Section 5: Oligopoly

Market structure
-dominated by few firms with large price making power(high concentration ratio)
-High barriers to entry
-high product differentiation

Conduct
-Firms are interdependent
-Interpendence results in price rigidity
-Non-price competition- advertising branding
-Profit max is not sole objective. Increasing market share is
-Firms use comepetitive or collusive stragies to make interdependence work to their advantage
-Temptation to collude is high, to make high profits

Concentration ratios
- An indicator of the degree of monopoly power
- Is equal to the total market share of largest firms in the market

Competitve
-compete on price
-one firm has lower costs than other
-larger number of firms producing similar prodcuts(but less than monopolistic)
-barriers to entry are relatively low
-normal profits are earned (closer to monpolistic competition)
-saturated markets where there are price wars and strong incentive to cheat on collusive agreement

Advantages
-industry standard could improve as fims collaborate on technology to save on duplication of R and D
-can achieve high levels of allocative and productive efficiency

Evaluation
-have high market power but less likley to exert it due to uncertinty and interdependence, so are more likely to collude

Examples
-Supermarket Chains: four companies – Morrisons, Sainsbury's, Asda and Tesco – control 74.4% of the grocery market.

-High-Street Banks: this sector is dominated by Natwest, Lloyds, Santander, Barclays, and HSBC.

-Detergent Market: this is a duopoly. In other words, there are just two major suppliers. The suppliers are Unilever and Procter & Gamble. The two multinationals control more than four-fifths of the nation's detergent market.

-Electricity Distribution: EDF Energy, Centrica, RWE npower, Scottish Power, E.on, Scottish and Southern Energy (SSE) control 95% of the market.
-operating systems e.g windows, apple

Collusive(tacit or overt)
-Formal/Overt is when firms agree on what prices to charge
-Informal/tacit happens without agreements as firms agree it is in the best interest to not compete

-maxismises joint profits
-lowers the cost of competition
-reduces uncertainty in the market

-price leaders are present
-barriers of entry is high
-firms have similar costs
-few firms in the market (makes it easier to see what other firms are doing)
-high brand loyalty so firms that cheat on collusive agreements won't benefit
-firms may still compete by differentiating products, improve brand name, sales and promotions
-regulation is weak and ineffective

Disadvantages
-higher prices results in loss of consumer welfare(not allocatively efffeicnt)
-regressive imapcts on low income earners
-reinfroces monopoly increasing barrier to entry
-Absence of competition leads to being X-inefficient(less incentive to innovate)

Advantages
-large profits can be earned so more capital investment and dynamic effeciny
-higher profit allows more govt tax =more govt revenue
-Can expolit EOS so AC falls

Evaluation
-formal collusion is unlikely to occur because it is illegal
-if it does occur it can break down easily as producer cheat the agreement
-compeition authority presence is high
-entry of non-cartel into the indutry
-Infromal collusion won't last long becuase producers change their output or price
-non-price compeition can lead to dynamic effecincy increasing consumer welfare
-firms are unlikely to increase prices too high otherwise more firms will enter the market
-level of barriers to entry

Examples
-OPEC, oil distribution agreement
-Fairtrade
-Pharmaceutical sector
-automobile sector

Effeciencies

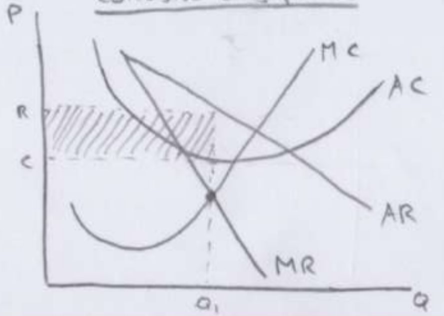
Competitive
-allocatively efficient: operating at AR=MC
-productively efficient: on lowest point of AC
-Can be dynamically efficient in SR

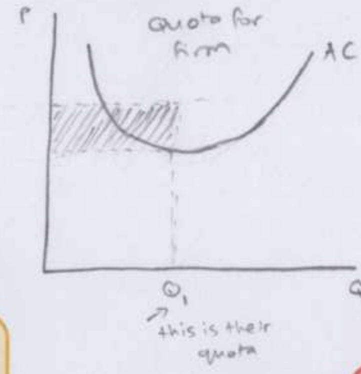
Collusive
-Not allocatively efficient: not operating at AR=MC
-Not productively efficient: not on lowest point of AC
-Can be dynamically efficient in LR
-earn supernormal profit in LR (but dont have the incentive to do so because new entrants threaten their market share)

Cooperation and Collusion
Cooperation: firms work togther on beneficial activites such as R and D, and product improvement
Collusion: firms work together to set to price to earn large profits a the expense of the consumer

Interdependence
-every descion of each firm imapcts each other
-when prices rise demand is price elastic: if prices rise the firm loses out on demand as consumer switch to other firms
-when prices decrease the is price inelastic: if prices are lowered the firm won't gain market share becuase all other firms will lower as well
-so prices remain stable/rigid resulting in non-price competition

Collusive oligopolies





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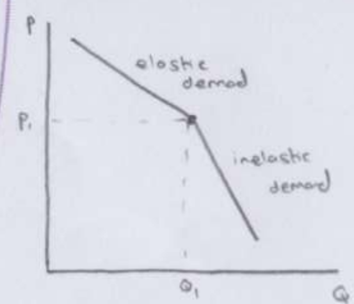
Interdependence (competitive oligopolies)



- No incentive to change prices so there is price rigidity for long periods of time

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