6.2 Lecture 14: Oligopoly Continued

6.2.1 Cartels

- Cartels are fundamentally unstable (incentive to "cheat" and raise own production) and because they are illegal (antitrust laws).
- Each member has an incentive to cheat on a cartel, and they can get away with it, because their additional production is fairly small relative to the total. If one firm cheats, it gets all of the benefit of selling more quantity, but only a part of the poisoning effect – that gets shared with all other firms in the market.

6.2.2 Many firms

- Noncooperative equilibrium leads to less output and more profits than does the competitive market case
- In terms of welfare, usually perfect competition > oligopoly > monopoly
- Quantity as an indicator of social welfare. Deadweight loss in welfare analysis comes from trades that aren't made.
- As the number of firms get large, the Cournot equilibrium approaches perfect competition – as the number gets small, it approaches monopoly.

6.2.3 Price competition

- **Bertrand competition**: firms set prices (instead of quantities) at the same time
- Two firms may be enough to remove market power if products are identical
- To avoid Bertrand competition, firms can product differentiate. Identical Bertrand duopolists drive price down to marginal cost. In other words, firms will set their prices at marginal cost.

6.2.4 TO KNOW – Conceptual Understanding

- Explain why cartels are unstable
- Compare welfare from different forms of competition (monopoly, oligopoly, perfect competition)
- Know the difference between quantity (Cournot) and price (Bertrand) competition

6.2.5 TO KNOW – Graphical and Math Understanding

- Solve for price and quantity when firms compete in a model of Bertrand price competition

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