

What Makes a Market an Oligopoly?

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By [Heather Hennerich](#)

Do you know of any industries in which just three or four companies supply most of a specific product?

Some examples:

- From the 1950s to the 1980s, three major broadcast television networks dominated the U.S. airwaves.
- After a series of mergers between 2005 and 2015, four major airlines controlled much of the U.S. market, as a [November 2018 Page One Economics essay](#) described.
- Even more recently, shortages and price increases brought attention to the U.S. baby formula market and global insulin market, which also had just a few suppliers.

Those markets could be considered “oligopolies”—markets in which only a few sellers or suppliers dominate.

Suppliers and sellers in an oligopoly [can command higher prices](#) than companies in a competitive market, and if one company in an oligopoly stops producing, it has a bigger effect on supply than it would in a competitive market.

Read on for more comparisons of oligopolies to other types of markets and to learn how to tell whether a particular market could be considered an oligopoly.

Four Market Structures

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|---------------------------------|---|
| Monopoly | A market for a good or service in which there is only one supplier, or that is dominated by one supplier. Barriers prevent entry to the market, and there are no close substitutes for the product. |
| Oligopoly | A market in which a few large firms dominate. Barriers prevent entry to the market, and there are few close substitutes for the product. |
| Monopolistic competition | A market structure where many firms produce similar but not identical products. |
| Perfect competition | A market in which there are many buyers and many sellers of an identical product. |

SOURCES: The St. Louis Fed Economic Education Department’s PowerPoint presentation “[Teaching Market Structures with a Competitive Gum Market](#)” and [Glossary of Economics and Personal Finance Terms](#).

What Is an Oligopoly?

As the table shows, in addition to having only a few sellers or suppliers dominating the market, an oligopoly has barriers to entering the market, and “there are few close substitutes for the product.”

In other words, certain conditions make it difficult for potential competitors to start selling or supplying a particular product or service within that industry, and there aren't many alternatives that could be used instead. Monopolies—markets in which one firm dominates—also have those barriers.

“Barriers to entry” could include factors such as costly equipment needed to produce a product, patents restricting who can use an invention, and government regulations that are difficult to meet, as a [Corporate Finance Institute article](#) outlined.

What Are Examples of Barriers to Entry?

In the case of the U.S. infant formula market, barriers to entry have included tariffs and [Food and Drug Administration standards](#). (Some of the infant formula market barriers were waived to help ease the shortage last year.)

Until the expansion of the cable TV market in the 1980s, the limited availability of broadcast frequencies helped to restrict the number of television networks, with the Federal Communications Commission in charge of allocating portions of the broadcast spectrum to stations.

Barriers to entry in the airline industry include high startup costs, such as for purchasing airplanes, competition for airport gates and large economies of scale, the *Page One Economics* essay said.

Government can put up barriers, as a St. Louis Fed Econ Lowdown [lesson on market structures \(PDF\)](#) outlined in discussing monopolistic markets. Such markets are rare, according to the lesson.

“Most commonly, [monopolistic markets] occur because government has granted a single firm the opportunity to supply a good or service. This is known as a ‘natural monopoly,’” according to the lesson, which gives the examples of electric and natural gas providers. Because of the expensive infrastructure needed for those services, such as wires and pipes entering people’s homes, it’s cheaper for one firm to provide the service than to build infrastructure needed for true competition.

“In exchange, government often regulates prices in these markets to ensure that these firms do not take advantage of their market power,” the lesson says.

How Can You Tell If a Market Is an Oligopoly?

A “concentration ratio” is one tool that can indicate whether a market is an oligopoly.

A concentration ratio is the combined market share of the largest firms in an industry, according to [Oxford Reference](#). That is, it’s the percentage of the industry’s products or services provided by those firms.

The number of firms used for the ratio can vary. A “four-firm” ratio is often used as a benchmark to show market structure, according to Oxford. But the ratios also can be calculated using the market share from the eight, five or three largest firms in the market, according to a September 2020 [Investopedia](#) article.

“A rule of thumb is that an oligopoly exists when the top five firms in the market account for more than 60% of total market sales,” the article says. “If the concentration ratio of one company is equal to 100%, this indicates that the industry is a monopoly.”

In 2015, the four major airlines controlled 80% of the U.S. market, the *Page One Economics* essay said. Three manufacturers have more than [90% of the global insulin market](#), according to a July 2022 press release from Grand View Research, a global market research and consulting company. That would make those markets oligopolies, according to the Investopedia rule of thumb.

What Are Two Types of Oligopolistic Markets?

Oligopolistic markets differ, and different types of markets have different effects on prices, as the Econ Lowdown lesson illustrates.



One such market is a **collusive oligopoly**, which has a few sellers who work together “to divide the market, set prices, or limit production,” the lesson says. Companies might, for example, agree to limit production to drive up prices. Such collusion is often illegal.



In a **competitive oligopoly**, the few sellers compete, which keeps the prices lower than they would be in a collusive oligopoly.

In general, more competition results in lower prices for consumers. So, a perfect competition market structure, in which lots of companies provide the same product, would result in lower prices, while a monopoly could mean the highest prices for consumers. Depending on whether they are collusive or competitive, oligopolies can be more like monopolies or more like perfect competition, respectively, as a [Khan Academy video](#) explains.

Can Oligopolies Change?

Market structures aren't necessarily fixed, as the *Page One Economics* essay illustrated with the example of U.S. airlines.

Airline ticket prices declined as low-cost carriers started expanding their routes in 2016, the essay said. A chart from online database FRED shows the [downward trend in airfares](#) before the COVID-19 pandemic.

"The proliferation of low-cost flights in recent years has pushed the airline industry, which was arguably an oligopoly, toward monopolistic competition," the essay said.

About the Author

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