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B.A. Part-1

Paper-1 (Microeconomics)

Topic – Monopoly (intro)

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MONOPOLY

Meaning:

The word 'monopoly' has been derived from the combination of two words i.e., 'Mono' and 'Poly'. 'Mono' refers to a single and 'Poly' to control.

In this way, monopoly refers to a market situation in which there is only one seller of a commodity. There are no close substitutes for the commodity it produces and there are barriers to entry. The single producer may be in the form of individual owner or a single partnership or a joint stock company. In other words, under monopoly there is no difference between firm and industry.

Monopolist has full control over the supply of commodity. Having control over the supply of the commodity he possesses the market power to set the price. Thus, as a single seller, monopolist may be a king without a crown. If there is to be monopoly, the cross elasticity of demand between the product of the monopolist and the product of any other seller must be very small.

Definition:

"Pure monopoly is represented by a market situation in which there is a single seller of a product for which there are no substitutes; this single seller is unaffected by and does not affect the prices and outputs of other products sold in the economy."

"Monopoly is a market situation in which there is a single seller. There are no close substitutes of the commodity it produces, there are barriers to entry."

~ Koutsoyiannis

"A pore monopoly exists when there is only one producer in the market. There are no dire competitions." ~ Ferguson

Features:

We may state the features of monopoly as:

1. One Seller and Large Number of Buyers:

The monopolist's firm is only firm; it is an industry. But the number of buyers is assumed to be large.

2. No Close Substitutes:

There shall not be any close substitutes for the product sold by the monopolist. The cross elasticity of demand between the product of the monopolist and others must be negligible or zero.

3. Difficulty of Entry of New Firms:

There are either natural or artificial restrictions on the entry of firms into the industry, even when the firm is making abnormal profits.

4. Monopoly is also an Industry:

Under monopoly there is only one firm which constitutes the industry. Difference between firm and industry comes to an end.

5. Price Maker:

Under monopoly, monopolist has full control over the supply of the commodity. But due to large number of buyers, demand of any one buyer constitutes an infinitely small part of the total demand. Therefore, buyers have to pay the price fixed by the monopolist.

Nature of Demand and Revenue under Monopoly:

Under monopoly, it becomes essential to understand the nature of demand curve facing a monopolist. In a monopoly situation, there is no difference between firm and industry. Therefore, under monopoly, firm's demand curve constitutes the industry's demand curve. Since the demand curve of the consumer slopes downward from left to right, the monopolist faces a downward sloping demand curve. It means, if the monopolist reduces the price of the product, demand of that product will increase and vice- versa. (Fig. 1).

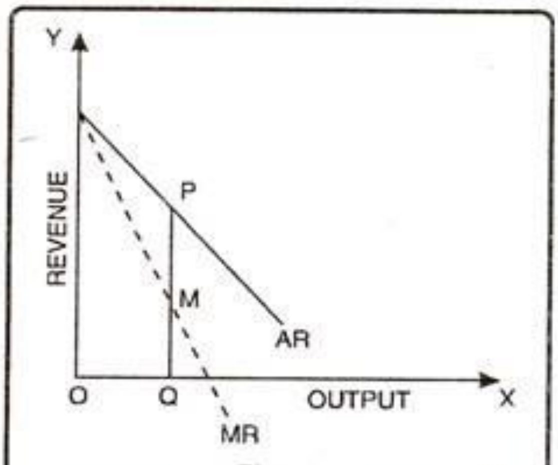

Fig. 1.

In Fig. 1 average revenue curve of the monopolist slopes downward from left to right. Marginal revenue (MR) also falls and slopes downward from left to right. MR curve is below AR curve showing that at OQ output, average revenue (= Price) is PQ whereas marginal revenue is MQ. That way AR > MR or PQ > MQ.