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Structural Change and Economic Dynamics
15 (2004) 119–135

STRUCTURAL CHANGE AND ECONOMIC DYNAMICS

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Niches and economic competition: implications for economic efficiency, growth and diversity

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Received 1 September 2001; received in revised form 1 October 2002; accepted 1 December 2002

Abstract

This article examines the relationship between market niches and economic competition and explores the consequences of niches for economic efficiency, growth and diversity of commodities. Concepts of a niche in everyday use, ecology, economics and business management are compared. Factors giving rise to market niches, some of which are institutional, are identified, and their links with barriers to entry and mobility are discussed. Common negative views about their consequences for competition and economic efficiency are outlined. However, the availability of niches can potentially have a very positive impact on economic growth and development as well as on the diversity of commodities. New measures of global diversity of commodities are introduced. Economic globalisation involves institutional change that reduces the availability of niches and threatens long-term economic growth and diversity of commodities. Niches also provide frictions in economic systems and may have stabilising properties.

JEL classification: F020; L000; O300

Keywords: Diversity of commodities; Entry barriers; Globalisation; Market competition; Niches

1. Introduction

Concepts of niches in relation to market competition and development are used more in the business management literature than in the economic literature. However, niche concepts

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doi:10.1016/S0954-349X(03)00002-X

are basic to much ecology and are widely applied to the analysis of competition between species (inter-specific competition) and less frequently to intra-specific competition (Begon and Mortimer, 1986).

Mainly niche concepts are applied in economics to market competition and the development of markets. In contrast to ecology, they are most widely applied in economics to competition between firms and businesses in the same industry, but sometimes they are also applied to competition between some industries or segments of industries.

Ecologists give greater attention to the availability of niches and their exploitation as a factor in biological evolution and biodiversity compared with the attention given by economists and specialists in business management to the role of market niches in economic growth, development and the diversity of available commodities. However, the creation of market niches via product differentiation is considered by von Mises as one of the most important means of competition, and thereby, of economic development (von Mises, 1961). This view is also apparent in the works of Schumpeter (1954).

Nevertheless, while product differentiation can be important in the competitive market process in creating market niches that give economic power and above-normal profit to their incumbents, they are not sufficient for these latter purposes. This is evident from the theory of monopolistically competitive markets as developed by Chamberlin (Chamberlin, 1933). In such markets, all firms in equilibrium produce slightly differentiated products and only make normal profits because there are no significant barriers to entry. Monopolistically competitive firms are unlikely to be a powerful force for economic development given Schumpeter's point of view (Schumpeter, 1954, Chapter 8). The economic incentive to innovate depends on there being some impediments to rapid use of innovation by entities other than the innovator.

Although Chamberlin (1933) does not specifically mention market niches in his theory of monopolistic competition, nor, unlike Schumpeter (1954), consider dynamic consequences of monopoly, his theory shows strong similarities with a niche-based approach. For example, intra-industry competition occurs but is moderated in the large group monopolistic competition case by businesses occupying market niches. As Chamberlin (1933), p. 81) says "... each producer within the group is a monopolist, yet his market is interwoven with those of his competitors, and he is no longer isolated from them".

While Chamberlin (1933) develops his theory of market equilibrium for competitive large groups of firms by assuming uniformity between firms and the type of sub-markets they occupy, he is at pains to point out that this is only for expositional convenience and that heterogeneity is the rule (Chamberlin, 1933, pp. 81–82). He emphasises that, in practice, the following is more usual:

> "... if high average profits lead new competitors to invade a general field, the markets of different established producers cannot be wrested from them with equal facility. Some will be forced to yield ground, but not by enough to reduce their profits below the minimum necessary to keep them in business. Others may be cut to the minimum, and still others may be forced to drop out because only a small demand exists or can be created for their particular variety of product. Others, protected by a strong prejudice in favour of theirs, may be virtually unaffected by an invasion of the general field—their monopoly profits are beyond the reach of competition" (Chamberlin, 1933, p. 82).