5 Forms of Market

Introduction :

Market is generally understood as a particular place or locality where goods are sold and purchased. But, in economics, market refers to an arrangement through which buyers and sellers come in contact with each other directly or indirectly and exchange of goods and services takes place among them.

Definition of Market :

According to Augustin Cournot, "Economists understand the term market, not any particular market place in which things are bought and sold, but the whole of any region in which buyers and sellers are in such a close contact with one another that the prices of the same goods tend to equality easily and quickly."

Thus, market is a network of dealings between potential buyers and potential sellers. At any point of time, a market will exist if there are :

1) Buyers and sellers
2) A product or service to be bought and sold
3) Price of the product
4) Close contact between buyers and sellers
5) Knowledge about market

Classification of Market :

Market can be classified on the basis of various criteria. This is shown in following fig. 5.1.

I) On the basis of place :

1) **Local market :** Local market is a market in which sellers sell and customers buy a product in the region or area in which it is produced.

2) **National market :** National market is a domestic market in a given country. Each national market is governed by the regulation of its own country.

3) **International market :** International market is a worldwide market in which buyers and sellers trade in goods and services across the national borders.

II) On the basis of time :

1) **Very short period :** Very short period is a period in which supply is fixed and price is determined by the demand. The time period is for a few days or weeks in which the supply of commodity cannot be increased.

2) **Short period :** Short period is a period of less than one year. In this period, firms can only make adjustments in inputs like labour to increase the supply of goods and services.

3) **Long period :** Long run is a period of time in which all factors of production and costs

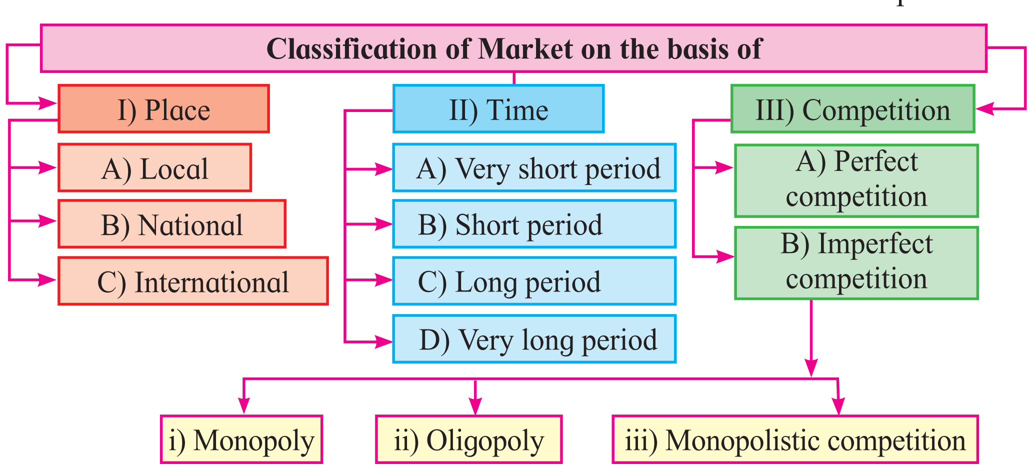


Fig. 5.1

are variable. In the long run, firms are able to adjust all costs. It is for a few years, generally up to five years.

4) **Very long period :** Very long period is a production time that is so long that all inputs are variable. It is of more than five years.

III) On the basis of Competition :

Competition among the sellers and buyers is the most important criteria for classification of markets in economics. Let us study the various types of markets on the basis of competition among the sellers :

A) Perfect Competition :

Meaning and Definition : Perfect competition is an ideal and imaginary concept of market rather than an actual market. According to Mrs. Joan Robinson, "Perfect competition prevails when the demand for the output of each producer is perfectly elastic."

A perfectly competitive market is one in which the number of buyers and sellers is very large. All the buyers and sellers are engaged in buying and selling a homogeneous product without any restrictions. Moreover both buyers and sellers possess perfect knowledge of market conditions.

Following are the features of Perfect Competition :

1) **Large number of sellers and buyers :** Under perfect competitions, there are large number of sellers and buyers. As mentioned earlier, each seller forms a negligible part in the total market. Hence, none of them is in a position to influence the price and supply in the market. Thus, sellers are price takers under perfect competition.

The number of buyers is also large. The share of each buyer is so negligible that none of them is in a position to influence the price in the market.

2) **Homogeneous product :** An important feature of a perfectly competitive market is that the product sold is homogeneous or identical in respect of size, design, colour, taste etc. All the products are perfect substitutes to each other.

3) **Free entry and exit :** There are no barriers to the entry and exit of firms. Any firm can enter or quit the industry at its own will. If there is hope of profit, the firm will enter the market and if there is possibility of loss the firm will leave the market.

4) **Single price :** A single uniform price prevails under perfect competition which is determined by the interaction of demand and supply.

5) **Perfect knowledge of market :** The buyers and sellers possess a perfect knowledge about the market conditions. Every seller and buyer has the knowledge about price, quality, source of supply of products etc.

6) **Perfect mobility of factors of production :** There is perfect mobility of factors of production under perfect competition. Labour and capital are mobile not only geographically but also occupationally.

7) **Absence of transport cost :** In perfect competition, price is uniform because we assume that transport cost does not exist. This assumption will lead to uniformity in price.

8) **No government intervention :** Laissez-faire policy is an important feature of perfect competition. It means there is absence of Government intervention in economic activities.

Price determination under Perfect Competition:

The interaction of demand and supply

determine price of the commodity in perfect competition. This is known as 'equilibrium price.' Marshall has compared the process of price determination to the cutting of cloth with a pair of scissors. Just as both the blades of scissors are required to cut the cloth, both the forces of demand and supply are essential to determine the equilibrium price in the market. This is explained with the help of the following schedule and diagram.

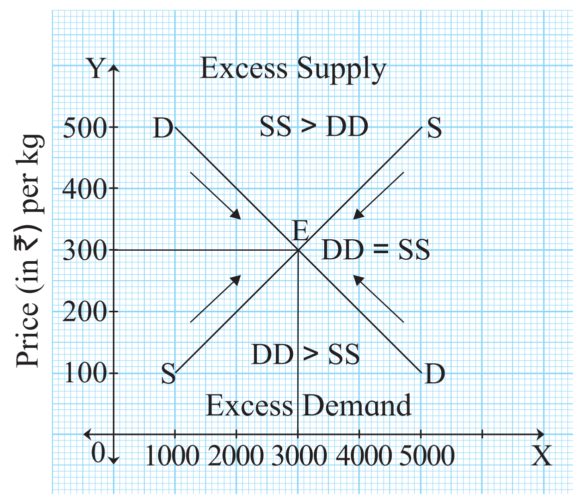
Table no 5.1 Demand and Supply Schedule

Price per Kg. of Apples (in ₹)	Quantity demanded (in Kg.)	Quantity supplied (in Kg.)	Relationship between DD and SS
100	5000	1000	DD > SS
200	4000	2000	DD > SS
300	**3000**	**3000**	**DD = SS**
400	2000	4000	DD < SS
500	1000	5000	DD < SS

From the table no 5.1, following conclusions can be drawn :

1) When price rises from ₹ 100 to ₹ 200 quantity demanded falls from 5000 kgs. to 4000 kgs. whereas supply increases from 1000 kgs. to 2000 kgs. This is because demand falls with rise in price and supply rises with a rise in price. This is the stage where demand is greater than supply (DD > SS).
2) When price rises to ₹ 300, quantity demanded and quantity supplied become equal that is 3000 kg. This is the stage of equilibrium where demand and supply become equal (DD = SS). Hence, ₹ 300 becomes the equilibrium price.
3) When price further rises from ₹ 400 to ₹ 500, demand falls from 2000 kgs. to 1000 kgs. and supply rises from 4000 kgs. to 5000 kgs. Thus, supply is greater than demand. (SS > DD).

The process of price determination is explained in the following figure 5.2. In this diagram, X axis represents quantity demanded and quantity supplied, whereas Y axis represents the price. DD is the downward sloping demand curve which shows inverse relationship between price and quantity demanded. SS is the upward sloping supply curve which shows direct relationship between price and quantity supplied. E is the equilibrium point where DD and SS curve intersect each other. Accordingly ₹ 300 is the equilibrium price and 3000 kgs. is the equilibrium quantity demanded and supplied. This equilibrium price is determined by market demand and market supply.



Quantity Demanded and Quantity Supplied (in kgs.)

Fig. 5.2

B) Imperfect Competition :

Imperfect competition is a type of market showing some but not all the features of a competitive market. Following are some of the types of imperfect market.

I) Monopoly :

Meaning and Definition : The term monopoly is derived from the Greek word 'Mono' which means single and 'poly' which means seller. Monopoly is a market in which there is only one seller who controls the entire market supply for a product which has no close substitute.

According to E. H. Chamberlin, "Monopoly refers to a single firm which has control over the supply of a product which has no close substitute."

Following are the main features of monopoly market :

1) **Single seller :** In monopoly, there is no competition as there is only one single producer or seller of the product. But, the number of buyers is large.

2) **No close substitute :** There are no close substitutes for the product of the monopolist. Therefore, the buyers have no choice. They have to either buy the product from the monopolist or go without it. The cross elasticity of demand for his product is either zero or negative.

3) **Barriers to entry :** Entry of the rivals is restricted due to legal, natural, technological barriers which do not allow the competitors to enter the market.

4) **Complete control over the market supply:** The monopolist has complete hold over the market. He is the sole producer or seller of the product.

5) **Price maker :** A monopolist can fix the price of his own product as he controls the whole market supply. Monopolist is a price maker.

6) **Price discrimination :** Monopolist being a price maker, he can charge different prices to different consumers for the same product, on the basis of time, place etc. Thus, price discrimination is an important feature of monopoly market. For example, students and senior citizens are provided railway tickets at concessional rates.

7) **No distinction between firm and industry:** A monopolist is the sole seller and producer of the product. A monopoly firm itself is an industry.

Types of monopoly :

Following are some of the types of monopoly :

1) **Private monopoly :** When an individual or private body controls a monopoly firm it is known as private monopoly. For example, Tata Group.

2) **Public monopoly :** When the production is solely owned, controlled and operated by the Government, it is known as public monopoly. It is usually welfare oriented. For example, Indian Railways.

3) **Legal monopoly :** This monopoly emerges on account of legal provisions like patents, trade mark, copyrights etc. The law forbids the potential competitors to imitate the design or form of the product registered under given branded names. For example, Amul products.

4) **Natural monopoly :** The monopoly created on the basis of natural conditions like climate, rainfall, specific location etc. is known as natural monopoly. For example, wheat from Punjab.

5) **Simple monopoly :** In simple monopoly, seller or a firm charges a uniform price for its product to all the buyers.

6) **Discriminating monopoly :** In discriminating monopoly, firm charges different prices to different buyers for the same product. For example, doctor charges different fees to different patients.

7) **Voluntary monopoly :** To avoid cut throat competition, some monopolists voluntarily come together and form a group of monopolists. This facilitates them to maximise the profit. For example, Organisation of Petroleum Exporting Countries (OPEC).

You should know :

Price descrimination under monopoly

Personal	Place wise	Time wise	Use
Doctors charge different fees to different patients	Differences in house rent in rural and urban areas	ST bus fare differs for over night and day time travels	Electricity charges are different for domestic and commercial uses

Find out :

Types of monopoly for the following products/services :

1) Tea in Assam ☐
2) Atomic energy ☐
3) Logo of a commercial bank ☐

Do you know?

Monopsony is the converse of monopoly. It exists when there are many sellers but only one buyer. Buyer's monopoly is rarely found. A monopsonist can exploit the sellers just as a monopolist may exploit the buyers. In the labour market, a particular kind of labour is used by one employer only.

II) Oligopoly :

The term oligopoly is derived from the Greek words 'Oligo' which means few and 'poly' which means sellers. It is that market where there are a few firms (sellers) in the market producing either a homogeneous product or a differentiated product. For example, mobile service providers, cement companies etc.

Features of oligopoly :

1) **Few firms or sellers :** Under oligopoly market, there are few firms or sellers. These few firms dominate the market and enjoy a considerable control over the price of a product.

2) **Interdependence :** The seller has to be cautious with respect to any action taken by the competing firms. Since there are few sellers in the market, if any firm makes the change in the price, all other firms in the industry also try to follow the same to remain in the competition.

3) **Advertising :** Advertising is a powerful instrument in the hands of oligopolist. A firm under oligopoly can start an aggressive and attractive advertising campaign with the intention of capturing a large part of market.

4) **Entry barriers :** The firm can easily exit from the industry whenever it wants. But has to face certain entry barriers such as Government licence, patents etc.

5) **Lack of uniformity :** There is a lack of uniformity among the firms in terms of their size. Some firms may be small while others may be of bigger size.

6) **Uncertainty :** There is a considerable element of uncertainty in this type of market due to different behaviour patterns. Rivals may join hands and co-operate or may try to fight each other.

III) Monopolistic competition :

Different brands of liquid cleaners :

Fig. 5.3

Meaning and Definition : Monopolistic competition is very realistic in nature. In this market there are some features of perfect competition and some features of monopoly acting together. Prof. E. H. Chamberlin coined this concept in his book "Theory of Monopolistic Competition" which was published in 1933.

According to Chamberlin, "Monopolistic competition refers to competition among a large number of sellers producing close but not perfect substitutes."

Following are the main features of monopolistic competition :

1) **Fairly large number of sellers :** In monopolistic competition, the number of sellers is large but comparatively it is less than that of perfect competition. Due to this reason sellers' behaviour is like monopoly.

2) **Fairly large number of buyers :** In this market there are fairly large number of buyers. Consequently, no single buyer can influence the price of the product by changing his individual demand.

3) **Product differentiation :** Product differentiation is the main feature of monopolistic competition. In this market, there are many firms producing a particular product, but the product of each firm is in some way differentiated from the product of every other firm in the market. This is known as product differentiation. Product differentiation may take the form of brand names, trade marks, peculiarity of package or container, shape, quality, cover, design, colour etc. This means that the product of a firm may find close substitutes and its cross elasticity of demand is very high. For example, mobile handsets, cold drinks etc.

4) **Free entry and exit :** Under monopolistic competition there is freedom of entry and exit, that is new firms are free to enter the market if there is profit. Similarly, they can leave the market, if they find it difficult to survive.

5) **Selling Cost :** Selling cost are peculiar to monopolistic competition only. It refers to the cost incurred by the firm to create more demand for its product and thus increase the volume of sales. It includes expenditure on advertisements, readio and television broadcasts, hoardings, exhibitions, window display, free gifts, free samples etc.

6) **Close substitutes :** In monopolistic competition, goods have close substitutes to each other. For example, different brands of soaps, toothpastes etc.

7) **Concept of group :** Under monopolistic competition, Chamberlin introduced the concept of 'Group' in place of industry. Industry means the number of firms producing identical products. A 'Group' means a number of firms producing differentiated products which are closely related. For example, group of firms producing medicines, automobiles etc.

Find out :

Close substitutes for the following products.

Products	Substitutes
1) Gemini Oil	
2) Colgate Toothpaste	
3) Red Label Tea	
4) Bru Caffee	
5) Activa Two-wheeler	

EXERCISE

Q. 1. A) Choose the correct option :

1) In economic sense, market includes following activities
   a) The place where goods are sold and purchased.
   b) An arrangement through which buyers and sellers come in close contact with each other directly or indirectly.
   c) A shop where goods are sold.
   d) All of the above.

Options : 1) a and b 2) b and c 3) a, b and c 4) only b

2) Classification of markets on the basis of place
   a) Local market, National market, International market
   b) Very short period market, Local market, National market.
   c) Short period market, National market, International market.
   d) Local market, National market, Short period market.

Options : 1) a, b and c   2) b, c and d
3) only a   4) a and d

3) Homogeneous product is a feature of this market.
a) Monopoly
b) Monopolistic competition
c) Perfect competition
d) Oligopoly

Options : 1) c and d   2) a, b and c
3) a, c and d   4) only c

4) Under Perfect competition, sellers are
a) Price makers   b) Price takers
c) Price discriminators   d) None of these

Options : 1) a, b and c   2) only b
3) only c   4) a and c

Q. 2. Give economic terms :

1) The market where there are few sellers.
2) The point where demand and supply curve intersect.
3) The cost incurred by the firm to promote sales.
4) Number of firms producing identical product.
5) Charging different prices to different consumers for the same product or services.

Q. 3. Complete the Correlation :

1) Perfect competition : Free entry and exit :: ☐ : Barriers to entry.
2) Price taker : ☐ :: Price maker :: Monopoly.
3) Single price : Perfect competition :: Discriminated prices : ☐

Q. 4. Find the odd word out :

1) Selling cost : Free gifts, Advertisement hoardings, Window displays, Patents.
2) Market sructure on the basis of competition : Monopoly, Oligopoly, Very Short Period market, Perfect competition.
3) Features of monopoly : Price maker, Entry barriers, Many sellers, Lack of substitutes.
4) Legal monopoly : Patent, OPEC, Copyright, Trade mark.

Q. 5. Answer the following :

1) Explain the features of Oligopoly.
2) Explain the types of Monopoly.

Q. 6. Observe the table and answer the questions :

Price of banana (per dozon) in ₹	Demand (in dozen)	Supply (in dozen)	Relation between DD and SS
10	500	100	DD > SS
20	400	☐	DD > SS
30	☐	300	DD = SS
40	200	☐	DD < SS
50	☐	500	DD < SS

1) Fill in the blanks in the above schedule.
2) Derive the equilibrium price from the above schedule with the help of a sutiable diagram.

Q. 7. Answer in detail :

1) Explain the meaning of Monopolistic competition with its features.
2) Explain the meaning of Perfect competition with its features.