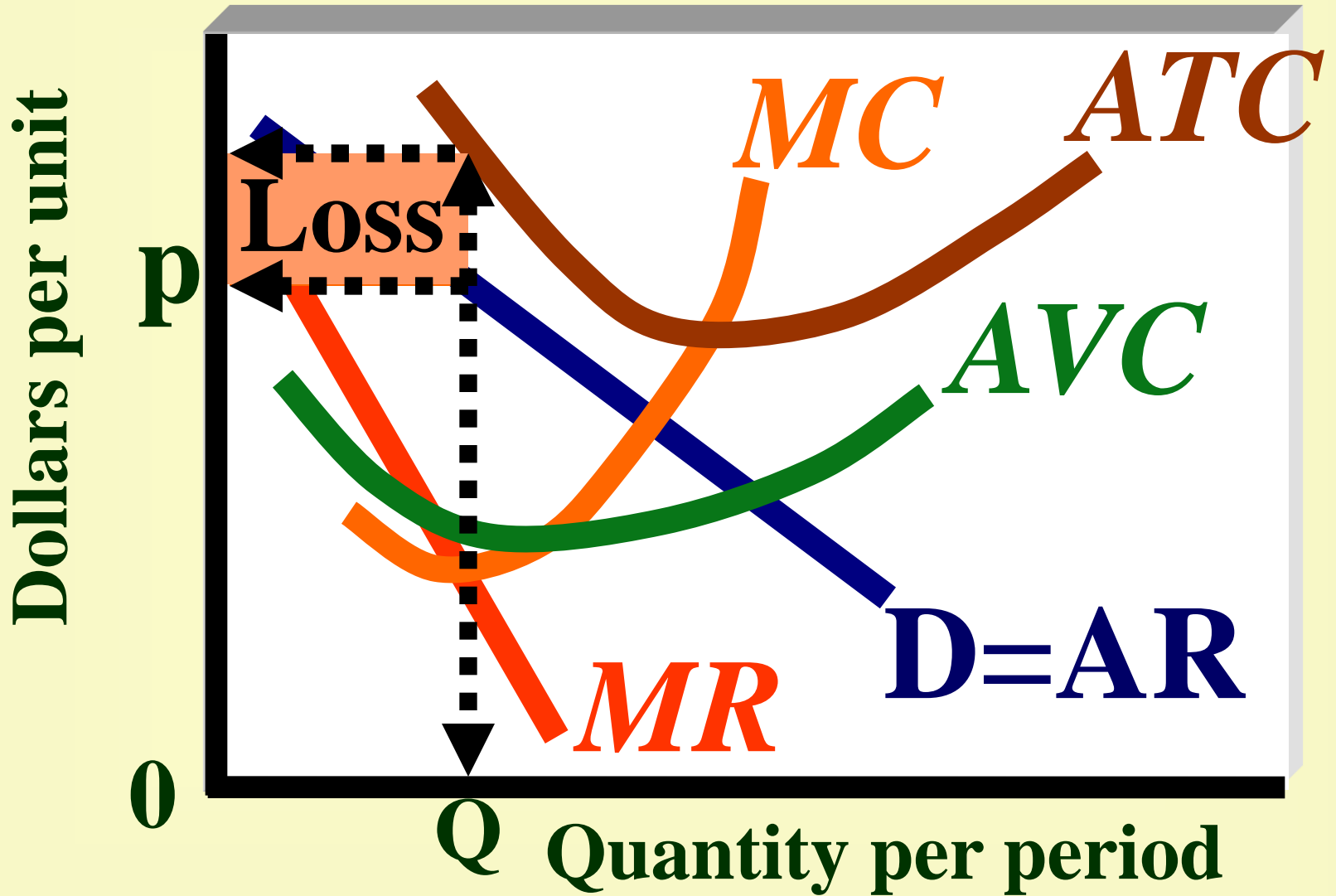
(a) Per Unit Cost & Revenue



(b) Total Cost & Revenue



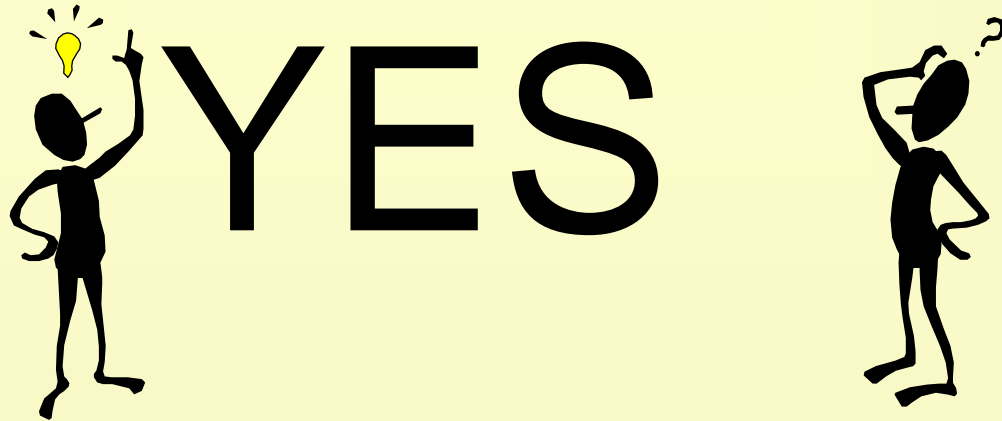
Minimizing Losses



When will a monopolist shut down?

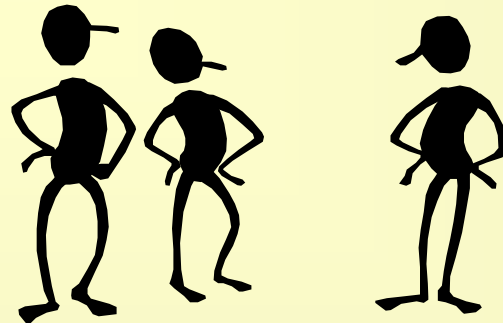
If no price covers
average variable cost

Can a monopolist earn an economic profit?



**Why do monopolies often
earn zero economic profit?**

Government regulation



How to compare perfect competition & monopoly?

- Higher prices & less output under monopoly
- Resource allocation

Why does a monopoly charge a higher price and produce a lower quantity than perfect competition?

Because of the different slopes of their demand and MR curves

a Perfect Competition & Monopoly

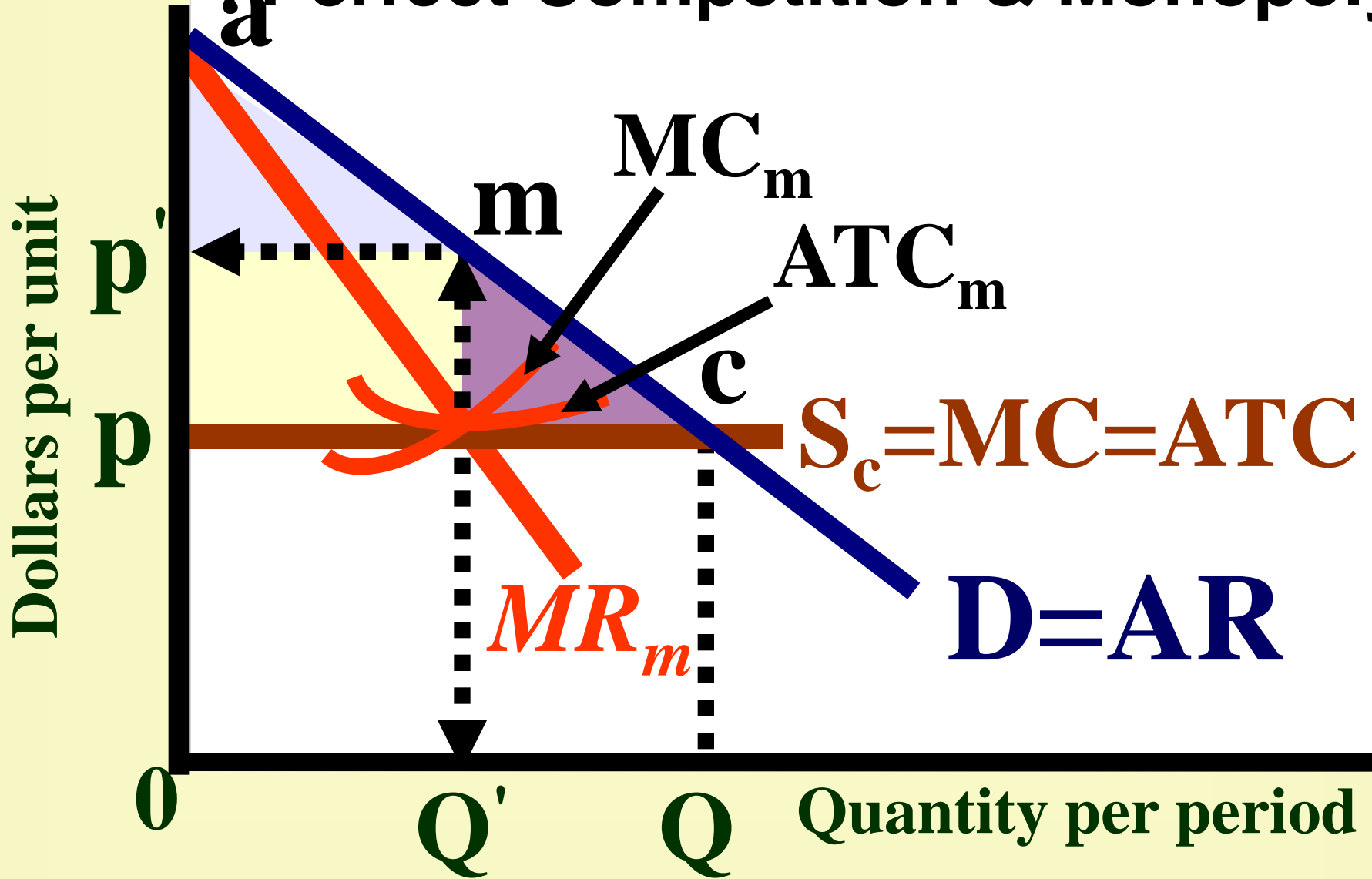


Exhibit 7

What is rent seeking?

Activities undertaken by individuals or firms to influence public policy in a way that will distribute income to them

END

Appendix

What is price discrimination?

Selling the same good
for different prices to
different consumers as
a way to increase profit

Price Discrimination High-Marginal-Value Consumer

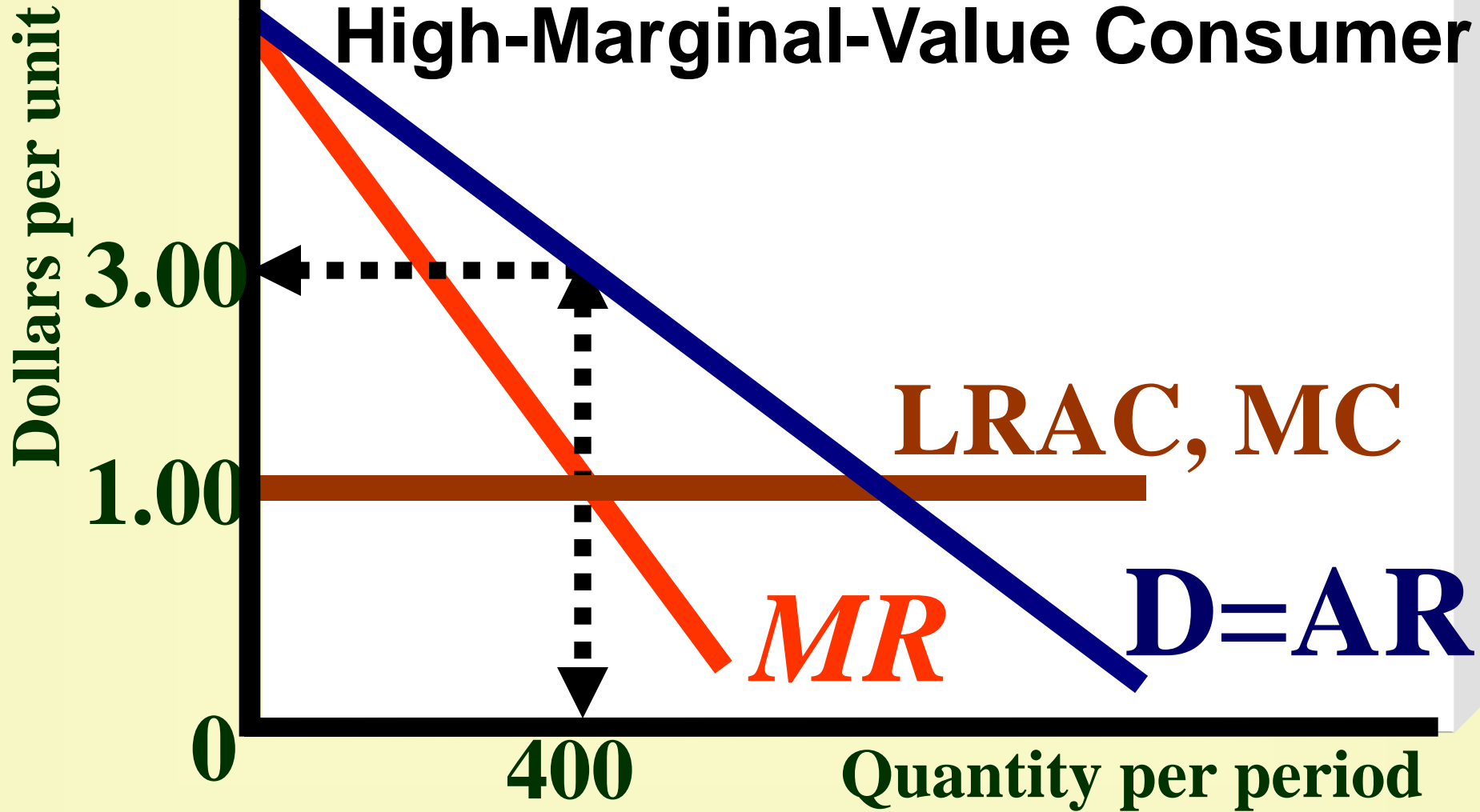
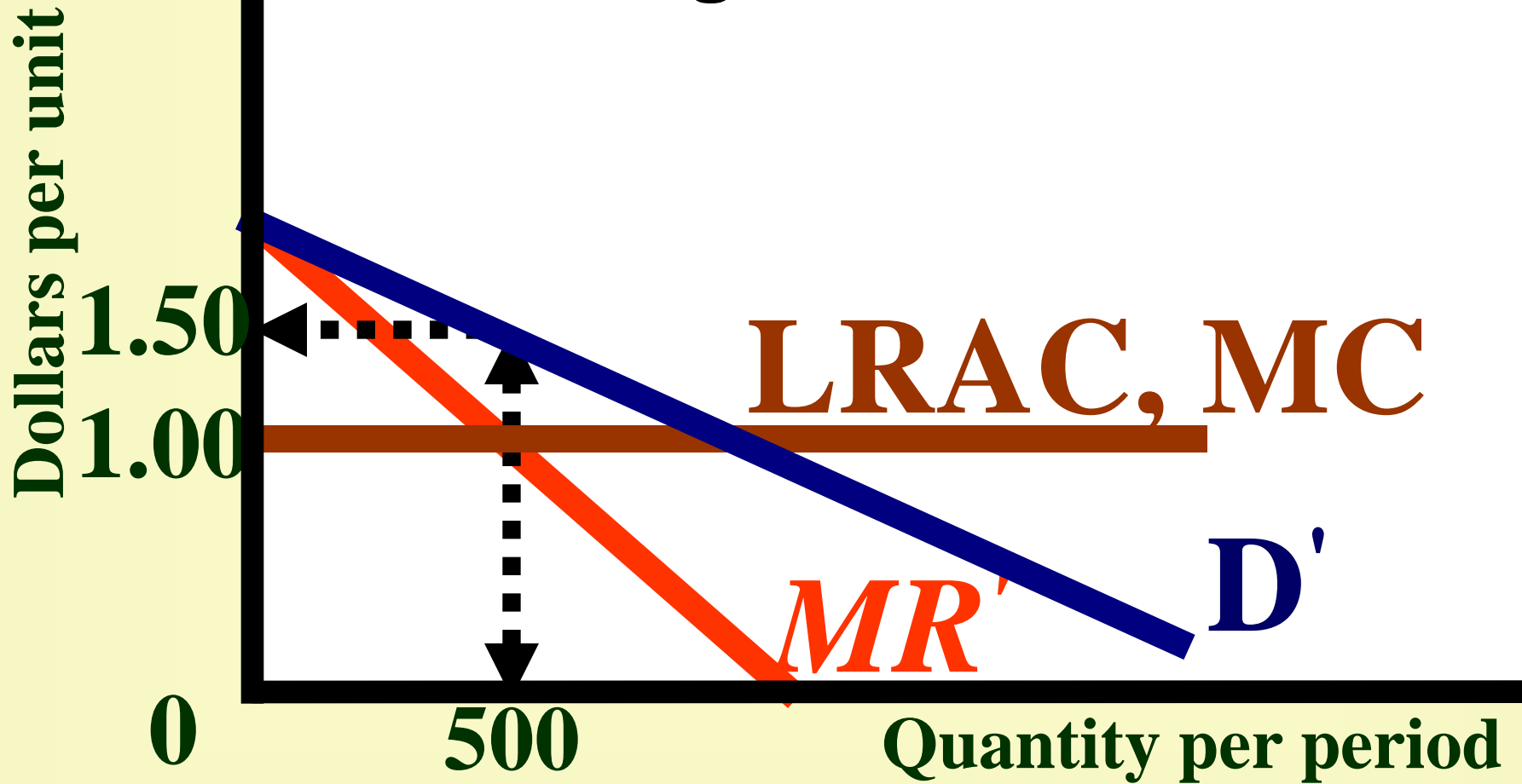


Exhibit 8 (a)

Price Discrimination Low-Marginal-Value Consumer



Monopolist charges different price for each unit sold, perfect price discrimination

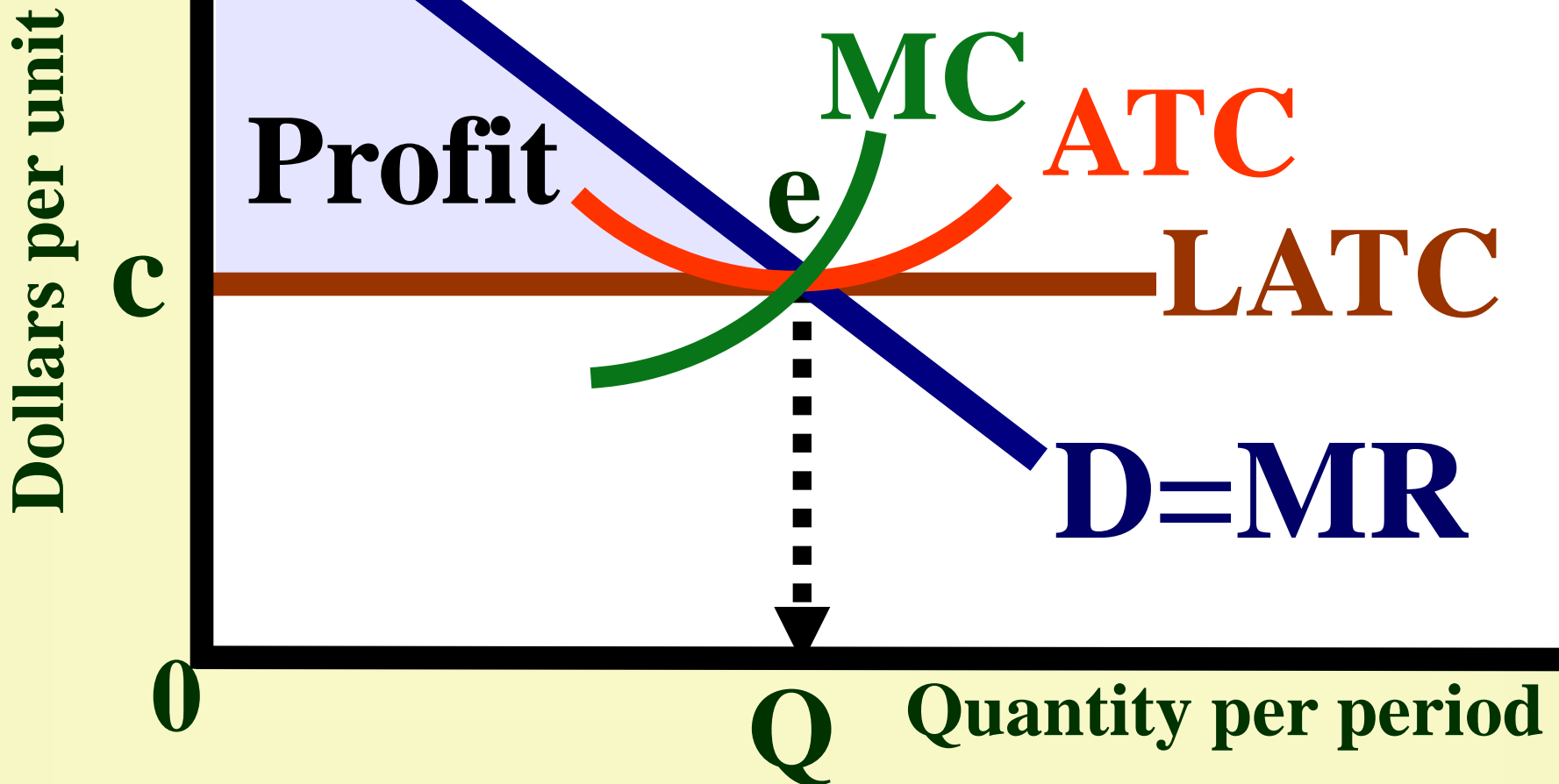


Exhibit 9

What does producer surplus represent for the perfectly discriminating monopolist?

Economic profit

What is deadweight loss?

A loss of consumer and producer surplus that is not transferred to anyone else; it can result from the monopolization of an industry