Monopolistically competitive market

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In Principles of Economics (third edition), N. Gregory Mankiw describes the market as the combination of buyers and sellers of a particular good or service (64). Economists have defined three key elements for any industry to be classified in the market: the number of firms, the similarity of the products and the ease of entering a certain industry. By using these features, four market structures can be classified—perfect competition, monopolistic competition, oligopoly and monopoly (442).

Among all the markets, monopolistic competition can be the most common structure related to our daily life. Restaurants, clothing stores, coffeehouses, and supermarkets are all examples of the monopolistically competitive industry. Therefore, it is important to understand what monopolistic competition is and learn how to gain profit in this market. According to Microeconomics (international edition) by R. Glenn Hubbard and Anthony P. O'Brien, monopolistic competition is in which many firms sell similar but not identical products with almost no barriers for the new comers (478).

Discriminating the differences of the markets is essential, not only for economists, but also for the people who want to start their own business. Among four market structures, oligopoly and monopoly can be distinguished easily since they possess relatively small amount of firms and are difficult to enter (442). But monopolistic competition and perfect competition—a market structure in which many sellers sell homogenous products (443) — share many features since they all have many firms and free enter, which can make people confused.

Therefore, it is important to find out the differences between these two markets. In Microeconomics (international edition) R. Glenn and Anthony

point out that the ability to decide the market price – also defined as market power (548) – can be one of the key distinctions (489). Although the products sold by monopolistically competitive firms are quite similar, they are not identical, which means that firms can decide the price of their products by differentiating and innovation (478).

On the contrary, Hubbard and Anthony state that owing to the completely homology of the products sold by perfectly competitive markets, they cannot choose the price they charge. If one of the firms increases its price, it will lose all its consumers because consumers can find the identical products with lower price effortlessly (443). That’s why the price of wheat is same in all markets but restaurants charges diverse prices to their cuisines, even they are all coffee bars.

So market power can be a sufficient tool to make a distinction between monopolistic competition and perfect competition. Then the most concerned question to the sellers rises: how does one make a the firm successful in the monopolistic competition since there are plenty of firms producing similar goods and new firms can enter smoothly triggering by the profit of existing companies? One of the significant methods provided by both of the books – Principles of Economics (380) and Microeconomics (492) – is advertising.

Take McDonald’s as an example. As a typical company in monopolistically competitive market, McDonald faces intense competition from plenty of rivals selling quite similar products, no matter how strenuously it tries to make innovations on its foods. Nevertheless, McDonald is still one of the most profitable fast food chain stores in the world. There are complex factors

for its achievement, but successful advertising campaign must be one of them.

As Mankiw argues in the Principles of Economics, advertising can successfully attract consumers and at the same time undermine the rivals by revealing the unique feature of McDonald's products directly to the public (494). Although keeping lucrative is really difficult based on the intense competition and easy entry of the monopolistic competition, by using the appropriate strategy like advertising and innovation on their products, companies are possible to earn the profit even over a long period of time.