Chapter 11 McConnell, Brue and Flynn 20th

Pure Competition in the Long Run

The previous chapter discussed how pure competition operates in the short run--the time period during which the individual firms in an industry are stuck with their current plant sizes and fixed-cost commitments. As you know, pure competitors shut down their operations, if prices are too low, or, if prices are high enough, they produce where MR = MC to minimize their losses or maximize their profits. Whether they make a profit or a loss depends on how high the market price is relative to their costs.

This chapter will extend the importance of the Purely Competitive Market Model by showing the result of the freedom of firms to enter or exit the industry. We know from Chapter 2 that profits attract entry and losses prompt exit.

In this chapter, we are keenly interested in how entry and exit relate to allocative and productive efficiency, and how continuing competition leads to new products and new business methods, replacing older products and older business methods through a process aptly referred to as creative destruction.