

Market Organization: Slides

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What is a “Market”?

- ❑ An **asset** is anything of durable value, whether physical or financial
Examples: Apple, computer, battery-stored energy, insurance contract, loan contract, ...
- ❑ A **service** is an action taken by an entity that provides benefit to another entity.
Examples: Haircut, health-care, labor, ...
- ❑ A **market** is any context in which trading (buying and selling) of an asset or service takes place

Important Aspects of Markets

- **Key Types of Market Participants and Forms**
 - **Participants:** Who trades with whom?
Examples: Business-to-business (B2B) transactions, business-to-consumer (B2C) transactions, ...
 - **Forms:** In what types of market structures does this trading take place?
Examples: Double auctions, single-sided auctions, bid-offer exchanges, bilateral trades, ...

- **Learning Behavior and Strategic Interaction**
 - **Processes** for price/quantity discovery
 - **Formation** of buyer-seller interaction networks

Possible Market Forms?

B1

B3

B2

Bean Producers

H1

H2

H3

H4

Hash Producers

Producer-Consumer
Connections??

Consumers

Possible Market Forms ... ?

□ Two basic forms of market trading:

- **Bilateral Trading**

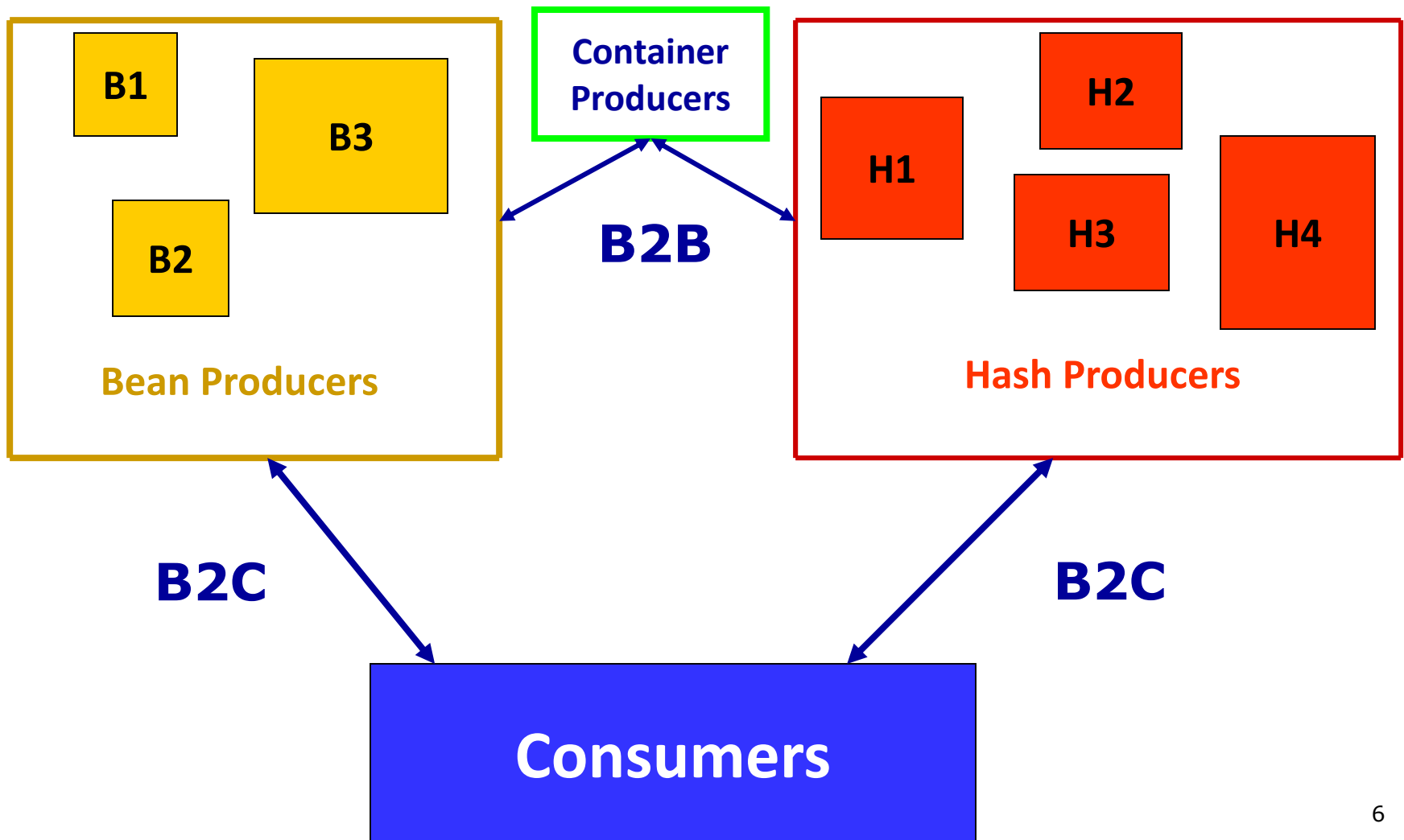
(Seller ↔ Buyer)

- **Mediated Trading**

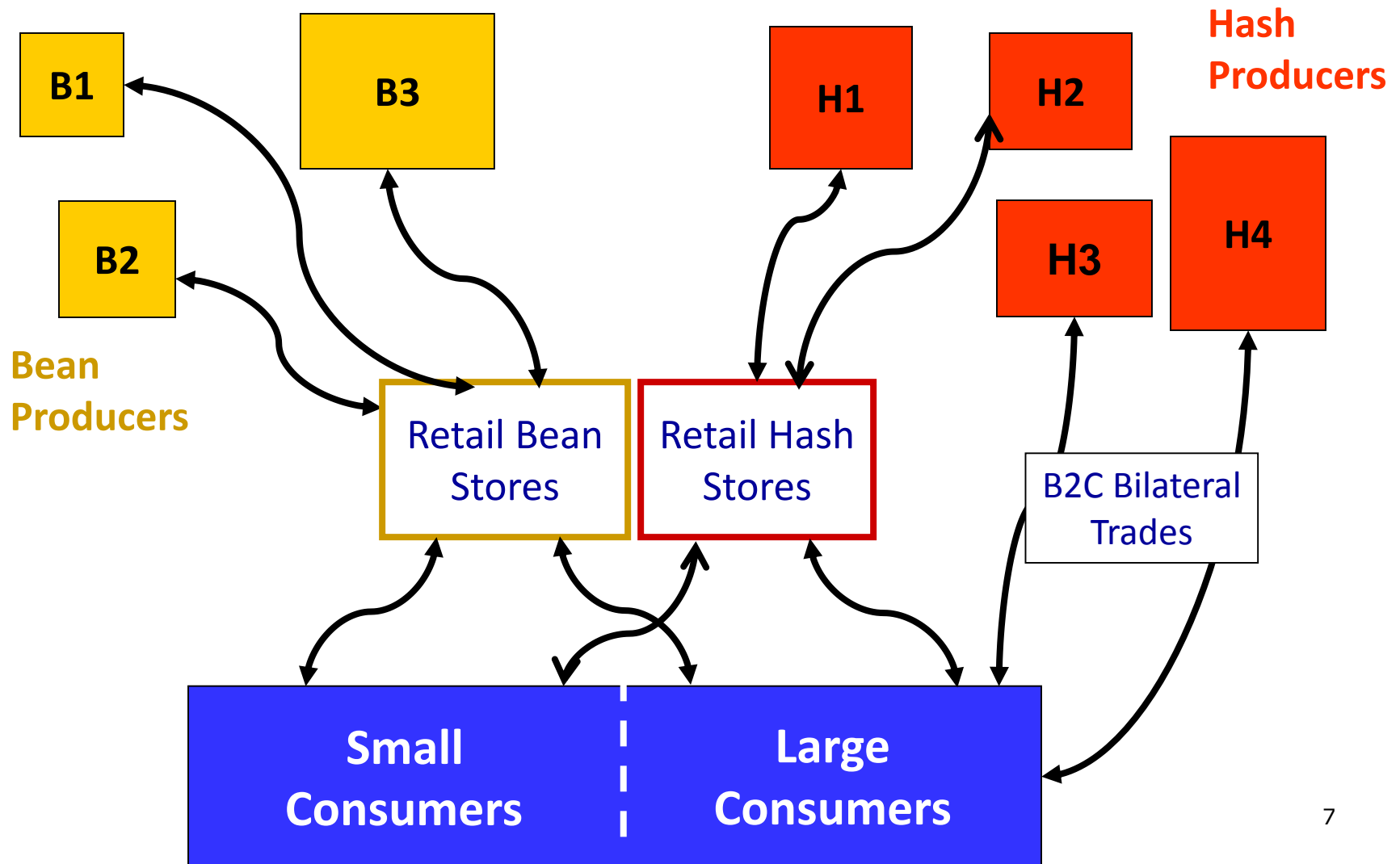
(Seller ↔ Mediator ↔ Buyer)

Example 1: Bilateral B2B & B2C Trade

B2B = Business To Business, B2C = Business To Consumer



Example 2: Combination of Bilateral and Mediated B2C Trades



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: Stockbroker; 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; ...

❑ 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