



# Unit 3

# Market Power and Monopoly (Ch. 9)

## 10/30

ECON 323 – MICROECONOMIC THEORY – DR. STRICKLAND



# Introduction

How do firms make decisions in other market structures?

Many firms have **market power**

- Most extreme case: **monopoly**

Monopolies arise from **barriers to entry**

# Sources of Market Power

(1) Economies of scale at every output level

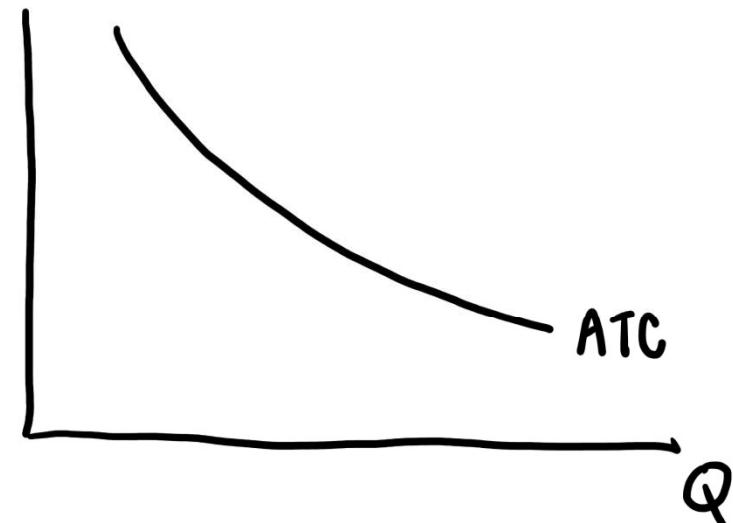
- Natural monopoly

e.g.  $TC = 100 + 10Q$

① ONE FIRM PRODUCES  $Q=2$

$$TC = 100 + 10(2) = 120$$

$$ATC = \frac{TC}{Q} = \frac{100}{Q} + 10 = \frac{100}{(2)} + 10 = \underline{\underline{60}}$$



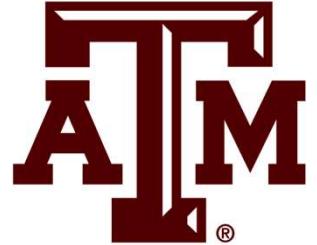
② TWO FIRMS PRODUCE  $Q=1$  EACH

$$TC \text{ OF EACH FIRM} = 100 + 10(1) = 110$$

$$TC \text{ OF INDUSTRY} = 110 \cdot 2 = 220$$

$$ATC \text{ OF INDUSTRY} = \frac{220}{2} = \underline{\underline{110}}$$

# Sources of Market Power



## (2) Consumer switching costs





# Sources of Market Power

## (3) Differentiation

- Product
- Spatial





# Sources of Market Power

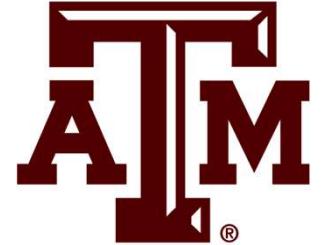
## (4) Absolute cost advantages

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# Sources of Market Power



## (5) Government regulation

abbvie

