CHAPTER 1 : DEMAND

Desire + ability to pay+Willing to buy = Demand

Determinants of demand

4Price of commodity*(P↑↓-D↓↑)*
4Price of related commodities:
- Substitutes *(P↑↓-D↑↓)*
- Complementaries *(P↑↓-D↓↑)*

4Income of consumers (I↑↓-*D*↑↓)
4Tastes & Preferences of Consumers*(Fav-D↑,Unfav-D↓)*
4Population*(Pop↑-D↑,Pop↓-D↓)*
4Climate & Weather *(Fav-D↑,Unfav-D↓)*
4Gov't Policies*(Fav-D↑,Unfav-D↓)*
4Expectations about future prices

Types of Demand

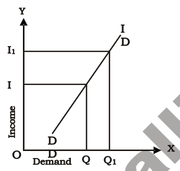
Price demand

Price	Demand
↑↓	↑↓

Income demand

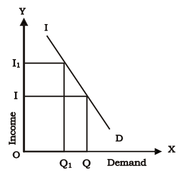
Superior goods

Income	Demand
↑↓	↑↓



Inferior goods

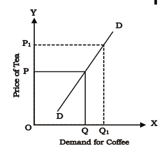
Income	Demand
↑↓	↓↑



Cross demand

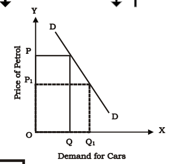
Substitutes

Price of Tea	Demand for coffee
↑↓	↑↓



Complementaries

Price of Petrol	Demand for car
↑↓	↓↑



Law of Demand

Assumptions

All the determinants of demand are assumed to be constant except price

Exceptions

4Giffen's paradox
(Generally inferior goods)
Demand curve-back ward bending
4Articles of distinction
(Veblen goods)
4Demonstration effect
4Future expectations about prices
4Irrational consumer

Importance

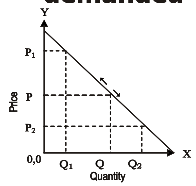
Useful to:
4Farmers
4Finance Minister
4Consumer
4Monopolist
(In determination of Price)

Reasons for downward sloping demand curve

4New Buyers
4Old Buyers
4Income effect
4Substitution effect

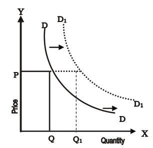
Changes in demand

Caused by Change in price
↓
Extension & contraction
↓
Movement along the same demand curve
↓
Change in quantity demanded

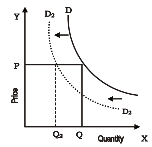


Caused by Change in other factors
↓
Increase & Decrease
↓
Shift in the demand curve
↓
Change in demand

Increase



Decrease



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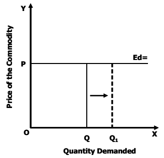
CHAPTER 2 : ELASTICITY OF DEMAND

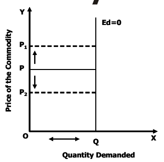
Price elasticity of demand

Degrees

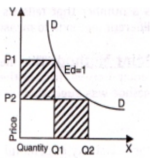
1) Perfectly elastic(∞)



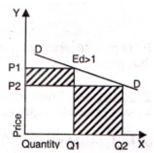
2) Perfectly inelastic (0)



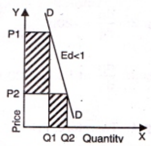
3) Unitary elastic (1)



4) Relatively elastic (>1)



5) Relatively In elastic (<1)

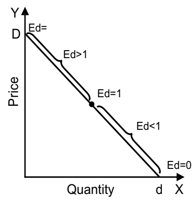


Methods

1) Point Method

$$Ep = \frac{dq}{dp} x \frac{p}{q} \quad \text{Or}$$

$$Ed = \frac{\text{lower segment}}{\text{Upper segment}}$$



2) Percentage Method

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

$$\frac{q}{q} \quad \frac{p}{p} = \frac{q}{p} \quad \frac{p}{q}$$

3) Arc Elasticity Method

$$Ed = \frac{q_2 \quad q_1}{p_2 \quad p_1} \quad \frac{p_1 + p_2}{q_1 + q_2}$$

4) Total out lay Method

Price	-	T.Exp
↑↓		↓↑ (Ed >1)
↑↓		↑↓ (Ed <1)
↑↓		Same(Ed =1)

Factors

1) Availability of Substitutes
*[If Available - Elastic
If not Available - Inelastic]*

2) Type of want
*[Necessary - Inelastic
Comforts, luxuries - Elastic]*

3) Consumer habits
*[Habitual consumers - Inelastic
Others - Elastic]*

4) No of purposes (uses)
*[Can be used -elastic
Can't be used -inelastic]*

5) Price Range
*[Very high /low -inelastic
Middle range-elastic]*

6) Postponement
*[Yes- elastic
No -inelastic]*

7) Proportion of Expenditure
*[Small -inelastic
High -elastic]*

Importance/uses

- Useful to business firms
- Determination of Price & output
- Determination of prices
- Useful to super markets
- Useful to finance minister
- Pricing factors of production
- Explains the paradox of plain theory
- Useful in foreign exchange rates
- Nationalising an industry
- Granting protection to industry

Income elasticity of demand

Formula

$$E_I = \frac{\% \, Change \, in \, demand}{\% \, Change \, in \, income} = \frac{q}{y} \quad \frac{y}{q}$$

Degrees

Negative (<0) -Inferior goods
Positive (>0) - Superior goods
0 to 1 - Necessaries
>1 - comforts/ luxuries

Cross elasticity of demand

Formula

$$E_C = \frac{\% \, Change \, in \, demand \, of \, x}{\% \, Change \, in \, price \, of \, y} = \frac{q_x}{p_y} \quad \frac{p_y}{q_x}$$

Degrees

Negative (<0) - Complementaries
Positive (>0) - Substitutes
Zero - Unrelated goods/ Independent goods

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CHAPTER 3: SUPPLY & ELASTICITY OF SUPPLY

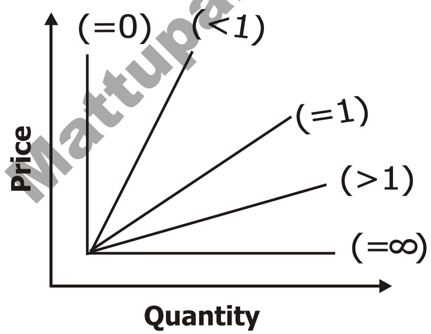
SUPPLY

Determinants
- Prices of Products
- Prices of related commodities
- Prices of factor of production
- State of technology
- Government policy
- Business policy
- Time
- Agreement among producers

Exceptions to law of supply
- Auction sale
- Fear of fall in prices in future
- Rare commodities
- Land
- Supply of labour

Elasticity of supply

Degrees of price elasticity of supply
- Perfectly elastic supply (=)
- Perfectly inelastic supply (=0)
- Relatively inelastic supply (<1)
- Relatively elastic supply (>1)
- Unit elastic supply (=1)



Determinants
- Nature of commodity
- Time
- Techniques of production
- Estimates of future

Importance
- Effect of price
- Quasi rent
- Better for

Measurements
- Point elasticity

$$E_s = \frac{q}{p} \quad \frac{p}{q}$$

- Arc elasticity

$$E_s = \frac{q_2 \quad q_1}{p_2 \quad p_1} \quad \frac{p_1 + p_2}{q_1 + q_2}$$

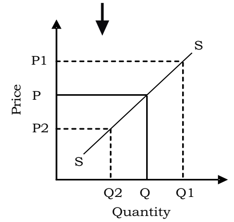
Changes in supply

Caused by change in price

Extension & contraction

Movement along the same supply curve

Change in quantity supplied



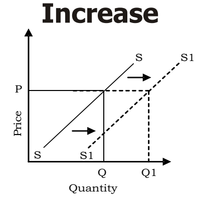
Caused by change in other factors

Increase & decrease

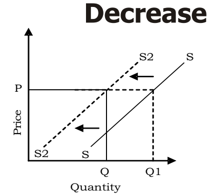
Shift in the supply curve

Change in supply

Increase



Decrease



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CHAPTER 4: THEORY OF CONSUMER's BEHAVIOUR

UTILITY

Cardinal (1,2,3...)

Marginal Utility analysis developed by Marshall

$$MU_n = TU_n - TU_{n-1}$$
$$= TU_{n+1} - TU_n$$
$$= \frac{TU}{Q}$$

Assumptions:

- 4Measurability of utility
- 4Marginal utility of money is constant
- 4Independent utility

Ordinal (I, II, III........)

Indifference curve Analysis developed by Hicks & Allen

Assumptions

- 4Rational consumer
- 4Scale of preference
- 4Diminishing marginal rate of substitution
- 4Assumption of consistency
- 4More units, more preference
- 4Scale of preference is

Properties

Indifference curve:

- slopes downwards from left to right
- are always convex to origin
- can never intersect with each other
- do not meet the axes
- need not be parallel to each other
- higher indifference curve gives higher level of satisfaction than lower one

Superiority

- 4Assumptions are near to reality
- 4Non measurability of utility
- 4Marginal utility of money is not constant
- 4Explain cause for Giffen Goods
- 4Two commodity model
- 4Marginal rate of Substitution

Marginal Utility Analysis

Law of Diminishing Marginal Utility

Assumptions

- 4Standard Units
- 4Identical Units
- 4No time interval
- 4No change in tastes & habits
- 4Some goods of special Nature
- 4Availability of substitutes &

Importance

- 4Price determination
- 4Finance minister
- 4Explains paradox of value
- 4Basis for economic laws
- 4Advantage to

Law of Equi-Marginal Utility

$$\frac{MU_a}{P_a} = \frac{MU_b}{P_b} = \ldots = \frac{MU_n}{P_n} = MU \ of \ money$$

Assumptions

- 4Indivisibility of goods
- 4Ignorance
- 4Unlimited resources
- 4Customs & fashions
- 4Measurability of Utility
- 4Constant utility of money

Importance

- 4Consumption
- 4Production
- 4Exchange
- 4Distribution
- 4Government

Theory of consumer's surplus

Consumers surplus=Willing price-Actual price

Criticisms

- 4Imaginary
- 4Measures mental satisfaction
- 4Difficult to calculate willing price
- 4Marginal utility of money is not constant
- 4Apply only in inflation
- 4Prestigious goods
- 4Changes from person to

Importance

- 4Price determination
- 4Useful to finance minister
- 4Price discrimination in discriminating monopoly
- 4Understanding the Water-diamond paradox
- 4Assessment of

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CHAPTER 5: PRODUCTION

LAND

Features

- Free gift of nature
- No cost of production
- Limited in supply
- Permanent
- Land has no mobility
- Land is heterogenous
- Land has multiple uses
- Land is a specific factors of production
- Land is subject to law

CAPITAL

Features

Capital is

- result of labour
- result of savings
- productive
- temporary
- mobile factor
- a passive factor
- not a free gift

Functions

- Provides subsistence
- Provides employment
- Provides raw materials
- Provides means of transport
- Provides tools & machines
- Increases labour Productivity

Capital formation

Stages

- Savings
- Mobilization of savings
- Investment of savings

Factors

- Ability to save
- Willingness to save
  a) Family affection b) Prudence,
  c) Habit, d) Social status
- Facilities to save
- Security
- Rate of interest
- Taxation

Forms of Capital

- Real capital & human capital
- Individual capital & Social Capital
- Fixed capital & Circulating capital
- Tangible capital & Intangible capital
- Sunk capital & floating capital
- Internal capital & external capital

ORGANISER

Different possible objectives

- Organic
- Economic
- Social
- Human

Problems

Problems relating to

- objectives
- location & size of plant
- finance
- organization structure
- marketing
- legal formalities
- industrial relations
- selecting & organising physical activities

Qualities

- Far- sightedness
- courage
- leadership
- organising the labour
- experience
- Knowledge of business
- Moral quality
- knowledge of

Functions

- Initiating a business enterprise & resource co-ordination
- Risk bearing or uncertainty bearing
- Innovations
- Organizing the business
- Managing the business
- Allocation of income
- Decision making

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Labour

Features

Labour-
- Means human exertion
- Power is co-extensive
- Is perishable
-Involves intelligence and judgement
-Is inseparable from labourer
-Has weak bargaining power
-Power differ's from labourer to labourer
-Efficiency of labour can increased
-Make choice between hours of labour & leisure
-Is less mobile than other factors

Mobility of Labour

Type

Occupational
(One job to another job in the same industry)

Horizontal
(In the same grade or at the same level)

Vertical
(Lower grade to higher grade)

Geographical
(One place to another place)

Factors

4Family-bond
4Information & knowledge
4means of transport & communication
4Level of literacy
4Poverty of labour

Factors affecting efficiency of Labour

4Racial qualities
4Health & strength of workers
4Standard of Living
4Education
4Personal qualities
4Social & political security
4Chances of promotion
4Trade unions
4Labour Laws

Division of Labour

Types

4Professional specialisation
(Auditors, Doctors, Engineers, Teachers, Carpenters)
4Specialisation by process
(Pins manufacturing)
4Territorial specialisation
(Cotton Mills in Gujarat, Cycle

ADVANTAGES

4Increases production
4Employment opportunities
4Efficiency
4Saving in time
4Saving in tools
4Large scale production
4Best quality of product
4Possibility of Mechanization

DISADVANTAGES

4Monotony
4Loss of skill
4Mistake will multiply
4Loss of sense of responsibility
4Risk of job
4Hinders mobility of labour
4Difficulty in distribution of

LIMITATIONS

4Extent of market
4Nature of demand
4Inventions
4Capital availability
4Technical knowledge
4Nature of Industry
4Labour availability

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CHAPTER 6: COST ANALYSIS

Determinants of cost

4Prices of factors of production
(If high- cost ↑, If low-cost ↓)

4Technology
(Advanced-cost↓,If not-cost↑)

4Size of plant
(Big-cost↓, small-cost↑)

4Capacity Utilization or output level
(Output level↑-cost↑, output level ↓-cost↓)

4Period
(Short run-cost↑, long run-cost↓)

4Stability of output
(If stable-cost↓, If unstable-cost↑)

4Law of returns operating
(Diminishing returns-cost↑, increasing returns-cost↓)

4Managerial efficiency

Components of cost

4Prime cost
(Direct material+direct wages+direct expenses)

4Production overheads
(Indirect material+indirect wages+indirect expenses)

4Production cost
(Prime cost+production over heads)

4Cost related to other functions
(Administrative over heads+selling over heads+ distribution over heads)

4Total cost

Relation between Average cost & Marginal Cost

4Average cost and Marginal cost can be calculated from total cost

4When Average cost falls Marginal cost also falls

4When Average cost rises Marginal cost also raises

4Marginal cost cuts Average cost at its optimum

Different types of costs

4**Implicit costs**
(Earnings of factors of production belonging to organizer himself)

4**Explicit costs**
(Remuneration paid to outside factors of

4**Accounting costs**
(All payments made by the entrepreneur to the suppliers of various factors of production)

4**Economic costs**
(Accounting cost {explicit}

4**Outlay costs**
(Actual outlay of funds like wages, material, rent)

4**opportunity costs**
(Cost related to foregone

4**Direct costs**
(Identified & traced to a particular product)

4**Indirect costs**
(Can not be identified & traced to a particular

4**Shutdown costs**
(Cost incurred after closing down of the business)

4**Abandonment costs**
(Cost related to retirement of fixed asset from use)

4**Money costs**
(Payment made to factors of production & other expenses)

4**Real costs**
(Pains & sacrifices of labour or efforts &

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CHAPTER7: PRODUCTION ANALYSIS

PRODUCTION FUNCTION

Short-Run
Law of variable proportions

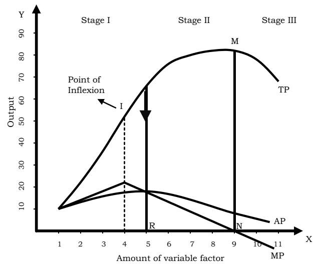
[Fixed factors -constant
Variable factors-vary]

Assumptions

4State of technology is constant

4Some inputs are kept to be fixed

4Law does not apply if they



1st stage
Law of increasing returns
Reasons

4Invisibility of fixed Factor of production

4Division of work &

2nd stage
Law of diminishing returns
Reasons

4Distributing optimum proportion

4Imperfect substitutability

3rd stage
Law of negative returns
Reasons

4Too much of variable factors in relation to quantity of fixed Factor

Long Run
(All factors are variable)

Law of returns to scale

1st stage
output > Input

Reasons

4Indivisibility

4Specialization

4Dimensional

2nd stage
output = Input

Reasons

4Exists in short period only

4Balancing

4Increasing returns to scale will not continue

3rd stage
output < Input

Reasons

4Expansion

4Entrepreneur

4Decreasing returns

Features

4Substitutability

4Complementary

Assumptions of production function

4Capital can be increased or decreased

4Production function implies to a given

Economies

Internal

4Technical :
-Big machines
-Bye- products
-Research
-Specilisation
-Linking process
-Workshops

4Managerial

External

4Cheaper source of raw materials & capital equipment

4Technical economies

4Development of skilled labour

4Growth of ancillary industries

4Better transportation &

Diseconomies

Internal

4Inefficient management

4Technical difficulties

4Production

4Financial

External

4Pollution

4Strains on infrastructure

4High factor

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CHAPTER8: MARKETS & CHAPTER 9 : PRICE &OUTPUT DETERMINATION

Features

- Every market have some commodities
- Competition
- Area

Types

On the basis of area

- Local market
  (buyers & sellers carry on business in a particular locality)
- National market
  (commodity is demanded and supplied all over the country)
- International market
  (commodity is demanded and supplied all over the

Basis of competition

- Perfectly competitive Market
  (large number of sellers selling homogeneous products)
- Monopoly
  (single seller of the Commodity having full control over the entire market)
- Imperfect Competition
  (It is a combination of monopoly & perfect competition)
- Oligopoly
  (only few sellers of a commodity each seller can influence the price-output policy of other

Basis of period of time

- Very short period Market
  (supply is more or less fixed)
- Short period market
  (one can change variable factors only but not fixed factors)
- Long period market
  (both fixed and variable factors can be changed)
- Secular period Market
  (changes can take place even in factors of

Factors effecting size of market

- Wide demand *(If - Yes↑, If -No↓)*
- Adequate supply *(If - Yes↑, If -No↓)*
- Durability *(If - Yes↑, If -No↓)*
- Portability*(If - Yes↑, If -No↓)*
- Grading and sampling
  (If - Yes↑, If -No↓)
- Transport and communications
  (If - Yes↑, If -No↓)
- Level of income*(If - high↑, If -low↓)*
- Development of financial institutions
  (If - Yes↑, If -No↓)
  - Availability of banks and other financial Institutions
  - Credit and banking habits of people etc

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CHAPTER 10: PRICE & OUTPUT DETERMINATION UNDER DIFFERENT MARKETS

Perfect Competition

Features

- Large number of buyers & Large number of sellers
- Products are homogeneous
- Free entry and free exist of firms
- Perfect knowledge of the market conditions
- Perfect mobility of factors of Production

Monopoly

Features

- Single seller of the product
- No close-substitutes
- Restrictions to entry
- Price maker
- Can't control supply & price
- Downward sloping demand

Sources

- Immobility of factors of production
- Ignorance
- Indivisibility
- Deliberate policy of

Monopolistic competition

Features

- Large number of Buyers and seller
- Product differentiation
- Control over price
- Freedom of entry or exit

Oligopoly

Features

- Interdependence
- Importance of advertising and selling costs
- Group behaviour
- Indeterminateness of demand curve

Discriminating Monopoly

Features

- Difference in elasticity of demand
- Market imperfections
- Legal sanction
- Existence of monopoly

Degrees

- **1st Degree**

  (In this the monopolist is able to sell each separate unit of his Product at different prices)

- **2nd degree**

  (In this buyers are divided into different groups and different price will be charged to different groups)

- **3rd degree**

  (In this seller divides his buyers into two or more than to sub markets & from each sub market a different price is charged)

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