Product has no close substitutes economics essay

Microeconomics is the study of individual economic units where we will use it in our daily lives. We will learn how to manage our money wisely so that we will be able to understand the economic concepts and theories. Besides that, we can also learn basic economics and have a better understanding of the economics of the market place.

2. 0 Definition of monopoly

According to Hashim, A. (2001) Comprehensive Economics Guide. 2nd ed. Singapore: Oxford University Press Pte Ltd, p. 84, Monopoly is an industry composed of a single seller of a product with no substitutes and with high barries to entry. A monopoly power exists when a single firm controls more than 25% of a market.

3. 0 Characteristics of monopoly

3. 1 One seller and a large number of buyers

3. 1. 1 A monopoly exists when there is only one seller of a product. For example, The Tenaga Nasional Berhad(TNB) has a monopoly of the electricity supply of Peninsular Malaysia. All houses and shops who get supply from Tenaga Nasional Berhad(TNB) will need to pay their electricity bill.

3. 2 Product has no close substitutes

3. 2. 1 The product sold by a monopolist should be no close substitutes. There are no other electricity supplier in Malaysia. There is only one supplier which is the Tenaga Nasional Berhad (TNB). There is no competition for their product. In Peninsular Malaysia, only Tenaga Nasional Berhad(TNB) supplies electricity to the country.

3. 3 Price maker

3. 3. 1 In a perfect competition, there will be no single firm can influence the price and this is called price taker. The Tenaga Nasional Berhad(TNB) will have the power to decide and control the price in the market since there are no competitors around.

3. 4 Restriction on the entry of new firms

3. 4. 1 In a monopoly market, there will be strict barriers to the entry of new firms and the barriers of entry are natural. A monopolist faces no competition because of barriers to entry.

3. 5 Advertising

AAdvertising in a monopoly market depends on the products sold. If the product are luxury goods such as imported items then the monopoly will need some advertisement to promote the consumers on the goods. Local public utility such as the electricity by Tenaga Nasional Berhad (TNB) need no advertisement since the consumers know from where to obtain such goods and they are the only corporation who supplies electricity.

4. 0 Introduction

5. 0 Differentiation of the features of the four market structures

Type of market

Number of firms

Freedom of entry

Nature of product

Examples

Implication of demand curve for firm

Perfect Competition

Very many

Unrestricted

Homogeneous

(undifferentiated)

Cabbages, carrots(these approximate to perfect competition)

Horizontal. The firm is a price taker

Monopolistic competition

Many/

several

Unrestricted

Differentiated

Builders, restaurants

Downward sloping, but relatively elastic. The firm has some control over price.

Oligopoly

Few

Restricted

1. Undifferentiated or 2. Differentiated

1. Cement

2. Cars, electrical appliances

Downward sloping, relatively inelastic but depends on reactions of rival to a price change

Monopoly

One

Restricted or completely blocked

Unique

Many prescription of drugs,

local water company

Downward sloping, more inelastic than oligopoly. The firm has considerable control over price.

5. 1 Number of firms

5. 1. 1 The perfect competition has large number of buyers and sellers. Firms are price taker because the quantity of a single seller sells in a market is so small compared to the overall industry. Besides that, the price is always constant where the seller can only decide the quantity to be sold and not the price of selling of a product. An example of the perfect competition is the duck producers. The price of the duck in the market is still depends on the demand and supply. The sellers can never control the price of the duck in the market even if they have high production, it will not affect much in that industry.

5. 1. 2 In a monopolistic competition, there are a large number of sellers. The number of firms exist in a monopolistic competition market is less than perfect competition. Due to the size of each firm which is small and hence, no individual firm can influence or control the market price. Therefore, each firm follows an independent price-output policy. The firm that produces toothpaste is in the monopolistic competition where there are many brands of toothpaste in Malaysia such as Darlie, Colgate and Polleney. They can never influence or control the price in of their products in the market.

5. 1. 3 In an oligopoly, the number of firms is small but the size of the firms is large. The market share of each firm is large enough to dominate the market. A few firms control the overall industry of an oligopoly. For example

the petroleum companies namely Shell, BHP, Caltex. They are large firms who have market shares which able to dominate the market.

5. 1. 4 Under monopoly, there is only one seller of a product and large number of buyers exist. A monopolist is a price maker since there is only one seller and no competitor and it has the power to control the price in the market. One of the examples of a monopoly is the Tenaga Nasional Berhad (TNB) where their company supplies electricity for the whole Peninsular Malaysia.

5. 2 Freedom of Entry

5. 2. 1 There is unrestricted freedom of entry and exit of the firms from the industry in the perfect competition and the monopolistic competition. A firm can easily enter the market and exit the market anytime they wish to. No restriction is imposed. If any firm who wish to open a fruit farms and operate the business if he/she has the necessary factors of production (land, labour and capital) he/she can always starts the business even there is a lot of fruit farms exist.

5. 2. 2 In an oligopoly market, there are various barriers to entry. Although similar to a monopoly, the firms in an oligopoly will restrict new firms to enter the market. The types of barriers to entry are economies of scale, forces to merge, ownership of patents and copyrights to name a few. This can be illustrated briefly by the petroleum industry in Malaysia where Mobil, Shell, Petronas and Caltex which already exist in the market and they control the market. The chances for a new firm to be formed in the petroleum

industry in Malaysia is very low due to the huge capital investment that they need to have a position in the market.

5. 2. 3 Under the monopoly market, there will be restricted freedom of entry and there are legal restrictions that restrict the entry of new firms into the industry. Hence there will be no competitors and competition for firms who are in the monopoly market. Telekom Malaysia (TM) is a good example of a monopoly since there is only one home telephone service in Malaysia which is Telekom Malaysia (TM) and not any other firms.

5. 3 Nature of product

5. 3. 1 The firms in a perfect competition must sell homogenous products. In the perfect competition structure, buyers cannot differentiate products in terms of quality, packaging, colour and design since they are identical. Furthermore, the firm cannot charge a different price for the same product which exist in the market. A classic example of this is the telecommunication service provider in Malaysia which are Digi, Maxis and Celcom. They provide customers with the same product in the market but buyers cannot differentiate their products no matter how, since they are all the same.

5. 3. 2 The monopolistic competition market sells differentiated products which are not identical. Each firms will have their own method to differentiate their products from other sellers to get more customers or consumers. Their products can be different in terms of the design, advertising, branding, and labelling. For example, when a perfume is nicely packaged in a box and labelled as ‘ best perfume’ then this product is in monopolistic competition.

5. 3. 3 Products in the oligopoly may be differentiated or undifferentiated. In Malaysia, the example of oligopoly market are petroleum and automobiles where petroleum is identical while cars are differentiated products.

5. 3. 4 Under monopoly market, the products produced has no close substitutes or unique. Tenaga Nasional Berhad (TNB) is one of the example of monopoly who is the electricity supplier from local public utility which has no close substitutes but if the buyers can find any other way to get electricity then this product is no more in monopoly and monopoly cannot exist if there is a competition or any substitute product.

5. 4 Implication of demand curve for firm

5. 4. 1 The demand curve for firm