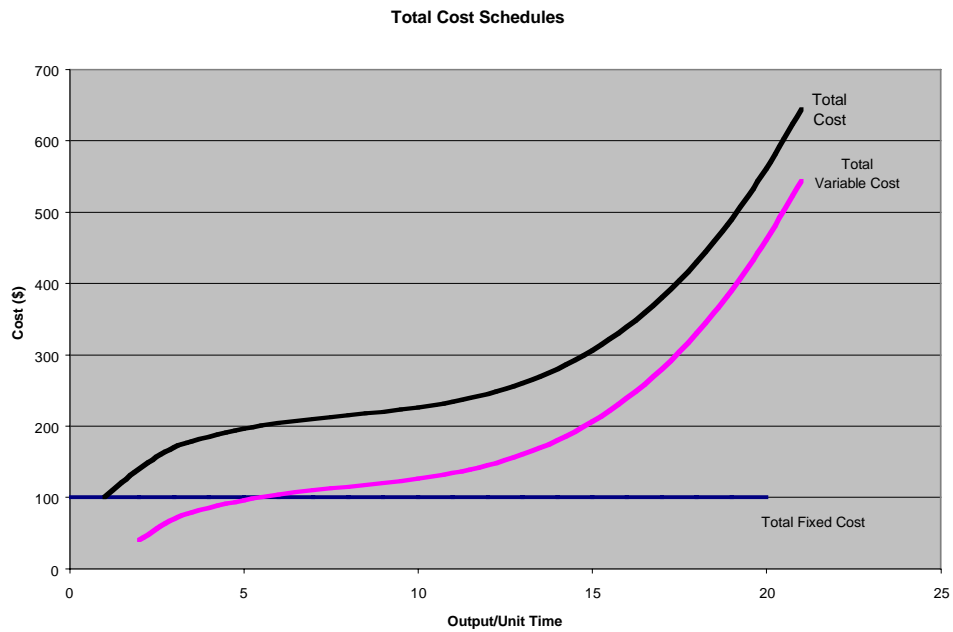
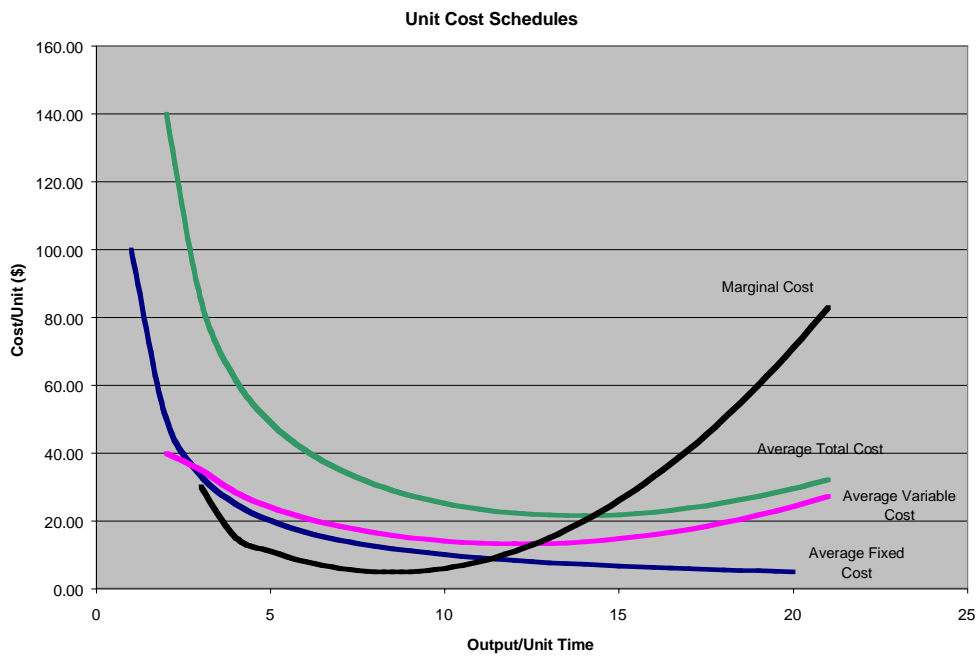


**Figure 5: Total cost schedules**



**Figure 6: Average and marginal cost schedules**



### c) Marginal Revenue

Marginal revenue (MR) refers to change in total revenue resulting from the sale of one more or one less unit of output. In a perfectly competitive market, the MR curve is also a horizontal straight line equal to the market price per unit.

$$MR = \frac{\text{Change in TR}}{\text{Change in } Q}$$

## 5.7 RULES FOR PROFIT-MAXIMISATION

Two important rules define the output that maximises each firm's profits.

- The first rule states that in the short-run, a firm should produce if and only if TR is not less than TC. This rule is also called the **shutdown rule**; and
- The second rule states that for the firm to be producing its profit-maximising output, MR should be equal to MC (MR = MC). This point is where the revenue from selling one additional unit is equal to the cost of producing that unit. Below this production level, the revenue per additional unit is greater than the cost but at a decreasing rate. After the point of equality, the cost of producing an additional unit will be greater than the revenue received for that unit at an increasing rate.

## 6.0 MARKET STRUCTURES

### 6.1 DEFINITION OF MARKET STRUCTURE

Structure refers to the characteristics of markets that influence the behaviour and performance of firms. These characteristics include the nature and number of consumers of the firm's products, the number of sellers, the type of product, the ease by which firms can enter and leave the industry, and a single firm's ability to influence demand by advertising.

#### *Market*

The market consists of firms and consumers buying and selling a well-defined product. Examples are markets for shoes, computers, wildlife safaris, maize, hunting, etc.

### *Industry*

A group of firms that sells a well-defined product or closely related set of products is said to constitute an industry. As in the above example, we have the shoe, computer, safari, maize and game hunting industries.

### **Competitiveness of a market structure**

This refers to the extent to which individual firms have power in a market to influence the price or other terms on which their product is sold. The less power an individual firm has to influence the market in which it sells its product, the more competitive is that market structure said to be.

## **6.2 TYPES OF MARKET STRUCTURES**

There are various types of market structures and the most important are:

- a) Perfect competition;
- b) Monopoly;
- c) Monopolistic competition;
- d) Oligopoly;
- e) Monopsony; and
- f) Oligopsony.

### **a) Perfect Competition**

Perfect competition is a market structure in which individual firms have **no power** to influence the price or other terms on which their product is sold. Individual firms are simply sell their products at the prevailing market price. One example from most large cities in the region is the commuter omni-buses that ferry people from the suburbs into the central business district. Internationally, the traders in foreign currency markets are another example.

*Assumptions:*

- The market contains a large number of buyers and sellers, each of which cannot individually influence demand or supply, and hence price,
- Firms produce goods that are identical or close substitutes, so that consumers do not care which firm's product they buy,
- All buyers and sellers are well-informed about alternatives and prices,
- All factors of production are free to move from one firm to another throughout the industry,
- There are no entry and exit barriers to firms.

**b) Monopoly**

In a monopoly, there is only one **sole supplier** of a commodity for which there are no close substitutes. It may be a single firm or a group of firms operating together. In this market structure, the firm or cartel has **total power** over that market to influence the price or other terms on which their product is sold. Monopoly firms are able to set the market price. Most countries in the region have state monopolies for the postal service, electricity, and phone service although these are gradually being broken up or privatised.

How does a monopoly arise and what are the barriers to entry?

- A monopoly firm possesses special proprietary knowledge, or skills, or a **copyright** or a **patent** on a particular product. The Polaroid camera, special drugs, and certain computer software are all examples of products where patent protection has created a monopoly.
- The firm is a large supplier with significant cost advantages that other firms cannot compete against. This is known as a **natural monopoly**.
- The product/service supplied is viewed to be strategic to the national interest or is a natural resource whose control can only be vested in one central authority. Post offices and other public utilities (water, energy, etc.) are prime examples in the region.

**c) Monopolistic Competition**

Monopolistic competition is a market structure in which individual firms have **some power** to influence the price or other terms on which their product is sold. Common examples include household consumer goods such as bar laundry soap, photocopy shops, and small businesses that offer typing services.

*Assumptions:*

- Market structure has large number of small firms;
- Each firm produces a slightly different or distinctive product;
- Product differentiation gives slight degree of market power; and
- Barriers to entry and exit are low.

Monopolistic competition results from:

- Cost of transport;
- Brand name attraction;
- Advertising and promotion;
- Extra services, credit or quality of service; and
- Consumers lack knowledge about the market.

**d) Oligopoly**

Oligopoly is a market structure such as petrol distribution or cellular phone services with following characteristics:

- Market structure is dominated by a few very large firms;
- Goods are close substitutes or only slightly different; and
- Barriers to entry are typically large.

**e) Monopsony**

Monopsony is a market structure in which there is only one **sole buyer** of a commodity. It may be a single firm or a "cartel". A good example is the state marketing board in many countries that are the sole buyer of agriculture produce. As a result it can influence the selling price of the commodity.

To help combat the monopsonistic buyer, either:

- A minimum market price must be established for cotton;
- Cotton farmers must be helped to market their cotton outside the area;
- Cotton farmers can organise a co-op to increase their market power; and
- Other cotton mills can be developed in the region.

### f) Oligopsony

This market structure has only a few large buyers, eg. two or three large cotton mills in the country. Table 6 summarises the various points related to the some of the above market structures.

**Table 6: Market structure and market power.**

KIND OF COMPETITION	NUMBER OF PRODUCERS AND DEGREE OF PRODUCT DIFFERENTIATION	PART OF ECONOMY WHERE PREVALENT	DEGREE OF CONTROL OVER PRICES
1. Perfect Competition	Many producers with identical products	Communal farmers, money markets	No control
2. Imperfect Competition			
a) Monopolistic Competition	Many producers with real and imagined product differences	Petrol stations, soaps, safari operations,	Little control
b-1 Oligopoly	Few producers, little or no product differences	Beer and soft drinks, lumber, fertiliser	Some Control
b-2 Oligopoly	Few producers, some product differences	Processed foods	Some control
c) Complete Monopoly	Single producer, unique product without close substitutes	State phone, postal and electricity services	Considerable control

Source: Adapted from Samuelson (1976).

## 6.3 NON-PRICE COMPETITION

This refers to a strategy to create marketable differences between products. Possible strategies include:

**a) Advertising**

- Set up your product as being different or better than the competition's product;
- Try to gain market share;
- Costs soon become built-in to the product price; and
- The consumer pays.

**b) Other Strategies**

- Quality, design, and more recently, the service;
- Often linked with an advertising program; and
- Segment the consumer market and attract more customers .

**Debate: Criticism against advertising and marketing**

The pressure to constantly innovate and improve is becoming critical factors in today's increasingly competitive global market. Is the need for sometimes frivolous changes worth the higher price at the counter? Look at any major supermarket in North America and compare 30 kinds of toothpaste, 40 different shampoos, dozens of soaps, several brands of plastic garbage bags and hundreds of other products. Can all these products be "new and improved", "environmentally friendly", "faster acting", "with super strength" etc.? Many of these competing products are actually made by the same companies! This marketing is assisted by huge advertising programmes in the media which costs millions of dollars. This cost is passed on to the consumer in the form of higher prices. When does the idea of consumer choice reach the saturation point?

**Debate: Points in favour of advertising and marketing:**

**Product differentiation and quality improvements do reflect a response to consumer desires and wants. Advertising is the price you pay to remain informed about consumer choices. The consumer is better off when product quality is improved through constant innovation and research. If the consumer is willing to pay the cost of product development, advertising, and better service, then these non-price competition strategies are a rational industry response.**