Chapter 14 – Monopoly and Antitrust Policy
The Four Types of Market Structure

- **Monopoly**
  - Tap water
  - Cable TV

- **Oligopoly**
  - Tennis balls
  - Computer Chips

- **Monopolistic Competition**
  - Novels
  - Movies

- **Perfect Competition**
  - Wheat
  - Milk

Number of Firms?
- One firm
- Few firms
- Many firms

Type of Products?
- Differentiated products
- Identical products
Monopoly

- How many of you have Cable Television where you live?
- How many of you have a washer and dryer?
- 80% of homes have Cable TV
  - More than clothes dryers, dishwashers, AC, or PCs
- Grew slowly at first because of technology limitations
  - Now had in many households
- Out of 9000 markets for Cable, only 400 have competing cable systems.
- In Manhattan only Time-Warner provides cable
  - Time-Warner is a monopolist in this case.
- **Monopoly**: A firm that is the only seller of a good or service that does not have a close substitute.
- **Example**: Light bulbs and Candles
Monopoly

- Are Xbox and PS2 substitutes?
  - Original Xbox costly to produce because of operating system and hard-disk
  - Microsoft not worried – Simply charge higher price
  - In the end MS charges similar price as PS2

- Are Xbox360 and PS3 substitutes?
  - PS3 can play Blu-rays
  - Blu-ray makes PS3 more expensive to produce
  - Sony not worried – simply charge higher price
  - In the end Sony charges similar price as MS and lost market share

- Key Point: Not monopolies because they affect each other
Sources of Monopoly

• Barriers to entry have to be high!
• Barriers are from four main sources
  1. Government blocks the entry of more than one firm into a market.
     ◦ How many firms can legally place a letter in your mailbox?
  2. One firm has control of a key resource necessary to produce a good.
  3. There are important network externalities in supplying the good or service.
  4. Economies of scale are so large that one firm has a natural monopoly.
Source of Network Externalities

- **Network Externalities**
  - When the usefulness of a product increases with the number of consumers who use it

- **Consider operating systems**
  - 95% of personal PCs use windows
  - Which OS will software developers target?

- **eBay**
  - First major auction house
  - Other auction houses exist, but eBay is the largest
  - If you are trying to sell products which auction would you use?
  - The Biggest one? How about for buying?
Network Externalities: Example

- QWERTY Keyboard

- Dvorak Keyboard
Source of Monopoly

- **Natural Monopoly**
  - A situation where economies of scale are so large that one firm can supply the entire market at a lower average total cost than can two or more firms.

- **What will happen to a firm with the size of B?**
  - __________
  - __________
  - __________
Modeling Monopoly

- Very Similar to Monopolistic Competition
- For **Monopoly**
  - Market Demand curve is the firm’s demand curve
  - Demand Curve is *downward sloping*.
  - To sell one more unit, the monopolist has to lower the price on all units
  - What does this tell you about the relationship between marginal revenue and price?
    - ____________________________________________________________
    - ____________________________________________________________
Monopoly

- **Example** – Time-Warner Cable

**Notice:**
- Demand Curve Downward Sloping
- MR Below Demand Curve

**Find Profits:**
- Go to the Best Point (MR = MC)
- Find Price from Demand Curve
- Find Revenue
- Find Costs
- Difference equals the profit or loss.

- What is going to happen to the profits of this firm?

- ________________
- ________________

![Diagram of Monopoly](image)
Monopoly vs. Perfect Competition

- How do price and quantity compare between monopoly and perf. comp?
- Monopolist:
  - ________________
  - ________________
- What happens to economic surplus in the case of Monopoly?
  - ________________
Monopoly and Surplus (or efficiency) loss

• If this were a perfectly competitive industry, where would the economic surplus be?
• Since the monopolist does not produce the competitive amount, what happens to surplus?

• Monopoly is associated with a deadweight loss
• Note that Price goes from $P_C$ to $P_M$ for a monopolist. Do you think this is better for consumers or producers?

• Some of consumer surplus is transferred to the monopolist
Monopolies and Government

- Because economic surplus is reduced under monopoly conditions, government regulates monopolies.
  - The two main things they consider
    - Market power
    - Can a merger result in lower costs
      - We don’t want to waste resources.

- Antitrust laws
  - 1880s, corporations operated independently, but gave some control to trusts.
  - Trusts organized agreements between firms to keep prices high.
  - The trusts mitigated the oligopoly effect