HSS 201: Economics for Engineers

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What is Market

It is a place where buyers and sellers of goods and services meet. Based on the number of sellers, a new market structure evolves.

1. Perfect Competition
2. Monopolistic Competition
3. Oligopolistic Competition
4. Monopoly

Perfect Competition

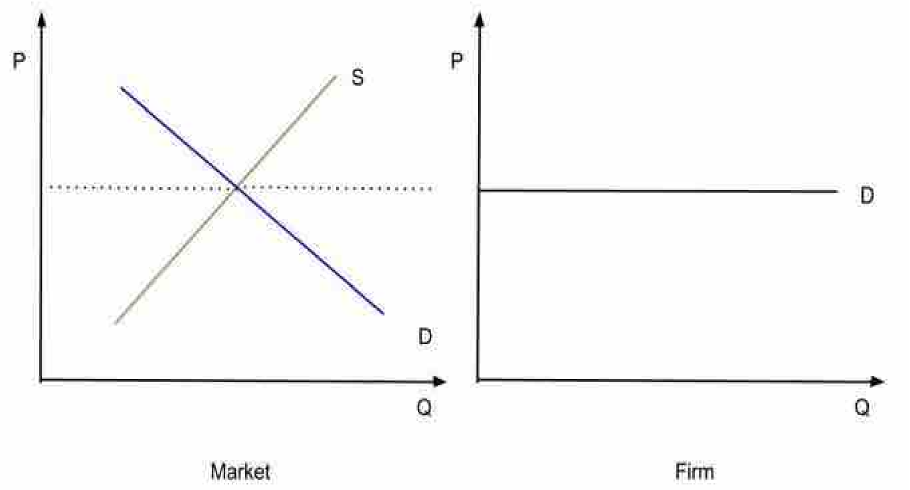
The Assumptions

1. Large No. of Buyers and Sellers
2. Homogeneous Products
3. Free Entry and Exit of Firms
4. Perfect Information
5. Zero Transportation Cost
6. Perfect Mobility of Factors of Production

Pure Competition: 1 - 3

Perfect Competition: 1 - 6

Demand and Supply in Perfectly Competitive Market



Possible Examples of Perfect Competition

1. Share Market
2. Agricultural Market

Monopoly

A monopoly is a market that has only one seller but many buyer.

The firm is a price maker and it can practice price discrimination.

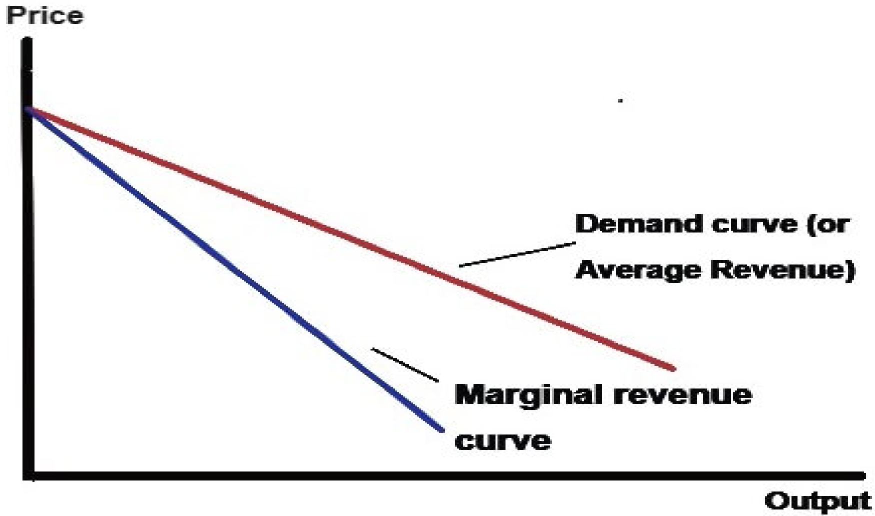
There is a restriction on entry to the market.

Revenue Equations of Monopoly

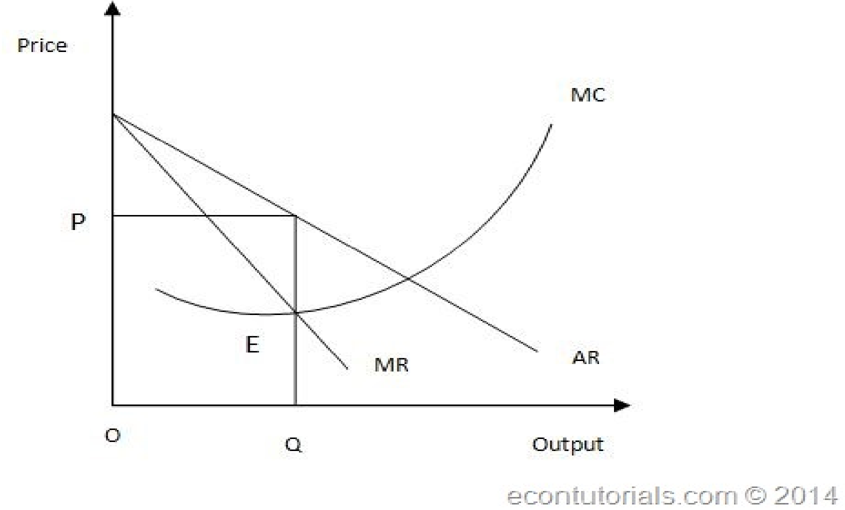
$$
\begin{aligned}
\text{TR} &= P(Q).Q \\
\text{AR} &= P(Q) \\
\text{MR} &= P(Q) + Q.\frac{dP(Q)}{dQ}
\end{aligned}
$$

The AR curve is the demand curve for a monopolist.

AR and MR Curves for a Monopoly



AR and MR curves in Monopolistic Competition



Examples

1. Indian Railways
2. Police
3. Forest Management
4. Army
5. Microsoft, a virtual monopoly

Monopolistic Competition

Chamberlin defines the monopolistically competitive industry as a 'group' of firms producing a 'closely related' commodity but not perfect substitutes of each other are called product group.

Characteristics

1. There are many or large number of firms
2. Products are differentiated; however they are close substitute of each other
3. Free unrestricted entry and exit
4. Presence of selling cost

   Independent decision making and multiplicity of prices
5. Imperfect knowledge – Information about cost, quality, price etc. is not uniformly available to all buyers and sellers in the market

Oligopolistic Competition

In markets, where firms have to take into account the actual and potential responses from rival firms. It is characterized by few sellers in the market.

There are only few dominant sellers in the market and sell either homogeneous or heterogeneous products. Firms decision making is interdependent.

Sometimes, to restrain competition, firms jointly decided on hou much to produce and how the total production is to be allocated between the different firms in the cartel. The joint decision means that the cartel can act like a monopoly. The firms mostly deal in homogeneous products.

If the number of firms is two in the industry and the competition is particularly called 'duopoly'.

There is a huge entry barrier in such industry in the form of high investment (say) and knowledge is imperfect.

Kinked Demand Curve for a Firm Under Oligopoly