LECTURE NOTES ON MANAGERIAL ECONOMICS FOR STUDENTS ACADEMIC USE BY-_DR.NEHA MATHUR

Perfect Competition:
Perfect competition refers to a market situation in which there are large number of buyers and sellers of homogeneous products.

The price of the product is determined by industry with the forces of demand and supply. For instance, if you require pen, there should be several shops selling pens.

Under conditions of perfect competition, every seller should be selling the same quality of pens at the uniform prevailing price in the market. You may buy a pen from any shop at price Rs. 10. If another shopkeeper charges Rs. 12 for same quality of pen, nobody will buy from him. But if a shopkeeper charges Rs. 9 all will buy pens from that particular shop. But, both these situations are unrealistic.

There must be one price prevailing throughout the market. Thus, perfect competition in a market structure is characterized by the complete absence of rivalry among individual firms.

Definitions:

"Perfectly competitive market is a situation where large number of buyers and sellers are engaged in the purchase and sale of identically similar commodities, who are in close contact with one another and who buy and sell freely among themselves." -Boulding

"The perfect competition is characterized by the presence of many firms; they all sell identically the same product. The seller is a price- taker." -Bilas

"Perfect competition prevails when the demand for the output of each producer is perfectly elastic." -Mrs. Joan Robinson

"Perfect competition is a market situation where there is large number of sellers and buyers, a homogeneous product, free entry of firms into the industry perfect knowledge among buyers and sellers of existing market

conditions and free mobility of factors of production among alternative uses."
-Lim Chong Yah

"Perfect competition describes a market in which there is complete absence of direct competition among economic groups'. -Ferguson

Assumptions:

A perfectly competitive market has following assumptions:

1. Large Number of Buyers and Sellers:

It means no single buyer or seller can affect the price. If a firm enters into the market or exit the market, there will be no effect on the supply. Similarly if a buyer enters into the market or exit from the market, demand will not be affected. Thus no individual buyer or seller can affect the price.

2. Homogeneous Products:

The second assumption of perfect competition is that all sellers sell homogeneous product. In such a situation, the buyers have no reason to prefer the product of one seller to another. This condition is present only when the commodity is a substance of definite chemical and physical composition i.e., salt, tin, specified grade of wheat etc.

3. No Discrimination:

Under perfectly competitive market, buyers and sellers must buy and sell freely among themselves. It implies that buyers and sellers must be willing to deal openly with one another to buy and sell at the market price. This may be true of one and all that may wish to do so without offering any special deals, discounts, or favours to selected individuals.

4. Perfect Knowledge:

A competitive market is (me in which the buyers and sellers are in close contact with each other. It means that, there is perfect knowledge of the market on the part of buyers and sellers. It implies that a large number of buyers and sellers in the market exactly know how much is the price of the commodity in different parts of the market.

In other words, there must be knowledge on the part of each buyer and seller of the prices at which transactions are being carried on, and of the prices at which other buyers and sellers are willing to buy or sell.

5. Free Entry or Exit of Firms:
In the long run, under perfect competition, firm can enter into or exit from the industry. There is no let or hindrance on firms as far as their entry into or exit from the market. In other words, there are no legal or social restrictions on the firm. Large number of sellers can be possible only if there is free entry of firms.

6. Perfect Mobility:
There must be perfect mobility of factors of production within the country which ensures uniform cost of production in the whole economy. It implies that different factors of production are free to seek employment in any industry that they may like.

7. Profit Maximization:
Under perfect competition, all firms have a common goal of profit maximization. Thus, there is absence of social welfare of the general masses.

8. No Selling Cost:
Under perfect competition, there are no selling costs.

9. No Transport Costs:
There shall not be any cost of transport between sellers. If transport costs exist buyers are prevented from moving from one seller to another to take advantage of price difference. This means that transport cost has no influence on the pricing of a product. In other words, these are always uniform price in the market.

Pure and Perfect Competition:
Many economists choose to use the term "Perfect Competition" rather than "Pure Competition." For instance, the American economists are particularly fond of using the term pure competition in preference to the term perfect competition, while the term perfect competition seems to be popular with the British economists.

However, Prof. Chamberlin made a distinction between perfect competition and pure competition.

According to Prof. Chamberlin pure competition includes:
(i) Large number of buyers and sellers,

(ii) Homogeneous products,

(iii) Free entry or exit of firms,

(iv) Free from checks,

(v) Lack of selling cost, and

(vi) Lack of transport costs.

Prof. R.A. Bilas also distinguished Perfect and Pure Competition as, “Perfect Competition implies pure competition but also considers other characteristics. Pure competition implies one degree of perfection-the complete absence of monopoly.

Generally, perfect competition will introduce the notion of perfect resource mobility and perfect knowledge.” Similarly, Prof. Baumol defined pure competition as an industry. It is said to be operating under pure competition when there are many firms, homogeneity of products, freedom of entry & exit, independent decision making.”

On the basis of these definitions, it can be said that pure competition is said to exist when element of monopoly is absent from the market. The Perfect Competition is a broader term than pure competition which involves absence of monopoly as well as perfection in many other respects, such as, perfect mobility of factors of production and perfect knowledge of the market. Therefore, producers have a perfect knowledge of the quantity and quality of available factors of production as well as the prices which can be charged for its product.

Thus, the distinction between pure and perfect competition is merely of degree, while every assumption of pure competition is also an assumption of perfect competition The concept of a perfectly competitive system includes one further assumption, viz., that there is perfect knowledge by both buyers and sellers of prevailing market prices, and the different range and quality of various goods, services and factors of production.