

Chapter 16: Monopolistic Competition
Principles of Economics, 7th Edition
N. Gregory Mankiw
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1. Between Monopoly and Perfect Competition
 - a. There is imperfect competition.
 - i. Most markets contain elements of both competition and monopoly.
 - b. Oligopoly is a market structure in which only a few sellers offer similar or identical products. P. 330.
 - c. Monopolistic competition is a market structure in which many firms sell products that are similar but not identical. P. 330.
 - i. *This describes a lot of business environments, although the conclusions are similar to those under competition.*
 - ii. **Figure 1: The Four Types of Market Structure. P. 331.**
 - iii. *There is no magic number that separates “few” from “many.”*
 - d. MC has the following attributes:
 - i. Many sellers,
 - ii. selling differentiated products and
 - iii. there is free entry.

2. Competition with Differentiated Products
 - a. *Monopolistically competitive markets offer the opportunity to bring in some real world considerations;*
 - i. *Transaction costs and*
 - ii. *Risk aversion.*
 - b. The Monopolistically Competitive Firm in the Short Run
 - i. *A relevant question is how they got here.*
 - ii. **Figure 2: Monopolistic Competitors in the Short Run. P. 333.**
 - c. The Long Run Equilibrium
 - i. As in monopoly, $P > MC$.
 - ii. As in competition, $TR = TC$ and there are no economic profits.
 - iii. **Figure 3: A Monopolistic Competitor in the Long Run. P. 334.**
 - d. Monopolistic Versus Perfect Competition
 - i. **Figure 4: Monopolistic Versus Perfect Competition. P. 335.**
 - ii. Excess Capacity
 - (1) *This only exists because people view the product as different.*
 - (2) *They must see value in the higher priced good.*
 - iii. Markup over Marginal Cost
 - e. Monopolistic Competition and the Welfare of Society
 - i. *If society did not consider that there were costs associated with the different products, the demand curve would be flat and this environment would not exist.*
 - (1) *However, costs are associated with uncertainty, location and time.*
 - ii. **In the News: Insufficient Variety as a Market Failure, P. 338.**
 - (1) If the Shoe Doesn't Fit
 - (2) Few people with unique tastes do not justify a product.

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3. Advertising
 - a. The debate over advertising
 - i. *Since in most cases it is incorporated in the price of the good, they would not do it if consumers did not value it.*
 - ii. The Critique of Advertising
 - iii. The Defense of Advertising
 - b. **Case Study: Advertising and the Price of Eyeglasses, P. 340.**
 - c. Advertising as a Signal of Quality
 - i. *This explains advertising that essentially contains no “information.”*
 - ii. *If I advertise, I either think that you are going to value the product if you buy it or people in past did that giving me the revenue to advertise now.*
 - d. Brand Names
 - i. **Table 1: Monopolistic Competition: Between Perfect Competition and Monopoly, P. 344.**
4. Conclusion
5. Summary