

Chapter 10 Project

Monopolistic Competition and Oligopoly

Purpose

In this chapter, you learned about imperfectly competitive markets, monopolistic competition, and oligopoly. Monopolistic competition is a market structure which combines elements of both perfect competition and monopoly. Like perfect competition, there are many buyers and sellers in the market. The products in a monopolistically competitive market, unlike those in perfect competition, are differentiated. Like monopoly firms, a firm in monopolistic competition has some control over the price of its product. Oligopoly markets have a few firms producing most of the output, and the firms in the industry are interdependent with respect to decisions concerning price and quantity of output produced.

The purposes of this exercise are to determine if you encounter monopolistically competitive markets and to determine how products are differentiated. You will also discover the interdependence of oligopoly firms.

Directions

This exercise has three parts. In the first, you will explain how products are differentiated in monopolistic competition. In the second, you will explain how a market in monopolistic competition reaches long-run equilibrium and compare the outcome with the outcome in perfect competition with respect to allocative and productive efficiency. In the third part, you will make price and output decisions that illustrate interdependence in oligopoly

Part 1 - Differentiated Products in Monopolistic Competition

1. Indicate how the following familiar products produced in monopolistic competition are differentiated. In the last four rows of the table, list some other products that you buy frequently in monopolistically competitive markets and explain how they are differentiated.

Product	How Differentiated
Fast food hamburgers	
Gas stations	
Bottled water	
Hotels	
Blue jeans	
Running shoes	

Part 2 - Monopolistic Competition in the Long Run

Suppose that after you graduate, you open a barbecue restaurant in a large city nearby. There are six other barbecue restaurants in town, but you are convinced that you can be successful by differentiating your restaurant and by advertising.

1. What are some possible ways that you can differentiate your restaurant?
2. If you and the other six barbecue restaurants earn economic profits, what will happen in the long run?
3. How does this long-run outcome differ from perfect competition and monopoly?
4. How could you use advertising to continue to earn economic profits in the long run?

Part 3 - Interdependence in Oligopoly

Suppose that there are only two gas stations, Station X and Station Y, in a small town out in a desert. The nearest gas station is 150 miles away. Currently, each station is selling 2,500 gallons of gas per week and making a profit of \$12,500 each. The following matrix shows profits for each firm if either or both decide to increase sales to increase profit.

	Station X sells 2,500 gallons	Station X sells 3,500 gallons
Station Y sells 2,500 gallons	Profit for X = \$12,500 Profit for Y = \$12,500	Profit for X = \$14,000 Profit for Y = \$10,000
Station Y sells 3,500 gallons	Profit for X = \$10,000 Profit for Y = \$14,000	Profit for X = \$10,500 Profit for Y = \$10,500

1. What is the likely outcome in this market?
2. Compare the equilibrium price and output of oligopoly with that of perfect competition, monopoly, and monopolistic competition.

3. As a consumer, which market structure do you prefer? Why?

Checklist

Part 1

- Identify products in monopolistically competitive markets.
- Differentiate products.

Part 2

- Answer questions pertaining to monopolistic competition in the long run.

Part 3

- Determine outcome of oligopoly.
- Compare equilibrium in an oligopoly with equilibrium in other market structures.