Class: B.Com Part I

Subject : Business Economics and Environment.

Paper : I

Unit : IV

Topic : Shortrun Equilibrium (Monopoly)

Sequence No : 7

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Subject

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Short Run Equilibrium Price and Output Under Monopoly:

Short Run Equilibrium of the Monopoly firm:

In the short period, the monopolist behaves like any other firm. A monopolist will maximise profit or minimize losses by producing that output for which Marginal cost (MC) equals Marginal Revenue (MR). whether a profit loss is made or not depends upon the relation between price and Average total cost (ATC) It may be made clear here that a monopolist does not necessarily makes profit. He may earn super profit or normal profit or even produce at a loss in the short run.

Assumptions:

1. That the number of sellers are independently ~~of exede~~
2. The product is differentiated from other product
3. The firm has a determinate demand curve (AR) which is elastic
4. That the factor-services are in prefectly elastic supply for the production of the product
5. No. of new firm enter the Industry

Conditions for the Equilibrium of a Monopoly Firm

There are two basic conditions for the equilibrium of the monopoly firm.

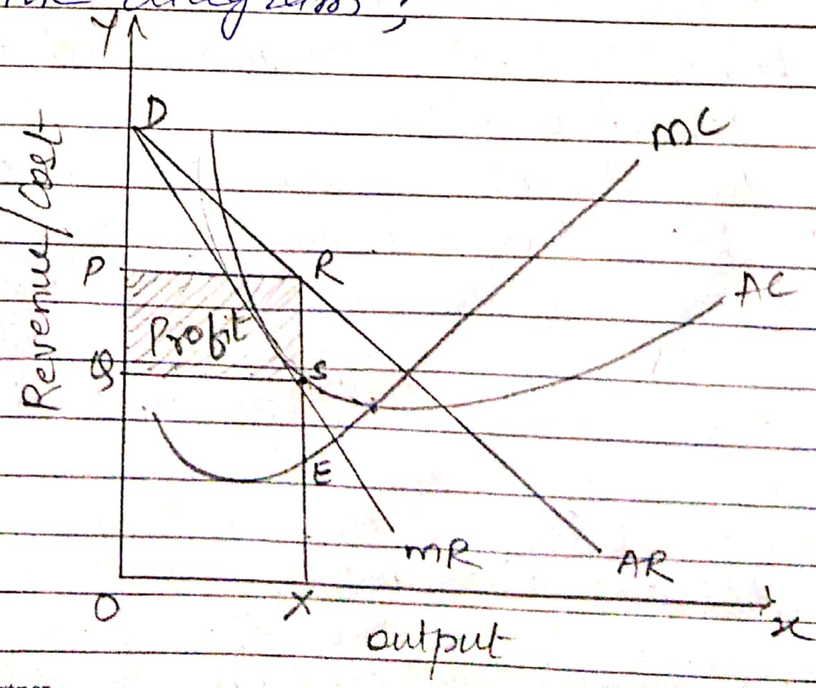
1. Condition MC = MR.
2. MC curve cuts MR curve from below ie MC is raising

Explanation

(a) Short Run Monopoly Equilibrium with Super Profit. (Extra Normal Profit).

In the short run period, if the demand for the product is high, a monopolist increase the price and the quatity of output. He can increase, the output by hiring more labour, using more raw matereal, increasing working hrs etc. However, he cannot change his fixed plant equipment. In case, the demand for the product falls, he then decrease the use of variable inputs, RM, labour etc.

As regards the price, the monopolist is a price maker. There is a greater tendency for the monopolist to have price which earns super profit. This can only be possible if the price (AR) is higher than Average Total Cost (ATC). The short run profit earned by the monopolist is now explained with the help of the diagram;



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Here monopoly firm is in equilibrium at point E where $MC = MR$. The Short-run marginal cost curve cut MR from below. At point E both the equilibrium condition are fulfilled. As a result therefore OP is monopoly price at OX level of monopoly output.

Here OX level of output, the Average total cost is $OQ = XS$. The profit per unit is QP. The short run monopoly profit is PRSQ. It is represented by the area of shaded rectangle.

At the output smaller than OX (~~cute point E~~) $MR > MC$. And therefore increased output upto to OX adds more to total receipt than to total Costs. In case the output is increased beyond OX add more to total Cost than to total receipts. This causes profits to decrease. So the best level of output for the monopolist firm where MC curve cuts the MC cure from below.