The three market types monopolistic, oligopolistic and competitive

ASSIGN BUSTER

1. 0 Describe the three market types monopolistic, oligopolistic and competitive.

There are three types of market, monopolistic, oligopolistic and competitive, I will describe each of these types of markets. Below is a diagram of how these markets are set out. 1. 1 Monopolistic (imperfect competition)Monopolistic markets lie between pure perfect competition and pure monopoly.

Within this type of market a firm's product will differ to that of its rivals, the difference may only be small (for example the packaging may be slightly different), or there could be a big difference. The various firms within this market type have the ability to look at the differences between their own products and that of their rivals products, this gives them some flexibility when they decide the price of the products, rather than taking the market price. Within this market type:* Goods and services are not homogenous.* The free entry of new competitors to this market type will be faced with some kind of barrier(s).

* Neither consumers nor competitors will have the perfect knowledge of this type of market.* Firms can point out differentiation from competitors. Within this market type organisations have the ability to charge prices that are higher than the marginal cost of producing the product. Therefore resources may not be used in the most efficient ways. An example of a monopolistic market is the UK banking industry. The goods and services that individual banks other are not homogenous, there is a financial barrier when a new competitor wants to enter the market.

Neither consumers nor competitors have the perfect knowledge of this industry. 1. 2 OligopolisticAn oligopoly is a market dominated by a few large suppliers. The level of market concentration is very high (i.

e. a large % of the market is taken up by the leading firms). Firms within an oligopoly produce branded products (advertising and marketing is an important feature of competition within such markets) and there are also barriers to entry. Many firms within modern economics operate within oligopoly markets.

Another important characteristic of an oligopoly is interdependence between firms. This means that each firm must take into account the likely reactions of other firms in the market when making pricing and investment decisions. This creates uncertainty in such markets. Within an oligopoly there may be intense competition, if there isn’t then they may collude to operate as virtual monopolies. An example of an oligopoly is BSkyB and OnDigital who operate within the satellite television broadcasting industry. BSkyB, part of News International Corporation, which is run by Rupert Murdoch, had been dominating the industry up until 1998.

The main reason why it was so successful was because for people to watch certain sporting events such as Premiership football etc, you had to subscribe to Sky. When digital television came along it was possible to have hundreds of channels, which enabled Sky to broadcast even more sporting events, more films, pay per view services and interactive services. Sky’s biggest rival was OnDigital; they launched their digital service just after Sky. Sky was ahead of OnDigital and they were selling four systems compared to

one system by OnDigital. However for Sky to gain market share they had to offer a good value package to consumers. This shows that in a highly competitive oligopoly such as this consumers will benefit.

Oligopolies can operate within a highly competitive manner, which will result in lower prices for consumers and more benefits. However they could operate like a monopoly, therefore the government must intervene and make sure that oligopolies operate within a competitive manner. It is believed that companies operating within an oligopoly may seek to be very competitive until they have a high market share, but once they have gained a high market share they tend to act more towards a monopoly. However this may not be sensible and companies must consider that if they do this rival companies may be tempted to enter the industry. 1. 3 Perfect competitionPerfect competition does not exist, but it is an ideal.

Perfect competition does not exist because its rare that products are identical, firms usually are unable to enter and exit markets at will, and the buyers and sellers don’t have the required perfect knowledge of the market etc. Within a perfect competition market competitors would be unable to charge prices above the market price because consumers will just purchase rival products. Additional units of output (marginal units) will be supplied until the cost or producing the marginal unit (marginal cost) is the same as the market price. This is very efficient because the market price reflects the marginal cost of producing units of output.

There will not be any producers that will charge below the market price, as this will not cover the costs of production, this includes a margin for profit

which is just enough to keep the producer in business. For perfect competition to exist there is precise criteria that must be met, below are some are the points:* There will be many suppliers each with unimportant market share; this means there won't be a single person or firm that can affect the market.* Each firm is too small to affect price via a change in market supply – each individual firm is assumed to be a price taker.* Each firm must produce homogeneous products.* Consumers have perfect information about the prices all sellers in the market charge.* All firms (industry participants and new entrants) have equal access to resources (technology, other factor inputs).

* No barriers to entry and exit of firms in long run – market is open to competition from new suppliers – this affects the long run profits made by each firm in the industry.* The buyers and sellers would require perfect knowledge of the market. Its important to note that very few industries will meet the precise criteria for a perfect competition market type, however there are some industries that come close, examples would be foreign currency exchanges. They come close because there are many buyers and sellers. Usually each trader is relatively small in comparison to the total market and has to take the price as given.

The product is homogeneous. However individual traders could move currency markets. 2. 0 Explain how organisations respond to market forces – e.

g. supply and demand, with reference to the UK banking industry. There are two market forces, supply and demand, I will explain each one with

reference to the UK banking industry and I will explain how they work against each other. Once the quantity that customers are willing to buy at a particular price equals the quantity that the producers are willing to sell at that same price then a successful balance will have been achieved. It is important to know that these market forces, demand and supply, work against each other. Obviously consumers want to pay low prices for goods, whilst organisations want to make profit.

Therefore a balance must be met so that both consumers and organisations are happy. 2. 1 DemandDemand can be defined as, " the quantity of a product that consumers will be prepared to buy at a given price over a period of time." 1There are three important parts in this definition:* Any given consumer must have the ability and will to purchase a product. E.

g. everyone wants a huge expensive house but not everyone can afford one.* Demand and price are directly linked.* A period of time is involved. If prices change over a long period of time then so will demand.

The main factors that effect demand in reference to the UK banking industry are:* Population* Income* Changing tastes (including advertising)* People's expectations of future price and output changes2. 1. 1 PopulationPopulation is concerned with the number of potential customers in the market. If there is an increase in population then there will be an increase in demand for goods and services.

If a company exports its products then it can increase its market. However there are other factors to consider:* Age distribution* Sex distribution* Geographical distributionAs the graph above shows when the population

increases demand for banking services increases too. The demand curve moves to the right as more customers open bank accounts or take out loans etc. As the demand curve moves to the right the price remains the same.

Banks respond to this by providing more facilities and better facilities whilst ensuring that prices are competitive. 2. 1. 2 IncomeIn the UK income has been rising steadily for a while now. Seeing as income has been rising this results in people being financially better off, they now have more disposable income. As the graph to the right shows when customer’s disposable income increases they will be less likely to make purchases on credit cards, therefore the credit card sales will decrease as the demand curve shows.

Banks respond to this by reducing interest rates so that people may be more inclined to use their credit cards or take out loans etc. 2. 1. 3 Changing tastes (including advertising)If a bank decides to start a heavy advertising campaign then demand will increase.

Different times of the year will affect how much customers borrow, e. g. at Christmas customers will be more inclined to borrow money. As the graph to the right shows as advertising increases the amount of banking services sold increases, this is also the same for the Christmas period. Banks respond to this by advertising low rate credit cards and loans at certain times of the year (Christmas), they also advertise debt consolidation loans just after Christmas. 2.

1. 4 People’s expectations of future price and output changesUnder the current economic conditions people are spending less and so demand for loans and credit cards will fall as shown on the graph to the right. Banks

respond to this by introducing lower rate credit cards and loans along with heavy advertisement campaigns. 2.

2 Elasticity of demandElasticity of demand can be defined as, “ the relationship between the proportionate change in price and the proportionate change in quantity demanded.” 2A numerical value can be provided using the formula below. Price up 10%, demand down 25%Demand is elasticPrice up 10%, demand down 2%Demand is inelasticPrice up 10%, demand down 10%Unitary elasticity of demandWith regards to the UK banking industry demand may increase or decrease due to interest rates and times of the year. Inelastic demand applies to the UK banking industry because if interest rates rise then consumers will be far less inclined to borrow any more money, however consumers will always borrow money because it may be the only way to purchase an expensive item such as a car. The same can be said about mortgages, if interest rates increase consumers will be less inclined to borrow as much, however people need a place to live so they will still be forced to buy a mortgage only it probably won’t be such a large mortgage. 2.

3 SupplySupply can be defined as, “ the quantity of a product suppliers are willing to make available and provide for a market at given prices over a period of time.” 3There are two important parts to this definition:* It underlines the role of price in deciding the quantity which suppliers are prepared to provide for the market.* A period of time is involved just as it was with demand. There are various factors that affect supply, they are:* Price* Physical and natural conditions* Indirect taxation / subsidies* Technology* Cost of the factors of production2. 3. 1 PricePrice is the most

important factor affecting supply because it is essential that there is enough money made to cover costs otherwise the company will be running at a loss and eventually collapse.

Banks respond to this by ensuring that their products are priced so that they cover all costs and make a healthy profit. 2. 3. 2 Physical and natural conditionsThis includes weather, which could affect crops and disrupt transport networks, natural disasters (severe flooding) and disease that can affect crops and animals. This affects banks because if they offer insurance services they could be faced with large payouts. They respond to this risk by ensuring premiums are set accordingly to the however high the risk may be, for example home insurance, homes that are located near high risk flood areas, river banks etc will be charged a higher insurance premium than a house that is in a low risk flood area.

2. 3. 3 Political / civil actionsThis includes new laws and legislation that governments may pass; examples could be changes to the Consumer Credit Act 1974 would affect supply. Civilian riots may affect supply too. Obviously changes to legislation may affect banks, especially if it was to the Consumer Credit Act 1974. Banks respond to this by keeping up to date with legislation and ensuring they are not breaking the law.

2. 3. 4 Indirect taxationThis is a tax placed on the production of a good or service; it is therefore an additional cost for the producer. Examples include hydrocarbon taxes on petrol and diesel, alcohol taxes on alcoholic drinks, tobacco taxes on cigarettes, import duties which are taxes on non EU products, and of course VAT which is an indirect tax (17. 5%) on more or less

all products sold in the UK. Banks respond to these costs by increasing their own prices accordingly to make a profit.

2. 3. 5 SubsidiesThe government may give out subsidies to companies to reduce their costs; obviously this has the opposite effect to taxes. This will actually increase supply. Examples of this are payments made under the CAP to EU farmers and payments made to businesses under the Regional Policy. Banks will respond to subsidies if they receive any, they will respond by reducing their prices, as they will not have as much cost to cover.

2. 3. 6 TechnologyIntroducing new technology may improve the quality of the product and the speed at which things are done. New computer systems may enable staff to become more efficient.

Examples include faster communications such as networking computers or broadband Internet access, new computer technology such as Internet shopping. New technology will increase supply. Banks have responded to this by implementing Internet banking systems, which allows customers to access their accounts whenever they like, and from where ever they may be. Banks have introduced better computer systems that allow their staff to work at a more efficient level and provide a better service to the customers. 2.

3. 7 Costs of the factors of productionAll organisations require factors of production so that they can produce products; each factor receives a payment or reward. These factors are:* Land (rent)* Labour (wages)* Capital (interest)* Enterprise (profit)If these change the costs of production will change and so that will change the position of the supply curve (right). Banks

respond to this by ensuring they keep costs down and that they are making sufficient profits. 2.

4 Explain how three organisations in the UK banking industry have responded to market forces in different ways. The three organisations within the UK banking industry that I have chosen to analyse are HSBC, Lloyds TSB, and NatWest. HSBC responded to market forces by introducing online banking so that its customers could access their bank accounts anywhere in the world and at any time. This service has been highly successful and there has been a drop in the amount of calls received at the call center, so labour costs will steadily decrease as more customers gain confidence in using internet banking. Soon customers will be able to apply and be accepted for loans and credit cards, again this will take away work from staff and therefore cut overheads in the long run. Lloyds TSB have responded to market forces by providing more products, in particular Lloyds TSB have introduced various insurance services these include car, home, travel, pet, and health insurance.

By doing providing these products it helps customers because they won't necessarily need to go to independent insurance brokers. These insurance services have become extremely popular with customers and Lloyds TSB have now firmly diversified into the insurance industry. NatWest have responded to market forces by offering both variable and fixed rate mortgages. Customers can apply for a mortgage any time of the day and receive a decision within two days.

This helps customers because they can have their current account, savings accounts etc linked with their mortgage, plus it's all within their bank. They don't have to go to a building society. NatWest now offer a ' 100% mortgage' which allows buyers who haven't got the required amount of money for the initial deposit to take out a mortgage without a deposit. This responds to demand from customers because house prices are very high at the moment. 3. 0 What is meant by competitive advantage? How do organisations gain / lose competitive advantage? Competitive advantage is defined as, " factor which enables a firm to compete successfully with competitors on a sustained basis.

" 4Organisations will always seek to gain competitive advantage over their rivals. According to Michael Porter in his book, Competitive Advantage, he suggests that there are two main ways to be competitive. The first is that a business gains competitive advantage through becoming the producer that produces at the lowest cost. This can be achieved through producing and providing products in the most efficient way possible; this can be done through the use of modern technology. With reference to the UK banking industry banks can achieve this by providing Internet banking facilities to their customers.

Another way of achieving this is by providing large quantities of the product. Due to heavy advertising banks have been able to set up more bank accounts. If a company wants to gain the advantage of becoming a low cost producer then its essential that the company has a large market share. Michael Porter explains that by becoming the market leader profits will follow.

In other words the bigger share of the market you have the more chance you have of lowering costs down to that of the competitors. The other way Michael Porter suggests is differentiation; this is to make your product better than that of the rivals. However it is important that the product is still bought by the customers. Within the banking industry there are certain credit cards, which may be highly desirable, however they are not within every customers reach.

However these cards are still successful because there are people that have the wealth to posses such a card. There are other ways to differentiate products this can be done through customer service, promotion, advertising, branding etc. Banks have been looking to gain a competitive advantage over each other through the customer service improvements, for example NatWest have linked better customer service, promotion and advertising on their latest advertisement, this advert gives the message that NatWest are a friendly and sensible bank, that their customer service is better because they provide local bank telephone numbers. Halifax has been successful in their recent advertisement campaign as many regard it as humorous. The best way to differentiate a product is to add value; this way customer's perceive it as being better value than rival offerings.

Competitive advantage can be lost through competitors providing a product at the same price. When the first online banking system was established that bank gained a competitive advantage. However rivals soon realise that they are losing out and so they release similar systems, perhaps at a lower price or higher quality / extra features so rivals will gain the competitive advantage. 4.

0 How do companies grow? Is size important? Explain economies of scale, acquisitions, takeovers, mergers, etc in the context of the UK banking industry. Describe briefly the importance of customer perceptions and the impact of technology on organisations. 4. 1 How do companies grow? Organic growth (‘ scale expansion’) of a bank is when a move from a smaller to a larger bank is financed using internal profits, capital raised from shareholders or by borrowing money (loans etc). The generation of profit is essential in order to finance growth.

Usually banks will want to quickly change the scale of their operations therefore they will be seeking capital for the bank, they can do this by seeking extra capital through stakeholders or they can borrow money from various financial institutions. As the growth below shows (under 4. 3) as the bank grows in size the costs increase, however output increases. The graph gives an example of how a bank may grow in size.

4. 2 Is size important? Size is important because if you want to gain a competitive advantage over a rival bank then you must have a large client base. This is important because the larger the bank is the better advantages you receive from economies of scale. A larger bank will be able to provide more services and products at a cheaper price, as its production costs will be lower than that of a smaller rival bank.

4. 3 Economies of scaleEconomies of scale can be defined as, ” the reductions in the average cost of producing a commodity in the long run, as the amount of output of the commodity increases. The larger a business is,

the more efficiently it can produce.” 5In simple terms economies of scale are the advantages of being big.

Larger companies have many advantages over smaller companies, which enable them to gain competitive advantage. As a company gets bigger its able to obtain a number of economies, or advantages of size. Because of economies of scale a larger bank is able to provide more products at lower costs of production. The graph below shows how economies of scale can be shown.

It shows how a company is able to provide higher outputs at lower average costs due to expansion over five year periods.