# Monopoly, perfect competition and imperfect competition essay sample

[Business](), [Marketing]()

Economists assume that there are a number of different buyers and sellers in the marketplace. This means that we have competition in the market, which allows price to change in response to changes in supply and demand. Furthermore, for almost every product there are substitutes, so if one product becomes too expensive, a buyer can choose a cheaper substitute instead. In a market with many buyers and sellers, both the consumer and the supplier have equal ability to influence price. In some industries, there are no substitutes and there is no competition. In a market that has only one or few suppliers of a good or service, the producer(s) can control price, meaning that a consumer does not have choice, cannot maximize his or her total utility and has have very little influence over the price of goods.

A monopoly is a market structure in which there is only one producer/seller for a product. In other words, the single business is the industry. Entry into such a market is restricted due to high costs or other impediments, which may be economic, social or political. For instance, a government can create a monopoly over an industry that it wants to control, such as electricity. Another reason for the barriers against entry into a monopolistic industry is that oftentimes, one entity has the exclusive rights to a natural resource. For example, in Saudi Arabia the government has sole control over the oil industry. A monopoly may also form when a company has a copyright or patent that prevents others from entering the market. Pfizer, for instance, had a patent on Viagra.

In an oligopoly, there are only a few firms that make up an industry. This select group of firms has control over the price and, like a monopoly, an oligopoly has high barriers to entry. The products that the oligopolistic firms produce are often nearly identical and, therefore, the companies, which are competing for market share, are interdependent as a result of market forces. Assume, for example, that an economy needs only 100 widgets. Company X produces 50 widgets and its competitor, Company Y, produces the other 50. The prices of the two brands will be interdependent and, therefore, similar. So, if Company X starts selling the widgets at a lower price, it will get a greater market share, thereby forcing Company Y to lower its prices as well.

There are two extreme forms of market structure: monopoly and, its opposite, perfect competition. Perfect competition is characterized by many buyers and sellers, many products that are similar in nature and, as a result, many substitutes. Perfect competition means there are few, if any, barriers to entry for new companies, and prices are determined by supply and demand. Thus, producers in a perfectly competitive market are subject to the prices determined by the market and do not have any leverage. For example, in a perfectly competitive market, should a single firm decide to increase its selling price of a good, the consumers can just turn to the nearest competitor for a better price, causing any firm that increases its prices to lose market share and profits.

Perfect competition is the market in which there is a large number of buyers and sellers. The goods sold in this market are identical. A single price prevails in the market. On the other hand monopoly is a type of imperfect market. The number of sellers is one but the number of buyers is many. A monopolist is a price-maker. In fact monopoly is the opposite of perfect competition. Firm under perfect competition and the firm under monopoly are similar as the aim of both the seller is to maximise profit and to minimise loss. The equilibrium position followed by both the monopoly and perfect competition is MR = MC. Despite there similarities, these two forms of market organization differ from each other in respect of price-cost-output.

There are many points of difference which are noted below.  Under perfect competition there are a large number of buyers and sellers in the market competing with each other. The price fixed by the industry is accepted by all the firms operating in the market. As against this under monopoly, there is only one single seller but a large number of buyers. The distinction between, firm and industry disappears under this type of market situation.  The average revenue curves under competition and monopoly take different shapes. The average revenue (price) curve under perfect competition is a horizontal straight line parallel to OX-axis. The industry demand curve or revenue curve slopes downward from left to right. But under monopoly the firm is itself the industry. There is only one demand curve common both to the monopoly firm and monopoly firm and monopoly industry. The average revenue curve under monopoly slopes downward and its corresponding marginal revenue curve lie below the average revenue curve. Under perfect competition MR Curve is the same as AR Curve.

Under perfect competition price equals marginal cost at the equilibrium output, but under monopoly equilibrium price is greater than marginal cost. Under perfect competition marginal revenue is the same as average revenue at all levels of output. Thus at the equilibrium position under perfect competition marginal cost not only equals marginal revenue but also average revenue. On the other hand under monopoly both the AR and MR curve slope downward and MR curve lies below AR curve. Thus average revenue is greater than marginal revenue at all levels of output. Hence at the equilibrium output of the monopolist price stands higher than marginal cost. Under competition price MR= MC. In monopoly equilibrium, price > MC. A competitive firm makes only normal profit in the long run. As against this a monopolist can make super normal profits even in the long run. In perfectly competitive market there is freedom pf entry and exit. Attracted by the supernormal profit earned by the existing firms the new competitive firms enter the market to compete away the supernormal profit. Output rises and profit becomes minimum.

Thus in the long run a competitive firm earns only normal profit. But under monopoly the firm continues earning supernormal profits even in the long run since there are strong barriers to the entry of new firms in the monopolistic industry. Under monopoly price is higher and output smaller than under perfect competition. Price output equilibrium is graphically shown in the diagram given below. AR = MR curve is the demand curve under perfect competition which is horizontal straight line. The downward sloping AR and MR curve are the average revenue and marginal revenue curves under monopoly. At equilibrium point E (MR = MC) a competitive firm produces ‘ OM’ output at OP market price. At point F a monopoly firm attains equilibrium producing OM, output at OP, price. OP competitive price is less than OP, (OP < OP,) and OM competitive output is greater than OM, output

(OM > OM,). A monopolist can discriminate prices for his product, a firm working under perfect competition cannot. The monopolist will be increasing his total profit by price discrimination if he find? Elastic ties of demand are different in different markets. As against his a competitive firm cannot change different prices from different buyers since he faces a perfectly elastic demand at the going market price. If he increases a slights rise in price he will lose the sellers and makes loss. Thus a competitive firm can not discriminate prices which a monopolist can do.

Monopoly and perfect competition represent two extremes along a continuum of market structures. At the one extreme is perfect competition, representing the ultimate of efficiency achieved by an industry that has extensive competition and no market control. Monopoly, at the other extreme, represents the ultimate of inefficiency brought about by the total lack of competition and extensive market control. Monopoly is a market structure with complete market control. As the only seller in the market, a monopoly controls the supply-side of the market. Perfect competition, in contrast, is a market structure in which each firmhas absolutely no market control. No firm in perfect competition can influence the market price in any way. The best way to compare monopoly and perfect competition is the four characteristics of perfect competition: (1) large number of relatively small firms, (2) identical product, (3) freedom of entry and exit, and (4) perfect knowledge. Number of Firms: Perfect competition is an industry comprised of a large number of small firms, each of which is a price taker with no market control. Monopoly is an industry comprised of a single firm, which is a price maker with total market control. Phil the zucchini grower is one of gadzillions of zucchini growers. Feet-First Pharmaceutical is the only firm that sells Amblathan-Plus, a drug that cures the deadly (but hypothetical) foot ailment known as amblathanitis.

Available Substitutes: Every firm in a perfectly competitive industry produces exactly the same product as every other firm. An infinite number of perfect substitutes are available. A monopoly firm produces a unique product that has no close substitutes and is unlike any other product. Gadzillions of firms grow zucchinis, each of which is a perfect substitute for the zucchinis grown by Phil the zucchini grower. There are no substitutes for Amblathan-Plus. Feet-First Pharmaceutical is the only supplier.

Resource Mobility: Perfectly competitive firms have complete freedom to enter the industry or exit the industry. There are no barriers. A monopoly firm often achieves monopoly status because the entry of potential competitors is prevented. Anyone can grow zucchinis. All they need is a plot of land and a few seeds. Feet-First Pharmaceutical holds the patents on Amblathan-Plus. No other firm can enter the market.

Information: Each firm in a perfectly competitive industry possesses the same information about prices and production techniques as every other firm. A monopoly firm, in contrast, often has information unknown to others. Everyone knows how to grow zucchinis (or can easily find out how). Feet-First Pharmaceutical has a secret formula used in the production of Amblathan-Plus. This information is not available to anyone else. The consequence of these differences include: First, the demand curve for a perfectly competitive firm is perfectly elastic and the demand curve for a monopoly firm is THE market demand, which is negatively-sloped according to the law of demand. A perfectly competitive firm is thus a price taker and a monopoly is a price maker. Phil must sell his zucchinis at the going market price. It he does not like the price, then he does not sell zucchinis. Feet-First Pharmaceutical can adjust the price of Amblathan-Plus, either higher or lower, and so doing it can control the quantity sold.

Second, the monopoly firm charges a higher price and produces less output than would be achieved with a perfectly competitive market. In particular, the monopoly price is not equal to marginal cost, which means a monopoly does not efficiently allocate resources. Although Feet-First Pharmaceutical charges several dollars per ounce of Amblathan-Plus, the cost of producing each ounce is substantially less. Phil, in contrast, just about breaks even on each zucchini sold.

Third, while an economic profit is NOT guaranteed for any firm, a monopoly is more likely to receive economic profit than a perfectly competitive firm. In fact, a perfectly competitive firm IS guaranteed to earn nothing but a normal profit in the long run. The same cannot be said for monopoly. The price of zucchinis is so close to the cost of production, Phil never earns much profit. If the price is relatively high, other zucchini producers quickly flood the market, eliminating any profit. In contrast, Feet-First

Pharmaceutical has been able to maintain a price above production cost for several years, with a handsome profit perpetually paid to the company shareholders year after year.

Fourth, the positively-sloped marginal cost curve for each perfectly competitive firm is its supply curve. This ensures that the supply curve for a perfectly competitive market is also positively sloped. The marginal cost curve for a monopoly is NOT, repeat NOT, the firm's supply curve. There is NO positively-sloped supply curve for a market controlled by a monopoly. A monopoly might produce a larger quantity if the price is higher, in accordance with the law of supply, or it might not. If the price of zucchinis rises, then Phil can afford to grow more. If the price falls, then he is forced to grow less. Marginal cost dictates what Phil can produce and supply. Feet-First Pharmaceutical, in comparison, often sells a larger quantity of Amblathan-Plus as the price falls, because they face decreasing average cost with larger scale production. MONOPOLY, CHARACTERISTICS:

The four key characteristics of monopoly are: (1) a single firm selling all output in a market, (2) a unique product, (3) restrictions on entry into and exit out of the industry, and more often than not (4) specialized information aboutproduction techniques unavailable to other potential producers. These four characteristics mean that a monopoly has extensive (boarding on complete) market control. Monopoly controls the selling side of the market. If anyone seeks to acquire the production sold by the monopoly, then they must buy from the monopoly. This means that the demand curve facing the monopoly is the market demand curve. They are one and the same. The characteristics of monopoly are in direct contrast to those of perfect competition. A perfectly competitive industry has a large number of relatively small firms, each producing identical products. Firms can freely move into and out of the industry and share the same information about prices and production techniques. A monopolized industry, however, tends to fall far short of each perfectly competitive characteristic.

There is one firm, not a lot of small firms. There is only one firm in the market because there are no close substitutes, let alone identical products produced by other firms. A monopoly often owes its monopoly status to the fact that other potential producers are prevented from entering the market. No freedom of entry here. Neither is there perfect information. A monopoly firm often has specialized information, such as patents or copyrights, that are not available to other potential producers.

The essence of a monopoly is a market controlled by a single seller. The “ mono” part of monopoly means single. This “ mono” term is also the source of such words as monarch–a single ruler; monochrome–a single color; monk–a solitary religious figure; monocle–an eyeglass for one eye; and monolith–a single large stone. The “ poly” part of monopoly means to sell. So the word itself, monopoly, means a single seller. The single seller, of course, is a direct contrast to perfect competition, which has a large number of sellers. In fact, perfect competition could be renamed multipoly or manypoly, to contrast it with monopoly. The most important aspect of being a single seller is that the monopoly seller IS the market. The market demand for a good IS the demand for the output produced by the monopoly. This makes monopoly a price maker, rather than a price taker. A hypothetical example that can be used to illustrate the features of a monopoly is Feet-First Pharmaceutical. This firm owns the patent to Amblathan-Plus, the only cure for the deadly (but hypothetical) foot ailment known as amblathanitis. As the only producer of Amblathan-Plus, Feet-First Pharmaceutical is a monopoly with extensive market control. The market demand for Amblathan-Plus is THE demand for Amblathan-Plus sold by Feet-First Pharmaceutical.

To be the only seller of a product, however, a monopoly must have a unique product. Phil the zucchini grower is the only producer of Phil’s zucchinis. The problem for Phil, however, is that gadzillions of other firms sell zucchinis that are indistinguishable from those sold by Phil. Amblathan-Plus, in contrast, is a unique product. There are no close substitutes. Feet-First Pharmaceutical holds the exclusive patent on Amblathan-Plus. No other firm has the legal authority to produced Amblathan-Plus. And even if they had the legal authority, the secret formula for producing Amblathan-Plus is sealed away in an airtight vault deep inside the fortified Feet-First Pharmaceutical headquarters. Of course, other medications exist that might alleviate some of the symptoms of amblathanitis.

One ointment temporarily reduces the swelling. Another powder relieves the redness. But nothing else exists to cure amblathanitis completely. A few highly imperfect substitutes exists. But there are no close substitutes for Amblathan-Plus. Feet-First Pharmaceutical has a monopoly because it is the ONLY seller of a UNIQUE product. Barriers to Entry and Exit.

A monopoly is generally assured of being the ONLY firm in a market because of assorted barriers to entry. Some of the key barriers to entry are: (1) government license or franchise, (2) resource ownership, (3) patents and copyrights, (4) high start-up cost, and (5) decreasingaverage total cost. Feet-First Pharmaceutical has a few these barriers working in its favor. It has, for example, an exclusive patent on Amblathan-Plus. The government has decreed that Feet-First Pharmaceutical, and only Feet-First Pharmaceutical, has the legal authority to produce and sell Amblathan-Plus. Moreover, the secret ingredient used to produce Amblathan-Plus is obtained from a rare, genetically enhanced, eucalyptus tree grown only on a Brazilian plantation owned by Feet-First Pharmaceutical. Even if another firm knew how to produce Amblathan and had the legal authority to do so, they would lack access to this essential ingredient. A monopoly might also face barriers to exiting a market. If government deems that the product provided by the monopoly is essential for well-being of the public, then the monopoly might be prevented from leaving the market.

Feet-First Pharmaceutical, for example, cannot simply cease the production of Amblathan-Plus. It is essential to the health and welfare of the public. This barrier to exit is most often applied to public utilities, such as electricity companies, natural gas distribution companies, local telephone companies, and garbage collection companies. These are often deemed essential services that cannot be discontinued without permission from a government regulation authority. Specialized Information

Monopoly is commonly characterized by control of information or production technology not available to others. This specialized information often comes in the form of legally-established patents, copyrights, or trademarks. While these create legal barriers to entry they also indicate that information is not perfectly shared by all. The AT&T telephone monopoly of the late 1800s and early 1900s was largely due to the telephone patent. Pharmaceutical companies, like the hypothetical Feet-First Pharmaceutical, regularly monopolize the market for a specific drug by virtue of a patent. In addition, a monopoly firm might know something or have a piece of information that is not available to others. This “ something” may or may not be patented or copyrighted. It could be a secret recipe or formula. Perhaps it is a unique method of production. One example of specialized information is the special, secret formula for producing Amblathan-Plus that is sealed away in an airtight vault deep inside the fortified Feet-First Pharmaceutical headquarters. No one else has this information.

Competition is very common and often times very aggressive in a free market place where a large number of buyers and sellers interact with one another. Economic theory describes a number of market competitive structures that takes into account the differences in the number of buyers, sellers, products sold, and prices charged. There are two extreme forms of market competitive conditions; namely, perfectly competitive and imperfectly competitive. The following article provides a clear overview of each type of market competitive structures and provides an explanation of how they are different to one another. What is Perfect Competition?

Perfect competition is where the sellers within a market place do not have any distinct advantage over the other sellers since they sell a homogeneous product at similar prices. There are many buyers and sellers, and since the products are very similar in nature there is little competition as the buyer's needs could be satisfied by the products sold by any seller in the market place. Since there are a large number of sellers each seller will have smaller market share, and it is impossible for one or few sellers to dominate in such a market structure. Perfectly competitive market places also have very low barriers to entry; any seller can enter the market place and start selling the product. Prices are determined by the forces of demand and supply and, therefore, all sellers must conform to a similar price level. Any company that increases the price over competitors will lose market share since the buyer can easily switch to the competitor's product.

What is Imperfect Competition?

Imperfect competition as the word suggests is a market structure in which the conditions for perfect competition are not satisfied. This refers to a number of extreme market conditions including monopoly, oligopoly, monopsony, oligopsony and monopolistic competition. Oligopoly refers to a market structure in which a small number of sellers compete with each other and offer a similar product to a large number of buyers. Since the products are so similar in nature, there is intense competition among market players, and high barriers to entry since most new firms may not have the capital, technology to startup. A monopoly is where one firm will control the entire market place, and will hold 100% market share. The firm in a monopoly market will have control over the product, price, features, etc. Such firms usually hold a patented product, proprietary knowledge/technology or holds access to a single important resource. Monospsony is where there are many sellers in the market with just one buyer and oligopsony is where there are a large number of sellers and a small number of buyers. Monopolistic competition is where 2 firms within a market place sell differentiated products that cannot be used as substitutes to each other. Perfect vs Imperfect Competition

Perfect and Imperfectly competitive markets are very different to one another in terms of the different market conditions that need to be satisfied. The main difference is that, in a perfectly competitive market place, the competitive conditions are much less intense, than any other form of imperfect competition. Furthermore, a perfectly competitive market structure is healthier as buyers have enough options to select from and aren’t, therefore, pressured to purchase one / few products and sellers are able to enter/exit as they please, which is opposite to most market conditions within an imperfectly competitive market place.

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Perfect and monopolistic competitions are both forms of market situations that describe the levels of competition within a market structure. Perfect competition and monopolistic competition are different to each other in that they describe completely different market scenarios that involve differences in prices, levels of competition, number of market players and types of goods sold. The article gives a clear outline of what each type of competition means to market players and consumers and shows their distinct differences. What is Perfect Competition?

A market with perfect competition is where there are a very large number of buyers and sellers who are buying and selling an identical product. Since the product is identical in all its features, the price charged by all sellers is a uniform price. Economic theory describes market players in a perfect competition market as not being large enough by themselves to be able to become a market leader or to set prices. Since the products sold and prices set are identical, there are no barriers to entry or exit within such a market place. The existence of such perfect markets are quite rare in the real world, and the perfectly competitive marketplace is a formation of economic theory to help better understand other forms of market competition such as monopolistic and oligopolistic. What is Monopolistic Competition?

A monopolistic market is one where there are a large number of buyers but a very few number of sellers. The players in these types of markets sell goods which are different to each other and, therefore, are able to charge different prices depending on the value of the product that is offered to the market. In a monopolistic competition situation, since there are only a few number of sellers, one larger seller controls the market, and therefore, has control over prices, quality and product features. However, such a monopoly is said to last only within the short run, as such market power tends to disappear in the long run as new firms enter the market creating a need for cheaper products. What is the difference between Perfect Competition and Monopolistic Competition? Perfect and monopolistic competition marketplaces have similar objectives of trading which is maximizing profitability and avoid making losses. However, the market dynamics between these two forms of markets are quite distinct. Monopolistic competition describes an imperfect market structure quite opposite to perfect competition. Perfect competition explains an economic theory of a marketplace which does not happen to exist in reality. Summary:

Perfect and monopolistic competitions are both forms of market situations that describe the levels of competition within a market structure. A market with perfect competition is where there are a very large number of buyers and sellers who are buying and selling an identical product. A monopolistic market is one where there are a large number of buyers but a very few number of sellers. The players in these types of markets sell goods which are different to each other, and therefore, are able to charge different prices. Monopolistic competition describes an imperfect market structure quite opposite to perfect competition. Perfect competition explains an economic theory of a marketplace which does not happen to exist in reality.