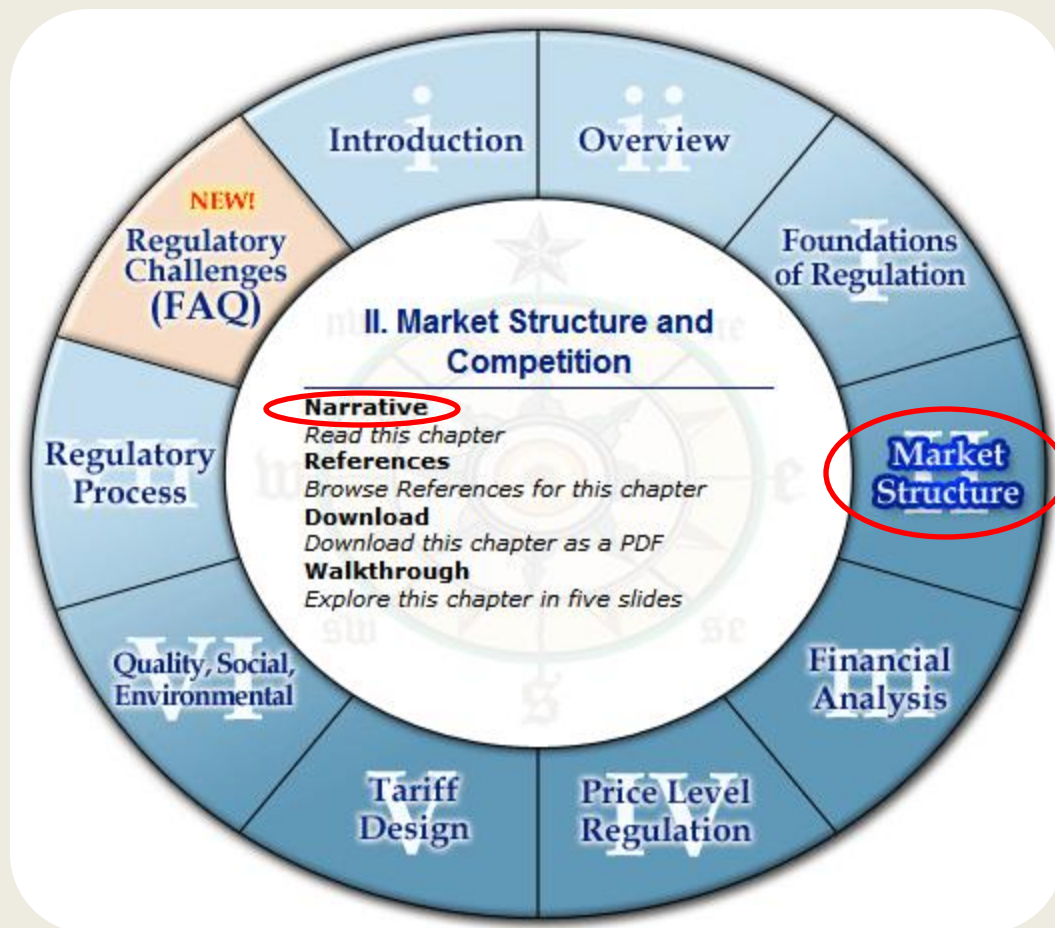


Market Structure and Competition

The Body of Knowledge on Infrastructure Regulation is divided into seven main sections. Chapter II is dedicated to issues dealing with **market structure and competition**.



Market structure refers to the number of firms involved in supplying a market and the relationships among those firms.

One of the basic problems addressed by regulation is the control of market power and the asymmetry between the government and operator with respect to objectives and information.

What happens when we subject the operator to competitive pressures?

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The BoKIR first examines Monopoly and Market Power. A monopoly exists when a single provider serves the entire market demand. This section includes definitions of important concepts such as natural monopoly, economies of scale and economies of scope, while also describing the tools that regulators have available for detecting market power.

Next, Competition in Utility Markets is examined. Regulators and policy makers implement competition in the utility market by removing legal and technical barriers to entry, monitoring anticompetitive conduct, restructuring the sector, and providing access to essential facilities. Legal barriers to entry include licenses restrictions and high license fees that sometimes limit the number of firms that can serve a market. Technical barriers to entry include sunk costs and other barriers to entry.

Then Competition for the Market is examined. When elements of the utility system exhibit natural monopoly characteristics, customers can still gain some benefits of competition through effective use of competition for the market. In these situations, the government often auctions off the right to be a monopoly. Doing so can improve the efficiency of the utility services. This section describes these auctions, touching over important subjects such as concessions.

Overall Conclusions

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Facilitating competition is one regulatory instrument for overcoming market power and asymmetries in objectives and information.

Competition in the market is generally the preferred form of competition, but competition for the market is often effective if competition in the market is infeasible or impractical because of natural monopoly. Generally if competition in the market is the policy choice, the regulator has an ongoing role of regulating access to essential facilities, ensuring that barriers to entry do not interfere with competitive dynamics, and monitoring the effectiveness of the competition. If one or more of the firms have significant market power, then regulators may use price cap regulation to control the residual market power until competition develops more fully.

Competition for the market involves having operators bid for the right to be the monopoly provider of the service. Because the future is uncertain, ongoing regulation of prices and renegotiation of the concession contract are common. Frequent rebidding of the concession may be an option for reducing the need for ongoing regulation and for renegotiation.

References

The principal resource featured in the BoKIR is the list of (and access to) references that is provided under each section. The literature includes decisions and publications by regulatory agencies and other governmental bodies; policy advisories by think tanks, consultants, donor agencies, etc.; and research by academics, consultants, and other experts.

In the Market Structure and Competition section, references are organized under the following categories:

- Monopoly and Market Power
 - Case Studies
 - Factors leading to monopoly
 - Pricing under monopoly – efficiency aspects and cost recovery
 - Basic economics of network industries
 - Definition and measurement of market power
- Competition in Infrastructure Markets
 - Case Studies
 - Approaches to competition
 - Competition for existing consumers vs. competition for new customers
 - Main forms of market and transaction organization
 - Transition aspects to introducing competition
 - Vertical separation and service unbundling
 - Access pricing and regulation of access to bottleneck facilities
 - Application of competition rules and antitrust principles in regulation
- Competition for the Market
 - Case Studies
 - General concepts and efficiency impacts
 - Basic auction theory
 - Practical applications of competition for the market
 - Termination, renewal, rebidding and renegotiation
 - Regulatory oversight of competitive procurement
 - Negotiating bids

Further divided into:

- Core References
- Sectoral References
- Other References

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Self Testing: Test your command of the BoKIR content for each section. Answers are provided with an explanation and with references for further study.

Which of the following is **false**?

- Micro-management by politically-motivated government officials sometimes led state-owned operators to have excessive numbers of employees and provide service primarily to politically powerful groups.
- Some state-owned operators have needed government subsidies to finance investments and cover other costs.
- Recent technological changes have increased the gains to vertical integration in electricity generation and telephony, which strengthens the argument for maintaining vertically integrated monopolies in these sectors.
- Some analysts argue that privately owned firms may operate more efficiently than state-owned enterprises because profit motives provide clear and consistent incentives to control costs.

Glossary: Keywords throughout the text are hyperlinked to a glossary for complete definitions (also available in other languages).

Market Power: The ability of a company to raise prices above the competitive level for a non-transitory time period. Generally, such power is based on absence of close product *substitutes*, a low degree of competitive rivalry, or the presence of entry barriers.