BUSINESS ECONOMICS

UNIT 1

DEFINITION OF ECONOMICS

different views on economics

1. **Wealth view on economics (Adam Smith's wealth definition)**

Adam Smith is considered as the father of modern economics and capitalism. he's the author of famous book will talk Nation 1776. gingerly the term wealth means money but in economics will it refers to those goods with satisfy human wants. all Goods that satisfy human wants are not wealth. flood example are water and sunlight are essential for our survival however, they are not regarded as wealth because they are available in plenty. therefore those goods that are very scarce and have any value are considered as wealth.

advantages of Adam smith's views on economics

1. It highlighted an important problem faced by each and every nation of the world i.e. creation of wealth.

2. the problems of poverty unemployment excetra can we solve the to Greater extent when and where it is produced and distributed equitably.

Criticisms of Adam smith's view on economics

1. wrong Nation about wealth
2. emphasises wealth much
3. money alone was given importance
4. Narrow meanin of wealth
5. No mention of Man's welfare
6. it does not study means

II welfare views on economics (Alfred Marshall's welfare definition)

Man is the center of his study. according to him,the study of man is more important since it is primary than the study of wealth, which is secondary . He says,"Economics is the study of mankind in the ordinary business of life . it examines that part of individual and social action, which is most closely connected with the attainment and with the use of the material requisites of well-being. thus, it is on the one side a study of wealth and on the other and more important side a part of the study of the man."

advantages of marshall's View

1. Marshall strengthned the weakness of wealth definition by emphasizing the importance of man along with wealth.

2. she has created a new philosophy by Shifting the emphasis from wealth to Welfare thus elevating the status of economics.

disadvantages of marshall's View

1. narrow scope

2. misrepresents the science of economics

3. exclusive activities that do not promote material welfare

4. excluded services

III Scarcity view on Economics(Lionel Robbins's Scarcity Definition)

you can only choose the Saints which studies human behavior as your relationship between

"economics is the science, which studies human behavior as a relationship between ends and scarce means, which have alternative uses ".

advantages of Robbins View

1. Robbins definition make study of Economics analytical .

2. Robbins's definition is applicable everywhere .

3. Robbins's definition serves to specify the nature scope and subject matter of economics.

disadvantages of robbins's View

1. **no human touch**
2. **Reduced economics to Merely theory of value**
3. **It is too narrow.**

modern view of economics (Samuelson's definition)

according to Samuelson, "economics is a social science concerned chiefly with the way Society chooses to its employ resources, which have alternative uses to produce goods and services for present and future consumption"

advantages of Samuelson's definition

1. **Samuelson's growth oriented definition recognize the dynamic changes taking place in the economy .**
2. **it includes the element of time.**
3. **it stresses the problem of scarcity of means in relation to unlimited means.**

scope of economics

subject matter of economics: "wants-efforts- satisfaction" is a complete circle describing the subject matter of economics.

1. **economics as a science and an Art**
2. **relationship of economics with other social sciences**

a) economics and sociology

b) economics and ethics

c) economics and politics

d) economics and history

e) economics and psychology

f) economics jurisprudence

g) economics and statistics

h. economics and mathematics

3. laws of economics

4. economic laws and other laws.

law of demand

Price of Apples (per dozen Rs.)	Quantity demanded (in dozen)
10	1,000
8	2,000
6	4,000
4	6,000
2	8,000

law of demand : the law of demand explains that inverse relationship between the demand and price. it can be stated as follows ," A rise in the price of commodity or service is followed by a reduction in the demand for it, and a fall in prices followed by an increase in demand, conditions of demand remain constant". This is law of demand.

it simply says that, it price falls, the demand increase and if price Rises, the demand decreases.

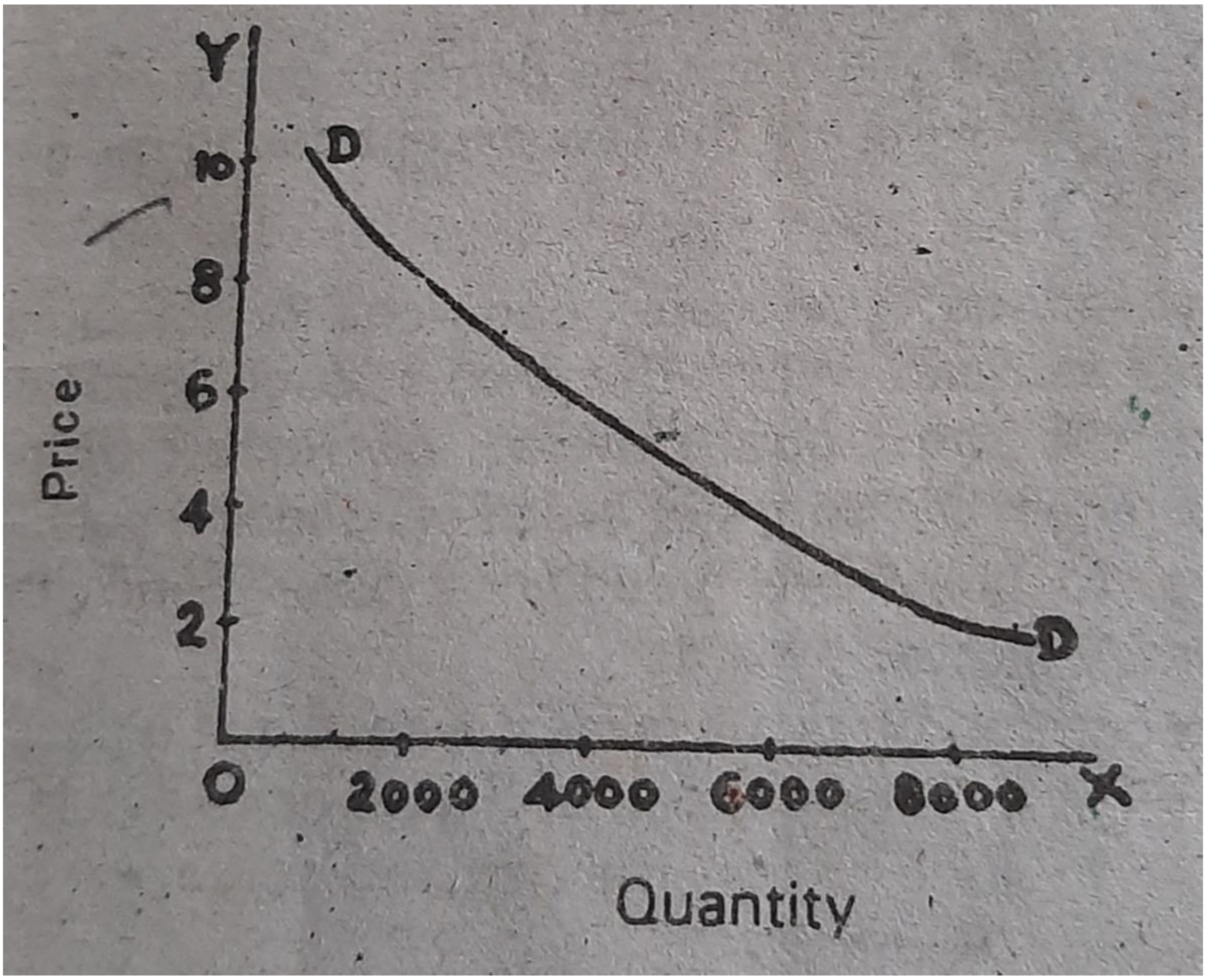
demand schedule and demand curve

the law of demand is Illustrated with the help of demand schedule and demand curve. Ademand schedule is a list of prices and quantities.

the table below represents an imginary demand schedule.

from the demand schedule it is clear that the quantity demanded Rises as price fall, and the quantity demanded Falls as the price Rises.

demand curve can be drawn from the demand schedule .



in the diagram DD is the demand curve. any point on the demand curve DD refers both price and quantity . the Demand curce dd is downward-sloping to the right. the downward slope of the curve indicates that the quantity demanded rises as price Falls.

the demand curves slope downwards because

1.the relation between price and quantity demanded is inverse. such an inverse relation can be shown only by a Falling curve.

2. as the price of commodity falls new consumer purchase a commodity

3. the existing consumers purchase additional unit of commodity as the temerity becomes cheaper. this is based on the law of diminishing marginal utility.

4. when the price of commodity Falls, the real income of the consumer increase. they increase the income enable the consumer to buy more and this effect is known as income effect .

5. when the price of commodity falls it becomes a cheaper good. so consumers have stood the cheaper Goods. this efect is called substitution effect.

law of supply

the law of supply can be stated as follows: “other things remaining the same if the price of a commodity Rises the supply is expanded, and as the price falls its supply is contracted”. in other words, the quantity offered for sales varies directly with the price.

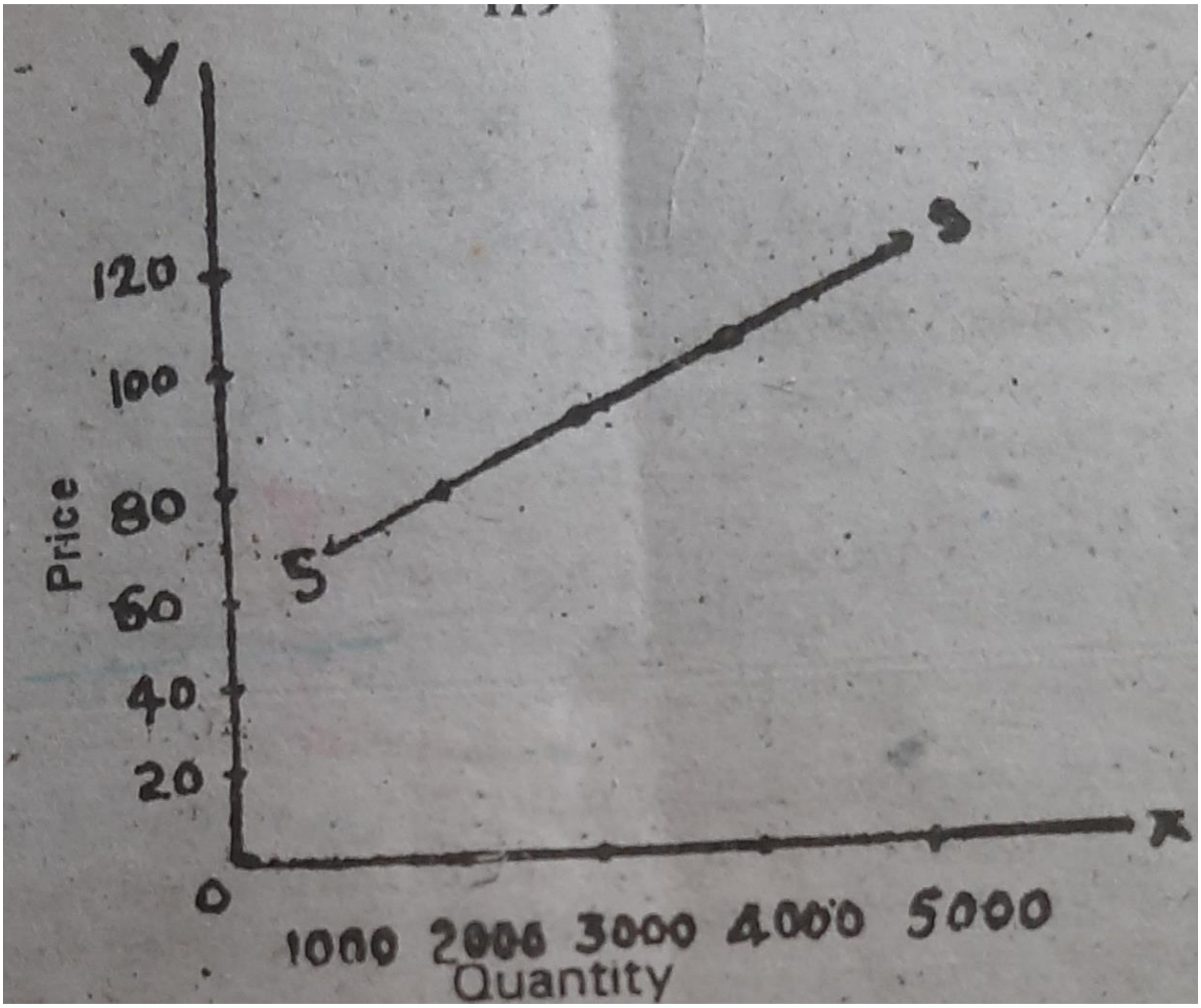
supply schedule

the direct relationship between price and Supply can be presented in the form of a table. discard Supply schedule. The following is an example of an imaginary Supply schedule relating to supply of paddy.

Price per bag Rs.	Quantity of supply bags
70	1,000
80	2,000
90	3,000
100	4,000
120	5,000

if we look at the supply schedule it is clear that when the price of Paddy rises the supply of paddy also rises, where as when the price of Paddy falls the supply of paddy also falls. it shows the direct relation between price and supply.

supply curve



OX- axis measures. amount of supply and OY- axis measures the Price. by marking points on the basis of the supply schedule. we get Supply Curve SS. the supply curve SS slopes upwards from left to right showing large supply at higher price.

Factors determining Supply

1. number of firms or sellers

2. level of technology

3. cost of production

4. price of related Goods

5. natural causes

6. government policy

micro and macro economics

1. Micro economic is the obverse of macro economic.

2.Micro analysisis the study of of particular, while macro economic analysis is the study of general.

3.Micro ecnomics studies the individual and parts of an economy, While macro economics studies as a whole

4. micro economics studies the individual farts that are mortal while micro economics studies the community that is immortal

5.To use a metaphor micro economics studies character of an individual tree,while macro econoics studies thq character of the entire forest.

6.Miro economics is simply a pure theory dealing with the mechanism ofvprices nd value ,while macro economic is a system of national policies dealing with savings, investment and employment activiities ,

7.Micro economics is concerned with an open economy while macro Economics is concerned with closed economics.

8.Prof.J.K.Metha says that maicro economics is a study of individual in respect of their behaviour, while macro economics is a study of the cmmunity in respect of its behaviour.

9.Micro economics is otherwise called price theory .macro economics is otherwise calledas income theory.

10.Marshall's famous book 'principal of economics' is an outstanding example of micro economics . Keunes'famous book ''General theory of employment interest and money'is an outstanding example of maco economics.

11.Micro economics assumed full employment .No such assumption in macro economics.

12.Marshall and other neo-cassical writer were interested in micro analysis. Keynens and other morden economics were interested in macro analysis.

13.The concept of equilibrium is made use of in micro as well as in in macro economics. In micro analysis it is partial equilibriu and in macro analysis it is general equilibrium.

14.Micro analysis is static analysis while macro analysis is a dynamic one.

15.Since micro-study takes into consideration of smaller units,this method is also referred to as ''Slicing method''.Macro economics studies the macro-quantitiesby splitting the ecnomics into sectors,or big lumps. Hence this method is also reffered to as ''lumping method''.

factors of production

production is the result of cooperation between different factors of production . Generally there are four factors of production are land labor capital and organization.

Land as a factor of production

the term land in economics include all Gifts of nature which yield an income. it refers to all the natural resources that are available to man on land.

characteristics of land: As a factor of production possess certain characteristics. they are as follows

1. land is a free gift of nature
2. land is fixed in Supply
3. land is permanent and not perishable
4. land is heterogeneous
5. land lacks Mobility

6. land is used for variety of purposes

7. land is subject to the law of diminishing returns .

Malthusian theory of population

labor Supply depends on the population of country . they are two well-known theories of population 1. Malthusian theory 2. Optimum Theory , Malthusian theory is associated with the name of T.R.Malthus. he wrote his essay on the principle of population in 1879.

Malthusian theory of population: "by Nature human food increase in a Arithmetical ratio, manhimself increases in the quick geometrical ratio unless want and vice stop him".

important features in the Malthsian theory

1.population is necessarily limited by the means of subsistence . in another words the size of a population is limited by availability of food

2. population increases faster than food production

3.malthus I said earlier that the population of country tends to double every 20 years but the food supply would be increases much less rapidly.

4. Malthus pointed out that there are two possible check that limit the growth of population

a. preventive checks: preventive checks are man-made . late marriage avoiding marriages self-rest- raint the etc. are preventive checks. it exercise their influences on the growth of a population by bringing down the birth rate.

b.positive checks:

limitation or criticisms:

1. the actual population has not increased in geometrical progression nor has the food supply in arithmetical Progressive in any country.

2. standard of living you know Advanced countries have actually gone up .

division of labor

specialization was commonly known as division of labour each person doing one job or each region producing only one product is known as division of labour.

advantages of division of labour

1. increase in production

2. increase in skill and dexterity

3. saving in time

4.saving in tools

5.introduction of Machinery

6.advantages of specialization

disadvantages of division of labour

1. monotony of work

2. narrow Outlook of the workers

3. decline in the mobility of Labour

capital

in economics the term Capital refers to that part of man made wealth, which is used for further production of wealth .

characteristics of capital

it is man-made factors of production

Capital has highest mobility of all the factors of production

functions of capital

provision for subsistence

provision for appliances

provision for marketing

provision for raw materials

production function

production function refers to the relationship between the input and the output of a firm.

factors affecting production function

1. size of the firm 2.nature of firms organization 3. relative price of the factors of production

Law of variable proportion or law of diminishing returns

The law of variable proportion is also called The Law of returns are the law of diminishing returns are the law of diminishing marginal productivity are the law of non-proportional returns.

There are three phases for the law of variable proportions

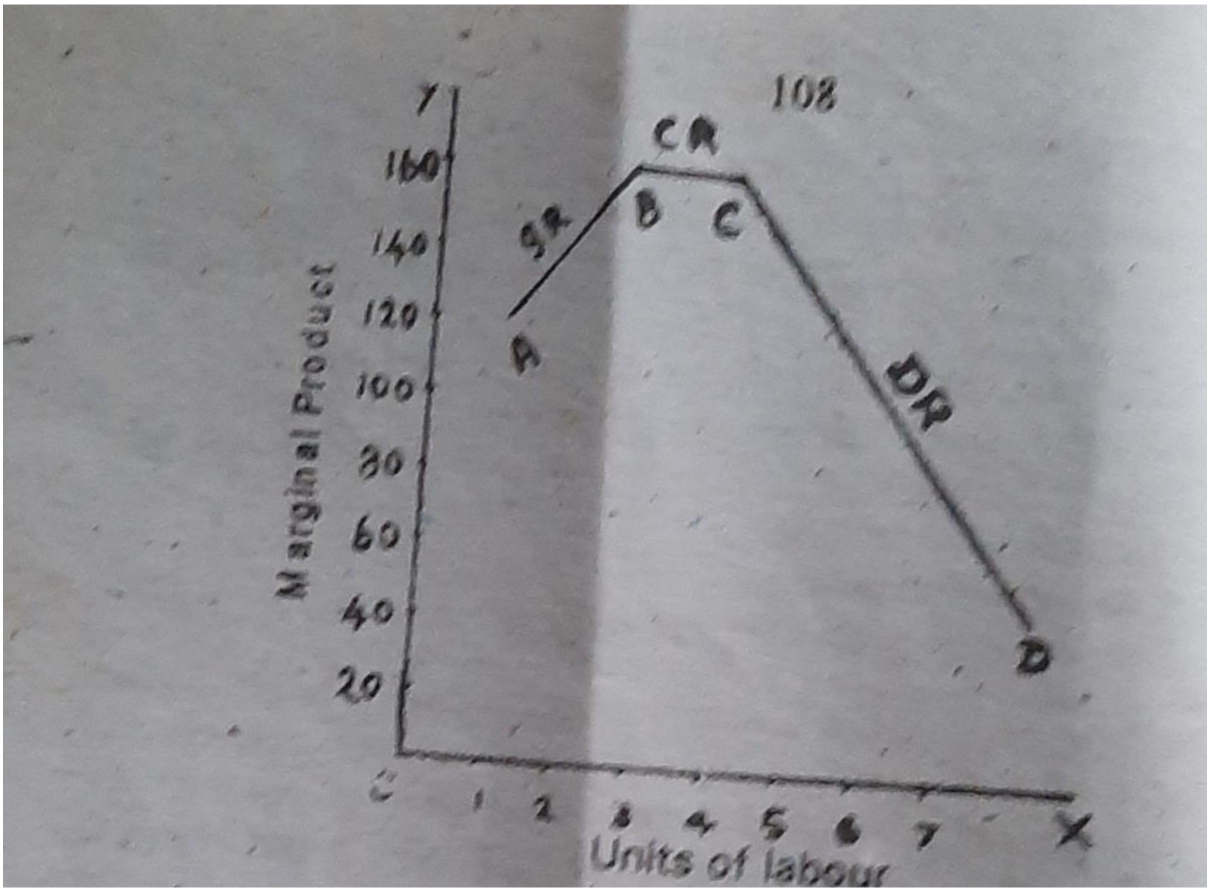
1. the law of increasing Returns
2. the law of constant Returns
3. the law of diminishing returns

Assumption of the law of variable proportion

1. Only one factor is variable others are constant
2. All the factors are homogeneous in character

Variable proportion can be easily explained by the table and diagram

Production increases more than proportionately (law of increasing returns) in the same proportion (constant returns) and less than proportionately (diminishing returns).



A successive doses of Labour are employed in 20 acres of land marginal product increase in the beginning but after this marginal product begin to diminish.

In this diagram AD curve has three parts . from A to B marginal product increase (law of increasing returns) from B to C marginal product remains constant (constant returns)and from C to D curve therefore   represents the three phases of the law of variable proportion .

REFERANCE BOOKS

1. G.SADAKOBAN – BUSINESS ECONOMICS
2. DR.RADHA   - BUSINESS ECONOMICS

BUSINESS ECONOMICS

CODE:18K1COAC01

UNIT 3, 4 & 5

Market Structure

1. **What is Market ? what factors do determine its size?**

   In economics, it refers to a particular commodity and also buyers and sellers of that commodity . for example the wheat Market, the tea market etc.,

   The key element in the structure of Market is the buyers, sellers and nature of competition.

   In short Market consists of the whole region in which buyers and sellers are in contact with one another .

   Benham Defines Market as any area over which buyers and sellers are in such close touch with one another yeah they're directly are dealers that the prices prevalent in one part of the market affect the prices in the other parts.

Classification of Market

On the basis of size the market may be classified into local, National and international markets . on the basis of competition the market may be classified into four perfect competition and imperfect competition. Imperfect competition is further classified into Monopoly, oligopoly monopolistic competition extra .

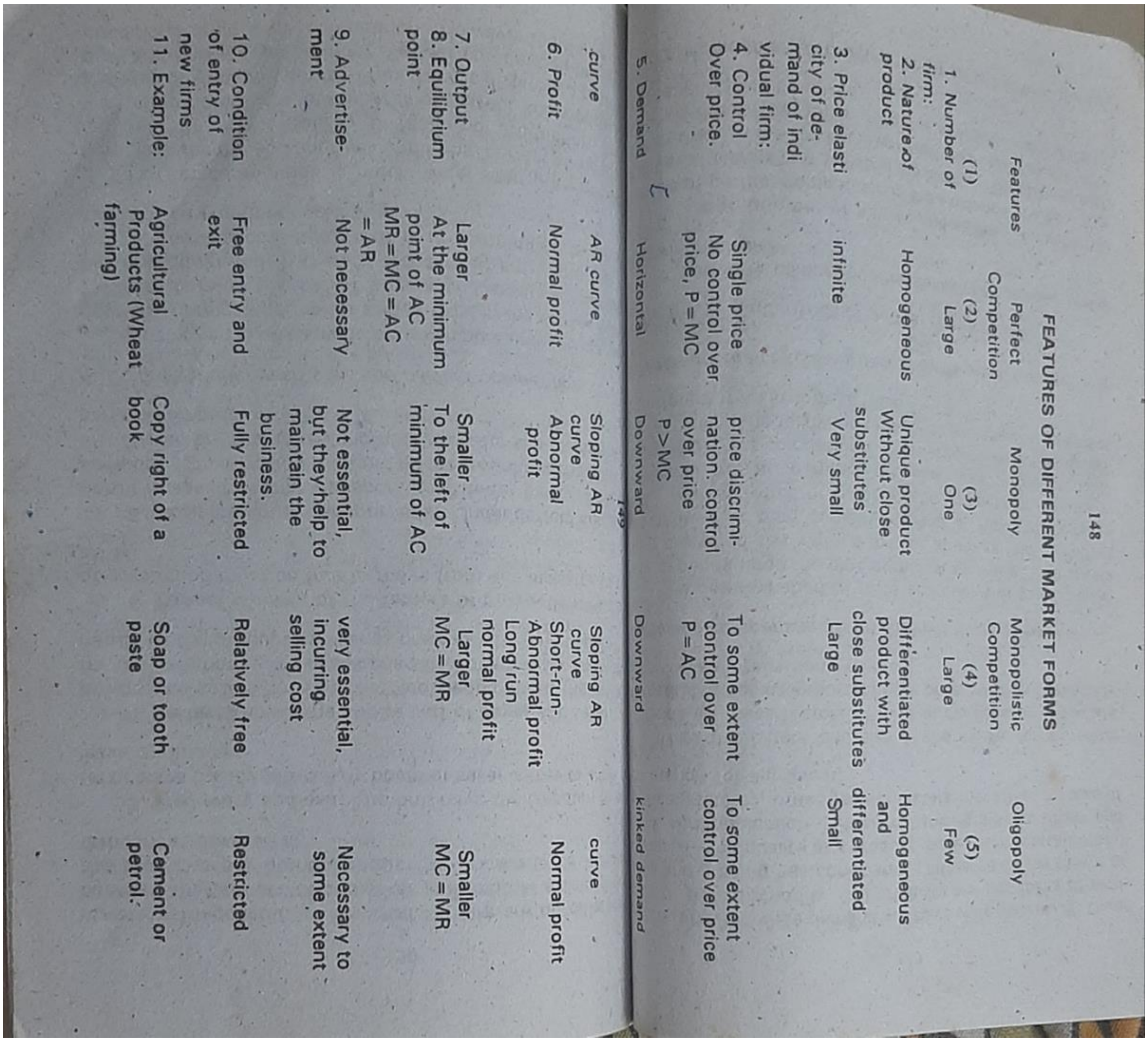
Size of the market are extent of a market

The size of Market at differs with the different, the Commodities. The following factors determine the size of market for a product.

1. Nature of demand .
2. Durability of the commodity
3. Portability and possibility of sampling and the grading has considerable influence on the extent of Market
4. The quality of a product Speedy Transportation on the quick communication .

2. **Make a comparison of the different forms of Market**

The determination of price and output of various products depends upon the type of Market structure. Economists have classified the various markets into i)perfect competition or pure competition and ii)imperfect competition



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FEATURES OF DIFFERENT MARKET FORMS

Features (1)	Perfect Competition (2)	Monopoly (3)	Monopolistic Competition (4)	Oligopoly (5)
1. Number of firm:	Large	One	Large	Few
2. Nature of product	Homogeneous	Unique product Without close substitutes	Differentiated product with close substitutes	Homogeneous and differentiated
3. Price elasticity of demand of individual firm:	infinite	Very small	Large	Small
4. Control Over price.	Single price No control over price, P=MC	price discrimination. control over price P>MC	To some extent control over P=AC	To some extent control over price
5. Demand curve	Horizontal AR curve	Downward Sloping AR curve	Downward Sloping AR curve	kinked demand curve
6. Profit	Normal profit	Abnormal profit	Short-run-Abnormal profit Long run normal profit	Normal profit
7. Output	Larger	Smaller	Larger	Smaller
8. Equilibrium point	At the minimum point of AC MR=MC=AC =AR	To the left of minimum of AC	MC=MR	MC=MR
9. Advertisement	Not necessary	Not essential, but they help to maintain the business.	very essential, incurring selling cost	Necessary to some extent
10. Condition of entry of new firms	Free entry and exit	Fully restricted	Relatively free	Restricted
11. Example:	Agricultural Products (Wheat farming)	Copy right of a book	Soap or tooth paste	Cement or petrol.

3. State the characteristics of perfect competition ?

A perfectly competitive market is characterized by the following features .

1. Large number of buyers and sellers :

   An important features of perfect competition is the existence of a very large number of buyers and sellers in the market .

2. Homogeneous product : the products sold by the sellers are homogeneous or identical.
3. Free entry and exit : The firm have the freedom to he enter or leave the industry.
4. Perfect knowledge on the part of buyer and seller: all the buyers and sellers have perfect knowledge about the market for the commodity.
5. Perfect mobility of the factor of production: factors of production must be free to move from one industry to another .
6. Absence of the transport cost : under perfect competition it is assumed that transport cars to do not exist.

4. Distinguish between pure and perfect competition.

Pure competition is said to exist in the market where i) there is large number of buyers and sellers ii) homogeneous product and iii) there is freedom of entry and exit for firms. The essential future of pure competition is the absence of any Monopoly element.

Perfect competition is much wider than pure competition. besides the above three conditions , perfect competition requires iv)perfect mobility of factors of production v) full and unrestricted competition and vi) perfect knowledge and absence of Transport costs. That's that is he a distinction between pure and perfect competition perfect condition has more conditions than pure competition . pure competition and perfect competition are interchangeable used.

4.**What are the evils of Monopoly ? or state the futures of Monopoly condition**

1. single seller : there is only one seller for the commodity and large number of buyers.
2. no close substitutes

3.discriminating Monopoly .

4. monopolist prevent others from entering the industry

5. there is no distinction between the firm of Industry. The firm and industry are one and the same thing.

Evil of Monopoly :

- Monopolist restricts output.

- Monopolist often charges high price.
- Monopoly leads to concentration of wealth in the hands of monopolist.
- Monopolist do not care to improve the quality of the product,
- Factors of production are paid less under monopoly.
- Monopolists resorts to wrong practices to prevent the entry of new firms with a view to establish absolute monopoly power.

5.What are the aims or objectives of business firms?

1. Aims of business firms - profit maximization : it is commonly assumed in price Theory the sole objective of a firm is to get maximum profits. The phone's always aims to maximise its profit.

   According to Lipsey "all decision are taken not up to achieve the common goal of maximizing the firm profits".

   A firm will go on increasing its output and thereby increasing its profits. Profits is the difference between total revenue (TR) and total cost (TC). The phone will be getting maximum profit at the level of output where the difference between total revenue and total cost is the greatest .

   According to Stonier and Hague, "A firm will be in equilibrium when your MR=MC , for it will then be earning maximum profits. The original entrepreneur will therefore fix his output so as to equate marginal revenue and marginal cost".
2. Sales maximization: Baumol says that firms are in interested in maximizing their sales revenue that is sales maximisation.
3. Satisfying Behaviour: the firms work for profits that are satisfactory rather than maximum.
4. Secure Profits: Rothchild says that the oligopolistic firm is interested in Secure profit (not maximum).
5. Other objectives: business firms have are there pools and objectives to promote other than profit maximization. they are a) welfare of the employees b) welfare activities to the society c)maintaining or increasing market shares d) growing for the sake of growing e) creating or maintaining are desirable Public Image f) maintaining a desirable financial position g) achieving good Labour Relations h) fulfilling social responsibilities and so on .
6. How does the firms determine the equilibrium output ?

   A firm can be defined as the unit that takes decisions with respect to production and sales of commodities.

   The word firm is used to denote a particular production unit or trading concern. The term industry includes all firms producing Commodities easily substitutable for one another. Example cotton textile industry.

1. Equilibrium of the firm: equilibrium means a stage of no change. Whenever an economic unit attains a position from which it does not like to change, it is said to be in equilibrium.
2. Profit maximization: (TR and TC) it is commonly assumed in price theory that the sole objectives of a firm is to get maximum profits.

   A firm will go on increasing its output and thereby increasing its profits. Profit is the difference between total revenue and total cost . A firm will be getting maximum profits at the level of output where the difference between total revenue and total cost is the greatest.

   MR=MC: according to stonier and Hague, "A firm will be in equilibrium when MR is equal to MC for it will then be earning maximum profits.

7. How is price determined under perfect competition ?

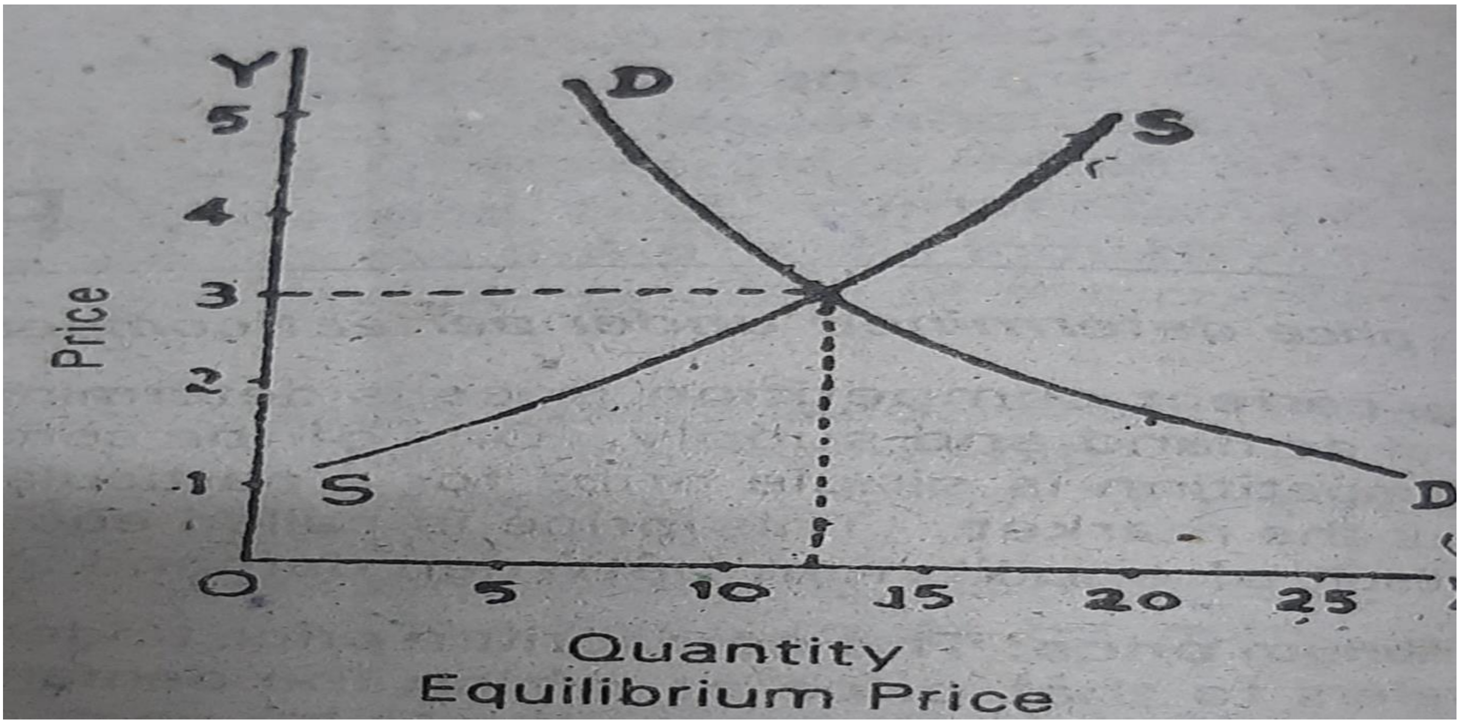
   Under perfect competition price is determined by the interaction of demand and supply. One of the conditions in the perfect competition is single price for a particular commodity throughout the market. This price is called equilibrium price. It is the result of equilibrium between demand and supply .

   Equilibrium price : the equilibrium price under perfect competition refers to that price at which the demand and supply of the commodity are in equilibrium with each other.

   The following table and figure shows how prices determined by the interaction of demand and supply

rice per kg.	Quantity demanded kgs.	Quantity supplied kgs
5	9	18
4	10	16
3	12	12
2	15	7
1	20	5

The table reveals that as the price falls that demand increases and Supply decreases as the price rises, the demand decreases and Supply increases . these trends are just because of the operation of the law of demand and supply. The demand curve and the Supply curve vary with the price. The demand curve normally slopes downwards. Supply curve normally slopes upwards.



In the figure DD is the demand curve. SS is the supply curve. When the price is Rs.3, 12 kgs are demanded and supplied. The quality demanded is equal to quantity supplied and price Rs.3. therefore it is the equilibrium price .

8. **Analyse the conditions in which the firm and the industry will be in equilibrium in the short and long periods under perfect competition. (OR)**
   Explain profit maximization under competitive conditions.

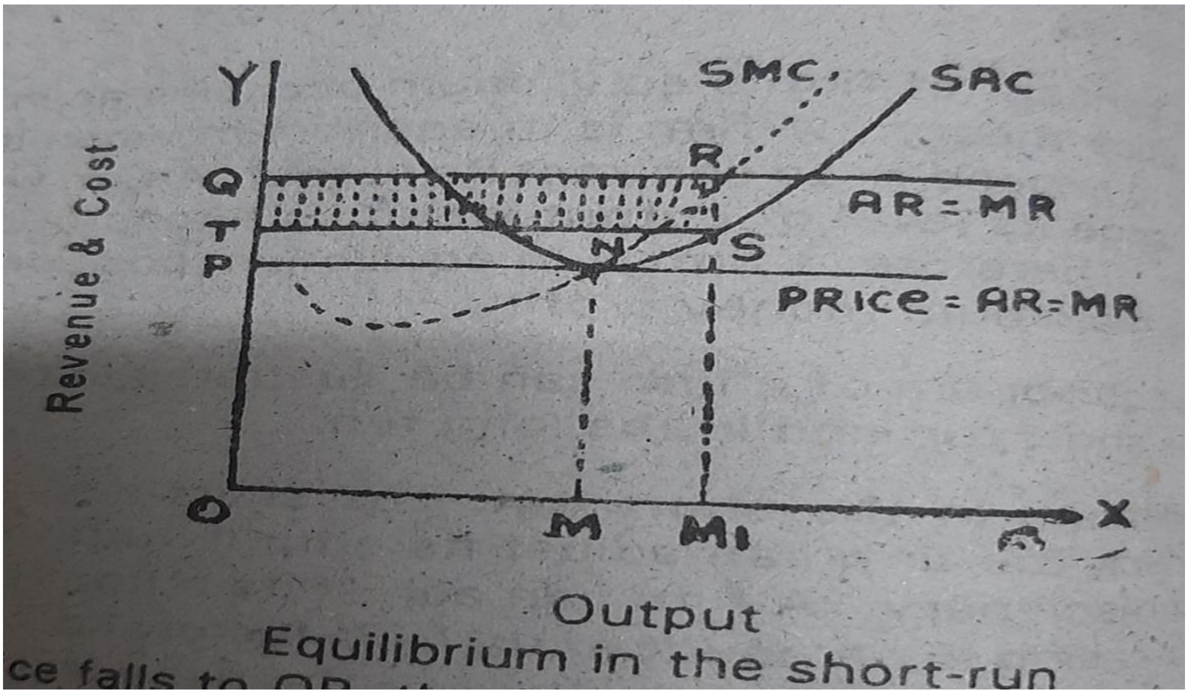
The concept of firm's equilibrium occupies an important place in price Theory. A firm is in equilibrium when it has no incentive to expand or to contract its output . A firm would not lie to change its level of output when its total profit are at maximum.

Equilibrium in the short run: the short run is a period during which the firm can adjust its outwput with the existing plant and machinery. During this period the fixed factors of production cannot be altered, in the short run neither new firms enter the industry nor the existing firms leaves it.

Diagrammatic illustration of short run equilibrium of the firm and industry : under perfect competition for an individual firm the price is given. so the demand or always Robin Yoko is perfectly elastic. it is assumed that all the firms possess identical cost conditions.

The following diagram illustrates the equilibrium in the short run.

In this diagram OX represent the output and OY represents revenue and cost. At the price OQ the firm is in equilibrium at the point R where MR=MC. Now the firm earns super normal profit which is equal to the area QRST. Profit is measured by the difference

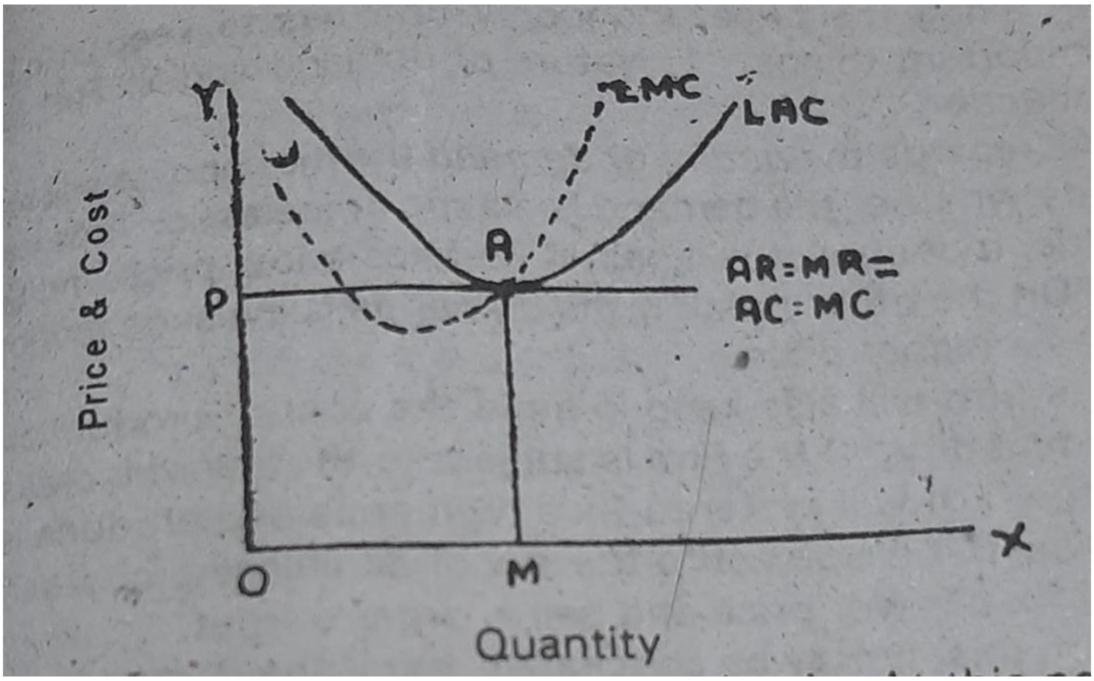


Equilibrium in the short-run

between and the AR and AC.

If price falls to OP, the firms is in equilibrium at point N where MR is equal to MC. Hear the equilibrium price is OP and the equilibrium output is OM.

Equilibrium of the firm and industry in the long run: in the long the firm of able to alter the output by changing the fixed as well as variable factors of production. Father form to achieve equilibrium two conditions must be satisfied 1. Price=marginal cost 2. price=average cost.



The long-run equilibrium of the firm can be Illustrated with the help of diagram . In the diagram x axis denotes the quantity and Y axis denotes price and cost .LAC is the long-run average cost. LMC is the long-run marginal cost . Firm is in equilibrium when it's produced OM output . at this level of firms MR is equal to MC. The LMC curve intersects MR curve at point A. At this point the firms AR is equal to its AC. The firm is earning normal profits. At this equilibrium level, the AR, AC and MC are all equal to each other and also to the price. Thus the normal profit maximizing output is attained when MR = MC =AR=AC. The industry as a whole will also be in equilibrium in this situation. There will be no tendency for any firm to enter or exit the industry from this level.

In the long period under competition output tends to be optimum. So the concept optimum firm is relevent in the long run.

9.Explain the conditions for short run Monopoly equilibrium with the help of a diagram.

Or

How price is determined under Monopoly?

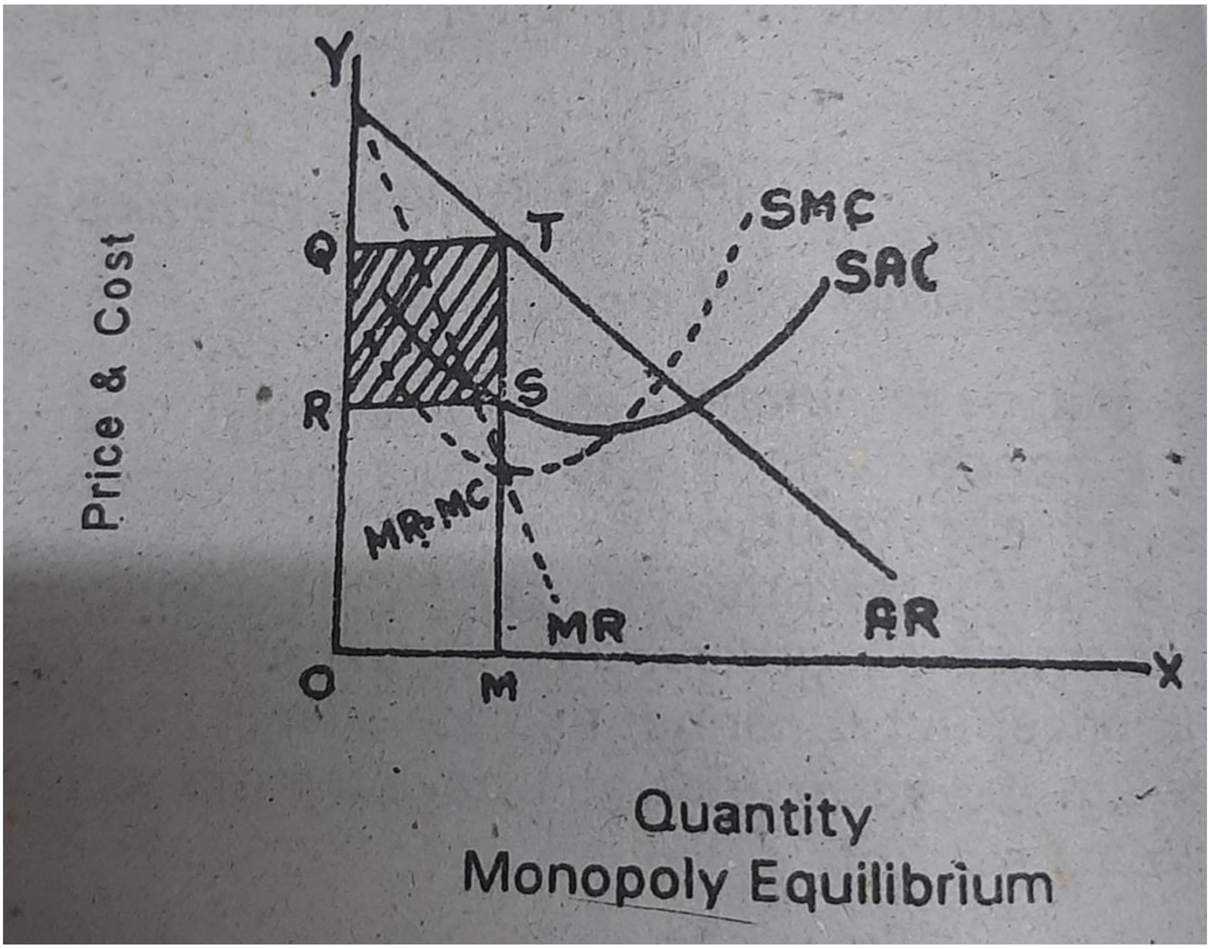
Price output determination under Monopoly : the main objectives of a monopoly firm is to secure maximum profit. The firm can achieve its objective in two alternative ways. The firm can you fix the price or it can fix the quality to be sold to the customers.

In fixing the price Monopoly firm has to keep in mind two important things. 1. Nature of demand and 2. the cost of production.

As regards the nature of demand , if the demand is inelastic monopolist fixes a higher price.

From this it may be concluded that if demand is elastic and the law of diminishing costs operates , the price of the product will be low . on the other hand if the demand is inelastic and the law of increasing cost operates, the price of the product will be high.

Monopoly equilibrium : the Monopoly firm will it attain equilibrium when the MC becomes equal to MR. The demand curve or AR curve is a downward sloping curve. The MR curve lies below the AR curve. The monopolistic fixes his equilibrium output where his MR is equal to the MC.



In the diagram, at the level output of OM, the MR=MC. This is the optimum level of output of a firm. This output will be sold by the firm by TM price. At this price the average revenue is greater than AC. So the firm earn a profit of TS per unit. The total profit of the firm earn is QRST as shown in the diagram. This shaded area represents the maximum profit which the firm can earn by selling its output.

Thus the monopolist will be in equilibrium at output OM, where MR=MC and the profits are the greatest. The above equilibrium analysis applies both to the short run and to the long run.

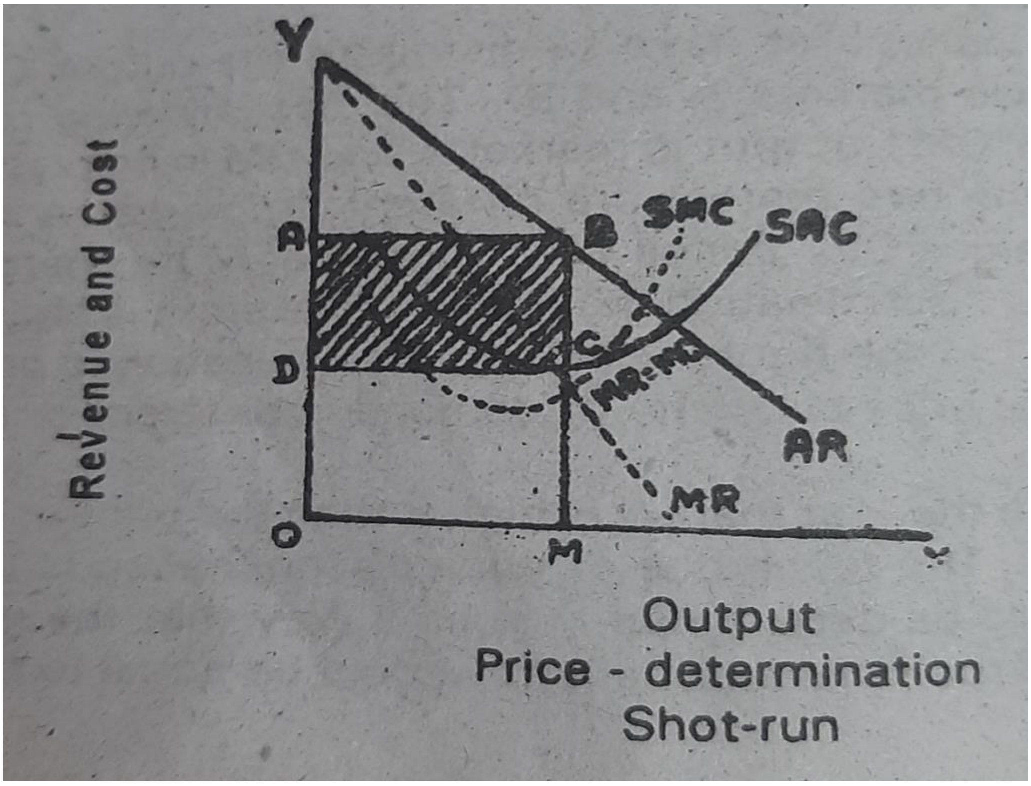
10. How is price determined under monopolistic competition?

Price determination under monopolistic competition short run equilibrium :

Under monopolistic competition different firms produced a different varieties of product. Each firm will fix price and output of its own product. Price determination can be shown through a diagram with the help of Revenue on Cost curves.

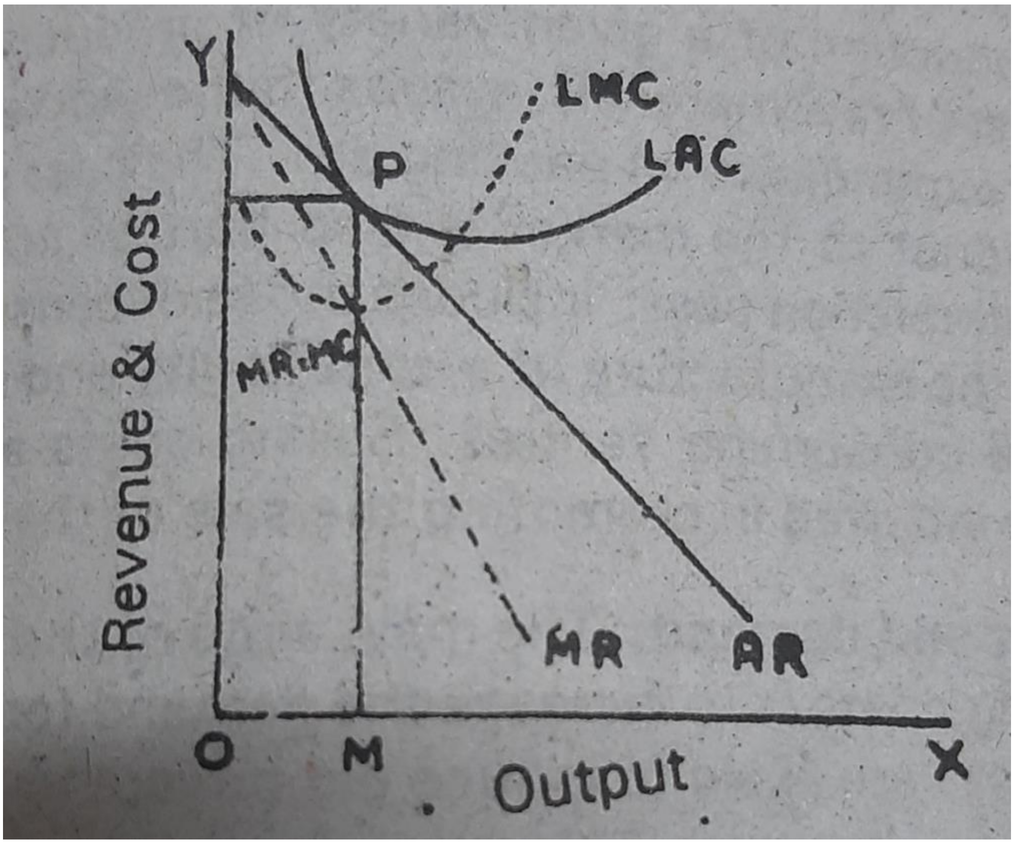
In the diagram AR average revenue Curve MR is the marginal revenue curve. SAC is the short run average cost curve . yes SMC is the short run marginal curve. The firms is in equilibrium where MR is equal to MC. OM is the equilibrium output and OA is the profit-maximizing price, the phone is yearning supernormal profit as indicated by the shorter the area of ABCD .

Monopolistic competition consists of several firms . the cost of various forms may be different. Therefore in the short run it is impossible for some firms to earn abnormal profits, for some to earn normal profits, while some may incur lossess. When the average revenue



is greater than average cost the firm is getting normal profits. When average revenue is equal to average cost the firm is getting normal profits. When average revenue is less than average cost the firm may incur loss.

Long run equilibrium : in the long run under monopolistic competition every firm will earn only normal profit. Supernormal profit or lossess will be competed away since that is free entry and exit of firms. Equilibrium is attained when MR is equal to MC; AR=AC. This has been Illustrated in the diagram .



In this diagram LMC and LAC are long period Average and marginal revenue curve. AR and MR are average and marginal revenue curve. In the figure AR is tangent to the AC curve at point P. The equilibrium output is OM and the price is OP1. It is clear that the firm earns only normal profits in the long run. All the firms in the group are also in equilibrium. This is called group equilibrium .

What is a oligopoly? what are the types of oligopoly ?

Oligopoly refers to a market in which there are few sellers. Prof. Stigler " situation in which firm bases is Market policy in the part of the expected behaviour of few close rivals".

Oligopoly is also termed as competition among the few. The best examples of oligopoly are markets for petroleum cigarettes etc. Most writers considered duopoly and oligopoly as the same . duopoly means just two sellers. since the nature of oligopoly problem and the nature of the duopoly problem are the same they have been considered together . duopoly models can also be taken as a oligopoly models .

Types of oligopoly: there are different types of oligopoly

1.Pure and differentiated oligopoly : oligopoly is said to be pure or perfect on the basis of product differentiation . in the case of pure oligopoly are the producers produce identical product . Stonie and Hague call pure oligopoly as oligopoly without product differentiation .

2. conclusive and not conclusive oligopoly : Nick inclusive oligopoly refers to the market situation where the phones combined together to fix the price and output of the industry . non conclusive oligopoly denotes lack of any understanding of agreement among firms. This classification is done on the basis of agreement or understanding among the firms.

3. open and close to oligopoly: an open a oligopoly refers to the market in a situation where the new firm are free to enter the industry. They closed the oligopoly refers to the market situation where the new firms are not allowed to enter the industry . the classification is done on the basis of freedom to enter the industry .

4. Partial and full oligopoly : partial oligopoly refers to the market situation where the industry is dominated by one large form which is considered as the leader of the group .

5. syndicated and organized a oligopoly : syndicated oligopoly refers to the situation where the firm sells their products through a centralized syndicate . organised oligopoly refers to a situation where the firms organize themselves into Central Association for fixing price output quotas etc.,

11. critically examine the marginal productivity theory of distribution . or

Explain the assumptions underlying the marginal productivity Theory .

And the marginal productivity theory of distribution attempts to explain how the income of a factor of production is determined. Theory was developed by JB Clarke wicksteed and the others during the 19th century. It was then popularized by Marshall and JR Hicks.

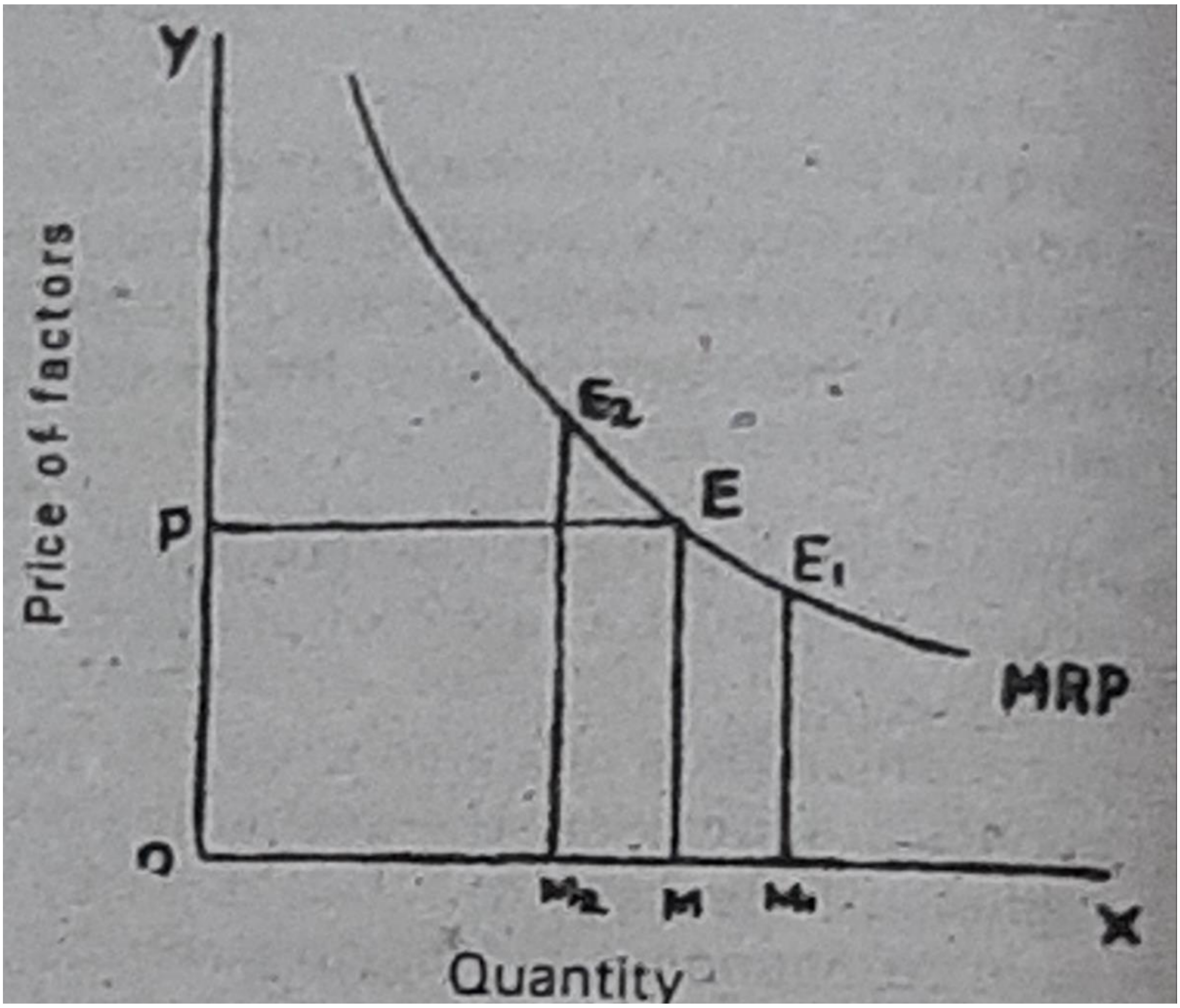
Marginal productivity theory of distribution

Producer employers are factor of production because of its productivity.

The price of which he is prepared to pay for that factor will depend upon its productivity. the greater the productivity of a Factor higher will be price. this is based on the common experience. The economists used this common experience and formed the marginal productivity theory of distribution. The marginal productivity theory of distribution states that the income of factor of production tends to equal to its marginal product.

The assumptions of the marginal productivity Theory is based on large number of assumptions: they are ,

1. Theory assume that there is perfect competition in the product and factor market .
2. It assumes that all units of the factor of production are homogeneous and perfect substituter for one another.
3. Theory assumes that there is full employment in the economy
4. The theory assumes that the factors of production are perfectly mobile. Theory: based on these assumptions the marginal productivity theory of distribution is explained. The marginal productivity Theory simply states, “that the price of a factor of production will tend to settle at the level of its marginal productivity”. generally this theory is used to explain the determination of wages in the labour market. But it is a general theory of distribution.



Theory of marginal productivity can be Illustrated with the help of diagram .

Here the MRP is the marginal productivity curve at OP price the quantity of factory employed is OM because at the level of employment marginal productivity is equal to price. If less factors are employed the marginal product E2 M2 is more than the price. So more factors will be employed till at OM1 when marginal revenue productivity is equal to price.

Therefore it is clear that the price of factor of production will tend to settle at the level of marginal productivity. Thus the marginal productivity theory of distribution states, that the price of a factor will be determined by marginal productivity.

Criticism of the theory

1. The assumptions of perfect competition in the product and factor market is unreal . today almost all markets are imperfect .
2. The assumptions all units of a factors of production are homogeneous and perfectly substitutable for one another is unbelievable. It is reasonable to say that all men are equally efficient.

Thus the marginal productivity theory is based on certain unreal assumptions. It is also inadequate to deal with their pricing of factors of production.

11. **Distinguish between gross interest and net interest.**

Gross and net interest : distinction is often made in economics between pure or net interest and gross interest. Pure interest is the payment for the use of capital alone. Gross interest includes several other items besides pure interest. The other items that are included in Grass interest are as follows .

5. Payment for risk : the lender has to face the risk of loss of capital . that is some of the borrowers may prove to be dishonest. To compensate for such possible losses the lender May charge and somethings over and above pure interest.
6. Payment for inconvenience: A lender has to face a good deal of inconvenience when leading money to a party . for example if the lender lends money during this. His money becomes locked up for a fixed period. He therefore compensates himself to this inconvenience by adding one or two percent to the net interest .
7. Reward for management : every lender has to incur some expenditure on the management of the loan .

12. explain the theories of interest (or) explain why interest is paid .

(Or)

Discuss the time difference theory of interest by Iriving Fisher.

Interesting theories explain why interest is paid? and how interest rates gets determined? The abstinence theory of Interest the waiting theory of interest and the time preference theory of Interest explain why interest is to be paid? They do not give you anything about how interest rates gets determined . the classical saving investment Theory, loanable fund Theory and Keynes liquidity preference theory explain not only why interest is to paid but also how interest rate gets determined .

1. The productivity theory of Interest : the contributor of this theory was the physiorcats.

   According to it, interest is paid because capital is productivity. Capital is used up to the point where the value of its output is equal to the current rate of interest .

2. Abstinence theory of Interest : this theory was expounded by senior . according to it, interest is paid as a reward for abstaining from consumption as part of the present income earned. To abstain from consumption involves sacrifice and interest is the payment for inducing such sacrifice .

   Marshall has improved seniors Theory . Marshalls refinement of seniors theory is popularly known as the waiting area of Interest .

2.a) waiting theory of Interest : Marshall has substituted the concept of waiting in the place of the concept of abstinence . according to him lending involving waiting. One who lends has to wait till such time the money borrowed is returned. Marshall precedes one step further. He says that waiting is a feature of any productive activity. The farmer cultivating land lands has to wait till the Harvest time. For anyone engaged in the production of any commodity there is a period of waiting. So Marshall says, that waiting is a separate factor of production. As a factor of production waiting is eligible for the reward, the reward payable to waiting is interest.

Criticism of the theory : the main criticism against the theory is that savings to not always involve suffering. Savings are made both by the rich and the poor. When a rich man saves there is no suffering or a abstinence on his part. Further it is a negative theory.

3. Agio theory of Interest: the Agio theory worked out by Bohm Bawerk he explains that interest is paid because of the Agio or premium placed by people on present Goods over future goods.

   Criticism : this theory is criticized on the grounds that it explains why Capital has a supply price but does not explain why capital is demanded. In short the demand side of the capital is ignored it is therefore a one sided Theory.

4. time preference theory of Interest: Fisher explains that the present satisfaction is considered superior to the Future satisfaction. it is because the tendency that man has to be enjoy the present satisfaction better than the future. this is tendency to called time preference.

There is a relation relationship between time preference and rate of interest if the rate of rate of time preference is higher than the rate of interest money would be borrowed for present consumption. It is lower money could be lent.

Criticism : there are two major difference in time preference Theory

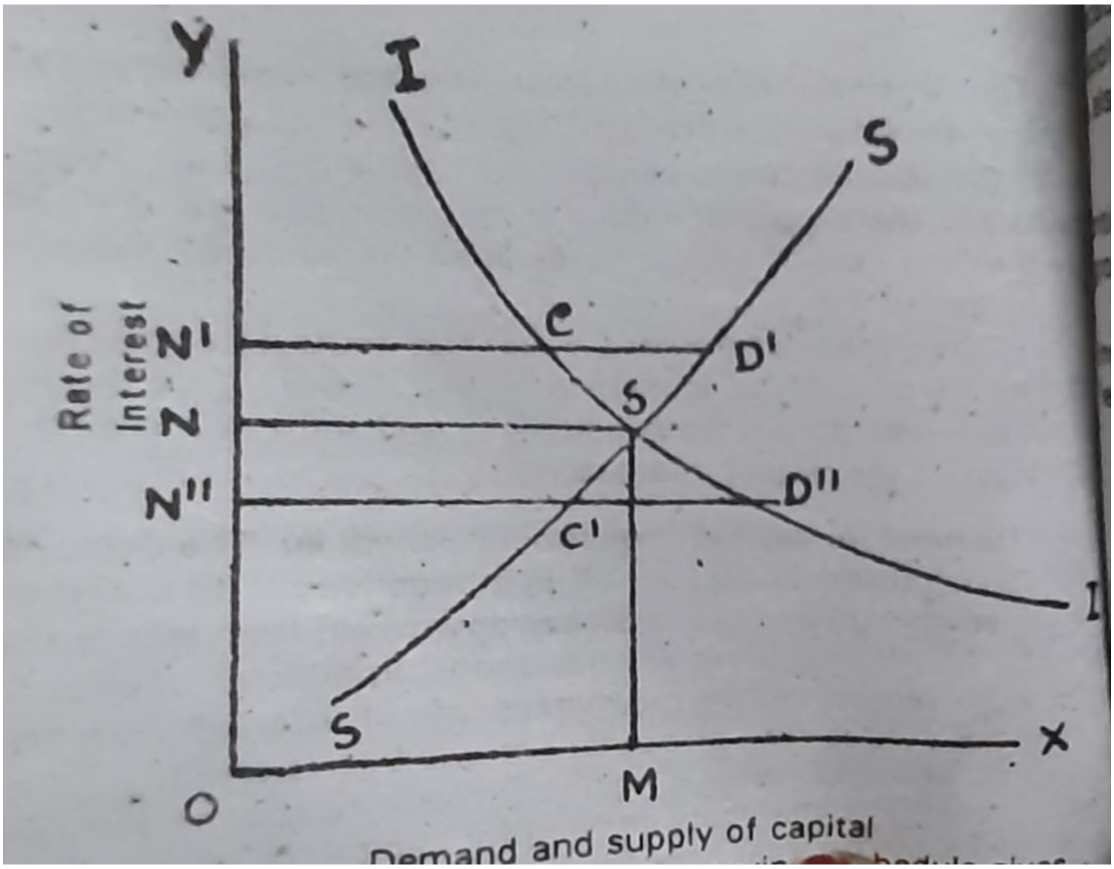
a. It takes into account only the supply of capital, ignoring the demand side.
b. Liquidity in the determination of Interest the main source of capital to business man in his Banks. Banks do not have time for preference. But they have liquidity preference .

13. critically examine the theory of Interest which tells that the rate of interest is determined by demand for and supply of capital .

The classical theory of Interest : the rate of interest settles at the point where the demand for capital is equal to the supply of capital. since the demand for Capital arises for investment and the supply of capital comes from savings. we can say that the rate of capital determined, the reality by savings and Investments.

Demand for Capital : the demand for Capital arises on account of its productivity. The marginal productivity curve of capital slopes downward from left to the right . an individual firm will decide the amount of capital to be employed compare the market rate of interest with the marginal productivity of capital. it will use that amount of capital, where is marginal productivity equal the market rate of interest. The aggregate demand for Capital will slope downwards to the right as shown in the diagram. The II curve is the aggregate investment demand curve.

Supply of capital: supply of capital come from the savings of the people. Other things remaining unchanged savings of people are related to the rate of interest. If rate of interest is high savings of people will tend to be high, rate of interest low, Savings of people will tend to be low. On the other words there is a positive or direct relationship between rate of interest on volume of savings. As the volume of savings is positively related to the rate of interest the Supply Curve of capital or the savings curve slopes upwards from left to right.



Interest rate determination : the saving schedule gives us a picture of what tends to happen to the supply side of the market for capital investment. The investment schedule give us a picture of what tends to happen at the demand side of the market for Capital. the equilibrium rate of interest gets determined at the point where the saving schedule cuts the investment schedule. In other words the equilibrium rate of Interest gets determined at the point where supply of capital equals demand for Capital as in the above diagram. This is the classical theory of Interest which is also known as demand and Supply theory of Interest .

Criticism of the theory: Keynes has been a prominent the critic of this theory. he had criticized this theory of several grounds .

1. As a pointed by keynes, the equality between savings and investment was brought about the about by the changes in the level of income and not by the rate of interest.
2. To Keynes investment may not be interested elastic as suggested by the classical Theory .
3. Keynes objected the classical theory of ground that it was determining the rate of interest is determined according to this Theory by the demand and supply of capital the supply of Captain various with a gender level of income .

   Conclusion in view of this inherent defect and serious shortcoming in the classical Theory it stands deject depressant the generally acceptable explanation in the interest rate determination at present is the liquidity preference theory of JM Keynes .

14.Discuss the loanable funds theory of Interest .

Loanable funds theory of Interest : according to this Theory, the rate of interest is determined by the demand for and supply of loanable funds. The loanable funds Theory takes into account the role of credit and hoarding , I'm that considers the rate of interest to be the function of 4 variables – savings (S), investment (i) and the desire to hoard(L) and the amount of money (M) it is expressed as : r(f) (S .I. L.M).

Supply of loanable funds : the supply of loanable funds comes from basic resources namely Savings, dishoarding Bank credit and disinvestment.

1. Savings one source of supply of loanable funds is saving. Saving of people are positively related to interest rate. That is people save more at a higher rate of interest than at a lower rate of interest. Hence the savings curve will tend to slope upwards.
2. Another source of supply of loanable fund is dishoarding of money from past Savings dishoarding is also positively related to the rate of interest.
3. Did the another source of supply of loanable funds he's banking predicted the Commercial Bank tends to create more credict when the rate of interest is decreasing.

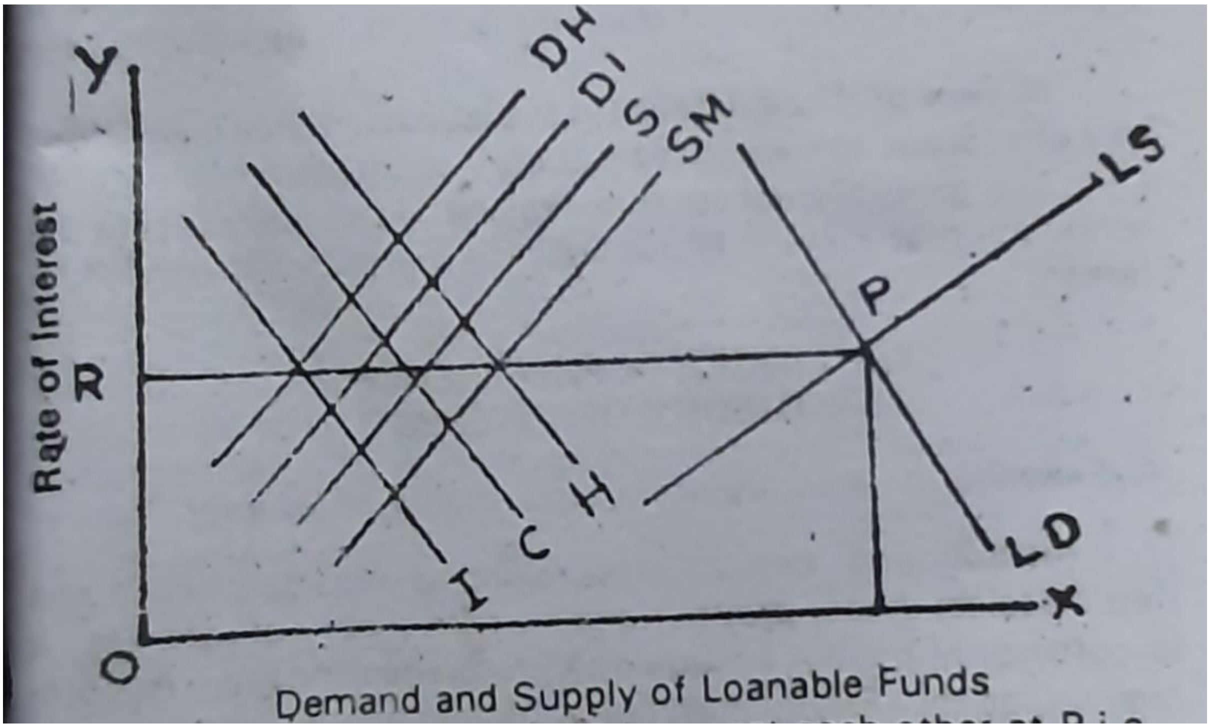
4. Loanable funds are also supplied sometime through disinvestment. It takes place when due to structural changes the existing stock of Capital Equipment is allowed to wear out without being replaced.

   By adding together these different sources of Supply loanable funds, we can get the total supply of loanable funds. The supply of loanable funds, is positively related to the rate of interest and hence, the supply curve of loanable funds is upward slopping. In the figure is given below, the curve denoted by the letters LS is this supply curve of loanable funds.

   Demand for loanable funds : the demand for loanable funds comes from three sources .

   1. Investment : the major part of the demand for loanable funds comes from business houses which borrow founds for various business purposes like purchase of raw materials, Capital Equipment, or building up investment.
   2. Consumption : out of the major sources source of demand for loanable funds comes the from that consumers who want to borrow funds for consumption purposes .
   3. Hoarding : lastly the demand for such funds has come from those who want to hoard money. At a higher rate of interest people will hoard or hold less money because much will be lent to take advantages of the higher interest rates .

      Interest rate determination : the supply of loanable funds gives us a picture of what tends to happen at the supply side of the market for loanable funds. The demand curve of loanable funds gives us a picture of what tends to happen at the demand side of the market for loanable funds. The equilibrium interest rate gets determined at the point of where the Supply Curve cuts the demand curve. In other words the equilibrium rate of interest rate determined at the point where the supply of loanable funds equal demand for loanable funds.



Both the curve LS and LD in the intersect each other at the p i.e. at the rate of interest rate War at this rate of interest to the loanable funds lent or supplied and the loanable funds borrowed or demanded are equal. Hence OR is the equilibrium interest rate which will tend to Prevail in the loan Market.

Criticisms : the neo-classical theory was subject to criticism Keynes and others.

1. It is pointed out that the neoclassical writers have only sought to differentiate between loanable funds and savings .
2. It is pointed out that the loanable funds theory is like the classical Theory determinate.

   The generally acceptable explanation of rate of interest determination at present is the liquidity preference theory of Interest.

14. **examine the liquidity different theory of Interest.**

Introduction : Keynes after rejecting classical Theory and neoclassical Theory propounded his own theory of Interest. It is commonly known as liquidity preference Theory. According to liquidity preference Theory " interest is the reward for parting with liquidity for specifie period.

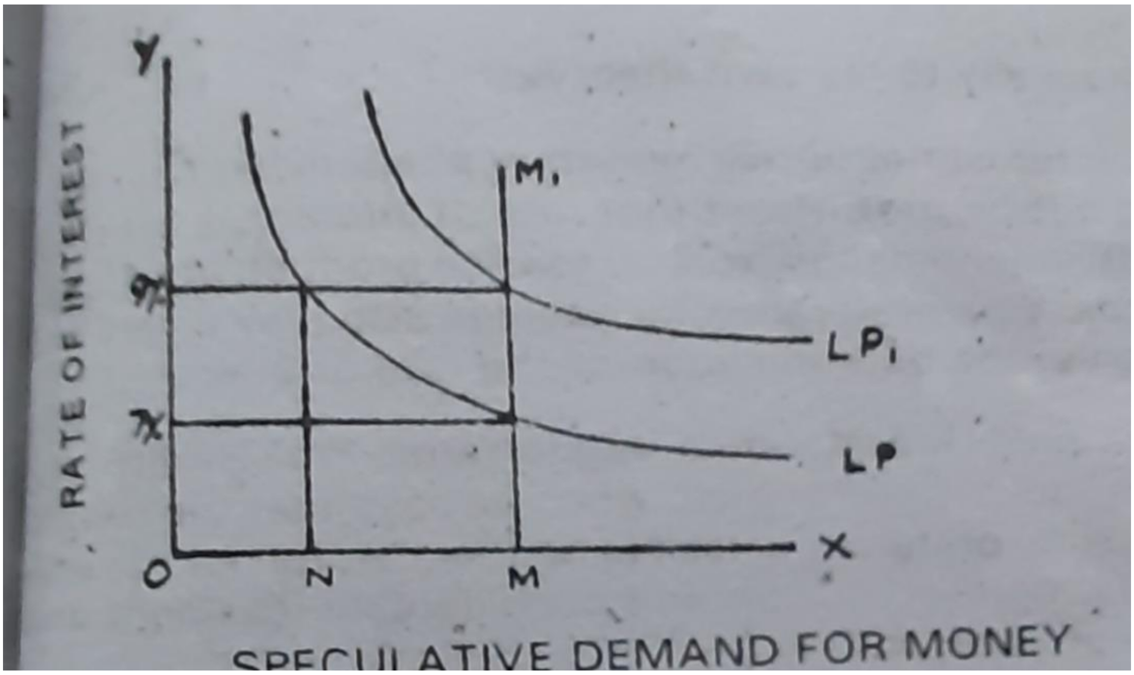
Liquidity preference Theory : according to Keynes interest is purely a monetary Phenomenon. Keynes defines interest as the reward paid for parting with the liquidity for a specified time . money is the most ridiculous asset and people generally like to keep this assets in cash. Therefore if they are asked to surrender this liquidity they must be paid reward. Keynes says that people desire to hold cash for the following motives.

1. The transaction motive: the transaction motive relates to the need for money for the current transaction of individual holds cash in order to reach the interval between the receipt of income and expenditure .
2. The precautionary motive: people hold part of the income as cash in their hand in order to meet any unexpected emergencies . they hold more money because they want to take proper precautions against unforeseen future like a sickness unemployment accident old age extra. The amount of money which people want to hold it depends upon individuals income and business activities .
3. The speculative motive: people holding cats receivers in order to take the advantages of Market Behaviour people hold money to purchase assets in anticipation of rise in their prices in the future. Keynes says that the object in view is to secure profit from knowing better than the market, what the future may bring forth.

   Supply of money and rate of interest: supply of money is another Factor determining the equilibrium rate of interest . supply of money comes from two different sources viz. The government and the banking system. Keynes assumes money supply in the short period remain unchanged. The Keynes rules out the possibility of any casual connection between interest and money supply in the short period.

Determination of rate of interest : according to this Theory the rate of interest is determined by the supply and demand for money. On the demand-side that is liquidity preference and on the supply side there is the total amount of money . equilibrium rate of interest is established at the point of intersection between the supply of money and the liquidity preference .

In the diagram the supply of money is indicated by the vertical straight line parallel of Y axis,(MM1). The liquidity preference can be represent by the downward-slopping curve LP. It shows the functional relationship between the rate of interest and the amount of money people desire to hold . in the figure LP intersect MM1 at 7 % the liquidity preference and the supply of money intersects. So the equilibrium rate of interest is 7% where demand for money and the supply of money are equal .



The following diagram illustrates this

If the liquidity preference changes to LP1 money supply remaining constant the rate of interest will rise to 9% so if the supply remains constant and the people's liquidity preference increases the rate of interest would rise.

Features of the theory: Keynes liquidity preference Theory I'll be interested in is the most accetable modern explanation of interest rate determination. The reasons are as follows

1. In the actual World rate of interest is your monetary phenomenon and not real phenomenon

2. The other theories of Interest are parts of only micro economics. Where as Keynes interest theory is not only a part of modern micro economics, but also an integral part of modern macroeconomics.

Criticism :

1.prof.Hansen aptly remarks the Keynesian theory of Interest suffers from the same fundamental flaw as the classical Theory .

2. interest not purely monetary phenomenon: it has been pointed out by Professor Hazlit that rate of interest is not purely monetary phenomenon, real forces like productivity of capital, thriftness time preference for savings also play a very significant part in the determination of the rate of interest .

3. liquidity preference vague term: Professor Hazlit objects the term liquidity preference,

4.Narrow version: in actual practice liquidity arses is not only an account of three motives as considered by Keynes.

15. what is the difference between gross and net profit ?

Meaning of profit:

profit is said to be the reward for the entrepreneur. It is the remuneration for the four factor of production namely Enterprise. Prof.Taussig says, " it is the mixed and vexed income". It is mixed income because it is made up the number of sources and vexed because economists unable to give a proper idea. Even now it remains one of the least satisfactory parts of economic doctrine.

1. Gross profit and net profit :
   Profit is the income received by the organizer or entrepreneur. In ordinary sense, a profit is equal to difference between total revenue and total cost of production. There are two types of costs, 1.Factors supplied from outside are explicit costs or paid out cost 2.Factors supplied by the organizer himself are implicit cost. Gross profit = total revenue - total explicit cost.

   The organization should be included in his cost. a) wages for his own labour b)interest for his own Capital c)rent for his own land d) depreciation of machinery etc., these costs are implicit cost and they should be deducted from gross profits the balance or Surplus is known ad Net profit or pure profit. Net profit is equal to total revenue - total explicit cost + total implicit cost.
2. Normal profit and supernormal profit : normal profit may be defined as the profit is the minimum necessary to induce the entrepreneur to remind and

work in the business. This may be termed as they return for the entrepreneur for organizing, managing, risk-taking etc.

Super normal profit is returnable the normal profits. It is excess profit which may be termed as residual Surplus. unlike a normal profit the existence of super normal profit is not pre-requisite for the existence of the firm.

Net profit= Normal profit+super normal profit.

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