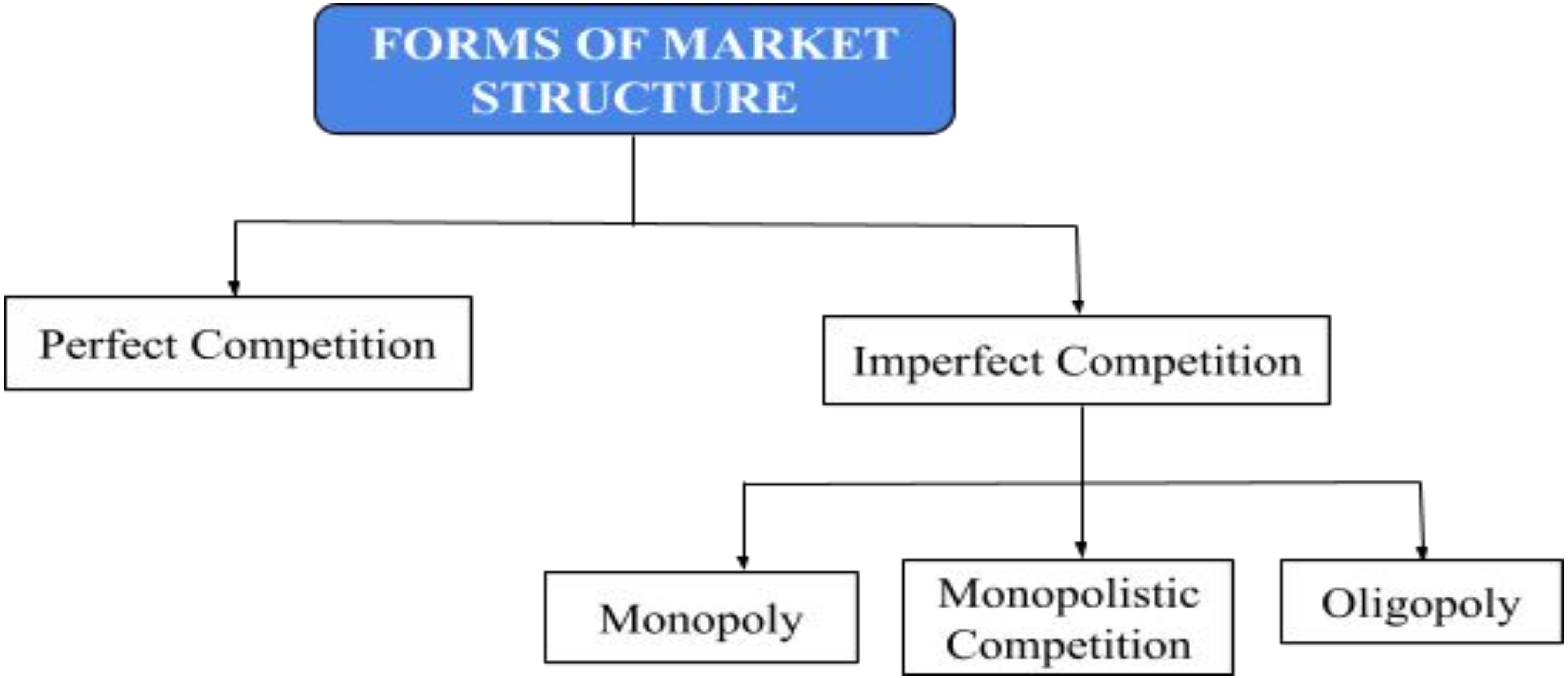
Market- Introduction

- Market is a term which is commonly used for a particular place or locality where goods are bought and sold.
- In economics market need not be specific place
- Agents and action – Consumers /producers(buyers/sellers)-demand and supply
- According to Prof. Samuelson, "A market is a mechanism by which buyers and sellers interact to determine the price and quantity of a good or service."

Based on competition, the market structure has been classified into two broad categories:

1. **Perfectly competitive. (Perfect Competition)**
2. **Imperfectly competitive. (Monopoly, Monopolistic competition and Oligopoly)**


FORMS OF MARKET STRUCTURE
Perfect Competition
Imperfect Competition
Monopoly
Monopolistic Competition
Oligopoly

Study points

- Definition
- EG
- Features
- Equilibrium

Definition

- **Perfect competition is defined as a market structure in which an individual firm producing homogenous commodities cannot influence the prevailing market price of the product on its own.**
- Perfect competition is a market structure characterized by complete absence of rivalry among individual firms .
- Price is determined not by firm by the industry

Example

- In reality its myth,
- Closet eg is for agricultural commodities(wheat and rice)

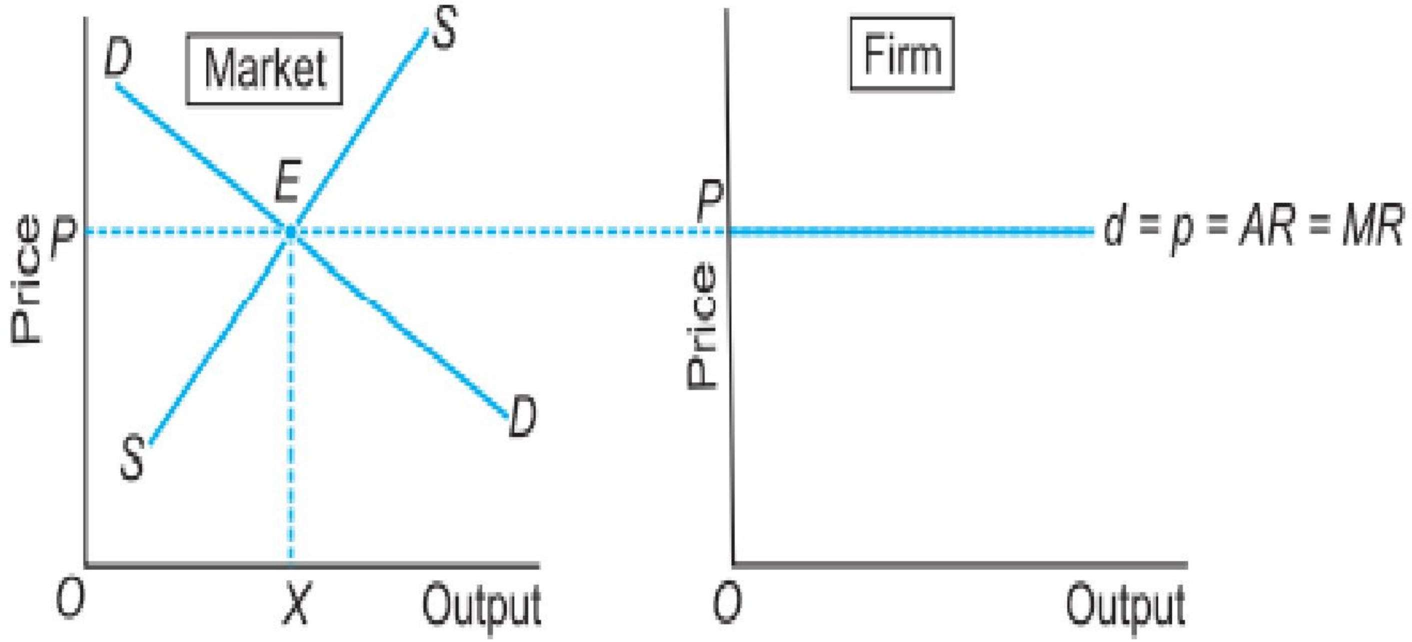
Features

- Very Large Number of Buyers and Sellers
- Homogeneous Product
- Free Entry or Exit of Firms
- Perfect Knowledge
- Perfect Mobility of Factors of Production
- Absence of Transportation Cost
- Absence of Selling costs

Features-

1. Very Large Number of Buyers and Sellers

- There are so many buyers and sellers that no individual buyer or seller can influence the price of the commodity in the market. He is a price-taker having no bargaining power in the market.
- The demand curve facing a firm is derived from the market equilibrium. In a perfectly competitive market, price of the commodity is determined by the intersection of the market demand and supply curves of the commodity. This occurs at point E where DD = SS.


Market
Firm
Price
Price
D
D
S
S
E
P
P
$d = p = AR = MR$
O
X
Output
O
Output

2. Homogeneous Product

Firms in the market produce a homogeneous product. Homogeneity of a product implies that one unit of the product is a perfect substitute for another. Products are homogenous in size, shape,quality.

3. Free Entry or Exit of Firms

The industry is characterized by freedom of entry and exit of firms(no cost involved). In a perfectly competitive market, there are no barriers to entry or exit of firms. Entry or exit may take time, but firms have freedom of movement in and out of an industry. Firms will earn only normal profit in long run.(normal profit profit just needed to carry out business.

4. Perfect Knowledge

Firms have all the knowledge about the product market and the factor market. Buyers also have perfect knowledge about the product market. uniform price exist and followed by sellers and buyers

5. Perfect Mobility of Factors of Production

The factors of production can move easily from one firm to another. Workers can move between jobs and between places.There is no geographical or occupational restriction.

6. Absence of Transportation Cost

All goods are produced locally. Transportation costs are zero.A producer can sell product at any place and buyer can buy from any place.

7. Absence of Selling costs-

Costs refers to advertisement of the product. It is zero.Since its assumed that buyers and sellers are aware of product and cost in market.

Imperfect Market structures

Monopoly-

- The word monopoly is derived from two Greek words ‘mono’ means single and ‘polo’ means to sell
- Monopoly is a market in which a single seller sells a product which has no substitutes
- • E.g. RBI , Rail transport

features

1. High barriers of entry
2. Price maker
3. Profit maximizer
4. No close substitutes
5. Single seller

6. price discrimination

Features of Monopoly

1. High barriers of entry:

Competitors are unable to break into the market due to a single company's control of it. Firms earn abnormal profits in long run. Barriers can be due to legal restrictions like licensing or patents or restrictions created by existing firms

2. Price maker: The Company that operates the monopoly can determine the price of its product without the risk of a competitor undercutting its price. A monopoly can raise prices at will. Firm and industry is same. So firms controls industry output. Influence price by changing supply.

3. Profit maximizer: a monopoly maximizes profits. Due to the lack of competition a firm can charge a set price above what would be charged in a competitive market, thereby maximizing its revenue.

4. No Close Substitutes. There are no close substitutes for the commodity. Eg electricity distant substitutes like inverter

5. Single seller:

In a monopoly one seller produces all of the output for a good or service. The entire market is served by a single firm. For practical purposes the firm is the same as the industry. Large of buyers exist for their products, no single buyer can influence price.

6. Price discrimination: in a monopoly the firm can change the price and quantity of the good or service. It is the act of charging different prices for the same product from different consumers. EG:same railway ticket sold at diff prices, electricity charges are different according to areas and function

examples

100%
IRCTC
Rail Network
100%
हिएलि HAL
Aviation Defence
96.5%
Nestlé
Cerelac
Presented by:
Trade Brains
Visit: portal.tradebrains.in
TOP INDIAN
COMPANIES
with
MONOPOLY
82%
Pidilite
Adhesive
68.2%
कॉनकॉर CONCOR
Cargo Carrier
70%
marico
Oil Products
73%
ITC Limited
Cigarettes
77%
HINDUSTAN ZINC
Zinc Mining
78%
कोल इण्डिया Coal India
Coal Mining

examples


Monopoly Examples
Railways
Luxxotica
Microsoft
AB InBev
Google
Patents
AT&T
Facebook
WallStreetMojo

Regulation of Monopoly

1. **Promote competition**. In some industries, it is possible to encourage competition, and therefore there will be less need for government regulation.

2. **Quality of service**. If a firm has a monopoly over the provision of a particular service, it may have little incentive to offer a good quality service. Government regulation can ensure the firm meets minimum standards of service.

3. **Prevent excess prices**. Without government regulation, monopolies could put prices above the competitive equilibrium. This would lead to allocative inefficiency and a decline in consumer welfare

Monopolistic competition

- Monopolistic competition is a type of imperfect competition such that many producers sell products that are differentiated from one another.
- It is a market structure at which large number of sellers dealing with differentiated commodities.
- The main feature of monopolistic competition is Product Differentiation

Product Differentiation means commodities marketed by each seller can be distinguished from the products marketed by other seller in the form of size, shape, brand, color etc..


Monopolistic Competition Examples
Smart Phone
iPhone
Samsung
Soft Drink
Coca-Cola
Pepsi
Clothing
ZARA
H & M
Taxi
Ola
Uber
EDUCBA


Monopolistic Competition Examples
Bakery Products
Bread
Cookies
Pastry
Hairdressing Industry
Hair Color
Hair Cuts
Facial
Restaurants
Burger
Pizza
Samosa
EDUCBA

Features of Monopolistic Competition

1. Large number of sellers and buyers

2. Product Differentiation
3. Freedom for entry and exit
4. Advertisement and selling cost
5. Non-Price Competition
6. Price control
7. Lack of perfect knowledge

Features

- 1. Large Number of Firms and Buyers:

Firm producing differentiated product and sellers are large in numbers in monopolistic competition but not as large in perfect completion. This means each has price output control to certain extent.

2. Product Differentiation

Product differentiation is the main feature of monopolistic competition.

Product differentiation means that product of different types, brands, and qualities will be available to customers in a fixed time period. Product differentiation occurs when buyer of product can differentiate between two products.

In this, firms are in large number but their products are different from each other in anyway, but these products are close substitutes of each other. Product differentiation is obtained due to characteristic of product like shape, measurement, colour, durability, quality etc. There are many examples of product differentiation like bath soaps Lux, Godrej, Camay, Rexona, etc.

3.Freedom of Entry and Exit of Firms

In the situation of monopolistic competition there is freedom of entry and exit of firms in the industry like perfect competition.but new firms will have to face some difficulty because esome productswill have legal patents.eg:

No rival firm can produce a product similar to woodland shoes

4. Selling Cost

- An important characteristic of monopolistic competition is that every firm spends more money in promoting its product under it. Firm gives advertisements in newspapers, cinemas, magazines, radio, T.V. etc. for selling its product in the maximum amount. The investment done on all these is called as Selling Costs.

5.Non-Price Competition

- :The main characteristic of monopolistic competition is that under it different firms without changing the costs of products compete with each other like the example of companies producing ‘Surf’ and ‘Ariel’. If you take a box of ‘Surf’, you will get a glass utensil similarly, with the box of ‘Ariel’ you will get the steel spoon. In this way, firms, by providing different types of facilities and products etc. to customers to attracts them toward their products. This type of competition is called as Non-Price Competition

6.Price control

- In monopolistic competition, a firm has control on cost of its production due to the product differentiation. But due to the availability of close substitute of opposite product firms do not have full control on cost in monopolistic competition. The cost of every firm is affected by cost policy of its competitors in market up to the certain limit.

7. Lack of perfect knowledge

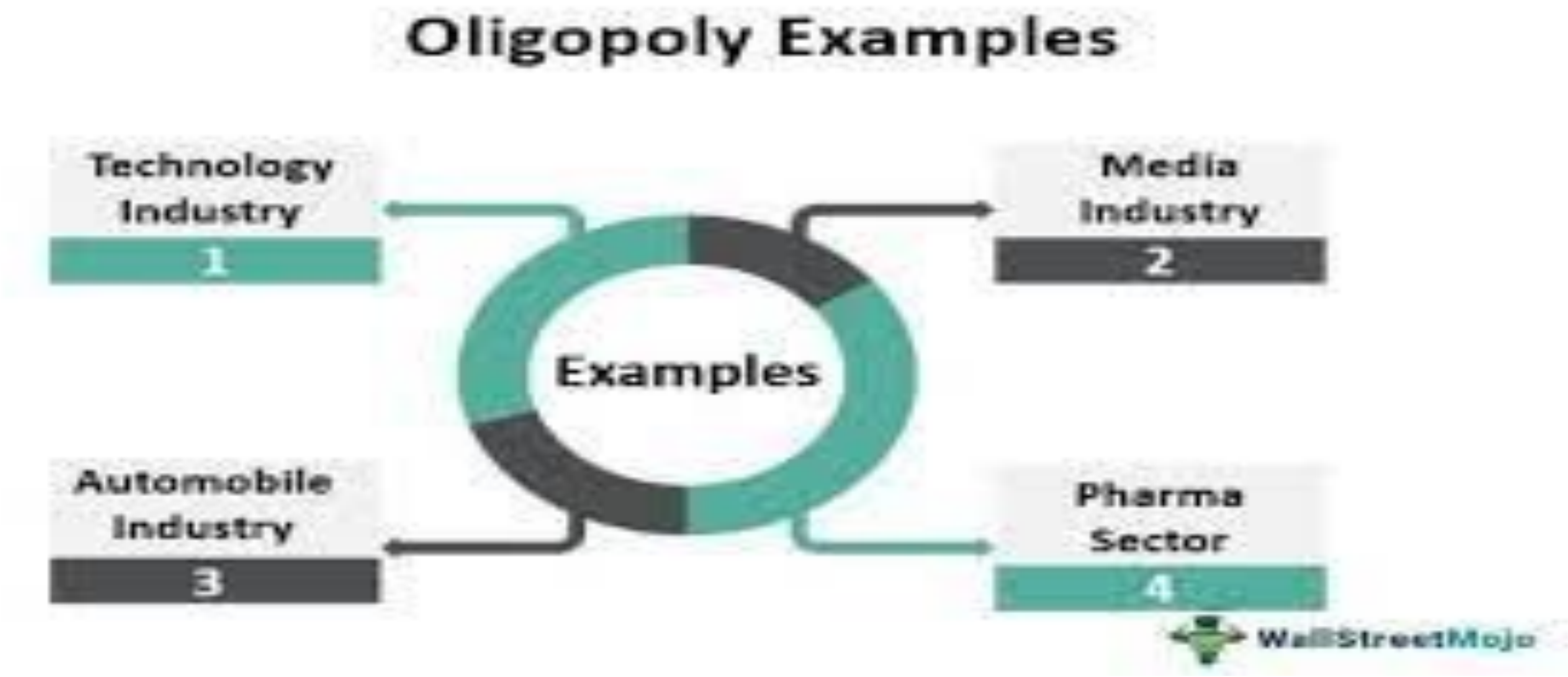
- Buyers and sellers don't have perfect knowledge about market. There are many products available being substitute for other but buyers may not be aware about this.

Comparison between three markets

Sl no	Reference	Perfect competition	Monopolistic competition	MOnopoly
1	Number of buyer and sellers	large	large	One seller and large buyers
2	product	homogenous	Product differentiation	Homogenous or differentiated
3	price	uniform	Not uniform because of product differ enation	Price discrimination
4	Entry of firms	Free entry	Not absolute freeedom	Not possible
5	Knowledge of market conditions	Perfect knowledge	Imperfect knowledge	Imperfect knowledge
6	Firm demand curve	Perfectly elastic	Relatively more elastic	Relatively less elastic
7	Degree of price control	No control over	Partial control	Full control over

Oligopoly

- **An oligopoly is a market characterized by a small number of firms who realize they are interdependent in their pricing and output policies. The number of firms is small enough to give each firm some market power.**
- The word oligopoly is derived from two Greek words ‘Oligo’ means few and ‘Polo 'means to sell.
- It is a market with few sellers dealing with homogenous and differentiated commodities.
- In oligopoly one firm’s action will cause its competitors to react. This shows that firms has interdependence under oligopoly.



Oligopoly Examples
Technology Industry
1
Media Industry
2
Examples
Automobile Industry
3
Pharma Sector
4
WallStreetMojo

Oligopoly in tele communication industry India

Features

1. Few Firms with Large Market Share
2. High barriers to entry
3.Interdependence
4.Inderterminate demand curve

- **Features of Oligopoly**
- 1. Few Firms with Large Market Share

- A market may have thousands of sellers, but if the top 5 firms have a combined market share of over 50 percent, it can be classified as an oligopolistic market. This is because the power is concentrated between a few sellers who are able to exercise power over the market.

2. High Barriers to Entry

- Oligopolistic firms maintain their position through a number of barriers to entry. For instance, brand loyalty, patents, and high start-up costs are but to name a few. These make it difficult for new entrants to build a presence in the market and attract customers.

3. Interdependence

Any action a firm takes in an oligopolistic market will strongly affect the actions of its competitors.

- The firms under oligopoly may produce homogeneous or differentiated product.

5. Under oligopoly, the exact behaviour pattern of a producer cannot be determined with certainty. So, demand curve faced by an oligopolistic is indeterminate (uncertain).

Kinked demand curve

- A kinked demand curve illustrates the interdependent behaviour of firms in oligopolies
- It suggests that if one firm raises its price, the other firms in the market will not follow, leading to a sharp drop in demand for the first firm's products, which can result in reduced profits.

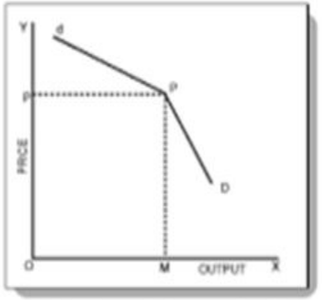


Fig. 1 : Kinked Demand Curve under oligopoly

Collusive Oligopoly

Collusive Oligopoly Sometimes, firms may try to remove uncertainty **related to acting independently and enter into price agreements** with each other. This is collusion.

- Collusion is either formal or informal. It can take the form of cartel or price leadership.
- A cartel is an association of independent firms within the same industry which follow the common policies relating to price, output, sale, profit maximization, and the distribution of products.
- In the oil and gas industry, the Organization of the Petroleum Exporting Countries (OPEC) is often used as an example of a cartel.

Cartel vs Collusion

- A cartel is an **agreement of cooperation formed between competitors in a specific industry.**
- Cartels are made up of companies in the same industry that traditionally compete against each other, but who have realized that it is mutually profitable for all players in the marketplace to work in cooperation to control market conditions.
- **Members of a cartel restrict levels of production and output thereby creating high demand for the product** and pushing prices higher beyond the equilibrium prices.

Collusion is a secretive agreement between two or more organizations, formed with the aim of gaining illegal mutual benefits.

- An example of collusion would be two companies that operate in the same industry secretively agree on a scheme to fix prices, thereby eliminating competition between the two firms.
- The main difference between cartel and collusion is that a cartel is more organized and is a formal arrangement such as the OPEC, whereas collusion is informal in nature and involves firms secretively fixing prices and agreeing not to compete in certain areas of the market.

- **Price leadership** is based on informed collusion. Under price leadership, **one firm is a large or dominant firm and acts as the price leader who fixes the price for the products while the other firms allow it.**

Non-price competition

- Non-price competition involves ways that firms seek to increase sales and attract custom through methods other than price. Non-price competition can include quality of the product, unique selling point, superior location and after-sales service.

- **Forms of non-price competition**
- Loyalty card – Some big business have invested considerably in loyalty cards which give ‘rewards’ or money back to customers who build up points/spending.
- Subsidized delivery - Amazon has been successful at pushing Prime Delivery accounts. This promises free next day delivery. Amazon is offering this delivery service as a loss leader. The cost of delivery is often higher than what a customer is actually paying.

- Advertising/brand loyalty - Firms spend billions on advertising because repeated exposure to famous brands can make consumers more likely to buy ‘trusted’ brands.
- After-sales service - For some goods, like TVs and car, offering free after-sales service can be a factor in encouraging customer trust. It can also be a profitable aspect of the business. For example, Apple Care offers a three-year warranty, but it is priced at a good margin.
- Coupons and free gifts- Some sellers provide coupons and free gifts along with product.

Product Pricing

- **price is amount of money needed to acquire a product.**

By product pricing presents an opportunity to set the right price for the by products of the main core product so as to earn incremental revenue. It is very important to set the right price for the by product so that it can be sold. Like any other pricing

Methods of pricing

- **Mark-up Pricing/cost plus pricing**
- Markup pricing or cost-plus pricing is a pricing strategy **where the price of a product or service is calculated by adding together the cost of the products and a percentage of it as a markup.** The percentage or markup is decided by the company usually fixed at the required rate of return.

Price = Cost (AC) + m (Margin)

- **Target Return Pricing**

It is a pricing method in which **a formula is used to calculate the price to be set for a product to return a desired profit or rate of return on investment assuming that a particular quantity of the product is sold.**

- **Penetration Pricing**

Penetration pricing is a marketing strategy used by businesses to attract customers to a new product or service by offering a lower price during its initial offering. Eg: Netflix subscription rates at beginning.

The lower price helps a new product or service penetrate the market and attract customers away from competitors. Market penetration pricing relies on the strategy of using low prices initially to make a wide number of customers aware of a new product.

The goal of a price penetration strategy is to entice customers to try a new product and build market share with the hope of keeping the new customers once prices rise back to normal levels.

- **Predatory pricing**
- It is a method of pricing in which a seller sets a price so low that other suppliers cannot compete and are forced to exit the market. Predatory pricing involves charging very low prices, the aim being to get rid of competitors so that the supplier can charge considerably higher prices later. The predator is willing to sell at a loss – below cost – for a period, in the hope that its rivals either go bust or decide stop selling that product. When competing companies have left the market, the predator pushes prices back up

Eg of predatory pricing

- Amazon is a well-known example of a company that uses predatory pricing. The company has been accused of selling certain products below cost to drive its competitors out of the market. For example, Amazon sold e-books for $9.99, which was below the wholesale price

- **Going rate pricing**
- It is when **a business sets the price of its product or service based on the market price**.
- The Going-Rate Pricing is a method adopted by the firms wherein the product is priced as per the rates prevailing in the market especially on par with the competitors.
- Eg:Going-rate pricing is often used on commodity products such as wheat, gold, or silver.

- **Price skimming**

Price skimming is a **product pricing strategy by which a firm charges the highest initial price that customers will pay and then lowers it over time.** As the demand of the first customers is satisfied and competition enters the market, the firm lowers the price to attract another, more price-sensitive segment of the population. The skimming strategy gets its name from "skimming" successive layers of cream, or customer segments, as prices are lowered over time.

Eg price skimming

- Electronic products – take the Apple iPhone, for example – often utilize a price skimming strategy during the initial launch period. Then, after competitors launch rival products, i.e., the Samsung Galaxy, the price of the product drops so that the product retains a competitive advantage