Who Sets the Price?

Read and compare four kinds of markets

E.3.2 "Compare and contrast the basic characteristics of the four market structures: monopoly, oligopoly, monopolistic competition, and pure competition."

NAME _____ DATE _____

1 READ AND MARK

Read it twice

YOUR JOB Underline clues about the number of sellers, circle clues about whether products are alike or different, and write 1 beside clues about entry barriers and 2 beside clues about pricing power.

Four Markets in One Town

1. Picture four markets serving the same town. In a monopoly, one seller supplies a product with no close substitute. The town's water utility may be the only provider of piped water because building a second pipe network would be costly. Customers cannot switch to another piped-water seller, so the utility has substantial pricing power, although regulations can limit its rates. An oligopoly has a few major sellers. On a regional air route, a small number of airlines may compete. Each watches the others' fares because a price cut by one can prompt a response from its rivals.

2. Now picture a street with many coffee shops. In monopolistic competition, many sellers offer products that are similar but not identical. One shop might feature quiet study tables, while another offers unusual flavors. Customers can choose among substitutes, yet a shop may charge a little more if customers prefer its version. New shops can generally enter, though opening one still takes money. Pure competition is different: many sellers offer an identical product, and entry is relatively easy. A wheat farmer selling a standard grade of wheat cannot usually set a higher price than the market price, since buyers can turn to other farmers.

3. Compare the markets by asking three questions: How many sellers are there, how different are their products, and how hard is it for a new seller to enter? The water utility and airlines face stronger barriers to entry than the coffee shops and wheat farmers. Yet the utility faces no rival piped-water seller, while airlines must consider one another's decisions. Coffee shops and wheat farmers both face many rivals, but coffee shops can stand out through differences that buyers value. Wheat farmers selling the same grade have less control over price. These patterns describe market structures, not guarantees about any seller's profits.

2 ANSWER WITH EVIDENCE

Use the passage

1. How do a monopoly and an oligopoly differ in the number of sellers and the need to respond to rivals?

2. Compare oligopoly and monopolistic competition in the number of sellers and the difficulty of entering the market.

3. Both monopolistic competition and pure competition have many sellers. How do their products and sellers' pricing power differ?

4. Which has more pricing power, a monopoly or a seller in pure competition? Use a condition in each market to explain your comparison.

3 YOUR TURN

Your own words

Invent a product and describe two versions of its market that fit two different market structures. For each version, name the structure and explain the number of sellers, product differences, and ease of entry; then compare the sellers' pricing power.

Who Sets the Price?

PART 1 · READ AND MARK

Underline clues about the number of sellers, circle clues about whether products are alike or different, and write 1 beside clues about entry barriers and 2 beside clues about pricing power. Accept any marking that follows this job and points at the right text.

PART 2 · ANSWERS

#	QUESTION	ANSWER
1	How do a monopoly and an oligopoly differ in the number of sellers and the need to respond to rivals?	**A monopoly has one seller with no direct rival, while an oligopoly has a few major sellers that watch and respond to one another.**
2	Compare oligopoly and monopolistic competition in the number of sellers and the difficulty of entering the market.	**An oligopoly has a few major sellers and stronger entry barriers. Monopolistic competition has many sellers, and new firms can generally enter more easily.**
3	Both monopolistic competition and pure competition have many sellers. How do their products and sellers' pricing power differ?	**In monopolistic competition, products differ, so a preferred seller may charge a little more. In pure competition, products are identical, so sellers have little control over the market price.**
4	Which has more pricing power, a monopoly or a seller in pure competition? Use a condition in each market to explain your comparison.	**A monopoly has more pricing power because customers cannot switch to another seller of a close substitute, although regulation may limit rates. A seller in pure competition has little pricing power because buyers can choose among many sellers of the same product.**

PART 3 · YOUR TURN (SAMPLE ANSWER)

Imagine a market for insulated lunch containers. At first, three large firms sell containers with different designs, and costly factories make entry difficult, so this is an oligopoly. Each firm has some pricing power but must watch the other two. Later, many small sellers offer distinctive colors and features, and new firms can enter more easily, so this is monopolistic competition. Sellers can still charge a bit more for a preferred design, but they face many alternatives.

Accept invented products and market conditions that consistently fit the two named structures. Pricing comparisons should follow from the stated number of sellers, product differences, and entry conditions.