

Perfect Competition Handout

Market structure refers to all characteristics of a market that influence the behavior of buyers and sellers when they come together to trade.

The keys factors in defining a market structure are:

- a. short run and long run objectives of buyers and sellers in the market
- b. beliefs of buyers and sellers about the ability of themselves and others to set prices
- c. degree of product differentiation
- d. technologies employed by agents in the market
- e. amount of information available to agents about the good and about each other
- f. degree of coordination or noncooperation agents may exhibit
- g. extent of entry and exit barriers.

A buyer or seller (agent) is said to be competitive if the agent assumes or believes that the market price is given and that the agent's actions do not influence the market price. We sometimes say that a competitive agent is a price taker.

Assumptions of Perfect Competition

1. Buyers and sellers are competitive. In other words buyers and sellers are **price takers**.
2. All firms produce **homogeneous (standardized) goods** and consumers view them as identical.
3. All buyers and sellers have **perfect information** regarding the price and quality of the product.
4. Firms can enter and exit the industry quickly at any time without having to incur special expenses. Thus firms have **freedom of entry and exit**.
5. There are **no transaction costs** to participate in the market.
6. Each firm bears the full cost of its production process. That is, there are **no externalities** that the firm imposes on others. An externality is a by-product of a good or service that affects someone not immediately involved in the transaction.
7. There is **perfect divisibility of output**.

Comparative analysis of ten markets

Consider the twelve markets listed below. To what extent do they satisfy the conditions for perfect competition. In each case give reasons for your conclusion.

1. Market for fresh vegetables in Madison, WI
2. Market for seed corn in Iowa
3. Market for delivered pizza in Ames, IA
4. Market for baseball players
5. Market for unskilled farm labor in California
6. World market for wheat
7. Secondary market for treasury bills (3-month)
8. Market for combines in the United States
9. Market for sport utility vehicles
10. Market for live cattle in western Iowa
11. Market for running shoes
12. Market for gasoline in Waverly, IA

y	FC	VC	C	AFC	AVC	ATC	MC	Demand/Price	TR	MR	Profit
0.00	200	0.00	200.00					184	0		-200.00
							64.00			184.00	
1.00	200	64.00	264.00	200.00	64.00	264.00		184	184	184.00	-80.00
							66.00				
2.00	200	130.00	330.00	100.00	65.00	165.00		184	368	184.00	38.00
							74.00				
3.00	200	204.00	404.00	66.67	68.00	134.67		184	552	184.00	148.00
							88.00				
4.00	200	292.00	492.00	50.00	73.00	123.00		184	736	184.00	244.00
							108.00				
5.00	200	400.00	600.00	40.00	80.00	120.00		184	920	184.00	320.00
							134.00				
6.00	200	534.00	734.00	33.33	89.00	122.33		184	1104	184.00	370.00
							166.00				
7.00	200	700.00	900.00	28.57	100.00	128.57		184	1288	184.00	388.00
							204.00				
8.00	200	904.00	1104.00	25.00	113.00	138.00		184	1472	184.00	368.00
							248.00				
9.00	200	1152.00	1352.00	22.22	128.00	150.22		184	1656	184.00	304.00
							298.00				
10.00	200	1450.00	1650.00	20.00	145.00	165.00		184	1840	184.00	190.00
							354.00				
11.00	200	1804.00	2004.00	18.18	164.00	182.18		184	2024	184.00	20.00
							416.00				
12.00	200	2220.00	2420.00	16.67	185.00	201.67		184	2208	184.00	-212.00
							521.00				
14.00	200	3262.00	3462.00	14.29	233.00	247.29		184	2576	184.00	-886.00
							681.00				
16.00	200	4624.00	4824.00	12.50	289.00	301.50		184	2944	184.00	-1880.00

y	FC	VC	C	AFC	AVC	ATC	MC	Demand/Price	TR	MR	Profit
0.00	200	0.00	200.00					97	0		-200.00
							64.00			97.00	
1.00	200	64.00	264.00	200.00	64.00	264.00		97	97	97.00	-167.00
							66.00				
2.00	200	130.00	330.00	100.00	65.00	165.00		97	194	97.00	-136.00
							74.00				
3.00	200	204.00	404.00	66.67	68.00	134.67		97	291	97.00	-113.00
							88.00				
4.00	200	292.00	492.00	50.00	73.00	123.00		97	388	97.00	-104.00
							108.00				
5.00	200	400.00	600.00	40.00	80.00	120.00		97	485	97.00	-115.00
							134.00				
6.00	200	534.00	734.00	33.33	89.00	122.33		97	582	97.00	-152.00
							166.00				
7.00	200	700.00	900.00	28.57	100.00	128.57		97	679	97.00	-221.00
							204.00				
8.00	200	904.00	1104.00	25.00	113.00	138.00		97	776	97.00	-328.00
							248.00				
9.00	200	1152.00	1352.00	22.22	128.00	150.22		97	873	97.00	-479.00
							298.00				
10.00	200	1450.00	1650.00	20.00	145.00	165.00		97	970	97.00	-680.00
							354.00				
11.00	200	1804.00	2004.00	18.18	164.00	182.18		97	1067	97.00	-937.00
							416.00				
12.00	200	2220.00	2420.00	16.67	185.00	201.67		97	1164	97.00	-1256.00
							521.00				
14.00	200	3262.00	3462.00	14.29	233.00	247.29		97	1358	97.00	-2104.00
							681.00				
16.00	200	4624.00	4824.00	12.50	289.00	301.50		97	1552	97.00	-3272.00