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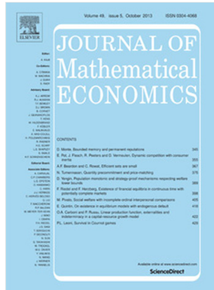

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When Do Imperfectly Competitive Firms Maximize Profits ? The Lessons from A Simple General Equilibrium Model with Shareholders' Voting

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Abstract

We consider a general equilibrium model with vertical preferences, where workers and consumers are differentiated respectively by their sensitivity to effort and their intensity of preference for quality. We consider a monopoly of which the shares are owned by a fraction of the general population. The price is determined through a vote among all the shareholders. We identify necessary and sufficient conditions for (i) an absolute (relative) majority to vote for the profit maximizing price; (ii) an absolute (relative) majority to vote for a different price. We argue that the more concentrated the ownership the more likely it is that the firm charges the profit-maximizing price.

Keywords: general equilibrium, profit maximization, vertical preferences, majority vote.

JEL codes: D4, D5, L2.

1 Introduction

Though its shareholders may have diverging preferences and may pursue very different interests, it is standard in the economic literature to assume that a firm's unique objective is profit maximization. This assumption is perfectly consistent with the heterogeneity of shareholders' objectives as long as the firm is a price-taker. But it has long been recognized (see for instance Marshall,1940, p. 402) that this ceases to be true when one moves to an imperfectly competitive environment[1]. This has been emphasized among others by Gabszewicz and Vial

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[1]Dierker and Grodal (1999) interestingly remembered that "the decision problem a multi-owner firm has to face presented a major motivation for K. Arrow to develop his theory of social choice".