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market types 1

Markets

Economics is looking at markets from a firm viewpoint – whereas marketing from a consumer viewpoint

Typical distinction between

- Perfect competition – markets/firms are perfectly competitive
- Imperfect competition – markets/firms are imperfectly competitive: monopolistic competition, oligopoly, monopoly

Given the unfeasibility of perfect competition (which renders the definbition of «imperfect competition» untenable) the following distinction is suggested:

- Passively competitive firms/markets
- Dynamically competitive firms/markets
- Non competitive firms/markets

Passive competitors

Features of Passive competitors

- Number of firms present in the market = a lot
- Number of consumers present in the market = a lot
- Business/operations share relative to the market = small – firms supply a small number of goods relative to the overall needs of the market
- Ability to impose a price on consumers = none, the firm is a price-taker
- Barriers to enter the market = some costs to set up a SME
- Product knowledge by consumers = imperfect, the choice being too wide

- Degree of product differentiation = none – products are similar
- Degree of product substitution = quasi perfect since the products are similar
- Degree of state intervention = none
- Examples = stock markets, agricultural industry, hospitality industry (not fast food) according to star classification
- Competitive elements = accidental location, accidental reputation, demographic growth

Cost-Revenue Analysis

a/Costs

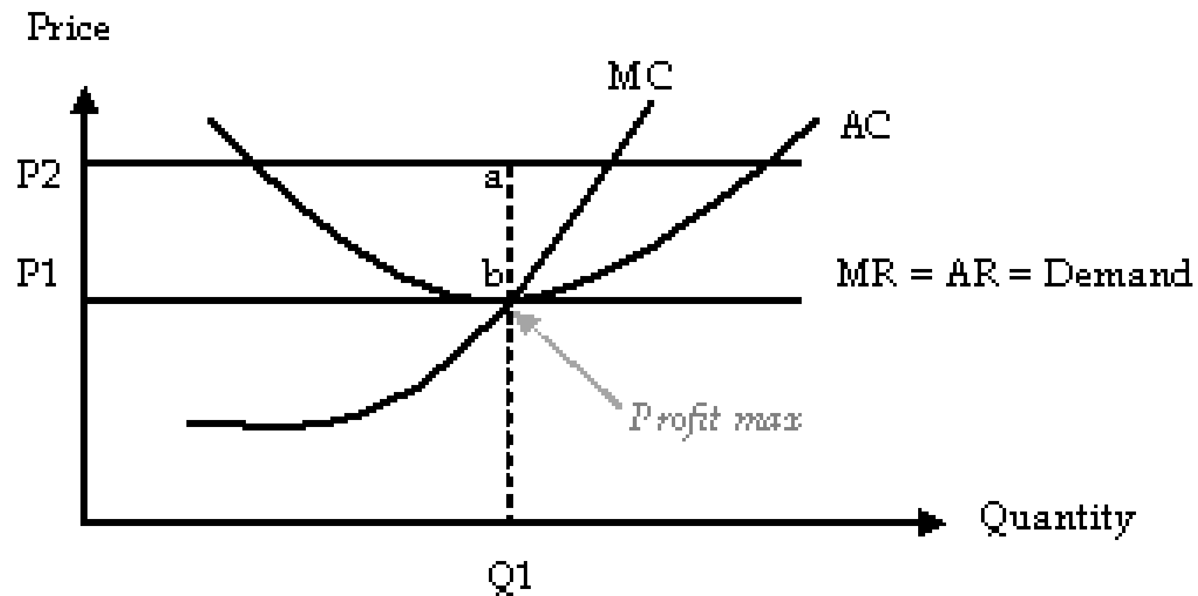
The price is set by producers at a equal to the minimum efficient scale i.e. minimum Average Costs: $P1 = AC\ min$.

At this level the producer earns revenue $R = P1 * Q1$, and makes a (normal) profit that is usually accounted under the costs i.e. as a margin.

b/Revenue

The fact that AR and MR curves are flat – perfectly elastic is because the firm can neither increase nor decrease its price without a cost. The firm is a price-taker.

Consequence passive competitors cannot use price strategies so as to generate (above-normal) profit shown by the area P2-P1-B-A. Even if they could use price strategies, this is risky for two reasons:


Price
MC
AC
P2
a
P1
b
MR = AR = Demand
Profit max
Quantity
Q1

- First, consumers are price-sensitive, and this is because they can easily switch from one producer to another, since in this type of market there are numerous competitors.

- Second, above normal profits would be reduced in the longer run since they would attract more firms into the market pushing the price down from P2 to P1.

Thus, since producers cannot change the price they are left with determining the quantity of production at a level that maximizes profit, which is where $MC = MR = P1$.

Since price strategies do not work there, however, other competitive elements?

- Products: such businesses produce similar products so the rate of substitution is high
- Advertising: too costly

There are more of the result of serendipity rather than volition