

Chapter 24 – Monopolistic Competition/Oligopoly

1. **Monopolistic competition** – somewhere in between monopoly and perfect competition. Here, a large number of firms compete, each firm produces a slightly different product, firms compete on product quality, price, and marketing, and firms are free to enter and exit
2. **Small Market Share** – each firm has a small part of the market supply, so each firm can deviate from the market price by a small amount
3. **Ignore other firms** – A firm in monopolistic competition does not pay attention to any one individual competitor. Since every firm is relatively small, no one firm can dictate market conditions.
4. **Collusion Impossible** – firms in monopolistic competition would like to be able to conspire to fix a higher price – called collusion. But because there are many firms, collusion is not possible
5. **Product differentiation** – it makes a product slightly different from the products of competing firms, making it a close but not perfect substitute. Some people would pay more for some varieties of products, such as Nike or Reebok over Adidas or Asics
6. **Competition Factors**
 - a. **Quality** – physics attributes that make it different from the products of other firms. Includes design, reliability, service, and ease of access to the product
 - b. **Price** – firms face a downward sloping demand curve, so firm can set both its price and its output. However, a firm that makes a high quality product can charge a higher price than a firm that makes a low quality product
 - c. **Marketing** – advertising and packaging. A firm that produces a high quality product wants to sell it at a high price, so it must advertise and package accordingly.
7. **Entry and Exit** – firms can freely enter/exit, so theoretically no one can make an economic profit in the long run
8. **Price and Profit – Short Run – almost like single priced monopoly**
 - a. Same story, marginal price = marginal revenue is the profit maximizing point, and like in a monopoly, the price is set as high as demand will allow at the profit maximizing output
 - b. Profit = (price – ATC) * quantity.
9. **Price and Profit – Long run** – Unlike single priced monopolies, free entry/exit results in 0 long run profit
 - a. As new firms enter, each firm has a smaller market share, so each firm's demand and MR curve shifts leftward, and although they still charge the maximum they can, as output falls since the profit max output drops, the price falls. In long run equilibrium, ATC = the demand price, and the profit is 0.
 - b. In a single priced monopoly, the monopoly can make a profit forever
10. **Capacity Output** – the output at which the ATC is at a minimum, or where the MC = ATC
11. Firms in monopolistic competition always have excess capacity in the long run, and the consumer pays the price that exceeds the minimum ATC. This happens because the demand curve slopes downward, and the demand curve slopes downwards because of product differentiation, so product differentiation creates excess capacity. In other words, although they CAN produce more, there isn't that much demand for the product, hence they don't. In perfect competition, demand is perfectly elastic, so they can produce as much as they want and still sell it
12. Monopolistic competition isn't efficient, since marginal benefit to the customer is more than the marginal cost. However, monopolistic competition brings variety and differentiation, so the benefit of that has to be taken into account
13. **Innovation and Product Development**
 - a. In order to make a profit, monopolistic firms must constantly be in product development, since whenever a new product emerges, imitators enter the market to set up similar products
 - b. The firm spends as much on development as the extra development brings in, when MC = MR
 - c. Changes don't always need to be innovative, as long as you can convince consumers to think they are. Changing the packaging might convince consumers it's a new product, hence bring in more revenues for almost no cost
 - d. Innovation is efficient if the producers marginal cost of product improvement equals the consumers marginal benefit
14. **Marketing** – to make consumer think specific products are different even if they're not (Amex compared to Visa)
 - a. Much of the final cost of a product is its marketing, not necessarily its production. However, if successful, marketing increases demand
 - b. Advertising shifts the ATC curve upwards, but if it can increase the demand by enough, it actually lowers the ATC
 - c. Advertising in general increases demand, but if advertising allows firms to make a profit, it might increase the number of firms, which would increase total industry output and decrease demand for a single company's product.
15. **The verdict** – monopolistic competition is inefficient, but allows for variety. Imagine if only one type of book, clothing, food, or drink was available. Hence, the real world is generally monopolistically competitive.
16. **Oligopoly** – To be added later

