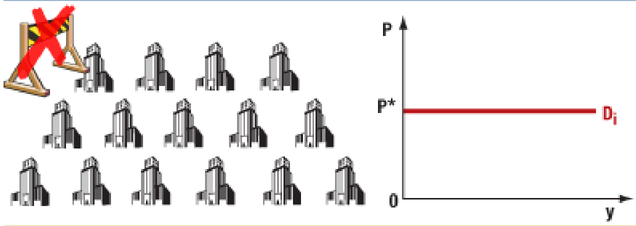
Understanding Market Structures

- **Perfect competition, monopoly**, **monopolistic competition**, **oligopoly** and are four common types of market structures. Market structure determines whether a firm has market power and whether it can make a profit in the long run.
- **Market structure** is determined by the **number of firms**, the **type of product** sold and the existence of **barriers to entry**.

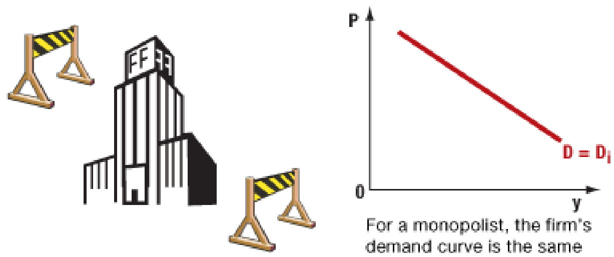
Perfect competition



- Large number of small firms
- Produce identical products
  * so, firms have no market power and take equilibrium price from the market as given.
- No barriers to entry
  * so, firms will continue to enter market if there are profit opportunities until economic profit is driven to zero.

A market characterized by **perfect competition** is one that has many firms producing identical goods and no barriers to entry. Firms are price takers and economic profit is zero in the long run.

Monopoly

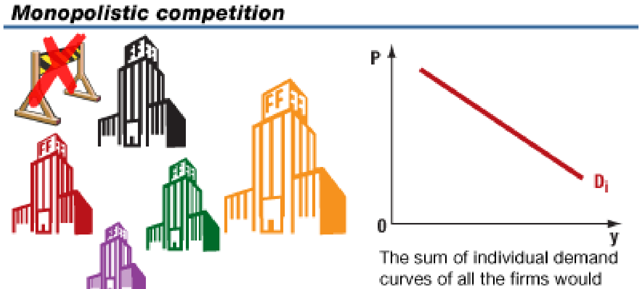


For a monopolist, the firm's demand curve is the same as the market demand curve.

- A single firm serves the entire market
- Excellent barriers to entry
  * so, a monopolist can set the price by choosing how much to produce.

A **monopoly** is an industry in which only one firm supplies the entire market. If a monopoly is to continue, there must be must significant barriers to entry for other firms. The monopolist is a price setter and has a demand curve identical to that of the market.

Monopolistic competition

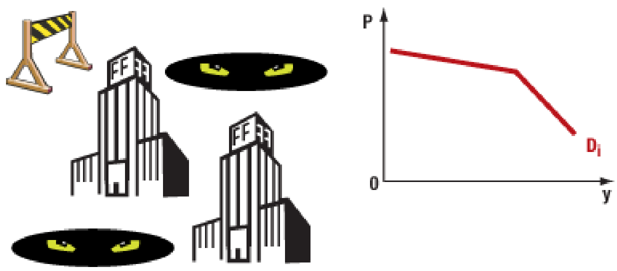


The sum of individual demand curves of all the firms would yield the market demand curve.

- A large number of firms
- Firms produce individualized or differentiated products
  * so, each firm has its own little version of a monopoly, and gets to exercise a little bit of market power.
- No barriers to entry

Monopolistic competition is a market in which firms try to carve up a market among themselves by attempting to slightly differentiate similar products. There are no barriers to entry and the sum of individual demand curves yields the market demand curve.

Oligopoly



- Small number of firms
- May produce identical or differentiated goods
- Firms base decisions strategically on the actions of their rivals
- There are barriers to entry

Oligopolies are markets in which a few firms try to watch each other, then to strategically react to what other firms do. Such firms may have kinked individual demand curves as shown to the left.

Overview

	Number of Firms	Type of Product Sold	Barriers to Entry
Perfect Competition	many	same	no
Monopolistic Competition	many	different	no
Oligopoly	few	?	some
Monopoly	one	unique	many

This table shows how the market structure is determined by the following characteristics: 1) number of firms 2) the type of product sold 3) barriers to entry