**Characteristics of an Oligopoly**

There are 6 main characteristics of an oligopoly. Let us look at these below:

 1. A Few Firms with Large Market Share

A market may have thousands of sellers, but if the top 5 firms have a combined market share of over 50 percent, it can be classified as an oligopolistic market. This is because the power is concentrated between a few sellers who are able to exercise power over the market.

2. High Barriers to Entry

Oligopolistic firms maintain their position through a number of [**barriers to entry**](https://boycewire.com/barriers-to-entry). For instance, brand loyalty, patents, and high start-up costs are but to name a few. These make it difficult for new entrants to build a presence in the market and attract customers. In industries such as retail – brand loyalty is a significant barrier to overcome.

These barriers to entry make it difficult for new firms to join and sets it apart from [**perfect competition**](https://boycewire.com/perfect-competition-definition/). As a result, these barriers to entry allow oligopolies to make higher profits due to limited competition.

3. Interdependence

Any action a firm takes in an oligopolistic market will strongly affect the actions of its competitors. As a result, we have what is often referred to as the ‘Prisoners Dilemma’, under Game Theory. For those who are not familiar with these terms: an oligopolistic firm will operate based on how they believe competitors will react. In other words, Company A expects Company X to reduce its prices, so will do so as well.

This can be sub-optimal as it reduces the power of a competitive market. For example, if Apple was to reduce the price of its iPhone by $200, Samsung would likely follow suit. So when Apple looks to take that decision, they will consider how they will benefit. They won’t receive a boost in demand because the competition is also the same price, so any initial benefit is lost. Often this can lead oligopolistic firms to just maintain the status quo and keep prices constant.

 4. Each Firm Has Little Market Power In Its Own Right

Leading on from interdependence; each firm has little market power, because other firms are quick to take advantage. For example, an oligopolistic firm cannot raise prices in fear that customers will flee to its competitors. One oligopolistic firm cannot dictate prices or supply because competitors are equally as ‘powerful’. On an individual basis, this keeps the firm in check. Yet it equally incentivises collusion as one firm is unable to get ahead.

### 5. Higher Prices than Perfect Competition

Under perfect competition, prices are just above [**marginal cost**](https://boycewire.com/marginal-cost-definition), leaving firms with small profits – if any. As oligopolies have combined market power, they tend to keep prices higher to obtain larger profits.

If any firms were to reduce prices, others would also follow suit, thereby reducing profits for all. This is where it becomes tricky in distinguishing between collusion and a natural state of oligopolistic competition. Do firms naturally keep prices higher due to fear that their actions will reduce their profits? Or, do they collude to keep prices and profits high?

### 6. More Efficient

Oligopolistic firms benefit from high levels of market share. At the same time, they benefit from [**economies of scale**](https://boycewire.com/economies-of-scale) – meaning it can produce at a lower cost. For instance, there are markets that have high [**fixed costs**](https://boycewire.com/fixed-cost-definition) such as car manufacturers. If new competitors want to enter, they have to spend millions on new factories and other infrastructure.

Consequently, this would increase costs for exisiting firms as the benefit they receive from economies of scale would decline. This means higher prices for customers and it is for this reason that such markets are better served under an oligopolistic market structure.