Types of available industry market structures

Understanding what is Industry market structures and different types of available industry market structures.

entify the dominant market structure to which the organization belongs with proper justifications and illustrations.

In order to accomplish aforesaid objectives, this assignment carried out an economical analysis for Dialog™ to identify the dominant market structure in which it's operating within.

1. 2 Background of the Industry

When considering all industries of Sri Lankan economy; mobile telecommunication industry can be identifying as one of major industry with high growth potential. The mobile phone usage has drastically increased in the past few years and mobile phone became essential day today equipment in the society. Mobile phones and mobile telecommunication can be identifying as a close complements commodities. As a result high demand for mobile phones was leads to enhance the growth potential of the Sri Lankan telecommunication industry. Following chart clearly indicating how the telecommunication industry dramatically increased from year 1992.

Figure 1

(Source: Telecommunication Regulatory Commission of Sri Lanka, 2010)

1. 3 Background of the company

Dialog Axiata PLC is country largest telecommunication service provider with over six million subscribers. Dialog launched its business operations in year 1995 under the name of Dialog GSM. It's a listed company in Colombo stock exchange and it was the country first USD one billion market capitalized company. Dialog currently operates on 2. 5G, 3G and 3. 5G communications networks and it was the first company which cover Jaffna peninsula in Northern Sri Lanka. Moreover company current portfolio consists of Dialog TV satellite service, Dialog CDMA, Dialog Broadband. (Dialog, 2010)

2. 0 Industry Market Structures

2. 1 Definitions

According Layton, Robbinson and Tucker (2005, p. 174) marketing structure refers to a classification system for the key characteristics of a market, including the number of firms, the similarly of the products they sell and the ease of entry into and exit from the market.

2. 2 Types of marketing structures

In economical context there are main four types of marketing structures available. Those are Perfect Competition, Monopolistic Competition, Oligopoly and Monopoly. In each type of marketing structure consist of different types of characteristics. Those characteristics of each market industries can state as follows.

2. 2. 1 Perfect Competition

According Layton, Robbinson and Tucker (2005, p. 174) perfect competition refers to a market structure characterised by (1) a large number of small firms, (2) a homogeneous product and (3) very easy entry into or exit from the market. Some of other charaecterstics of perfect competition includes;

Horizontal demand curve (firms act as a price takers)

Both the buyers abd sellers possess perfect knowledge about the markets.

No transport costs within the markets.

Perfect mobility of factors of production

(Industry market structures[Handout], n. d., p. 1)

2. 2. 2 Monopolistic competition

According Layton, Robbinson and Tucker (2005, p. 234) monopolistic competition refers to a market structure mainly characterised by (1) many small sellers, (2) a differentiated product and (3) easy market entry and exit. Some of other characteristics include;

Products are close substitutes to each other and they are branded (e. g. soap, liquor etc.).

If the price is increased, the firm will not lose all its customers.

If the price is decreased, the firm will not win all the customers who are with the competitors.

Firms often cut prices to increase its market share.

Firms also use advertising and special promotions to gain market share.

(Industry market structures[Handout], n. d., p. 2)

2. 2. 3 Oligopoly

According Layton, Robbinson and Tucker (2005, p. 208) oligopoly is a market structure characterised by (1) few sellers, (2) either a homogeneous or a differentiated product and (3) barriers to market entry. Some of other characteristics include;

Perfect Oligopoly refers to homogeneous products such as oil & steel.

Imperfect Oligopoly refers to differentiated products such as Cars.

Firms are interdependent.

If a firm increases its price above the market price, the others will not follow and the firm will rapidly lose sales.

If a firm reduces its price below the market price, the others will follow and the firm will slowly increase its sales.

Firms will avoid price wars and concentrate on non-price strategies to win market share. They use strategies such as better product design and finish, improvement of quality, better packing, after sales services, effective distribution, advertising, promotions, guarantees etc.

Kinked demand curve

(Industry market structures[Handout], n. d., p. 3)

2. 2. 4 Monopoly

According Layton, Robbinson and Tucker (2005, p. 208) monopoly is a market structure cauterised by (1) a single sellers, (2) a unique product and (3) extremely difficult or impossible entry into the market.

3. 0 Dominant Market Structure of the Company

After considering all aforesaid characteristics of industry market structures, it is identified that the Dialog is operate within Oligopoly Market Structure. This can justify from the following characteristics of oligopoly in related to Dialog.

3. 1 Characteristics of the Oligopoly Market Structure in related to Dialog

There are many characteristics that distinguish the oligopoly market structure from other market structures; the behavior of firms in this market structure also differs significantly from other market structures. Those characteristics include,

3. 1. 1 Few sellers in the market

According to the definitions of oligopoly it can be identified that this type of market structure is consist of few sellers and its usually ranging from 2-10. When considering the Sri Lankan mobile telecommunication industry, it is clearly can identify that there are only five service suppliers existed within the market. Following chart shows how the total revenue of the market divides among the five service suppliers.

Figure: 2

Source: Business International (2009)

3. 1. 1. 1 Concentration Ratio

According to Joseph, G. (2008, p. 199) concentration ratio represent the extent of the market supplied by a given number of firms. For example when considering four concentration ratio, its shows the portion of market supply by the leading firm of the industry. When we apply this into Sri Lankan mobile telecommunication industry, it is clear that nearly 95% of market share split among main four suppliers of the market. (Dialog, Mobitel, Etisalat, Airtel) Four concentration ratio theory suggest that if the concentration ratio of major four firms of a single industry is greater than or equal to 40%; that market which the firms are operate in more likely to be a oligopoly market. Since 95% of total Sri Lankan mobile telecommunication supply operate by the major four suppliers, it can be prove the fact that the Dialog is operate within the oligopoly market.

3. 1. 2 Mutual interdependence of the firms

One main characteristic of an oligopolistic market structure is that the firms are interdependent. Each firm is affected by its rivals actions, thus if Dialog decides to pursue policies to increase sales, then it will be at the expense of the competitors. The rivals may then respond by taking action to increase their market share, therefore no firms can afford to ignore the actions of the rival firms. It is thus impossible to predict the implications on a firm due to a change in price without considering the reactions of the rivals.

3. 1. 3 Barriers to entry

The oligopoly market structure has high barriers to entry. Barriers to entry may include patent rights, laws and industry regulations, high capital investment and etc. The high sunk cost or the high initial capital investment is the major barrier to entry to the mobile telecommunications market. When considering Dialog, it’s operates within an oligopoly market structure where there is high barriers to enter into the market. All the firms operate within Sri

Lankan mobile telecommunication industry should licenses granted under Section 17 of the Sri Lanka Telecommunications Act No 25 of 1991 as amend. (Telecommunication regulatory commission of Sri Lanka, 2010) This is a significant reason for firms in an oligopolistic market structure to earn normal profits.

3. 1. 4 Non-price competition

Firms in the oligopolistic market structure attempts to avoid price competition as price wars may arise. Thus “ brands” are established, Dialog is a well establish brand in the mobile telecommunication market, which highlights a certain characteristic that create a competitive edge for the company. Dialog boasts about the island wide coverage they offer.

Non-price competition may be in the form of sales promotions, special packages or even better facilities or clarity would matter. Dialog GSM also sponsors many sports activities such as the rugby tournament. Innovation is another form of price competition; Dialog launched the first Sinhala/Tamil sms facility as well as 3. 5 G facility in there service operations.

3. 1. 5 ‘ L’ shaped average cost curves

Economic studies suggest that the average cost curves of large firms operating in an oligopolistic market structure is ‘ L’ shaped rather than ‘ U’ shaped. Reason for this is because large firms face the same average variable cost regardless of increase or decrease in output. (Anderton, 2006, pg. 363)

Figure 3

Source: Alain Anderton – Economics 3rd edition 2006, pg. 363

3. 1. 6 Kinked demand curve

As mentioned above the demand curve of a normal firm is a downward sloping strait line. A firm in the oligopolistic market has a kinked demand curve; this theory was founded by Paul Sweezy from the USA and R. Hall and C. Hitch in the UK. (Anderton, 2006, pg. 363)

Figure 4

Source: Alain Anderton – Economics 3rd edition 2006, pg. 364

The theory suggests that a firm in an oligopoly market, like Dialog must make an assumption of how one firm (Mobitel/Etisalat) might react to price changes in the market. The kinked demand curve model assumes that there will be an asymmetrical reaction to a change in price. Thus if Dialog increases its price, other firms will not react. On the other hand if Dialog reduces the price, then other firms will also reduce its price to prevent losing their market share.

In the diagram shown below the profit maximizing level is where the MC (marginal cost) curve cuts the MR (marginal revenue). Thus if the MC of the firm lies anywhere between MC1 and MC2, the profit maximizing output will be P1 and Q1. Hence prices will remain stable even with considerable change in cost. (Sloman, 2004, Pg 208).

However the kinked demand curve model has two main limitations that must be noted. Although it shows price stability, it may be due to other reasons- Dialog may not want to revise prices frequently because it is inconvenient to establish new price list, new accounting policies, and it may upset it customers. Another drawback is that the model does not explain how the prices are being set in the first place. This is a serious drawback for a firm during periods of inflation, where Dialog like other firms in an oligopoly market will raise prices due to increase in cost and demand. This model suggests that the price will be raised only, when the marginal cost increases above MC2 which is illustrated in the diagram below.

Figure 4

Source: Industry market structures[Handout/ Course material], n. d., p. 3)

4. 0 Conclusion

From this report it has identified the dominant market structure of the Sri Lankan Telecommunication market with respect to Dialog Company. Thus by applying all relevant theories into practice, this report has identified Oligopoly as the dominant market structure of Dialog Company.

This fact has justified with illustrations by highlighting all relevant characteristics of the Oligopoly market structure such as few sellers in the market, mutual interdependence of the firms, barriers to entry, non-price competition, ‘ L’ shaped average cost curves, kinked demand curve with relate to Dialog Company.