What is a “Market”?

- In modern usage, a **commodity** is anything of use that is available for purchase and sale in standardized form.

  **Examples**: Haircut (service), Compaq Presario 6000 PC (physical asset), Australian dollar (financial asset), cell phone minutes, bandwidth

- A **market** is any context in which trading (buying and selling) of a commodity takes place
Important Aspects of Markets

- **Key Types of Market Participants and Forms**
  - **Participants:** Who trades with whom? [e.g. business-to-business (B2B) transactions, business-to-consumer (B2C) transactions, etc.]
  - **Forms:** In what types of market structures does this trading take place? [e.g. double auctions, single-sided auctions, exchanges, bilateral trades, etc.]

- **Learning Behavior and Strategic Interaction**
  - Price/quantity discovery *processes*
  - *Formation* of buyer-seller interaction networks
Possible Market Forms?

Bean Producers

Producer-Consumer Connections??

Hash Producers

Consumers
Possible Market Forms?

- Two basic forms of market trading:
  - 1. **Bilateral** trading (Seller ↔ Buyer)
  - 2. **Mediated** trading
    (Seller ↔ Mediator ↔ Buyer)
Example 1: Bilateral B2B & B2C Trade
(B2B=Business To Business, B2C=Business To Consumer)

Bean Producers  Container Producers  Hash Producers

B1  B3  H2  H1  H3  H4

B2B

B2C

Consumers
Example 2: Combination of Bilateral and Mediated B2C Trades

Bean Producers

Retail Bean Stores

Large Consumers

Small Consumers

Retail Hash Stores

B2C Bilateral Trades

Hash Producers
Key Types of Market Mediators

- **Broker**
  - Facilitates trade by matching buyers with sellers
  - Does not take a position in the assets he/she trades (i.e., does not maintain an inventory of the assets)
  - Earns profits through commissions charged to buyer/seller
  - **Examples**: Stock broker; Real estate broker

- **Dealer**
  - Facilitates trade by matching buyers with sellers
  - Takes position in assets traded (“makes the market”)
  - Earns profits by *buying low* and *selling high*
  - **Examples**: Bond dealer; Car dealer; Retail store owner; “Load-Serving Entities” (LSEs) in competitive retail markets that can set their own contract terms.
Key Types of Mediated Market Forms

- **Auction markets**
  - Centralized facility (clearing house) managed by brokers
  - **Examples:** Day-ahead energy markets, art auctions, U.S. Treasury bill auctions, etc.

- **Over-the-Counter (OTC)**
  - Decentralized facility managed by dealers
  - **Examples:** NASDAQ stock market, gov’t bond market

- **Exchanges (Hybrid of Auction and OTC)**
  - Centralized facility conducted through specialized broker/dealer intermediaries
  - **Examples:** Retail stores, NYSE EuroNext, Electric power exchanges for financial energy contracts
Learning Behavior & Strategic Interaction in Markets

- **Price/Quantity Discovery**
  - *For sellers*, seeking to determine the most profitable amount to produce and/or the most profitable price to charge per unit in order to compete for business against rival sellers
  - *For buyers*, seeking to determine what items are available for purchase and which sellers are willing to accept the lowest prices for the items they wish to purchase

- **Buyer-Seller Interaction (Relational Goods)**
  - How to behave in longer-term relationships (e.g., job situations, servicing contracts, loan contracts, repeat purchases from same supplier, etc.)
  - Trust, honesty, punctuality, etc.
Key Types of Procurement Processes that Must Be Carried Out in Markets

- **Terms of Trade**: Set production and price levels
- **Seller-Buyer Matching**:
  - Identify potential suppliers/customers
  - Compare/evaluate opportunities
  - Make demand bids/supply offers
  - Select specific suppliers/customers
  - Negotiate supplier/customer contracts
- **Trade**: Transactions carried out
- **Settlement**: Payment processing and shake-out
- **Manage**: Long-term supplier/customer relations