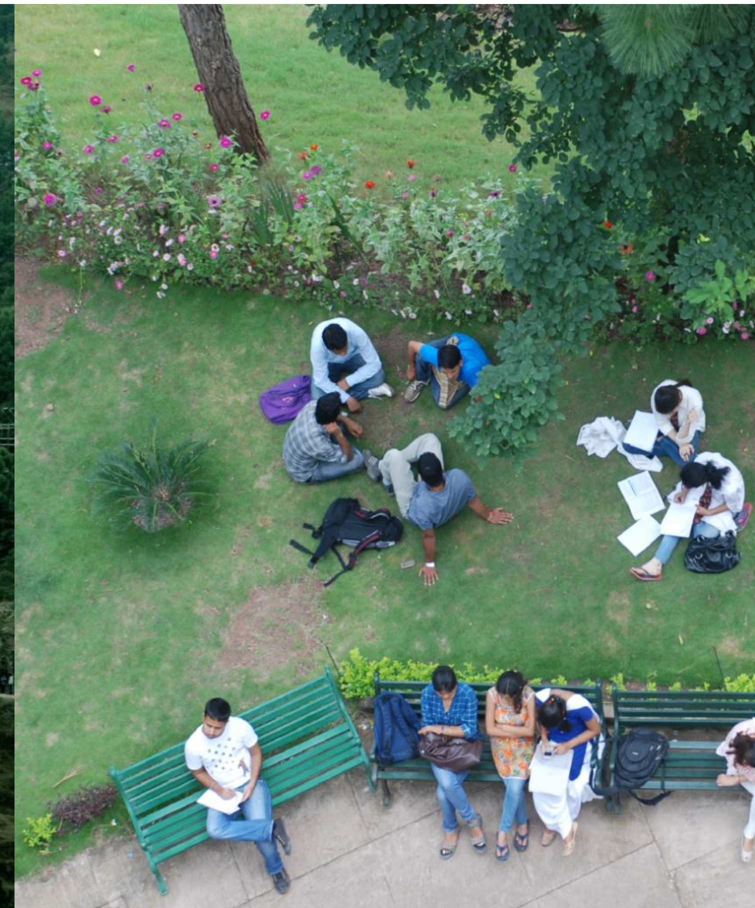
Shoolini University

PRINCIPLES OF ECONOMICS

Lecture 28: MARKET STRUCTURES

OCTOBER, 2015



TOPICS TO BE DISCUSSED

1. Market Structures

- Meaning
- Competitive Vs Imperfect Markets

MARKET STRUCTURE

- **Market Structure:** those characteristics of the market that significantly affect the behavior and interaction of buyers and sellers

- Competition in the market drives demand, supply and market price

- Greater the competition in a given market, more sensitive the market price is to changes in supply and demand

DETERMINANTS OF MARKET STRUCTURE

- Number and size of sellers and buyers
- Conditions of entry and exit
- Type of product – homogenous (identical) or differentiated
- Control over supply/output
- Control over price
- Barriers to entry
- Demand

COMPETITION AND MARKET PRICE

Example- In the diamond trade, DeBeers of South Africa controls the supply of diamonds, thus prices remain high and relatively stable with predictable annual price increases.

Gold market: there are many suppliers worldwide and the price fluctuates daily on commodity exchanges.

Stock Market

PERFECTLY COMPETITIVE MARKET

- Also known as pure competition
- Many sellers: there are enough so that a single seller's decision has no impact on market price.
- Homogenous or standardized products: each seller's product is identical to its competitors'.
- Firms are price takers: individual firms must accept the market price and can exert no influence on price.
- Free entry and exit: no significant barriers prevent firms from entering or leaving the industry.

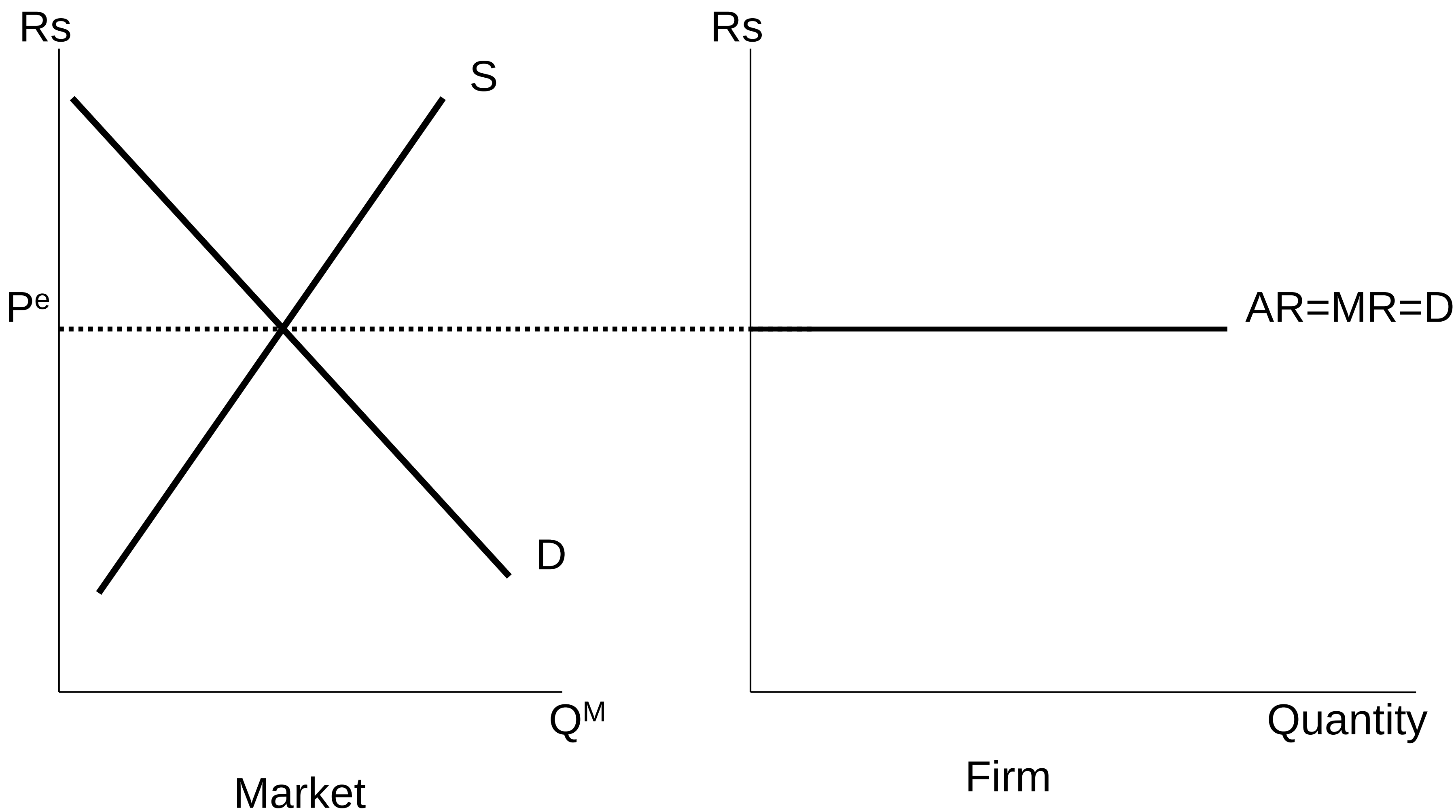
PERFECTLY COMPETITIVE MARKET

- Transportation cost does not affect the price
- Lack of selling cost
- Perfect mobility of inputs & goods & services
- Free from checks

DEMAND CURVE IN PURE COMPETITION

- Demand curve is perfectly elastic and parallel to x-axis
- AR=MR
- Marginal revenue (MR) is the increase in total revenue resulting from a one-unit increase in output.
- Since the price (AR) is constant in the perfect competition, increase in total revenue from producing 1 extra unit (MR) will equal to the price. Therefore, P= MR in perfect competition.

SETTING PRICE



PROFIT MAXIMIZATION

Necessary Conditions:

- MR = MC
- MC should cut MR from below
- Profit: Compare per unit price (AR) with per unit cost (AC)

PROFIT POSSIBILITIES IN SHORT RUN

- Supernormal Profit (AR>AC)
- Normal Profit (AR=AC)
- Losses (AR<AC)

THANK YOU ☺