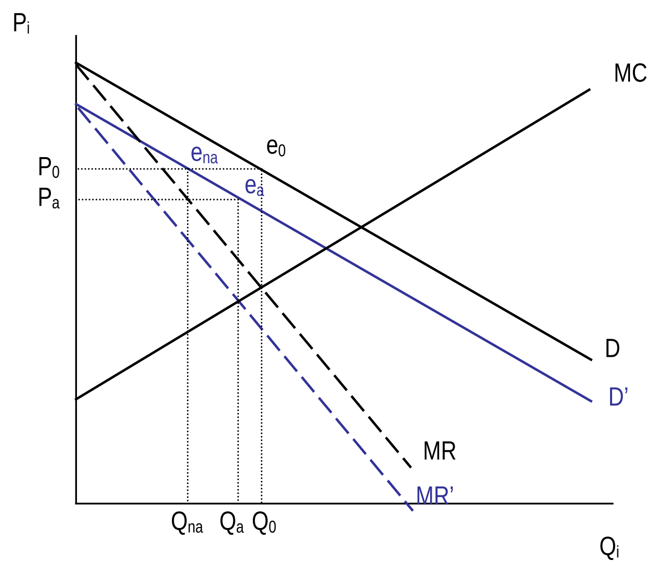
Economics 314 — Spring 2014
Daily Question #21 — March 31

The figure below shows the choice of adjusting vs. not adjusting price for a monopolistically competitive firm if other firms in the economy *do not* adjust their prices. *D* and *MR* are the original demand and marginal revenue curves, the versions with primes reflect a decline in aggregate demand.



1. Why does the marginal cost curve not shift downward in the case that other firms do not change price?

2. Why is the downward shift in the demand and marginal revenue curves relatively small when other firms do not change price?

3. Explain why e_{na} and e_a are the output/price points that the firm would choose if it, respectively, does not adjust prices or does adjust prices. Shade the area in the diagram that represents the lost profits from not changing prices.