MANAGERIAL ECONOMICS

Prof. Trupti Mishra
Shailesh J. Mehta School of Management,
IIT Bombay

Lecture No - **34 : Game Theory**

Session Outline

Collusive models of oligopoly
Game Theory

Price leadership

- In this form one firm sets price and other firms follow it because it is advantageous to them or because they prefer to avoid uncertainty.
- If the product is homogenous and if there are no transport costs, the same price will be charged by all firms.
- However if the product is differentiated , prices will differ but the direction of their change will be the same and the same price differential will be more or less maintained.

Price leadership

Types

- Price leadership by a low cost firm
- Price leadership by a large (Dominant firm)
- Barometric Price leadership

Price leadership

- Price leadership by a low cost firm
- Price is set by the low cost firm.

Price leadership

- ***Price-leadership*** is a form of oligopoly in which one dominant firm sets prices and all the smaller firms in the industry follow its pricing policy.

Price leadership

- Price leadership by a dominant firm
- Oligopoly market is dominated by few firms among which one may be the largest player.
- Example : Google, Intel, Nokia, IBM, Maruti, Godrej etc.
- The other firms acknowledge the leadership of the largest firm for price determination.

Price leadership

- Price leadership by a dominant firm
- A dominant firm is a leader in term of market share or presence in all segments, or just being the pioneer in particular product category.
- Leader is very large in size and earns economies of scale, produces optimum output at which it is able to maximize returns.

Price leadership

- Price leadership by a dominant firm
- This dominant firm may be either a **benevolent** or an **exploitative firms**.
- A benevolent firm allows other firm to exist by fixing a price at which small firms may also sell.

Price leadership

- Price leadership by a dominant firm
- Creation of Benevolent Firm:

- It lets other exist so that it does not have to face allegation of monopoly creation.
- It earns sufficient margin at this price an still retains market leadership.
- Success of this type of leadership depends on the assumptions that others will follow the leader.

Price leadership

- Price leadership by a dominant firm
- An exploitative leader fixes a price at which small inefficient players may not survive and thus it gains a large share of the market.

Price leadership

- Price leadership by Barometric firm
- Some markets may be such that no single player is so large to emerge as leader, but there may be one firm which has better understanding of the markets.
- This firm acts like a barometer for the market.
- A barometric has better industry intelligence and can preempt and interpret its external environment in an effective manner.

Session References

Micro Economics :ICFAI University Press
Managerial economics – Geetika, Ghosh and Choudhury
Managerial Economics – D N Dwivedi
Managerial Economics – Dr Atamanand