Managerial Economics
Unit-4 Market Structure

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Market Structure: Market Structure Perfect Competition, Imperfect competition – Monopolistic, Oligopoly, duopoly sorbent features of price determination and various market conditions.

In This Unit We Cover the Following Topics

Please welcome for any correction or misprint in the entire manuscript and your valuable suggestions kindly mail us brijrbedu@gmail.com.

4.1 MARKET

Market in common parlance means a particular place where buyers and sellers meet for exchange (purchase & sales) of goods & services. In economics, the term market refers to the whole of region in which buyers and sellers of a commodity are in competition with one another.

According to *Chapman*, "The term market refers not necessarily to a place but always to a commodity and the buyers and sellers who are in direct contact with one another."

Thus, market refers as an area over which buyers and sellers negotiate the exchange of a well-defined commodity.

Features of Market

There are following features of market.

Commodity→ For the existence of market, a commodity is essential which is to be bought and sold. There cannot be a market without commodity.

Buyers & Sellers→ Buyers & sellers are also essential for market. Without buyers & sellers the sale & purchase activity cannot be conducted which is essential part of a market.

Area→ There should be an area in which buyers and sellers of the commodity exist. It is not essential that the buyers and sellers should come to a particular place to transact business.

Close Contact→ There should be close contact and communication between buyers and sellers. This communication may be established by any method, not necessarily by physical contact.

Competition→ There should be some competition among buyers and sellers of the commodity in a market.

4.2 TYPES OF MARKET STRUCTURES

There are following types of market structures.

1. Perfect Competition.
2. Imperfect Competition.
   a) Monopoly.
   b) Monopolistic Competition.
   c) Oligopoly.

Distinguishing Features of Various Types of Market Structures

Assumptions	Market Types			
	Perfect Competition	Monopolistic Competition	Oligopoly	Monopoly
Number of Sellers	Many	Many	Few	One
Product Differentiation	None	Slight	None to Substantial	Extreme
Degree of Control over price	None	Some	Some	Very considerable
Type of Goods	Homogeneous product	Differentiated product	Homogenous & Differentiated product	No substitute product
Entry & Exit of Firms	Free	Free	Difficult	Very difficult
Price	Perfect Knowledge	Non-Price Competition	Non-Price Competition	Price Discrimination
Examples	Agricultural products	Firms manufacturing Tooth pastes	Firms manufacturing Cars	Indian Railways, Torrent Power in Agra

4.3 PERFECT COMPETITION

Perfect competition exists when there are a large number of buyers & sellers of a homogeneous or identical product and its prices is determined by the forces of demand and supply. In this, all buyers and sellers are fully aware of the prices at which transactions take place and no seller can influence the prevailing price by his independent action. In such a market, industry is the price maker and firm is price taker.

Thus, a commodity sells at the same price since every seller takes the price as given by the industry. The seller, at this given price, can only decide how much to sell in the market.

The products in the market are standardized and homogenous and are perfect substitutes of one another. Firms are free to enter or leave the market. There is perfect mobility of factors of production.

Features of Perfect Competition

Large number of buyers & sellers→ There are a large number of buyers and sellers of the commodity in this market. Due to large numbers none of them can influence the prevailing price in the market. In fact, the price of the commodity is determined by the aggregate demand and the aggregate supply in the whole industry.

Homogeneous Product→ Products sold in the market are homogeneous, i.e., they are identical in all respects like quality, color, size, design, etc. They are perfect substitutes of one another. The products sold by different firms in the market are equal in the eyes of the buyers.

Free Entry & Exit of Firms→ There is no economic, natural or social restriction on the entry & exit of a new firm into the industry. Old firms are free to leave the industry. If the industry is making profits, new firms can enter the market to earn profits. Similarly, if the industry suffers losses, some individual firm may quit the market.

Perfect Knowledge of Market→ The buyers & sellers have perfect knowledge about the prices and costs prevailing in the different parts of the market. Advertisement & selling techniques do not affect the buyer's preferences. Clearly, this leads to emergence of uniform price of the product.

Perfect Mobility of Factors of Production→ There is perfect mobility of factors of production within different regions, industries, and firms without any hindrance. The factors are free to enter an industry if considered profitable and leave the industry when remuneration is inadequate.

4.4 MONOPOLY

The term 'monopoly' is made of two words: mono + poly. Here 'mono' means one and 'poly' implies the seller, thereby the literal meaning of the word Monopoly is one seller or one producer. Thus, monopoly refers to that form of market organization wherein there is a single firm or producer producing a commodity for which there are no close substitutes.

Monopoly is the opposite of perfect competition. It exists whenever an industry is in the hands of a single producer due to which he has the power to influence the market price. By reducing its output, it can force the price up, and by increasing its output it can force the price down. Therefore, the firm itself is the price maker and not the price taker.

Features of Monopoly

Single Seller→ There is only one seller or producer of a commodity in the market. As a result, the monopoly firm has full control over the supply of the commodity. The monopolist may be an

individual, a firm or a group of firms, or a Government Corporation or even Government itself. Naturally, a monopoly firm can exploit the buyers by charging almost any price for its product.
No Close Substitutes→ The product sold by the monopolist in the market has no close substitute. Though some substitutes of the product may be available yet either they are not close substitutes or not accessible to the buyers or both.
Difficult Entry of Firm→ The monopolist controls the situation in such a way that it becomes very difficult for a new firm to enter the monopoly market and compete with the monopolist by producing a homogeneous or identical product. The monopolist tries his utmost block the entry of a new firm.

4.5 MONOPOLISTIC COMPETITION

Monopolistic competition refers to a market situation in which there are many firms which sell closely related but differentiated products. Although the products are substitutes of each other yet they can be differentiated from each other on the basis of color, quality or brand name.

According to J.S. Baing, "Monopolistic competition is found in the industry where there is large number of small sellers, selling differentiated but close substitute products."

According to Leftwitch, "Monopolistic competition is a market situation in which there are many sellers of a particular product but the product of each seller is in some way differentiated in the minds of consumers from the products of every other seller."

The market is called monopolistic competition since it contains both the competitive element and monopoly element. There is competition among a large number of firms and at the same time each firm enjoys some measure of monopoly because of its brand name, color, size or shape of its product. As a result, competitive element keeps the price of the product in a close range. Markets of products like toothpastes, shoes, cycles, Television, pens, pain killing drugs, etc. are examples of monopolistic competition.

Features of Monopolistic Competition

Large number of Sellers→ The number of firms selling similar product is fairly large but not very large as in perfect competition and have a small share in the market. As a result, firms are in a position to influence marginally the price of the product due to its brand name.
Product Differentiation→ The products of different firms are not identical but can be substituted for one another. Products are not the same but are closely similar to each other. But still they are not perfect substitutes. The products of different sellers are differentiated on the basis of brands. These brands are generally so much advertised that a consumer starts associating the brand with a particular manufacturer and a type of brand loyalty is developed.
Free Entry or Exit→ New firms can enter the market if found profitable. Similarly, inefficient firms already operating in the market are free to quit the market if they incur losses.
Non-price competition→ Sellers try to compete on basis other than price, as for example, aggressive advertising, product development, better distribution arrangements, efficient after-sales services, and so on. Sellers attempt to promote their products not by cutting prices but by incurring high expenditure on publicity and advertisement and other sales promoting techniques.

4.6 OLIGOPOLY

Oligopoly is often described as '*competition among the few*'. When a few big firms (three to seven) in a market selling their homogeneous products (steel or cold drinks) or differentiated products (bikes or cars), oligopoly is said to exist. Here entry of a new firm in the industry is quite difficult. In this way, position of oligopoly lies between that of monopolistic competition and monopoly.

Features of Oligopoly

A few sellers→ There are few firms each of which produce a substantial part of total output of the industry. Number of firms is so small that each seller knows that he can influence the price by his own action.
Interdependence→ There is interdependence in decision-making of the few firms which comprise the industry. This is because when the number of competitors is few, any change in price, output, product, by a firm will have direct effect on the fortune of the rivals, who will then retaliate in changing their own prices, output or advertising techniques.
Price rigidity→ Mostly prices are stable since no firm dares to change the price for fear of retaliatory actions by rival firms.
Advertising & selling costs→ Due to interdependence, the firms have to employ various aggressive and defensive marketing weapons to gain a greater share in the market or to maintain their share. For this various firms have to incur cost on advertising and other measures of sales promotion.
Non-price Competition→ The firms avoid price cutting and try to compete on non-price basis because if they start under cutting one another, a type of price-war will emerge which will drive a few of them out of the market, as customers will try to buy from the seller selling at the cheapest price.

4.7 DIFFERENCE BETWEEN PERFECT COMPETITION & MONOPOLY

S.No.	Perfect Competition	Monopoly
1)	There are a large number of firms in the market and no single firm can influence the market.	There is only one firm in the market and it has the power to influence the market.
2)	Products are having perfect substitutes.	Products have no substitute.
3)	There is the free entry & exit of the firms.	There is restriction or very difficult entry of a new firm.
4)	Firm is the price-taker, not the price-maker.	Firm is price-maker, not price-taker.
5)	Prices are uniform in the market, as there is no price discrimination.	There is price discrimination, i.e., a firm charges different price from different customers.
6)	In the long run, a firm earns only normal profit.	In the long run, the firm manages to earn abnormal profit.

4.8 DIFFERENCE BETWEEN PERFECT COMPETITION & MONOPOLISTIC COMPETITION

S.No.	Perfect Competition	Monopolistic Competition
1)	There are a large number of firms in the market and no single firm can influence the market.	There is fairly large number of firms in the market but has some control to influence the market.
2)	Products are homogenous.	Products are differentiated.
3)	Perfect competition among the seller in the market.	Both the situations exist side-by-side competition between sellers as well as monopoly of the firm.

4)	A firm cannot have independent price policy. It is price-taker, not the price-maker.	A firm can have independent price policy. It is price-maker.
5)	No selling costs for promoting sales due to homogeneous product.	Significant impact of selling cost through various types of advertisements.

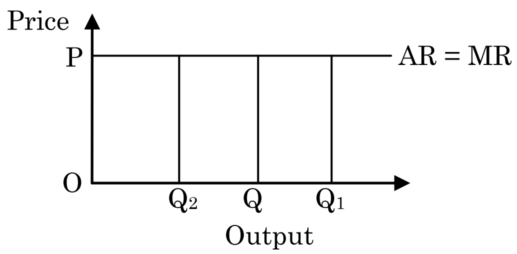
4.9 DIFFERENCE BETWEEN PERFECT COMPETITION & MONOPOLY

S.No.	Monopolistic Competition	Monopoly
1)	There is fairly large number of firms in the market but has some control to influence the market.	There is only one firm in the market and it has the power to influence the market.
2)	Products are differentiated.	Products are homogeneous.
3)	Products have many close substitutes.	Products have no substitute at all.
4)	There is the free entry & exit of the firms.	There is restriction or very difficult entry of a new firm.
5)	Both the situations exist side-by-side competition between sellers as well as monopoly of the firm.	No competition in the market due to one seller.
7)	Significant impact of selling cost through various types of advertisements.	No significant impact of selling costs due to only one product in the market.
8)	Price discrimination by an individual firm is not possible.	There is price discrimination, i.e., a firm charges different price from different customers.
9)	In the long run, a firm earns only normal profit.	In the long run, the firm manages to earn abnormal profit.

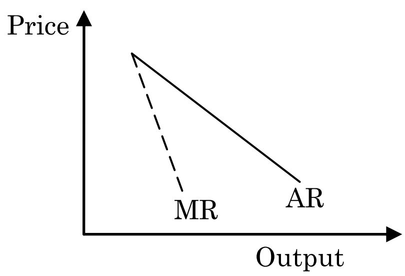
4.10 PRICE DETERMINATION UNDER VARIOUS MARKET CONDITIONS

where AR = Average Revenue, MR = Marginal Revenue

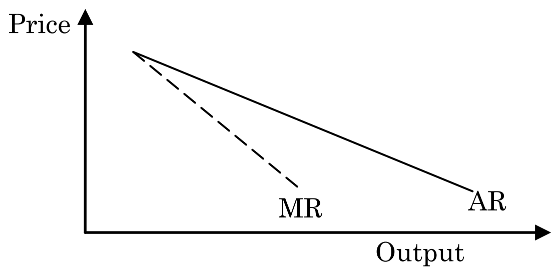
Perfect Competition



Monopoly



Monopolistic Competition



Oligopoly