RATU NAVULA COLLEGE
YEAR 12 ECONOMICS 2021

WEEKLY HOME STUDY LESSON NOTES – Week 4
(# 45 – 49)

Strand: (2) Microeconomics **Lesson 45**
Sub Strand: (2.4) Market Structures
L/Outcome: - Define Oligopoly.
- Discuss the characteristics of Oligopoly market.

4. OLIGOPOLY

Definition

- is a market structure consisting of a few, relatively large firms selling products which are close substitutes and are price makers.

Characteristics of Oligopoly

1. **Few sellers few large firms** dominate the supply to an entire market. Each firm produces a significant portion of the total output.
2. Each firm produces produce **homogeneous** or **differentiated product**
   - ✓ If the firms produce a *homogeneous* product, like cement or steel, the industry is called a pure or perfect oligopoly.
   - ✓ If the firms produce a *differentiated* product, like automobiles, the industry is called differentiated or imperfect oligopoly.
3. Firms under oligopoly are **interdependent**. Interdependence means that actions of one firm affect the actions of other firms.
4. **Non-Price Competition**: Under oligopoly, firms are in a position to influence the prices. They follow the policy of price rigidity. Price rigidity refers to a situation in which price tends to stay fixed irrespective of changes in demand and supply conditions.
5. **Strong barriers to entry**. prevent entry of new firms into the industry. Patents, requirement of large capital, control over crucial raw materials, etc, are some of the reasons, which prevent new firms from entering into industry.
6. **Advertisements**: Due to severe competition and interdependence of the firms, various sales promotion techniques are used to promote sales of the product
7. Oligopolistic is faced by **kinked demand curve** because of competition from other oligopolists in the market
8. **Formation of cartels** a group of firms get together to enjoy monopoly power.
9. Competition is very fierce and often known as **cut throat competition**.

Class Activity

1. Cartels are formed in oligopoly market structures in order to
   A. act as price takers. C. identify problems in the market.
   B. enjoy some market power. D. share profits with other oligopolists

2. The kinked demand curve is usually illustrated by the _______________ market.
   A. oligopoly C. perfect competition
   B. monopoly D. monopolistic competition

Strand: (2) Microeconomics **Lesson 46**
Sub Strand: (2.4) Market Structures (Oligopoly)
L/Outcome: - List the examples of Oligopoly market
- Explain the how cartels are formed.

Examples of Oligopoly

Formation of cartels

- A **cartel** is defined as a group of firms that gets together to make output and price decisions.
- cartels arise in markets where there are few firms and each firm have a significant share of the market.
- Firms under oligopoly market situation form an open collusion or a group of firms form an agreement to set the price and the quantity in the industry and enjoy monopoly power and act as price makers.

Obstacles to Collusion

- Demand and cost differences
- Number of firms - large number of firms would lead difficulty to manage.
- Cheating
- Recession in the economy.

Class Activity

1. The oligopoly market structure is formed by
   - A. Many sellers
   - B. Few sellers
   - C. Many buyers
   - D. Single seller

2. Oligopolies are able to enjoy monopoly power through
   - A. product differentiation
   - B. cut throat competition
   - C. price leadership
   - D. formation of cartels

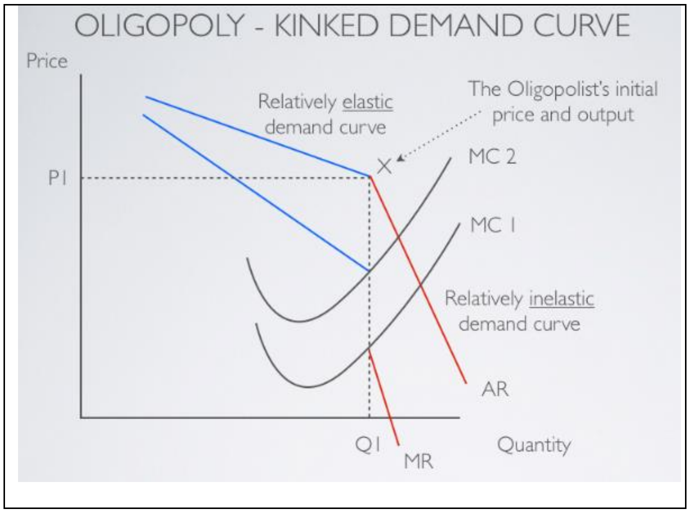
Strand: (2) Microeconomics **Lesson 47**
Sub Strand: (2.4) Market Structures (Oligopoly)
L/Outcome: - Explain the types of Collusions by Oligopolies.
- Explain the nature of demand curve of Oligopolies.

Types of Collusion by Oligopolies to safeguard their interest

1. **Formal collusion** - when firms make formal agreement to stick to high prices.
   - ✓ This can involve the creation of a cartel.
   - ✓ The most famous cartel is OPEC (Oil Petroleum and Exporting Countries) – an organisation concerned with setting prices for oil.
2. **Tacit collusion** - where firms make informal agreements or collude without actually speaking to their rivals.
   - ✓ This maybe to avoid detection by government regulators.
1. **Price leadership**. It is possible firms may try to unofficially collude by following the prices set by a market leader.
   - ✓ This enables them to keep prices high, without ever meeting with rival firms.
   - ✓ This kind of collusion is hard to prove whether it is unfair competition or just the natural operation of markets.

Nature of the Oligopoly demand curve

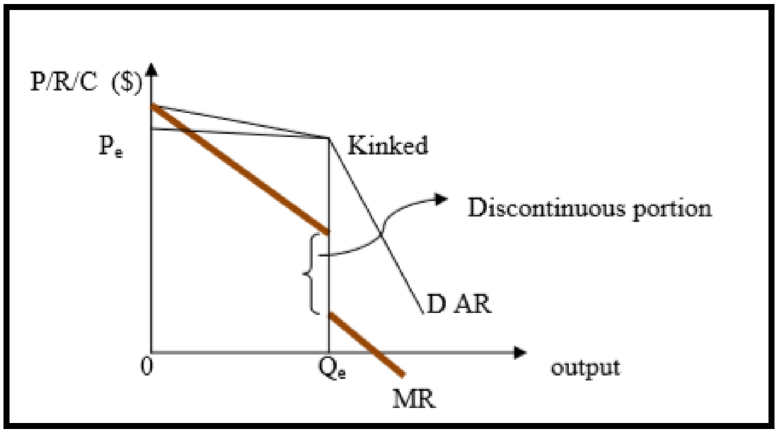
- The market demand curve that the oligopolist actually faces is the kinked-demand curve, labelled as AR = D
- The oligopolist faces a kinked-demand curve because of competition from other oligopolists in the market.
- If the oligopolist increases its price above the equilibrium price. it is assumed that the other oligopolists in the market will not follow with price increases of their own. The oligopolist will then face the more elastic market demand curve
- because at these higher price's consumers are more likely to switch to the lower-priced products provided by the other oligopolists in the market.
- If the oligopolist reduces its price below, it is assumed that its competitors will follow suit and reduce their prices as well. The oligopolist will then face the relatively less elastic (or more inelastic) market demand curve



Strand: (2) Microeconomics **Lesson 48**
Sub Strand: (2.4) Market Structures (Oligopoly)
L/Outcome: - Explain the marginal revenue curve of Oligopoly
- Explain the profits under Oligopoly

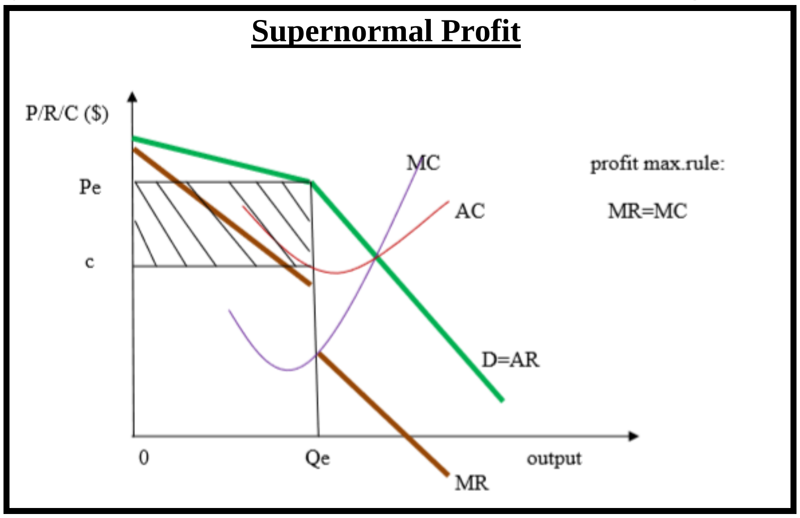
Marginal Revenue Curve for an Oligopolist

- There is a discontinuity in the marginal revenue curve for an oligopoly firm because of price rigidity or price stickiness at kinked.



Profits under Oligopoly

- Oligopolists mostly make supernormal profits both in short run and long run



Class Activity

1. The discontinuity in the marginal revenue curve for oligopolies occurs due to

A. Price rigidity
B. Price leadership
C. Predatory competition
D. Cut throat competition

2. Oligopolist is faced with kinked demand curve because

A. The rival firms match price reduction but do not match price increases.
B. The firms compete through product differentiation
C. There are very few sellers in the market
D. There is huge sunk cost

Strand: (2) Microeconomics **Lesson 49**
Sub Strand: (2.4) Market Structures (Oligopoly)
L/Outcome: - Explain the performance of oligopoly

Performance of Oligopoly

- There is no guarantee of efficiency
- Firms are unlikely to achieve economies of scale
- P > MC i.e. mark up pricing leads to misallocation of resources or exploitation of consuming public.
- Research and development undertaken by firms. Each has sufficiently high profits to find such development and innovation. It is advantageous to consumers because of better product quality.
- They are able to enjoy monopoly power through formation of cartels.

Government controls over Imperfect Market structures

- Government controls over imperfect market structures
- Government uses Competition laws - law that promotes or maintains market competition by regulating anti-competitive conduct by companies.
- Competition law is known as antitrust law or anti-monopoly law to protect public interest and maintain fair competition.
- Government also uses taxation to control monopoly power
- Government uses regulations and legislations to control monopolies in Fiji.
- Government also subsidizes monopolies

Class Activity

1. Complete the table by naming the type of market structures in order of the number of firms in the market.

No. of Firms	**Market Structure**
One firm (seller)	
Two firms	
A few firms	
Many firms	
One firm (buyer)	
Many buyers and sellers	

Worksheet

REF: 2018

A moderate *oligopoly* creates a stable structure, and moderate competition provides a healthy and lively market.

With reference to the above statement, discuss;

- **three** features of an oligopoly
- illustrate with **graph** the nature of the demand curve and profit maximisation
- **three** types of collusion oligopolist could use to safeguard their interest.