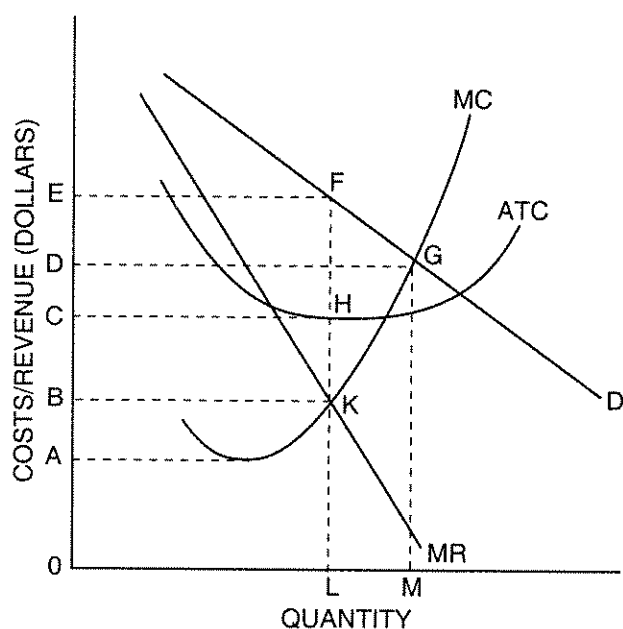


## Monopolistic Competition



Figure 40.1

### Monopolistically Competitive Firm in the Short Run



1. Use Figure 40.1 to answer these questions.

- At what level of output will this firm operate? OL
- What is marginal revenue at this level of output? OB
- What price will this firm charge for its product? OE
- The area of which rectangle is equal to total revenue? OEFL
- What is the firm's average total cost? OC
- The area of which rectangle is equal to the firm's total cost? OCHL
- Is the firm making profits or incurring losses? Making economic profits
- The area of which rectangle is equal to profits or losses? CEFH

2. Would the demand curve for a monopolistic competitor be more or less elastic than the demand curve for a monopolist? Justify your answer. *More elastic. Because there are many competitors, the monopolistic competitor will lose sales to these producers if it raises prices.*
3. What are the characteristics of a monopolistically competitive market? In what sense is there competition and in what sense is there monopoly in this type of market structure? *Monopolistic competition is characterized by many firms selling a differentiated but similar product. It is similar to monopoly because the firm has some control over price. It is similar to perfect competition because there are few barriers to entry, many competitors and long-run profits may exist but probably will be low.*
4. What are three examples of monopolistically competitive markets? *Almost all retailing is done under conditions of monopolistic competition.*
5. True, false or uncertain, and why? “Monopolistic competition is just another form of pure monopoly.” *False. It has many characteristics of perfect competition.*
6. True, false or uncertain, and why? “Monopolistic competition is even better than perfect competition.” *Uncertain. Monopolistic competition does allow price and quality competition. Consumers have a wider choice under monopolistic competition. However, price is higher and output lower than under perfect competition. Monopolistic competition also creates excess capacity.*
7. True, false or uncertain, and why? “In the long run, monopolistic competitors produce at their most efficient point.” *False. Monopolistic competitors do not operate at the bottom of their average cost curve (productive efficiency) or where  $P = MC$  (allocative efficiency).*