

Minor clarification on homework 3, problem 1. 05/22/03

The monopoly "revenue" of 150 is before deducting costs. Also the "operating cost" is not incurred if the entrant enters and drops out because its cost is too high (that's what "immediately drops out" is meant to imply). So for the incumbent, pricing low incurs an immediate cost of -40. For the entrant, simply entering incurs a one-time cost of 100 (which it loses even if it enters and is knocked out immediately by a lower-cost incumbent). For the incumbent and entrant, their net profits (excluding the -40 and -100 costs noted above) if they survive are the 150 revenue minus operating cost (which is 20 or 30 for the incumbent, and 25 for the entrant).