Determining the Social Cost of Monopoly

Key Concepts:

- The result of having a monopolistic market as opposed to a competitive market is restricted output and a higher price.
- Monopoly creates a social cost, called a deadweight loss, because some consumers who would be willing to pay for the product up to its marginal cost (MC), are not served.

**Where is the Supply Curve?**

In a monopoly, there is no supply curve because monopolists are price setters and not price takers. In the graph on the left, the MC curve is not the firm's supply curve.

In a competitive market, firms have to passively take the market price as given. The supply curve describes the quantities they will put on the market at any given price.

If the firm is a monopoly it does not need that information because it is setting the price.

**Price in a Competitive Market**

In a competitive market, marginal cost tells us the social cost of producing a product, and the demand curve tells us the social benefit of producing the product. The competitive price/output is determined where marginal cost intersects the demand curve, as on the left.

Recall from previous lectures that at the competitive price/output combination social value is maximized.

**Price in a Monopoly**

Recall from the monopoly lectures that a monopolist restricts the output to the point at which $\text{MC} = \text{MR}$ and increases the price to what the market will bear.

The result of a monopoly is restricted output and higher price.
Because of the monopolist's restriction of output, you can see that there are people who would be willing to pay up to the marginal cost who are not being served. The reduced output is the difference between $Q_c - Q_m$. The shaded area in the graph on the left represents the loss of economic value from a monopoly. The loss is called **deadweight loss**.