**COMPARISON OF THE CHARACTERISTICS OF PERFECTLY COMPETITIVE, MONOPOLISTICALLY COMPETITIVE, AND MONOPOLISTIC MARKETS, AND HOW CHANGES IN PRICING IN EACH MARKET AFFECT BUYERS’ PURCHASE DECISIONS**

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Course

Due Date

**CASE STUDY: PERFECTLY COMPETITIVE, MONOPOLISTICALLY COMPETITIVE, AND MONOPOLISTIC MARKETS**

Market Structures in economics can be classified into 5: Perfectly Competitive Markets, Monopolistically Competitive Markets, Oligopolistic Markets, Duopolistic Markets, and Monopolistic Markets. This essay will discuss, compare, and contrast the Characteristics of Monopolistic Markets, Monopolistically Competitive Markets, Perfectly Competitive Markets, and Organizations in each market, as well as how changes in their pricing affect the purchase decisions of buyers. A perfectly competitive market is a theoretical model that describes a market structure with specific characteristics. In this type of market, there are many buyers and sellers, all of whom are price takers, meaning they have no control over the market price of the product they are buying or selling. Additionally, there are no barriers to entry or exit, and perfect information is available to all market participants (Mankiw N. Gregory, 2022). Understanding the characteristics of a perfectly competitive market is essential for economists and policymakers in assessing the efficiency and competitiveness of real-world markets (Ladoke Akintola, 2020). A monopolistically competitive market is a type of market structure that lies between perfect competition and monopoly, exhibiting some characteristics of both. In this market structure, many firms are competing against each other, but each firm has a certain degree of market power due to product differentiation. This means that firms can differentiate their products in terms of quality, branding, and other attributes, allowing them to have some control over the price they charge (Mankiw N. Gregory, 2022). A monopolistic market is a market structure characterized by a single seller or producer selling a unique product or service, with no close substitutes. In this type of market, the seller has significant control over the price and quantity of the product, allowing them to maximize profits and exercise market power (Mankiw N. Gregory, 2022).

**CHARACTERISTICS OF PERFECTLY COMPETITIVE, MONOPOLISTICALLY COMPETITIVE, AND MONOPOLISTIC MARKETS AND EXAMPLES**

**Perfectly Competitive Market**

* There are numerous buyers and sellers in the market. The presence of many buyers and sellers ensures that no single participant can wield enough market power to influence prices (Mankiw N. Gregory, 2022).
* Goods and services are homogenous, meaning that there is no differentiation among products. This ensures that buyers have no preference for one seller over another and are willing to switch suppliers without any cost.
* There is perfect information in a perfectly competitive market. Buyers and sellers have complete knowledge about the prices, quality, and availability of products (Pindyck S. Robert & Rubinfeld L. Daniel, 2018). This information symmetry ensures that all buyers and sellers can make informed decisions.
* There are no barriers to entry or exit in a perfectly competitive market, allowing new firms to enter or existing firms to leave the market freely. This ensures that the market remains competitive and prevents any one firm from exerting monopolistic power.
* In a perfectly competitive market, each buyer and seller is a price taker, meaning they must accept the prevailing market price and adjust their behavior accordingly (Pindyck S. Robert & Rubinfeld L. Daniel, 2018). They must accept the market price determined by the forces of supply and demand.

An example of an organization operating in a perfectly competitive market is *Ilara Dairies.*

**Monopolistically Competitive Market**

* There is a large number of sellers, each offering slightly differentiated products. a monopolistically competitive market consists of many firms competing against each other. This large number of sellers leads to competition and product differentiation (Mankiw N. Gregory, 2022). This product differentiation allows firms to have some control over pricing and gives them the ability to attract customers based on unique features or branding. Product differentiation also leads to a greater variety of choices for consumers, as firms aim to cater to different preferences and needs (Pindyck S. Robert & Rubinfeld L. Daniel, 2018).
* There is freedom of entry and exit into the market, meaning that new firms can easily enter to compete with existing ones. This creates a dynamic market where firms are constantly striving to differentiate themselves and attract customers. This easy entry and exit allow for greater competition and innovation in the market, as firms constantly strive to differentiate themselves and attract customers. It also ensures that inefficient firms are forced to improve or exit the market, leading to overall market efficiency (Mankiw N. Gregory, 2022).
* Firms in a monopolistically competitive market engage in non-price competition, such as advertising and product development, to create perceived differences between their products and those of their competitors. This non-price competition can lead to increased consumer choice and product innovation (Mankiw N. Gregory, 2022). This also creates further complexity in understanding the true value of a product (Perloff M. Jeffrey, 2017).
* In these markets, there is incomplete knowledge about prices, costs, and product offerings, leading to uncertainty for both buyers and sellers. One reason for imperfect information is the presence of differentiated products, which makes it difficult for buyers to compare prices and quality across different brands (Mankiw N. Gregory, 2022).
* In a monopolistically competitive market, advertising and branding play a crucial role in differentiating products and creating brand loyalty among consumers. With the presence of many firms producing similar products, advertising helps firms highlight the unique features or benefits of their products and create a distinct brand image. Advertising also helps in informing and persuading consumers about the existence and merits of certain brands, thus increasing product demand and market share. Branding, on the other hand, involves creating a unique name, logo, or design that identifies and distinguishes a product from other competitors in the market. Successful branding helps firms build customer trust, establish a reputation, and create a loyal customer base (Mankiw N. Gregory, 2022).

An example of an organization operating in a monopolistically competitive market is *KFC.*

**Monopolistic Market**

* In a monopolistic market, there is only one seller who dominates the market and offers a unique product. This lack of competition allows these sellers to have a significant amount of control over the prices and supply of goods and services (Mankiw N. Gregory, 2022).
* In a monopolistic market, the company possesses significant control over the price it charges for its products or services. Since there are no close substitutes available, the company can set higher prices without losing customers to competitors. This allows the monopolistic firm to maximize its profits. Furthermore, the lack of competition means that there is no pressure to lower prices to match or beat competitors (Mankiw N. Gregory, 2022).
* Another characteristic of a monopolistic market is the presence of barriers to entry. Barriers to entry refer to factors that make it difficult for new firms to enter the industry and compete with existing firms. These barriers can include high start-up costs, economies of scale that give larger firms a cost advantage, exclusive access to resources or technology, and legal or regulatory restrictions. These barriers enhance the market power of existing firms and prevent new entrants from challenging their dominance (Mankiw N. Gregory, 2022).
* Inefficiency is another characteristic of a monopolistic market. Due to the lack of competition, monopolistic firms have no incentive to operate efficiently or improve productivity (Pindyck S. Robert & Rubinfeld L. Daniel, 2018). They can afford to be wasteful and inefficient in their production processes, resulting in higher costs and lower overall productivity. This inefficiency ultimately leads to higher prices for consumers, as firms can pass on their higher costs to the market (Pindyck S. Robert & Rubinfeld L. Daniel, 2018). Additionally, monopolistic firms may lack the motivation to invest in research and development or technological advancements, further hindering efficiency and innovation. Overall, the absence of competitive pressures in a monopolistic market allows for inefficiencies to persist, leading to negative consequences for both firms and consumers.
* Monopolistic markets often face government intervention due to their ability to exploit their market power and harm consumers. Government regulation may be necessary to prevent monopolistic firms from engaging in anticompetitive practices such as price fixing or predatory pricing. For example, in the case of Microsoft, the U.S. government brought an antitrust lawsuit against the company in 1998, alleging that it engaged in anticompetitive practices to maintain its monopoly in the operating systems market. This case demonstrates the need for government regulation to ensure that monopolistic firms do not abuse their market power to the detriment of consumers (Mankiw N. Gregory, 2022).

An example of an organization operating in a monopolistic market is *Kenya Power.*

**COMPARISONS BETWEEN THE THREE MARKETS**

* Both Perfectly Competitive and Monopolistically competitive markets have a large number of sellers in the market while a Monopolistic Market has only one seller in the market (Mankiw N. Gregory, 2022).
* Both Perfectly Competitive and Monopolistically Competitive markets have freedom of entry and exit into a market while a Monopolistic Market has barriers to entry and exit of the market (Mankiw N. Gregory, 2022).
* Products in Perfectly Competitive Markets are homogenous, while products in Monopolistically Competitive Markets are similar but differentiated and products in a monopolistic Market are very unique/ are only sold by that one seller (Mankiw N. Gregory, 2022).
* In a perfectly competitive market neither buyers nor sellers have any control over the price of a commodity while a seller in a Monopolistic market has significant control over the price of a commodity since it has no competitors (Mankiw N. Gregory, 2022). However, this control has a limit. This limit is implemented by the government to protect the consumers. On the other hand, in a Monopolistically Competitive market, sellers have some type of control over their pricing. This is because each seller offers a differentiated product.
* Both Perfectly competitive and Monopolistically competitive markets strive for efficiency through investing in innovation and research but in a monopolistic Market the seller is rather unbothered since they have sole control over the market (Pindyck S. Robert & Rubinfeld L. Daniel, 2018).

**How Changes in Pricing in the three markets will affect buyers' purchase decisions**

1. Perfectly Competitive Market- In a perfectly competitive market, where there are many buyers and sellers, pricing changes typically have a significant impact on buyers' decisions. According to (Mankiw N. Gregory, 2022), an increase in price may lead buyers to seek alternatives or postpone their purchase, as they have access to a wide range of similar products at competitive prices. On the other hand, a price decrease may stimulate demand and encourage buyers to make immediate purchases while taking advantage of the lower price. In the given example, if the price of *Ilara* increases, the buyer would choose to buy *Lato* instead since they are both whole milk.
2. Monopolistically Competitive Markets- In a monopolistically competitive market where goods are similar but differentiated, changes in pricing will have a varying impact on buyers’ decisions. On one hand, an increase or decrease in price will bring about a perceived increase or decrease in quality (respectively) thus encouraging buyers to continue buying or not buy the items (respectively), (Mankiw N. Gregory, 2022). Buyers may also be encouraged to buy a good when the price increases due to customer loyalty. On the other hand, price-sensitive buyers may buy the item with the decreased price and not buy the item with the increased price. In the given example, an increase in the pricing of KFC will not affect the purchase decisions of the consumer due to customer loyalty.
3. Monopolistic Market- In a monopolistic Market changes in price do not affect the buyers’ purchase decision since there are no substitutes in the market (Mankiw N. Gregory, 2022). In the example given, if Kenya power electricity prices increase, the buyers’ purchase decision will not change. They will still purchase electricity provided by the organization.

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