Market Structure

1. ***Perfect Competition***
2. ***Monopoly***
3. ***Monopolistic Competition***
4. ***Oligopoly***

Perfect Competition

- ***Many sellers.***
- ***Standardized product.***

  Homogeneous good means that each seller's product is identical to that of other sellers.
- ***Sellers have small shares of the market.***

  Market share is a single seller's percentage of total sales over any period.
- ***Firms don't consider the reactions of competitors when deciding how much to produce or what price to charge.***
- ***Information is freely available***
- ***Free entry into and exit from the market.***

Perfect Competition

In a perfectly competitive market, an individual seller cannot influence the market price of its product.

*A **competitive firm** is one that sells its product in a perfectly competitive market.*

A competitive firm is "price taker," because it can only react to the market price and cannot cause the market price to go up or down.

Box 1. Market Price and the Demand for the Output of a Competitive Firm

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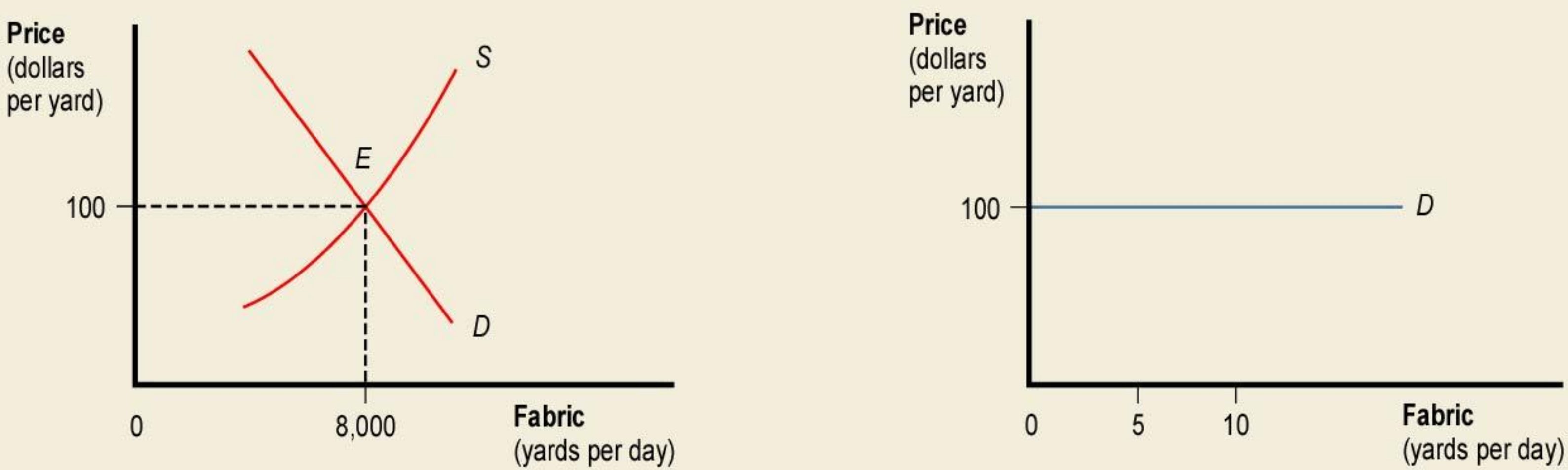
The market price of fabric is $100. A competitive firm can sell all the fabric it wishes at that price. The demand for a competitive firm's output is infinitely elastic at the market price. The output of any one firm is a perfect substitute for that of any other firm.



A. The competitive market

B. The demand for output of a competitive firm

Pure Monopoly

- *A single seller of a product that has no close substitutes.*

*A firm has **monopoly power** if it can influence the market price of its product by making more or less of the product available to buyers.*

Pure Monopoly

*A **barrier to entry** is a constraint that prevents additional sellers from entering a monopoly firm's market.*

- *Barriers to entry of additional sellers in the market must prevail for a profitable monopoly to be maintained:*
  - *Patents, secret processes, control of a key input, cost advantage of large-scale production, government franchises, special ability or technological advantages others can't duplicate.*

Barriers to entry

1) ***Government Franchises***

2) ***Licenses Patents and Copyrights***

They give creators of new products and works of literature, art, and music exclusive rights to sell or license the use of their inventions and creations.

3) Ownership of the Entire Supply of a Resource.

4) Cost Advantages of Large-Scale Operations and the Emergence of Monopolies.

Economies of scale are cost savings that result from large-scale production.

In economics, *average cost* and/or unit cost is equal to total cost divided by the number of goods produced (the output quantity, Q).

Natural monopoly I

A firm that emerges as a single seller in the market because of cost or technological advantages contributing to low average costs of production.

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The demand for a monopolist's product is the market demand.

- *To sell more, the more the firm must lower the price.*
- *The amount the seller chooses to offer for sale will influence the market price of the product.*

Price Discrimination I

THE PRACTICE OF SELLING A CERTAIN PRODUCT OF GIVEN QUALITY AND COST PER UNIT AT DIFFERENT PRICES TO DIFFERENT BUYERS

CONDITIONS:

1. *The seller must be able to control the price of its product.*

2. *The product that's sold at more than one price must not be resalable.*

3. *The seller must be able to determine how willingness and ability to pay vary among prospective buyers.*

Imperfect Competition

- *Prevails when more than one seller competes for sales with other sellers of similar products, each of which has some control over price.*
- *Under monopolistic competition, control of price comes from the differentiation of products among sellers.*
- *Under oligopoly, a few sellers with large market shares can influence price by controlling market supply.*

Monopolistic Competition

- *Many sellers.*
- *Each seller’s product is differentiated by brand name, quality, or other means.*
- *Free entry is possible in the market.*
- *Firms are grouped into industries according to the similarity of their products.*
- *Firms don’t consider the reactions of their rivals when pricing products or setting sales goals.*

Product group

- *represents several closely related, but not identical, items that serve the same general purpose for consumers.*

Oligopoly

- *A few sellers dominate the sales of a product.*
- *Entry of new sellers into the market is difficult or impossible.*
- *At least some firms have a large enough share of the market to influence the price.*
- *Firms consider their rivals' reactions when setting prices, sales targets, or advertising.*

Oligopolistic Price Wars and Market Contestability

- *A price war is the continual cutting of prices in a market by oligopolistic rivals until P = ACmin. Firms cut prices thinking their rivals won't follow. Once P = ACmin, firms fear rivals won't follow price increases.*
- *Market contestability also pushes prices down, to P = ACmin, as firms fear raising prices will attract new rivals.*

Collusion and Cartels

- *Fear of a price war provides incentive for oligopolistic rivals to collude to keep prices high and to prevent entry of new firms.*
- *A cartel is a group of firms acting together to coordinate output decisions and control prices as if they were a monopoly. To be successful, cartels must prevent new firms from entering their market.*

Other Oligopoly Models

- *In some markets, one firm acts as a price leader, setting prices to maximize profits, and other firms follow.*
- *In some markets, price rigidity results when firms fear their rivals won't match price increases, but will match price cuts--this results in a kinked demand curve.*