

Regulation Of Monopoly Policy

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A monopoly may be referred to as a market scenario where only one producer has exclusive control over the supply of goods and services. In most countries, monopolies have control over a majority of the factors within the market, including natural resources. As a result of these excessive market manipulations, some consequences occur as a result of the existence of monopoly firms. Some of these consequences include price discrimination, provision of low quality and quantity goods, and due to low competition, there is no creativity and innovation in the monopoly's production process (Berg et al. n.p). Hence, the policy regarding the regulation of monopolies must be enacted to protect the customers, as well as the infant industries within the local market.

Whenever we are considering the economy, three factors come to mind: supply, demand, and price. Since a monopoly has the potential to increase prices indefinitely, this becomes its biggest disadvantage for different consumers. Lack of industrial competitiveness makes the monopoly price the price of the market, and the monopoly demand becomes the market demand (Berg et al. n.p). As the only supplier, a monopoly may also decline to provide services to its customers. The regulation of monopolies is important for the following reasons:

Prevent Excess Price

Without government regulation, monopolies would take advantage and set their prices above the equilibrium price. As a result, there would be a decline in customer welfare, and it would also lead to allocative inefficiency.

Quality Of Service

In a case where a manufacturer has monopoly power over the provision of a specific service, it may have fewer incentives to provide high-quality services. Through government regulations, standards are set, and monitoring the monopoly also ensures that these required standards of service are met.

Monopsony Power

Firms with monopoly power also have the opportunity to take advantage of the monopsony buying power. To illustrate, a supermarket may use the prevailing market situation to jam the profit margins of farmers. Government regulation ensures that these big firms do not use monopsony buying power to take advantage of the small farmers.

Promote Competition

For some industries, even if a monopoly exists, there is still a possible way to encourage competition through the support of the government.

Natural Monopolies

Due to the large economies of scale, some firms automatically become monopolies since the most efficient firm becomes the leader. However, in such cases, it becomes practically impossible to enhance competition, and therefore, it becomes essential to regulate the firm to avoid the misuse of monopoly power.

Furthermore, the growth and prevalence of monopolies may result in an economic crisis. The government would, therefore, undertake various activities to enact the policy of monopoly regulation. The government regulates monopolies in the following ways:

Price Capping By Regulators RPI-X

For the privatized industries like gas, water, and electricity, the federal government has developed various bodies that regulate these institutions. These regulatory bodies include the Office of Rail Regulator (ORR), OFGEM for regulating the electricity and gas markets, and, finally, OFWAT, which focuses on the regulation of water industries. Their most basic function is that they have the ability to control the proliferation of prices. One way they can achieve this is through the use of the RPI-X formula, where X represents the quantity by which they have to reduce their prices in real terms. So if the inflation rate is three per cent and X is one per cent, then firms can only increase the actual price by two per cent, that is $(3\% - 1\% = 2\%)$ (Mayo 210). If the regulators perceive that the firm can make efficiency savings and that it is charging its customers too much, the body can decide to increase the level of X to a higher margin. For instance, in the early years of telecom regulation, the level of X was extremely high, and this was because the efficiency savings made it possible for big cuts in prices.

For the water industry, its regulation formula varies slightly, and it is $RPI -/+K$. Where K is the investment amount, the water firm is required to implement. If a water company needs to invest in better water pipes, the institution will have to increase its prices to finance the investment. One of the advantages of regulation through RPI-X is that the regulator can set price increases based on the potential efficiency savings and the state of the industry. Also, if the firm reduces the costs it incurs by more than X, it may be able to increase its profit margins. In other words, there is an excellent incentive for reducing costs. As a final point, where there is no competition, the regulatory measure of RPI-X may be used as a means of increasing competition (surrogate competition) (Spence 423).

Nonetheless, there are also some disadvantages of this method of regulation. First, it is difficult and,

at times, costly to decide what level X should be. Second, there is the danger of regulatory recapture. This happens when the regulators become lenient on the firms, and they allow them to make supernormal profits through the increase of prices (Rochet n.p). Third, most firms argue that these regulators are stringent, and they prevent them from making adequate profit required for investment. To finish, if a firm becomes more efficient, it may be punished by having high levels of X . Thus, it cannot retain its efficiency reserves.

Merger Policy

The federal government has the policy to investigate the type of mergers that would generate monopoly power. In case a new alliance forms a firm that controls more than 25% of the market share, it is referred to the competition commission. This commission has the authority to block or allow the merger.

Breaking Up A Monopoly

In severe circumstances, the government may choose to dissolve a monopoly because the firm has become very powerful. This occurs in rare cases, for example, when the American government attempted to break Microsoft Corporation, but lastly, the action was let go.

Regulation Of Quality And Service

The regulators may also observe the quality of all services offered by each monopoly firm, such as when the rail regulators examine the safety records of railway firms to ensure that the firms do not cheat. Likewise, in electricity and gas markets, the regulators will ensure that the concerns of the old folks are considered. For example, monopolies were restricted from cutting down gas supplies during the winter period.

One of the obstacles facing the policy of regulation of monopolies is that some of these monopolies have grown to great extents, and the government can do nothing to control them. Due to the large market share that most monopolies have, the government may shy away from interfering with these organizations. This is because the government knows that if it tries to tamper with the activities of some monopolies, the economy shall suffer, thus leading to a state of economic crisis (Posner 815).

In conclusion, the regulation of monopolies is an important issue, and it needs to be addressed with seriousness. Monopolies, at times, tend to take advantage of the customers, and this is because they know there is no close competition. Due to a lack of competitiveness, they offer products of poor quality and services that are not up to the required standards. Through regulation, the government can restrict the operation of monopolies, and it also ensures that these firms provide high-quality services and products.

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