Potsdam Research Seminar in Economics

ABSTRACT:

Market size, competition, and R&D investment by oligopolistic and monopolistically competitive firms

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Markets in many industries are dominated by a few big firms that expand their market share and intensively invest in R&D activities. Thus, this study investigates the factors that cause such firms to engage in such behavior. This study constructs a model in which oligopolistic (monopolistic) firms can (cannot) influence market conditions, assuming both types of firms can invest in R&D to improve their productivities. Accordingly, when market size increases, the outputs and R&D investments of oligopolistic firms increase relative to monopolistic firms. When oligopolistic firms are sufficiently abundant, market expansion raises their market share. Ultimately, a subsidy policy enables the economy to achieve the second-best allocation.