Comparison Of Marris's Model With Baumol's Sales Maximisation Model

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Compare the instrumental variables and their use in each of the two models.

1. PRICE

    Both models assume a given price structure. Baumol's model assumes a known downward-sloping demand curve, from which total revenue is presumably derived.

    Marris states that price determination is not his main concern. He implies that the price structure will emerge either after a period of economic warfare. Thus in both models price is a parameter rather than a policy variable. It seems that these models are applicable to large firms which have considerable monopoly power so as to afford to ignore their competitors' reactions.

2. THE LEVEL OF OUTPUT

The level of output is an important policy variable in both models. Baumol treats firms as 'output-makers' rather than 'price-makers'. The level of output is determined by the optimal revenue value (R*), and by advertising, given the market price.

In Marris's model the level of output is not explicitly determined. From his model the level of diversification (d) is determined. It is not explained how from d the firm will reach decisions about the optimal output levels.

3. ADVERTISING AND R&D EXPENDITURE

The advertising expenses play a prominent role in Baumol's model. Their level is determined directly from the solution of his model. Baumol does not examine the implications of R & D expenses.

In Marris's model advertising is not treated explicitly. Its effects are reflected in the profit margin m. Since, however, m absorbs both the effects of A and R & D expenditures, the level of each one of these activities is not uniquely determined.

4. FINANCIAL POLICY

Financial policy is explicitly treated in Marris's model, in which it plays a crucial role. Baumol does not deal explicitly with the financial policy of the firm. However, financial policy considerations are implicit in his model, when he discusses the minimum profit constraint for internal and external purposes.