The pros and cons of an oligopoly

Because monopoly markets have high barriers to entry, such as patents, limit pricing, cost advantages, advertising and marketing, research and development to name a few, monopolies enjoy the benefit of making super normal profits in the short run equilibrium and by extension in the long run equilibrium. This however can result in an unequal distribution of income in the sense that some profits will be dispersed to shareholders as dividends, thus some low income consumers may be exploited because of higher prices and some of their purchasing power may be conveyed using dividends in the higher income brackets. Some of these supernormal profits however can also be injected into research and development programmes, hence producing innovative products, if it wants to and overall producing a better quality product for consumers, for e. g., the pharmaceutical industry. On the other hand, there is a possibility for a monopoly to make losses as well, this transpires in the short run if the selling price is lower than the cost of the output of the product.

Depending on its size, a monopoly can achieve economies of scales, which is when the cost per unit falls as output increases. A monopolist will seek to maximize profits by setting output where MR= MC, and output is at Qm and Price Pm as illustrated below.

monopoly

Therefore, even if the total cost of production has risen, the cost per unit of production would fall, allowing increased profit margins to a monopolist by not reducing its MC, however still benefiting consumers since the cost is already low.

Some may argue though that because of the lack of rivalry, a monopolist can rather mislead consumers through innovation of ineffective or poor quality produced products. Additionally, because a substitute product is out ruled in cases of a monopoly market, it seeks to exploit consumers through setting high prices and lowering output levels contrary to perfect competition, subsequently, deriving at a downfall in consumer surplus and a deadweight welfare loss which leads to monopolies being allocatively inefficient. It is allocatively inefficient in the sense that price is greater than marginal cost (P> MC), whereas, in a competitive market, consumers would benefit through lower prices as shown on diagrams below through tutor2u:

http://tutor2u. net/economics/content/diagrams/efficiency2. gif

http://tutor2u. net/economics/content/diagrams/monopoly_welfare. gif

Monopolies are also said to be productively inefficient because it is not producing output at the lowest point on the average cost curve (AC).

Another major disadvantage of a monopolist which may surface is the matter of price discrimination. Monopolies find it very profitable to charge different prices of different units of the same product. Yes a monopolist must lower its prices of products in order to increase sales; however, this would only occur in districts where the demand for the product is price elastic. Monopolists will never lower its prices below the middle of its demand curve where demand for the product is price inelastic; else its opportunity of achieving higher revenues will fall. A price discriminating monopolist is demonstrated, again via tutor2u, where P1, Q1 is price discriminating:

http://tutor2u. net/economics/content/diagrams/pricing2. gif

The United States of America were the first nation to undertake antitrust legislation and enforcement. Only since World War II, have other nations done the same. The Sherman Antitrust Act of 1890 (15 U. S. C. A 1 etseq.) is the basis for antitrust law.

These are legislation sanctioned by the federal and various state governments to standardize trade and commerce by inhibiting unlawful restraints, price-fixing and monopolies in the effort to promote and protect competition in the market, and to encourage the production of quality goods and services available at the lowest prices to consumers, hence the fundamental goal of protecting public welfare through positive competition.

According to section 2 of Sherman Act (15 U. S. C), any person monopolizing, attempting to monopolize, or combine or conspire with any other person to monopolize any part of the trade or commerce among the several states, or with foreign nations, shall be deemed guilty of a felony and on conviction thereof, shall be punished by a fine not exceeding $10, 000, 000 in cases of a corporation, or if any other person, they would be fined $350 000 or by imprisonment not exceeding three years, or by both said punishments in the discretion of the court.

In conclusion, I agree that a monopoly can pose great number disbenefits in a market and to society as a whole, however I strongly believe that with a government’s permission, through patents, trademarks, copyrights and franchises, monopolies can be beneficial to society by creative production of products or services as well as providing financial incentives to local artists,

writers, entrepreneurs, etc, something a firms operating in a competitive market may not be able to provide.

Word Count: 850 words