CHAPTER 8

MARKET STRUCTURE

- This chapter covers the types of market such as perfect competition, monopoly, oligopoly and monopolistic competition, in which business firms operate.

Market Structure

- Basically, when we hear the word **market**, we think of a place where goods are being bought and sold.

- In economics, market is a place where buyers and sellers are exchanging goods and services with the following considerations such as:
  - Types of goods and services being traded
  - The number and size of buyers and sellers in the market
  - The degree to which information can flow freely

Two Types of Market Structure

- Perfect or Pure Market
- Imperfect Market

Perfect Market

Perfect Market is a market situation which consists of a very large number of buyers and sellers offering a homogeneous product. Under such condition, no firm can affect the market price. Price is determined through the market demand and supply of the particular product, since no single buyer or seller has any control over the price.

Perfect Competition is built on two critical assumptions:

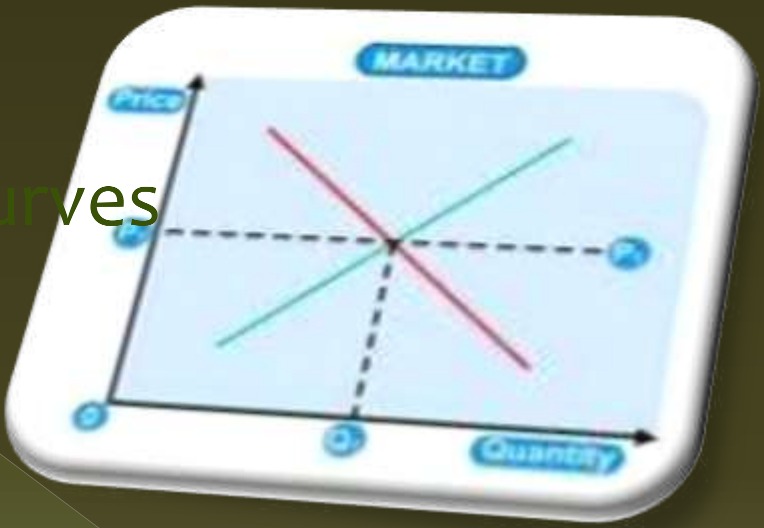
- The behavior of an individual firm
- The nature of the industry in which it operates

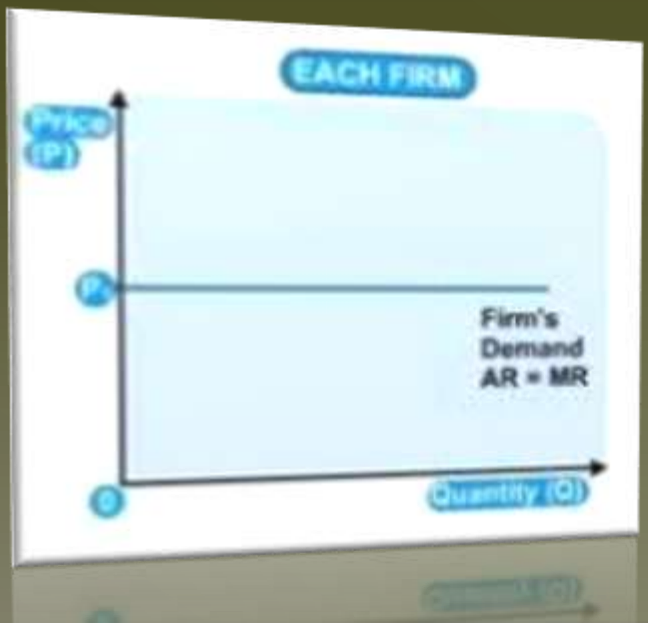
- The firm is assumed to be a price taker
- The industry is characterized by freedom of entry and exit

Demand curves for industry and firm in perfect competition

Industry

- Normal demand and supply curves
- More supply at higher price





Firm

- Price takers
- Have to accept the industry price

Perfect Competition cannot be found in the real world. For such to exist, the following conditions must be observed and required:

- A large number of sellers
- Selling a homogenous product
- No artificial restrictions placed upon price or quantity
- Easy entry and exit
- All buyers and sellers have perfect knowledge of market conditions and of any changes that occur in the market
- Firms are "price takers"

Characteristics of Perfect Competition

- There are very many small firms
- All producers of a good sell the same product
- There are no barriers to enter the market
- All consumers and producers have ‘perfect information’
- Firms sell all they produce, but they cannot set a price.

Short-run Analysis of Perfect Competition

- The firm's objective is to produce the level of output that will maximize profit
- Some inputs are variable and therefore fixed costs arise regardless whether the firm is operating or not
- Since the firm is a price taker, it has no control on the price of a product

Short-run equilibrium under a Perfect Competition Market

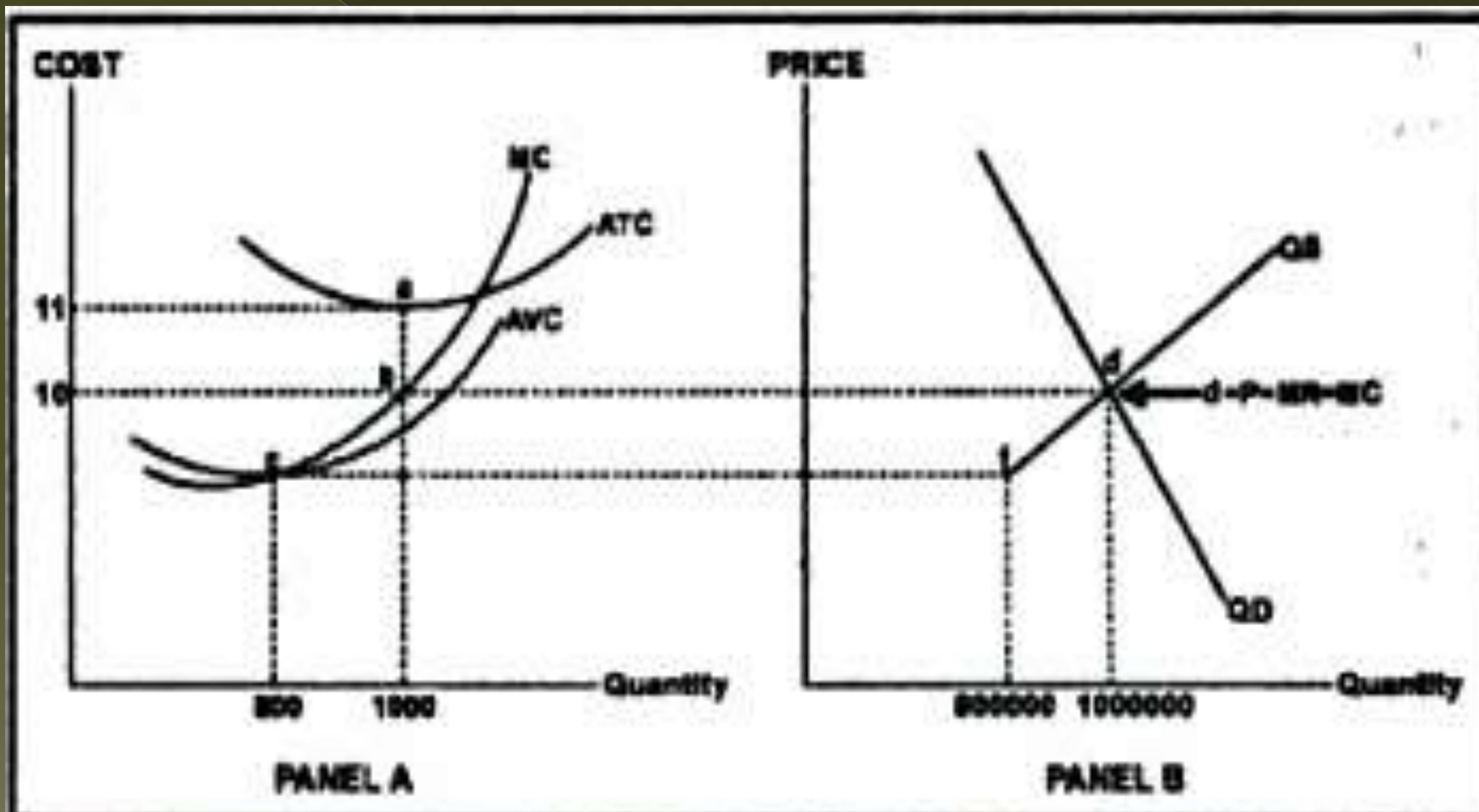


Figure 82. Short-run Equilibrium under Perfect Competition