Firms differentiate their output ← price makers
Barriers to entry = low/none

Monopolistic Competition

- Low markup

Monopolistic Competition - a market structure that has
- Free entry
- Many different firms
- Product differentiatintion

"compete away" economic profits to zero
- e.g. Apple bees
- if barrier to entry high and (somewhat) differentiated, economic profit might be sustainable
- between monopoly and perfect competition
- produce the output level at which price = long-run AC
- inefficient because price != min. ATC

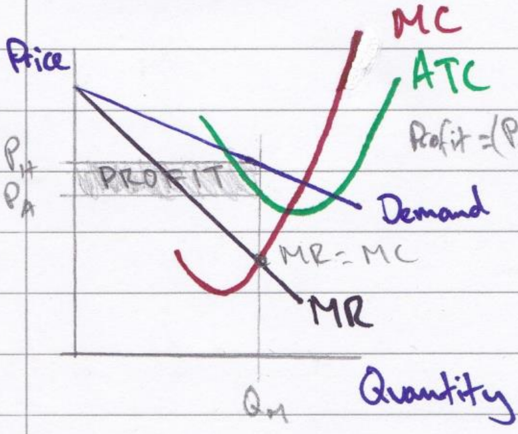
Style	Location	Trade off: ↓ Quality, Prices, Fast service vs ↑ Quality, Prices, Slow service
Clothing stores	Gas stations	
Food court	Dry cleaners	
	Barber shops	

less elastic than competitive market

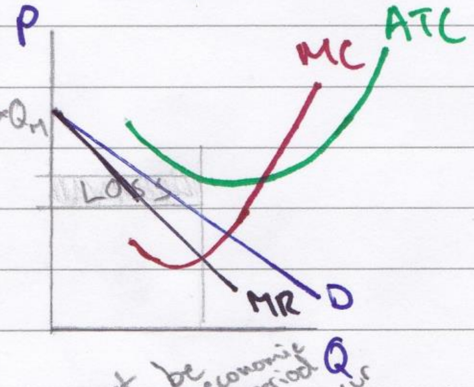
Monopolistic Competition Short Run

MR<P
- MR=MC

Profitable | **Unprofitable**



Profit $=(P_M - P_A)\times Q_M$

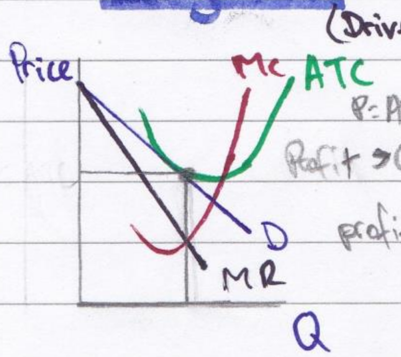


Determines price
level of output
Consider MR and MC

Long Run

cannot be guaranteed an economic profit in any period and might incur losses

- Profitable
(Drives Economic profit to 0), profit max when MR=MC
P=ATC, Entry and exit stops, remain in industry
Profit >0, Firms enter, demand ↓ (curves downward) and spreads, demand shifts left
profit will == 0 due to entry of firms
↑ in MR = ↑P, ↓Q



- Not profitable
Firms exit, demand ↑ and narrows

Market power - output changes as cost changes
Excess capacity = monopolistic competitive firms produce less than cost-minimizing level of output

Highest under a monopoly
Lowest under a monopolistic competition

(economic inefficiency)

Markup - = (P - MC) difference between MC and P of monopolistic competitor
- possible when firms has market power
and sells a different product
- consumers pay more

Inefficiency when
- ATC ↑ compared to perfect competition
Firm could ↓ prices to sell more

- Markup, P > MC

- Government intervention/regulation may put firms out of business

Highly differentiated product = ↑ markups
↑ excess capacity
↑ ~~higher~~ prices

Less differentiated product = ↓ markups
↓ excess capacity
↓ prices

Successful

demand curve shifts right
cost curve shifts upward

<u>Advertising</u>

False advertising regulated by FTC

2% of US economic input
To - provide information to consumers
- differentiate product
- ↑ demand

But creates brand loyalty
So - more inelastic demand
- ↑ prices