4. OLIGOPOLY

Q:1 Define Oligopoly. Explain its Features?

(A) Oligopoly :- Oligopoly is one of important market Structure where Very few firms are Selling either Homogeneous or differentiated Products.

When firms are selling Homogeneous goods is known as Perfect Oligopoly market.

When firms are selling differentiated goods is known as Imperfect oligopoly market.

The word Oligopoly is taken from Greek word- 'Oligous' which means 'Few' and 'Poly' means Seller.

(B) Meaning :- According to Feller —

" Oligopoly means Competition among the Few "

(C) Examples of Oligopoly are —

Automobiles sellers, Electronic sellers, Cement Sellers, Oil Producing Companies, mobile service Providers etc.

(D) Features OF Oligopoly :- economicsguidance.com

1. **Few Sellers :-** Under Oligopoly market, there are Few Sellers who enjoy more Control Over the Product.

2. **Interdependence :-** The Sellers in Oligopoly market, depends on each other. If any firm makes Changes in Price OF Product, design, advertising or Nature of Product etc. then Other firms will also try to bring same changes

in market. Thus in Oligopoly market, all the Firms are inter-dependence regarding Price and Out Put Policy.

③ **Advertisement and Selling Cost :-** Advertising is a Powerful instrument in the hands of Oligopolist Each firm tries to attract consumers towards its Product by incurring more expenditure on Advertisement and Selling Cost.

According to Prof. Boumol - "Under Oligopoly Advertising can become Life and Death matter".

④ **Lack of Uniformity :-** There is a Lack of Uniformity among the firms in terms of their size. Some firms may be very small while others may be too Large.

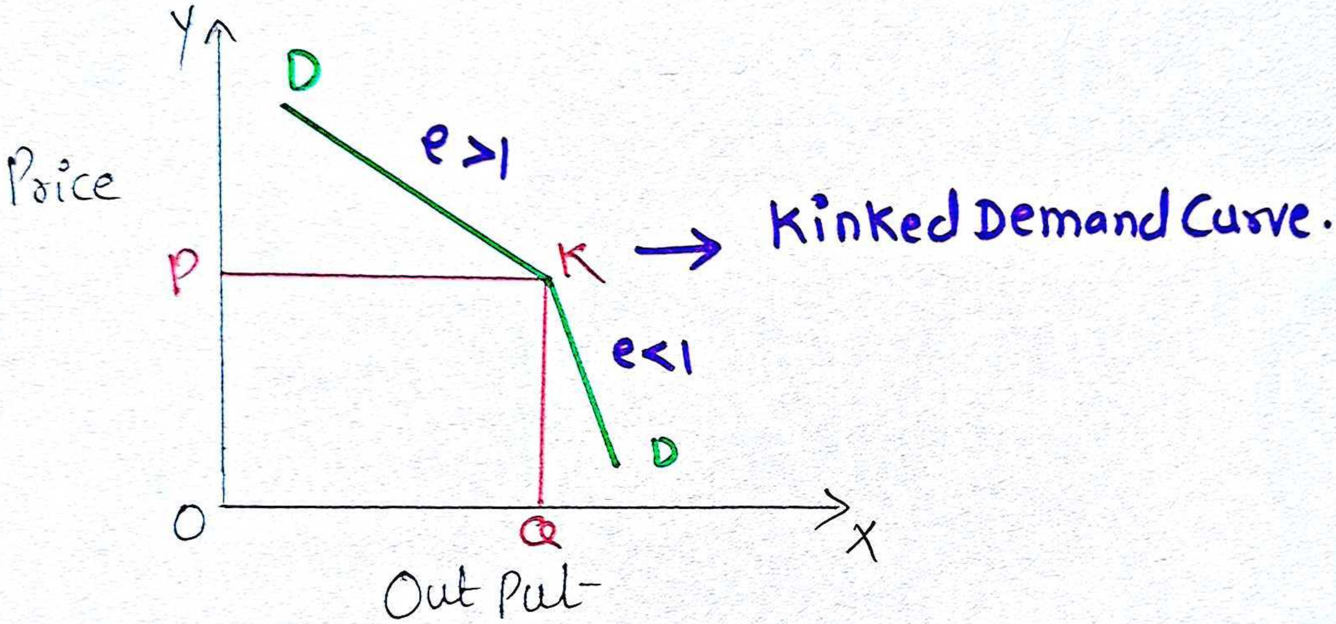
⑤ **Entry Barriers :-** In Oligopoly market, there is close Competition among the sellers. There is no barriers to either entry into or Exit from Industry in Short-Run. But in the Long-Run, firm has to Face Certain Entry barriers such as Government Licence, Patents etc.

⑥ **Competition :-** In Oligopoly market, there is tough Competition among the sellers. Every seller keep watch over any move of its rival to stand in the market. Generally there is Price war in the market.

⑦ **Uncertainty :-** In Oligopoly market, we Observe Uncertainty due to different behaviour Patterns. Rivals may Join Hands and Co-operate each other or Rivals may try to fight with each other.

⑧ **Indeterminate :-** In Oligopoly market, It is difficult to draw accurate demand curve. An Oligopolist demand curve is Uncertain because Sellers Price Policy Out Put Policy are Unpredictable. All Firms are interdepéndce on each other. Thus we get indeterminate demand curve in Oligopoly market.

⑨ **Kinked Demand Curve :-** According to Paul sweezy, Firms in Oligopolistic market have Kinked demand Curve.



Q:2 Write Short Note → Collusive and Non-Collusive Oligopoly.

Ⓐ **Introduction :-** In Oligopoly market, we observe Competition and Collusion. The sellers are interdependence on each other for Price policy. Due to tough Competition few Sellers Collude with each other.

Ⓑ **Types OF Oligopoly Market :-**

① **Non-Collusive Oligopoly :-** Under non-Collusive Oligopoly market, Firms behave independly even though they are interdependent in market. Every seller keep watch over any move OF its rivals to stand in the market. Kinked demand Curve Model is the example OF Non-Collusive Oligopoly.

Main Features of Non- Collusive Oligopoly market :-

i) Few Large firms

ii) Entry Barriers

iii) Non- Price Competition

iv) Product differentiation

v) Interdependance in Decision-making etc.

② Collusive Oligopoly :-

To Reduce Competition and Uncertainty in market Few firms work together. firms makes Cartel to determine Price. Due to Price-Fixing these firms Control supply and enjoy monopoly Power in Market.

Main Features OF Collusive Oligopoly

i) Market is dominated by Few Large firms

ii) Price fixation / Price Leader

iii) Inelastic Demand

iv) Reduce Competition etc.

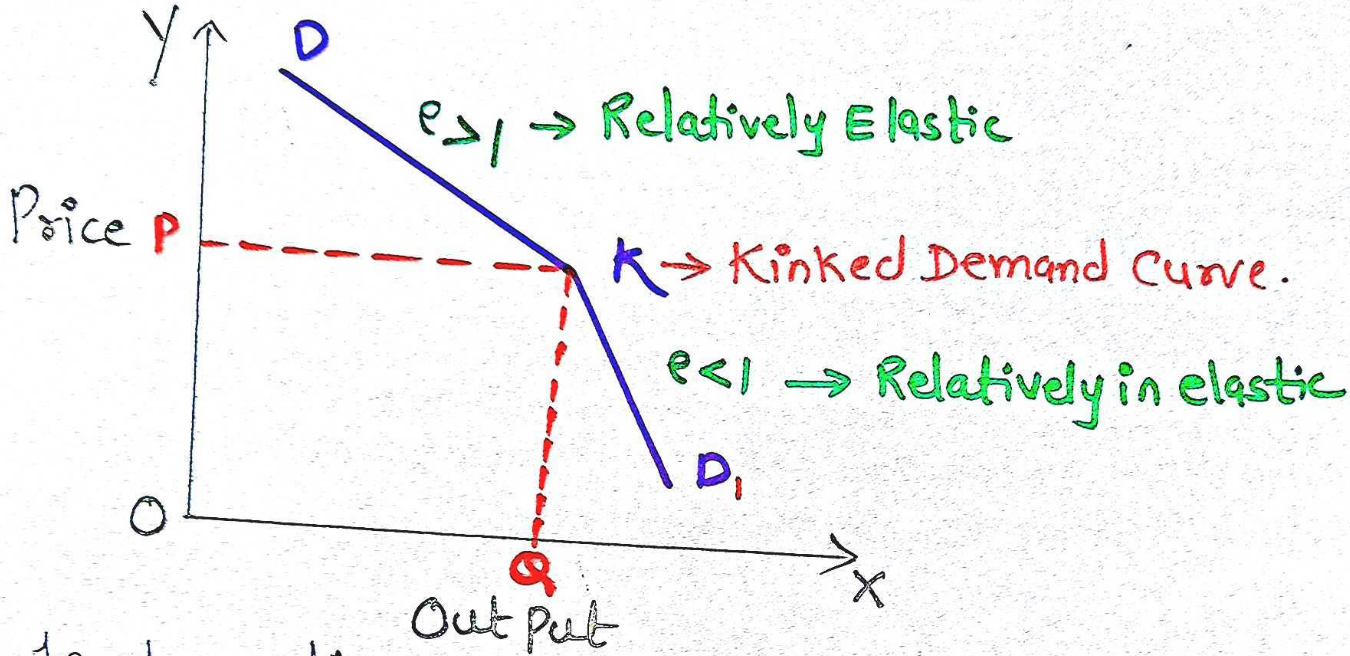
The dominant firm may take the Role OF Price Leader and decide the Price and output Policy For market. It helps to reduce Competition among the firms.

Q:3 Explain the Equilibrium OF an Oligopoly firm Facing Kinked Demand Curve? OR
Discuss the Price Rigidity in Oligopoly market with the help oF Kinked Demand Curve?

Ⓐ Price Rigidity In Oligopoly Market :-

Due to Uncertainty and Interdependence OF firms in Oligopoly market leads to Indeterminateness OF Demand Curve.

According to Paul Swerzy an American economist, there is Kinked Demand Curve in Oligopoly market. Due to Kinked demand Curve, there is Rigid Price Fixed in the market Shown in following diagram ⟶

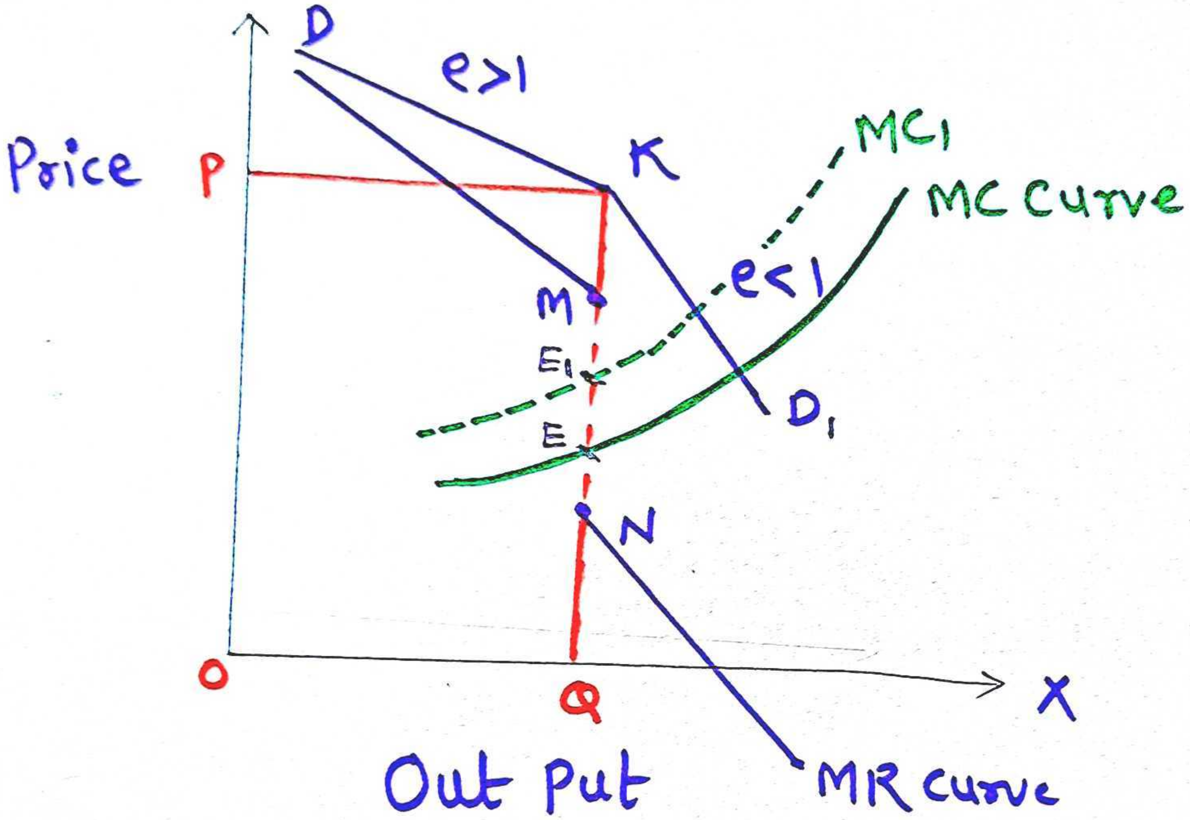


In above diagram —

1) DD_1 is Kinked Demand Curve in Oligopoly market. It is made up of Two Parts —
   i) DK — Relatively Elastic $(e>1)$
   ii) KD_1 — Relatively inelastic $(e<1)$
2) There is Kink (Turning Point of market) on Demand Curve at Point K. Here Producers sell OQ output at Rigid Price OP.
3) IF Producers try to raise the Price, it will reduce the Sales in market as demand is Relatively elastic.
4. If Producer try to reduce the Price, Rivals will Quickly take action on it due to Close interdepence in market.
4. Thus OP Rigid Price is Fixed in Oligo Poly market.

(B) Equilibrium OF firm in Oligopoly Market :-

A Producer enjoy Equilibrium in Oligopoly market at Kinked demand curve where Rigid Price is fixed in Market. It is explained with the help of following diagram:



In above Figure we Observe—

1. DD_1 is Kinked demand Curve in oligopoly market. It is made up of two segments—
   i) DK – Relatively Elastic (e>1)
   ii) KD_1 - Relatively inelastic (e<1)
2. The Kink – K in oligopoly market cannot determined at specific Period of time. It make be Vary from One month to one year or 2 years etc.
3. The Producer in Oligopoly market, enjoy Equilibrium at Point K. Here OQ output is sold at OP Price.
4. The time gap between two Demand Segments is Very special because during that Period Marginal cost

may be increase due to -

- increase in Cost of Raw-material
- Increase in wages of Labour,
- Increase in Price of Power, fuel,
- Increase in government Taxes
- Increase in Transport cost etc.

5) When Producer enjoy Equilibrium at Point E, where MR = MC. Here Producer enjoy Excess Profit due to Low Cost of Production

6) when Producer enjoy Equilibrium at Point E_1, where $MR = MC_1$. Here Producer enjoy Normal Profit due to increase in Marginal Cost

7. Thus In Oligopoly market, Producer fix Rigid Price OP. Here Producer cannot increase or decrease the Price - OP. He has to anyhow enjoy Equilibrium at Kink-demand curve.

Q84 Discuss the Reasons for forming Cartels and their Effects? OR
Explain the Model of Collusive Oligopoly?

A) Collusive Oligopoly | Cartel formation :-

Firms Under Oligopoly market, wants to have Collusive Oligopoly by Cartel formation.. Cartel helps to reduce-

i) Uncertainity in market.
ii) Interdependence on each other.
iii) Price war
iv) Cut Throat competition etc.

(B) **Meaning :-** " A Cartel is an agreement among Competing firm to Collude (Join) together to earn higher Profits. "

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(C) Types of Collusive Oligopoly

1. Market sharing cartel
2. Centralised Cartel.

1. **Market sharing Cartel :-** Under this market, each member gets the Exclusive (Special) rights to Operate in Particular area.

2. **Centralised Cartel :-** Under this market, Cartel will decide – Price of Product
– Distribution of Product
– Norms of Profit sharing etc.

Example – OPEC is best example of Centralised Cartel.

Some Cartel Formed secretly. They may or may not have written Agreement. Such Cartels are harmful for markets.

(D) Effects of Collusive Oligopoly / cartel :-

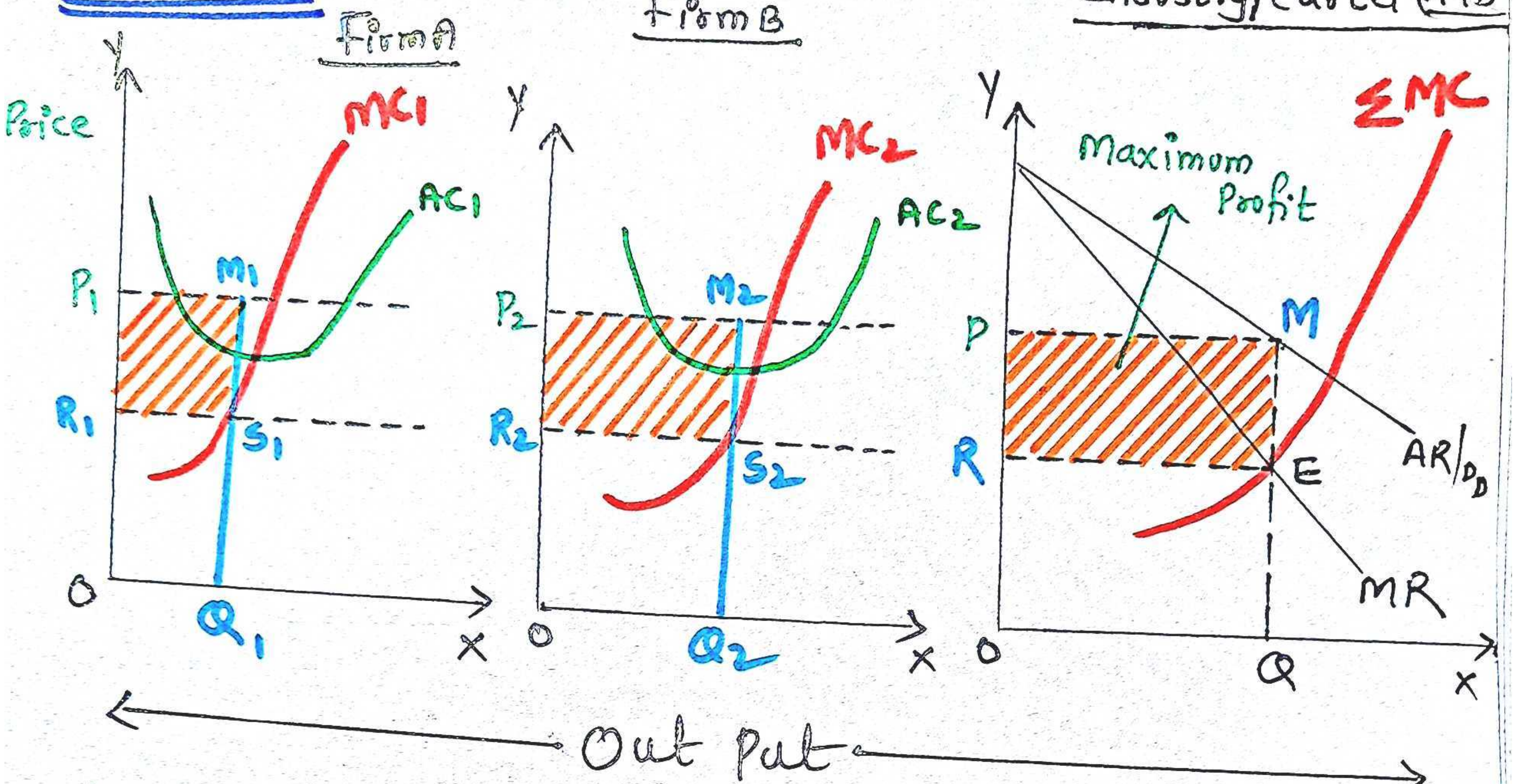
(1) Maximum Profit Under Centralised Cartel :-

Under Centralised Cartel, a Cartel will enjoy maximum Profit at Equilibrium Level where–

Industry's MC = Industry's MR.

Let us assume that there are Two Firm A and B.
Firm A is Low Cost Firm and Firm B is High cost Firm.
Both Firms A and B are Producing Homogeneous Product.

Diagram :-



In above diagram we Observe —

1) Firm A have Low cost of MC_1. Here Producer enjoy Less Profit = $P_1R_1S_1M_1$ after selling OQ_1 output.

2) Firm B have high cost of MC_2. Here Producer enjoy High Profit = $P_2R_2S_2M_2$ after selling OQ_2 output.

3) After Centralised Cartel – Firm A + Firm B = Industry

i) Marginal Cost Curves added Horizontally $MC_1 + MC_2 = \Sigma MC$

ii) Output Produced together – $OQ_1 + OQ_2 = OQ$

iii) Same Price = OP is charged in market.

iV) Now Cartel Enjoy maximum Profit at Equilibrium where $MR = \Sigma MC$

Maximum Profit = PREM

Maximum output = OQ Level

(2) Non-Price Competition :- In Oligopoly market, Price remain Rigid due to indeterminateness of demand Curve.

IF Cost of Production is Same, Price will also remain Same for Different Firms.

But IF Cost of Production is different, then Low Cost Firm try to fix Low Price. In such Cases Cartel may break.

Thus firms do not Change the Price. Price Remain Same but they follows Non- Price competition. It means firms Provide Secret Discounts, Commission, additional Facilities and Services to Retailers and Consumers.

Q:5 What is Price Leadership? Explain Various types and Limitations of Price Leadership?

(A) Price Leadership :- In a free Oligopoly market, there is always a Price War in the market which Provide more benefits to Consumers.

To avoid unhealthy competition, it is necessary to have One Leader firm which decide the Price.

Thus Price Leadership is informal and tacit understanding between Producers in Oligopoly market.

(B) Types OF Price Leadership :-

1. Dominant Firm Leadership :- In Oligopoly Market, a firm Producing goods and Services at Large Scale, enjoy Position of Dominant firm in market.

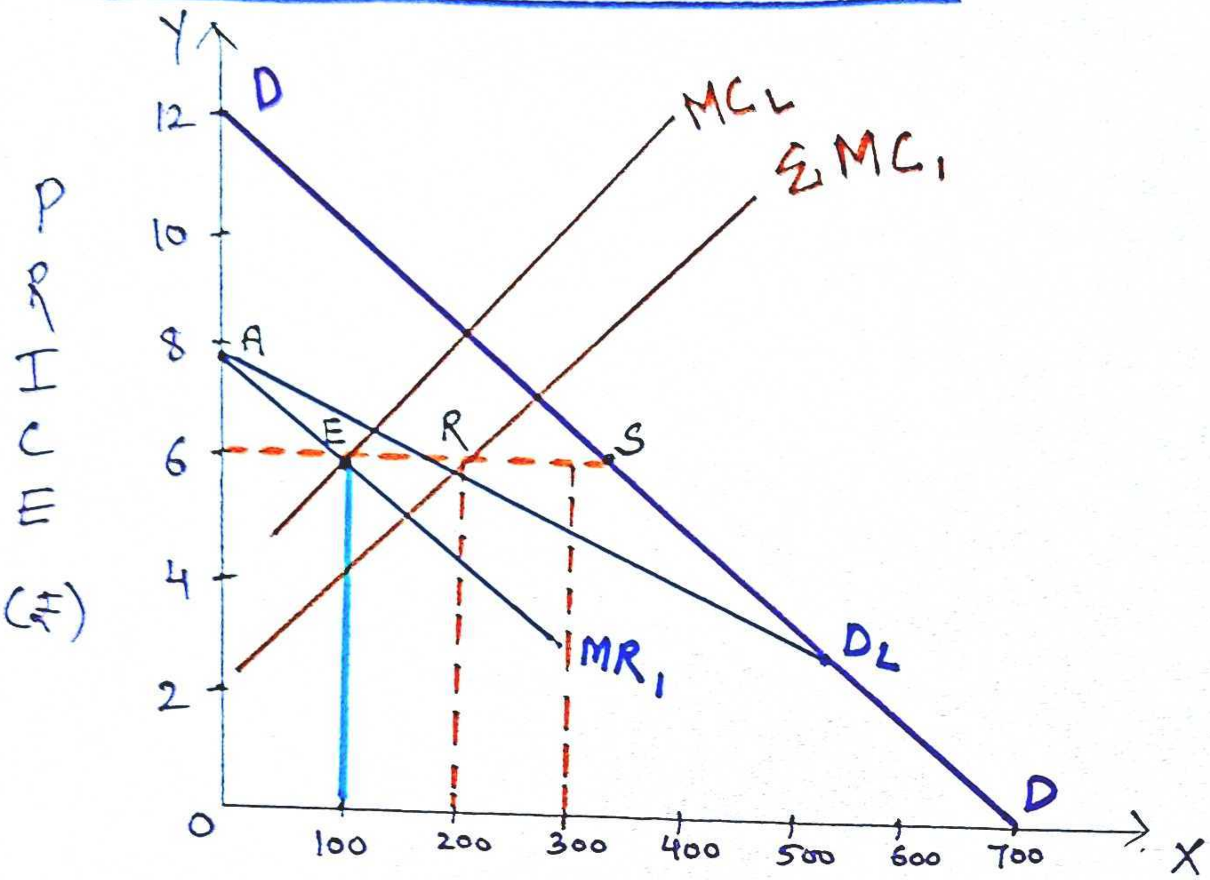
The Dominant firms have great influence over the market. But the small firms have to accept the decisions of Dominant firms. The Dominant firms, decide its own Demand Curve and fixes the Price of Product which bring maximum profit.

② **Barometric Price Leadership :-** Here Large, experienced and Respected firm Plays role of Price Leadership.
The Leader firm brings changes in Price and other firms Follow him willingly. He takes the decision regarding market conditions, Cost of Production, Competition etc.

③ **Aggressive Price Leadership :-** A Large and dominant become Leader of Oligopoly market due to its Aggressive Price Policies. It compels other firms to accept its Price Policy. The Followers has to Follow the decision of Price Leader.

④ **Low Cost Firm Leadership :-** An Oligopoly firm which enjoys the benefits of Low Cost of Production decide the Low Price for the Product. The High Cost firms Will not be able to sell their Products at higher Price. So they are forced to sell their goods at Low Price. shown in Following diagram——

Low Cost Price Leadership



In above diagram we Observe —

1) DD is the market demand curve for the Product.
2) D_L is the demand Curve of Leader firm whose have Less Cost of Production.
3) MR_L is Revenue Curve of Leader firm and MC_L is Marginal Cost Curve of Leader Firm. where Leader Enjoys Equilibrium at Low Cost ₹ 6

$MR_L = MC_L$ = ₹ 6 = 100 units

4) ΣMC_1 is the marginal Cost curve of Followers.

MC_1 = R Price = 200 units.

5) Thus Total out Put sold in Oligopoly market = 300 units
100 units are sold by Leader and
200 units are sold by followers at ₹ 6.

(c) Limitations of Price Leadership :-

1. **Product Differentiation :-** If the Oligopoly is selling differentiated Product, the Leadership will become difficult. Each Firm incur huge amount on advertisemen to attract Customer.

2. **Non- Price Competition :-** The Followers may follow the Price Set by Leader but they may follow non-Price Competition tactics. Firms Provide secret discounts, Commissions, additional Facilities to Retailers and Customers.

3. **Difference in Cost of Production :-** A Producer, Produce goods and Services at Low Cost become Leader of market. If Followers have Lower Cost than a dominant Leader firm, it become difficult to be Leader of market.