1 MARKET STRUCTURE PERFECT COMPETITION AND MONOPOLY EXTREME CASES

1.1 *Market Structure*

1.2 *Types of Markets*

1.3 *Two Extreme Cases*

(a) *Perfect Competition*

(b) *Monopoly*

1.1 MARKET STRUCTURE

Market is usually understood as a place where sellers (producers) and buyers meet for settling a transaction. A market is also defined "as a group of firms and individuals that are in touch with each other in order to buy or sell some good." In today's situation with the progress in the communication system, it is not necessary to have a physical or personal contact in a physical or geographical market area. Transactions take place through electronic commerce, mobile commerce or with the help of other communication media. What is essential is to have a communication between the buyer and seller for settling a transaction.

Depending on the commodity and supporting factors a market can be local, national or international. For company stocks / shares the markets have become national and in certain cases they are

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internationally traded. Currency market is an example of international market.

A given type of market within the market structure depends on many factors such as (i) nature of commodity, (ii) freedom of entry and exit, (iii) control over supply, (iv) control over price, etc. Based on the above and other factors there are different types of markets which together form the structure of market in the economy.

1.2 TYPES OF MARKETS

A market structure comprises different forms of markets. To which type a market belongs depends on a number of factors. They include the number of sellers and buyers, the nature and characteristics of a commodity, the influence exercised by the sellers or buyers in the market, the role, need and effects of advertisement or selling cost and a host of other factors.

In this section we are dealing with commodity markets, that is, where goods and services are bought and sold. In economic analysis markets are generally classified into four categories, that is (1) Perfect Competition, (2) Monopoly, (3) Oligopoly and (4) Monopolistic Competition.

1. **Perfect Competition** is a market situation where we have a large number of sellers and buyers. The commodity sold is identical with no quantitative and qualitative differences. The large number of buyers and sellers naturally prevent a single seller or buyer from influencing the price. In a perfect competition a seller is a price taker. He accepts the price determined in the market by the total demand and supply. Commodity being identical there is no scope for any price differential and discrimination. Both sellers and buyers have complete information of market which helps establish uniform price.

   There is no restriction for any person to produce and sell the existing commodity. So also whoever wants to exit from the market is free to do so. Examples are market for agricultural commodities and street food vendors (as suggested by some

economists) in developing countries. They, however, are only a nearby examples.

2. **Monopoly** market is different from perfect competition. Here we have one producer (seller) selling the homogeneous or an unique product. The producer has almost near total control on the supply hence he can decide the price and output. However in order to maximise the profit he would control either price or output. Being a sole supplier he could discriminate the price between buyers as well as between markets.

Like perfect competition it is difficult to have a real situation of monopoly market where a producer has a total control over the supply. The nearest example that we can have are the public utility services which are usually controlled by the government. Railway services are the monopoly of the Central Government. Similarly BMC is the sole supplier of drinking water.

It is expected that the government would not exploit the consumers since it has a responsibility to enhance the welfare of the community. Wherever such a monopoly is allowed in the private sector, the government acts as a regulator.

Entry to the market is highly restricted or almost nil. If the entry is allowed then the market would not remain as a monopoly.

Advertising may be resorted to only as a informative devise in order to make consumers aware of the existence and usefulness of the product.

3. **Monopolistic competition** is a market situation where there are many sellers, selling differentiated products. Garments, soaps and detergents are some examples. Monopolistic competition is clearly visible in retail trade where sellers sell differentiated products.

Entry to the market is not difficult though not as free as perfect competition. Since a product is differentiated, restricting the entry through patent right is difficult.

Product differentiation is done through a different design, size, colour and other characteristics associated with the product. However the products remain close substitute to each other.

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Selling cost is the essential aspect of monopolistic competition. Each producer tries to convince the consumer that his product is better than that of his competitors. Advertisements through different media is resorted to. Non-price competition like additional discount, longer warranty period, etc. is also widely prevalent.

Demand for the product of a monopolistic competitive firm is elastic since the products are close substitutes.

Though price is determined by the market forces yet there is enough scope for price differentiation based on product differentiation. Each firm may claim its product is superior to its substitute in terms of quality attributes.

4. **Oligopoly** market has few sellers selling standardised or differentiated commodities. The common examples are airlines, automobile manufacturers, computer manufacturers, steel, cement, medical drugs, chemicals, petroleum, broadcasting / telecasting.

Entry to oligopoly market is free, however in reality it is very difficult as there are many barriers such as technology, finance etc. Being small in number there is a possibility of these firms joining together and forming a cartel, as is the case of organisation of petroleum exporting countries (OPEC). Oligopoly firm may have an implicit understanding whereby they influence price.

Each firm may have some influence over the price specially when the product is differentiated. Price of a oligopoly product can be decided by a dominant firm which becomes a leader.

Advertising is also resorted since oligopoly firms compete with each other. They also indulge in non-price competition to attract customers.

If the number is small, there is always a tendency for the firms to come together and form a cartel for the purpose of increasing price and profits.

There is also a possibility of the oligopoly marketing turning into monopoly through mergers and acquisition.

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Table 1.1 : Market Structure and Characteristics

Market Structure	Examples	No. of Produ-cers	Nature of Product	Power to influence Price	Barriers to Entry	Non price Competition
Perfect Competition	Some agricultural commodities	Large	Standardised (identical)	None	Nil	None
Monopoly	Public utilities	One	Unique Product	Consi-derable	Very High	Advertising (Informative)
Oligopoly	Computers, Crude oil, Steel, Airlines	Few	Standardised or Differentiated	Some	High	Product differentiation and Advertising
Monopolistic Competition	Garments	Many	Differentiated	Some	Low	Product differentiation and Advertising

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