LESSON 12

OTHER FORMS OF MARKETS

In the last chapter we gained knowledge about different forms of market and studied in detail the meaning and special features of Perfect Competition. In this chapter we will study Monopoly, Monopolistic competition and Oligopoly. Monopoly is totally opposite of Perfect Competition. It provides insight into the operation of other imperfectly competitive market (i.e. Monopolistic competition and Oligopoly). In this chapter, the description of Monopoly and Imperfect Competition is given.

Monopoly -

Monopoly is a market situation where a producer produces such good, which has no close substitute. There is only one seller or producer.

Various economists have defined monopoly as follows-

Stonier and Hague- "The monopolist is the sole producer of a product which has no closely competing substitutes."

Prof. Lerner – "Monopolist is a producer who faces a sloping demand curve of commodity i.e his sale curve is inelastic."

Prof. Chamberlin- "Monopolist is one who generally has full control over the supply of a commodity and in most of the cases instead of conducting supply, he conducts price."

Features of Monopoly-

1) In a monopoly market, there must be only one seller, one producer or one supplier.
2) The good produced has no close substitute.
3) Their elasticity of demand is very less.
4) Monopoly firm is an industry in itself i.e there is no difference between an industry and firm.
5) The demand curve is downward sloping which signifies that a monopolist can sell more quantity at a higher price. As such the MR curve of a monopolist is situated below the AR(D) curve.
6) Monopolist can determine either price or supply. He cannot control both price and supply at one time. If he determines the price of his good then the level of production is determined be the demand of the consumer.
7) The aim of monopolist is to earn maximum profit.
8) There are strong barriers and hinderances on entry of new firms in the industry. These restrictions can by artificial, economic or financial . This can be explained by a simple example.

Sometimes product discrimination is so influential that a consumer recognises a commodity by its brand name. Financial restrictions mean inability of a firm to mange finance as large amount of capital is required .Structural restrictions like the government issues patent (licence) to many firms which is for a long period and a firm is the sole producer. Government provides degree or licence for instance a teacher cannot practice medicine without a medical degree. Economic reason proves to be a great hinderance in entry of firms. For example the average cost of a firm declines due to economies of scale. For this reason natural monopolies can be seen in field of public utility goods such as production of electricity, water and telephone etc. to be regulated by government.

Source of Monopoly-

There are many reasons for the emergence of monopoly situation. The chief among them is restriction on the entry of new firms. There are three main factors responsible for these restrictions.

- The control of producer over important raw material essential for production process.
- The patent right is given by government to a firm to produce and sell his good.
- Due to increasing economies of scale a firm produces at a low cost comparative to other firms.

The above description depicts Imperfect

Monopoly or Normal Monopoly. In a Pure Monopoly, firm produces such goods which have no substitute and the cross elasticity is zero. Beside this, the firm is so powerful that a consumer spends his entire income on the goods produced by that firm. As a result the average revenue curve (AR) is rectangular hyperbola. In reality, this is an impossible situation, hence we study Imperfect Monopoly. The examples of monopoly in India are – Indian Railways, State electricity corporation government's control over nuclear production etc.

Average Revenue and Marginal Revenue Curves in Monopoly.

Monopolist is the sole producer of such good which has no close substitiutes hence demand curve is a negatively sloping curve i.e if the sale of a good is increased its price has to be decreased. As a result, Marginal Revenue Curve falls twice the rate as the Demand Curve. Both curves originate from this common point on vertical line. This is depicted by following table and figure12.1

Revenue Curve in Monopoly- In table 12.1 Total Revenue (column 3) is obtained by multiplying price with quantity (column 1 and column 2) marginal revenue (column 4 is obtanied by dividing changes in total revenue with change in quantity.

Table 12.1

Revenue curves in Monopoly

Price (1)	Quantity (2)	Total Revenue(3)	Marginal Revenue(4)
9	0	0	-
8	1	8	8
7	2	14	6
6	3	18	4
5	4	20	2
4	5	20	0
3	6	18	-2
2	7	14	-4
1	8	8	-6

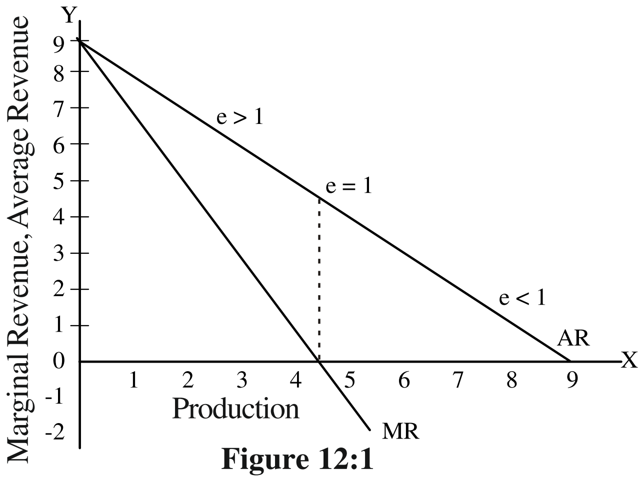

Figure 12:1

In the above Figure 12.1 both curves begin from a common point on the vertical axis MR Curve maintains an equal distance with the vertical line and AR curve. MR curve depicts the change between total revenue and change in quantity of production. When AR is elastic, MR is positive beacause increase in production causes TR to increase.When AR is unitary elastic i.e e =1, then MR is zero as increase in production leaves TR unchanged. Whereas when AR is inelastic i.e e<1, then MR is negative, an increase in production result in reduction in TR. That's why a producer does not produce in this stage. He tries to maximise his total revenue by selling less output at a higher price. On the other hand, cost of production is less on low production In this way he tries to maximise his profit.

The determination of price and output in a monopoly market is done through two methods 1.Total cost and total revenue method and 2. Marginal revenue and marginal cost method. In short run, a monopolist can get normal profit, abnormal profit or loss, but in long-run he earns only abnormal profit. A monopolist practices price discrimination to increase his profit.

Price discrimination- According to Prof. Stigler- "Price discrimination is sale of technically similiar products at different prices which are not proportional to their marginal cost."

Imperfect competition –

The book written by Mrs Joan Robinson- " The Economics of Imperfect Competion" and by Prof. E.H Chamberlin, "Theory of Monopolistic Competition" respectively are quite famous. The market situation found closer to reality is described in these books. The features of both Imperfect Competition and Monopoly are found in imperfet competition. Now we will study the structure of Monopolistic Competition,Oligopoly and Duopoly market.

Monopolistic Competition -

According to E.H. Chamberlin – "Monopolistic Competition is a challenge to the traditional view point of economics that in competition and monopoly are alternative and that individual prices are to be explained in term of either one or the other. By contrast, it is held that most ecomomic situations are composites of both competiton and monopoly". The above definition clearly shows that monopolistic competition is the market situation midway between the extremes of perfect competition and monopoly. It is nearer to the real world situation. The structure of this market can be understood more deeply by studying its follwing features.

Features:-

1. Large number of firms – Under monopolistic competition there are large number of firms but their size is very small so they are unable to influence production, they all work independently. The quantity and policy of sale does not affect each other. Their need for capital is also less because of their small size. The production technique is simple. The economies of scale are limited. This market structure can be seen in retail market service sector. At national level cotton textile industry, food processing, electric appliances are some of its examples. This market structure is also visible in local market like retailer, petrol station, newspaper, shop, restaurant, etc.

2.Product Differentiation

Unlike Perfect Competition rather such goods are produced which are perfect substitute nor like Monopoly, which have no substitutes. Under monopolistic market, such goods are produced which have close substitutes. Goods produced are alike but not identical.

i. The products differ from one another in colour, shape, brand, quality packing etc.

ii. Products are also differentiated through patents and trademarks . In india which have patents like Dell, Hindustan Unilever Limited, Reliance industry limited etc. Similarly, the various trade marks of tooth paste are Patanjali, Colgate, Palmolive, Close-up etc.

iii. Today's age is called the age of advertisement because of advertisements & publicity. They play an important role in creating differentiation in products. It is done to increase sales. Beside providing information to consumers, advertisement also influences them psychologically.

iv Difference in work-skill and credit facilities also creates product discrimination.

In this way, price differentiation is the important feature of monopolistic competition which makes demand relatively elastic (e>1). Besides this, every producer has monopoly over the production of his specific product though it is very limited

3. **Free entry and exit of the firm.** As the size of firms is small so the less capital and easy technique is needed. For this reason new firm can easily enter the group and exit on incurring losses.

4. Many firms together in the market is known as group. Instead of industry the term 'group' is used. The products in industry are homogeneous. In monopolistic competition products are close subsitute of each other. That's why term 'group' is used.

5. There is difference in selling-cost. This is also an important feature of this market structure.

6. Non-price competition is also an important feature of monopolistic competition. The price of production being constant the firms compete by offering gifts, free maintenance services etc. to attract buyers.

Average and Marginal Revenue curves

The increase or decrease of price in Monopolistic Competition has a great influence on demand with slight increase in price of a good. The consumer in its place buys the good having lesser price as close substitutes are available.

Thus demand is relatively elastic e > 1. The demand of a good on specific price depends on the price of substitutes, advertisements, interest, fashion and income

of the consumer. The slope of demand curve is less slanting or relatively elastic.

The elasticity of firm's average revenue curve depends on following elements-

A The amount of product differentiation between the firms.

B The preferences of consumers.

C The number of firms in the group.

The importance of concept of monopolistic competition is decreasing. Some of its criticism are as which products of firms should be kept under this market structure? There are limited number of firms having important brands which can be kept under Oligopoly. Sometimes very less product differentiation is found. Inspite of the criticism it is an important and real market structure which helps in the study of Oligopoly

Oligopoly-

Oligopoly is that form of market where there are few sellers. They sell both homogeneous and differentiated goods. If there are only two sellers of a good then, it is called Duopoly. It is the simplest form of Oligopoly.

Automobiles, cement, steel, and aluminium etc. are some of the in Indian examples of Oligopoly markets.

Many firms think it to be beneficial to organise themselves to do away with competition, the merger of the various firms take form of Oligopoly. Due to vast investment, only few firms are functional (operative) in production. The size of some firms becomes big due to economies of large scale of returns.

Features of Oligopoly

1. **Interdependence-** Mutual interdependence is found due to few number of sellers. Every firm

Table 12.1 Classification of Markets

Basis	Types	Features
Product Defferentiation	Pure Oligopoly Impure Oligopoly	Firms produces homogeneous goods Firms produces differentiated goods
Agreement	Collusive Non Collusive	Firms determine output and price There is no agreement between the firms.
Freedom of entry	Open Oligopoly Closed Oligopoly	In a market when firms can enter an industry. When firms cannot freely enter an industry.
Co-ordination	Business Oligopoly Organised Oligopoly	The sale of commodities is through centralised business. When firms get together to determine price and output.
Price Leadership	Partial Complete (Perfect)	In partial industries the price is determined by leader (big) firm which is called Price Leadership Firm. All the firms are mutually inter-dependent and influence each other's price and output.

is capable of influencing the production and price as they have a large share in the market. The price policy, sale process(style), production policy, advertisement, type of product etc. Influence all the firms in the industry. If a particular firm wants to increase its sale by decreasing the price, then what will be the reaction of other firms ? Will they too decrease the price? Will they increase advertisement expenditure? Will they change the quantity of product? These are some of the questions which are to be ensured before determining the price- policy by a firm.

2. **Competition-** In Oligopoly, sellers are influenced by each other as they are few in number. Every firm keeps an eye on the move of other competitive firms and are ready for retaliation (counter-action). The actual competition is reflected in this market form.

3. **Advertisement –** In words of Prof. Baumol- "Under Oligopoly , advertising can become a life and death matter." Due to mutual dependency among firms, they have to incurr a good deal of cost on advertisments and other measures of sales promotion to maintain their share in the market.

4. **Price Rigidity-** If a firm cuts down the price to increase sales, then other firms will also follow it. As a result price-war takes place, which is not profitable to any firm. On the contrary, if any firm increases price to earn more profit then sales will go down. As a result in both the situations prices stay constant.

5. **Rivalry between the firms-** There is continuous competition among firms to earn profit and maintain their dominance. There is always a situation of struggle and rivalry among the firms.

Demand curve in Oligopoly (Average Revenue)

The Demand Curve in Oligopoly is indeterminate due to excessive interdependency among the firm, Initially, Paul M. Sweezy put forward the hypothesis of kinked demand curve.

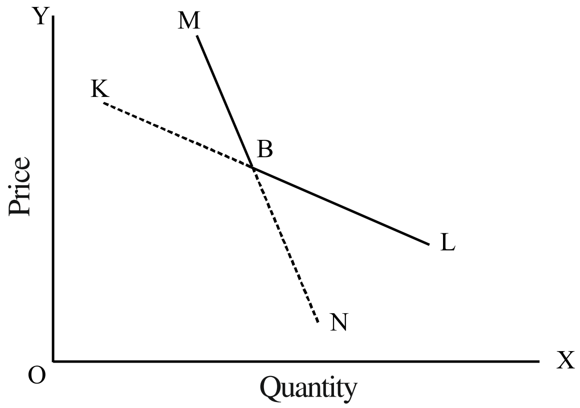

Figure 12.3

In the figure 12.3 there are two demand curves KL, which is more elastic and MN, which is less elastic. An oligopolist has to face more elastic demand curve at higher price and inelastic demand curve at lower price. The demand curve of a Oligopoly is kinked at a determined price.In the above figure, B is the kinked point.

Important points-

1. Monopoly means single producer or single seller.
2. A monopolist produces a good which has no close subsititutes.
3. There are external barriers on the entry of new firms in monopoly market.
4. Product differentiation is an important feature of monopolistic market.
5. In Oligopoly, there are few big firms which produce both homogeneous and differentiated products.
6. The demand curve in oligopoly is kinked.

Exericse Question

Objective Type Questions:-

1. In a Monopoly market there are/is-
   (A) Many sellers
   (B) Few sellers
   (C) One seller
   (D) Two sellers
2. Who propounded the "Theory of Monopolistic competition"-
   (A) Prof. E.F Chamberlin
   (B) Mrs. John Robinson

(C) Edwin Canon

(D) Alfred Marshal

3. Which is not the feature of Oligopoly?

(A) Interdependence

(B) Price rigidity

(C) Indefinite demand curve

(D) Single seller

4. Which type of goods are produced in Monopoly Market-

(A) goods which have close substitute

(B) goods which have perfect substitute

(C) goods which have no close substitute

(D) None of the above

5. The elasticity of monopolist demand curve is

(A) Less then 1 (e<1)

(B) More then 1 (e>1)

(C) Equal to 1 (e=1)

(D) Zero

Very Short Answer Type Questions :-

1. Write the meaning of monopoly.
2. What is the main objective of Monopolist?
3. What is the meaning of Price-discrimination?
4. Which market's feature is Product Differentiation?
5. Write one feature of Oligopoly market.

Short Answer Type Questions :-

1. Define Monopolistic Market.
2. Explain the statement. "actual competition is found in Oligopoly."
3. Write any two features of Oligopoly Market.
4. Write any two features of Monopolistic Competition.
5. Write the meaning of Imperfect Competition.

Essay Type Questions :-

1. Explain the statement, "Monopoly Market is the situation of extreme limit".
2. Write in detail the features of Monopolistic Market.
3. Write the meaning and features of Oligopoly Market.
4. What is Product Differentiation ? How it is done by various methods?
5. Compare Monopoly and Monopolistic Market.

Answer Table

1	2	3	4	5
C	A	D	C	A