

Managerial Economics

B.B.A. Ist SEM

M.E Intro:-

Managerial Economics helps to make Important business decision by the application of economic theory and Method with an aim of ensuring that business decision meet their intended goal. The term Managerial Economics refers to the integration of economic theory with business practice. Economics provides tools, while, Managerial Economics applies these tools to the management of business. Thus Managerial Economics means the application of economics theories to solve the problems of business.

Definitions

According to Spencer and Siegelman! "Managerial Economics is the integration of economic theory with business practice for the purpose of facilitating decision-making and forward planning by management."

Nature of Managerial Economics or Characteristics

1. Problem-Solving:- Managerial Economics aims to find out optimal solutions of the business problems faced by firms.
2. Micro-Economic:- Micro-Economics is the branch of Economics that deals with the individual unit of an economy. Managerial Economics aims to make decision by the analysis and finding the optimal solution of the business concerns/firms.
3. Pragmatic:- Managerial Economics is a practical part not theoretical at some places it ignores difficult abstract issues of economic theories as well as at some places it also incorporates complications ignored by economic theory in order to analyse the overall situation in which managerial decision-making take place.

②

Normative :- Positive Economics deals with the actual or existing Economics Phenomenon. Normative Economics, Prescribes what ought to be.

5. Conceptual :- Managerial Economics is based on strong Economic Concepts.

Macro Economic ! - When all the individual matters are added-up and it becomes a matter of analysing the problems of the economy or the nation as a whole, we call it macro-economics. Managerial Economics does not prescribe solutions of business problems in isolation. It takes the help of some macro-economic theories to understand and adjust to the environment in which the firm operates.

7. Deals with the Application of Economics Theory and its Application. Economic theory which can be applied to business management are as follows:-

(1) Demand Analysis! - Law of demand, Elasticity of demand, Factors affecting demand,

(2) Production Analysis! - Law of variable proportions, Law of returns to scale, Economies and diseconomies of scale.

(3) Market Analysis! - Nature of product Market like perfect competition, monopoly competition, product pricing and out decisions in different forms of Market.

Study of Allocation of Resources :-

(i) input Allocation :- includes raw material,

labour hours, Machine hours etc

(ii) out put Allocation :- includes meeting ~~co~~ customer's demand in different segments of market at different locations.

(iii) Allocation of funds :- includes efficiency of usage of cash or cash and other resources.

g. Goal oriented :- Managerial Economics is goal oriented and prescriptive. It deals with how decisions should be formulated by managers to accomplish the organisational goal.

Scope or Subject Matter of Managerial Economics



1. Cost and Production :- The estimation of cost are of great use for making management decisions.

2. Pricing Decisions, Policies and Practices :- Its numerous aspects are the price determination in various market forms Pricing policies, Pricing method, differential pricing, Productive and price forecasting.

3. Profit Management :- The important topics covered under this area are nature and ~~management~~ measurement of profit Profit Policies, and techniques of profit planning like break-even analysis.

4. Capital Management :- The main topics covered under this area are cost of capital, rate of return and selection of projects. (L1)

5. Analysis of Business Environment :- The environment factor effects business adverse as well as favourable. Therefore, manager must consider the environmental factor in the process of decision-making.

6. Allied Disciplines :- Therefore mathematical tools are widely used in determining relationships between economic variables. Similarly, statistical and accounting principles are used in taking business decisions.

Demand Analysis and Forecasting :- A major part of managerial decision-making depends on accurate estimate of demand. A forecast of future sales refers to the speculations made about the sales in the future.

Managerial Economics with other Subjects

Managerial Economics and Statistics - Managers do not have exact information about the variables affecting decisions and have to deal with the uncertainty of future events. The theory of probability on which Statistics is based upon, provides logic for dealing with such uncertainties.



Managerial Economics and Mathematics :- We require a set

of mathematical tools as it involves estimating of various economic relationships, predicting relevant economic factors used in decision-making and forward planning.

Knowledge of geometry, trigonometry and algebra is essential requirement.

3. Managerial Economics and Accounting :- Managerial Economics is also closely related to accounting which is concerned with recording the financial operation of a business firm. Accounting information is one of the principal sources of data required by a managerial economist for his decision making purpose.

Managerial Economics and Operation Research :- The significant relationship between Managerial economics and operation Research can be highlighted with reference to certain important problems of Managerial Economics which are solved with the help of OR techniques, like allocation problem, competitive problem, waiting line problem and inventory problem.

Managerial Economics and Economics :- Economics has two main divisions (i) Micro Economics (ii) Macro Economics. Business Economics have also found the following main areas of Economics as useful in their work:-

- (1) Demand theory (2) Theory of the firm - Price, output and investment decisions.
- (3) Business financing (4) Public finance and fiscal Policy.
- (5) Money and banking (6) National income and social accounting
- (7) Theory of international trade and (8) Economics of developing countries

UNIT II DEMAND

Meaning and Definition of Demand

The concept of demand refers to the quantity of goods or services that consumers are willing and able to purchase at various prices during a period of time.

Definition

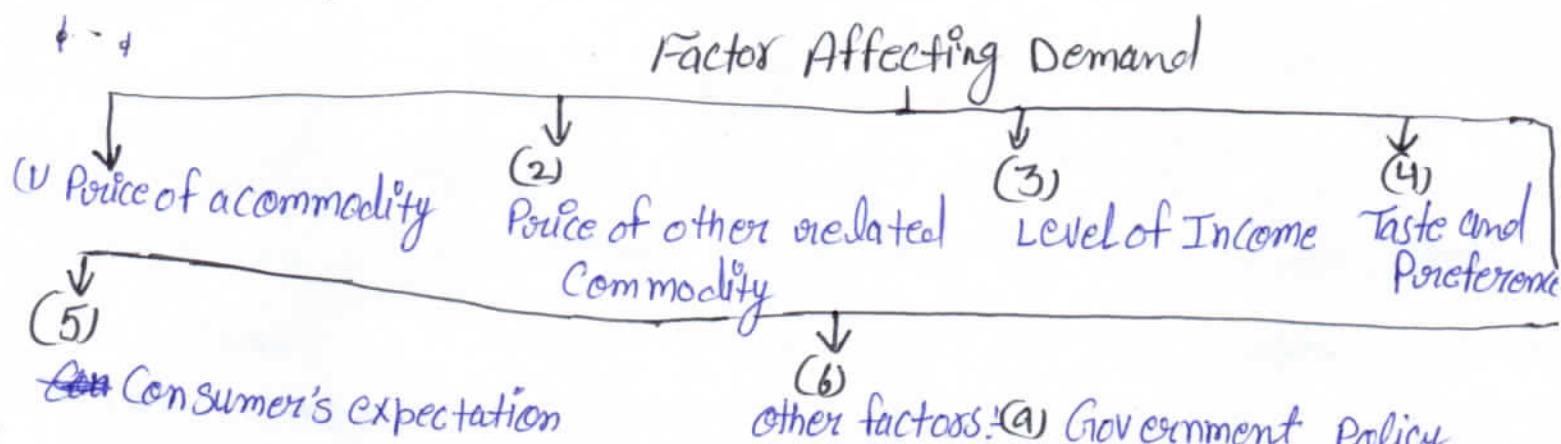
"Demand is effective desire. It implies three things:

- (1) Desire to possess a thing.
2. Means for purchasing it and
3. Willingness to use these means for purchasing it."



Factors Affecting Demand

There are number of factors which influence the demand for a commodity. Important among those are:-



Factors Affecting Market Demand!

- (1) Growth of Population
- (2) Climate and Weather Condition
- (3) Advertisement
- (4) Government Policy
- (5) Distribution of Income and Wealth.

Law of Demand

Law of demand explain the relationship between price and demand of a commodity. It has been a practical experience that when the Price of a Commodity increases its demand decreases and vice-versa.

Definition

According to Prof. Marshall, "The amount of demanded increases with a fall in Price and decreases with a rise in Price."

- there are three essentials of the law of demand
- (1) There are inverse relationship between prices and demand of a commodity.
 - (2) It is only a qualitative statement and not quantitative statement.
 - (3) Price is an independent variable and demand is a dependent variable.
It means that demand is function of Price

Assumptions of the Law of Demand

If the other thing remaining the same is an important clause of the Law of demand this law is based upon the following assumption:-

1. There should be no change in the income of consumer.
2. There should be no change in the nature, tastes and preferences of consumer.
3. There should be no change in the price of related good.
4. Consumer should not come to know about any new substitute product.
5. The commodity should not be a prestige commodity.
6. There should be no hope of change in the price of commodity in near future.

Why does a Demand Curve Slope Downward to the Right?

Law of demand explain that the demand of a commodity increases on a fall in its price and decreases on an increase in its price. A Study of demand curve explain that a demand curve always slopes downward to the right.

Following are the causes that explain the inverse relationship between price and demand of a commodity.

1. Law of Diminishing Marginal Utility : For this reason, he will be ready to pay purchase more of a commodity only when it is offered to him on a lower price. If the commodity offered to him at a higher price he will restrict its consumption.
2. Income Effect : As the price of a commodity falls it means an increase in the real income of a consumer.

3. Substitution Effect : When the price of a commodity increases the consumer feel this commodity costlier in comparison to its substitute commodities and as a result the consumer prefers to consume substitute goods.

4. Change in Number of Consumers :
 - If the price of a commodity increase it change the number of its consumers in two ways (i) Some consumers will discontinue and some consumer will purchase less quantity of it. So demand of goods will decrease.

5. Different Uses of Commodity : If a commodity can be put to several uses its demand will be effected more by a change in its price. e.g. Electricity.

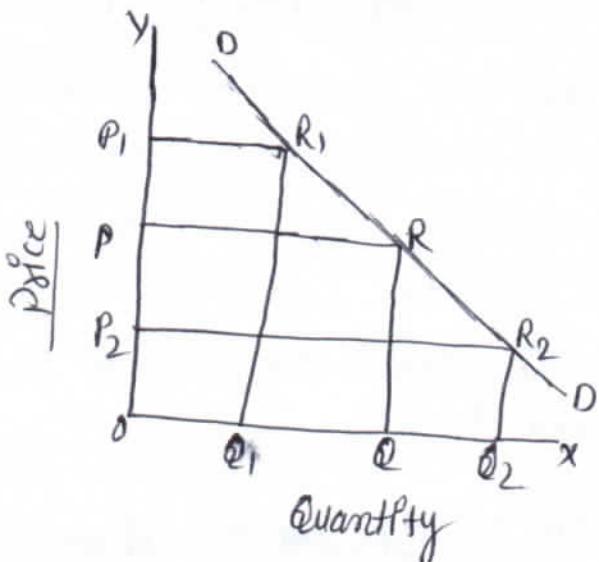


Fig Demand Curve.

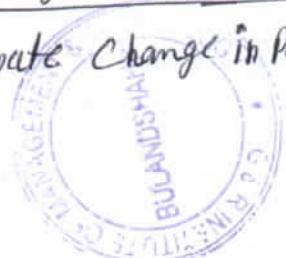
Demand curve in given diagram demand curve is DD Price of Commodity on OY and quantity demanded on OX
 OQ quantity will be demanded at price OP. When Price increases to OP₁ quantity demanded to OQ₁ when Price decreases to OP₂ quantity demand increase to OQ₂

Elasticity of Demand

According to Prof. Marshall. The elasticity of demand in a market is great or small according to as the amount demanded increases much or little for a given fall in price or diminishes much or little for a given rise in price.

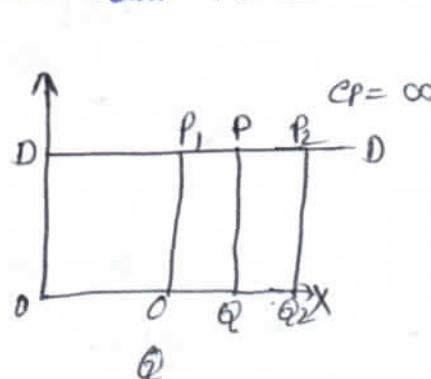
It can be concluded that elasticity of demand is the rate at which the quantity demanded of a commodity changes in response to a given change in its price.

Price elasticity of demand. Proportionate change in the quantity demanded
Proportionate Change in Price.



There are five degrees of Price elasticity of demand:-

1. Perfectly Elastic Demand :- ($e_p = \infty$): It refers to that situation in which a small change in price will cause an infinitely large change in demand. at a particular price



P_x	D_x
10	10
10	20
10	30

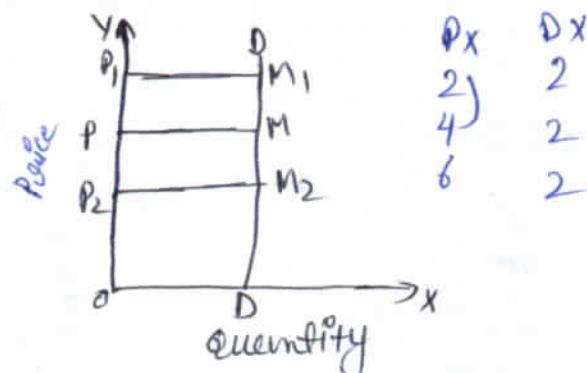
$$\begin{aligned} e_d &= \frac{\Delta Q}{Q} \times \frac{P}{\Delta P} \\ &= \frac{20-10}{10} \times \left(\frac{10}{10-10} \right) \left(\frac{10}{0} \right) = \frac{100}{0} = \infty \end{aligned}$$



2. Perfectly Inelastic Demand :- ($e_p = 0$)

When there is no change in demand as a result of change in price

$$\begin{aligned} e_d &= \frac{\Delta Q}{Q} = \frac{P}{\Delta P} \\ &= \frac{2-2}{2} \left(\frac{2}{4-2} \right) \\ &= \frac{0}{2} \left(\frac{2}{2} \right) = \frac{0}{4} = 0 \end{aligned}$$

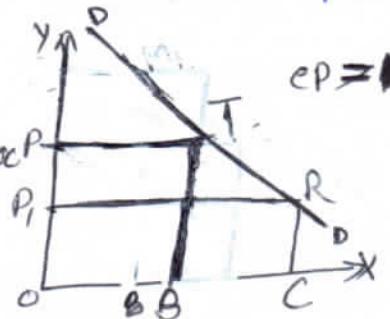


3. Unitary Elastic Demand ($e_p = 1$) when proportionate change in the price of a commodity and proportionate change in its demand is equal.

Eg. 25% Price increase than 25% Demand fall

$$\begin{aligned} TE &= P \times Q \\ &= OP \times OB \\ &= Ax T \square OPTB \text{ Price of } P = \alpha P \\ TE &= P \times Q \\ &= O P_1 \times O C \\ &= Area O P_1 R C \end{aligned}$$

$$\text{Area } \square O P T B = \text{Area } \square O P_1 R C$$



P_x	D_x
2	2
4	4
6	6

(11)

4. More Elastic Demand ($EP > 1$) When Proportionate Change in the quantity demanded of a Product is more than the Proportionate change in its Price.
 Eg. Price of a commodity increase by 5% and Commodity decreases by 20% ($EP > 1$)

$$P = OP \quad Q = OB$$

$$TE = \frac{PQ}{OP}$$

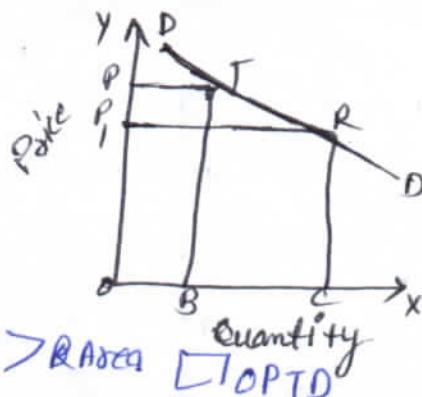
$$= OP \times OB$$

$$= \text{Area } \square OP TB$$

$$P = OP_1 \quad Q = OC$$

$$TE = OP_1 \times OC$$

$$= \text{Area } \square OP_1 RC \quad \text{Area } \square OP_1 RC > \text{Area } \square OP TB$$



5. Less Elastic Demand :- ($EP < 1$) :- It refers to a situation in which the change in demand is less than proportionate change in Price. The demand for articles of Necessity is of this type.

$$P_y = OP \quad Q_x = OB$$

$$TE = P_x Q$$

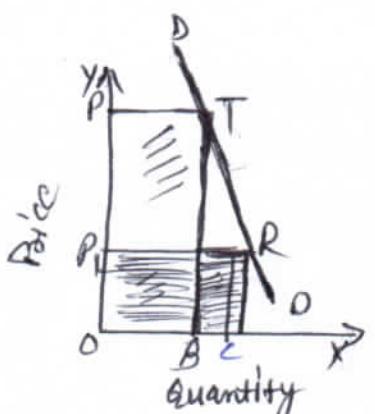
$$= OP \times OP$$

$$= \text{Area } \square OP TB$$

$$P = OP_1 \quad Q = OC$$

$$TE = P_x Q$$

$$= OP_1 \times OC = \text{Area } \square OP_1 RC$$



Factors Affecting the Elasticity of Demand :-

(1) Nature of Commodity:-

- (a) Necessaries:- (i) Life Saving such as Meats, Cloths, house, Medicine etc.
 (ii) Efficiency Saving necessities such MILK, ghee, transportation
 Electricity, fruits, entertainment, etc. (iii) Traditional necessities
 Such as the expenses on birth, marriage, death and other Social tradition etc.

(b) Comfortable Goods:- Such as coolers, refrigerators, TV, Scooters etc.

(c) Luxurious Goods:- Such as air-Conditioners, DVD Player/CD Player and Car etc.

2. Availability of substitutes:- If a number of substitutes are available for a commodity its demand will be elastic if a commodity has no substitute its demand will be inelastic. The demand of salt is inelastic mainly due to this reason.

3. Income of Consumers:- Rich people are less affected by the change in price so demand will tend to be inelastic because they will demand the commodity at all the levels of price. If poor people its demand will tend to be more elastic because these people are most affected by price change.

4. Different Uses of Commodity:- If a commodity can be put several uses the demand of such commodity will be elastic

5. Postponement of the Use of Commodity:- If the commodity is of the nature that its use can be postponed for a particular time its demand will be elastic for example, the demand of TV, refrigerators, washing etc.

6. Demand of Complementary Goods! — Demand of complementary goods depends upon the demand of main product the demand of complementary goods also will be elastic. Complementary goods like Petrol is complementary to Scooters and Cars.
7. Habit of Consumers! — the demand of such product or brand will be relatively inelastic.
8. Share in Total expenditure! — If a consumer is spending only a small fraction of his total income on the consumption of a good commodity the demand of such commodity will be inelastic. The demand of Salt.
9. Durability of the Commodity! — the demand of such commodity will be elastic such commodity used for a long time.
10. Distribution Income and wealth in the Society! — unequal distribution of Income and wealth in a society the demand of commodities in general in such society will be relatively inelastic.

Importance of elasticity of demand
In business decisions



- (1) Helpful in Price Determination! — He can fix a higher price for the product the demand of which is inelastic. On the contrary the price of product with elastic demand should be kept low.

2. Importance to a Monopolist!— If the demand of his product is inelastic he can fix relatively higher price but if the demand of his product is elastic, he will have to fix lower price.

3. Importance for the Government!— Higher tax on the commodities the demand of which is inelastic, the rate of tax should be low for the commodities having elastic demand because high rate of tax on such commodities may fail in collecting revenues for the government.

4. Helpful in Price Discrimination!— Price discrimination means a marketing strategy under which different price are determined for a single product for different consumers or different market. The monopolist can fix higher price of his product for the markets or consumers with inelastic demand.

5. Helpful in Price Determination in Case of Joint Supply!— Two or more products are produced together the price for such products are determined on the basis of their elasticity of demand.

6. Helpful in the Determination of Reward for Various factors of Production!— Factors of production such as land, labour, capital, organisation, and enterprise. A factor with inelastic demand can always bargain a higher price. Vice-versa

7. Importance in International Trade!— This concept helps government in determining the rates of exchange for its currency in relation to other currency of world.
(i) Rate of tariff

It explains the Paradox of Poverty Amidst Plenty! For example a farmer get bumper crop. It should bring prosperity to him but if the demand of the commodity is elastic it will not happen. The problem become more serious when the product is perishable. In this case the farmer will get less bumper crop. The farmer will remain poor even on getting

Various Methods of determining Price elasticity of demand

(1) Total expenditure Method !

- Dr - Alfred Marshall
- Price and Total Expenditure Relationship
- Price Change — Total EXP - Percent change $\frac{\Delta EXP}{EXP}$

$$\text{Total Expenditure} = \text{Price} \times \text{Quantity demand}$$

(1) Compli!

Price	Quantity demand	Total EXP	Unitary elastic
Rs 10	100 units	Rs 1000 (10×100)	
Rs 5	200 units	Rs 1000 (5×200)	$E=1$

$P \uparrow \downarrow$ = Total EXP. remain unchanged.

2 Compli?

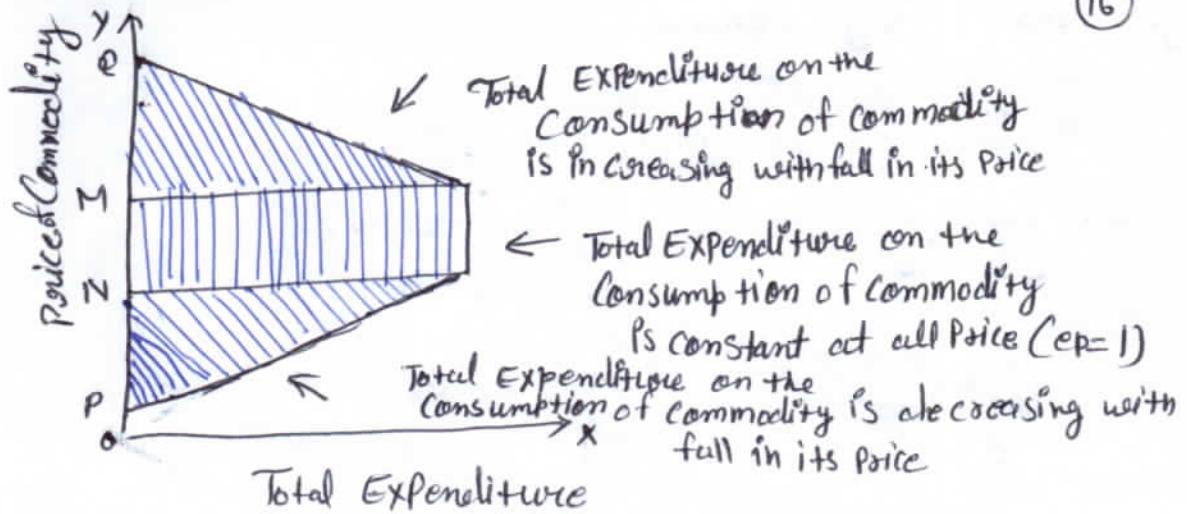
↓ R10	100 unit	1000 (10×100)	↑ Relatively Elastic demand
R 6	200 units	R 1200 (6×200)	
		$P \uparrow \downarrow$ = Total EXP ↓ ↑	$E > 1$

3 Compli?

Price	Quantity demand	Total EXPem.	Relatively Inelastic demand
Rs 10	100 units	R 1000 (10×100)	
Rs 6	150 units	R 900 (6×150)	$E < 1$

$P \downarrow \uparrow$ ~~Rs 10~~ = Total EXP ↓ ↑

Unitary Elastic $\rightarrow P \uparrow \downarrow$ Total EXP unchange
 Relatively Elastic $\rightarrow P \uparrow \downarrow$ Total EXP ↓ ↑ (opposite or Inverse)
 Relatively Inelastic $\rightarrow P \uparrow \downarrow$ Total EXP ↓ ↑ (Same direction)
 Same relation



2. Percentage or Proportionate Method of Flux: This Method is Improvement of total outlay Method because total outlay Method does not provide a numerical measurement of the elasticity of demand. Its Propounded by Prof. Flux. According to this Method elasticity of demand for a commodity is measured by dividing Proportionate Change in the quantity demanded of the commodity brought in response to proportionate change in its price.

$$\frac{\Delta Q}{Q} \times \frac{P}{\Delta P}$$

% Change in demand / % Change in Price
Change in demand / Change in Price



We Compare

Percentage Change in any demand with % Change in Price

$$Ed = \frac{\% \text{ Change in demand}}{\% \text{ Change in Price}}$$

symbolically $Ed = \frac{\text{Change in Price}}{\text{Price}} : \frac{\Delta Q}{Q} \div \frac{\Delta P}{P}$

$$Ed = \frac{\Delta Q}{Q} \times \frac{P}{\Delta P}$$

$$Ed = \frac{\Delta Q}{\Delta P} \times \frac{P}{Q}$$

Eg. Price ↓ Qty demand
 8 ↓ 10 unit ↑
 6 14 unit ↓

$$Ed = \frac{\Delta Q}{\Delta P} \times \frac{P}{Q}$$

$$= \frac{4^2}{2} \times \frac{8-4}{10-6}$$

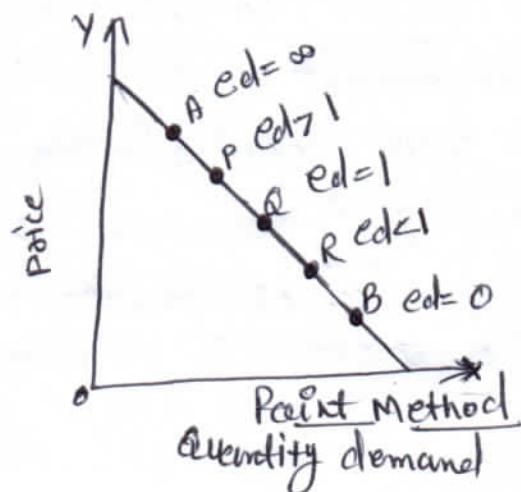
$$= \frac{8}{5}$$

(Now - Old)
 $\Delta Q = (14 - 10)$
 $\Delta Q = 4$
 $\Delta P = (6 - 8)$
 $\Delta P = -2$ Negative Ignore

$Ed = 1.6$

$Ed > 1$ Relatively elastic demand ($\% \text{ demand} > \% \text{ price}$)

3.



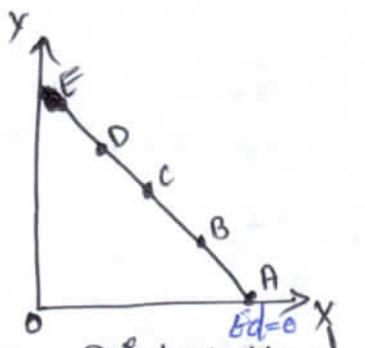
3 Geometric Method OR Point Method

- Dr Alfred Marshall.
- We will able to find out elasticity at a point in a given demand curve



$$Ed = \frac{\text{Lower Seg}}{\text{Upper Seg}}$$

$$Ed = \frac{L}{U}$$



at a A Point

$$= \frac{\text{Lower Seg}}{\text{Upper Seg}}$$

$$Ed = 0$$

Point Method

$$= \frac{O}{AL}$$

at a B Point

$$= \frac{\text{Lower seg}}{\text{Upper seg}} = \frac{AB}{BE}$$

(AB < BE)

$$\frac{4}{6} < 6$$

$$\frac{AB}{BE}$$

$$\boxed{Ed = 1}$$

$$At a C = \frac{AC}{CE}$$

$$\boxed{Ed = 1}$$

At a Point D

$$= \frac{AD}{DE} (AD > DE)$$

$$Ed > 1 \quad \frac{6}{4}$$

at a Point E

$$\frac{L}{U}$$

$$= \frac{AE}{CE}$$

$$\boxed{Ed = \infty}$$

Income elasticity of Demand



Watson Income elasticity of demand is the rate of change of quantity with respect to change in income other factors remaining constant.

Measurement of Income Elasticity :- Income elasticity can be measured with the help of the following formula:

$$E^I = \frac{\text{Proportionate change in quantity demanded}}{\text{Proportionate change in income}}$$

$$E^I = \frac{Q_1 - Q_2}{Q_1} + \frac{I_1 - I_2}{I_1}$$

Where Q_1 Initial demand

I_1 = Initial Income

Q_2 = NEW demand

I_2 = NEW INCOME

(14)

$$ei = \frac{\Delta Q}{Q_1} \div \frac{\Delta I}{I_1}$$

where ΔQ = Change in demand

I = Initial income

ΔI = change in Income

Q = Initial Q.D.

KIND OF INCOME ELASTICITY OF DEMAND :-

(a) Positive Income Elasticity of Demand :- If $E_I > 0$ demand of

Quantity increases with increases in Income and vice versa

(b) Negative Income Elasticity of Demand :- If $E_I < 0$ demand decrease

A commodity increase in income of consumer and increase with fall in income

(c) Zero Income Elasticity of Demand :- When demand for

a commodity does not respond. $E_I = 0$



2. CROSS ELASTICITY OF DEMAND :-

Cross elasticity of demand measures the responsiveness of demand for a commodity say tea when price of other related commodity say coffee changes by a small amount.

$$ec = \frac{\% \text{ Change in quantity demanded by Commodity X}}{\% \text{ Change in quantity demanded by Commodity Y}}$$

(a) Positive it implies that goods are close substitutes.

(b) Negative it means such goods are complementary.

(c) Zero ($ec=0$) it denotes goods are independent goods.

Factors Affecting Supply

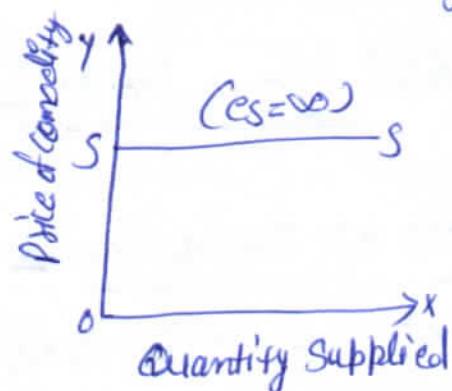
1. Natural Factors : the agricultural production cannot increase beyond a certain limit, climatic conditions.
2. Goals of Producers : if the object of a firm is to capture the market by attaining maximum sale revenue the firm will increase the supply.
3. Technological Know-how : Technological improvement, its cost, cost of production declines.
4. Price of Factors of Production : For example, if the wages of labour increase or prices
5. Price Related Goods : especially Substitute Goods.
6. Price of Commodity : $P_A \leftarrow P_B \leftarrow P_C$
7. Expectation of Further Change in Price : if price of a commodity increased and still there is hope of further increased in its price the supply will decrease because the sellers would like to store it.
8. Agreement among Producers : supply of that commodity will decrease it creates artificial scarcity in the market.
9. Taxation Policy : Heavy taxes discourage producer and as a result its supply will decrease.
10. Means of Transportation and Communication :

Types of Elasticity OF SUPPLY

1 Perfectly Elastic Supply ($E_S = \infty$)

Price	Quantity supplied
10	10,000
10	9000
10	8000

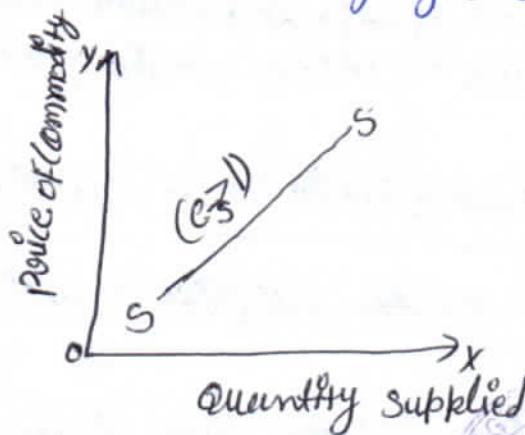
When supply of a commodity changes without any change in its price it is called perfectly elastic supply.



2 Highly Elastic Supply ($E_S > 1$)

Price	Quantity supplied
10	10,000
8	6,000
6	3,000

When supply of a commodity changes in a greater proportion than a change in its price it is called highly elastic supply.

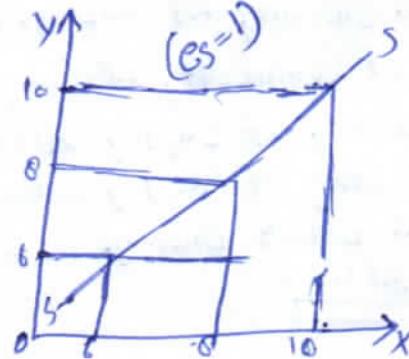


3. Elastic Supply ($Es=1$)

Elastic supply

Price per kg	Quantity Supplied
10	10,000
8	8,000
6	6,000

when proportionate change in supply and proportionate change in price are equal, it is called elastic supply



4. Less Elastic Supply or Inelastic Supply ($Es < 1$)

Less Elastic supply

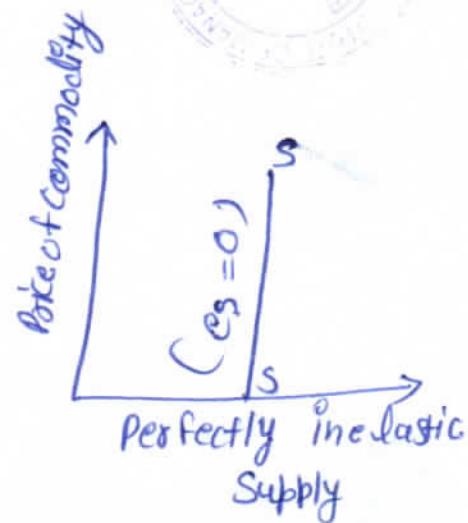
Price	Quantity supplied
10	10,000
8	6,000
6	5,000



5. Perfectly inelastic supply

Perfectly inelastic supply

Price	Quantity supplied
10	10,000
8	10,000
6	10,000



(2)

Method of Measuring Price Elasticity of Supply

(1) Proportionate Percentage Method = $es = \frac{\% \text{ Change in Supply}}{\% \text{ Change in Price}}$

ΔQ = Change in quantity
 P = Price of commodity ΔP = Change in price
 Q_2 = Quantity of supply after change in price
 Q_1 = Quantity of supply before change in price
 P_1 = Price before change P_2 = Price after change.

2- Point Method,

Factors Influencing Elasticity of Supply

- (1) Nature of Commodity
- (2) Time
- (3) Stage of Law of Return
- 4. Number of Products Being Produced by an Industry
- (5) Production Methods and Technique.
- (6) Agricultural Products:

Unit 3Market AnalysisMarket Structure

It refers to the nature and degree of competition in the market for goods and services. Market Structure affects the behaviour and performance of firms in the Industry.

Basics of Market Classification

- (1) On the Basis of Area:- Classified as Local Markets, regional Market, national Markets, and International Market.
- (2) On the Basis of Nature of Transactions:- Classified as spot market and future market.
- (3) On the Basis of Volume of Business:- Market are classified as wholesale and retail markets.
- (4) On the Basis of Commodities and Services:-
- (5) On the Basis of Time:- Classified on the basis of time as Very Short Period, short Period, long Period and very long Period
- (6) On the Basis of Legality:- as open market and black market
- (7) On the Basis of Status of Sellers:- Classified as primary secondary and terminal markets
- (8) On the Basis of Nature of Competition:- three factors depending upon which there is competition in the Market are
 - (1) Factor of Substitution
 - (2) Factor of Interdependence
 - (3) Factor relating to easy entry

The two types of competition on which the types of market depend are:- (25)

- (1) Perfect Competition:- Many sellers sell same type of products to many buyers.
- (II) Imperfect Competition:- The various forms of imperfect competition are monopoly, monopolistic competition, oligopoly and duopoly.

Perfect Competition

Boulding's Perfect competition market is a situation where large number of buyers and sellers are engaged in the purchase and sale of identically similar products and who are in close contact with each other as well as who buy and sell freely among themselves.

Characteristics of Perfect Competition:-

- (1) Large Number of Buyers and Sellers:-
- (2) Homogeneous Product:-
- (3) Freedom of Entry and Exit:-
- (4) Limited Share in the Market:-
- (5) Perfect Knowledge of the Market:-
- (6) Perfect Mobility Among factors:-
- (7) Absence of Transportation Cost:-
- (8) Uniform Price:-

Price Determination

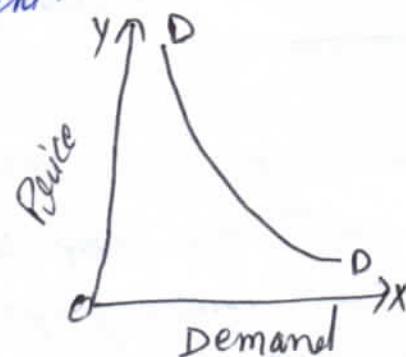
Under Perfect Competition

Under the Perfect Competition a firm is only a Price taker. Market price of the commodity is determined by that point in which demand and supply intersect each other.

Price of a commodity is determined by two forms.

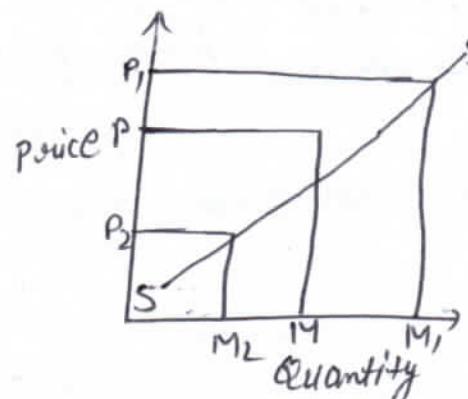
(1) Market Demand :-

Demand has inverse relationship between demand and supply so, the demand curve slope downwards from left to right.



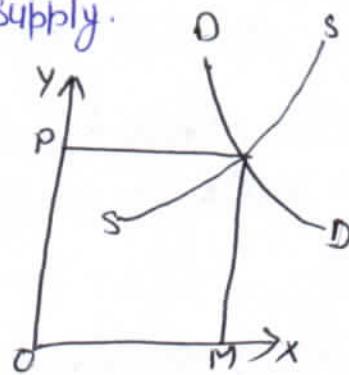
(2) Market Supply :-

Every supplier want more supply at a high price. So, there is a direct relationship between price and supply. If price of product is higher then supply of product is also high.



Price Determination or Equilibrium of Demand and Supply.

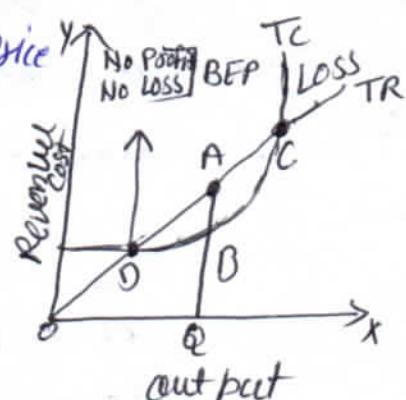
Price will be determined at the point where both the total demand is equal to total supply.



Explain the Equilibrium of A Firm
in Perfect Competition.

Perfect competition is a market in which large number of buyer and sellers compete with each other in the purchase and sale of a commodity without having any influences over the market price of the commodity.

1. In perfect competition there is a single price for a commodity in the whole market
2. All the firms are price takers. They have to sell their products at a fixed price. No individual firm can influence the price
3. A firm can sell any quantity of its product at given price. $AR = MR$.



Monopoly

The term Monopoly is made up of two words:- Mono-Poly-Mono means 'single' and Poly means 'seller'. So Monopoly states such a market in which only a single seller exists. The producer in Monopoly Market has full control on the market

Marshall

Characteristics of Monopoly:-

- (1) Single Seller of A Product:-
- (2) No Close Substitutes:-
- (3) Strong Barriers to Entry of New Firm:-
- (4) Large Number of Buyers:-
5. Free Price Policy:-
6. No Competition:-

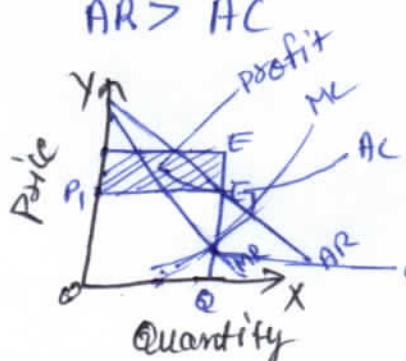


Price Determination Under Monopoly

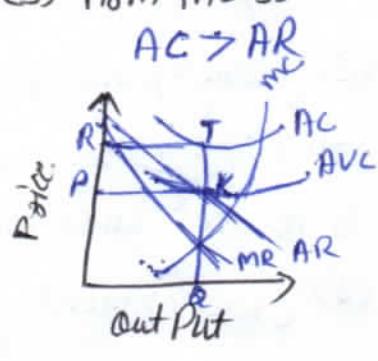
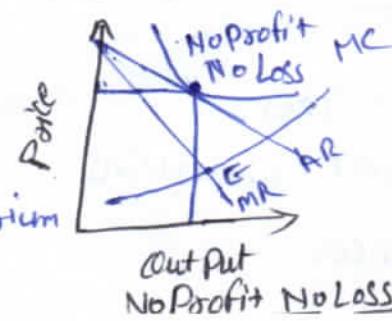
A Monopoly firm aims at earning maximum profits where a monopolist adjusts his output and attains maximum profits by fixing price. This maximum profit is earned at that level of output where MR is equal to MC.

Equilibrium of Monopolist firm in short run:-

- (1) Abnormal Profit $AR > AC$
- (2) Normal Profit ($no\ profit, no\ loss$)
- (3) firm in Loss.



$$AC = AR$$



Oligopoly

Oligopoly is that form of Imperfect Competition where there are a few firms in the Market producing either a homogeneous product or producing products which are close but not perfect substitute of each other.

Monopolistic Competition

Characteristics of Monopolistic (Imperfect competition)

- (1) Large Number of Buyer and seller:-
- (2) Imperfect Knowledge of the Market.
- (3) Product Differentiation
- (4) Free Entry and Exit of Firms
- 5 Non - Price Competition:
- 6 Expenditure on Advertisement and other selling cost

Statement Perfect competition is A Myth

- (1) Large Number of Buyer and seller
- (2) Agreement among seller
- (3) Homogeneity of product
- (4) Free Entry and Exit of Firms
- 5 Perfect knowledge of Market Conditions
- (6) Government Interference.



UNIT 4Importance of Pricing

Pricing is very important to customers. Industries and for promotion of business activity. This can be discussed as under.

1. Importance of Pricing to Consumers:-

- (a) Pricing affects the purchasing power.
- (b) Price indicate product quality.
- (c) Pricing depends upon the right decision of the marketer to take a right decision for pricing level.

2. Importance of Pricing to Firms:-

- (a) Pricing determines Profitability.
- (b) Pricing determines market share.
- (c) Pricing determines firm success and loss.
- (d) Pricing results in inter-firm rivalry.
- (e)

3. Importance of Pricing to Economy:-

- (a) Price influences factors of production such as Capital, Land, Machines.
- (b) Price of the product govern the demand and supply.
- (c) Price affects Saving and investment.
- (d) Price control the demand of the product.

Factors Influencing Pricing(1) Internal Factors:-(i) Organisational Factor:-

(2) Market Mix

(3) Product differentiation

4. Cost of Product:

5. Objectives of the firm.

II External Factors:-

(1) Demand:-

(2) Suppliers:-

(3) Competition:-

(4) Economic Conditions:-

(5) Government:-

(6) Buyer:-



Method of Price Determination

(I) Methods of Determining Price on the Basis Cost

(I) Cost Plus Pricing Method:-

$$\text{Price Per Unit} = \frac{\text{Total Cost}}{\text{Number of Units produced}} + \frac{\text{Total Required Profit}}{\text{Number of Units}}$$

Enterprises Fix a certain Percentage of Profit to determine the Price:-

$$\text{Price Per Unit} = \text{Average total Cost per Unit} + 15\% \text{ of total Cost per Unit}$$

(II) Marginal Cost or Incremental Cost Pricing:- This Policy is adopted

Only Short run under this method is equal to the Variable Cost per unit of product.

III Break -even Point Pricing Method

Break even Point
Means the level of production at which total cost of production and total sales revenue of an enterprise are equal. there is no profit no loss to the enterprise. this method also can be adopted by an enterprise in long run. In this method Price of Production is equal to the average total cost of production.

4. Pricing method Based on Rate of Return

— This method is used by the enterprise which wants to earn profit at a certain rate of return on investment. This method is not very practical when there is tough competition in the market.

Methods of Pricing Determination on the Basis of Market Condition

1. Pricing at Market Price level or Going Rate Pricing:-
- (2) Pricing Below Competitive Level.
- (3) Pricing Above Competitive Level.
- (4) Purchasing Power Pricing:-

Pricing Policies

- (1) Value-based Pricing:-
- (2) Product Line Pricing:-
- (3) Loss Leader Pricing:-
4. Peak Load Pricing



5 Affordability-based Pricing:-

(33)

(6) Price Discrimination / Differential Pricing Strategy:-

(7) Prestige Pricing:-

(8) Market and Demand Based Pricing:-

g. Cycle Pricing.



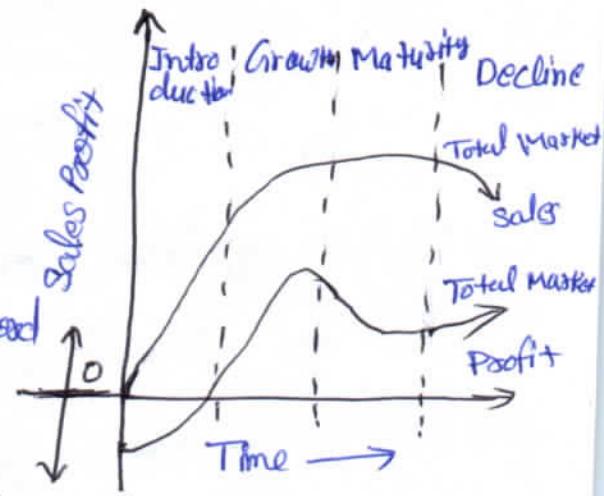
Product Life Cycle

From its birth to death a Product exists in different stages and in different Competitive environments.

william J. Stanton

Phases

- 1) Introduction! — Profit are non-existent
- 2) Growth! — rapid market acceptance
- 3) Maturity! — Period of slowdown in sale
- 4) Decline! — Period when Sales Show a downward and Profit erode.



Steps in Price Determination

- 1) To Forecast the Demand of Product:-
- 2) To Anticipate the Reactions of Competitors:-
- 3) To Determine Expected Share of Market:-
- 4) To Select a Suitable Price to Achieve Market Objectives:-
- 5) To Consider Marketing policies to the Enterprise:-
- 6) Selection of a Specific Price:-

Problems In the Estimation of National Income of India

I. General or Procedural Problems:-

- (1) Non-availability of Data:-
- (2) Economic Differentiation of Activities:-
- (3) Production for self-Consumption:-
- (4) Non-monetised sectors:-
- (5) False Information Regarding Production and Income.
- (6) Problem of Double Counting:-

II Conceptual Problems

- (I) Problem of New Goods and Services:-
- (II) Problem of the Constituents of National Income:-



Unit 5

(35)

Economic Growth

Economic Growth refers to an increase in the goods and services produced by an economy over a particular period of time.

Theories of Economic Growth :-

- (1) The Classical Approach:- Adam Smith laid emphasis on increasing returns as a source of economic growth.
- (2) The Neoclassical Approach:-
- (3) The Post Modern Approach:-



Ways of Generating Economic Growth

- (1) Increase in the amount of physical capital goods in the economy:-
- (2) Technological Improvement:-
- (3) Grow the labour force:-
4. Increases in Human Capital:-

Importance of Economic Growth

- (1) Reduction in poverty.

- (2) Reduced Unemployment:-
- (3) Improved Public Services:-
- (4) Reduced Debt to GDP Ratios:-
- (5) Political Aspect:-

Limitation of Economic Growth

- (1) Inequality and Distribution:-
- (2) Negative Externalities:-
- (3) Conflict with the Environment:-
- (4) It Depends on what is produced:-
- (5) Unsustainable:-

Causes of Disequilibrium in BoP

- (1) Domestic inflation:-
- (2) Technological Change:-
- (3) Short Supply.
- (4) Fall in Demand:-

Causes of Inflation

- (1) Demand Side
 - (a) Increase in Public Expenditure:-
 - (b) Deficit Financing:-
 - (c) Cheap Money Policy.

- (d) Increase in Disposable Income:-
- (e) Black Money:-
- (f) Increased Investment:-
- (g) Reduction in Indirect Taxes:-
- (h) Reduction in Public Debt:-
- (i) Increase in Population:-
- (j) Increase in Exports:-

(2) Supply Side

- (k) Reduced Production
- (l) Technical Change
- (m) Industrial Disputes
- (n) Natural Factors
- (o) Shortage of Raw Material.
- (p) Productive Capacity
- (q) Shortage of Food Grain
- (r) International Effect
- (s) Industrial and Agriculture Policies
- (t) War and Internal Emergency
- (u) Artificial Scarcity.

Effects of Inflation

(38)

Effects on Production or Economic Growth !

- (1) Discouragement of Saving
- (2) Set back to Investment
- (3) serious Deterioration in the Quality of Goods produced:-
- (4) Hoarding of Essential Goods:-
- (5) Stimulus to speculation:-
- (6) Flight from Domestic Currency:-

Effects on Distribution or Employment !

- (1) Wages and Salary Earners:-
- (2) Debtors and Creditors:-
- (3) Investors:-
- (4) Producers:-

Non-economic Effects of Inflation

- (1) It helps in creating political instability
- (2) inflation redistributes income in favour of the rich
- (3) It deals with the serious blow in business morality and Ethics.
- (4) It not only disrupts the smooth functioning of the economy but it also prepares the ground for social and political upheavals.